

International Business: Environments and Operations

Chapter 5 Trade and Factor Mobility Theory

Multiple Choice: Circle the letter of the one best choice according to the textbook:

- 1) Factor mobility refers to the movement of which of the following combinations?
 - A) capital, technology and people
 - B) currency, profits and raw materials
 - C) labor, capital and management
 - D) trade, profits and materials

- 2) In the text, Costa Rica devised a strategic trade policy to accomplish what goals?
 - A) attract industries that promised high growth and higher wages
 - B) develop and grow local industries to keep capital in Costa Rica
 - C) attract industries that were "green" and produced sustainable products
 - D) attract companies that were acceptable to the U.S.

- 3) Which of the following statements about Costa Rica and its approach to trade and factor-mobility strategy is true?
 - A) Costa Rica decided to select industries that would produce competitive products and improve workers' skills.
 - B) Costa Rica decided to attract industries acceptable to its major trading partners.
 - C) Costa Rica decided to select industries on a least cost basis.
 - D) Costa Rica decided to invite industries that were highly technical.

- 4) All countries face the questions of what, how much, and with whom they should import and export. How they answer these questions primarily affects whether _____.
 - A) nontradable goods become tradable
 - B) products go through a lengthy life cycle
 - C) companies adhere to laissez-faire export policies
 - D) a company's present production location will be competitive

- 5) The trade theory that says a country should export more than it imports is known as _____.
 - A) mercantilism
 - B) absolute advantage
 - C) comparative advantage
 - D) import substitution

- 6) Under mercantilism, governments sought to influence trade by _____.
 - A) establishing bilateral trading agreements with other countries
 - B) limiting exports
 - C) limiting imports and subsidizing exports
 - D) encouraging the development of manufacturing in their colonies

- 7) Which of the following UNDESIRABLE results will most likely occur for a country running a favorable balance of trade?
 - A) higher unemployment
 - B) higher domestic interest rates
 - C) fewer funds to invest abroad
 - D) granting credit that may be risky

8) Neomercantilism describes the approach of countries that try to run a favorable balance of trade to _____.

- A) build up gold reserves
- B) achieve a social or political objective
- C) lower their rates of inflation
- D) buy raw materials more cheaply

9) According to Adam Smith's theory of absolute advantage, specialization allows countries to increase their efficiency for each of the following reasons EXCEPT _____.

- A) labor could become more skilled by repeating the same tasks
- B) transportation costs could be lowered by producing closer to markets
- C) labor would not lose time in switching from the production of one kind of product to another
- D) higher production would provide incentives for the development of more effective working methods

10) Which of the following is most likely a basis for a Jamaican natural advantage in international trade?

- A) product technology developed by a Jamaican company
- B) high literacy rates among Jamaican citizens
- C) the use of English as the primary language
- D) beautiful beaches and climate

11) As a leading exporter of luxury automobiles, Germany has built a strong reputation in engineering. Germany's trade most likely relies on a(n) _____.

- A) outward immigration restriction
- B) natural advantage
- C) acquired advantage
- D) neomercantilist policy

12) Assume the following conditions: In the United States it takes 5 units of resources to produce a ton of potatoes and 10 to produce a ton of coal. In Canada it takes 6 units of resources to produce a ton of potatoes and 9 to produce a ton of coal. According to the theory of absolute advantage,

- _____.
- A) the United States should export potatoes to Canada and import coal from Canada
 - B) the United States should export coal to Canada and import potatoes from Canada
 - C) the United States should import both potatoes and coal from Canada, while concentrating on production of more valuable goods
 - D) there would be no basis for trade

13) Comparative advantage differs from absolute advantage in that the former _____, whereas the latter _____.

- A) holds that countries should specialize their production; does not
- B) holds that trade should be kept as nearly in balance as possible; says countries should seek a favorable balance of trade
- C) bases trade on natural advantages; bases trade on acquired advantage
- D) states that there is a basis of trade even if one country can produce everything more efficiently than another country; does not deal with this issue

- 14) The comparative advantage theory holds that a country will gain from trade _____.
- A) when it exports products for which it has an acquired advantage and imports products for which another country has a natural advantage
 - B) if it exports goods it can produce more efficiently than other countries and imports goods other countries can produce more efficiently than it can
 - C) even though it can produce all goods more efficiently than other countries
 - D) if it exports products using its abundant production factors in exchange for products for which it has scarce production factors
- 15) According to the theory of comparative advantage, a country gains from foreign trade even though it may have an absolute advantage in the production of all products because _____.
- A) the country will forego producing its less efficient output in order to produce its more efficient output
 - B) workers become more efficient through specialization
 - C) economies of scale will reduce cost
 - D) there will be more incentive to develop cost-saving technologies
- 16) Assume the following conditions: In the United States it takes 4 units of resources to produce a ton of potatoes and 5 to produce a ton of coal. In Canada it takes 6 units of resources to produce a ton of potatoes and 10 to produce a ton of coal. According to the theory of comparative advantage, _____.
- A) there would be no basis for trade
 - B) the United States should import potatoes from Canada and export coal to Canada
 - C) the United States should export both potatoes and coal to Canada
 - D) the United States should export potatoes to Canada and import coal from Canada
- 17) Which of the following assumptions was made in the original theories of absolute and comparative advantage?
- A) Specialized labor seeks efficiency.
 - B) Labor resources are fully employed.
 - C) Countries pursue objectives other than economic efficiency.
 - D) Production networks enable countries to concentrate on particular functions.
- 18) The free trade theories of specialization primarily assume that _____.
- A) specialization leads to unemployment, but production gains compensate for job losses
 - B) resources can move internationally from the production of one good to another
 - C) resources can move domestically from the production of one good to another
 - D) countries have objectives other than economic efficiency
- 19) The free trade theories of specialization primarily assume that _____.
- A) domestic resources are unable to move from the production of one good to another
 - B) countries have objectives other than economic efficiency
 - C) specialization triggers unemployment
 - D) resources are immobile internationally
- 20) Nontradable goods are best defined as _____.
- A) products and services for which exporting costs are excessive
 - B) factors of production that exceed safety regulations
 - C) goods used for national defense
 - D) products that comprise a portion of the inputs for finished products

- 21) Countries with varied climates and varied natural resources generally _____ than countries with less varied climates and natural resources.
- A) have lower per capita incomes
 - B) depend less heavily on trade
 - C) have more ethnic subgroups
 - D) have higher endowments of capital relative to labor
- 22) Countries with large land areas are generally less dependent on trade than countries with small land areas because of _____.
- A) highly restricted economic scales
 - B) self-sufficiency with natural resources
 - C) higher transportation costs related to foreign trade
 - D) the development of unique products that have a limited demand
- 23) Eight of the top 10 exporting and importing countries are countries with _____.
- A) cheap labor forces
 - B) small land masses
 - C) natural advantages
 - D) developed economies
- 24) The trade theory that says countries should concentrate production on those products using their most abundant production factors is the _____.
- A) factor proportions theory
 - B) theory of comparative advantage
 - C) theory of absolute advantage
 - D) theory of nontradable goods
- 25) El Salvador has a population density of about 620 people per square mile and neighboring Honduras a population density of about 115 people per square mile. According to the factor proportions theory of trade, one would expect El Salvador's exports to Honduras to _____.
- A) have a lower labor-to-land ratio than its imports from Honduras
 - B) have a higher labor-to-land ratio than its imports from Honduras
 - C) embody more capital per square mile than its imports from Honduras
 - D) embody more capital per worker than its imports from Honduras
- 26) Tests to substantiate the factor proportions theory have had mixed results most likely because _____.
- A) labor migration quickly outdates any studies
 - B) most countries have a favorable balance of trade
 - C) labor skills and education are not homogeneous
 - D) large and small countries have different trade policies
- 27) Most world trade takes place _____.
- A) between developed countries and developing countries
 - B) among developed countries
 - C) among developing countries
 - D) between raw material exporters and manufacturing exporters

- 28) One way that developed countries specialize in order to gain acquired advantages is by _____.
- A) allocating research efforts more heavily in specific sectors
 - B) emphasizing production in natural resource endowments
 - C) restricting imports to those in the service sector
 - D) subsidizing the transport of exports
- 29) Why is the United States both an exporter and importer of such products as vehicles and passenger aircraft?
- A) Buyers procure similar products for replacement parts.
 - B) Transportation costs and cultural differences limit exporters.
 - C) Companies differentiate products to appeal to different consumers.
 - D) Bilateral trading agreements require this interchange for a number of products.
- 30) Which of the following statements is most likely FALSE?
- A) Developing countries trade mainly with developed countries.
 - B) Developed countries trade mainly with other developed countries.
 - C) Cultural similarity among countries enhances their trade with each other.
 - D) The greater the geographic distance between countries, the greater the trade.
- 31) According to the product life cycle theory, production and sales are primarily domestic in the introductory stage because _____.
- A) businesses need quick market feedback
 - B) tariff reductions remain under negotiation
 - C) international transport costs are too high
 - D) international patents have not been approved
- 32) According to the PLC theory, at an early stage of a product's life cycle the product is likely to be made in a more _____ method than in its later stages.
- A) capital-intensive
 - B) labor-intensive
 - C) land-intensive
 - D) low-cost
- 33) According to the PLC theory, what is the most likely reason that companies manufacture products in locations with high labor rates during the introductory stage of a product's life cycle?
- A) Doing so allows use of long production runs using capital-intensive methods.
 - B) Many consumers are willing to pay high costs for the newest products.
 - C) Transportation costs are reduced by focusing on markets in developed countries.
 - D) Import restrictions prevent production in countries other than the ones making product innovations.
- 34) According to the PLC theory, developing countries have their best production advantage in which stage of the product life cycle?
- A) growth
 - B) maturity
 - C) decline
 - D) introduction

35) Which of the hypothetical new products, if successful, would most likely diffuse its production and sales according to the product life cycle theory?

- A) a Ferrari sports car selling for \$200,000 to a niche, upper-end market
- B) a Sony television that receives global transmissions without a satellite dish or cable connection, introduced at a high price but targeted eventually for sale to a mass market
- C) a new Diet Coca-Cola soft drink flavored with cranberries
- D) a Kyocera plastic chip carrier, which is expected to be quickly obsolete because of innovations

36) All of the following are types of products that are usually exceptions to what is predicted by the product life cycle theory EXCEPT _____.

- A) trendy clothing
- B) luxury items
- C) differentiated products
- D) consumer durables

37) Contrary to the product life cycle theory, there has been an increased tendency for companies to _____.

- A) sell products only in their home markets throughout the cycle
- B) produce and sell products in countries where counterfeiting is low
- C) introduce new products simultaneously in domestic and foreign markets
- D) sell new products in developing countries before expanding into developed countries

38) All of the following are features of the diamond of national advantage theory EXCEPT _____.

- A) firm strategy, structure, and rivalry
- B) strategic trade policy regulations
- C) related and supporting industries
- D) demand conditions

39) The diamond of national advantage would be best used to answer which of the following questions?

- A) How do developed countries prevent the trade of blood diamonds?
- B) How can developing countries create a significant trade surplus?
- C) Why do specialized competitive advantages differ among countries?
- D) Why do most innovative products originate in developed countries?

40) According to the diamond of national advantage theory, the domestic existence of all four conditions best explains _____.

- A) the essence of an industry's development
- B) the position of a product in its life cycle
- C) where globally competitive firms develop and sustain themselves
- D) why countries rely on abundant factor endowments

41) Costa Rica applied the concepts of the diamond of national advantage theory to help transform its economy by _____.

- A) building domestic demand for its products and services
- B) looking globally to develop favorable conditions
- C) following import substitution policies
- D) concentrating on nontradable goods

- 42) Which of the following best supports a nation's decision to implement a strategic trade (industrial) policy?
- A) The policies have usually resulted in big payoffs.
 - B) Governments, rather than entrepreneurs, should take the risks of developing new industries.
 - C) Consumer needs would otherwise not be met.
 - D) Government actions should target industries that are believed to give the country its best export advantages.
- 43) A governmental strategic trade (industrial) policy is one that _____.
- A) lessens dependence on foreign military goods
 - B) seeks reciprocal free trade agreements between developed and developing countries
 - C) targets the resources needed to support industries that seem to fit best with the country's advantages
 - D) limits imports to encourage domestic production of what would otherwise be imported
- 44) Which of the following statements most likely undermines the arguments for a strategic trade policy?
- A) Entrepreneurs, rather than governments, should take business risks.
 - B) Developed countries have production lead time over developing countries.
 - C) If big companies can figure out what products to develop, so can governments.
 - D) Governments have limited resources, so industries with greater growth potential should be targeted.
- 45) Between now and 2050, countries undergoing a simultaneous population reduction and an increased percentage of retirees in the population most likely will need more _____.
- A) imports
 - B) immigrants
 - C) domestic products
 - D) favorable balances of trade
- 46) The most internationally mobile factor of production is _____.
- A) labor
 - B) management
 - C) long-term capital
 - D) short-term capital
- 47) All the following are reasons for the lower international mobility of people than capital EXCEPT which one?
- A) The differences in economic return between countries are lower for people than for capital.
 - B) It is more expensive to move people than capital.
 - C) People may have to learn another language and adapt to a different culture.
 - D) International capital transfers have less cumbersome legal restrictions than international movements of people.
- 48) All of the following are examples of international labor mobility EXCEPT _____.
- A) a manager assigned by an MNE to work short-term abroad
 - B) a refugee who takes up employment in another country
 - C) a college student on a study abroad program
 - D) an illegal immigrant working in another country

- 49) Labor and capital mobility are intertwined because _____.
- A) illegal workers sometimes pay large sums to people who smuggle them into another country
 - B) people cannot emigrate to another country unless they bring capital with them
 - C) companies receive tax benefits for hiring immigrants
 - D) immigrants bring an investment in human capital with them
- 50) Brain drain is a term that describes _____.
- A) a country's loss of educated, productive people
 - B) a nation's shift from an emerging market to a developed economy
 - C) the exportation of high-technology products in exchange for low-technology products
 - D) the unauthorized use of patents, copyrights, and technology by the counterfeiting industry
- 51) Which of the following is the LEAST likely result of outward migration?
- A) Emigrants remit capital used to start businesses in their home countries.
 - B) Nations receive more foreign aid.
 - C) Nations lose highly educated and productive workers.
 - D) Countries receive remittances from emigrants.
- 52) Country X brings in a large number of unskilled immigrants to meet its labor needs. Which of the following is the LEAST likely to occur in Country X as a result?
- A) Country X will develop a long-term class of "have-nots" if the children of immigrants remain unskilled.
 - B) Country X will need more unskilled people in the future if immigrant children become skilled.
 - C) The continual supply of unskilled labor will delay the development of labor saving technology in Country X.
 - D) Country X will experience a significant transfer of knowledge and a resulting rise in start-up businesses.
- 53) In this example, assume that both trade and production factors are internationally mobile. Using domestic labor, the labor cost per silicon chip is \$.10 in Japan and \$.20 in the United States. Using domestic capital, the capital cost per chip is \$.10 in Japan and \$.05 in the United States. Chip transportation in either direction is \$.10. Japanese labor is willing to work in the United States for \$.15 per chip including the workers' transport cost. U.S. capital will go to Japan at a cost of \$.08 per chip including transaction costs. Which silicon chips will the United States buy?
- A) those made in Japan with Japanese labor and capital
 - B) those made in the United States with U.S. labor and capital
 - C) those made in Japan with Japanese labor and U.S. capital
 - D) those made in the United States with Japanese labor and U.S. capital
- 54) The inability of a company to gain foreign production factors to use in its domestic operations most likely _____.
- A) entices the company to export its own production factors
 - B) stimulates the company to adopt efficient substitute methods of production
 - C) stimulates foreign companies to invest in that domestic market
 - D) causes the company's products to move more rapidly through their life cycles

55) All of the following are reasons that foreign investment may stimulate exports from the home (donor) country EXCEPT which of the following?

- A) The investor often sends home-country components to its facilities abroad.
- B) The investor often sends home-country equipment to its facilities abroad.
- C) Home-country aid usually goes where the investments are made.
- D) The foreign facility is adept at selling the investors' home country products.

56) Analysts conclude that the finite supply of natural resources will most likely _____.

- A) cause a higher proportion of world trade to occur among developed countries
- B) cause a higher proportion of world trade to occur among developing countries
- C) serve as an advantage for developing countries in their sales to developed countries
- D) create a greater portion of world trade in the form of services

57) Research shows that urbanization leads to higher productivity. Which of the following is the LEAST likely reason for this?

- A) Urbanization establishes an inflow of immigrants who will work for less money.
- B) In urban areas, firms can more easily find people with the exact skills they need.
- C) Urbanization allows for economies in moving supplies and finished products.
- D) In urban areas, knowledge flows more easily from one company to another and from one industry to another.

58) The premise that there will be more finely tuned specialization of production among countries is most likely based on the idea that companies will _____.

- A) depend more on production of nontradable goods and services
- B) encourage urbanization in emerging countries that lack infrastructure
- C) establish facilities in dispersed locations to hinder domestic competition
- D) take advantage of wage and skill differences among countries

59) Costa Rica's recent economic transformation to depend more on high-tech manufacturing is largely due to its adoption of _____ trade policy.

- A) an import substitution
- B) a comparative advantage
- C) a factor proportions
- D) a strategic

60) All of the following factors most likely led to Costa Rica's attraction of high-tech FDI EXCEPT the country's _____.

- A) demand for high-tech products
- B) literacy rate
- C) quality of life
- D) political stability

Short Answer:

61) As an international business manager, how can you benefit from an understanding of international trade theories?

62) In a short essay, discuss the theory of mercantilism, and discuss favorable and unfavorable balances of trade as they apply to international business.

- 63) In a short essay, discuss the theory of absolute advantage and the reasons a country's efficiency improves based on this theory.
- 64) What is the difference between the free trade theories of absolute advantage and comparative advantage? How can free trade improve global efficiency?
- 65) What assumptions underlie the theories of specialization in international trade? What are the limitations of these assumptions?
- 66) What is the theory of country size? How is country size determined? How does country size affect national trade patterns?
- 67) What is the country similarity theory? According to this theory, what factors affect trade patterns?
- 68) In a short essay, discuss the four stages of the international product life cycle.
- 69) What are the arguments for and against nations developing and implementing strategic trade policies?
- 70) From an economic standpoint, why do production factors move from one country to another?