Question 1
a. What is the main advance of the Ricardian model? That is, what is its most significant contribution to economics? Be sure to show this result using a series of well-labeled diagrams.
b. According to the Ricardian model, what is the impact of free trade on output prices? Be precise in your discussion.

Question 2
a. Using a diagram, show the impact of a tariff on a small economy. Specifically, indicate the impact on the domestic market price and the domestic consumption. Is it possible for a small economy to benefit from a tariff? Does anyone benefit from a tariff? Explain.
b. With this in mind, evaluate the following comments from Pat Buchanan:

“With tariffs, we can shift the burden of taxes off the incomes of U.S. workers and small business, onto consumers of foreign goods. ‘By the tariff system’, said Abraham Lincoln, ‘the whole revenue is paid by the consumer of foreign goods … The man who contents himself to live upon the products of his own country pays nothing at all.’”

Question 3
Assume labor and capital are the only two inputs. Modernia is a universally capital abundant country that produces capital-intensive personal computers and labor-intensive fax machines. Capital can be employed in either industry and can move back and forth readily between the two. Labor is specialized; some labor is suited to produce personal computers and other labor to produce fax machines. Computer labor is useless in producing fax machines and fax labor is useless in producing computers. If Modernia opens trade with a country with identical tastes, what will happen in the short run on:

a. Modernia’s prices and production of computers and fax machines? What information/theorem did you use as the basis for your answer?
b. Wages of computer labor in Modernia? How do you know? Illustrate this effect using a diagram.
c. Wages of fax labor in Modernia? How do you know? Illustrate this effect using a diagram.
d. The price of capital in Modernia? How do you know? Illustrate this effect using a diagram.
e. What would be the effect of opening trade on factor prices in the long run?