Problem Set #3

1. In September 1980 Senator Robert Dole proposed a tariff of $0.40 per gallon of ethyl alcohol imported into the United States. Use partial equilibrium analysis and assume the world price of ethyl alcohol is constant.

   A. Show graphically and explain the effects of the imposition of this tariff on the U.S. market for ethyl alcohol.

   B. Senator Dole claimed that ethyl alcohol was an infant industry in the United States. Explain why protection of an infant industry may be economically justified. What questions would you try to answer before accepting this reason for protecting the industry?

2. The United States government has convinced foreign producers of clothespins to reduce their level of exports to the United States through a VER. Assume that the supply of imports into the United States under free trade is infinitely elastic at the going world price.

   A. Show graphically and explain the effects of this VER on the U.S. market for clothespins. Use partial equilibrium analysis.

   B. U.S. market demand for clothespins is expected to decline over the next few years, due to growing consumer acceptance of substitutes. Show graphically and explain the effects of this shift in demand, if the VER quantity is left unchanged.

   C. How would your answer to part B differ, if the United States uses a tariff (instead of a VER) to reduce the level of imports of clothespins? Explain.
3. Assume that all imports of socks into the United States come from the developing countries. The United States has decided that it must maintain a domestic production level of socks higher than now exists.

You are chosen to represent the developing countries in sock negotiations with the U.S.

The U.S. is willing to consider three methods of assuring its minimum domestic production level:

1. A tariff on imports
2. A domestic production subsidy,
3. The imposition by the exporting countries of a voluntary export restraint.

Discuss each of these options from your point of view as a representative of the developing countries, and compare their effects on the interests of the developing countries as exporters. Use partial equilibrium graphical analysis, and assume that the world price of socks is unaffected by U.S. demand for sock imports.