

Place your name on the back of this sheet of paper and nowhere else. Staple your answers face up on the front of this sheet of paper. Failure to follow these directions will cost you 10 points. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to type this assignment will cost you 10 points. If you use double-sided printing or print on the back of scrap paper, I will give you one additional point.

1) (15 points) According to the article linked below, there is a customs union between San Marino and the EU. Do you think that the formation of the CU had more trade creation or trade diversion? Explain your logic using two of the criteria we listed. In case you were unaware, San Marino is a country just under 24 square miles completely surrounded by Italy. A circle of 24 square miles would have a radius of about  $2\frac{3}{4}$  miles.

<https://trade.ec.europa.eu/access-to-markets/en/content/eu-san-marino-customs-union>

2) (25 points) Draw the CU S/D diagram which has both trade creation and trade diversion. Explain why the graph looks as drawn. Show the trade creation and diversion. Explain how you found them.

3) (15 points) NAFTA was, and USMCA is currently a free-trade area. Why do we still need customs officials on the borders between the countries?

4) (15 points) Why hasn't the USA converted USMCA to a customs union? I.e., what is the biggest drawback to a CU over a FTA?

5) (10 points each) For each of the following, explain why it means that the customs union is more likely to increase the welfare of the country.

A) Greater pre-union trade among the members.

B) Larger number of countries in the CU.

C) Lower CU tariffs with the rest of the world.