STOCKHOLM UNIVERSITY
Department of Economics

Course name:	**Economic Integration**
Course code:	**EC7311**
Examiner:	**Rikard Forslid**
Number of credits:	**7,5 credits**
Date of exam:	**February 12th 2017**
Examination time:	**3 hours (09.00 -12.00)**

Write your identification number on each paper (the number stated in the upper right hand corner on your exam cover).

Do not write answers to more than one question on each paper. Answer in a concise fashion. Explain notions/concepts and symbols. If you think that a question is vaguely formulated, specify the conditions used for solving it. Only legible exams will be marked. No aids are allowed.

The exam consists of 4 questions, 100 points in total. For the grade E 45 points are required, for D 50 points, C 60 points, B 75 points and A 90 points.

Results will be posted on mitt.su.se 15 working days after the exam, at the latest

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Good luck!

Question 1 (25p)

The European integration has lead to lower trade costs between its members. At the same time this implies that countries outside EU are disfavoured in the European market. Analyse the effects of this type of preferential trade liberalisation. Compare the welfare effects of a tariff reduction and a reduction of frictional trade barriers.

Question 2 (25p)

Analyse the effects of economic integration in a model with two sectors: X and Y. The X-sector is characterized by increasing returns to scale, free entry, and Cournot competition. The Y-sector has constant returns to scale and perfect competition. Utility of the representative consumer is given by

$$U=(nX)^{\alpha}Y^{1-\alpha}$$

,and the cost function of X-sector firms is

$$C=f+cX,$$

where all notation has its usual meaning.

Question 3 (25p)

Analyse formally the heterogeneous firm model by Melitz. What is the effect of trade liberalization in this model?

Question 4 (25p)

a) Explain how the CAP-system has become so burdensome (expensive) that it takes almost half of EUs budget.

b) The convergence criteria for entering the euro-system involved a deficit of max 3 percent and a debt to GDP ratio of max 60 percent. These figures are consistent with a steady-state ("German golden rule") of an inflation of 2 percent and a growth rate of real GDP of around 3 percent. Debt levels have risen in Europe since the financial crisis. What growth rate is consistent with a steady-state if the debt to GDP ratio is 80 percent (and inflation unchanged at 2 percent)?