



Stockholm  
University

Department of Economics

**Course name:** International Economics  
**Course code:** EC2301  
**Type of exam:** Main  
**Examiner:** Anders Åkerman  
**Number of credits:** 7,5 credits  
**Date of exam:** Monday 8 January 2018  
**Examination time:** 3 hours (14:00-17:00)

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

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.**

**Answer in Swedish or English.**

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The maximum number of credits is 99 (for answers on the exam) + 15 (for assignments).  
Credits correspond to grades as follows:

90 – 115	A
80 – 89	B
70 – 79	C
60 – 69	D
50 – 59	E
0 – 49	F

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Your results will be made available on your “My Studies” account ([www.mitt.su.se](http://www.mitt.su.se)) on January 29 at the latest.

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**Good luck!**

1. Explain the following concepts in 50 words maximum for each concept. (3 points per concept, i.e. maximum 24 points).

- a) Vertical foreign direct investment
- b) Internal economies of scale
- c) Comparative advantage
- d) Voluntary export restraint
- e) Intra-industry trade
- f) Monopolistic competition
- g) Gravity model of international trade
- h) Abundant factor

2. Many reasons for why the United Kingdom voted to leave the European Union have been proposed. A common one is that imports from the EU hurt low-skilled British workers. This question will ask you to analyze what effect Brexit (the UK's exit from the EU) may have on relative wages for high-skilled and low-skilled workers in the UK using the **Heckscher-Ohlin model** of international trade.

Suppose that there are two industries: financial services and manufacturing. Further assume that there are two factors of production, low-skilled and high-skilled workers, and that finance is high-skill intensive and manufacturing is low-skill intensive. Further assume that the United Kingdom is abundant in high-skill labor (i.e. it has relatively more high-skilled workers than the rest of the EU).

a) Show using the Heckscher-Ohlin model of international trade how relative wages for low-skilled and high-skilled workers are determined when the UK is a member of the EU (i.e. when there is free trade between the UK and the rest of the EU). Explain your answer. (9 points)

b) Now suppose that the UK leaves the EU. For simplicity, we will model this as autarky, i.e. that all trade between the UK and the EU stops. How do real wages of low-skilled and high-skilled workers change (remember that the UK is abundant in high-skilled labor)? Explain your answer. (9 points)

c) Describe also how the relative output of financial services versus manufacturing in the UK changes with Brexit. Explain your answer. (7 points)

*THE EXAM CONTINUES ON THE FOLLOWING PAGE*

3. Suppose that two countries, the US and Canada, can produce two goods: cars and clothes. Assume that the US requires 3 workers to produce a car and 2 workers to produce a unit of clothes. Canada needs 6 workers to produce a car and 5 workers to produce a unit of clothes. Use the **Ricardian model** of international trade to answer the following questions.

a) Draw the Production Possibility Frontiers for both countries. Assume that the countries have 60 workers each. (5 points)

b) Under autarky, what are the relative prices of the two goods in the two countries? Explain your answer. (5 points)

c) Under autarky, how many cars can a US worker buy if he or she spends all income on cars? Likewise, how many units of clothes could a US worker buy under autarky? Explain your answer. (5 points)

d) State within what range the relative price will be under free trade. Which country will export what good? Explain your answer. (5 points)

e) Choose any price level in the price range you give as answer to question d). Assuming that this price will be the relative price under free trade, answer question c) for the case of free trade instead. Explain your answer. (5 points)

4. You are writing a report on the effect of trade policy for the steel sector of a small country. Suppose that the country is an importer of steel.

a) Show and explain the welfare effects of an import tariff on steel. (7 points)

b) Show and explain the welfare effects of an import quota on steel. (7 points)

c) Suppose now that the country you analyze is a large country. How would your answers to a) and b) change? Explain your answer. (5 points)

d) Using what you have learnt in the course on the political economy of international trade policy, give two reasons why actual trade policy might not always be the policy that maximizes national welfare but rather something that prioritizes the welfare of certain groups more than others? Explain your answer. (6 points)