



Stockholm
University

Department of Economics

Course name: International Economics
Course code: EC2301
Type of exam: Retake
Examiner: Anders Åkerman
Number of credits: 7,5 credits
Date of exam: Sunday 11 February 2018
Examination time: 3 hours (09:00-12:00)

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.

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

Your results will be made available on your “My Studies” account (www.mitt.su.se) on Friday 2 March at the latest.

Good luck!

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

- a) absolute advantage
- b) labor intensive industry
- c) customs union
- d) most favored nation (MFN) status
- e) infant industry
- f) corporate social responsibility
- g) labor pooling
- h) trade diversion

2. This question will ask you to use the **specific factor model** to analyze a simplified version of a liberalization of trade between South Korea and the United States. Assume that there are two goods that people want to buy: kimchi (fermented cabbage) and cars. Assume that there are three production factors: land, capital and labor. Land is specific to kimchi, capital is specific to cars and workers can work in both industries.

- a) Describe using a graph how workers allocate in autarky between the two sectors in South Korea. Explain your answer. (10 points)
- b) Assume that, under autarky, kimchi is cheaper in South Korea than in the US. How does the price of kimchi in South Korea change when South Korea opens up to international trade? Explain your answer. (5 points)
- c) Describe using a graph how workers in South Korea reallocate between sectors after South Korea and the US open up to trade with each other. Explain your answer. (5 points)
- d) Describe how the real wage of workers and the real returns of land and capital change in South Korea with trade liberalization. Explain your answer. (5 points)

THE EXAM CONTINUES ON THE FOLLOWING PAGE

3. A large part of international trade today is intra-industry trade, i.e. that countries exchange similar products belonging to the same industry. A commonly used model to analyze this type of trade is the so-called model of **monopolistic competition**, where each firm benefits from internal returns to scale and sells a differentiated product.

- a) Explain the difference between internal and external returns to scale. (10 points)
- b) Describe what this model says about the relationship between firms' average cost and the number of firms (the so-called CC curve in the model). Explain your answer. (5 points)
- c) Describe what this model says about the relationship between firms' prices and the number of firms (the so-called PP curve in the model). Explain your answer. (5 points)
- d) Use a graph with price and cost on the vertical axis and the number of firms on the horizontal axis to describe what happens to welfare when two identical countries start to trade with each other. Explain your answer. (5 points)

4. Use the **Ricardian model** of international trade to analyze the following case of trade liberalization between the European Union (EU) and China. Suppose that there are two goods: cheese and pepper. Assume that the EU needs 10 labor hours to produce 1kg of cheese and 20 labor hours to produce 1kg of pepper. China, on the other hand, needs 20 labor hours to produce 1kg of cheese and 5 labor hours to produce 1kg of pepper.

- a) Describe the relative autarky price of cheese in the EU and China, respectively. Explain your answer. (6 points)
- b) If the two countries start to trade, what will the pattern of trade be? Explain your answer. (6 points)
- c) Do the countries gain or lose from trade? Explain your answer. (6 points)
- d) Suppose that China suddenly experiences a technological improvement in cheese production and is now able to produce 1kg of cheese using only 2.5 labor hours. What will the new pattern of trade be? Explain your answer. (7 points)