



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: Saturday 8 June 2019
Examination time: 3 hours (15:00-18:00)
Aids: No aids are allowed.

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

Start each new question on a new answer sheet.

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.

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 Ladok account (www.student.ladok.se) within 15 working days from the date of the examination.

Good luck!

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

- a) Comparative advantage
- b) Most favored nation (MFN)
- c) External economies of scale
- d) Voluntary export restraint
- e) Median voter
- f) Intra-industry trade
- g) Dynamic increasing returns
- h) Quota rents

2. This question asks you to analyze the welfare effects of potential US import tariffs on cars. Use a partial equilibrium analysis where you can analyze the effect of a tariff on consumer and producer surplus as well as the government budget. Assume that the US is a net importer of cars under free trade.

- a) First analyze the effect of a US import tariff on cars. Using a graph, show the effects of a tariff on consumer surplus, producer surplus and government income in the US. (5 points)
- b) What is the total effect on US welfare? (4 points)
- c) Now assume that the US introduces an import quota instead. Using a graph, show the effects on consumer surplus, producer surplus and government income. (4 points)
- d) When setting its import tariffs, how can the US use the fact that it is a large country and that its trade policies affect world prices? (4 points)
- e) Assume that the tariffs are directed towards car exports from the EU. The EU is also an economic entity that is large enough to affect world prices. Describe the welfare effects of a US import tariff for the EU using a graph. (4 points)
- f) Using trade policy, how can the EU respond to the US import tariff? (4 points)

THE EXAM CONTINUES ON THE FOLLOWING PAGE

3. Assume that the world consists of Norway and Sweden and that these countries do not trade with each other. There are two goods in this world: timber and mobile phones. Assume that Sweden needs 1 worker to produce a unit of timber and 2 workers to produce a mobile phone. Norway needs 6 workers to produce a unit of timber and 3 workers to produce a mobile phone. We assume for simplicity that both countries have 24 workers each. Use the Ricardian model to answer the following questions.

- a) Draw the Production Possibility Frontiers for timber and mobile phones in both countries. (4 points)
- b) Assume that both countries produce both goods in autarky: what will the autarky prices be in the two countries? (4 points)
- c) Now we allow the countries to trade with each other. Assume that the equilibrium with trade is such that one country fully specializes in the production of timber and the other country in mobile phones. Which country specializes in which good? (4 points)
- d) Give one potential global relative price that would generate full specialization in both countries. (4 points)
- e) Using this price, draw the Consumption Possibility Frontiers for both countries for the case when trade is possible. Compare with the Production Possibility Frontiers. What does this say about how welfare changes in the two countries? (4 points)
- f) How can it be that a country that is less productive at producing all goods can still benefit from trade? (5 points)

4. Imagine that you are advising a small country on the short run effects of opening up to trade. Use the specific factor model to conduct your analysis. Policymakers in a country are interested in who in the country will gain and who will lose from trade. They are also interested in the overall welfare effects of trade.

Assume that there are three factors of production: low-skilled workers, high-skilled workers and capital. Moreover, assume that there is a low-tech and a high-tech good. Capital is used to produce both goods but high-skilled workers are specific to the high-tech good and low-skilled workers are specific to the low-tech good.

- a) Describe using a graph how the allocation of capital is determined (i.e. how much capital is allocated to each sector). (5 points)
- b) Assume now that the relative price of high-tech goods in terms of low-tech goods is lower in this country than in the rest of the world. What does this say about the relative endowments in the country of low-skilled and high-skilled workers compared to the rest of the world? (5 points)
- c) How will the relative wage between high-skilled and low-skilled workers change when the country opens up to trade? Use a graph to explain. (5 points)
- d) What does the model say about how trade affects overall welfare in the country? Use a graph to explain. (5 points)
- e) Is it possible to make sure that everyone gains from trade? If so, how? (5 points)