

**Examination
for the lecture
“International Trade”
(20384)**

Preliminary Remarks:

- **Time:** 2 hours.
 - **Aids:** no aids are allowed, except a bilingual dictionary.
 - **Language:** English. Answers in German are possible for students who are registered in German-speaking programmes of the University.
 - **Structure:** 4 questions (1,2,3,4). Each question is to be answered using standard tools of economic reasoning. Each question is weighted equally and consists of three parts. In each question, a maximum of 30 points can be reached. The total number of points is 120.
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Question 1:

In a Ricardo model with two countries (Home and Foreign), two goods (wine and cheese) and one factor of production (labour), a country specializes in the production of the good that it produces with a comparative cost advantage.

- (a) Show graphically and explain verbally that this form of specialization leads to gains from trade for all.
- (b) Explain why international differences in absolute levels of labour productivity do not matter for the structure of trade.
- (c) Show graphically and explain verbally how the pattern of trade and specialization looks like when there are more than two goods.

Question 2:

International trade within industries (“intra-industry trade”) can be explained by scale economies and product differentiation.

- (a) Show – graphically and explain economically – in a model of monopolistic competition how economies of scale and product differentiation interact.
- (b) Show graphically and explain economically, how the move from autarky to trade works in this model.
- (c) Assume that a minimum of average cost exists as marginal cost rises above average cost at a certain level of production. Does the industry produce at the minimum average cost in the long run? If so, why? If not, why not?

Question 3:

A country introduces an import tariff on good x. To analyze the effects of this tariff, use an appropriate partial equilibrium model.

- (a) Choose a model of a large country with perfect competition. Show graphically and explain verbally how the tariff affects prices, production and consumption as well as the welfare of the country. Use the concepts of consumer and producer surplus.
- (b) Choose a model with the presence of monopoly power. Show graphically and explain verbally how an import tariff affects monopoly power.
- (c) Compare the effects of an import tariff and an import quota. Do this for the case of perfect competition (part (a) above) and in the presence of monopoly power (case (b) above). Which one – import tariff or import quota – fares better in terms of limiting monopoly power, and why?

Question 4:

One of the oldest and most widespread arguments for protection of an industry is the so-called **infant industry argument**.

- (a) Explain the precise economic logic of the infant industry argument as a case for
 - [i] tariff protection of an industry in a developing country (“policy of import substitution”)
 - [ii] subsidization of an industry in an industrial country (“industrial or technology policy”).
- (b) Evaluate the two types of policies ([i] and [ii]) on the grounds of static welfare economic theory.
- (c) Evaluate the two types of policies ([i] and [ii]) with respect to the actual historical experience that was made with them in the last few decades.