

**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.
-

Question 1:

Assume a **Heckscher-Ohlin model** with two countries (Home and Foreign), two goods (cloth and food) and two factors of production (labor and land).

- Explain economically what the specialization pattern will be. Do this with a particular view to the factor intensities of production in the two sectors.
- Show graphically and explain verbally that (and how) trade leads to international factor price equalization.
- Explain why, in reality, we do not typically observe international factor price equalization. Which assumptions of the model are violated in reality?

Question 2:

Assume a **standard trade model** with two countries, two goods and two factors of production. Show graphically and explain economically how and why the terms of trade are affected by

- biased growth in one of the two countries,
- an international income transfer between the two countries,
- a tariff on imports in one of the two countries.

Please, turn the page!

Question 3:

"It is a well-confirmed empirical fact that, within individual industries, there are two groups of firms: firms that export and firms that do not export. In a way, trade and competition may be viewed as a selection process by which some firms do and others do not survive as suppliers to foreign markets."

- (a) Show graphically and explain economically how **differences in production costs** can account for the selection process referred to in the quotation.
- (b) Show graphically and explain economically how the **existence of trade costs** can account for the selection process referred to in the quotation.
- (c) Make a judgement on whether and to what extent parts (a) and (b) describe empirically relevant cases.

Question 4:

The government of a country decides to levy a **tariff on imports** of good x. In a press conference, the minister of economic affairs of the country explains the new policy stance. In particular, he makes the following statement: "The protection is a temporary measure. It is to last only until the protected import-competing industry has grown into a size that makes it internationally competitive."

- (a) Assume the minister is a good economist. Explain what precise economic logic of dynamic efficiency lies behind his argument.
- (b) Assume that the country concerned is a (relatively poor) developing country, which still lacks a strong manufacturing base. Apply the logic from part (a) to this prototypical situation. Summarize the historical record with so-called import-substitution policies in developing countries.
- (c) Assume that the country concerned is a (relatively rich) industrialized country. Apply the logic from part (a) to this prototypical situation. Evaluate the problems and prospects of so-called industrial and technology policies in highly industrialized countries.