

**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:

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

- (a) “Trade leads to gains for all.” Show graphically that this statement is true. Give a verbal explanation of its economic rationale.
- (b) “Trade is an efficient form of indirect production.” Show algebraically that this statement is true.
- (c) Assume that there are more than two goods, but still two countries and one factor of production. Show graphically and explain economically how the pattern of trade and specialization then looks like.

Question 2:

“International trade within industries can be explained by scale economies and product differentiation. Therefore, this type of trade has nothing to do with factor endowments. However, it has a lot to do with the size of the market that is created by free trade.”

- (a) Show graphically and explain economically that, in a theoretical framework of monopolistic competition, this statement is correct.
- (b) A theoretical model is one thing, reality is another one. How realistic is the model and its assumptions?
- (c) Explain why, even with trade, the economy does not produce at the minimum of average cost (if there is such a minimum).

Please, turn the page!

Question 3:

Within individual industries, there are often, side by side, firms that export and firms that only deliver to the domestic market.

- (a) Show graphically and explain economically how differences in production costs can account for this fact.
- (b) Show graphically and explain economically how the existence of trade costs can account for this.
- (c) Make a judgement on whether and to what extent parts (a) and (b) describe empirically relevant cases. What other forms of firm heterogeneity may be responsible for firms' engaging in or refraining from trade?

Question 4:

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 (part (b) above). Which one – import tariff or import quota – fares better in terms of limiting monopoly power, and why?