International Trade: Theory and Policy 5EN455
Final Examination – January 14, 2014

This is the final (and the only) examination. It will take 60 minutes.

In order to pass successfully the exam, read the following instructions carefully:
• write legibly, unintelligible handwriting will not be corrected and will receive zero points
• make answers short and to the point – irrelevant material may be penalized
• the exam has 4 pages, make sure you have all pages
• negative points are awarded for wrong answers (only) in part I
• if you have a question, you must ask it publicly and I will answer publicly
• any violation of academic honesty will be punished to the fullest extent possible

I. Multiple choice questions (circle the correct answer) – more than one answer can be correct, points are subtracted for incorrect answers (30 points total)

1. (6 points) International trade (as opposed to autarky) in a Krugman model
   a. increases number of varieties consumed, utility and wages
   b. increases number of varieties consumed, utility and decreases prices
   c. increases number of varieties consumed, utility
   d. increases total number of varieties produced in each country

2. (6 points) Among reasons for existence of international trade are NOT:
   a. preference for variety among consumers
   b. differences in factors of production endowments among countries
   c. differences in competitive structures among countries
   d. none of the above is correct

3. (6 points) Lloyd-Gruber index is used to measure
   a. the extent of trade in similar goods
   b. the revealed comparative advantage
   c. the size of the market
   d. the level of international division of labour

4. (6 points) Compute optimal tariff for a good M in a small country A if you know elasticity of demand for M in country A ( - 3,0), elasticity of demand for M in country ( - 4) and elasticity of demand for M in the world market ( - 3,5).
   a. 50 %
   b. 40 %
   c. 33 %
   d. none of the above is correct

5. (6 points) Magnification effect
   a. holds only in 2x2x2 economy;
   b. means that price of the final goods rises more in relative terms than the price of the factor of production;
   c. holds quite generally – regardless of number of countries in a model;
   d. none of the above is true.
II. True, False or Uncertain? Explain in space provided! (30 points total)

1. (6 points) Rybczinski proposition holds in the weaker sense – i.e. an increase in the available amount of factor of production “on average” decreases the production of goods using this factor of production.

2. (6 points) PPF in a neoclassical model is curved and concave as a result of diminishing returns of each and one factor of production as opposed to PPF in a model of comparative advantage where it is linear.

3. (6 points) Identical countries with the same technology, same homothetic utility function and same endowment of factors of production have no room for international trade.

4. (6 points) Technological differences in the Ricardian model do not preclude international trade (are the reason for it in fact) but give rise to differences in wages between countries.

5. (6 points) In neoclassical framework (2x2x2), an increase in the price of a final good increases the reward to the factor of production used intensively in the production of the good and reduces the reward to the other factor.
III. Write a detailed answer (40 points total)

1. (20 points) Assume demand bias in countries A and B for domestic production. Show graphically the situation where there is NO room for trade due to this bias.

2. (20 points) Explain the differences / the equivalence between tariffs and quotas imposition if there is a monopoly structure of the industry in a country.