International Economics (2645) Exam January 16, 2013. Duration 4 h
Allowed accessories: calculator. Examiner: Staffan Ringbom

1. Explain shortly (3p/sub-question, max 15p)

    (a) Comparative advantage

    (b) non-sterilized interventions (in foreign exchange market)

    (c) the uncovered interest parity

    (d) carry trade

   (e) the infant industry argument (for tariff protection)

2. Trade Theory, Hekscher-Ohlin...

    (a) Explain the intuition behind the Hekscher-Ohlin theorem and the factor-price-equalization theorem. (7p)

    (b) Explain roughly how the developed countries can protect them selves against low wages in undeveloped countries. (5p)

    (c) Explain what is likely to happen to the aggregate price level and wages in less developed countries during a "catching-up" process when they become "more developed". (3p)

3. A two-sector economy has natural resources and labour. Although the technology would imply constant returns to scale, the production function for a fixed amount of natural resources show diminishing returns to scale. The production function in sector one is $Q_1 = 100L_1^{0.8}$ and $Q_2 = 400L_2^{0.8}$ in sector two . There exist 5624 units of labour available in the economy per period. The world market prices for the final products are $p_1 = 100$ and $p_2 = 25$ respectively. Graph the production possibility frontier. (In order to get scores, remember put in the units and levels of labour and produced quantities on the the axis in your graph). How much will be produced of Q_1 and Q_2 respectively, and what is GDP in the economy (5)? What is the equilibrium wage level and what is the distribution of the GDP between the capitalists and the workers (3p)?

4. Explain the idea behind the model with internal and external imbalances, (including Explain the "4-zones of discomfort") (9p), (see Figure 1) Using this model explain a) the imbalances within EMU and how these imbalances could be solved for (3p), b) the global imbalances we observe today, (e.g China vs. US) and how these imbalances could be solved for (3p).
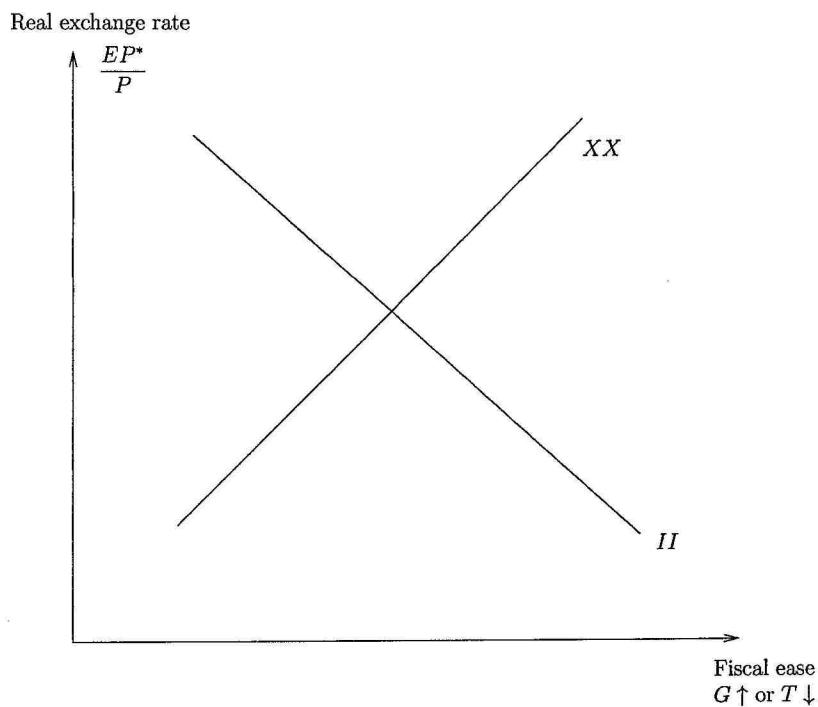
1

Real exchange rate

$$\frac{EP^*}{P}$$
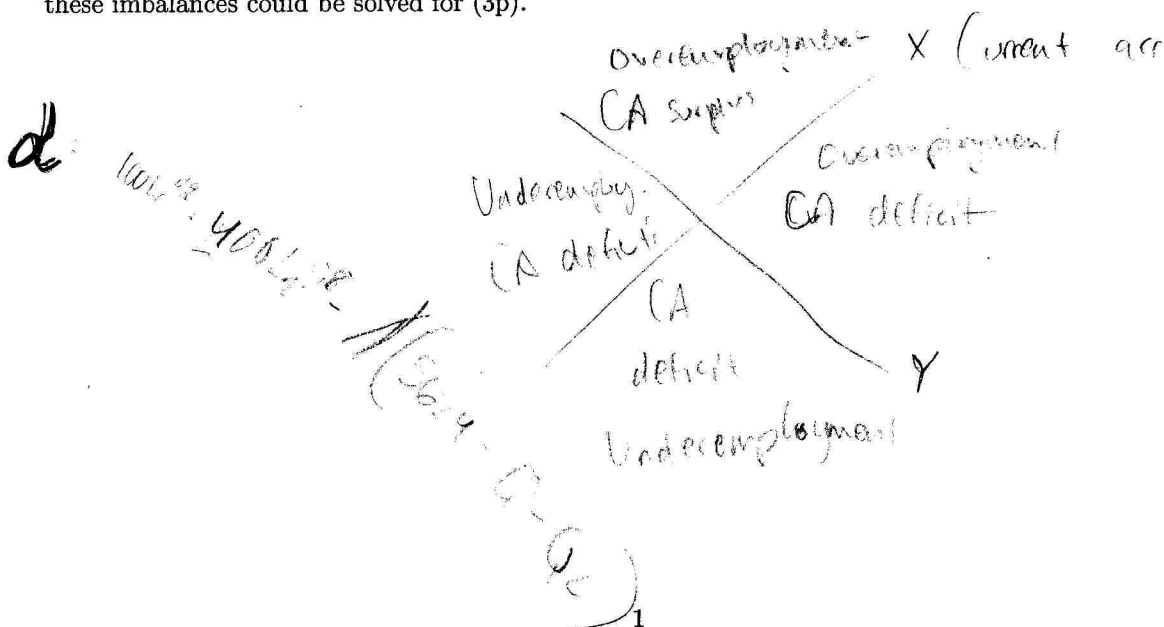
Figure 1: Graph for question 4

5. Home's demand & supply for wheat are given by:

$$D = 100 - 20p, \qquad S = 20 + 20p$$

Foreign's demand & supply for wheat are given by:

$$D^* = 80 - 20p^*, \qquad S^* = 40 + 20p^*$$

1. In the absence of trade what are the prices in Home and Foreign for wheat? Suppose we have free international trade in the wheat market. 2. What is the world market price for 1 unit of wheat? 3. How much wheat is traded internationally? 4. What are the welfare gains from free international trade, for Home and Foreign respectively? 5. How are the welfare effects distributed among the producers and consumers, in Home and in Foreign respectively (Hint. Graph the domestic demand supply schedule in one graph and the Foreign schedule in an other. By imposing the world market price in the models argue how big the welfare gains are) (15p)

$100 - 20p + 80 - 20p = 20 + 20p + 40 + 20p$

$100 - 20p + 80 - 20p - 20 - 20p \ 40 - 20p \qquad = 0$

$-20p - 20p - 20p - 20p \qquad\qquad = -100 - 80 + 20 + 40$

$-40 \qquad = -120$

$\qquad\qquad \approx ?$

2