**Exam SØK2006 – Winter 2021**

Professor: Gonzalo Dona

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| *For each of the questions in this exam you should keep in mind always:*   * *Models, graphs, and theory are ALWAYS necessary and good. Even better when explicit.* * *Short and clear answers are encouraged.* * *Keep your mind open to ideas from every side.* * *Note: I can only give points to non-blank answers* |

1. Explain why it is said that free trade is always beneficial. Choose the best model for the purpose seen in class to fundament your answer. (25pt)

**A: students must use the Ricardian model, and develop it to show how both parties benefit. A perfect answer uses the right model, solves for it using an example, and concludes clearly and unambiguously from the result.**

1. Given that trade is always beneficial for the countries involved (as you just showed) What is the most common reason there are groups opposing free trade? Use a model learned in class to fundament your answer. (15pt)

**A: students should use the specific resource or HO model to show that trade brings with it a redistribution. From this result they should be able to conclude that the losers are likely to oppose free trade.**

1. Explain terms of trade, use a graph. Show in the graph what happens when the ToT worsen for a country. (10pt)

**A: just define terms of trade (Pe/Pi), show in a graph how welfare can be increased when they increase. Three elements: BC (autarky), BC (trade, a straight line with ToT slope), and indifference curve). Besides all standard requirements of any graph**

1. Suppose there are very important economies of scale involved in producing goods that are intensive in low skill labor. Show why a tariff might end up being ineffective in increasing home production in this case. (20pt)

**A: Key element is a graph showing that a tariff that is not enough to eliminate the cost advantage between cost at current production in place A and cost at zero production in place B will not effectively promote local production.**

1. A lot of debate was raised by the decision of the US Government (Trump administration) of introducing **retaliatory** tariffs against countries that they perceived behaved unfairly, most notably China. You should use what we have discussed in class, but not limit yourself to it. Remember both China and the US are real countries that will be with us for a very long time. Argue FOR the Trump tariffs. (30pt)

**A: Make the following points: eliminate or reduce current protectionism from China, eliminate or reduce abuses from China (theft too), collect revenue (US would get a transfer from Chinese producers), get a long-term benefit at a short-term cost, benefit its low-skilled labor. Considering the question, students should refrain from criticizing the tariffs other than to make an argument or as a secondary thought.**