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**UNIVERSITY OF LONDON**

**279 0016 ZA**

**BSc degrees and Diplomas for Graduates in Economics, Management, Finance and the Social Sciences, the Diploma in Economics and Access Route for Students in the External Programme**

**International Economics**

Wednesday, 24 May 2006 : 2.30pm to 5.30pm

Candidates should answer **FOUR** of the following **TEN** questions: **QUESTION 1** of Section A (40 marks) and **THREE** questions from Section B (20 marks each).

**Candidates are strongly advised to divide their time accordingly.**

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## SECTION A

Answer all **eight** parts of question 1 (40 marks in total).

1. Consider each of the statements listed in (a) to (h) below. For each statement indicate whether you consider it to be true, false or uncertain. You should support your decision by writing a brief justification or explanation. *Unsupported answers will receive no marks.*
  - (a) It is possible for a country to have an absolute advantage in all goods, but a comparative advantage in none.
  - (b) China has an abundant supply of labour. An increase in Chinese exports of labour-intensive goods will increase wages in China.
  - (c) Countries with similar production structures and patterns of trade benefit the most from customs unions.
  - (d) An import-competing producer always prefers an import quota to an import tariff.
  - (e) If Uncovered Interest Parity fails to hold, then there must be unexploited free arbitrage opportunities in the foreign exchange market.
  - (f) If the Law of One Price holds, then Purchasing Power Parity (PPP) must also hold.
  - (g) A devaluation of the exchange rate will eventually improve the economy's current account.
  - (h) Under a currency board arrangement, the domestic monetary authorities give up control of the money supply.

## SECTION B

Answer **three** questions from this section (20 marks each).

2. 'Free movement of goods in international trade is basically a substitute for free movement of factors of production'. Discuss.
3. Why is intra-industry trade a problem for conventional trade models based on comparative advantage? How can we explain this sort of trade? Can the two types of trade be reconciled?

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4. Suppose world agricultural trade were to be fully liberalized. Examine the likely welfare effects for developed and developing regions. Why has progress in trade negotiations aiming towards the liberalization of agricultural trade been so slow?
5. EU enlargement will eventually give rise to free movement of labour within the enlarged EU. Who will be the winners and losers of the resulting migration in the short-run and long-run? What effects are there for 'sending' and 'host' countries? Will the EU gain as a whole?
6. Economists generally support a policy of free trade. Why is free trade hardly ever observed in practice?
7. What are the effects of the Stability and Growth Pact for Eurozone countries in the event of asymmetric shocks? In light of your answer, discuss the case for fiscal federalism in Europe.
8. How can we reconcile Optimum Currency Area (OCA) theory with the existence of single currencies over quite different geographical areas (for example, the Euro in the Eurozone)?
9. Excessive exchange rate volatility is often put forth as an argument in favour of fixed exchange rates. Use a model to explain why exchange rates may overshoot their long-run value in the short run, giving rise to excessive volatility.
10. Using the AA/DD framework, discuss the effects of an increase in the nominal interest rate by the monetary authorities.

END OF PAPER