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UNIVERSITY OF LONDON

279 0016 ZB

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.

PLEASE TURN OVER

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) If productivity is high enough in all sectors, a country can have a comparative advantage in all goods.
 - (b) Suppose that Australia has an abundant supply of land relative to labour. An increase in Australian inward migration will improve the Australian trade balance at unchanged terms of trade.
 - (c) The optimum tariff is always positive.
 - (d) The effective rate of protection can never be negative.
 - (e) If interest rates in Japan are less than in the US then the foreign exchange markets expect the US dollar to appreciate against the yen.
 - (f) If a country is observed to run a current account surplus this implies that its government is also running a budget surplus.
 - (g) Fiscal policy is always more effective than monetary policy.
 - (h) In the AA/DD model a permanent increase in the money supply leads to an equivalent permanent depreciation of the exchange rate.

SECTION B

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

2. 'The main propositions of the Heckscher-Ohlin model fail empirically because the assumptions of the model are unrealistic'. Discuss.
3. Explain how trade based on comparative advantage generates gains from trade. In what other ways might trade generate gains?

PLEASE TURN OVER

4. Suppose world agricultural trade were to be fully liberalized. How would that affect the countries of your region? Why has progress in trade negotiations aiming towards the liberalization of agricultural trade been so slow?
5. What factors give rise to foreign direct investment (FDI)? How would you assess the gains and costs of FDI for the sending and host countries?
6. Suppose a quota on an import good is replaced with a tariff that yields the same domestic price as occurs with the quota. Examine the welfare effects on the domestic economy of such a switch.
7. Does the persistence of a bilateral China/US trade surplus imply that the Chinese currency is undervalued? Explain your answer.
8. Outline the progress of economic integration in your region. Why is it less than appears to be the case in Europe?
9. What determines exchange rates in a regime of floating 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 to examine the effects of:
 - (a) a temporary fiscal contraction.
 - (b) a permanent fiscal contraction.

END OF PAPER