AFRICAN ECONOMIC RESEARCH CONSORTIUM

Collaborative PhD Programme in Economics for Sub-Saharan Africa

COMPREHENSIVE EXAMINATIONS IN CORE AND ELECTIVE FIELDS

FEBRUARY 13 – MARCH 3, 2017

INTERNATIONAL ECONOMICS

Time: 08:00 – 11:00 GMT **Date: Tuesday, February 21, 2017**

INSTRUCTIONS:

Answer a total of **FOUR** questions: **ONE** question from Section A, **ONE** question from Section B, and **TWO** questions from Section C (which must be either Question 5 or 6 AND Question 7 or 8).

The sections are weighted as indicated on the paper.

Section A: (15%)

Answer only ONE Question from this Section

Question 1

Distinguish between inter-industry trade and intra-industry trade. Explain three factors that can give rise to intra-industry trade. **[15 marks]**

Question 2

(a) Distinguish between covered and uncovered interest parity. **[5 marks]**

(b) Explain the main idea behind the Monetary approach to the balance of payments. **[5 marks]**

(c) Explain the purchasing power parity theorem. **[5 marks]**

Section B: (25%)

Answer only ONE Question from this Section

Question 3

(a) Explain how a tariff can lower the domestic price of the imported good in a large country case. **[22 marks]**

(b) Is the Stolper-Samuelson theorem still valid under this situation? **[3 marks]**

Question 4

Using the monetary approach to balance of payments, illustrate and explain the effects of a monetary expansion under fixed exchange rates. **[25 marks]**

Section C: (60%)

Answer TWO Questions from this Section;

Which Must be Either Question 5 or 6 AND Question 7 or 8

Choose EITHER Question 5 or 6

Question 5

(a) Is trade liberalization the only ingredient for high economic growth? Discuss with reference to African countries. **[15 marks]**

(b) Using a hypothetical example, explain the concepts of trade creation and trade diversion in a customs union. **[15 marks]**

Question 6

Consider the respective profit functions of a home firm and a foreign firm that are specified as:

$$\pi(x,y,s) = xp(x+y) - c(x) + sx$$

$$\pi^*(x,y) = yp(x+y) - c^*(y)$$

The firms compete for sales in the market of a third country. The duopolists do not sell any output in their own domestic markets. An export subsidy is granted to the home firm by the home country government. [Where *c(x)* is the cost function (starred for the foreign firm), *p(x +y)* is the inverse demand for the good and the variable s stands for the specific subsidy provided by the home government. The domestic firm produces commodity x and the foreign firm produces y; and $p = p(q)$, $q = x + y$, $dp/dq = p'$].

(a) Derive the basic solution of the model. **[10 marks]**

(b) Determine the impact of the subsidy on the output of the home and foreign firms. **[10 marks]**

(c) Graphically interpret your results in (b) above. **[10 marks]**

Choose EITHER Question 7 or 8

Question 7

The following money demand functions represent the simple monetary model of exchange rate determination:

$$m_t^D - p_t = \alpha_1 y_t - \alpha_2 i_t,\ \alpha_1, \alpha_2 > 0$$

$$m_t^{D*} - {p_t}^* = \alpha_1 {y^*}_t - \alpha_2 {i_t}^*$$

where the asterisks denote foreign variables.

(a) Clearly outlining the assumptions, derive the exchange rate equation. **[10 marks]**

(b) Explain fully how each of the domestic variables affects the exchange rate in (a) above. **[10 marks]**

(c) Using the flexible price monetary model (FLMA) in the steady-state, illustrate and explain the adjustments to a once-and-for-all unanticipated permanent increase in the relative monetary growth. **[10 marks]**

Question 8

(a) Discuss the impact of the global financial crisis on African markets. [**20 marks**]

(b) Examine Africa's policy responses to the global financial crisis. [**10 marks**]