

MSc in International Shipping, Finance and Management

Full-Time Program

SAMPLE EXAM: International Economics

PART I. Choose your correct answer for each of the statements below

- 1. A tariff of €5 per unit of imports by a small country will:**
 - (a) increase the domestic price of the imported good by €5, and leave unchanged the international price to foreign producers
 - (b) increase the domestic price of the imported good by €5, and reduce the international price received by foreign producers
 - (c) increase the domestic price of the imported good by €5, and leave unchanged the price received by domestic and foreign producers
 - (d) increase the domestic price of the imported good by €3, and leave unchanged the price received by domestic and foreign producers

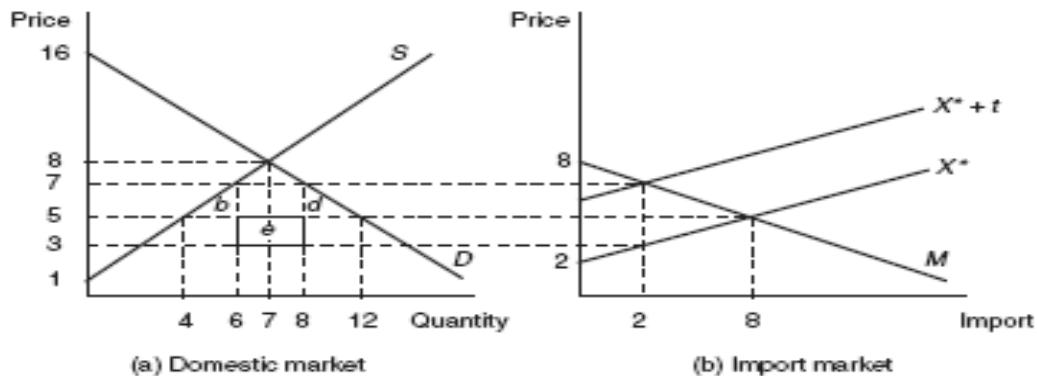
- 2. If the dollar ____ from 1.0 Euro per dollar to 0.9 Euros per dollar, the Euro ____ from 1.0 dollar to 1.1 dollars per Euro.**
 - (a) appreciates; appreciates
 - (b) appreciates; depreciates
 - (c) depreciates; depreciates
 - (d) depreciates; appreciates

- 3. If the interest rate on euro-denominated assets is 7 percent and it is 5 percent on dollar-denominated assets, and if the dollar is expected to appreciate at a 4 percent rate, for Francois the Frenchman the expected rate of return on dollar-denominated assets is**
 - (a) 11 percent, (b) 9 percent, (c) 3 percent, (d) 1 percent

- 4. If the domestic (annual) interest rate is 7%, the rest of the world interest rate is 2%, the one year expected exchange rate (number of units of domestic currency that exchange with one unit of foreign currency) is 200, then UIP implies:**
 - (a) the current exchange rate will be about 190
 - (b) the current exchange rate will be about 210
 - (c) the current exchange rate will be about 195
 - (d) the current exchange rate will be about 205

- 5. Assume UIP, and that the current (spot) exchange rate is equal to the expected future exchange rate. A sudden revision of the beliefs about the future expected exchange rate, e.g., because of an unanticipated event like an earthquake, leads to:**
 - (a) an equi-proportional change in the spot exchange rate in the opposite direction
 - (b) an equi-proportional change in the spot exchange rate in the same direction
 - (c) a more than proportional change in the spot exchange rate in the same direction
 - (d) a more than proportional change in the spot exchange rate in the opposite direction

The following information relates to questions (6)-(7): The diagrams below describe the market for an imported commodity in, Home, a **large open economy**.



6. Assume the free trade world price is $p_w = €5$. Then, the free trade consumer surplus (CS) and producer surplus (PS) are:

(a) CS = 50 and PS = 20 (b) CS = 20 and PS = 50
 (c) CS = 66 and PS = 8 (d) CS = 15 and PS = 25

7. Home government imposes a non-prohibitive tariff $t = €4$. As a result, Home experiences an overall welfare:

(a) Gain of €4 (b) Loss of €2 (c) Loss of €6 (d) Gain of €8

8. A country produces two commodities (X, Y). If the relative price of X is $(p_X / p_Y) = 2/3$, which of the following sentences can be true:

(a) $MPL_X = 12$ and $MPL_Y = 8$ (b) $MPL_X = 8$ and $MPL_Y = 12$
 (c) Labor units per unit of X is 0,0833 and per unit of Y is 0,125
 (d) answers (a) and (c)

9. A tariff per unit on imports by a large country:

a. raises consumers' surplus abroad and lowers it domestically
 b. reduces consumers' surplus domestically and abroad
 c. increases producers' surplus domestically and abroad
 d. transfers the cost of the tariff to producers and consumers in the exporting country

10. In a small open economy supply for the imported good is perfectly inelastic (vertical line). An import tariff creates a welfare loss of (the lectures' notation):

i. $(c + d)$ ii. $(a + b + d)$ iii. $(a + c)$ iv. $(a + c + d)$

PART II: Briefly state your opinion (True/False, Why) for each of the following statements.

1. A country gains from international trade when it produces and consumes beyond its autarky production (and consumption) possibilities frontier.
2. Covered Interest Parity (CIP) holds when expected returns on domestic and foreign deposits are equal, even though exchange rate risk is not hedged.
3. Foreign exchange forward and futures contracts both eliminate exchange rate risk by fixing a future exchange rate, and therefore both are standardized instruments traded on organized exchanges with active secondary markets.

PART III (3.5 points): Choose to answer ONE of the following problems

A. Consider two countries Spain (*S*) and Italy (*I*), which produce and consume two goods, olives (*O*) and cheese (*C*). For good “C” its price is $p_c = 1$. Labor (*L*) is the only factor of production in the two countries. Spain’s labor force is $\bar{L}^S = 360$ work hours (w.hrs) and Italy’s is $\bar{L}^I = 600$ (w.hrs).

a. Autarky: Spain uses-up 300 w.hrs in the production of “O” producing $Q_O^S = 60$ units of this good. The production of “C” is $Q_C^S = 15$ units. Italy uses-up 300 w.hrs in the production of “O” producing $Q_O^I = 150$ units of the good. The production of “C” is $Q_C^I = 100$ units. What is the opportunity cost of a unit of “O”, and equivalently, the opportunity cost of a unit of “C” in each country?

b. Free trade: Free trade commences between the two countries at a world relative price of “C” equal to 1.2 “O”.

i. Describe the pattern of absolute and comparative advantage in the two countries. How does the countries’ size, *i.e.*, the size of their labor force, affects the pattern of comparative advantage between them? Calculate the levels of production of the two goods.

ii. At this new world relative price, the “C”- exporting country consumes 70 units of “C”. Calculate the levels of consumption, exports, and of imports of the two goods between the two countries.

B. Consider today that you noticed the following exchange rate quotations in the stock markets of New York and Frankfurt: $E_{\text{€}/\$} = 0.830$, $E_{\text{€}/\text{CAD}} = 0.661$ and $E_{\$/\text{CAD}} = 0.792$. (Note: CAD – Canadian dollar)

- a.** Calculate if there is any opportunity for arbitrage.
- b.** If there is an arbitrage opportunity, what steps will you take to make an arbitrage profit, and how much will it be, if you have \$1,000,000 available for this purpose.
- c.** What happens if you initially were to sell US\$ for €?