

## **ECON3315: INTERNATIONAL ECONOMIC ISSUES – Fall 2017**

### **ASSIGNMENT 2**

DUE Tues December 5th (in my CoB mailbox or under my office door by 4pm, or by 11.59pm if submitted on turnitin.com)

1. For each of the following identify in which part of the balance-of-payments accounts it appears (current account, capital account or financial account) and whether it is a credit or debit in the US's balance of payments:
  - a. An American resident's sale of a share of Johnson & Johnson stock by transferring funds from a bank account
  - b. An French woman's purchase of an airline ticket from United Airlines (a US airline company)
  - c. The Swiss government's purchase of US Treasury bills in exchange for US\$ reserves.
  - d. A US importers purchase of Saki (rice wine) from Japan
  - e. \$50 million of foreign aid to Haiti
  - f. A loan by an American bank to a Mexican company.
2. During the gold standard era, most currencies were tied to the price of gold. What is the exchange rate between US dollars and Norwegian krona if one dollar is convertible into 1/10th ounce of gold and one Swiss franc is convertible into 1/40th ounce of gold?
3. Given the foreign exchange rate table H1 published by the Federal Reserve (see <http://www.federalreserve.gov/releases/h10/current/>), calculate cross rates for a specified date for the table for:
  - a) Mexican peso per Swedish krona
  - b) Swiss franc per Euro
  - c) New Zealand dollar per Canadian dollar
  - d) Japanese yen per South African Rand
  - e) Australian dollars per Chinese yuan
4. The following questions refer to the reading I circulated entitled "Why isn't the whole world developed?"
  - a. What does the geography hypothesis state?
  - b. What does the culture hypothesis of development state?
  - c. How does the institutions hypothesis explain the difference in prosperity among nations?

5. Suppose the country, Burondo, is one of the poorest countries in the world. Its economy is heavily reliant on income from the export of oil. There are only two oil extracting companies in Burondo. Both are owned by the government. A large part of the earnings from oil exports go toward financing the President's lifestyle and entourage. Burondo has not had a single democratic election ever since it gained independence fifty years ago. Although Burondo is said to have abundant oil resources, only a small proportion is extracted every year because the extraction process is so inefficient. Transporting goods in and out of the country is costly, as Burondo is surrounded by lofty mountain ranges. The gross enrolment ratio in this country is very low and as a result, most of the adult population is illiterate. Life expectancy is also quite low. Agriculture is collectivized in Burondo and so, food shortages are common in the country.

Using the information given, distinguish between the fundamental and proximate causes of prosperity (or its absence) in Burondo.

6. Look at the following map of Nogales, a twin city that is divided by the U.S. border.

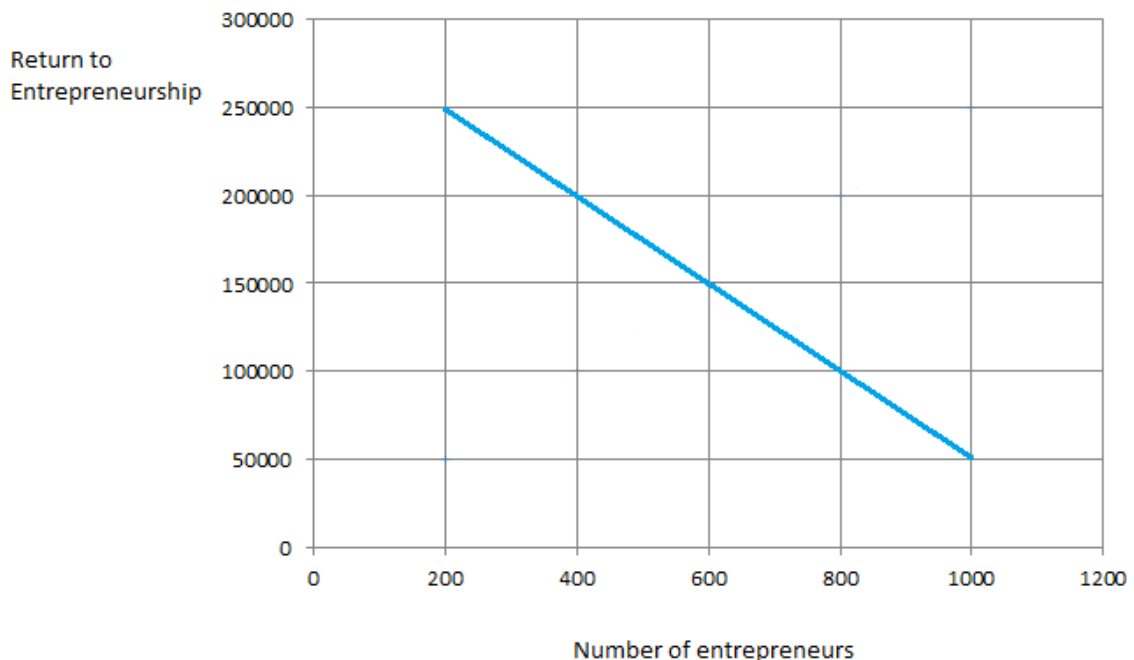


One part of Nogales lies in the U.S., in Arizona, and the other part lies in Sonora, Mexico. Life in Nogales, Mexico is very different from life in Nogales, Arizona. The average income in Nogales, Mexico is about one-third the average income in Nogales, Arizona. Education levels, life expectancy, and health conditions are better in Nogales, Arizona than in Nogales, Mexico. Unlike Nogales in Arizona, Nogales in Mexico has only recently adopted political reforms, bringing it closer to functioning as a democracy. The law and order situation and crime rates are also relatively better in Nogales, Arizona than in Nogales, Mexico. Since both cities are located so close to each other, they share similar geographical conditions and climate. The

inhabitants of both cities also share a common ancestry and enjoy the same type of food and music. Based on this information and your own research, what factors do you think can explain why Nogales, Arizona is so much more prosperous than Nogales, Mexico?

7. Zimbabwe, formerly known as Rhodesia, was a British colony for around ninety years. It became independent in 1980. The then Prime Minister of newly-formed Zimbabwe, Robert Mugabe, implemented a forced land redistribution policy, where commercial farms were confiscated from white farmers and turned over to black Zimbabweans. Mugabe also proceeded to confiscate shares in companies that were not owned by black Zimbabweans. In the following years, agricultural production in the country fell sharply. Zimbabwe, the country that used to be called the breadbasket of Africa, is now seeing food shortages in certain parts of the country.
  - a. Would Zimbabwe be considered to have extractive or inclusive institutions? Explain your answer.
  - b. Why would a government undertake policies that would adversely affect the lives of its citizens?
8. a. The following graph shows the return-to-entrepreneurship curve in a certain country.

If the opportunity cost of entrepreneurship in this country is \$150,000, find the equilibrium level of entrepreneurship in the economy.



- b. Suppose the government of this country decided to expropriate the assets of private firms. Expropriation means that the government buys the assets of private firms, even if the owners are unwilling to sell to the government. Other things remaining unchanged, what do you think will happen to the equilibrium level of entrepreneurship in the economy? Use the graph to explain your answer.
  
- c. The government reduces the fee that needs to be paid to obtain a trade license in this country. Other things remaining the same, how will this policy affect entrepreneurship? Use your graph from part a. to explain your answer.

Patrick Crowley  
November, 2017

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Patrick Crowley, November 2017.