Bachelor of Arts Examination, 2017

(3rd Year, 6th Semester)

Economics (Honours)

International Economics II

Time : Two hours Full Marks : 30

*Answer **question No. 1** and **any two** questions*

1. Answer any four:
   a) Derive the condition that guarantees stability of balance of payments equilibrium.
   b) When exchange rate is fixed, it is possible for a small economy to determine its own rate of interest? Justify.
   c) The home economy purchases a factory in the foreign country. Where is the return on the factory purchased accounted for in the home country's balance of payments accounts? Give reasons for your answer.
   d) In an economy with output being more than full employment and balance of payments deficit, will an increase in taxes be an appropriate policy to reach full employment and balance of payments equilibrium?
   e) How will a permanent increase in money supply growth in the foreign country impact on the real home-to-foreign exchange rate? Give reasons for your answer.
   f) What is forward exchange rate? What is meant by covered interest parity condition? 2.5x4=10

2. a) In the presence of repercussion effects, show that the equilibrium is dynamically stable. What condition guarantees the stability of the equilibrium?
   b) Again in the presence of repercussions effects, if the pattern of spending in the home country changes from domestic to imports, will there be a change in the world market equilibrium condition? Justify.
   c) Will such a shift in the expenditure pattern, as described in 2(b), lead to a change in the equilibrium income of both the countries?
   d) If at the initial equilibrium as in 2(b), the home savings propensity changes relative to the foreign propensity to save in the ratio of 3:4, how does the equilibrium get affected? 3+2+2+3

3. a) In an open economy with government and rest of the world, show that the long run equilibrium relationship is necessarily in terms of savings and investment.
   b) What will be the impact of balance of payments surplus on the macroeconomy In the presence of sterilization?
   c)In terms of this relationship in (a), what are the macroeconomic implications for an open economy with large current account deficit? Does it address the "twin deficit" problem often faced by an open economy? 3+3+4

4. (a) Is the short-run equilibrium in an open economy involving the output and asset markets always stable?

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b) What kind of changes in output and exchange rate can be brought about with a temporary increase in government expenditure?
c) How does the open economy adjust to permanent changes in fiscal policy?
d) The open economy introduces permanent changes in monetary policy when confronted with recession following contraction of demand. How does the open economy adjust to such changes? 2+2.5+2.5+3

5. a) An open economy, in the short-run, is away from the equilibrium at a point with excess demand for goods and excess supply of the economy's currency in the asset market. Will the economy come back to the equilibrium in the short run? Justify your answer.

b) Can expansionary monetary policy restore full employment equilibrium if there is a temporary decline in demand for goods produced in the home country? Justify your answer.

c) How does the open economy adjust in the long-run to the permanent increase in money supply? 3+3+4