MACHAKOS UNIVERSITY

University Examinations for 2019/2020 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

THIRD YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS AND STATISTICS

BACHELOR OF ECONOMICS

EAE 307: INTERNATIONAL ECONOMICS 1

DATE: 21/1/2021   **TIME: 2.00-4.00 PM**

INSTRUCTIONS:

  (i)   **Answer question one (Compulsory) and any other two questions**

  (ii)   **Do not write on the question paper**

  (iii)   **Show your working clearly**

QUESTION ONE (COMPULSORY) (30 MARKS)

a)   Clearly distinguish between International Trade and International Finance   (2 marks)

b)   Using well labeled diagrams for country A and country B, explain how specialization and trade along lines of comparative advantage can increase the total world output of the two goods (X, Y) available for consumption. Country A has comparative advantage in production of good X and country B has comparative advantage in production of good Y.
        (6 marks)

c)   If the price of an imported HP computer is 1000 dollars under free trade, and the domestically assembled Mercer computer is made using 500 dollars worth of hardware and 200 dollars worth of software:

Calculate the effective rate of protection (ERP) for the Mercer computer if a 10% tariff is imposed on HP computers, 5% tariff on imported hardware and 8% tariff on imported software used in assembling Mercer computers in Kenya.   (6 marks)

d)   Explain Mercantilist beliefs' challenges   (5 marks)

e)   Explain the effect of a quota on International Trade with help of a well labeled   diagram

(8 marks)

f)   State three main properties of indifference curves   (3 marks)

QUESTION TWO (20 MARKS)

a)   Explain four main reasons why countries impose tariffs   (4 marks)

b)   Using mathematical expression show and clearly explain how David Ricardo's theory of comparative advantage is an improvement on Adam Smith's theory of absolute advantage

(10 marks)

c)   Explain three main types of dumping   (6 marks)

QUESTION THREE (20 MARKS)

a)   (i)   Define "Terms of Trade"   (2 marks)

(ii)   A country's terms of trade and imports is as shown in the table below:

Terms of Trade	Demand for Imports	Supply of Exports
1X: 1Y or $P_X/P_Y = 1$	20 Units	-
1X: 2Y or $P_X/P_Y = 2$	32 Units	-
1X: 3Y or $P_X/P_Y = 3$	90 Units	-
1X: 4Y or $P_X/P_Y = 4$	140 Units	-

A.   Calculate the country's respective exports   (2 marks)

B.   Show the country's Offer Curve in a well labeled diagram   (6 marks)

b)   Explain Paul Krugman's model based on monopolistic competition   (10 marks)

QUESTION FOUR (20 MARKS)

a)   Explain the the Imitation Lag Theory of Trade   (8 marks)

b)   Explain Paul Samuelson's Factor Price equalization theory (1948)   (8 marks)

c)   Explain the Leontief Paradox   (4 marks)

QUESTION FIVE (20 MARKS)

a)   Using a well labeled diagram explain welfare effect of a tariff on a small country. (8 marks)

b)   Use modern concept of opportunity cost to explain the theory of comparative advantage

(6 marks)

c)   Explain various beliefs of Mercantilism theory   (6 marks)