INSTRUCTIONS TO CANDIDATES:

1. Please read all instructions carefully before answering the questions.

2. This paper consists of 10 pages and 3 compulsory sections. Please ensure that you have all of them.

3. Section A consists of fifteen questions and students must answer ALL questions on the MCQ sheet.

4. Section B consists of five questions and students must answer ALL questions.

5. Section C consists of two questions and students must answer ONE question.

6. Please use separate answer books for EACH SECTION.
SECTION A

- Answer ALL the multiple choice questions (Section A) on the MCQ answer sheet provided.
- Please note negative marking does not apply.
- Each question in this section is worth 3 marks.

Question 1 is based on the diagram below.

1. Refer to the figure above, which shows a country's possible production possibility frontiers and indifference curves. If the country is producing at ________, then moving to ________ will cause utility to ________.
   A) point b; point c; remain unchanged
   B) point c; point b; increase
   C) point c; point b; decrease
   D) point a; point c; remain unchanged
   E) point d; point e; increase

2. Use the information given in the table below to answer the question (Q1).

<table>
<thead>
<tr>
<th>Output per Hour</th>
<th>United States</th>
<th>South Africa</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computers</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Shoes</td>
<td>6 pairs</td>
<td>3 pairs</td>
</tr>
</tbody>
</table>

Which country or countries has an absolute advantage and comparative advantage in shoes?
A) South Africa has an absolute and comparative advantage in shoes.
B) The United States has an absolute and comparative advantage in shoes.
C) The United States has a comparative advantage and South Africa has an absolute advantage in shoes.
D) South Africa has a comparative advantage and the United States has an absolute advantage in shoes.
E) Both South Africa and the United States have a comparative disadvantage and absolute disadvantage in shoes.
3. The graphs below show domestic supply and demand curves for a good in two countries, with prices measured in the same currency.

If these are the only two countries in the world and if they open to free international trade:
A) Consumers of the good in Country B will benefit from trade.
B) Producers of the good in Country B will benefit from trade.
C) The welfare of Country A as a whole will fall.
D) The quantity of the good demanded in Country B will become larger.
E) The price of the good in both countries will be the one labeled PB.

4. The Stolper-Samuelson Theorem predicts
A) which factors are abundant.
B) the income distribution effects of trade.
C) which goods will be exported.
D) which goods will be imported.
E) the importance of intra-industry trade.
5. Factor Price Equalisation means that,

A) All workers are equally productive.
B) If a country fails to trade, its skilled workers will earn no more than its unskilled workers.
C) Trade causes the return to human capital to be the same as the return to physical capital.
D) For countries to trade fairly, they must tax factors of production so that firms in all countries pay the same factor prices.
E) Free trade causes identical factors in different countries to be paid nearly the same as they would be in autarky.

6. Trade diversion is likely to be smaller:

A) The closer is the partner’s export price to the tariff-inclusive price for imports from countries outside the bloc.
B) The more elastic is import demand
C) The less elastic is import demand
D) The higher is the country’s tariff rate on the product
E) The lower is partner cost compared to outside-world cost

7. Suppose that the world price of automobiles is $10000 and domestic producers of automobiles use $5000 worth of imported inputs and no domestic inputs. What rate of effective protection would be provided to the domestic auto industry by a 25% tariff on imported automobiles and a 50% tariff on inputs?

A) -0.25
B) 0
C) 0.25
D) 0.50
E) 1

8. The macroeconomic view of a trade deficit implies that, other things equal, the imposition of a tariff will reduce South Africa's trade deficit.

A) Because exports will be promoted and imports cannot possibly change
B) Because imports will be reduced and exports cannot possibly change
C) Only if the tariff has no impact on South Africa's spending or income
D) Only if the tariff leads to increased income in South Africa relative to its spending
E) Only if the tariff leads to increased spending by South Africa relative to its income
9. Which of the following is False about the equation \( GL_i = 1 - \frac{|X_i - M_i|}{X_i + M_i} \)?

A) If \( X = M \), then this implies that all of the industry’s trade is intraindustry.
B) If either \( X < M \) or \( M < X \), then this necessarily implies that \( GL > 1 \).
C) The GL index is in general greater in high technology industries.
D) The equation is also known as the Grubel-Lloyd index
E) The equation can measure the relative importance of intraindustry trade.

**Question 10** is based on Figure 10.1 below. Figure 10.1 illustrates good X market for Utopia a "small" country. Suppose the rest of the world can supply good X to Utopia at a price of $1 per unit.

**Figure 10.1: Utopia’s good X Market**

10. Referring to the above Figure, the imposition of an import quota equivalent to a 100% ad valorem tariff, limits imports to ______ good X. If the government auctioned off import licenses to highest bidder, the revenue effect would be $______.

A) 55 ; 50
B) 50 ; 100
C) 20 ; 100
D) 30 ; 30
E) 50 ;100
Question 11 is based on Figure 11.1 below. Figure 11.1 illustrates the domestic market for wheat in a small country.

![Figure 11.1](image)

11. According to the above Figure 11.1, the net loss in national welfare as a result of the subsidy is:
A) $200 millions
B) $300 millions
C) $400 millions
D) $500 millions
E) $2.2 billions

12. In balance-of-payments accounting, the sale of a foreign production facility by a SA firm is a _________ item in the SA balance of payments; the deposit of funds in a foreign bank account by a SA citizen _________ item in the SA balance of payments.
A) Debit; also is a debit
B) Debit; is a credit
C) Credit; is a debit
D) Credit; also is a credit
E) Non recorded; is also a non recorded

13. In which of the following relationships between the expected future spot rate \(E(e)\) of a foreign currency and the current forward rate \(E(f)\) of a foreign currency would a speculator have an incentive to buy foreign currency in the forward market?
A) \(E(e) < E(f)\)
B) \(E(e) > E(f)\)
C) \(E(e) = E(f)\)
D) \(1/E(e) = 1/E(f)\)
E) \(1/E(e) = E(f)\)
14. As long as governments allow free trade, the law of one price works well for _______traded commodities.
   A) all
   B) rarely
   C) heavily
   D) cheaply
   E) domestically

15. An increase in capital inflows in South Africa will result in a(n)_______foreign currency and a(n)_______the South African Rand in the foreign exchange market.
   A) increase in the demand for; increase in the supply of
   B) increase in the supply of; increase in the demand for
   C) shortage of; surplus of
   D) surplus of; shortage of
   E) decrease in the supply of; decrease in the demand for
SECTION B

- You must answer **All** questions in this section.
- For each question, state whether you regard the question as **True** or **False** AND **Substantiate** your answer in not more than five sentences. Think carefully before answering each question.
- Each question in this section is worth 5 marks.

1. Free trade can hurt people in the import-competing industries in the short run, but in the long run, everybody ends up gaining from free trade.

2. According to the Heckscher-Ohlin theory, countries should engage in a lot of intra-industry trade,

3. Refer to the Figure 3.2 below. As a result of specialization and trade, cloth production in the world is increased by 3 yards.

![Figure 3.2](image)

4. The law of one price holds better for gold than for Big Mac burgers.

5. If the European Union (EU) removes export subsidies on sugar. This will definitely raise the price of sugar in the EU and reduce it in the rest of the world.
SECTION C

- This section contains a choice of questions. You must answer **One** of the following two questions.
- Read all the questions carefully.
- Each question selected is worth 30 marks.

QUESTION 1

In 1970, one major dumping case was brought against Sony of Japan. Sony was selling televisions made in Japan to the United States consumers for $180 while charging Japanese consumers $333 for the same model. In response to the threat issued by the United States government, Sony shifted its supply for the United States market to a factory built in California, but did not change the prices of televisions in either country.

(i) What are the two official definitions of ‘dumping’?

(ii) Outline the main reasons why an exporting firm might engage in dumping.

(iii) In the case of Sony, evaluate the conditions required to make this type of dumping profitable? Make use of diagrams in examining this question.

QUESTION 2

Use the figure below describing the simultaneous equilibrium of the Forex and U.S. Money markets, to explain the impacts of income growth and monetary policy changes on the nominal exchange rate of the U.S. dollar to the euro (E$/€), the return on U.S. monetary assets (R$) and prices in the U.S. in both the short-run and the long-run of the events identified:

![Diagram](image-url)
(a) The U.S. monetary authorities increase the money supply. (5)

(b) Explain what is meant by the notion of exchange rate overshooting, and identify clearly with reference to the figure what causes this overshooting to take place. (10)

(c) The relative income of U.S. citizens increases due to rising productivity levels in the U.S. relative to Europe. (5)

(d) If the U.S. dollar's nominal value were pegged to the Euro, identify and explain clearly what actions U.S. monetary authorities would need to undertake to maintain the pegged rate following the event identified in part (c) above. Would the actions by the monetary authorities have any effect on the U.S dollar's real value relative to the Euro? Explain. (10)