Name ______________________________ University ID_______________

ECON 4311 – Fall 2023 Final
Economy of Latin America
December 18, 2023

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Allowed utensils: Pen, paper, eraser, and non-graphic calculator.

General Instructions:

- You have 1 hour and 15 minutes (from 17:00 to 18:15) to complete the exam.
- Do NOT remove the staple from your examination sheets.
- The exam consists of 25 multiple choice questions (each worth 2.8 points) and 6 free-response questions, (each worth 5 points).
- There is only one (1!) valid answer per multiple choice question (MCQ), and no points will be subtracted for wrong answers.
- Answer all MCQ questions in the sheet provided below.
- If you make a mistake in answering a MCQ and want to change the answer, do cross the 4 options (A, B, C, D) and clearly write on the right of box D the letter of your final answer.
- Be short and to the point in the free-response questions.
- Make sure to submit all pages of your examination.

Good luck!

MCQ Answer Sheet

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How to answer:

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Questions:

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Multiple Choice Questions (MCQ): 70 points

1. Select the correct answer. Adam Smith challenged the view that countries could increase welfare with mercantilism. To challenge this view, he used the concept of:
   (a) Absolute advantage.
   (b) Comparative advantage
   (c) Both (a) and (b) are correct.
   (d) None of the above.

2. Select the *correct* answer about most-favored-nation (MFN) status.
   (a) MFN status is a principle of non-discrimination that eliminates tariffs so that foreign producers can compete in equal conditions with domestic producers.
   (b) MFN status is a principle of non-discrimination that eliminates quotas so that foreign producers can compete in equal conditions with domestic producers.
   (c) MFN status is a principle of non-discrimination that ensures that the nation with MFN status gets as high of a quota as that placed on any contracting party involved in trade with the country granting MFN.
   (d) MFN status is a principle of non-discrimination that ensures that the nation with MFN status gets as low of a tariff as that charged to any contracting party trading with the country which grants MFN.

3. According to the Heckscher–Ohlin model, what causes differences across countries in opportunity costs of producing goods?
   (a) Factor abundance.
   (b) Factor intensity.
   (c) Changes in the distribution of wages.
   (d) Both (a) and (b) are correct.

4. The entry "unilateral transfers" is reflected in national accounts in:
   (a) The financial account.
   (b) The current account.
   (c) The FDI account.
   (d) None of the above.

5. Select the correct answer. The Bretton Woods' system:
   (a) It was a system of international payments that linked foreign currencies to the USD, and the USD to gold.
   (b) It was a system of international payments that allowed currencies to fluctuate within 1% of the fixed exchange rate.
   (c) It is a dollar-pegged exchange-rate regime
   (d) All of the above.

6. The terms of trade of Argentina today could be computed as Argentina's
   (a) Import prices divided by export prices times 100.
   (b) Export prices divided by import prices times 100.
   (c) Export prices divided by the sum of export and import prices times 100.
   (d) Import prices divided by the sum of export and import prices times 100.
7. Which of the following best describes the concept of domestic currency appreciation.
   (a) It takes more foreign currency to acquire 1 unit of domestic currency.
   (b) It takes more domestic currency to acquire 1 unit of foreign currency.
   (c) It takes less domestic currency to acquire 1 unit of foreign currency.
   (d) None of the above.
8. Select the correct answer. La Década Perdida (The Lost Decade):
   (a) Has its roots in the large amounts of money that Latin American countries borrowed in the 1960s and the 1970s to promote ISI.
   (b) Is a sovereign debt crisis that resulted in a decade of missed growth.
   (c) Required the intervention of foreign governments such as the US government to be resolved.
   (d) All of the above.
9. Which of the following occurred in the 1980s and compromised the position of Latin American countries in international markets:
   (a) Higher commodity prices.
   (b) Political instability in East Asia.
   (c) Volcker shock.
   (d) None of the above.
10. Most countries in the world learned a lesson from the trade war of the 1930s and started liberalizing their economies, but Latin America did not. Why?
    (a) Structuralism.
    (b) Old tradition of high tariffs and quotas.
    (c) Latin America already enjoyed a liberalized economy.
    (d) Both (a) and (b) are correct.

11. Why should we (1) expect higher FDI investments in Latin America than in high-income economies, and (2) why has there been scarce FDI investment?

    (a) (1) MPK(Latin America) $>$ MPK(high-income economies), and (2) due to corruption and high criminal activity.

    (b) (1) MPK(Latin America) $<$ MPK(high-income economies), and (2) due to corruption and high criminal activity.

    (c) (1) MPK(Latin America) $>$ MPK(high-income economies), and (2) due to political instability and ISI policies.

    (d) None of the above.

12. How has capital flown historically into the Latin America region?

    (a) Mostly in the form of debt.

    (b) Mostly in the form of FDI.

    (c) Mostly in the form of portfolio capital.

    (d) None of the above.

13. Select the correct answer. Flexible exchange rates:

    (a) Are rates of exchange between domestic and foreign currencies determined by market conditions.

    (b) Are rates of exchange between domestic and foreign currencies determined by a "pegged system" to another currency or basket of currencies.

    (c) Were adopted by all countries which participated in the system of Bretton Woods.

    (d) None of the above.

14. An interesting fact about the Latin America region is that from 1990 to 2014, remittances as a share of the world total:

    (a) Have grown, almost doubling from 5 to 10%.

    (b) Have shrank, almost halving.

    (c) Have remained roughly constant.

    (d) None of the above.

15. Which of the following conclusions from "*How Has NAFTA Affected the Mexican Economy?*" by Meredith et al. is correct:

    (a) NAFTA had a net negative impact in the Mexican economy.

    (b) NAFTA substantially boosted FDI in Mexico.

    (c) NAFTA decreased TFP in Mexico.

    (d) None of the above is correct.

16. "*Lessons from the Monetary and Fiscal History of Latin America*" by Esquivel, Kehoe and Nicolini (2020) teaches us that:

    (a) Countries that have excessively high levels of foreign-denominated currency debt are more prone to exhibit large rates of economic growth.

    (b) Commodity prices were the main factor determining the economic fate of Latin American countries.

    (c) An increased level of fiscal discipline generally leads to increased levels of macroeconomic stability.

    (d) None of the above.

17. From '*The Monetary and Fiscal History of Argentina, 1960–2017*" by Buera and Nicolini we learn that:

    (a) Despite large fiscal deficits during the past, Argentina has a low debt burden today.

    (b) Once confronted with fiscal deficits, Argentina's governments have been vert able to tame them.

    (c) Argentina has typically shown good economic performance during periods of hyperinflation.

    (d) Fiscal deficits drive inflation throughout Argentina's history.

18. Debt monetization consists in:

    (a) Selling more bonds or raise further taxes to finance public spending.

    (b) Borrowing more money from international markets to finance public spending.

    (c) Borrowing more money from the central bank to finance public spending.

    (d) None of the above.

19. Which of the following is true about the Brazilian stabilization plans of the 1980-90s?

    (a) Most plans were successful in controlling inflation for sufficiently long times.

    (b) Not all plans had effects of inflation rates.

    (c) Brazil went through 6 different official currencies in less than a decade.

    (d) None of the above.

20. Select the correct answer.

    (a) Dollarization can help reduce borrowing costs.

    (b) Dollarization, as well as a currency union, places restrictions on monetary policy.

    (c) The most common way of assessing a country's degree of dollarization is to look at the ratio of deposits in foreign currency to total deposits.

    (d) All of the above.

21. According to "*Dollarization in Argentina*" by Velde and Veracierto (2005):
    (a) Argentina considered pegging the Argentinian peso to the dollar using a 1-to-1 exchange rate.
    (b) Argentina's convertibility plan included reforms to reduce the government's budget deficit, promote trade liberalization, and deregulate the banking industry.
    (c) Both (a) and (b) are correct.
    (d) None of the above.

22. Which of the following is true about full dollarization.
    (a) It is associated with price stabilization.
    (b) It reduces macroeconomic uncertainty in dollarized countries.
    (c) It is associated with increased investment (both domestic and foreign) and decreased borrowing costs in dollarized countries.
    (d) All of the above.

23. Select the correct answer.
    (a) In comparison to European counterparts, Latin American governments are very effective in reducing income inequality with redistribution policies.
    (b) In comparison to the rest of the world, Latin America presents low rates of absolute poverty.
    (c) Although Latin America has substantially reduce the level of economic inequality during the past two decades, it is still today the most unequal world region.
    (d) Both (b) and (c) are correct.

24. Select the correct answer about relative poverty.
    (a) It is an ideal measure to make cross-country comparison when it comes to poverty.
    (b) It can result in outcomes such as two countries with the same distribution of income having different levels of relative poverty.
    (c) All countries provide clear definitions of relative poverty.
    (d) None of the above.

25. Which of the following, if any, are causes of poverty and inequality in Latin America?
    (a) Long history of extractive institutions.
    (b) Import Substitution Industrialization.
    (c) Dual labor markets and tedious business regulations.
    (d) All of the above.

Short Questions: 30 points

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1. **Use diagram(s) to compare a situation of autarky with one of free-trade, and explain the effects of opening up to trade on equilibrium prices and quantities for a country who is disadvantaged in the production of that good, as well as the associated welfare gains and losses.** *Clearly indicate what each object in the graph is, and explain the nature of welfare losses/gains.*

2. **Assume money velocity grows at 2% per year, and real GDP is expected to grow at 4%. At what rate should the monetary authority make the money supply grow in order to achieve price stability?** *Show every step of your calculations.*

3. **Suppose the Mexican government has committed to a fixed exchange rate of 2P/\$. A recent policy from the United States has prohibited the importation of Mexican products. Since Mexico's export revenues come in its majority from the United States, the exchange rate will be affected. Illustrate this effect in a graph, and also illustrate what the Mexican government needs to do in order to keep a fixed exchange rate.** *You need to indicate what each object in the graph is, and also discuss policy actions in words.*

4. **State *clearly* the Stolper–Samuleson, and provide an example that can help us understand that theorem and its implications.** *Extra: 2 bonus points if both theorem and example clear and complete.*

5. **Explain the different forms of debt financing in international capital markets, and give one example for each type.**

6. **Explain the different types of exchange-rate regimes, and illustrate graphically the main differences between them in the face of fluctuations in economic conditions. Give one example for each type of exchange-rate regime.** *You need to indicate what each object in the graph is, and discuss policy actions in words.*