

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 150 points (to be scaled up to 210 points) and is scheduled to take 75 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I can give extra time but not much.

1) (12 points) For EITHER the method of resolving a debt crisis in Part A OR the method in Part B, explain how it works and why a creditor might be willing to do it.

- A) Refinancing the debt.
- B) Deb-equity swaps.

2) (12 points) Answer EITHER Part A OR Part B.

- A) There is a moral hazard problem with doing what is described in Question #1, Part A. Explain what the moral hazard is and why it may cause problems in the future.
- B) When we calculated comprehensive wealth, we used the term “natural capital”. What does that mean and why is it important for the economy in the future?

3) (14 points) For EITHER the tax in Part A OR the tax in Part B, determine if you think it is a good tax. Make sure you discuss whether it meets two of the requirements for a good tax. You can choose which two.

- A) tax on all international trade
- B) tax on pollution

4) (14 points) For EITHER the situation in Part A OR the situation in Part B, explain why it is a potential problem. Also determine if it is an illiquidity problem or a insolvency problem. Explain your logic.

- A) NPV of debt/exports is 300%.
- B) Debt service/revenue is 17%.

5) (14 points) Answer EITHER Part A OR Part B.

- A) What is meant by the ANS Gap? Write the formula for it and state why each term is important.
- B) How can regulating pollution achieve the optimal amount of pollution? Would you recommend this method to a developing country? Explain your logic.

6) (14 points) Answer EITHER Part A OR Part B.

- A) 70% of the US government budget is considered “non-discretionary”. These are bills that have to be paid like Social Security, Medicare, Medicaid, and interest payments. Are they current expenditures or a recurrent expenditures? Explain your logic. Give an example of the other type of expenditure and state why that is in the other category. So, if “non-discretionary” expenditures are current, give an example of recurrent and if they are recurrent, give an example of current.
- B) What are SOEs? How do they affect the budget? Why do they have that impact?

7) (14 points) Answer EITHER Part A OR Part B.

- A) Explain one of the ways that micro-finance occurs. Why is that method of finance successful?
- B) Explain two reasons why informal financial markets are necessary in developing countries.

8) (16 points) Answer EITHER Part A OR Part B.

A) Explain how large reserve requirements can cause shallow finance. Why is shallow finance bad for the economy?

B) One of the tools of the central bank is open market operations. Explain how the central bank could use that to fight inflation. Why would it have the desired effect?

9) (16 points) For EITHER the item in Part A OR the item in Part B, define it and state both how it can help the developing country and how it can hurt the developing country.

A) Joint venture requirements

B) Domestic content laws

10) (24 points) Answer EITHER Part A OR Part B.

A) Draw the MEC/MAC diagram the way I drew it in class. Explain why the MAC line looks as drawn. Explain why points to the left of where the curves cross are not optimal.

B) Draw the Environmental Kuznets Curve for a race to the bottom. Explain why it takes its shape. Do you think this is a likely scenario? Explain your logic.