

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 I won't give much.

1) (12 points) Answer EITHER Part A OR Part B.

A) The book says that one determinant of which countries get the most ODA is *foreign policy objectives*. Explain why this is true, including an example.

B) The book says that one determinant of which countries get the most ODA is *country size*. Explain why this is true, including an example.

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

A) Explain how informal regulations can reduce pollution. What should Congress do that could help the process? State why that is important.

B) Argentina currently has hyper-inflation. If they do not want to get rid of their own currency, what can the BCRA (the Argentinian central bank) do to stop the problem? Tell me which tool you are proposing they should use, how they should use it, and why that would have the desired effect.

3) (12 points) Answer EITHER Part A OR Part B.

A) Why do we have different definitions of money, for example, M1, M2, and M3?

B) What are the three uses of money? For ONE of them, does M1, M2, or M3 do a better job? Explain your logic.

4) (14 points) Answer EITHER Part A OR Part B.

A) Suppose you are in charge of a poor country and there is a creditor panic starting, where the creditors are selling off your country's assets. Which of the four ways in the book to respond would you do? Why would you do that? How would that be good in the long-run?

B) When a country is likely to default on its loans and bonds, sometimes, the borrower will convince the lenders to reduce the debt by writing off some of the debt. Why would the lenders be willing to do that?

5) (16 points) Answer the question referring to two of the criteria we give for a good tax. Answer EITHER Part A OR Part B.

A) For a general sales tax, what is one criterion which it is good at? Explain your logic. What is one criterion which it is bad at? Explain your logic.

B) For a property tax, what is one criterion which it is good at? Explain your logic. What is one criterion which it is bad at? Explain your logic.

6) (16 points) Answer EITHER Part A OR Part B.

A) According to the IMF, there are eight countries in West Africa that use the currency, West African CFA Franc. According to Wikipedia, there had been several other countries which were in that arrangement but left and started their own currencies. Do you think the ones who stayed in the arrangement or the ones who left the arrangement to start their own currencies, made the better decision? Explain your logic.

B) If you were a coup leader forming a new government of a poor country, how would you determine

whether you would have some type of pegged exchange rate (peg, adjustable peg, or crawling peg) or some type of floating (clean or dirty aka managed) exchange rate? I am asking for one aspect of the country which would help you to decide which is best. For example, it might be the percentage of people who are left-handed (although, that would be a stupid one). How would that aspect of the economy determine the exchange rate regime which you feel is best? Explain your logic.

7) (16 points) Answer EITHER Part A OR Part B.

A) Economists often complain that too much of poor countries' budgets are spend on state-owned enterprises (SOEs). Why do they cost the government? Is that a current or recurrent expenditure? Explain your logic.

B) Economists often complain that too much of poor countries' budgets are spend on wages. Why do economists say that? Is that a current or recurrent expenditure? Explain your logic.

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

A) An economist writing in the Colombo Telegraph (a Sri Lankan newspaper), recently argued that the IMF loan will not help Sri Lanka and implies that he thinks the country will be worse off because of it. Obviously, you know nothing about that situation, but what do you guess is the logic he used? Explain your logic. Do not go to it now, but the article can be found at:

<https://www.colombotelegraph.com/index.php/debt-divestiture-discontent/>

B) Your book says one thing which can be done to increase the probability that ODA will help the country, is to have recipient participation. Give two reasons how that would make the aid more effective.

9) (18 points) For EITHER of the criteria below, explain why that is an indication that the country is in serious trouble. Is that a problem of illiquidity or insolvency? Explain your logic.

A) the debt service/revenue is greater than 10% - 15%

B) The short-term foreign debt/foreign exchange reserves approach a 1 to 1 ratio

10) (18 points) Answer EITHER Part A OR Part B.

A) Draw the MEC/MAC diagram. Use it to prove that the current method of regulating pollution is not the least costly way to get to the optimal point.

B) Draw the MEC/MAC diagram. Use it to explain how cap-and-trade of permits can achieve the optimal point with the least costs.