MACHAKOS UNIVERSITY

University Examinations for 2018/2019 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

THIRD YEAR SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS

EAE 307: INTERNATIONAL ECONOMICS I

DATE: 24/7/2019 **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) i)In a world of two countries A and B and two goods X and Y, write in algebraic terms, statement "good Y is capital intensive" and "good X is labor intensive" (2 marks)

ii) Define "factor abundance" according to:

- The price-based definition (1 mark)
- The quantity-based definition (1 mark)

iii) By stating Adam Smith's theory of absolute advantage and David Ricardo's theory of comparative advantage, give the difference between them (3 marks)

iv) Give five positive and three negative contributions of international trade to Kenya's economy (4 marks)

b) i) Use the concept of opportunity cost (OC) to demonstrative that Uganda and Kenya can gainfully exploit their respective comparative advantage in their resource endowment to benefit from trade. (6 marks)

ii) Give price-based definition of dumping (2 marks)

c) If the price of an imported HP computer is 2000 dollars under free trade, and the domestically assembled Mercer computer is made using 1000 dollars worth of hardware and 400 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. (10 marks)

QUESTION TWO (20 MARKS)

a) Highlight and clearly explain the three mercantilist trade policies and practices that are still key cornerstones in Kenya's trade policies?
(6 marks)

b) Use examples to explain the difference between specific and Ad Valorem tariffs

(4 marks)

c) Using a well labeled sketch diagram, show the welfare effect of imposing a tariff on an imported good by a small country (Kenya) (10 marks)

QUESTION THREE (20 MARKS)

a) Outline and briefly explain the main assumptions of Heckscher – Ohlin model

(5 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 based on effort of another country used to produce good X in the home country (14 marks)

QUESTION FOUR (20 MARKS)

a) Briefly explain two non-tariff barriers (4 marks)

b) Give two main reasons that explain the inter-industry trade between countries with the same level of economic development (2 marks)

c) Name and explain three types of dumping (6 marks)

d) Outline four major competing explanations for the Leontief paradox (8 marks)

QUESTION FIVE (20 MARKS)

a) Use an appropriate diagram to show the tariff revenue effect following the imposition of a tariff on an imported good by a small country (10 marks)

b) Use factor equalization theory to show that in theory with the normal working of the East African Community, wages and interest rates in the five member countries should be the same. (10 marks)