

INTERNATIONAL MONEY AND FINANCE

Exercises for Chapter 1

Answers

1. What do you understand by globalisation?

Globalisation refers to the dynamic process driving the international integration of goods, services and financial markets. As the very term suggests, globalisation has been far reaching geographically, affecting lifestyles, production, consumption and work practices in all hemispheres of the world. It means that economies have become far more interdependent as a result of greatly increased flows of exports, imports, foreign investment and other financial flows. With increased international economic interdependence, production, spending and finance are less constrained by political borders.

2. What were Adam Smith, David Ricardo and John Stuart Mill's arguments for international trade?

Trade allows greater specialisation in production, which in turn expands markets, lowers costs and prices, and raises income in the long term.

3. Briefly summarise economic arguments for and against globalisation.

For:		Against:
➤ Efficiency; specialisation therefore wealth generation.	and	➤ Equity; income distribution.
➤ Increase in total output.		➤ Environmental and other externalities.
➤ Maximise consumer choice.		➤ 'Protectionist' arguments such as foreign investment.

4. *Discuss the fundamental drivers of globalisation.*

The fundamental drivers of globalisation have been technological advance and liberalisation of international markets for goods, services and finance.

5. *Give an example of how financial and economic fluctuations in an economy's trading partners significantly affect domestic asset values and economic activity.*

China's large stimulus package in answer to the global financial crisis and strong growth over the last few decades created an investment boom for Australia.

Countries with large debt levels in Europe gave Germany, an exporting country, a competitive advantage with the depreciation of the Euro.

The Asian financial crisis resulted in the depreciation of the Australian dollar and an increase in competitiveness.

6. *Download exports, imports and international capital flows for USA, China and Argentina and discuss the difference. Is there data for North Korea and Zimbabwe?*

It should be clear, that countries with greater international trade are stronger economies than economies with little trade.

7. *The ratio of an economy's exports and imports to its national income is indicative of openness. Calculate this for the countries in the above question. How do all the countries compare economically?*

It should be clear, that countries with greater international trade are stronger economies than economies with little trade.

8. *What are the implications for increased international capital mobility and how does this occur?*

International capital mobility results in a closer relationship between domestic and world interest rates.

9. *What do you understand by the Tinbergen rule? How is Figure 1.2 compatible with the Tinbergen rule? How does this apply for Europe?*

Jan Tinbergen formally established that macroeconomic policy could not adequately hit its policy targets, unless the authorities controlled at least as many policy instruments. This raises questions over Europe's ability to help the individual countries in its union economically.

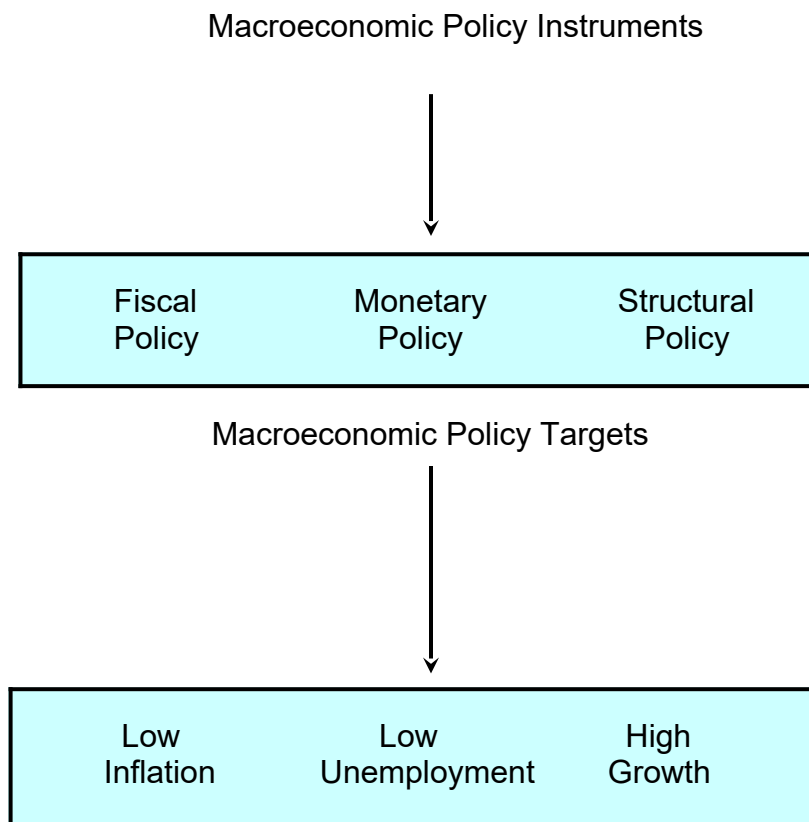


Figure 1.2 Macroeconomic policy instruments and targets

10. How does financial globalisation affect this rule?

The application of the instruments will be profoundly affected through international capital flows and exchange rate fluctuations.

11. What are some of the similarities and difference between globalisation now and in the late 1800s?

Similarities	Differences
➤ Substantial movement of people. People have knowledge. ➤ Spurred by rapid development in technology, particularly transport and communication. ➤ International capital flows. ➤ % of production of tradable goods.	➤ Smaller geographical area of globalisation in the 1880s. ➤ There are well-established supranational institutional framework fostering international economic exchanges. In contrast, in the first globalisation era, all economic institutions were strictly nationally based and no independent authorities existed to oversee the economic conduct of participants in international exchange.