

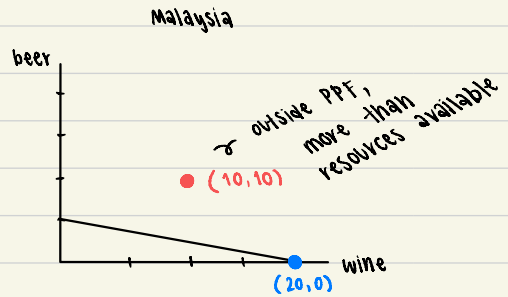
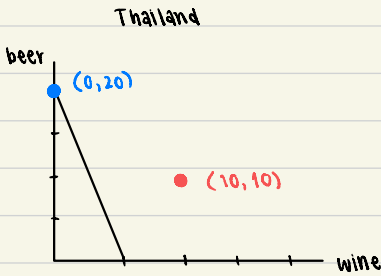
Exercise 8 -

- absolute advantage = able to use fewer resources to produce a good  
 comparative advantage = able to produce at a lower opportunity cost  
 all countries will gain from free trade + specialization

2.

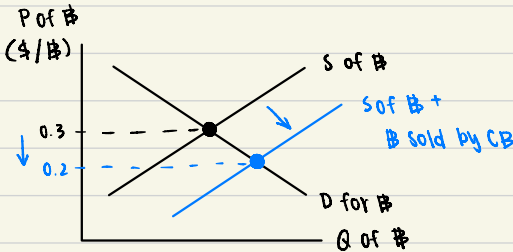
	Thailand		Malaysia	
Beer	4	20	1	5
Wine	1	5	4	20

- specialization
- specialization + free trade



- CA surplus : trade surplus ( $X > M$ ), primary & secondary income inflows > outflows  
 KA deficit : Increase in ownership of foreign assets, money is flowing out  
 BOP Identity : In theory,  $CA + FA = 0$

4.



฿ devaluation:

CB sells THB and buys USD  
 (foreign reserves) to increase  
 supply of ฿

5. floating ER regime : equilibrium exchange rate is purely determined by demand & supply model with no government intervention

-  $X \uparrow$ ,  $D \uparrow$ , appreciation

-  $S \uparrow$ , depreciation

- unstable economic / political situation, discourages foreign investors,  $D \downarrow$ , depreciation

6. Inflation  $\Rightarrow$  appreciation :  $i = r + \pi$  so  $i \uparrow \rightarrow$  attracts foreign investors  $\Rightarrow D \uparrow$

depreciation : domestic goods become more expensive  $\Rightarrow X \downarrow$ ,  $M \uparrow \rightarrow D \downarrow$

7. PPP = 400 USD : 300 GBP

$$1.33 \text{ USD} : 1.00 \text{ GBP} = \underline{1.33 \$ / \pounds}$$

8.  $NER = 40 \text{ \$/\pounds}$       1 apple = 20  $\text{\$}$  & 1  $\pounds$

$$RER (\text{\$/\pounds}) = 40 \times \frac{1}{20} = \underline{2}$$

9. LOP assumes that transportation costs are small  $\Rightarrow$  price of similar goods are almost the same in different countries