Exercise 8

International Economics

1. What is the difference between “absolute” and “comparative” advantages? What are the main implications of these two theories? (i.e. what do they suggest?)

2. The table below shows the amount of production that <u>one worker</u> in each country can produce. Assume that each country has 5 workers. **<u>Draw a PPF and show</u>** that both countries will benefit from trade.

	Thailand	Malaysia
Beer	4	1
Wine	1	4

3. What do “current account surplus” and “capital account deficit” represent? What is the “Balance of Payment Identity”?

4. Suppose the current market exchange rate is \$0.3 / 1 Baht. Use the foreign exchange market diagram to explain how the Central Bank of Thailand can “devalue” Thai baht to \$0.2 / 1 Baht under the fixed exchange rate regime.

5. How does the floating exchange rate regime work? Under such regime, how does each of the following events affect Thai Baht (assumed to be a domestic currency)?
   - The rest of the world imports more from Thailand.
   - More Thai investors invest abroad.
   - Thailand will leave ASEAN (similar to the UK leaving the EU).

6. In the floating exchange rate regime, why might inflation cause a currency to appreciate and depreciate?

7. Suppose an iPhoneX is priced at 400 USD in the US and 300 GBP in the UK. Calculate the PPP exchange rate between USD and GBP.

8. Suppose the nominal exchange rate is 40 THB / 1 GBP. One apple costs 20 THB in Thailand, but costs 1 GBP in the UK. Calculate the real exchange rate.

9. What assumptions are required for the Law of One Price to hold?

1. What is the difference between "absolute" and "comparative" advantages? What are the main implications of these two theories? (i.e. what do they suggest?)

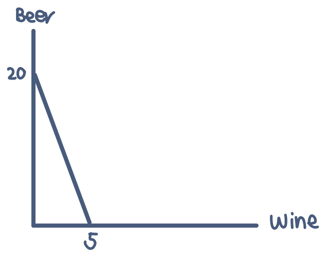
absolute advantages — when one country use a fewer resources of production than other country.

comparative advantages — when one country produce a good at lower oppatunity cost than other country.

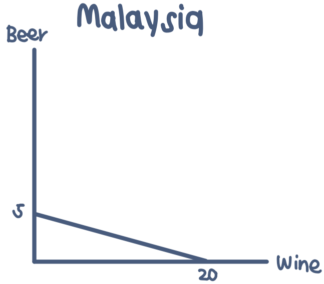
2. The table below shows the amount of production that <u>one worker</u> in each country can produce. Assume that each country has 5 workers. **<u>Draw a PPF and show</u>** that both countries will benefit from trade.

	Thailand	Malaysia
Beer	4	1
Wine	1	4

Thailand



Malaysia



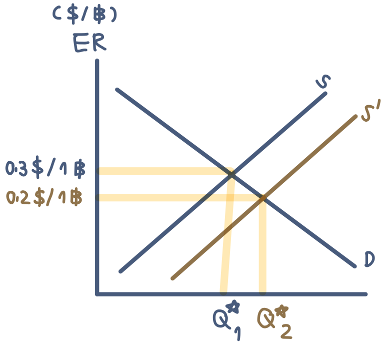
3. What do "current account surplus" and "capital account deficit" represent? What is the "Balance of Payment Identity"?

current account surplus : when we have exports > imports

capital account deficit : when we have outflow > inflow

Balance of payment identity is CA+KA = 0, when we have current account surplus while capital account deficit.

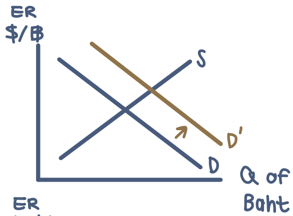
4. Suppose the current market exchange rate is \$0.3 / 1 Baht. Use the foreign exchange market diagram to explain how the Central Bank of Thailand can "devalue" Thai baht to \$0.2 / 1 Baht under the fixed exchange rate regime.



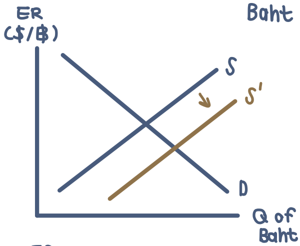
CB can devalue Thai Baht by increasing supply of baht. CB will sell baht and buy more USD. This will lead to depreciation in USD.

5. How does the floating exchange rate regime work? Under such regime, how does each of the following events affect Thai Baht (assumed to be a domestic currency)?
   - The rest of the world imports more from Thailand.
   - More Thai investors invest abroad.
   - Thailand will leave ASEAN (similar to the UK leaving the EU).

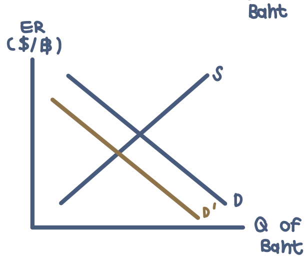
Floating Exchange Rate Regime : demand & supply curve which can change because some factor can affect demand & supply of currency. And we have to know that who demand ฿ and who supply ฿.

1. 

Demand in ฿ will increase, so ฿ will appreciate because the rest of the world want ฿ more.

2. 

supply of THB will increase, so ฿ will depreciate because Thai investor want to buy other currencies for investing.

3. 

when Thailand left ASEAN, it means that other ASEAN country will not want ฿ anymore, so demand of ฿ will decrease. THB will depreciate.

6. In the floating exchange rate regime, why might inflation cause a currency to appreciate and depreciate?

- Inflation makes interest rate increase. When interest rate increase, foreigners will want to buy ฿ to invest in Thailand. so when the demand of ฿ increase, THB will appreciate.
- Inflation makes domestic goods are expensive so Thai ppl will want to buy abroad capitals at lower price. As a result, export will be reduced and import will increase so that THB depreciate.

7. Suppose an iPhoneX is priced at 400 USD in the US and 300 GBP in the UK. Calculate the PPP exchange rate between USD and GBP.

$$\frac{400}{300} = \frac{4}{3} = 1.33 \text{ USD} : 1 \text{ GDB}$$

8. Suppose the nominal exchange rate is 40 THB / 1 GBP. One apple costs 20 THB in Thailand, but costs 1 GBP in the UK. Calculate the real exchange rate.

↳ 40 THB

40 THB : 1 GBP

$$\frac{40}{20} = 2$$

9. What assumptions are required for the Law of One Price to hold?

The price of the same good in different country should be the same.