QB365 Question Bank Software Study Materials

International Economics Important 2,3 & 5 Marks Questions With Answers (Book Back and Creative)

12th Standard

Economics

Total Marks : 75

2 Marks

10 x 2 = 20

1) What is International Economics?

Answer : International Economics is a specialized field of Economics that deals with the economic interdependence among countries and studies the effects of such interdependence and the factors that affect it.

2) Define International trade.

Answer : (i) International trade refers to the trade or exchange of goods and services between two or more countries.
(ii) It is a trade among different countries or trade across political boundaries.

3) State any two merits of trade.

Answer : (i) Availability of variety of goods for consumption.
(ii) Generation of more employment.
(iii) Industrialization of backward nations.
(iv) Division of labour and specialisation.

4) What is the main difference between Adam Smith and Ricardo with regard to the emergence of foreign trade?

Answer : (i) According to Adam Smith, the basis of international trade was absolute cost advantage.
(ii) To Ricardo the basis of trade is comparative cost advantage.
(iii) Trade can take place even if the absolute cost difference is absent but there is comparative cost difference.

5) Define Terms of Trade.

Answer : The rate at which goods of one country are exchanged for that of another country i.e. ratio of export price and import price.

6) What do you mean by Balance of Payments?

Answer : (i) The balance between the values of goods and services exchanged between two countries.
(ii) It is a trade in both visible and non visible items.

7) What is meant by Exchange Rate?

Answer : The rate at which one currency is exchanged for another currency.

8) Mention the Similarities of Internal and International Trade.

Answer : (i) Specialization is the basis of both, domestic as well as foreign trade.
(ii) Both have same requisites, viz., two parties, two commodities and determination of relative prices.
(iii) Gains or benefits, is the primary concern of the regions or nations involved in trade.

9) What is internal trade?

Answer : (i) Internal trade refers to the exchange of goods and services within the political and geographical boundaries of a nation.
(ii) It is a trade within a country.
(iii) This is also known as 'domestic trade' or 'home trade' or 'Intra-regional' trade.

10) What is nominal exchange rate?

Answer : (i) If 1 USD = Rs. 75,
(ii) Nominal exchange rare = 75 / 1 = 75

(ii) Nominal exchange rate = 75 / 1 = 75

(iii) This is the bilateral nominal exchange rate.

3 Marks 10 x 3 = 30

11) Describe the subject matter of International Economics.

Answer : Pure Theory of Trade

(i) This component explains the causes for foreign trade, composition, direction and volume of trade, determination of the terms of trade and exchange rate, issues related to balance of trade and balance of payments.

Policy Issues

(i) Policy issues such as free trade vs. protection, methods of regulating trade, capital and technology flows, use of taxation, subsidies and dumping, exchange control and convertibility, foreign aid, external borrowings and foreign direct investment, measures of correcting disequilibrium in BoP are covered.

International Cartels and Trade Blocs

(i) Economic integration, cartels, customs unions, monetary unions, trade blocs, economic unions and multinational corporation are covered

International Financial and Trade Regulatory Institutions

(i) Financial institutions like IMF, IBRD, WTO are part of International Economics.

12) Compare the Classical Theory of international trade with Modern Theory of International trade.

Answer :

S.NO	CLASSICAL THEORY OF INTERNATIONAL TRADE	MODERN THEORY OF INTERNATIONAL TRADE
1	International trade is on the basis of labour theory of value.	International trade is on the basis of general theory of value.
2	It presents a one factor (labour) model.	It presents a multi factor (labour and capital) model.
3	It attributes the differences in the comparative costs to differences in the productive efficiency of workers in the two countries.	It attributes the differences in comparative costs to the differences in factor endowments in the two countries.

13) Explain the Net Barter Terms of Trade and Gross Barter Terms of Trade.

Answer : Net Barter Terms of Trade

1. This was developed by Taussig in 1927.
2. The ratio between the prices of exports and of imports is called net barter terms of trade.
3. Viner calls it commodity terms of trade.
4. $T_n = (P_x/P_m) \times 100$
5. Tn is Net Barter Terms of Trade
6. Px is Index number of export prices
7. Pm is Index number of import prices
8. This measures the gain from International Trade.
9. If T_n is greater than 100, it is terms of trade which means that for a rupee of export, more of imports can be received by a country.

Gross Barter Terms of Trade

1. Developed by Taussig in 1927 as an improvement over the net terms of trade.
2. It is an index of relationship between total physical quantity of imports and the total physical quantity of exports.

$Tg = (Q_m/Q_x) \times 100$

3. Q_m is Index of import quantities
4. Q_x is Index of export quantities
5. If for a given quantity of export, more quantity of import can be consumed by a country, the terms of trade are favourable.

14) Distinguish between Balance of Trade and Balance of Payments.

Answer :

S.NO	BALANCE OF TRADE (BOT)	BALANCE OF PAYMENTS (BOP)
1	Only export and import of commodities are included in BoT	Export and import of commodities and services are included in BoP
2	i.e. Movement of goods or visible trade	Trade in both visible and non visible items.

15) What are import quotas?

Answer : (i) It is a trade restriction that sets a limit on the quantity of a good that can be imported into a country in a given period of time.

(ii) Quotas are used to benefit the producers of good in that economy.

16) Write a brief note on flexible exchange rate.

Answer : Also known as floating exchange rate, the exchange rates are freely determined in an open market by market forces of demand and supply.

17) State the objectives of Foreign Direct Investment.

Answer : FDI has the following objectives.

(i) Sales Expansion

(ii) Acquisition of resources

(iii) Diversification

(iv) Minimization of competitive risk

18) What are the general advantages of International Trade?

Answer : (i) Availability of variety of goods for consumption.

(ii) Generation of more employment opportunities.

(iii) Industrialization of backward nations.

(iv) Improvement in relationship among countries.

(v) Division of Labour and specialisation.

(vi) Expansion in Transport Facilities.

19) State the Correction of Balance of payment Disequilibrium - Trade Measures.

Answer : Trade measures include measures to promote exports and to reduce imports.

1. Export Promotion

Exports may be encouraged by

i) reducing or abolishing export duties,

ii) providing export subsidy,

iii) encouraging export production by giving monetary, fiscal, physical and institutional incentives. (Then local people and domestic industries would suffer)

2. Import Control

Imports may be controlled by

i) imposing or enhancing import duties,

ii) restricting imports through import quotas,

iii) licensing and even prohibiting altogether the import of certain non- essential items. But this would encourage smuggling.

20) Suppose the exchange rate between Indian Currency and US Dollar is Rs. 65 = $1.If it changes to 1$ = Rs. 55, the value of which currency increased or decreased?

Answer : (i) The value of Rs. has increased because now it is enough if we give less Rs. (55) for the same $1.(ii) The value of$ has decreased, so American goods become cheaper.

(iii) It encourages import of American goods.

5 Marks 5 x 5 = 25

21) Explain briefly the Comparative Cost Theory.

Answer : **Introduction**

1. David Ricardo formulated comparative cost theory.

2. J. S. Mill, Marshall, Taussig refined it.

Theory

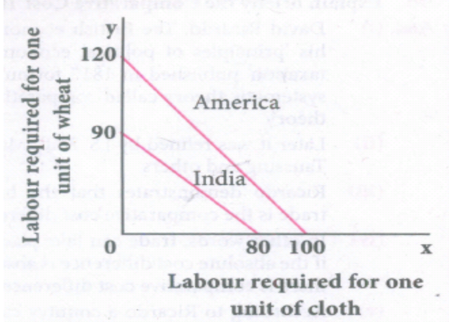
1. Trade can take place even if absolute cost difference is absent but there is comparative cost difference.

Illustration

2. Ricardo's theory is explained with an example of production costs of cloth and wheat in America and India.

(Units of labour needed to produce one unit)

Country	Cloth	Wheat	Domestic Exchange Ratios
America	100	120	1 Wheat = 1.2 Cloth
India	90	80	1 Wheat = 0.88 Cloth



(i) India has absolute advantage in production of both cloth and wheat.

(ii) But, India will produce wheat where she enjoys comparative cost advantage (80 / 120< 90 / 100).

(iii) For America the comparative cost disadvantage is lesser in cloth production.

(iv) So America will specialize in cloth production and export it to India in exchange for wheat.

(v) Both nations gains.

(vi) With trade India can get 1 unit of cloth and 1 unit of wheat by using 160 labour units (80+80). With no trade India has to use 170 units of labour (80+90).

(vii) The same explanation applies to America too.

Criticisms

(i) Labour cost is a small portion of the total cost. So the theory based on labour cost is unrealistic,

(ii) Labourers in different countries are not equal in efficiency.

22) Bring out the components of balance of payments account.

Answer : **Introduction**

(i) The credit and debit items are shown vertically in the BoP account of a country.

(ii) Horizontally, they are divided into 3 components.

Current Account

(i) It includes all international trade transactions of goods and services, international service transactions (tourism, transportation, royalty fees) and international unilateral transfers (gifts, foreign aid).

Capital Account

(i) Financial transactions consisting of direct investment and purchases of interest bearing financial instruments, non interest bearing demand deposits and gold are included.

Official Reserve Assets Account

(i) Consist of movements of international reserves by governments and official agencies to accommodate imbalances arising from the current and capital accounts.

(ii) The official reserve assets include its gold stock, holdings of its convertible foreign currencies, SDR and its net position in the IMIF.

23) Discuss the various types of disequilibrium in the balance of payments.

Answer : **Cyclical Disequilibrium**

Cyclical Disequilibrium occurs because of:

(i) Two countries may be passing through different phases of business cycle.

(ii) The elasticities of demand may differ between countries.

Secular Disequilibrium

(i) It occurs because of long-run and deep rooted changes in an economy as it advances from one stage of growth to another.

(ii) In the initial stages of development, domestic investment exceeded domestic savings and imports exceeded exports, as it happened in India since $1951.

Structural disequilibrium

(i) Structural changes in line economy may also cause BoP disequibrium

(ii) Structural changes include development of alternative sources of supply, development of better substitutes, exhaustion of protective resources or changes in transport routes and costs.

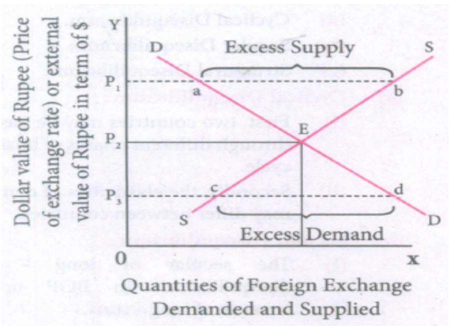
24) How the Rate of Exchange is determined? Illustrate.

Answer : (i) The equilibrium rate of exchange is determined in the foreign exchange market according to the general theory of value, by the interaction of demand and supply,

(ii) Y axis represents exchange rate, be cos value of rupee in terms of dollars

(iii) X axis represents demand and supply of forex.

(iv) E is the equilibrium point where DD intersects SS. The exchange rate is P_2.



25) Explain the relationship between Foreign Direct Investment and Economic development.

Answer : 1. FDI is an important factor in global

2. Foreign trade and FDI are closely related.

3. In developing countries like India FDI in tie natural resource sector like plantations, increases rade.

4. Foreign production by FDI is useful to substitute foreign trade.

5. FDI is also influenced by the income generated from the trade and regional integration schemes.

6. FDI accelerates the economic growth by facilitating essential imports needed for development programs like capital goods, technical know-how, raw materials, other inputs and even scarce consumer goods.

7. When the export earnings of a country are not sufficient to finance for imports, FDI may be required to fill the trade gap.

8. FDI is encouraged by foreign exchange shortage, desire to create employment and acceleration of the pace of economic development.

9. Many developing countries strongly prefer foreign investment to imports.