

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

The review session's time will be determined, probably 4/24.

Chapter 10: How do you do a **project appraisal** using the **cost-benefit analysis** and a **NPV** calculation. This is just like in Chapter 8 except we also have the value of the equipment at the end of the time. What are **opportunity costs** and how do they relate to the **shadow prices**? How do **commercial project appraisal** differ from **economic project appraisal** and **social project appraisal**? Be able to do a calculation like that in the table on Page 357. Why does using the shadow price of labor instead of the wage rate always increase the NPV while using the shadow price of foreign exchange has an ambiguous effect on the NPV? What is **rent seeking**? Why is it bad? (I am not referring to what the Dead Kennedys sing about.) How do the following hurt a country's ability to have entrepreneurs start new companies: **corruption, licenses & permits, laws restricting firing employees, poor courts for enforcing contracts, lack of domestic savings, and taxes on firms**? Explain how MNCs benefit the **host country** through **supplying capital, creating employment, provide expertise, specialization in production, access to the world, and spillovers**. Understand how MNCs hurt the host company by taking profits out of the country, giving the locals less control over decisions, and uneven bargaining power. Understand the pros and cons of the following policies **export process zones, tax holidays, trade barriers, joint venture requirements, and domestic content laws**. Understand what determines the different types of savings: **foreign savings, private domestic savings, domestic government savings, and domestic corporate savings**. For private domestic savings, understand why the **life-cycle model** may or may not hold. If it does not hold, we will use the **Keynesian model of savings** which is  $S = -a + (1-b)(Y - T)$ . What is **Ricardian Equivalence**? Why might it hold and why might it not hold? Understand why  $I = (T-G) + S_p + (M-X)$ . Foreign savings can come in the form of **official savings** and **private savings**. The former is usually **concessional** (gifts or lower interest rates.)

Chapter 11: What are **fiscal and monetary policies**? What is a **public good**? Why should the government provide it? What are the differences between **current** and **recurrent** expenditures? Why do they matter? How do **wages, salaries, capital goods, maintenance, military spending, interest payments, subsidies, state-owned enterprises (SOEs), and intergovernmental transfers** affect the budget? Note that they vary greatly in size between countries, but each type of spending has its own unique properties. What is meant by **tax capacity**? What are the advantages and disadvantages of the following types of taxes: **taxes on international trade, personal & corporate income taxes, and sales & excise taxes** (including VATs)? What is the problem with raising taxes too high? What other sources of taxes might be available? How can changes in tax administration and/or tax reform help the government to collect more money? How do taxes affect saving, investment, income redistribution, and equity? Why might taxes be inefficiently collected?

Chapter 12: What is meant by the **financial system**? How does it relate to **monetary policy**? What are **micro-credit institutions**? What are the **three uses of money**? What is in, and what are the differences between **M1, M2, and M3**? What is meant by **financial intermediation**? How does it affect risk and stabilize the economy when working correctly? What are the problems with **inflation**? In general, what

are the differences between **chronic inflation**, **acute inflation**, and **hyperinflation**? What are the effects of them? What is meant by **fixed (pegged) exchange rate**, **adjustable peg**, **crawling peg**, **managed (dirty) float**, **wide band system**, and **clean float**? What are the advantages and disadvantages of each? What are **international reserves**? Understand why  $M = DR + IR$ . Use it to explain why having a fixed exchange rate causes the central bank to lose control over the money supply. What are the **four tools** the central bank can use to control the money supply. (**Moral suasion** is not in my macroeconomics textbooks because it is ineffective.) How can **credit ceilings** be used to affect the inflation rate? What is meant by **shallow finance** and **financial deepening**? How do the following cause shallow finance: low real interest rates, restrictions on entry to the financial market, and high required reserves? What are **informal credit markets** and **micro-finance**?

Chapter 13: What is the difference between **illiquid** and **insolvent**? What are the advantages and disadvantages of foreign borrowing? For the **six debt indicators on Page 461**, understand why those would indicate too large of a debt, either illiquidity or insolvency and either a **debt service problem**, **external transfer problem**, or **internal transfer problem**. Understand the equations on Pages 462 - 463 and how they relate to the issue, especially 13-2 and 13-4. What is meant by **debt overhang**? What can cause a **debt crisis**? What is the impact upon the country of the crises? How can they get out of the problem? What are the pluses and minuses of the **proposals on Pages 471 and 472**? How can short-term capital flows affect the crises? What is meant by **defensive lending** and **completion point**? Why do they matter? How do short-term loans help the problem? What is a **creditor panic**? What causes it? What can be done about it? What are the advantages and disadvantages of the **solutions on Pages 489-490**? How does **moral hazard** relate to the situations?

Chapter 20: What are **greenhouse gases**? Be able to draw and explain the four different **Environmental Kuznet Curves**. Understand what the terms **comprehensive wealth**, **total wealth**, **produced capital**, **natural capital**, and **intangible capital** and why those are important. Understand how we calculate **saving**, **net saving (NS)**, and **adjusted net saving (ANS)**. Why do we care about ANS and the **ANS Gap** and the **Malthusian term**? What are **externalities** and **common-pool resources (CPRs)**? Understand the problems they cause. Be able to use the S/D (**SMC/PMC/D**) diagram to explain why externalities result in sub-optimal outputs. Explain why the **Coase Theorem** means the end result does not depend upon who has the **property rights**. Understand when it may not hold and why it might not hold then. Be able to use the **MEC/MAC** diagram to find the optimal level of pollution. Understand why the curves look like I drew rather than what the book drew. How can **taxes**, **subsidies**, **tradable permits (cap-and-trade)**, and **regulations** be used to get the market to the optimal point? What are the advantages and disadvantages of them? How might **informal regulation** work? Why is **climate change** such a big problem and why is it hard to address?

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This is the non-graded Assignment #10A that will be reviewed with Assignment #10.

- 1) (15 points each) For each of the following, explain why the criteria would mean the debt is not sustainable. In your explanation, explain whether it is a debt service problem, external transfer problem, or an internal transfer problem. Explain your logic.
  - A) NPV debt/revenue is 250%
  - B) Debt service/exports is 30%
  - C) NPV debt/GDP is 55%
- 2) (20 points) What is a creditor panic? How might restructuring debt eliminate the problem? Explain your logic.

3) (25 points) Bono (singer for U2) has long advocating debt reduction for developing countries to prevent a debt crisis. What is good about that? What is bad about it? Do you agree with him? Explain your logic.

4) (10 points) Explain the difference between being illiquid and insolvent.

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Material on the final exam, but not on Exam #4

Chapter 14: What is *foreign aid*? What is the difference between *concessional* and *non-concessional assistance*? What are **ODA** and **private voluntary assistance**? What are **multi-lateral aid, IMF** and **World Bank**? Why do governments give aid for foreign policy, to fight poverty, to small countries, commercial ties, and to help democracies? Understand the reasons why some people feel that aid is good for the economy, while others think it has little or no effect, and others feel it depends upon certain circumstances. What is the **poverty trap**? Why might the effectiveness of aid depend upon what it is used for and whether or not the money is **fungible**? What is the *principal-agent problem* and how does it relate to the IMF? What can be done to improve the effectiveness of aid? Does **conditionality** affect the effectiveness of the aid? How can **country selectivity, recipient participation, harmonization & coordination**, and **results-based management** improve the results?

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**Questions based on the material after Exam #4**

1) (20 points) Some people feel that all foreign aid other than emergency assistance, like for a drought or tsunami, hurts the country in the long run. Explain their logic.

2) (20 points) What is meant by concessional assistance? Explain why that may work better than non-concessional assistance.

3) (10 points) Why might the fungibility or non-fungibility of aid play a role as to whether the aid will be a net help or a net detriment to the receiving country?

4) (15 points) What is the principal-agent problem? How does it relate to foreign aid?

5) (25 points) Do you think that most non-emergency aid normally helps the recipient country, normally has no long-term impact, or normally hurts the recipient country? Explain your logic.

6) (10 points) Why is harmonization and coordination among donor countries important?