

Take Home Exam – Part II
Due November 25 (Tuesday)

Choose and answer **two** out of the following questions if you are an **undergraduate** student, or **three** if you are a **graduate** student. In your answers, you must present your arguments by resorting to economic theory as much as you can, and be clear on the causality of the events you are referring to. While it is important to bring up historical events (or data) to back up your (theoretical) argument, *merely listing up historical events may not contribute to your grade. **Merely reorganizing the lecture notes available on the course website will not contribute to your grade either.** Again, construct your arguments.* Content errors and misconceptions may lead to reductions in the grade, but more weight will be placed on your argument flows. Having a good balance in presenting big-picture arguments and specific events/policies will always help. This exam is not testing the originality of your answers. ***You should instead refer to the assigned readings*** and other materials to back up your arguments. Please make sure you cite references in appropriate and *consistent* manners and present a bibliography at the end of the exam.

For each question, you must answer within three pages. *Use a #12 font and type in double space.* *If you go over the page limit or use a different font size, points will be reduced.* Do not skip extra lines between paragraphs. *PLAGIARISM WILL LEAD TO A LOSS OF THE GRADE FOR THIS ASSIGNMENT* (not just a question that contains plagiarism). *No information from Wikipedia and any other online encyclopedia shall be used.*

Exams must be printed out (no email or fax please!). You must not consult with your fellow students, but may ask the instructor to clarify what the questions are asking.

You must hand in your exam by or at the beginning of the lecture on the due date. Points will be lowered if exams are handed in any other way.

QUESTIONS:

Question 1

Some people claim that China is to be blamed for the U.S. housing bubble and the resultant subprime crisis. What is their argument? Does the U.S. housing bubble have anything to do with China's economic policy? What is the economic background that has made China implement a policy that may have affected the U.S. economy?

Question 2

Why does the United States keep pressing China to allow exchange rate flexibility? What can happen to the value of the Chinese currency, i.e., the renminbi (人民币) once it is allowed to fluctuate more freely? What would be the potential benefit to the U.S. and China? Would there be any demerits to China? Why do Chinese leaders seem so reluctant to change the

current situation? China currently holds more than \$3.6 trillion of foreign reserves, about 1/3 of which are held in the form of dollar-denominated assets (mainly, U.S. treasuries). Why does China hold such a massive amount of foreign reserves? Are there any incentives for China to reduce dollar-denominated assets? What would be the consequence if China reduced the amount of dollar-denominated assets?

Question 3

China's economic liberalization policy started in 1978. Why did it start in 1978? How was the situation of the Chinese economy? What kind of liberalization policies were implemented? Which sector(s) succeeded (relatively speaking) and which did not?

Question 4

Why are many of the Asian economies, most notably China, holding a massive amount of international reserves? Is their motivation related to the experience of the Asian financial crisis of 1997-98? How did the Asian crisis occur? What could happen to a country with an overvalued currency? What was the role of the IMF? Could the massive international reserves holding by emerging market economies cause any risk or problems in the international financial market or the world economy?

Question 5

What were the merits of joining the World Trade Organization for China? Why did Chinese policy leaders want their country to join the WTO? What kind of merits or demerits did other countries envision for themselves from China's entry to the WTO? Why did some countries oppose the idea? Why did some U.S. politicians oppose to it?