

**INTRODUCTION TO THE ECONOMICS OF DEVELOPING COUNTRIES  
(ECO 2117C, WINTER 2012)**

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**MIDTERM EXAM – ANSWER KEY – VERSION A**

**Part 1: Multiple choice questions**

**Grading: 20 questions, 2.5 points per correct answer**

1. Development economics is the study of the
  - a) alleviation of absolute poverty.
  - b) transformation of institutions.
  - c) allocation of resources in developing countries.
  - d) all of the above.

Answer: D

2. Which measure adjusts for differing relative prices across countries?
  - a) purchasing power parity income levels
  - b) GNP price deflators
  - c) foreign exchange rate conversions to U.S. dollars
  - d) the exchange rate

Answer: A

3. Conditions of today's developed countries at the start of their industrialization differ from conditions in the developing world in that:
  - a) population growth rates were higher.
  - b) more advanced technology was available.
  - c) there were more opportunities for development assistance.
  - d) none of the above.

Answer: D

4. The dependency burden is:
  - a) a measure of the degree to which the less developed countries are dependent on the rich industrial countries.
  - b) the percent of the population that is below 15 and above 65 years of age.
  - c) the average number of children that a woman gives birth to during her lifetime.
  - d) the number of babies born per 1000 persons.

Answer: B

5. Which of the following is not a policy proposal of the neoclassical counter-revolution school?
  - a) promoting trade unions
  - b) privatizing state-owned enterprises
  - c) welcoming multinational corporations
  - d) promoting free trade

Answer: A

6. Which of the following is an assumption of the Lewis two-sector model?
- a) surplus labour in the rural sector
  - b) high unemployment in the urban modern sector
  - c) rising real urban wages
  - d) rising marginal product of labour in the rural sector

Answer: A

7. According to the theory of structural patterns of development, which of the following tends to occur as a country develops?
- a) a shift from industry and services to agriculture
  - b) an increase in the percentage of income spent on food
  - c) growth of the rural sector
  - d) none of the above

Answer: D

8. The underlying assumption of the Harrod-Domar growth model is that:
- a) the incremental capital-output ratio is given by  $k = Y/K$ .
  - b) growth can be sustained only if agricultural productivity rises.
  - c) growth is mainly determined by capital accumulation.
  - d) developing countries save too much and invest too little.

Answer: C

9. The Gini coefficient provides a measure of:
- a) the level of poverty.
  - b) the level of relative inequality.
  - c) disguised unemployment.
  - d) the rate of growth.

Answer: B

10. According to Kuznets, in the process of development inequality in an economy will normally:
- a) first rise and then fall.
  - b) first fall and then rise.
  - c) remain about the same.
  - d) show no definite pattern.

Answer: A

11. With modern sector enrichment growth, inequality will:
- a) first rise and then fall.
  - b) first fall and then rise.
  - c) remain about the same.
  - d) none of the above.

Answer: D

12. Higher income countries tend to have lower levels of absolute poverty because:
- more employment opportunities
  - more public assistance
  - greater entrepreneurship opportunities.
  - all of the above.

Answer: D

13. Which of the following policies may decrease the level of capital intensity in industry?
- a decrease in the cost of capital
  - a decrease in the minimum wage
  - a decrease in the elasticity of substitution
  - all of the above.

Answer: B

14. What conclusion can be reached from the following data on income shares?

	<b>Percentage of Income Received by</b>	
	<b>Lowest 40%</b>	<b>Highest 20%</b>
Bangladesh	17.3	45.3
Indonesia	14.4	49.4

- absolute poverty is more widespread in Bangladesh
- the size distribution of income is more unequal in Bangladesh
- Bangladesh had adopted a strategy of redistribution with growth
- none of the above

Answer: D

15. Assuming that the Gini coefficient for Egypt is 0.403 and the Gini coefficient for Australia is 0.404, it is possible to conclude that both Egypt and Australia have
- virtually the same number of households in absolute poverty.
  - virtually the same percentage of households in absolute poverty.
  - virtually the same level of the Human Development Index.
  - none of the above.

Answer: D

16. The total poverty gap is the:
- absolute number of people below the international poverty line.
  - percentage of the population below the international poverty line.
  - consumption (measured in dollars) necessary to bring everyone below the poverty line up to the line.
  - percentage of a country's total consumption necessary to bring everyone in the country below the poverty line up to the line.

Answer: C

17. In stage III of the demographic transition:
- the birth rate and the death rate are relatively low.
  - the birth rate and the death rate are relatively high.

- c) the birth rate is relatively high and the death rate is relatively low.
- d) the birth rate is relatively low and the death rate is relatively high.

Answer: A

18. The Malthusian population trap assumes that:

- a) contraception is unavailable.
- b) technological progress may be rapid.
- c) fertility increases with per capita income.
- d) all of the above.

Answer: C

19. Which of the following is a direct implication of the view that childbearing is an economic decision?

- a) People will not have additional children unless they can earn a profit from doing so.
- b) Fertility should fall with improved opportunities for women to work in jobs outside the home.
- c) Social factors have no effect on childbearing decisions.
- d) Compulsory education will increase fertility because educated children have the potential to earn higher salaries.

Answer: B

20. According to the Harris-Todaro model, a reduction of the informal sector can be achieved through:

- a) Programs of integrated rural development
- b) Urban job creation
- c) Tertiary education expansion
- d) Elimination of factor price distortions

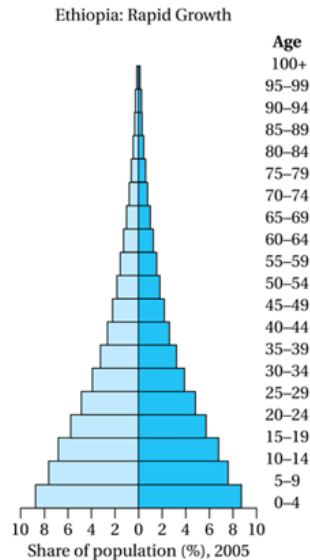
Answer: A

## Part 2: Short answer questions

Grading: the maximum score for each question is indicated below

Instructions: Please write clearly and use only the boxes indicated for the answer. Use the blank pages at the end of this handout to make notes before you answer questions.

### Question 1: Population growth – hidden momentum of population growth (10 points)



Using the example of Ethiopia, explain what the hidden momentum of population growth is, and the two main reasons for this phenomenon.

Answer: see also p. 277-278 in textbook & lecture slides

The hidden momentum of population growth is the tendency of population growth rates to continue to be large even after birth rates have declined substantially. There are two reasons for that. The first is that high birth rates depend on social, economic, and institutional forces and therefore cannot be altered overnight. As shown in the graph, young people greatly outnumber their parent, which is an indicator of large birth rates in the previous generation. The second is related to the age structure of the population. Even if the next young adult generation in Ethiopia have less children, the fact that the total number of couples having two children is much greater than the total number of couples who previously had more children means that the total population will still increase substantially before levelling off.

**Question 2: Comparing development - Human Development Index (HDI)**

Question 2A: Which three aspects of human development does the HDI capture, and which four indicators are used to measure those aspects? (5 points)

Answer: see also p. 47-54 in textbook & lecture slides

Living standard – GDP per capita

Longevity – Life expectancy

Knowledge – Adult literacy and school enrolment

The table below lists the HDI scores and GDP per capita of several developing countries.

Country	Human Development Index (HDI)	GDP Per Capita (PPP, U.S. \$)
<b>Low Human Development</b>		
Niger	0.340	627
Afghanistan	0.352	1,054
Dem. Rep. Congo	0.389	298
Ethiopia	0.414	779
Rwanda	0.460	866
Côte d'Ivoire	0.484	1,690
Malawi	0.493	761
<b>Medium Human Development</b>		
Bangladesh	0.543	1,241
Pakistan	0.572	2,496
India	0.612	2,753
South Africa	0.683	9,757
Nicaragua	0.699	2,570
Gabon	0.755	15,167
China	0.772	5,383
Iran	0.782	10,955
Thailand	0.783	8,135

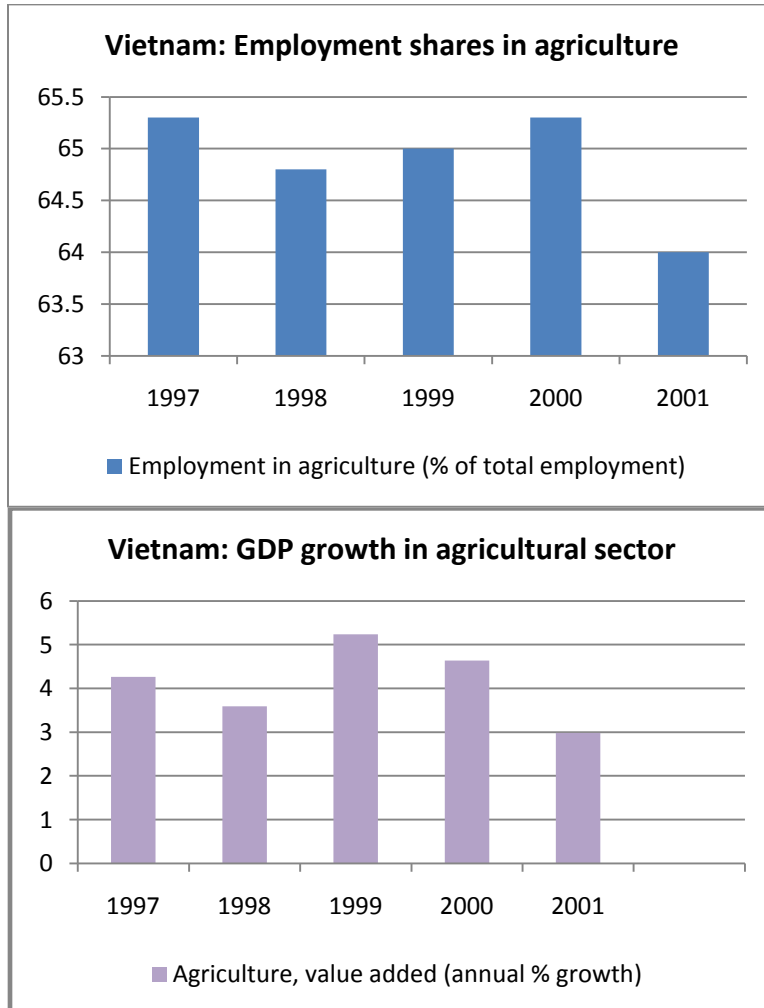
Question 2B: Is GDP per capita (PPP) a good indicator of development? Use the data in the table to illustrate your point. (7 points)

Answer: see also p. 50-52 in textbook & lecture slides

GDP per capita (PPP) gives an indicator of a country's standard of living. However, ranking countries only by income is not enough to capture important differences in countries' development levels. Thus, it is important to consider other indicators and the HDI summarizes important aspects of development such as education and health. For example, Afghanistan has a relatively large income but low HDI. Nicaragua has a relatively low income, but relatively large HDI.

**Question 3: Economic growth theories and Vietnam case study**

‘Vietnam has experienced high growth and substantial poverty reduction for more than a decade’ (p.1, Hyun, 2005). The figures below show the employment share and the GDP growth in the agricultural sector for Vietnam.



Question 3A: Which growth pattern was experienced by Vietnam over this period? Justify your answer using only the information provided in the graphs above. (6 points)

Answer: also p. 221-222 in textbook, Vietnam case study material & lecture slides

Observing the annual GDP growth rate and employment rate for agriculture from 1997 to 2001, we found GDP from agriculture grew faster than employment in agriculture (which actually decreased). The GDP growth in agriculture was motivated by improvement of productivity rather than employment increasing. Therefore, this growth pattern corresponds to traditional-sector enrichment growth.

Question 3B: Given the growth pattern highlighted in question 3A, what would you expect to observe in terms of trends in poverty and inequality in Vietnam over the 1997-2001 period? (8 points)

Answer: also p. 222-223 in textbook, Vietnam case study material & lecture slides

In the traditional-sector enrichment typology, growth results in higher income, a more equal relative distribution of income, and less poverty.

**Question 4: Rural-urban migration: Harris-Todaro model**

The equilibrium in the Harris-Todaro model is given by:

$$— , \quad (1)$$

where

**is agricultural income**

**is employment in manufacturing**

**is total urban labour pool**

**is the urban minimum wage**

Question 4A: Many cities in developing countries have a large informal sector with precarious working conditions. Despite that, rural residents keep migrating to urban areas. In light of the Harris Todaro model, how do you explain this phenomenon? Focus on the intuition of the model; do not refer to the equations. (8 points)

Answer: also p. 340-342 in textbook & lecture slides

The reason why rural residents keep moving to urban areas in spite of unemployment is that the expected wage they obtain in the city is larger than the agricultural wage. Thus, a potential immigrant compares her current rural wage to her expected urban wage, which depends on the probability of getting an urban job and the urban wage rate.

Question 4B: Use equation (1) to explain what characterizes a situation of equilibrium in the Harris-Todaro Model. (6 points)

Answer: also p. 340-342 in textbook & lecture slides

The equilibrium in the Harris-Todaro model corresponds to a situation where the expected urban wage is equal to the actual rural wage. In this situation, there is no rural-urban migration.