

1. Explain the de Melo-Robinson model (the 123 model) of equilibrium in the traded and non-traded goods sectors using a diagram. In particular,
 - a. Explain the impact that an inflow of foreign exchange will have on exports and the real exchange rate (measured as the relative price level for traded and domestic goods) in this model.
 - b. Based on your answer to (a), discuss the impact that an increase in international borrowing by a country (like the recent surge in the U.S. fiscal deficit) might have on the performance of the export sector and on prices.

2. Using the Bangladesh version of the 123 model, which includes the estimates for each question below:
 - a. discuss the impact of an increase in import tariffs by 10% (i.e. a new 10% tax) on volumes of exports and imports, and on the real exchange rate (i.e. the relative price of non-tradables to tradables).
 - b. discuss the impact of an increase in foreign capital inflows (represented by foreign savings) equal to 10% of base GDP. Again, please focus on exports, imports, and the relative price of non-tradables to tradables.
 - c. Assume that a 10% import tax is imposed (exercise a above) following a surge in foreign savings (from exercise b above) equal to 10% of GDP. Again, discuss the impact on exports, imports, and the relative price of non-tradables to tradables.