Examination: European Integration **Wintersemester: 2005/2006**
Examiner: Dr. G. Groh 1557
The following aids can be used: Dictionary

Student number: ______________ Faculty: ______________

Name: ______________ First name: ______________

Date: ______________

Important hints:

- This exam consists of 25 questions.
- General rule for all questions: From the 4 given answer proposals, exactly one is correct.
- Valuation:
  - correct answer: 1 point
  - no answer: 0 points
  - wrong or more than one answer: $-\frac{1}{3}$ point
- The intersection point of the crosses has to be *within* the boxes, not outside (☒ instead of ×☐). Crosses outside the boxes will *not* be counted!
- Use a ball-point pen or s.th. similar but *not* a lead pencil!
- If you have made a cross at the wrong alternative and want to correct it, please write this plainly at the margin beside the question.
- Time available: 60 minutes.

1. The following statement is correct:

   - ☐ The European Coal and Steel Community (ECSC) was founded in 1952 by the Treaty of Paris which was preceded by the Spaak-report 1951.
   - ☐ The European Economic Community (EEC) and the European Atomic Energy Community (EURATOM) were founded in 1957 by the Treaties of Rome which were preceded by the conference of Messina 1955.
   - ☐ The Exchange Rate Mechanism (ERM) and the European Currency unit (ECU) were introduced by the European Monetary System (EMS) in 1979 which in turn was developed in the Delors-report of 1975.
   - ☐ The European Union (EU) was established by the "Maastricht-Treaty" 1992 which was prepared on the Summit of Madrid in 1991.

2. The Single European Act (SEA) of 1986

   - ☐ set a deadline (end of 1992) for the removal of interstate tariffs among the EU member countries.
   - ☐ introduced the "cooperation"-procedure between the Council of Ministers and the European Parliament.
   - ☐ unified the separate Commissions of the European Coal and Steel Community (ECSC) and the European Economic Community (EEC) to one single institution.
   - ☐ extended voting by qualified majority in the Council of Ministers to all areas which required unanimity so far.

3. The following countries (among others) fully implement the Schengen-Agreement:

   - ☐ Norway, Iceland, France, Italy.
   - ☐ Belgium, Ireland, Luxembourg, Germany.
   - ☐ Spain, Portugal, Great Britain, France.
   - ☐ Netherlands, Austria, Italy, Poland.

4. The “Committee of Permanent Representatives” (COREPER) is

- ☐ an institution comprising representatives of different social groups (employees, employers, professionals and consumers).
- ☐ an institution comprising representatives of the various regions in the EU (elected municipal or regional politicians).
- ☐ an institution supporting the European Commission.
- ☐ an institution supporting the Council of Ministers.

5. The current rules determining the composition of the European Commission and the weighting of votes in the Council of Ministers are laid down in

- ☐ the “Treaty on European Union.”
- ☐ the “Treaty of Amsterdam.”
- ☐ the “Treaty of Nice.”
- ☐ the “European Constitution.”

6. The enforcement of EU-law vis-à-vis the member states and the supervision of its implementation are tasks of

- ☐ the Council of Ministers.
- ☐ the Court of Auditors.
- ☐ the European Commission.
- ☐ the European Parliament.

7. The following EU-countries (among others) have meanwhile adopted the Euro:

- ☐ Italy, France, Denmark, Belgium, Netherlands.
- ☐ Finland, Ireland, France, Germany, Greece.
- ☐ Spain, Portugal, Sweden, Luxemburg, Italy.
- ☐ Austria, Estonia, Germany, Great Britain, Spain.

8. The European Central Bank (ECB)

   - ☐ has to maintain price stability in the Euro-area under the provision, that the exchange rate of the Euro vis-à-vis the US-dollar remains within narrow bounds.
   - ☐ has to maintain price stability in the Euro-area under the provision, that other economic goals of the member countries are not endangered.
   - ☐ is formally independent in its monetary policy but accountable to the European Parliament.
   - ☐ is fully independent in its monetary policy and not accountable to any EU-institution nor any national government.

9. One of the main tasks of the "Governing Council" of the European Central Bank (ECB) is

   - ☐ the implementation of the monetary policy in the Euro-area.
   - ☐ the formulation of the monetary policy of the Euro-area.
   - ☐ to report on progress towards convergence by countries which aim to adopt the Euro.
   - ☐ the management of the current businesses of the ECB.

10. The "Eurosystem" comprises

   - ☐ the European Central Bank (ECB) and the national central banks of those EU-countries which have adopted the Euro.
   - ☐ the European Central Bank (ECB) and the national central banks of all EU-countries, whether they have adopted the Euro or not.
   - ☐ the European Central Bank (ECB) and the national central banks of all European countries, whether they belong to the EU or not.
   - ☐ the national central banks of all EU-countries which have adopted the Euro, but not the European Central Bank (ECB).

11. The following statement is correct:

- ☐ One consequence of a customs union is, that for at least one participating country imports from the world market will be substituted by imports from the partner countries.
- ☐ Although single member countries can suffer a loss from the formation of a customs union, the total gain for the customs union as a whole always suffices to compensate this loss.
- ☐ A customs union can have the consequence, that after its formation a member country imports even more goods from the world market than before.
- ☐ After the formation of a customs union, the gains and losses in producers' surplus across all member countries will always add up to zero.

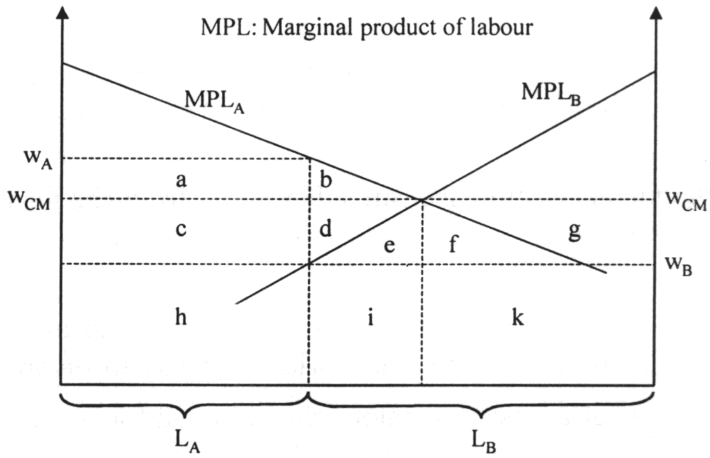
12. The following statement is correct:

- ☐ The formation of a customs union is not in line with the most-favoured-nation principle.
- ☐ In contrast to a customs union, trade diversion cannot occur in a free-trade-area.
- ☐ The extension of a customs union to a common market will always lead to additional welfare effects.
- ☐ The EU-25 in its present form is a complete common market.

13. With regard to capital market integration within the EU (or former EC, respectively) the following statement is correct:

- ☐ Capital movements between the EU-countries were almost completely substituted by the free trade in goods and services.
- ☐ Goods market integration and capital market integration have largely worked as a substitute for labour mobility between the EU-countries.
- ☐ Full capital market liberalization between the founding members of the EC was already achieved together with the abolition of tariffs.
- ☐ The full capital market liberalization within the EU led to a rapid evolution of unregulated offshore-markets like the "Euro-markets."

14. Have a look at the following picture:



Let L_A denote the labour force of country A and L_B the labour force of country B. Prior to the establishment of a common labour market between both countries the real wage w_A prevails in country A and w_B in country B. After labour market liberalization the common wage rate w_{CM} emerges. Assume furthermore, that also after the opening of the labour market

- migrant workers remain inhabitants of their home country (like, e.g., commuters)
- capital remains immobile between the two countries.

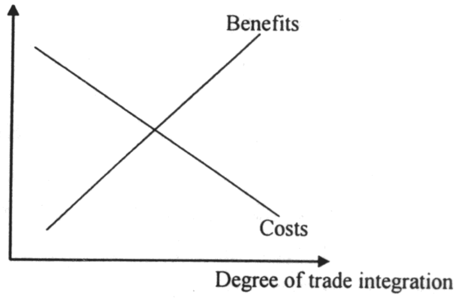
After the formation of the common labour market

- ☐ domestic output in country A decreases by area $b + d + e + i$ and a net loss for all inhabitants of A (taken together) equal to area b emerges.
- ☐ domestic output in country A increases by area $b + d + e + i$ and a net gain for all inhabitants of A (taken together) equal to area $b + d$ emerges.
- ☐ domestic output in country B increases by area $e+i$ and a net gain for all inhabitants of B (taken together) equal to area $b + d$ emerges.
- ☐ domestic output in country B decreases by area $e+i$ and a net gain for all inhabitants of B (taken together) equal to area d emerges.

15. Consider again the picture of question 14 and take the same assumptions as given as before, especially that capital remains immobile and that migrant workers remain residents of their home country. As a consequence of the introduction of the common labour market

- ☐ the income of workers from country A decreases by area a whereas the income of capital owners of the same country increases by area $a + b$.
- ☐ the income of workers from country A decreases by area $a + b$ whereas the income of capital owners of the same country increases by area b.
- ☐ the income of workers from country B increases by area $d+e+i$ whereas the income of capital owners of the same country decreases by area $e + f + g$.
- ☐ the income of workers from country B increases by area $d + e + f + g$ whereas the income of capital owners of the same country decreases by area $e + i$.

16. Consider the following diagram displaying the costs and benefits of a monetary union for a given group of countries:



Assume, that due to successful labour market reforms the degree of wage flexibility increases in all participating countries. As a consequence,

- ☐ the "costs-curve" will shift to the right.
- ☐ the "costs-curve" will shift to the left.
- ☐ the "benefits-curve" will shift to the right.
- ☐ both curves will remain unaffected.

17. In the picture of question 16 it is implicitly assumed that

- ☐ a monetary union enhances further trade integration.
- ☐ a complete common market already exists prior to the formation of a monetary union.
- ☐ the probability of asymmetric shocks depends negatively on the degree of trade integration.
- ☐ a higher degree of trade integration makes the occurrence of asymmetric shocks more likely.

18. Assume, one of the new member countries of the EU plans to introduce the Euro in a few years. With a debt-to-GDP ratio $b = B/Y$ of 120 %, however, it does not fulfill all Maastricht-criteria. Assume, that the nominal rate of interest, r, is 5 % and that the current GDP has a value of 2500 monetary units. Which of the following policies will be successful in reducing the debt-to-GDP ratio b at the current point in time, if support from monetary policy is not available? (Hint: Recall the government's intertemporal budget constraint $\dot{b} = g - t + \left(r - \dot{Y}/Y\right) \cdot b - \dot{M}/Y$ with $g = G/Y$ and $t = T/Y$, G denoting government expenditure, T tax revenue, Y nominal GDP and M money supply.)

- ☐ A primary surplus $(T - G)$ of 50 monetary units and an induced growth rate of nominal GDP $(\dot{Y}/Y)$ of 3 %.
- ☐ A primary surplus $(T - G)$ of 75 monetary units and an induced growth rate of nominal GDP $(\dot{Y}/Y)$ of 2.5 %.
- ☐ A total deficit $(G - T + rB)$ of 50 monetary units and an induced growth rate of nominal GDP $(\dot{Y}/Y)$ of 2 %.
- ☐ A total deficit $(G - T + rB)$ of 75 monetary units and an induced growth rate of nominal GDP $(\dot{Y}/Y)$ of 2.5 %.

19. Recall the 2-country-version of the Barro-Gordon model. Assume, that monetary policy in country A is conducted by a "hard-nosed" central bank attaching high weight to a low rate of inflation and only little weight to employment. In this country, the long-run equilibrium is characterized by an inflation rate of 2 % and an unemployment rate at its natural level of 5 %. In country B there is a "wet" central bank which is well-known to pursue a highly inflationary policy already for more than 20 years. Not surprisingly, the long-run rate of inflation is 15 % whereas the natural rate of unemployment is the same as in country A. After several unsuccessful attempts to reduce inflation in the past, country B now starts a new trial and has 2 options to do so:

a) to publicly announce a new monetary policy and to actually implement a monetary contraction

b) to form a monetary union with country A with the common central bank being a close copy of country A's central bank.

Under these circumstances it can be expected that for country B

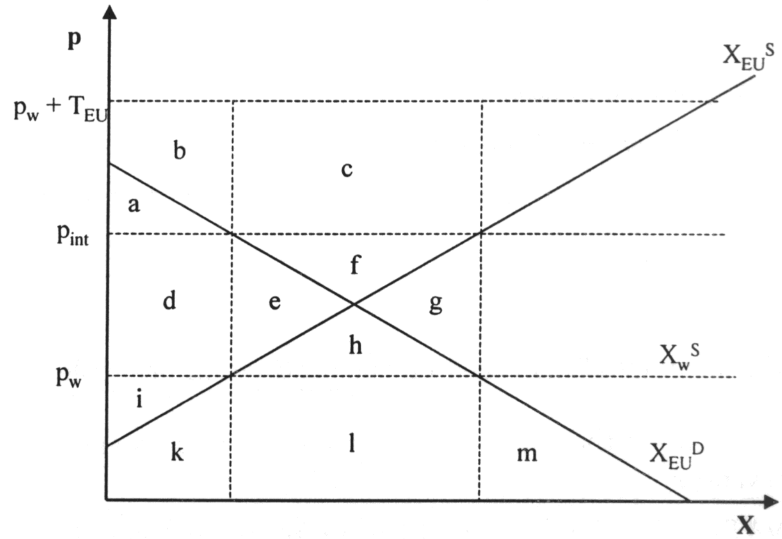
- ☐ alternative b) leads to a faster adjustment to a lower inflation equilibrium, but to higher losses in terms of output and employment during the transition process in comparison to alternative a).
- ☐ alternative b) leads to a faster adjustment to a lower inflation equilibrium and to lower losses in terms of output and employment during the transition process in comparison to alternative a).
- ☐ alternative b) leads to a slower adjustment to a lower inflation equilibrium, but to higher losses in terms of output and employment during the transition process in comparison to alternative a).
- ☐ alternative b) leads to a slower adjustment to a lower inflation equilibrium and to lower losses in terms of output and employment during the transition process in comparison to alternative a).

20. Under free market conditions incomes in the agricultural sector come under pressure, since technical progress in this sector usually takes place in conjunction with

- ☐ a high price elasticity and a high income elasticity
- ☐ a high price elasticity and a low income elasticity
- ☐ a low price elasticity and a high income elasticity
- ☐ a low price elasticity and a low income elasticity

of the demand for agricultural products.

21. Have a look at the following picture, which describes the situation on the market for an agricultural good X in the EU:



Let p_w denote the world market price for this product and T_{EU} the common external tariff levied by the EU on potential imports. Furthermore p_{int} is the intervention price guaranteed to EU-producers in conjunction with the Common Agricultural Policy. In comparison to a situation of fully free trade (including third countries) this system leads to the following changes in aggregate welfare for the EU (i.e. the sum of the changes in consumers' surplus, producers' surplus and costs for the intervention authorities):

- ☐ If surpluses can be sold on the world market by the intervention authorities (at price p_w), the total welfare loss for the EU as a whole is equal to area e+g+2h+l.
- ☐ If surpluses can be sold on the world market by the intervention authorities (at price p_w), the total welfare loss for the EU as a whole is equal to area e+g+2h.
- ☐ If surpluses cannot be sold on the world market by the intervention authorities, the total welfare loss for the EU as a whole is equal to area e+g+2(h+l)+k+m.
- ☐ If surpluses cannot be sold on the world market by the intervention authorities, the total welfare loss for the EU as a whole is equal to area e+g+2(h+l).

22. In conjunction with the reform process of the Common Agricultural Policy (CAP) the following statement is correct:

- ☐ As a result of the implementation of the Mansholt-plan, variable import levies were replaced by fixed ones, allowing world market prices to affect EU import prices.
- ☐ The MacSharry reforms introduced (among other measures) the principle of "modulation," according to which direct payments for farmers were reduced to finance measures for rural development.
- ☐ The CAP-reforms of 2003 fully removed quotas for milk and sugar, but maintained the system of intervention buying for cereals and beef.
- ☐ The reforms according to the "Agenda 2000" introduced further cuts of support prices and further direct payments to farmers.

23. A French and a German firm producing washing-machines want to merge. The combined world wide turnover of both firms is 70 million Euro, 80 % of which is made in France. The assessment of the planned merger is a competency of

- ☐ the European Commission.
- ☐ the national merger authorities.
- ☐ both the European Commission and the national merger authorities.
- ☐ the Council of Ministers.

24. If value-added-tax (VAT) is based on the destination principle,

- ☐ the VAT-rate of the country of consumption applies and the latter also receives the tax revenues.
- ☐ the VAT-rate of the country of consumption applies but the country of production receives the tax revenues.
- ☐ the VAT-rate of the country of production applies and the latter also receives the tax revenues.
- ☐ the VAT-rate of the country of production applies but the country of consumption receives the tax revenues.

25. The current situation for value-added-taxes (VAT) and excise duties in the EU is as follows:

- ☐ VAT-rates are fully equalized among the EU member states, whereas the latter can choose excise duties at their discretion.
- ☐ Excise duties are fully equalized among the EU member states, whereas the latter can choose VAT-rates at their discretion.
- ☐ For VAT-rates and excise duties minimum rates are fixed for all EU member states, whereas the concrete level can be chosen freely.
- ☐ Both VAT-rates and excise duties can be freely chosen by the EU member states without any limitations.