Written Exam Economics Summer school 2017

An Economic History of Europe

Question 1

This question asks you to describe the preindustrial growth experience of England using historical data.

i. Briefly explain the theoretical determinants of preindustrial growth.
   - *The answer should discuss the Smithian and Malthusian determinants of preindustrial growth, with particular emphasis on the interaction between demography and economics and the role of technological progress. It is good if the student discusses the nature of technological progress in preindustrial times, and why this implies low to moderate rates of growth.*

ii. Economic historians often use GDP/capita estimates and real wages to assess historical standards of living. Discuss the relative advantages and disadvantages of these measures when using historical data.
   - *The answer should highlight that data on nominal wages and prices are relatively easily available, making the construction of real wages simple, whereas historical estimates of GDP/capita are based on many assumptions and are therefore less certain. On the other hand, GDP/capita is a better measure of living standards, since not all income comes from wages (it is also for example from land and capital). Moreover, historical wages are usually for day wages, which mean it is necessary to use assumptions about the number of days worked per year.*

iii. Make a graph (or graphs) illustrating GDP/capita for England and real wages for London over the long run.
   - *The graph should focus on the preindustrial period, thus avoiding the 'hockey stick' whereby the preindustrial data will look very flat due to the massive growth in incomes after ca. 1800. The students have practiced making these graphs in the exercise classes, and should use the New Maddison dataset for GDP/capita and Bob Allen's real wage data. It is excellent if the student is able to overlay the two data series in the graph, for example using two axes or index numbers, but it is not necessary.*

iv. Do you observe in your graph(s) any evidence for increases in living standards in preindustrial times? Why might your findings differ depending on whether you use GDP/capita or real wages?
   - *GDP/capita shows an increase, but real wages are flat for much of the period. The answer should demonstrate the formal relationship between real wages and income per head presented in the textbook (Box 4.3). It would be relevant to discuss the conclusions of both Clark (2007) and Fouquet and Broadberry (2015) in the answer.*

Question 2

In what way are banks important for economic development? Explain your answer with reference to the historical experience.

- *The answer should relate in particular to section 7.6 of the textbook. In short, banks increase the opportunity cost of hoarding, so increasing the savings ratio; they match borrowers and savers, and thus increase the efficiency of the use of savings; and fractional reserve banking increases the monetarization of the economy. The answer should also make* *clear, however, that fractional reserves in particular also mean that bank crises can occur, with often large and persistent effects on economic growth. Finally, it could be relevant to refer to the analysis by Pascali (2016), although a deep understanding of this paper is not necessary.*

Question 3

Many economists now believe that the Gold Standard played a role in prolonging the Great Depression. Why is this?

- *The answer should highlight the importance of the 'Open Economy Trilemma'. Unrestricted capital mobility and fixed exchange rates means that it is impossible to use monetary policy. It would be good if the student discusses briefly why the Gold Standard implies fixed exchange rates. The answer could for example compare the experiences of the UK and France. The former left the Gold Standard and devalued earlier, allowing it to escape from the Great Depression earlier. Leaving the Gold Standard meant that countries could devalue, thus avoiding deflation; making exports more competitive; inflation reduced product wages and real interest rates; and in general monetary policy could be used. It could be relevant to incorporate the conclusions of Eichengreen and Irwin (2010) regarding the connection between the Gold Standard and protectionism, and Klovland (1998) for the Scandinavian experience.*

Question 4

Define globalization. Describe when globalization has taken place in history, and explain why we might expect periods of globalization to be associated with economic growth.

- *Globalization should be defined as market integration on a world scale, although it is very good if the answer nuances this with alternative definitions. The role of the Law of One Price should be discussed, and how it relates to markets for goods, capital and labor. The first era of globalization was in the late nineteenth century, where free trade combined with perfect capital mobility under the Gold Standard and relatively free movement of labor (and mass migration to e.g. the US). The second era of globalization was after the Second World War. Attempts were made to ease trade restrictions (e.g. GATT rounds), capital became mobile after the collapse of the Bretton Woods System in the 1970s, although labor mobility remains very restricted. As for the relationship between globalization and economic growth, a large number of considerations are possible, only some of which are given here. Free trade according to comparative advantage will increase productivity and ease the flow of ideas embodied in goods. Capital mobility should in principle mean that capital flows to areas where it gets the highest return, i.e. leading to investment in underdeveloped countries. Labor mobility allows ideas to flow more freely around the world, and might lead to wage convergence. It is good if the answer nuances this with the risks of globalization: principally that it usually has distributional consequences, so not all will benefit. Finally, it could be relevant to refer to the paper by Rajan and Zingales (2003), where they argue that openness to capital and trade is an important precondition for financial development and hence economic growth.*