

Written Exam at the Department of Economics summer school 2019

An Economic History of Europe

Final Exam

12 August 2019

(3-hour open book exam)

Suggested Answers

Question 1

You are asked to consider the preindustrial growth record of countries, and the reasons for income inequality between nations in the world today.

- i. Briefly describe the determinants of preindustrial growth.
 - *The answer should discuss the Smithian and Malthusian theories. A good answer would explain how these offset each other, making the theoretical prediction about the extent of preindustrial growth unclear.*
- ii. Why is the historical growth record of present day developed countries important for understanding inequality in the levels of income between economies today?
 - *The answer should explain that the timing of the take-off to modern growth can to a certain extent explain relative living standards today. Countries which took off earlier are generally richer today.*
- iii. Use the Maddison database to illustrate the disparate patterns of economic growth between different parts of the world over time (hint: you might not want to try to graph all the countries in the database!). Provide a brief explanation of the patterns you observe.
 - *Since the question is about preindustrial growth, as well as modern income inequality, it is good if the answer divides the data into both preindustrial and post-industrial periods (thus making it easier to see changes in living standards over time in the preindustrial period, without levels being dwarfed by the post-industrial period). Standard formalities about making graphs should be observed. The explanation could relate to both (i) and (ii) above.*
- iv. Should we expect income inequality between countries to increase or decrease in the future? Motivate your answer.
 - *The answer to this question can be quite broad and can touch on issues such as convergence and how to measure inequality. In general, the answer depends on three questions: 1) Will all nations obtain modern economic growth; and 2) Will latecomers initially grow much faster? The conclusion in the textbook is optimistic given the historical experience of latecomers, and the historical experience of institutional convergence and broader education.*

N.B. The 2013 version of the Maddison database is in the file “mpd_2013-01.xlsx”.

Question 2

Discuss the role of human capital for industrialization. In your answer be sure to define the concepts of human capital and industrialization precisely. Consider both the first industrial revolution in England and later industrialization episodes through “catch-up”.

- *Human capital is the combination of skills, knowledge and experience embodied in labour, and is closely related to education. Industrialization involves the widescale adoption of industry, and is often associated with the introduction of new technologies and institutions (the factory system), as well as with the transfer of labour from agriculture to industry.*

The first industrialization began in England in the late eighteenth century, although human capital is often considered to have played a relatively minor role. The scientific foundation for new discoveries was often quite shaky until the mid-nineteenth century. It might be mentioned that Unified Growth Theory suggests an important role for human capital during the second phase of the Industrial Revolution, however, when science became more important. For the case of France, Squicciarini and Voigtlaender (2015) have demonstrated that upper-tail knowledge was a proximate driver of industrial growth.

It is good if the answer reflects an understanding that human capital facilitates catch-up due to the non-rival nature of knowledge. By the end of the nineteenth century most nations in Europe had people who followed and participated in R&D, and Europe had the necessary institutional requirements for technology transfer, including a sufficient minimum level of education. Moreover, technology-diffusion models stress that the stock of human capital matters for how well follower countries adjust to new economic conditions.

Question 3

Why did many countries introduce trade protection during the Great Depression? Explain how monetary policy could be (and was) used to alleviate the pressures which led countries to restrict trade.

- *The answer should start by explaining what the Great Depression was. In particular, it is relevant to relate the discussion to the workings of the gold standard (the “rules of the game” and the open economy trilemma).*

With the onset of the Great Depression, American demand for imports fell, and other countries saw widening current account deficits which they were unable to finance due to a lack of international liquidity (the international capital market was greatly hit by the depression). This problem was exacerbated by American trade policy (Smoot-Hawley). Countries thus saw no other option but to impose barriers to trade.

Eichengreen and Irwin (2010) demonstrate that countries that remained on the gold standard longer became more protectionist. An alternative would be to leave the gold standard and devalue and/or use monetary policy (this should be related to the trilemma). Empirical studies have demonstrated that countries which left the gold standard earlier recovered faster from the Great Depression. Part of the reason was that they could thus avoid deflation, and the good answer would discuss why deflation is harmful.