Suppose Ukraine discovers large deposits of oil in the Black Sea continental shelf and becomes an oil-exporting country. What will be the consequences of such discovery? You have to explain through economic reasoning how and why each change would occur. (hint: look in your book for “Dutch Disease”)

1. (1 point) What will happen to the value of Ukrainian currency? Assume floating exchange rate.

2. (2 points) What will happen to the trade balance of Ukraine? Explain how both exports and imports will be affected.

3. (2 points) Before discovery of oil fields, Ukraine exported steel and some agricultural products (sunflower oil, sugar). After discovery of oil, what will happen to those industries? How will the discovery of oil affect their competitive positions on the world markets?

4. (2 points) Ukraine imports electronics, cars, textiles and many other consumer products. Many of those products are also manufactured at home. Thus, for many domestic products there are many imported substitutes and vice versa. How does discovery of oil affect domestic import-competing producers of consumer goods (Hint: how will exchange rate affect relative prices)

5. (2 points) What will happen to Ukrainian non-traded sector (i.e. goods and services that are neither exported nor imported)? (Hint: answer to this question depends on answers to questions 3 and 4. There will be reallocation of resources across different sectors of the economy – the import competing sector, exporting sector and nontradables).

6. (1 point) Why is it called a “disease”? What kind of “cure” would you suggest?