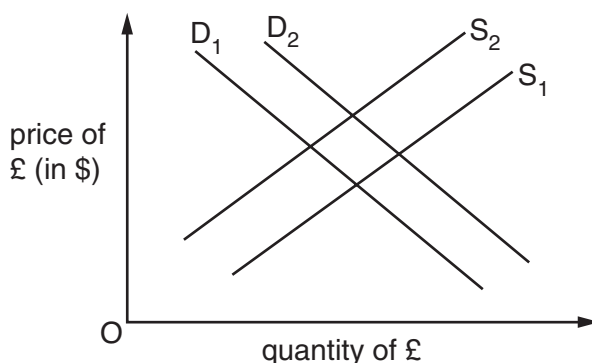


- 26** In the diagram  $D_1$  and  $S_1$  are the initial supply and demand curves of the pound sterling (£) on the foreign exchange markets.



What will cause the demand curve to shift to  $D_2$  and the supply curve to  $S_2$ ?

- A** a depreciation of the pound sterling
  - B** a decrease in UK interest rates
  - C** an increase in the price levels of other countries
  - D** an increase in the level of UK import tariffs
- 27** Which of the following combinations indicates that a country has a freely floating exchange rate?

	nominal exchange rate	foreign currency reserves
<b>A</b>	depreciates by 20%	decrease by \$1 billion
<b>B</b>	depreciates by 20%	unchanged
<b>C</b>	unchanged	decrease by \$1 billion
<b>D</b>	unchanged	unchanged

- 28** In the United States a representative basket of goods costs \$4000.

At the current actual exchange rate between the US\$ and the £ sterling the same basket of goods in the UK would cost \$5000.

What can be deduced from this?

- A** The £ sterling is 25% over-valued against the US\$.
- B** The £ sterling is 20% under-valued against the US\$.
- C** The purchasing power parity exchange rate of the £ sterling is \$1.25 to the £.
- D** The purchasing power parity exchange rate of the £ sterling is \$0.80 to the £.