***Macroeconomics, 10e, Global Edition* (Parkin)**
Chapter 26 The Exchange Rate and the Balance of Payments

1 The Foreign Exchange Market

1) The term "foreign currency" refers to foreign
I. coins
II. notes
III. bank deposits
A) II only.
B) II and III only.
C) I and II only.
D) I, II, and III.
Answer: D
Topic: Financing International Trade
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) If portable disk players made in China are imported into the United States, the Chinese manufacturer is paid with
A) dollars.
B) yuan, the Chinese currency.
C) international monetary credits.
D) euros, or any other third currency.
Answer: B
Topic: Financing International Trade
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) If the United States sells beef to Japan, the U.S. beef producer is paid with
A) dollars.
B) yen, the Japanese currency.
C) international monetary credits.
D) euros, or any other third currency.
Answer: A
Topic: Financing International Trade
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) When Safeway supermarkets in the United States buys strawberries from Mexico,
A) it uses dollars to pay Mexican farmers.
B) it uses pesos to pay Mexican farmers.
C) it may use any currency it chooses.
D) the transaction shows up in the U.S. capital account.
Answer: B
Topic: Financing International Trade
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) Americans demand Japanese yen in order to
A) buy Japanese products.
B) supply American goods in Japanese markets.
C) allow the Japanese to buy U.S. products.
D) balance the current account.
Answer: A
Topic: Financing International Trade
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) Which of the following statements is correct?
I. The exchange rate is a price.
II. The exchange rate is different from other prices because it is NOT determined by supply and demand.
A) only I
B) only II
C) I and II
D) neither I nor II
Answer: A
Topic: The Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) The exchange rate is the
A) opportunity cost of pursuing a nation's comparative advantage.
B) price of one country's currency expressed in terms of another country's currency.
C) ratio between imports and exports.
D) interest rate that is charged on risk-free international capital flow.
Answer: B
Topic: The Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

8) The exchange rate is the price at which the ________ of one country exchanges for the ________ of another country.
A) currency; goods
B) goods; goods
C) currency; currency
D) currency; financial instruments
Answer: C
Topic: The Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) A decrease in the value of a currency in terms of other currencies is known as
A) an appreciation.
B) a depreciation.
C) a par value.
D) a gold point.
Answer: B
Topic: The Exchange Rate, Currency Depreciation
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

10) When the value of one currency falls relative to another currency, the exchange rate for the first currency has
A) depreciated.
B) appreciated.
C) demanded.
D) revalued.
Answer: A
Topic: The Exchange Rate, Currency Depreciation
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

11) By definition, currency depreciation occurs when the value of
A) all currencies fall relative to gold.
B) one currency falls relative to another currency.
C) one currency rises relative to another currency.
D) gold falls relative to the value of currencies.
Answer: B
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) Suppose that the exchange rate between the dollar and the peso changed from 6 pesos per dollar to 8 pesos per dollar. This change means that the
A) peso appreciated.
B) dollar depreciated.
C) peso depreciated.
D) Both answers A and B are correct.
Answer: C
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) If the dollar's value changes from 120 yen per dollar to 110 yen per dollar, the dollar has
A) depreciated.
B) appreciated.
C) demanded.
D) devalued.
Answer: A
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

14) Which of the following examples definitely illustrates a depreciation of the U.S. dollar?
A) The dollar exchanges for 120 euros and then exchanges for 100 euros.
B) The dollar exchanges for 100 euros and then exchanges for 120 yen.
C) The dollar exchanges for 1 pound and then exchanges for 1.2 pounds.
D) The dollar exchanges for 250 yen and then exchanges for 275 euros.
Answer: A
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

15) When the U.S. dollar depreciates against the yen, the yen becomes ________ expensive and the U.S. exchange rate ________.
A) more; rises
B) less; rises
C) more; falls
D) less; falls
Answer: C
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

16) When the U.S. dollar depreciates against the yen, the yen ________ and the exchange rate ________.
A) appreciates; rises
B) depreciates; rises
C) appreciates; falls
D) depreciates; falls
Answer: C
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

17) Last year the exchange rate between U.S. dollars and Mexican pesos was 10 pesos per dollar. Today is it 11 pesos per dollar. Here, the dollar ________ against the peso, and the peso ________ against the dollar
A) appreciated; depreciated
B) depreciated; appreciated
C) appreciated; appreciated
D) depreciated; depreciated
Answer: A
Topic: The Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

18) Suppose the exchange rate of the U.S. dollar was 1.50 British pounds = $1.00 (U.S.) on Wednesday, and on Monday the exchange rate was $.75 (U.S.) = 1.00 British pound. Which of the following best describes what happened between Wednesday and Monday?
A) The U.S. dollar appreciated against the British pound.
B) The British pound appreciated against the U.S. dollar.
C) The U.S. dollar depreciated against the British pound.
D) Both answers B and C are correct.
Answer: D
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) An increase in the value of a domestic currency in terms of other currencies is known as
A) an appreciation.
B) a depreciation.
C) a flexible exchange rate.
D) a term not given in the above answers.
Answer: A
Topic: The Exchange Rate, Currency Appreciation
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

20) Which of the following examples definitely illustrates an appreciation of the U.S. dollar?
A) The dollar exchanges for 120 euros and then exchanges for 100 euros.
B) The dollar exchanges for 100 yen and then exchanges for 125 euros.
C) The dollar exchanges for 1 pound and then exchanges for 1.2 pounds.
D) none of the above
Answer: C
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

21) Suppose the exchange rate of the U.S. dollar was 1.00 euro = $0.50 on Thursday, and on Friday the exchange rate was $1.00 = 2.10 euros. Which of the following best explains what has happened between Thursday and Friday?
A) The U.S. dollar appreciated against the euro.
B) The euro appreciated against the U.S. dollar.
C) The U.S. dollar depreciated against the euro.
D) Both answers B and C are correct.
Answer: A
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

22) If the pound-dollar exchange rate changes from £0.60 per dollar to £0.65 per dollar, then the pound has ________ against the dollar and the dollar has ________ against the pound.
A) depreciated; depreciated
B) appreciated; depreciated
C) appreciated; appreciated
D) depreciated; appreciated
Answer: D
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

23) If 100 Japanese yen buy more U.S. dollars today than yesterday, the dollar has ________ and the yen has ________.
A) depreciated; appreciated
B) appreciated; depreciated
C) depreciated; depreciated
D) appreciated; appreciated
Answer: A
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

24) If the value of a dollar rises in terms of yen, the dollar has ________ and the yen has ________.
A) appreciated; appreciated
B) appreciated; depreciated
C) depreciated; appreciated
D) depreciated; depreciated
Answer: B
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

25) If the Japanese yen was 123 per dollar and now is 114 yen per dollar, it can be said that
A) the yen appreciated against the dollar.
B) the yen has depreciated against the dollar.
C) the dollar has appreciated against the yen.
D) None of the above answers is correct.
Answer: A
Topic: The Exchange Rate, Currency Appreciation
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

26) If the exchange rate falls from 120 yen per dollar to 100 yen per dollar, the dollar has ________ and the yen has ________.
A) depreciated; appreciated
B) appreciated; depreciated
C) depreciated; depreciated
D) appreciated; appreciated
Answer: A
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

27) Suppose $1 will buy 1.20 euros in January and 1.10 euros in December. As a result,
A) the dollar has appreciated.
B) the euro has appreciated.
C) the euro has depreciated.
D) U.S. exports have increased.
Answer: B
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

Currency	2007 exchange rate (per U.S. dollar)	2008 exchange rate (per U.S. dollar)
Euro	0.9954	1.0747
Japanese yen	102.20	114.90
Canadian dollar	1.44	1.50

28) The table above shows the exchange rates between various currencies and the U.S. dollar. Between 2007 and 2008, the U.S. dollar ________ against the euro and ________ against the Japanese yen.
A) depreciated; depreciated
B) appreciated; appreciated
C) appreciated; depreciated
D) depreciated; appreciated
Answer: B
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

29) The table above shows the exchange rates between various currencies and the U.S. dollar. Between 2007 and 2008, the Japanese yen ________ against the U.S dollar and the euro ________ against the U.S. dollar.
A) appreciated; appreciated
B) depreciated; appreciated
C) depreciated; depreciated
D) appreciated; depreciated
Answer: C
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

30) Suppose the exchange rate of the U.S. dollar was 1.50 British pounds = $1.00 on Wednesday, and on Monday the exchange rate was $0.75 = 1.00 British pound. Which of the following best explains what has happened between Wednesday and Monday?
A) The U.S. dollar appreciated against the British pound.
B) The British pound appreciated against the U.S. dollar.
C) The U.S. dollar depreciated against the British pound.
D) Both answers B and C are correct.
Answer: D
Topic: The Exchange Rate, Currency Appreciation and Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

31) When people who are holding the money of some other country want to exchange it for U.S. dollars, they ________ U.S. dollars and ________ that other country's money.
A) demand, supply
B) supply, supply
C) supply, demand
D) demand, demand
Answer: A
Topic: The Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

32) Which of the following creates a demand for U.S. dollars?
A) Toyota, a Japanese firm, purchasing land in Texas
B) a U.S. restaurant purchasing Mexican tomatoes
C) a U.S. tourist catching a show in London
D) a Japanese tourist catching a show in London
Answer: A
Topic: The Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

33) When the exchange rate falls, in the foreign exchange market the
A) quantity demanded of the currency increases.
B) demand for the currency increases.
C) quantity demanded of the currency decreases.
D) demand for the currency decreases.
Answer: A
Topic: Law of Demand for Foreign Exchange
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

34) The law of demand in the foreign exchange market refers to the relationship between the
A) exchange rate and the quantity of U.S. dollars demanded
B) interest rate and the exchange rate
C) interest rate and the quantity of U.S. dollars demanded
D) U.S. price level and the exchange rate
Answer: A
Topic: The Law of Demand for Foreign Exchange
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

35) The law of demand for dollars in the foreign exchange market means that the
A) lower the exchange rate, the greater the quantity of dollars demanded.
B) higher the exchange rate, the smaller the quantity of dollars demanded.
C) lower the exchange rate, the smaller the quantity of U.S. exports demanded.
D) Both answers A and B are correct.
Answer: D
Topic: The Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

36) With everything else the same, in the foreign exchange market the
A) larger the value of U.S. exports, the greater is the quantity of dollars demanded.
B) lower the exchange rate, the smaller the amount of U.S. exports.
C) the lower the exchange rate, the smaller is the expected profit from buying dollars.
D) the higher the exchange rate, the cheaper are U.S.-produced goods and services.
Answer: A
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

37) In the foreign exchange market, a change in which of the following will result in a movement along the demand curve for U.S. dollars?
A) the exchange rate
B) the U.S. interest rate
C) the interest rate in the foreign country
D) the expected future exchange rate
Answer: A
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

38) The demand curve for U.S. dollars slopes downward because as the dollar ________ U.S. goods become ________ expensive to foreign residents, so they purchase fewer U.S. goods, and the quantity of dollars demanded decreases.
A) appreciates; more
B) appreciates; less
C) depreciates; more
D) depreciates; less
Answer: A
Topic: The Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

39) When the U.S. exchange rate falls, U.S. goods become ________ to foreign residents and U.S. exports ________.
A) less expensive; increase
B) less expensive; decrease
C) more expensive; decrease
D) more expensive; increase
Answer: A
Topic: The Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

40) As the exchange rate ________, the ________ is the value of U.S. ________.
A) falls; greater; imports
B) falls; greater; exports
C) rises; greater; exports
D) rises; smaller; imports
Answer: B
Topic: The Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

41) As the value of U.S. exports ________, the quantity of ________ demanded increases.
A) increases; foreign currencies
B) increases; dollars
C) decreases; dollars
D) None of the above is correct because the value of U.S. exports has nothing to do with the quantity of dollars or foreign currency demanded.
Answer: B
Topic: Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

42) The quantity of dollars demanded by foreign nations increases as
A) U.S. residents purchase more foreign goods.
B) foreigners purchase more U.S. goods.
C) more U.S. residents travel abroad.
D) U.S. exports fall.
Answer: B
Topic: Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

43) Exports of U.S. goods creates a ________ U.S. dollars and creates a ________ foreign currencies.
A) demand for; demand for.
B) supply of; supply of
C) demand for; supply of
D) supply of; demand for
Answer: C
Topic: Law of Demand for Foreign Exchange, Exports
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

44) Suppose China Airlines wants to purchase a French Airbus. The price of the Airbus is 95 million Euro. If the exchange rate is 1 euro per 10 yuan, the price of this airplane to China Airlines is
A) 950 million yuan.
B) 85.5 million yuan.
C) 10 million yuan.
D) 9.5 million yuan.
Answer: A
Topic: Law of Demand for Foreign Exchange, Exports
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

45) Suppose China Airlines wants to purchase a French Airbus. The price of the Airbus is 95 million Euro. If the exchange rate is 1 euro per 9 yuan, the price of this airplane to China Airlines is
A) 855 million yuan.
B) 85.5 million yuan.
C) 83.6 million yuan.
D) 10.6 million yuan.
Answer: A
Topic: Law of Demand for Foreign Exchange, Exports
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

46) If nothing else changes, the ________ the current exchange rate, the ________ is the expected profit from holding dollars, all other things remaining the same.
A) higher; larger
B) lower; smaller
C) lower; larger
D) The premise of the question is wrong because the exchange rate has nothing to do with expected profit from holding dollars.
Answer: C
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

47) A factor helping determine demand for the dollar in the foreign exchange market is
A) the expected future exchange rate.
B) the expected future interest rate.
C) the amount of U.S. imports.
D) the supply of U.S. dollars.
Answer: A
Topic: Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

48) If the exchange rate falls, then the expected profit from holding the currency
A) does not change.
B) increases.
C) decreases.
D) can either increase or decrease.
Answer: B
Topic: Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

49) As the expected profit from holding dollars ________, the quantity of ________.
A) increases; dollars demanded increases
B) increases; dollars demanded decreases
C) decrease; foreign currency demanded decreases
D) None of the above answers is correct.
Answer: A
Topic: Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

50) The lower the exchange rate today, *ceteris paribus*, the
A) greater is the expected profit from buying U.S. dollars today and holding them.
B) smaller is the expected profit from buying U.S. dollars today and holding them.
C) greater is the expected profit from buying foreign currency today and holding it.
D) smaller the quantity of U.S. dollars demanded in the foreign exchange market today.
Answer: A
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

51) The higher the exchange rate today, the
A) smaller is the expected profit from buying U.S. dollars today and holding them.
B) greater is the expected profit from buying U.S. dollars today and holding them.
C) smaller is the expected profit from buying foreign currency today and holding it.
D) greater the quantity of U.S. dollars demanded in the foreign exchange market today.
Answer: A
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

52) When the U.S. exchange rate rises and the expected future exchange rate does not change, the expected profit from buying U.S. dollars today
A) also rises
B) falls
C) does not change
D) may rise, fall, or stay the same
Answer: B
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

Investor	Expected future value of a dollar (francs per dollar)
Investor A	120
Investor B	100
Investor C	85

53) Using the table above, if the current market value of the dollar is 125 francs per dollar,
A) investor A expects dollar appreciation, but B and C expect depreciation.
B) investor A expects dollar depreciation, but B and C expect appreciation.
C) all three investors expect the dollar to appreciate.
D) all three investors expect the dollar to depreciate.
Answer: D
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

54) Using the table above, if the current market value of the dollar is 125 francs,
A) investor A holds dollars, but B and C hold francs.
B) investor A holds francs, but B and C hold dollars.
C) all three investors hold francs.
D) all three investors hold dollars.
Answer: C
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

55) Using the table above, if the current market value of the dollar is 70 francs,
A) investor A expects dollar appreciation, but B and C expect depreciation.
B) investor A expects dollar depreciation, but B and C expect appreciation.
C) all three investors expect the dollar to appreciate.
D) all three investors expect the dollar to depreciate.
Answer: C
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

56) Using the table above, if the current market value of the dollar is 70 francs,
A) investor A holds dollars, but B and C hold francs.
B) investor A holds francs, but B and C hold dollars.
C) all three investors hold francs.
D) all three investors hold dollars.
Answer: D
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

57) Using the table above, if the current market value of the dollar is 90 francs,
A) investor A expects dollar appreciation, but B and C expect depreciation.
B) investor C expects dollar depreciation, but A and B expect appreciation.
C) all three investors expect the dollar to appreciate.
D) all three investors expect the dollar to depreciate.
Answer: B
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

58) Using the table above, if the current market value of the dollar is 110 francs,
A) investor A expects dollar appreciation, but B and C expect depreciation.
B) investor C expects dollar depreciation, but A and B expect appreciation.
C) all three investors expect the dollar to appreciate.
D) all three investors expect the dollar to depreciate.
Answer: A
Topic: The Law of Demand for Foreign Exchange, Expected Profit
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

59) When you arrive at the airport in Paris and go to the bank window to exchange dollars into euros, you are
A) selling euros to the French.
B) avoiding the use of foreign exchange markets.
C) contributing to U.S. exports.
D) None of the above answers is correct.
Answer: D
Topic: Supply in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

60) In the foreign exchange market, the higher the dollar's exchange rate, the
A) larger the supply of dollars.
B) smaller the quantity supplied of dollars.
C) smaller the supply of dollars.
D) larger the quantity supplied of dollars.
Answer: D
Topic: Law of Supply for Foreign Exchange
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

61) When the U.S. exchange rate rises, foreign goods become ________ and U.S. imports ________.
A) less expensive; increase
B) more expensive; decrease
C) less expensive; decrease
D) more expensive; increase
Answer: A
Topic: The Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

62) Other things remaining the same, the ________ the exchange rate for dollars, the greater the ________ in the foreign exchange market.
A) higher; quantity of dollars supplied
B) higher; quantity of dollars demanded
C) lower; value of U.S. imports
D) higher; expected profits from holding dollars
Answer: A
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

63) The demand for Mexican tomatoes by an American food grocery chain creates a
A) demand for the U.S. dollar.
B) demand for an interest rate differential.
C) supply of Mexican pesos.
D) supply of U.S. dollars.
Answer: D
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

64) Consider the market for dollars. If the exchange rate rises from 2 pesos per dollar to 4 pesos per dollar,
A) the supply curve of dollars shifts leftward.
B) the supply curve of dollars shifts rightward.
C) there is an upward movement along the supply curve for dollars.
D) there is a downward movement along the supply curve for dollars.
Answer: C
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

65) As the exchange rate ________, the quantity of dollars ________ on the foreign exchange market ________.
A) rises; supplied; increases
B) falls; supplied; increases
C) rises; demanded; increases
D) falls; demanded; decreases
Answer: A
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

66) In the foreign exchange market, the supply curve for dollars slopes upwards because
A) as the exchange rate rises, imports become more expensive, and more dollars are supplied to pay for the imports.
B) as the exchange rate rises, imports become cheaper, and more dollars are supplied to pay for the increase in the quantity of imports.
C) as the exchange rate rises, more dollars are supplied since the profit from selling dollars falls.
D) supply curves always slope upwards.
Answer: B
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

67) In the foreign exchange market, which of the following results in a movement along the supply curve of dollars?
A) a change in the expected future exchange rate
B) a change in the U.S. interest rate
C) a change in the current exchange rate
D) None of the above answers are correct.
Answer: C
Topic: The Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

68) When a good is imported into the United States, there is created a
A) supply of foreign currency with no effect on the market for the dollar.
B) demand for dollars with no effect on markets for foreign currencies.
C) supply of foreign currencies and a demand for dollars.
D) demand for foreign currencies and a supply of dollars.
Answer: D
Topic: Law of Supply for Foreign Exchange, Imports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

69) Other things remaining the same, the
A) larger the value of U.S. imports, the smaller is the quantity of foreign currency demanded.
B) larger the value of U.S. imports, the greater is the quantity of U.S. dollars supplied to the foreign exchange market.
C) lower the exchange rate, the cheaper are foreign-produced goods and services.
D) higher the exchange rate, the greater is the expected profit from selling dollars.
Answer: B
Topic: Law of Supply for Foreign Exchange, Imports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

70) The larger the value of U.S. imports, the greater the quantity of ________ causing the quantity supplied of dollars to ________.
A) U.S. dollars demanded; increase
B) U.S. dollars demanded; decrease
C) foreign currency demanded; increase
D) foreign currency demanded; decrease
Answer: C
Topic: Law of Supply for Foreign Exchange, Imports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

71) The ________ the exchange rate, the ________ are foreign-produced goods and hence the greater the quantity of dollars supplied.
A) higher; cheaper
B) lower; cheaper
C) higher; more expensive
D) lower; more expensive
Answer: A
Topic: Law of Supply for Foreign Exchange, Imports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

72) The ________ the exchange rate, the ________ are foreign-produced goods and hence the smaller the quantity of dollars supplied.
A) lower; more expensive
B) lower; cheaper
C) greater; cheaper
D) greater; more expensive
Answer: A
Topic: Law of Supply for Foreign Exchange, Imports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

73) A factor determining the supply of U.S. dollars in the foreign exchange market is the
A) expected future exchange rate.
B) expected future interest rate in the United States.
C) U.S. supply of exports.
D) expected future interest rate in foreign countries.
Answer: A
Topic: Law of Supply for Foreign Exchange, Expected Profit
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

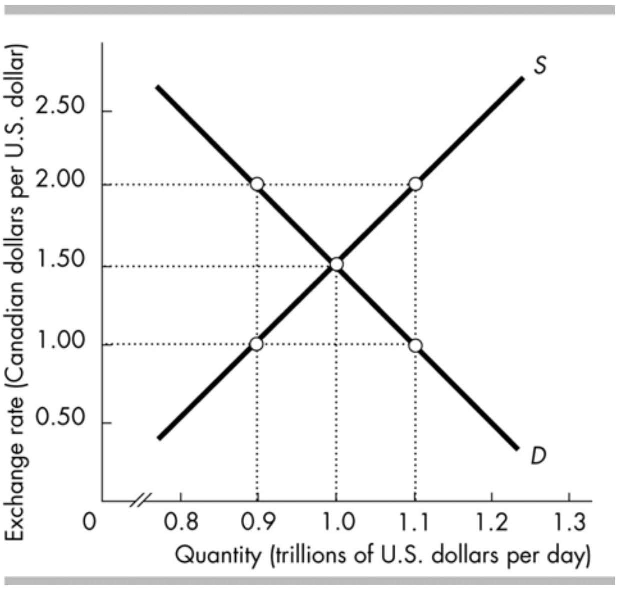
74) The ________ the expected profit from holding a foreign currency, the greater is the ________ in the foreign exchange market.
A) larger; quantity demanded of dollars
B) smaller; quantity demanded of foreign currency
C) larger; quantity supplied of dollars
D) None of the above is correct because the expected profit has nothing to do with the supply and demand for dollars or foreign currency.
Answer: C
Topic: Law of Supply for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

75) The higher the dollar's exchange rate, the ________ the expected profit from holding dollars and so ________ dollars are supplied.
A) larger; more
B) larger; fewer
C) smaller; more
D) smaller; fewer
Answer: C
Topic: Law of Supply for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

76) Consider the market for dollars. The higher the exchange rate, the ________ is the expected profit from holding foreign currency and the greater is the ________.
A) larger; quantity of dollars supplied
B) larger; leftward shift in the demand curve for dollars
C) smaller; quantity of dollars supplied
D) smaller; leftward shift in the demand curve for dollars
Answer: A
Topic: Law of Supply for Foreign Exchange, Expected Profit
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

77) If the equilibrium exchange rate for the dollar is 110 yen per dollar and the current exchange rate is 120 yen per dollar, then the
A) supply curve of U.S. dollars shifts rightward.
B) dollar will depreciate.
C) dollar will appreciate.
D) demand curve for U.S. dollars shifts rightward.
Answer: B
Topic: Equilibrium Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

78) Consider the market for euros. Suppose the exchange rate is ________ its equilibrium. This means that the quantity of euros ________ is greater than the quantity of euros ________ and the exchange rate will ________.
A) above; supplied; demanded; fall
B) below; supplied; demanded; rise
C) above; demanded; supplied; fall
D) below; demanded; supplied; fall
Answer: A
Topic: Equilibrium Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking



79) In the figure above, the equilibrium exchange rate is: $1 U.S. equals
A) $2.00 Canadian.
B) $1.50 Canadian.
C) $0.50 Canadian.
D) none of the above
Answer: B
Topic: Equilibrium Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

80) If the exchange rate between the dollar and Japanese yen is below the equilibrium exchange rate, there will be a ________ of dollars, and the exchange rate will ________.
A) surplus; fall to the equilibrium level
B) shortage; change only when the supply curve shifts leftward
C) shortage; rise to the equilibrium level
D) surplus; rise to the equilibrium level
Answer: C
Topic: Equilibrium Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

81) If the exchange rate is above equilibrium, there will be ________ in the foreign exchange market.
A) a surplus
B) a shortage
C) a decrease in demand
D) an increase in demand
Answer: A
Topic: Equilibrium Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

82) Suppose the exchange rate between the U.S. dollar and the French franc is 0.25 francs per dollar. If a television sells for 100 francs in France, what is the dollar price of the television set?
A) $400
B) $25
C) $50
D) $200
Answer: A
Topic: Study Guide Question, The Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

83) Suppose that a dollar buys 120 yen. If a VCR sells for 18,600 yen in Japan, the price of the VCR in dollars is ________.
A) $186.00
B) $223.20
C) $120.00
D) $155.00
Answer: D
Topic: Study Guide Question, The Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

84) Suppose that the yen-dollar foreign exchange rate changes from 130 yen per dollar to 140 yen per dollar. Then the yen has
A) depreciated against the dollar, and the dollar has appreciated against the yen.
B) depreciated against the dollar, and the dollar has depreciated against the yen.
C) appreciated against the dollar, and the dollar has appreciated against the yen.
D) appreciated against the dollar, and the dollar has depreciated against the yen.
Answer: A
Topic: Study Guide Question, Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

85) Suppose the peso-dollar foreign exchange rate changes from 50 pesos per dollar to 30 pesos per dollar. Then the peso has ________ against the dollar and the dollar has ________ against the peso.
A) appreciated; depreciated
B) appreciated; appreciated
C) depreciated; appreciated
D) depreciated; depreciated
Answer: A
Topic: Study Guide Question, Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

86) If the U.S. exchange rate rises, the price to foreigners of U.S.-produced goods and services ________ and the quantity of U.S. dollars demanded ________.
A) rises; decreases
B) rises; increases
C) falls; decreases
D) falls; increases
Answer: A
Topic: Study Guide Question, Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2 Exchange Rate Fluctuations

1) Important factors that change the demand for dollars and shift the demand curve for dollars include which of the following?
I. Interest rates around the world.
II. The current exchange rate.
III. The expected future exchange rate.
A) I and II
B) I and III
C) II
D) I, II, and III
Answer: B
Topic: Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) With everything else the same, which of the following would increase the demand for U.S. dollars in the foreign exchange market?
I. a rise in the U.S. interest rate
II. a fall in interest rates in foreign countries
III. a rise in the expected future exchange rate
A) I only
B) I and II only
C) I and III only
D) I, II, and III
Answer: D
Topic: Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) The demand for dollars in the foreign exchange market will increase (so that the demand curve shifts rightward) if
A) the U.S. interest rate differential falls.
B) the expected future exchange rate falls.
C) the exchange rate for the dollar falls.
D) None of the above answers is correct.
Answer: D
Topic: Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) In the foreign exchange market, an increase in the world demand for U.S. exports shifts
A) demand curve for U.S. dollars rightward
B) demand curve for U.S. dollars leftward
C) supply curve for U.S. dollars leftward
D) supply curve for U.S. dollars rightward
Answer: A
Topic: Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) Airbus is a European jet airline producer. Indian Airlines wants to buy 23 Airbus planes from Airbus, due to increased demand for world travel. As a result, the
A) demand curve for euros shifts rightward.
B) demand curve for euros shifts leftward.
C) quantity demanded for euros increases as the euro/rupee exchange rate increases.
D) quantity demand for euros decreases, on matter what the euro/rupee exchange rate is.
Answer: A
Topic: Changes in the Demand for Dollars, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) Hyundai is a large South Korean company that produces finished steel products. Hyundai plans to buy raw steel from U.S. Steel. As a result, the
A) demand curve for U.S. dollars shifts rightward.
B) demand curve for U.S. dollars shifts leftward.
C) demand curve for South Korean won shifts rightward.
D) demand curve for South Korean won shifts leftward.
Answer: A
Topic: Changes in the Demand for Dollars, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) Hyundai is a large South Korean company that produces finished steel products. Hyundai plans to buy raw steel from U.S. Steel. As a result, the demand curve for U.S. dollars ________ and the demand curve for South Korean won ________.
A) shifts rightward; does not shift
B) shifts rightward; shifts leftward
C) does not shift; shifts leftward
D) shifts leftward; shifts rightward.
Answer: A
Topic: Changes in the Demand for Dollars, Exports
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

8) Airbus is a European jet airline producer. Indian Airlines wants to buy 23 Airbus planes from Airbus, due to increased demand for world travel. As a result,
A) the demand curve for European euros and the supply curve for Indian rupees both shift rightward.
B) the demand curve for European euros shifts rightward and the supply curve for Indian rupees shifts leftward.
C) only the demand curve for Indian rupees shifts rightward.
D) only the demand curve for European euros shifts rightward.
Answer: A
Topic: Changes in the Demand for Dollars, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) Saudi Telecom is a major producer of telecommunications equipment in Saudi Arabia. The Free Market Iraqi Conglomerate (FMIC) is a collections of over 100 firms that wish to upgrade the communications infrastructure of Iraqi. When FMIC buys $4.5 million U.S. dollars worth of equipment from Saudi Telecom, the
A) demand curve for Saudi Arabian riyals and the supply curve for Iraqi dinars both shift rightward.
B) demand curve for Saudi Arabian riyals and the supply curve for U.S. dollars both shift rightward.
C) demand curve for Iraqi dinars and the supply curve for U.S. dollars both shift rightward.
D) demand curve for U.S. dollars shifts rightward.
Answer: A
Topic: Changes in the Demand for Dollars, Exports
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

10) The U.S. interest rate minus the foreign interest rate is called the ________.
A) foreign interest rate differential
B) U.S. bond rate differential
C) U.S. interest rate differential
D) U.S. stock yield differential
Answer: C
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

11) Suppose the U.S. interest rate is 6 percent and the world interest rate is 5 percent. The U.S. interest differential is
A) -1 percent.
B) 1.2 percent.
C) 1 percent.
D) -0.83 percent.
Answer: C
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) Other things remaining the same, the U.S. interest rate differential increases if the U.S. interest rate
A) rises and foreign interest rates remain constant.
B) falls and foreign interest rates remain constant.
C) falls and foreign interest rates rise.
D) remains constant and foreign interest rates rise.
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) Which of the following occurrences would NOT shift the demand curve for U.S. dollars in the foreign exchange market?
A) an increase in the U.S. exchange rate
B) an increase in the expected future U.S. exchange rate
C) an increase in U.S. interest rates
D) an increase in foreign interest rates
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

14) The interest rate in Canada rises while the interest rate in the United States does not change. The
A) demand curve for Canadian dollars will shift leftward.
B) demand curve for Canadian dollars will shift rightward.
C) demand curve for U.S. dollars will shift rightward.
D) demand curves Canadian and U.S. dollars will remain unchanged.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

15) If the U.S. interest rate rises while interest rates in the rest of the world do not change, the higher U.S. interest rate
A) decreases the demand for dollars.
B) increases the demand for dollars.
C) has no effect on the demand for dollars.
D) will stop all trading between the currencies of the U.S. and other countries.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

16) An increase in the interest rate in the United States compared to the interest rate in Great Britain will
A) increase the U.S. interest rate differential.
B) increase the demand for pounds.
C) shift the demand curve for dollars rightward.
D) Both answers A and C are correct.
Answer: D
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

17) The demand for dollars in the foreign exchange market will decrease and the demand curve will shift leftward if
A) the U.S. interest rate differential decreases.
B) the expected future exchange rate rises.
C) the exchange rate for the dollar rises.
D) None of the above answers is correct.
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

18) Suppose the current exchange rate between the euro and the United States dollar is 1.15 euros per dollar. If interest rates in the United States increase and interest rates in Europe remain unchanged then
A) the demand for dollars will increase.
B) the demand for dollars will decrease.
C) the demand for euros will increase.
D) None of the above answers is correct.
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) If the interest rate in the United States increases, then in the foreign exchange market the
A) demand for U.S. dollars will remain unchanged.
B) demand for U.S. dollars will increase.
C) demand for U.S. dollars will decrease.
D) supply of U.S. dollars will increase.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

20) If the interest rate on Japanese yen assets falls, the
A) quantity of dollars demanded will increase.
B) quantity of dollars demanded will decrease.
C) demand for dollars will increase.
D) demand for dollars will decrease.
Answer: C
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

21) If the interest rate on Swiss franc assets increases, the
A) quantity of dollars demanded will decrease.
B) demand for dollars will increase.
C) demand for dollars will decrease.
D) quantity of dollars demanded will increase.
Answer: C
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

22) Today, the dollar is worth 1.15 euros. Due to changes in economic conditions, in one month people come to expect the dollar will be worth 1.20 euros. This belief
A) increases the demand for dollars.
B) decreases the demand for dollars.
C) increases the demand for euros.
D) increases the value of exports to Europe.
Answer: A
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

23) If there is an increase in the expected future U.S. exchange rate, there is
A) an upward movement along the demand curve for dollars.
B) a downward movement along the demand curve for dollars.
C) a leftward shift of the demand curve for dollars.
D) a rightward shift of the demand curve for dollars.
Answer: D
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

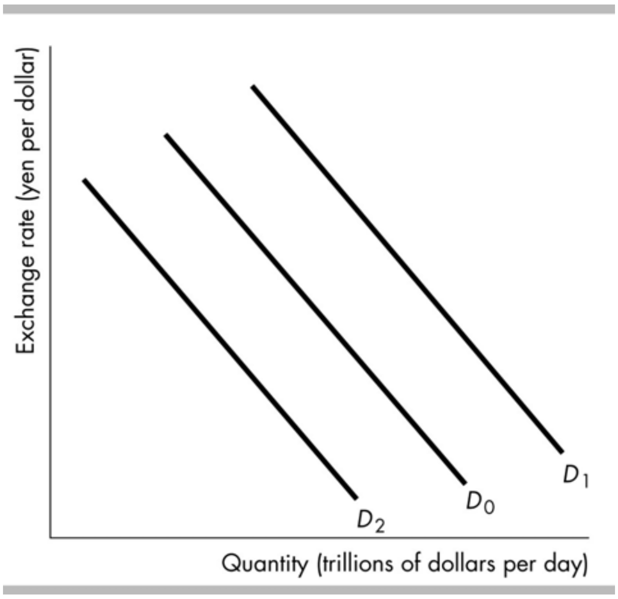
24) If people expect the foreign exchange rate for dollars to rise in the future,
A) the demand for dollars decreases.
B) the demand for dollars increases.
C) the demand for dollars is unaffected.
D) there is a movement along the demand curve for dollars.
Answer: B
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

25) U.S. residents come to believe that the dollar will depreciate in the future, that is, the exchange rate in the future will be lower than the current exchange rate. As a result,
A) the demand curve for dollars shifts rightward.
B) the demand curve for dollars shifts leftward.
C) there is a movement upward along the demand curve for dollars.
D) None of the above answers are correct.
Answer: B
Topic: Change in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

26) U.S. residents come to believe that the dollar will appreciate in the future, that is, the exchange rate in the future will be higher than the current exchange rate. As a result,
A) the demand curve for dollars shifts rightward.
B) the demand curve for dollars shifts leftward.
C) there is a movement downward along the demand curve for dollars.
D) None of the above answers are correct.
Answer: A
Topic: Change in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

27) If growth in the United States speeds up so that investors believe they can make a bigger profit from U.S. assets, the ________ U.S. dollars will ________.
A) demand for; increase
B) demand for; decrease
C) supply of; increase
D) supply of; decrease
Answer: A
Topic: Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

28) Today the U.S. dollar is worth 1.5 Canadian dollars. Because of changes in economic conditions, people come to believe that by the end of the month the U.S. dollar will be worth 1.2 Canadian dollars. This belief
A) increases the demand for U.S. dollars.
B) decreases the demand for U.S. dollars.
C) decreases the demand for Canadian dollars.
D) decreases the value of exports to Canada.
Answer: B
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking



29) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_1 could occur when
A) the expected future exchange rate decreases.
B) the U.S. interest rate rises.
C) people expect that the dollar will depreciate.
D) foreign interest rates increase.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

30) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_1 could occur when
A) the expected future exchange rate falls.
B) the U.S. interest rate drops.
C) people expect that the dollar will depreciate.
D) foreign interest rates drop.
Answer: D
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

31) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_2 could occur when
A) the U.S. interest rate falls.
B) the U.S. interest rate rises.
C) people expect that the dollar will appreciate.
D) foreign interest rates fall.
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

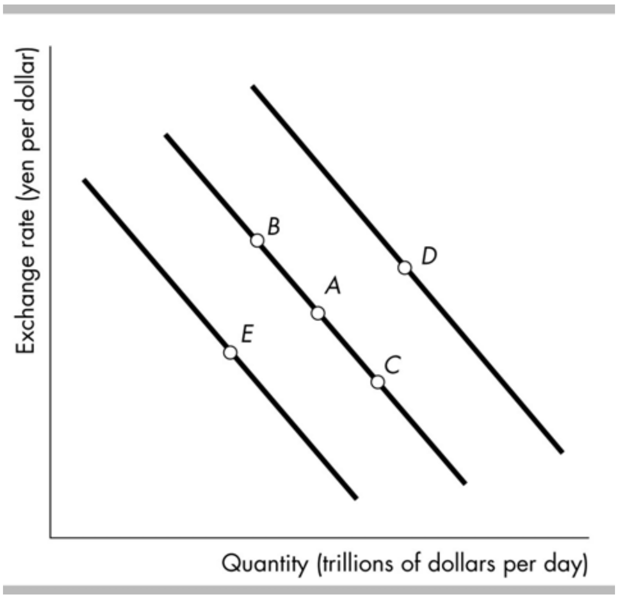
32) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_2 could occur when
A) the expected future exchange rate increases.
B) the U.S. interest rate falls.
C) people expect that the dollar will appreciate.
D) foreign interest rates fall.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

33) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_2 could occur when
A) the expected future exchange rate increases.
B) the U.S. interest rate rises.
C) people expect that the dollar will appreciate.
D) foreign interest rates rise.
Answer: D
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

34) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_1 could occur when
A) foreign interest rates increase.
B) the U.S. interest rate falls.
C) people expect that the dollar will depreciate.
D) the expected future exchange rate increases.
Answer: D
Topic: Change in Demand for Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

35) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_1 could occur when
A) the expected future exchange rate falls.
B) the U.S. interest rate decreases.
C) people expect that the dollar will appreciate.
D) foreign interest rates increase.
Answer: C
Topic: Change in Demand for Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

36) In the figure above, the shift in the demand curve for U.S. dollars from D_0 to D_2 could occur when
A) the expected future exchange rate increases.
B) the U.S. interest rate rises.
C) people expect that the dollar will depreciate.
D) foreign interest rates fall.
Answer: C
Topic: Change in Demand for Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills



37) The above figure shows the demand curve for dollars in the yen/dollar exchange market. A movement from point *A* to point *B* means that the
A) quantity supplied of dollars has increased.
B) quantity demanded of dollars has increased.
C) quantity demanded of dollars has decreased.
D) quantity demanded of yen has decreased.
Answer: C
Topic: Law of Demand for Foreign Exchange
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

38) In the above figure, suppose the economy is initially at point *A*. The interest rate in Japan rises relative to the interest rate in the United States. As a result, there will be a change from point *A* to a point such as ________.
A) point *B*
B) point *C*
C) point *D*
D) point *E*
Answer: D
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

39) In the above figure, suppose the economy is initially at point *A*. People come to expect the future U.S. exchange rate to be lower. As a result, there is a change from point *A* to a point such as ________.
A) point *B*
B) point *C*
C) point *D*
D) point *E*
Answer: D
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

40) In the above figure, suppose the economy is initially at point *A*. People come to expect the future U.S. exchange rate to be higher. As a result there is a change from point *A* to a point such as ________.
A) point *B*
B) point *C*
C) point *D*
D) point *E*
Answer: C
Topic: Changes in Demand for Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

41) A change in which of the following changes the supply of dollars and shifts the supply curve of dollars?
I. An increase in the exchange rate.
II. A change in interest rates.
III. A decrease in the expected future exchange rate.
A) I
B) I and II
C) II and III
D) I, II, and III
Answer: C
Topic: Changes in the Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

42) Interest rates in the United States rise relative to interest rates in other countries. As a result, in the foreign exchange market
A) the supply curve of dollars shifts leftward.
B) the supply curve of dollars shifts rightward.
C) the demand curve for dollars shifts leftward.
D) there is an upward movement along the supply curve of dollars.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

43) With everything else the same, in the foreign exchange market which of the following increases the supply of U.S. dollars?
I. a fall in the U.S. interest rate
II. a fall in interest rates in foreign countries
III. a rise in expected future exchange rate
A) I only
B) I and II only
C) I and III only
D) I, II, and III
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

44) If interest rates in Mexico decrease while the interest rates in the United States remain unchanged then
A) the supply of Mexican pesos will increase.
B) the supply of Mexican pesos will decrease.
C) the supply of U.S. dollars will increase.
D) None of the above answers is correct.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

45) If interest rates in Japan rise and those in the United States do not change, there is
A) a decrease in the supply of dollars.
B) an increase in the supply of dollars.
C) a downward movement along the supply curve for dollars.
D) None of the above answers is correct.
Answer: B
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

46) If the U.S. interest rate differential increases, then in the foreign exchange market the
A) quantity of U.S. dollars supplied increases.
B) supply of U.S. dollars decreases.
C) demand for U.S. dollars does not change.
D) supply of U.S. dollars increases.
Answer: B
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

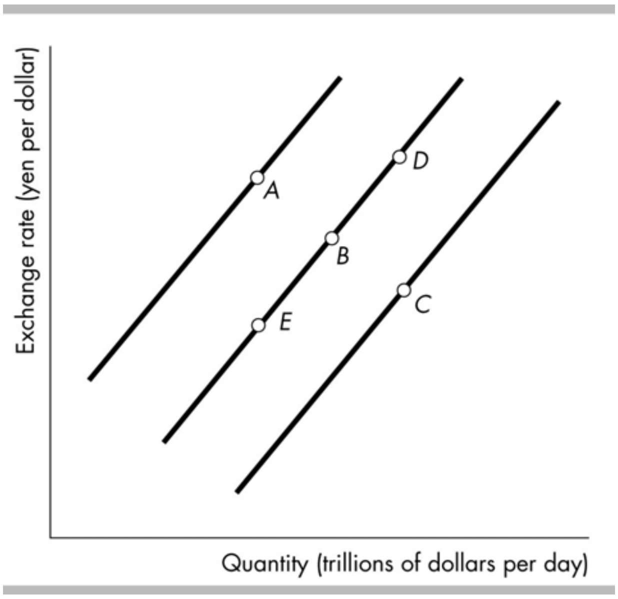
47) The supply curve of U.S. dollars shifts leftward. This could have been influenced by ________.
A) a rise in the U.S. interest rate differential
B) a fall in the expected future exchange rate
C) an increase in the U.S. exchange rate
D) a decrease in the U.S. exchange rate
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

48) As the expected future exchange rate for dollars increases,
A) the expected profit from selling U.S. dollars today falls.
B) the supply of U.S. dollars decreases.
C) the U.S. interest rate will fall.
D) Both answers A and B are correct.
Answer: D
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

49) People come to expect the exchange rate for the dollar to rise from 90 yen per dollar to 111 yen per dollar in a month. As a result,
A) the supply curve of dollars shifts leftward.
B) the supply curve of dollars shifts rightward.
C) the demand curve for dollars shifts leftward.
D) there is a downward movement along the supply curve of dollars.
Answer: A
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

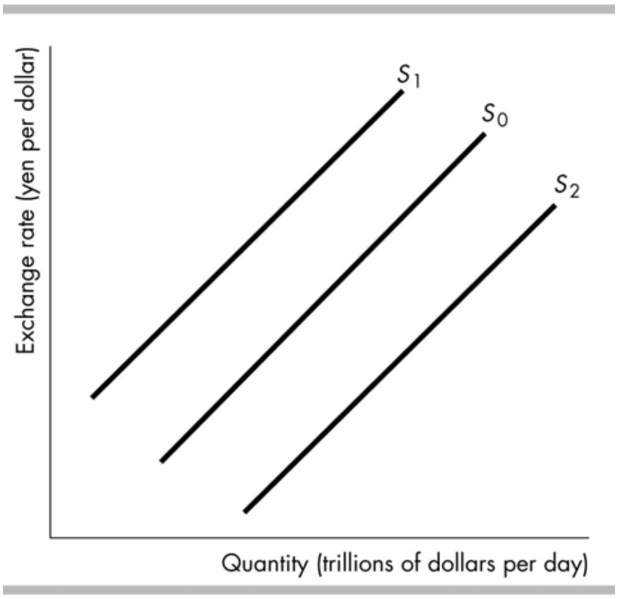
50) If the expected future exchange rate rises, the currency's
A) quantity supplied increases.
B) supply decreases.
C) supply increases.
D) exchange rate falls.
Answer: B
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

51) The supply of dollars in the foreign exchange market decreases and that the supply curve shifts leftward if
A) the U.S. interest rate differential decreases.
B) the expected future exchange rate rises.
C) the exchange rate for the dollar rises.
D) All of the above are correct.
Answer: B
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking



52) In the figure above, suppose the economy is initially at point *B*. Then the interest rate in Japan rises relative to the interest rate in the United States. This change ________ the supply of dollars and the market moves to a point such as ________.
A) decreases; *A*
B) decreases; *E*
C) increases; *D*
D) increases; *C*
Answer: D
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

53) In the figure above, suppose the economy is initially at point *B*. If people come to believe that the exchange rate will fall in the future, the supply of dollars ________ and the market moves to point such as ________.
A) decreases; *A*
B) decreases; *E*
C) increases; *D*
D) increases; *C*
Answer: D
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills



54) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_1 could occur when
A) the U.S. interest rate differential increases.
B) the U.S. interest rate differential decreases.
C) the expected future exchange rate falls.
D) the current exchange rate falls.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

55) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_1 could occur when
A) the U.S. interest rate falls.
B) foreign interest rates fall.
C) the expected future exchange rate falls.
D) the current exchange rate falls.
Answer: B
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

56) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_1 could occur when
A) the U.S. interest rate rises.
B) foreign interest rates rise.
C) the expected future exchange rate falls.
D) the current exchange rate rises.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

57) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_2 could occur when
A) the U.S. interest rate falls.
B) the expected future exchange rate rises.
C) the U.S. interest rate differential increases.
D) the current exchange rate falls.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

58) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_2 could occur when
A) foreign interest rates rise.
B) the expected future exchange rate rises.
C) the U.S. interest rate rises.
D) the current exchange rate falls.
Answer: A
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

59) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_1 could occur when
A) the expected future exchange rate rises.
B) the U.S. interest rate differential decreases.
C) the expected future exchange rate falls.
D) the current exchange rate falls.
Answer: A
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

60) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_2 could occur when
A) the current exchange rate rises.
B) the current exchange rate falls.
C) the expected future exchange rate rises.
D) the expected future exchange rate falls.
Answer: D
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

61) In the figure above, the shift in the supply curve for U.S. dollars from S_0 to S_2 could occur when
A) the expected future exchange rate falls.
B) the U.S. interest rate differential increases.
C) the expected future exchange rate rises.
D) the current exchange rate falls.
Answer: A
Topic: Changes in Supply of Dollars, Expected Future Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

62) If the U.S. interest rate differential increases, in the foreign exchange market the demand for U.S. dollars ________ and the supply of U.S. dollars ________.
A) increases; increases
B) increases; decreases
C) decreases; increases
D) decreases; decreases
Answer: B
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

63) When the U.S. interest rate rises relative to that in other counties, in the foreign exchange market the demand for U.S. dollars ________ and the supply of U.S. dollars ________.
A) increases; increases
B) increases; decreases
C) decreases; increases
D) decreases; decreases
Answer: B
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

64) Other things remaining the same, if the U.S. interest rate differential increases, the demand curve for U.S. dollars shifts ________ and the supply curve of U.S. dollars shifts ________.
A) rightward; rightward
B) rightward; leftward
C) leftward; rightward
D) leftward; leftward
Answer: B
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

65) If the Federal Reserve increases interest rates,
A) the demand curve for U.S. dollars shifts rightward and the supply curve of U.S. dollars shifts leftward.
B) the demand curve for U.S. dollars shifts leftward and the supply curve of U.S. dollars shifts rightward.
C) the demand curve for U.S. dollars and the demand curve for European euros both shift rightward.
D) only the demand curve for U.S. dollars shifts rightward.
Answer: A
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

66) If the Federal Reserve increases interest rates, *ceteris paribus*,
A) the supply curve of U.S. dollars shifts leftward and the supply curve of European euros shifts rightward.
B) the demand curve for U.S. dollars shifts leftward and the supply curve of U.S. dollars shifts rightward.
C) the demand curve for U.S. dollars and the demand curve for European euros both shift rightward.
D) only the demand curve for U.S. dollars shifts rightward.
Answer: A
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

67) If the European Central Bank increases interest rates,
A) the demand curve for European euros shifts rightward and the supply curve of European euros shifts leftward.
B) the demand curve for European euros shifts leftward and the supply curve of European euros shifts rightward.
C) the demand curve for European euros and the demand curve for U.S. dollars both shift rightward.
D) only the demand curve for European euros shifts rightward.
Answer: A
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

68) Other things remaining the same, if the expected future exchange rate rises, the demand curve for U.S. dollars shifts ________ and the supply curve of U.S. dollars shifts ________.
A) rightward; rightward
B) rightward; leftward
C) leftward; rightward
D) leftward; leftward
Answer: B
Topic: Changes in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

69) Relative to the yen, from 2005-2007 the U.S. dollar
A) appreciated due to an increase in the interest rate differential and expectations of a higher future exchange rate.
B) appreciated due to a decrease in the interest rate differential and expectations of a lower future exchange rate.
C) depreciated due to an increase in the interest rate differential and expectations of a higher future exchange rate.
D) depreciated due to a decrease in the interest rate differential and expectations of a lower future exchange rate.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

70) Relative to the yen, from 2007-2009 the U.S. dollar
A) appreciated due to an increase in the interest rate differential and expectations of a higher future exchange rate.
B) appreciated due to a decrease in the interest rate differential and expectations of a lower future exchange rate.
C) depreciated due to an increase in the interest rate differential and expectations of a higher future exchange rate.
D) depreciated due to a decrease in the interest rate differential and expectations of a lower future exchange rate.
Answer: D
Topic: Changes in the Exchange Rate
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

71) The U.S. dollar will depreciate in value if
A) the demand curve for U.S. dollars shifts rightward.
B) the demand curve for U.S. dollars shifts leftward.
C) the supply curve of U.S. dollars shifts rightward.
D) Both answers B and C are correct.
Answer: D
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

72) The U.S. dollar will depreciate in value if
A) the demand for the dollar increases.
B) the demand for the dollar decreases.
C) the supply of foreign exchange decreases.
D) U.S. citizens choose to buy fewer foreign goods.
Answer: B
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

73) The U.S. dollar will appreciate in value if
A) the demand curve for U.S. dollars shifts rightward.
B) the demand curve for U.S. dollars shifts leftward.
C) the supply curve of U.S. dollars shifts rightward.
D) Americans choose to buy more foreign goods.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

74) Suppose $1 will buy 150 yen in January and 200 yen in December. This change could have occurred if the
A) demand curve for dollars shifted rightward.
B) demand curve for dollars shifted leftward.
C) supply curve of dollars shifted rightward.
D) demand curve for yen shifted rightward.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

75) If the demand for a country's currency increases, the currency
A) appreciates.
B) depreciates.
C) stays the same.
D) could either appreciate, depreciate, or stay the same.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

76) An increase in the U.S. demand for imports will ________ the supply of dollars and lead the dollar to ________.
A) increase; appreciate
B) decrease; appreciate
C) increase; depreciate
D) decrease; depreciate
Answer: C
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

77) Which of the following will lead to an appreciation of the U.S. dollar against the British pound?
A) an increase in British demand for U.S. imports
B) an increase in U.S. demand for British imports
C) an increase in British interest rates
D) a decrease in British demand for U.S. assets
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

78) Assume that there is an increased demand in the United States for European wines. If all other factors are held constant, this change will result in
A) an increase in the exchange rate for euros.
B) an appreciation of the dollar.
C) a movement along the demand curve for euros.
D) a decrease in the value of the euro.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

79) An increase in foreign demand for U.S. exports will ________ the demand for dollars and lead the dollar to ________.
A) increase; appreciate
B) increase; depreciate
C) decrease; appreciate
D) decrease; depreciate
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Modified 10th edition
AACSB: Reflective Thinking

80) An increase in the Japanese interest rate will ________ the demand for dollars and lead the dollar to ________.
A) increase; appreciate
B) increase; depreciate
C) decrease; appreciate
D) decrease; depreciate
Answer: D
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

81) An increase in the Japanese interest rate will ________ the supply of dollars and lead the dollar to ________.
A) increase; appreciate
B) increase; depreciate
C) decrease; appreciate
D) decrease; depreciate
Answer: B
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

82) Which of the following will lead to a depreciation of the dollar against the British pound?
A) an increase in British demand for U.S. imports
B) an increase in U.S. interest rates
C) a decrease in British demand for U.S. assets
D) a decrease in U.S. demand for British goods
Answer: C
Topic: Changes in the Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

83) If the Federal Reserve raises the U.S. interest rate, foreigners'
A) demand for U.S. dollars will increase and the exchange rate will rise.
B) demand for U.S. dollars will decrease and the exchange rate will fall.
C) demand for U.S. dollars will increase and the exchange rate will fall.
D) demand for U.S. dollars will decrease and the exchange rate will rise.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

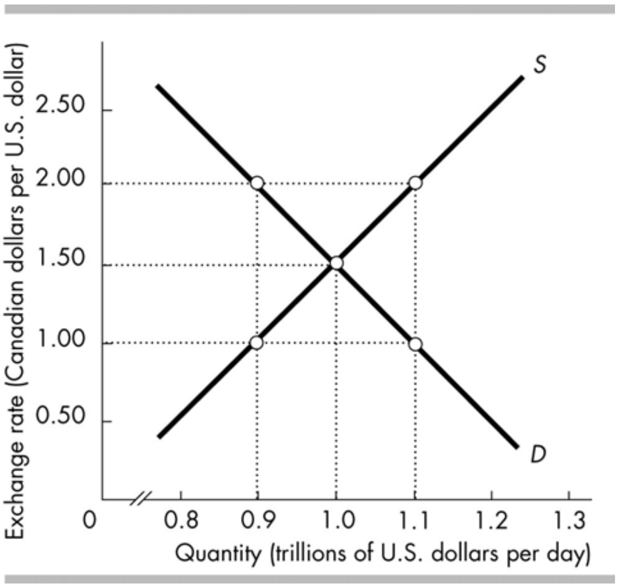
84) Suppose the exchange rate for the U.S. dollar rises. This could be caused by
A) an increase in U.S. import demand.
B) a decrease in the world demand for U.S. exports.
C) a fall in the expected future exchange rate.
D) an increase in the U.S. interest rate differential.
Answer: D
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: New 10th edition
AACSB: Analytical Skills

85) Suppose that the U.S. exchange rate is expected to fall in the future. As a result, in the foreign exchange market, there will be
A) an increase in the demand for dollars, a decrease in the supply of dollars, and a rise in the equilibrium exchange rate.
B) an increase in the demand for dollars, a decrease in the supply of dollars, and a fall in the equilibrium exchange rate.
C) a decrease in the demand for dollars, an increase in the supply of dollars, and a rise in the equilibrium exchange rate.
D) a decrease in the demand for dollars, an increase in the supply of dollars, and a fall in the equilibrium exchange rate.
Answer: D
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

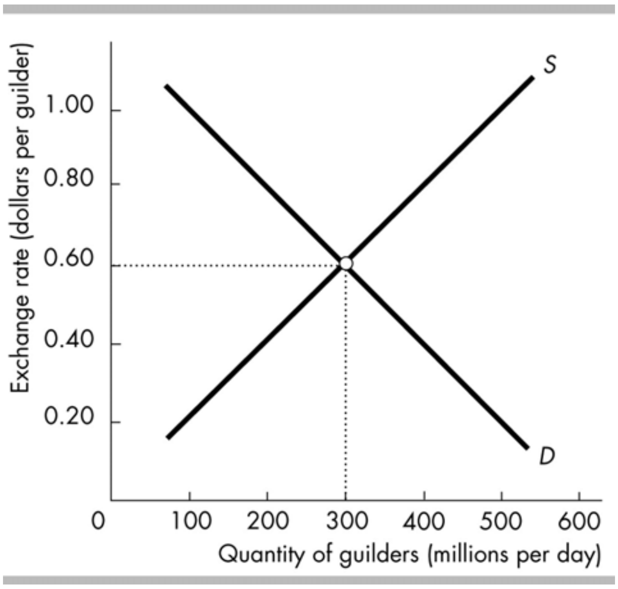
86) Suppose the market for dollars is in equilibrium, then the expected future exchange rate rises. What effect does this change have on the current exchange rate?
A) It will rise.
B) It will fall.
C) It will remain unchanged.
D) Because both the supply and demand curves shift, the effect on the exchange rate is unpredictable.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Modified 10th edition
AACSB: Reflective Thinking

87) If people expect the dollar to depreciate, then the
A) demand for dollars will decrease, the supply of dollars will increase, and the exchange rate will fall.
B) demand for dollars will decrease, the supply of dollars will not change, and the exchange rate will fall.
C) supply of dollars will increase, the demand for dollars will not change, and the exchange rate will fall.
D) demand for dollars will increase, the supply of dollars will decrease, and the exchange rate will rise.
Answer: A
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

88) Suppose the exchange rate for the U.S. dollar falls. This could be caused by
A) a decrease in U.S. import demand.
B) an increase in the world demand for U.S. exports.
C) an increase in the U.S. interest rate differential.
D) a fall in the expected future exchange rate.
Answer: D
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: New 10th edition
AACSB: Analytical Skills



89) In the figure above, an increase in the U.S. interest rate relative to that in Canada shifts the demand curve for U.S. dollars ________ and shifts the supply curve of U.S. dollars ________.
A) leftward; leftward
B) leftward; rightward
C) rightward; leftward
D) rightward; rightward
Answer: C
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills



90) Using the above figure, which of the following is correct?
A) 1 guilder will sell for $2.
B) 1 dollar will sell for 1/2 guilder.
C) A shortage of guilders exists at an exchange rate above $0.60.
D) A surplus of guilders exists at an exchange rate above $0.60.
Answer: D
Topic: Equilibrium Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

91) Using the above figure, an increase in the demand for Dutch goods by U. S. consumers will lead to
A) a depreciation in the Dutch currency.
B) an appreciation in the Dutch currency.
C) an increase in the supply of Dutch currency as foreign exchange.
D) a decrease in the supply of Dutch currency as foreign exchange.
Answer: B
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

92) What factors can change expectations about the exchange rate?
A) interest rate parity
B) purchasing power parity
C) real GDP parity
D) Both answers A and B are correct.
Answer: D
Topic: Exchange Rate Expectations
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

93) Adjusted for risk, interest rate parity
A) holds only for larger countries.
B) holds only between the U.S. and Canada.
C) holds only when purchasing parity holds.
D) always holds.
Answer: D
Topic: Interest Rate Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

94) If there are equal rates of return between assets in two currencies, then there is
A) purchasing power parity.
B) interest rate parity.
C) parity of exchange.
D) foreign exchange parity.
Answer: B
Topic: Interest Rate Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

95) If in Chicago the interest rate is 5 percent a year and in Vancouver it is 4 percent a year, ________.
A) the quantity of Canadian dollars purchased will increase
B) the Canadian dollar is expected to depreciate
C) interest rate parity does not exist
D) the U.S. dollar is expected to depreciate
Answer: D
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

96) Suppose that the U.S. interest rate is 5 percent and the Turkish interest rate is 50 percent. The effect of this difference in the foreign exchange market is that
A) all funds flow to Turkey to get the higher interest rate.
B) an American investor is guaranteed to make an additional 45 percent in dollar terms by investing in Turkey.
C) investors expect the Turkish currency to rise in value (appreciate) against the dollar.
D) investors expect the Turkish currency to fall in value (depreciate) against the dollar.
Answer: D
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

97) Suppose that the U.S. interest rate is 5 percent and the Japanese interest rate is 1 percent. The effect of this difference in the foreign exchange market is that
A) all funds flow to the United States to get the higher interest rate.
B) a Japanese investor is guaranteed to make an additional 4 percent in yen terms by investing in the United States.
C) investors expect the yen to appreciate against the dollar.
D) investors expect the yen to depreciate against the dollar.
Answer: C
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

98) Suppose a deposit in New York earns 6 percent a year and a deposit in London earns 4 percent a year. Interest rate parity holds if the
A) U.S. dollar appreciates by 2 percent a year.
B) U.S. dollar depreciates by 2 percent a year.
C) U.K. pound depreciates by 2 percent a year.
D) None of the above answers is correct because interest rate parity requires that the interest rates be the same in both countries.
Answer: B
Topic: Interest Rate Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

99) Suppose a British bank offers a 3 percent interest rate while a U.S. bank offers a 7 percent interest rate. People must expect the U.S. dollar will
A) depreciate 4 percent.
B) appreciate 4 percent.
C) appreciate 10 percent.
D) depreciate 10 percent.
Answer: A
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

100) According to interest rate parity, if the interest rate is 1 percent in the European Union and the euro is expected to appreciate 3 percent, the comparable interest rate in the United States will be
A) 4 percent.
B) 3 percent.
C) 2 percent.
D) 1 percent.
Answer: A
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

101) Suppose a Japanese bank offers a 4 percent interest rate and U.S. banks offer a 2 percent interest rate. People must expect the yen to
A) depreciate by 2 percent.
B) appreciate by 2 percent.
C) depreciate by 6 percent.
D) appreciate by 6 percent.
Answer: A
Topic: Interest Rate Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

102) The idea that the value of money is equal across countries is known as
A) interest rate parity.
B) the expected profit parity effect.
C) purchasing power parity.
D) exchange rate parity.
Answer: C
Topic: Purchasing Power Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

103) If the prices in the United States rise faster than those in other countries,
A) the exchange rate rises.
B) the exchange rate falls.
C) then interest rate parity must not hold.
D) the interest rate in the United States falls.
Answer: B
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

104) Suppose the exchange rate between the U.S. dollar and the Mexican peso was $1 = 5 pesos. A can of Pepsi sells for $2 in Boston and 12 pesos in Mexico City.
A) Purchasing power parity prevails with these prices.
B) Purchasing power parity does not prevail with these prices.
C) The U.S. dollar would be expected to depreciate.
D) None of the above answers is correct.
Answer: B
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

105) Suppose the exchange rate between the dollar and the euro is 2 euros per dollar. The price of a clock in Europe is 20 euros while the price of the same clock in the United States is $5. From these prices and exchange rate, it can be concluded that
A) purchasing power parity holds.
B) money buys more in the United States.
C) money buys more in Europe.
D) interest rate parity holds.
Answer: B
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Analytical Skills

106) Suppose the exchange rate between the U.S. dollar and the Jamaican dollar was $1 U.S. = $40 Jamaican dollars. A beach towel sells for $20 in Miami and $60 Jamaican in Negril.
A) Purchasing power parity does not prevail with these prices.
B) The U.S. dollar would be expected to depreciate.
C) The Jamaican dollar would be expected to appreciate.
D) All of the above are correct.
Answer: D
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

107) If the price level rises in the United States but not in foreign nations and the current exchange rate does not change, the expected future exchange rate
A) rises.
B) falls.
C) stays the same.
D) You can't tell from the given information.
Answer: B
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

108) According to purchasing power parity, a rise in inflation in the United States. relative to the rest of the world will lead to
A) a balance of payments surplus.
B) a balance of payments deficit.
C) an exchange rate appreciation.
D) an exchange rate depreciation.
Answer: D
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

109) Suppose that U.S. inflation is 3 percent and Turkish inflation is 70 percent. The effect of this discrepancy on the foreign exchange market is that
A) the Turkish currency will depreciate.
B) the dollar will depreciate.
C) it is impossible for interest rate parity to hold.
D) the Turkish currency will appreciate.
Answer: A
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

110) According to purchasing power parity, the foreign exchange market will
A) undervalue the dollar if inflation in the United States is greater than it is elsewhere.
B) no longer demand dollars if the inflation rate in the United States exceeds that of other nations.
C) adjust the value of the exchange rate to reflect differing inflation rates between nations.
D) result in a flow of dollars out of the United States whenever its rate of inflation is below that of other nations.
Answer: C
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

111) When a nation's currency depreciates, the country might
A) have an inflation rate that exceeds the inflation rate in nations with which it trades.
B) have an inflation rate below the inflation rate in nations with which it trades.
C) be responding to an increase in the demand for its currency.
D) be responding to a decrease in the domestic demand for foreign currencies.
Answer: A
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

112) In France, the price of a computer is 1,227.6 euros. In Japan, the price of the same computer is 137,920 yen. If a U.S. dollar can buy 1.023 euros or 119.93 yen, then purchasing power parity ________.
A) is equal to interest rate parity and the computer is cheaper in North America
B) does not hold and the computer is cheaper in France
C) does not hold and the computer is cheaper in Japan
D) holds and the computer is the same price everywhere
Answer: C
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

113) Suppose that the price of an identical sport-utility vehicle is $32,000 in U.S. dollars in the United States and $32,000 in Canadian dollars in Canada. Suppose in addition that the exchange rate between Canada and the United States is one Canadian dollar equals $0.75 U.S. dollar. Does purchasing power parity hold for SUVs between the United States and Canada?
A) Yes, because SUVs have the same price in each local currency.
B) No, because SUVs are more expensive in Canada than the United States.
C) No, because SUVs are more expensive in the United States than in Canada.
D) Without knowing interest rates, we can't say.
Answer: C
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

114) Suppose that the price of an identical sport-utility vehicle is $32,000 in U.S. dollars in the United States and $32,000 in Canadian dollars in Canada. Suppose in addition that the exchange rate between Canada and the United States is one Canadian dollar equals $0.75 U.S. dollar. Based on this information what will happen to the exchange rate between the United States and Canada?
A) The value of the U.S. dollar will fall as U.S. residents purchase SUVs in Canada.
B) The value of the Canadian dollar will fall as Canadians purchase SUVs in the United States.
C) The exchange rate will stay the same because purchasing power parity already holds.
D) The value of the Canadian dollar will fall because Canadian prices are lower than U.S. prices.
Answer: A
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

115) Suppose that $1 U.S. costs $1.50 Canadian. If in St. Louis a CD costs $10 U.S. and in Montreal it costs $15 Canadian, then ________.
A) purchasing power parity exists
B) Canadians will buy CDs in St. Louis
C) Americans will buy CDs in Montreal
D) Virgin Records will have an incentive to build more stores in North America
Answer: A
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

116) The nominal exchange rate is
A) the value of the U.S. dollar expressed in units of foreign currency per U.S. dollar.
B) the real exchange rate multiplied by the ratio of the U.S. price level to the foreign price level.
C) the relative price of U.S. produced goods to foreign produced goods.
D) a measure of the quantity of the nominal GDP of other countries that we get per unit of U.S. nominal GDP.
Answer: A
Topic: The Nominal Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

117) The real exchange rate is the
A) relative price of U.S. produced output relative to foreign-produced output .
B) price of foreign goods relative to the price of domestic goods
C) trade-weighted index
D) current account balance
Answer: A
Topic: The Real Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

118) The real exchange rate is
A) the relative price of U.S. produced goods to foreign produced goods.
B) the nominal exchange rate multiplied by the ratio of the foreign price level to the U.S. price level.
C) the money price of foreign produced goods relative to the money price of U.S. produced goods.
D) a measure of how much currency exchanges for a unit of another currency.
Answer: A
Topic: The Real Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

119) If the nominal exchange rate rises and price levels stay constant, the real exchange rate will
A) rise
B) fall
C) stay constant
D) could rise, fall or stay constant
Answer: A
Topic: The Real Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

120) Given the U.S. price level *P*, the foreign country price level *P**, and the nominal exchange rate *E* in foreign currency per U.S. dollar, the real exchange rate *RER* is given by
A) *RER = E x (P/P*)*
B) *RER = E x (P*/P)*
C) *RER = (P/P*) / E*
D) *RER = P x (E/P*)*
Answer: A
Topic: The Real Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

121) Given the U.S. price level *P*, the foreign country price level *P**, and the real exchange rate *RER* in foreign currency per U.S. dollar, the nominal exchange rate *E* would be given by
A) *E = RER x (P/P*)*
B) *E = RER x (P*/P)*
C) *E = (P/P*) / RER*
D) *E = P x (RER/P*)*
Answer: A
Topic: The Nominal Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

122) Initially the nominal exchange rate between the South Korean won and the U.S. dollar is 950 won per dollar. If the nominal exchange rate increases to 1000 won per dollar and the U.S and Korean price levels do not change, the real exchange rate
A) is the same as before.
B) is greater than before.
C) is less than before.
D) More information is needed to answer the question.
Answer: B
Topic: The Real Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

123) If the price level in the U.S. is 120, the price level in South Africa is 140, and the nominal exchange rate is 7 South African rands per dollar, then the real exchange rate is
A) 6 South African goods per U.S. good.
B) 8.4 South African goods per U.S. good.
C) 9.8 South African goods per U.S. good.
D) 1.4 South African goods per U.S. good.
Answer: A
Topic: The Real Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

124) Suppose your firm wants to import sugarcane from Brazil. The exchange rate is 3 Brazilian reals per U.S. dollar and sugarcane costs 36 reals per ton. How much is a ton of sugarcane in U.S. dollars?
A) $12
B) $39
C) $108
D) $109
Answer: A
Topic: The Real Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

125) In the long run, the nominal exchange rate
A) is a monetary phenomenon, determined by the quantities of money in two countries.
B) is not related to the real exchange rate, since the real exchange rate is the true value of currencies.
C) will not change if prices in one country change, since prices are nominal variables.
D) is fixed by world central banks, as indicated by the fixed exchange rate system.
Answer: A
Topic: Nominal Exchange Rate in the Long Run
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

126) A decrease in the demand for U.S. exports ________ the demand for U.S. dollars and shifts the demand curve for U.S. dollars ________.
A) increases; rightward
B) decreases; rightward
C) decreases; leftward
D) increases; leftward
Answer: C
Topic: Study Guide Question, Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

127) A decrease in the expected future exchange rate ________ the demand for U.S. dollars and shifts the demand curve for U.S. dollars ________.
A) increases; rightward
B) decreases; rightward
C) decreases; leftward
D) increases; leftward
Answer: C
Topic: Study Guide Question, Changes in the Demand for Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

128) Of the following, when would the U.S. exchange rate rise the most?
A) When the supply of and demand for U.S. dollars increase.
B) When the supply of U.S. dollars increases and the demand for them decreases.
C) When the supply of U.S. dollars decreases and the demand for them increases.
D) When the supply of and demand for U.S. dollars decrease.
Answer: C
Topic: Study Guide Question, Changes in the Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3 Exchange Rate Policy

1) The Fed
A) allows a flexible exchange rate, though their actions can impact the exchange rate.
B) has no influence on the exchange rate.
C) sells U.S. dollars to China in an attempt to depreciate the U.S. dollar.
D) alternates between a flexible, fixed, and crawling peg exchange rate policy depending on economic conditions.
Answer: A
Topic: Exchange Rate Policies
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

2) Which of the following exchange rate policies uses a target exchange rate, but allows the target to change?
A) crawling peg
B) flexible exchange rate
C) fixed exchange rate
D) moving target
Answer: A
Topic: Exchange Rate Regimes
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) ________ can intervene directly in the foreign exchange market by buying or selling dollars.
A) Congress
B) The Fed
C) The International Monetary Fund
D) The U.S. Treasury department
Answer: B
Topic: The Fed in the Foreign Exchange Market
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) The Federal Reserve can influence the exchange rate by
A) changing interest rates.
B) buying or selling dollars.
C) Both answers A and B are correct.
D) None of the above answers is correct
Answer: C
Topic: The Fed in the Foreign Exchange Market
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) The Fed ________ intervene in the foreign exchange market by supplying dollars and the Fed ________ intervene in the foreign exchange market by demanding dollars.
A) can; can
B) cannot; can
C) can; cannot
D) cannot; cannot
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) Suppose the Fed wants to fix the U.S. dollar/Mexican peso rate at 11 pesos per dollar under a fixed exchange rate policy. If the exchange rate falls to 10 pesos per dollar, the Fed can
A) buy dollars.
B) sell dollars.
C) attempt to freeze all sales of dollars.
D) any of the above actions could take place.
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) Suppose the target exchange rate set by the Fed is 100 yen per dollar. If the demand for dollars temporarily increases, to maintain the target exchange rate, the Fed can
A) sell dollars.
B) buy dollars.
C) violate interest rate parity.
D) violate purchasing power parity.
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

8) Suppose the target exchange rate set by the Fed is 100 guilders per dollar. If the demand for dollars temporarily decreases, to maintain the target exchange rate, the Fed can
A) sell dollars.
B) buy dollars.
C) increase U.S. exports.
D) increase U.S. imports.
Answer: B
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) Suppose the target exchange rate set by the Fed is 150 yen per dollar. If the demand for dollars permanently decreases the Fed
A) can permanently meet the target by selling dollars.
B) can permanently meet the target by buying dollars.
C) must violate both interest rate parity and purchasing power parity to permanently meet the target.
D) cannot permanently maintain the target rate.
Answer: D
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

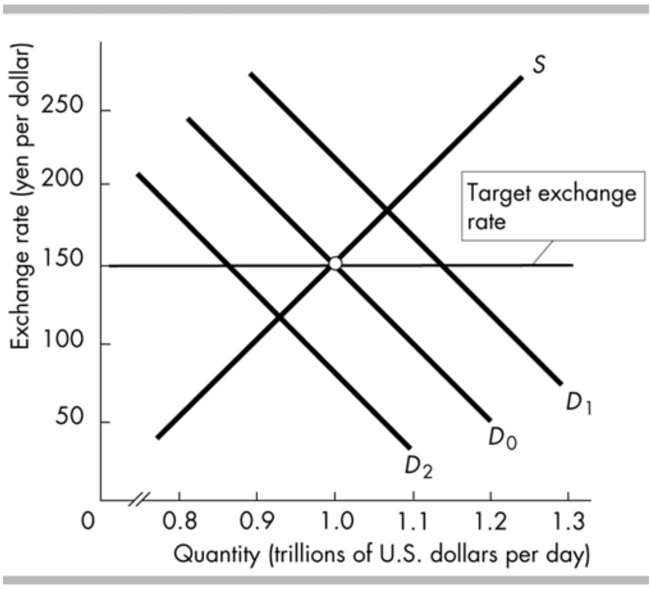
10) If the Fed sets a target exchange rate that is higher than the current exchange rate, then
A) the Fed must sell dollars.
B) the Fed must buy dollars.
C) the Fed can do nothing in the short run.
D) will try to print more dollars for foreign distribution.
Answer: B
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

11) If the exchange rate is higher than the Fed's target exchange rate, the Fed would
A) implement purchasing power parity.
B) implement interest rate parity.
C) buy dollars.
D) sell dollars.
Answer: D
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) If the Fed wants to depreciate the dollar against the yen, the Fed will
A) increase the supply of dollars by selling yen.
B) increase the demand for dollars by selling yen.
C) decrease the supply of dollars by selling yen.
D) increase the supply of dollars by buying yen.
Answer: D
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) Suppose the current exchange rate between the Chinese yuan and the United States dollar is 7 yuan per dollar. If the Fed sought to drive up the exchange rate to 8 yuan per dollar then it would
A) buy dollars.
B) sell dollars.
C) buy yuan.
D) sell dollars and buy yuan.
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

14) If the target exchange rate is 100 yen per dollar and the current exchange rate is 90 yen per dollar, the Fed will
A) sell dollars and the demand for dollars will increase.
B) sell dollars and the demand for dollars will decrease.
C) buy dollars and the demand for dollars will increase.
D) buy dollars and the demand for dollars will decrease.
Answer: C
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking



15) In the above figure, suppose the demand for dollars *temporarily* increases so that the demand curve shifts to D_1. To maintain the target exchange rate, the Fed
A) can sell dollars.
B) can buy dollars.
C) must violate interest rate parity but not purchasing power parity.
D) cannot maintain the target exchange rate.
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

16) In the figure above, suppose the demand for dollars *temporarily* decreases so that the demand curve shifts to D_2. To maintain the target exchange rate, the Fed
A) can sell dollars.
B) can buy dollars.
C) must violate both interest rate parity *and* purchasing power parity.
D) cannot maintain the target exchange rate.
Answer: B
Topic: The Fed in the Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

17) In the above figure, suppose the demand for dollars *permanently* decreases to D_2. To maintain the target, the Fed
A) can buy dollars.
B) can sell dollars.
C) must decrease the nation's net exports.
D) cannot permanently maintain the exchange rate target of 150 yen per dollar.
Answer: D
Topic: The Fed in the Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

18) If the Fed raises the U.S. interest rate, the demand for dollars ________ and the exchange rate ________.
A) increases; rises
B) increases; falls
C) decreases; rises
D) decreases; falls
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) Epsilon is a country whose unit of currency is the omega. New information leads people to expect that the omega will appreciate next year. To keep the foreign exchange value of the omega fairly steady, the Bank of Epsilon will ________ enough omegas on the foreign exchange market so that the ________ omegas will ________.
A) buy; demand for; increase
B) sell; supply of; increase
C) buy; demand for; decrease
D) buy; supply of; decrease
Answer: B
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

Exchange rate (yen per dollar)	Quantity of dollars demanded (billions)	Quantity of dollars demanded (billions)
180	200	230
160	220	220
140	240	210
120	260	200
100	280	190

20) The table above gives the supply and demand schedules of U.S. dollars. Suppose that the Fed spends $30 billion and buys foreign securities. As a result, the U.S. dollar will ________.
A) depreciate by 20 yen per dollar
B) appreciate by 20 yen per dollar
C) depreciate by 140 yen per dollar
D) appreciate by 180 yen per dollar
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

21) If the Fed wants to depreciate the U.S. dollar against the British pound, it will ________.
A) sell foreign exchange
B) decrease the money supply
C) sell British pounds
D) sell U.S. dollars
Answer: D
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

22) If a nation's central bank increased domestic interest rates, the nation's exchange rate would change if the country's exchange rate was a
A) a flexible exchange rate.
B) a fixed exchange rate.
C) a crawling peg.
D) a nominally fixed exchange rate.
Answer: A
Topic: Exchange Rate Policies
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

23) China has used a fixed yuan exchange rate and a crawling peg exchange rate. In both cases, China pegs its currency to the
A) U.S. dollar
B) Japanese yen
C) euro
D) Mexican peso
Answer: A
Topic: China's Exchange Rate Policy
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

24) If the People's Bank of China adopted a flexible exchange rate policy,
A) the U.S. dollar would depreciate.
B) the U.S. dollar would appreciate.
C) the yuan would depreciate.
D) the yuan-U.S. dollar exchange rate would rise.
Answer: A
Topic: China's Exchange Rate Policy
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

25) Since 1997, the People's Bank of China has
A) allowed a flexible exchange rate to boost exports.
B) managed its exchange rate to help control inflation.
C) strictly followed a fixed exchange rate to boost exports.
D) purchased U.S. dollars to appreciate the yuan.
Answer: B
Topic: China's Exchange Rate Policy
Skill: Conceptual
Question history: New 10th edition
AACSB: Reflective Thinking

26) By fixing its exchange rate, China is most likely
A) achieving a low inflation rate by anchoring to the U.S. inflation rate.
B) keeping its export prices low.
C) making it easier to compete in world markets.
D) Both B and C.
Answer: A
Topic: China's Exchange Rate Policy
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

27) All of the following statements are correct EXCEPT:
A) China's exchange rate policy boosts exports in the long run.
B) China's exchange rate policy is mainly an attempt to control inflation.
C) China's exchange rate policy results in a depreciated yuan.
D) China's exchange rate policy does not impact the real exchange rate in the long run.
Answer: A
Topic: China's Exchange Rate Policy
Skill: Conceptual
Question history: New 10th edition
AACSB: Reflective Thinking

28) If a country's central bank does not intervene in the foreign exchange market, the country has
A) a crawling peg exchange rate policy.
B) a fixed exchange rate policy.
C) a flexible exchange rate policy.
D) no exchange rate policy.
Answer: C
Topic: Study Guide Question, Exchange Rate Policy
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

29) If the Fed sells U.S. dollars, the exchange rate
A) rises.
B) does not change.
C) falls.
D) changes, but the direction depends on whether the Fed affected the demand for dollars or the supply of dollars.
Answer: C
Topic: Study Guide Question, The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4 Financing International Trade

1) A country's balance of payments accounts record
A) the country's net indebtedness to foreigners.
B) its international trading, borrowing, and lending.
C) the flow of human and nonhuman resources between it and its trading partners.
D) only its official transactions with other governments.
Answer: B
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) When the United States imports goods and services from the rest of the world,
A) we receive payments from the rest of the world.
B) we make payments to the rest of the world.
C) we increase our inflation rate.
D) we decrease our inflation rate.
Answer: B
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) When we export goods to foreign countries, we
A) receive payments from the rest of the world.
B) make payments to the rest of the world.
C) increase our inflation rate.
D) decrease our inflation rate.
Answer: A
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) Balance of payments accounts include
A) the net interest income account.
B) the current account.
C) Both answers A and B are correct.
D) Neither answer A nor B is correct.
Answer: B
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) Which of the following is recorded in the U.S. balance of payments account?
I. foreign investment in the United States
II. U.S. investment abroad
III. the U.S. government deficit or surplus
A) III only
B) I and II
C) I and III
D) I, II and III
Answer: B
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) A country's balance of payments accounts records
A) only the goods and services purchases among countries over a period of time.
B) the international trading, borrowing, and lending positions of a country over a period of time.
C) the flow of human and non-human capital among countries over a period of time.
D) only official transactions between governments over a period of time.
Answer: B
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) A country's balance of payments accounts include all of the following EXCEPT
A) military account.
B) current account.
C) capital and financial account.
D) official settlements account.
Answer: A
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

8) In part, a country's current account measures
A) its current debt as opposed to its long-term debt.
B) borrowing and lending activity between the country's residents and foreigners.
C) net increases and decreases in a country's holdings of foreign currency.
D) receipts from the sale of goods and services to foreigners and payments for goods and services bought from foreigners.
Answer: D
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) The account that records the receipts from the exports of goods and services sold abroad, the payments for imports of goods and services from abroad, net interest income paid abroad, and net transfers is the ________.
A) current account
B) official settlements account
C) international capital account
D) capital and financial account
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

10) Which international account is used to record payments for imports, receipts from exports, net interest paid abroad and net transfers?
A) the capital and financial account
B) the current account
C) the official settlements account
D) the trade account
Answer: B
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

11) Which of the following is included in a nation's current account?
I. the import of services
II. a change of foreign currency holdings
III. net transfers, such as foreign aid payments
A) I and III
B) I and II
C) II and III
D) III only
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) The current account
A) measures our exports minus our imports taking into account interest payments paid to and received from the rest of the world.
B) measures our imports minus our exports.
C) does not account for interest payments paid to and received from the rest of the world.
D) is part of GDP.
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) The current account is
A) the difference between exports and imports, also taking into account interest payments to and from the rest of the world.
B) the amount of money the government keeps on hand to pay its bills taking account of the interest payments on its debt.
C) is the amount of tax revenue that the government expects to collect.
D) is the total amount of interest payments that the U.S. owes to foreign countries.
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

14) The largest part of the U.S. current account consists of
A) Fed transfers of U.S. dollars to other central banks.
B) net transfer payments between the United States and Mexico.
C) receipts from exports and payments for imports.
D) net borrowing between the United States and other countries.
Answer: C
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

15) Suppose that the U.S. government gives foreign aid to Turkey. This transaction would directly
A) increase the U.S. current account.
B) decrease the U.S. current account.
C) increase the U.S. capital and financial account.
D) decrease the U.S. capital and financial account.
Answer: B
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

16) An American consumer buys a French luxury product in New York. In the U.S. balance of payments accounts, this transaction directly appears in
A) the official settlements account.
B) the imports part of the current account.
C) the net transfers part of the current account.
D) the capital and financial account.
Answer: B
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

17) Which of the following contributes to a current account surplus for a country?
A) having tourists visit the country
B) importing textiles
C) having foreigners buy government securities from the country's government
D) importing financial services
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

18) In 2010, the U.S. current account had a
A) deficit of $436 billion.
B) surplus of $436 billion.
C) deficit of $439 billion.
D) surplus of $439 billion
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

19) The current account records all transactions below EXCEPT for
A) net exports of goods and services.
B) net interest income.
C) net foreign investment.
D) net transfers.
Answer: C
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

20) Which of the following is NOT included in the U.S. current account?
A) U.S. investment abroad
B) net interest income
C) net transfers
D) imports of goods and services
Answer: A
Topic: Balance of Payments Accounts, Current Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

21) The balance of payments account which records foreign investment in the United States and U.S. investments abroad is the
A) capital and financial account
B) current account
C) official settlements account
D) None of the above because foreign investment in the United States is included in one account and U.S. investment abroad is included in another account
Answer: A
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

22) The account that records foreign investment in the United States minus U.S. investment abroad is the
A) capital and financial account.
B) official settlements account.
C) current account.
D) U.S. official reserves account.
Answer: A
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

23) The capital and financial account measures ________.
A) foreign investment in the United States minus U.S. investment abroad
B) capital produced outside of the United States minus capital produced inside the United States
C) capital used inside the United States but manufactured outside the United States
D) capital used outside the United States but manufactured inside the United States
Answer: A
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

24) Which of the following is included in a nation's capital and financial account?
I. the purchase of foreign stocks and bonds
II. the sale of foreign stocks and bonds
III. importing a piece of capital equipment
A) I only
B) I and II
C) III only
D) I, II and III
Answer: B
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

25) Which of the following transactions is <u>NOT</u> recorded in the capital and financial account?
A) foreign investment in the United States
B) U.S. investment abroad
C) statistical discrepancy
D) net interest income
Answer: D
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

26) A negative balance in the capital and financial account means the economy is
A) lending to the rest of the world
B) running a capital account surplus
C) borrowing from the rest of the world
D) importing more than it is exporting
Answer: A
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

27) Which of the following transactions directly leads to a surplus on the U.S. capital and financial account?
A) An American purchases a share of stock on the Tokyo exchange.
B) An American sells wheat to an African nation.
C) A Japanese resident purchases a U.S. government bond.
D) A resident of France visits the United States.
Answer: C
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

28) A German publishing company buys an American publishing company based in New York. In the U.S. balance of payments accounts, this transaction directly appears in
A) the official settlements account.
B) the imports part of the current account.
C) the net transfers part of the current account.
D) the capital and financial account.
Answer: D
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

29) In 2010, the U.S. capital and financial account had a
A) deficit of $439 billion.
B) surplus of $439 billion.
C) surplus of $115 billion.
D) deficit of $115 billion.
Answer: B
Topic: Balance of Payments Accounts, Capital and Financial Account
Skill: Recognition
Question history: New 10th edition
AACSB: Reflective Thinking

30) The official settlements account records the change in ________.
A) international trade
B) U.S. official reserves
C) foreign investment and domestic investment
D) the reserves held by banks and the Fed
Answer: B
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

31) Which of the following accounts records the change in U.S. official reserves?
A) current account
B) capital and financial account
C) official settlements account
D) none of the above
Answer: C
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

32) The account that records changes in the U.S. government's holdings of foreign currency is the
A) capital and financial account.
B) official settlements account.
C) current account.
D) U.S. official reserves account.
Answer: B
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

33) If the U.S. government increased its holdings of British pounds, definitely
A) the capital and financial account would increase.
B) the capital and financial account would decrease.
C) there would be an increase in U.S. official reserves.
D) there would be a decrease in U.S. official reserves.
Answer: C
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

34) If the U.S. government decreased its holdings of Mexican pesos, definitely
A) the capital and financial account would increase.
B) the capital and financial account would decrease.
C) there would be an increase in U.S. official reserves.
D) there would be a decrease in U.S. official reserves.
Answer: D
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

35) Which of the following statements is INCORRECT?
A) Payments for imports and receipts from exports are recorded in the current account.
B) Foreign investment in the United States and U.S. investment abroad are recorded in the capital and financial account.
C) A change in U.S. official reserves is recorded in the official settlements account.
D) Net interest income is recorded in the official settlements account.
Answer: D
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

36) The official settlements account of a country measures
A) the receipts from goods and services bought and sold, and transfers to and from foreigners.
B) borrowing and lending between the country's residents and foreigners.
C) the net increase or decrease in the country's official reserves.
D) net transfer payments between the country's citizens and foreigners.
Answer: C
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

37) U.S. official reserves are the ________.
A) reserves of U.S. dollars held by the World Bank
B) U.S. government's holdings of foreign currency
C) reserves of U.S. dollars held by foreign banks
D) holdings of foreign currency by the public and the banks
Answer: B
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

38) The change in U.S. official reserves is equal to
A) borrowing from abroad plus the current account deficit.
B) the current account balance plus the capital and financial account balance.
C) the current account balance minus the capital and financial account balance.
D) foreign investment in the United States minus U.S. investment abroad.
Answer: B
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

39) An official settlements account balance of -$5,000 means
A) official reserves of foreign currency increased $5,000
B) official reserves of foreign currency decreased $5,000
C) the country is exporting more than it is importing
D) the country is importing more than it is exporting
Answer: A
Topic: Balance of Payments Accounts, Official Settlements Account
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

40) To pay for a current account deficit, a country can
A) borrow money from abroad
B) lend money abroad
C) increase official reserves to cover the shortfall
D) transfer money from the capital account to the official settlements account
Answer: A
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

41) If a country is importing more than they are exporting, the current account will have a ________ balance and the capital and financial account will have a ________ balance.
A) negative; positive
B) negative; negative
C) positive; negative
D) positive; positive
Answer: A
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

42) If foreign investment in the United States exceeds U.S. investment abroad, there is a ________; and when U.S. investment abroad exceeds foreign investment in the United States, there is ________.
A) current account surplus; a current account deficit
B) current account surplus; an official accounts surplus
C) capital and financial account surplus; a capital and financial account deficit
D) capital and financial account deficit; a capital and financial account surplus
Answer: C
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

43) When there is a current account deficit and the official settlements account equals 0, then
A) exports exceed imports for the country.
B) the country is an exporter of capital.
C) the capital and financial account has a surplus.
D) the country has a budget surplus.
Answer: C
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

44) If U.S. imports increase, the sum of the balance of payments accounts (the sum of the current account plus capital and financial account plus official settlements account)
A) becomes negative.
B) becomes positive.
C) becomes negative or positive depending on the government budget deficit or surplus.
D) does not change.
Answer: D
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

45) The sum of the current account, capital and financial account, and official settlements account is
A) a positive number if the country has a trade surplus.
B) a negative number if the country has a trade deficit.
C) positive or negative depending on whether the domestic exchange rate is appreciating or depreciating.
D) always equal to zero.
Answer: D
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

46) Suppose the current account of a country is in balance and the official settlements account equals 0. A new transaction occurs so that the current account is now in surplus, but the official settlements account does not change. From this we know that
A) the balance of trade is now in surplus.
B) the government is running a budget deficit.
C) the capital and financial account is now in deficit.
D) the government must make official reserve transactions.
Answer: C
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

47) If the current account balance is $30 billion, and the capital and financial account balance is $35 billion, then the official settlements account balance is ________ billion, and the official reserves ________.
A) $5 billion; increase
B) -$5 billion; increase
C) $5 billion; decrease
D) -$5 billion; decrease
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

48) If the current account balance is -$100 billion and the capital and financial account balance is $80 billion, then the official settlement account balance is
A) -$20 billion.
B) $20 billion.
C) always 0.
D) impossible to determine with the information given.
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

49) If the U.S. current account balance is -$500 billion and the capital and financial account balance is +$510 billion,
A) the U.S. official settlements account balance is $10 billion.
B) the U.S. government's holdings of foreign currency increases by $10 billion.
C) foreign investment in the United States is smaller than the U.S. investment abroad.
D) U.S. exports are greater than U.S. imports.
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

50) If the current account has a negative balance of $100 and the capital and financial account has a positive balance of $80, there will be ________ in official reserves of ________.
A) a decrease; $20
B) an increase; $20
C) an increase; $180
D) a decrease; $180
Answer: A
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

51) If the current account has a positive balance of $100 and the capital and financial account has a negative balance of $90, there will be ________ in official reserves of ________.
A) a decrease; $10
B) an increase; $10
C) an increase; $190
D) a decrease; $190
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

Item	Billions of dollars
Exports of goods	1000
Imports of goods	-665
Exports of services	410
Imports of services	-590
Net interest income	0
Net transfers	-15
U.S. investment abroad	-600
Foreign investment in the United States	400
Official settlements account	60

52) The data in the table above are the U.S. balance of payments. The current account balance is
A) $140 billion.
B) $155 billion.
C) $170 billion.
D) -$45 billion.
Answer: A
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

53) The data in the table above are the U.S. balance of payments. The data show that
A) the United States has a current account surplus.
B) the United States has a capital and financial account surplus.
C) The United States loaned $400 billion to the rest of the world.
D) Both answers A and B are correct.
Answer: A
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

54) The data in the table above are the U.S. balance of payments. The capital and financial account balance is
A) $0.
B) -$80 billion.
C) -$200 billion.
D) +$200 billion.
Answer: C
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

55) The data in the table above are the U.S. balance of payments. The sum of the current account plus capital and financial account plus official settlements account is equal to
A) $0.
B) -$335 billion.
C) $140 billion.
D) -$60 billion.
Answer: A
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

Item	Billions of dollars
Imports of goods and services	750
Exports of goods and services	1,000
Net interest income	-50
Net transfers	-50
U.S. investment abroad	-350
Foreign investment in the United States	200

56) The data in the table above are the U.S. balance of payments. What is the current account balance?
A) $0
B) $150 billion
C) -$100 billion
D) -$150 billion
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

57) The data in the table above are the U.S. balance of payments. What is the capital and financial account balance?
A) $0
B) $150 billion
C) -$350 billion
D) -$150 billion
Answer: D
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

58) The data in the table above are the U.S. balance of payments. If there is no statistical discrepancy, what is the balance in the official settlements account?
A) $150 billion
B) -$150 billion
C) $50 billion
D) $0
Answer: D
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of dollars
Exports of goods and services	635
Imports of goods and services	555
Net interest income	-18
Net transfers	22
Urland's investment abroad	467
Foreign investment in Urland	321

59) The above table shows some of the balance of payments accounts for Urland. What is Urland's balance on the current account?
A) $80 billion
B) $62 billion
C) $84 billion
D) $47 billion
Answer: C
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

60) The above table shows some of the balance of payments accounts for Urland. What is Urland's balance on the capital and financial account?
A) -$146 billion
B) -$183 billion
C) -$99 billion
D) $142 billion
Answer: A
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

61) The above table shows some of the balance of payments accounts for Urland. What is Urland's balance in the official settlements account?
A) $405 billion
B) $62 billion
C) $99 billion
D) $37 billion
Answer: B
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Millions of crumbs
Imports of goods and services	2,000
Exports of goods and services	3,000
Borrowing from the rest of the world	1,500
Net investment income paid to foreigners	60
Net transfers paid to foreigners	60

62) The table above shows the transactions made during 2011 by the citizens of Biscuit, whose currency is the crumb. During 2011, the official reserves increased by 380 million crumbs. Calculate the current account balance.
A) -880 million crumbs
B) -1,000 million crumbs
C) 1,000 million crumbs
D) 880 million crumbs
Answer: D
Topic: Current Account Balance
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

63) The table above shows the transactions made during 2011 by the citizens of Biscuit, whose currency is the crumb. During 2011, the official reserves increased by 380 million crumbs. How many million crumbs did Biscuit lend to the rest of the world in 2011?
A) -500
B) 500
C) 240
D) 2,000
Answer: D
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

64) When we have a negative current account, we are
A) borrowing from the rest of the world.
B) lending to the rest of the world.
C) running a government budget surplus.
D) None of the above is correct.
Answer: A
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

65) Which of the following statements about the balance of payments accounts is correct?
A) The current account must be greater than the capital and financial account.
B) The sum of all three accounts is always zero.
C) The official settlements account is typically larger than both the capital and financial account and the current account.
D) Typically the capital and financial account is near zero because it equals the difference between the current account and the official settlements account.
Answer: B
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

66) Over the last 25 years, according to the United States balance of payments,
A) the current account and the capital and financial account balances tend to move in the same direction.
B) the current account and the capital and financial account balances tend to move in opposite directions.
C) there is no clear relationship between the current account balance and the capital and financial account balance.
D) the official settlements balance fluctuates greatly from year to year.
Answer: B
Topic: Patterns and Trends in International Trade
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

67) During most of the 1980s, 1990s, and 2000s the U.S. has had a ________ current account balance and a ________ capital and financial account balance.
A) positive; positive
B) positive; negative
C) negative; positive
D) negative; negative
Answer: C
Topic: Patterns and Trends in International Trade
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

68) If a country is currently lending more to the rest of the world than it is borrowing from the rest of the world, the country is a
A) net borrower.
B) debtor nation.
C) net lender.
D) creditor nation.
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

69) Suppose Italy lends 1.5 billion euros to other nations and borrows 1 billion euros from other nations. Italy definitely is a
A) net borrower.
B) net lender.
C) creditor nation.
D) debtor nation.
Answer: B
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

70) If a country lends more to foreign countries than it borrows from foreign countries in a year, then definitely that year
A) it has a current account deficit.
B) it is a creditor nation.
C) it is a debtor nation.
D) it is a net lender.
Answer: D
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

71) Which of the following countries are net lenders?
I. Japan
II. United States
A) I only
B) II only
C) both I and II
D) neither I nor II
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

72) If a country is currently borrowing more from the rest of the world than it is lending to the rest of the world, the country is a
A) net borrower.
B) debtor nation.
C) net lender.
D) creditor nation.
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

73) Suppose this year Angola borrows $100 million from foreign countries while it lends $15 million. Angola definitely is a
A) net borrower.
B) net lender.
C) creditor nation.
D) debtor nation.
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

74) If a country during its entire history has invested more in the rest of the world than the rest of the world has invested in it, the country is a
A) net borrower.
B) debtor nation.
C) net lender.
D) creditor nation.
Answer: D
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

75) A creditor nation means a nation
A) whose exports exceed its imports.
B) whose current account is larger than its capital account.
C) whose current lending to the rest of the world exceeds its borrowing from the rest of the world.
D) through its history has invested more in the rest of the world than other countries have invested in it.
Answer: D
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

76) Over its history, Spain has loaned more money abroad than foreigners have lent to it. Spain is a
A) net lender.
B) net borrower.
C) creditor nation.
D) debtor nation.
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

77) If a nation during its entire history has borrowed more from the rest of the world than it has lent to the rest of the world, the country is a
A) net borrower.
B) debtor nation.
C) net lender.
D) creditor nation.
Answer: B
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

78) A debtor nation means a nation
A) whose imports exceeds its exports.
B) whose current account is less than its capital account.
C) through its history has invested less in the rest of the world than other countries have invested in it
D) whose current lending to the rest of the world exceeds its borrowing from the rest of the world.
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

79) Over its history, Brazil has borrowed more from the rest of the world than it has loaned to the rest of the world. Brazil
A) eventually will have a balance of payments account that does not balance.
B) is a debtor nation.
C) is a creditor nation.
D) has no current account balance.
Answer: B
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

80) A country that during its entire history has borrowed more from the rest of the world than it has lent to it is a ________, and a country that during its entire history has invested more in the rest of the world than other countries have invested in it is a ________.
A) debtor nation; investor nation
B) borrower nation; creditor nation
C) debtor nation; creditor nation
D) net borrower nation; net lender nation
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

81) A net borrower is a country that ________, while a net lender is a country that ________.
A) borrows more than it lends; owes more to foreigners than foreigners owe to it
B) decreases its stock of outstanding foreign debt; lends more than it borrows
C) borrows more than it lends; lends more than it borrows
D) lends more than it borrows; borrows more than it lends
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

82) This year a country loaned more to the rest of the world than it borrowed from the rest of the world. In addition, the country has invested more in the rest of the world than other countries have invested in it. The country is currently a ________ and also a ________.
A) net lender; creditor nation
B) net borrower; creditor nation
C) net borrower; debtor nation
D) debtor nation; net lender
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

83) A country that borrows more from the rest of the world than it lends to it in a year is called a ________, and a country that lends more to the rest of the world than it borrows from it in a year is called a ________.
A) borrower; lender
B) importer; exporter
C) net borrower; net lender
D) gross borrower; gross lender
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

84) Today, the United States is a
I. net borrower
II. net lender
III. debtor nation
IV. creditor nation
A) I and IV
B) II and IV
C) I and III
D) II and III
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

85) If a country has a capital and financial account surplus, that country's stock of international indebtedness is
A) increasing.
B) decreasing.
C) constant.
D) zero.
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Analytical Skills

86) If a country has a capital and financial account deficit, that country's stock of international indebtedness is
A) increasing.
B) decreasing.
C) constant.
D) zero.
Answer: B
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Analytical Skills

87) Since the mid 1980s, the United States has been a net ________ and a ________ nation.
A) borrower; creditor
B) lender; creditor
C) borrower; debtor
D) lender; debtor
Answer: C
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

88) If we import more than we export from the rest of the world we
A) must borrow an equal amount from the rest of the world.
B) can lend an equal amount to the rest of the world.
C) are running a trade surplus.
D) are helping to finance investment in the rest of the world.
Answer: A
Topic: Rest of the World Sector
Skill: Recognition
Question history: Previous edition, Chapter 7
AACSB: Reflective Thinking

89) If U.S. net exports are positive,
A) other countries borrow from the United States to pay for some of the goods they purchase from the United States.
B) other countries make loans to the United States so that the United States can pay for some of the goods it purchases from other countries.
C) the United States sells some of the assets it owns in other countries to pay for some of the goods it sells to other countries.
D) the United States borrows from other countries to pay for some of the goods the United States purchases from them.
Answer: A
Topic: Rest of the World Sector
Skill: Conceptual
Question history: Previous edition, Chapter 7
AACSB: Reflective Thinking

90) The main item in the current account balance is
A) net interest income.
B) net transfers.
C) net exports.
D) net taxes.
Answer: C
Topic: Current Account Balance
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

91) The value of net exports increases when the value of ________.
A) exports of goods and services minus imports of goods and services decreases
B) imports of goods and services increase
C) imports of goods and services decrease
D) exports of goods and services decrease
Answer: C
Topic: Current Account Balance
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

92) The current account balance is defined as
A) the value of exports - the value of imports.
B) the amount of exported capital assets + net interest income.
C) the value of exports - the value of imports + net interest income + net transfers.
D) the difference between the import and export of official reserves.
Answer: C
Topic: Current Account Balance
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

93) The current account balance is equal to
A) net exports + net interest income + net transfers.
B) net exports - net interest income - net transfers.
C) net exports + net interest income - net transfers.
D) net interest income + net transfers - net exports.
Answer: A
Topic: Current Account Balance
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

94) Which of the following are included in the U.S. current account balance?
I. exports to Japan
II. interest payments made to Canada
III. transfer payments made to Israel
A) I only
B) I and II
C) I and III
D) I, II and III
Answer: D
Topic: Current Account Balance
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

95) All of the following are a current account transaction EXCEPT
A) importing services.
B) exporting goods.
C) investing abroad.
D) importing goods.
Answer: C
Topic: Current Account Balance
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

96) If net interest and net transfers are zero, and a country's exports exceed its imports, the country definitely has ________.
A) a current account surplus
B) a current account deficit
C) a capital and financial account surplus
D) an official settlements account surplus
Answer: A
Topic: Current Account Balance
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

97) If net interest and net transfers are $0, and a nation's purchases of foreign goods and services are $3.5 billion while its sales of goods and services to foreigners are $4.5 billion,
A) it has a $1 billion surplus in its balance of payments.
B) it has a $1 billion deficit in its current account.
C) it has a $1 billion surplus in its current account.
D) its capital and financial account shows a surplus.
Answer: C
Topic: Current Account Balance
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Analytical Skills

98) The country of Pimm exports $500 billion worth of goods and services and imports $400 billion worth of goods and services. Net interest income paid abroad is $50 billion and net transfers are $0. The current account balance is ________.
A) $50 billion
B) $25 billion
C) $175 billion
D) $975 billion
Answer: A
Topic: Current Account Balance
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

99) The private sector surplus or deficit equals
A) saving minus investment.
B) net taxes minus government purchases.
C) investment minus saving.
D) government purchases minus net taxes.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

100) Net exports equals
A) exports of goods and services minus imports of goods and services.
B) imports of goods and services minus exports of goods and services.
C) the government sector balance plus the private sector balance.
D) Both answers A and C are correct.
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

101) The government sector balance is equal to ________.
A) net taxes minus government purchases of goods and services
B) tariffs minus imports
C) saving minus investment
D) exports minus imports
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

102) The private sector balance is equal to ________.
A) income minus consumption minus net taxes
B) income minus consumption minus investment
C) saving minus investment
D) income minus consumption
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Reflective Thinking

103) A net exports deficit or surplus equals
A) taxes minus savings plus public and private investment.
B) the government sector balance plus the private sector balance.
C) net lending by both the private and public sector plus savings minus investment.
D) net worth plus the government sector balance minus the private sector balance.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

104) Which of the following is correct?
A) Net exports equals the government sector balance plus the private sector balance.
B) The government sector balance equals net exports plus the private sector balance.
C) The private sector balance equals net exports plus the government sector balance.
D) Net exports equals the current account plus the capital account plus the official settlements account.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

105) Which of the following statements is true?
A) If private saving is greater than private investment, then the private sector has a surplus.
B) If private investment is greater than private saving, then the private sector has a deficit.
C) If private investment is greater than private saving, then either the government or net export sector must have a surplus.
D) All of the above answers are correct.
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

106) Which of the following equations represents the private sector balance?
A) $X - M$
B) $T - G$
C) $S - I$
D) $C + S + T$
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Analytical Skills

107) X is exports, M is imports, T is net taxes, G is government expenditure, C is consumption expenditure, S is saving, and I is investment. The government sector balance is equal to
A) $T — G$
B) $C + S + T$
C) $S — I$
D) $X — M$
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Analytical Skills

108) Suppose $X - M$ = net exports; $T - G$ = government sector balance; and $S - I$ = private sector balance. What relationship exists among these variables?
A) $(X - M) + (T - G) + (S - I) = 0$
B) $(X - M) = (T - G) + (S - I)$
C) $(T - G) + (X - M) = (S - I)$
D) $(T - G) = (X - M) + (S - I)$
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Recognition
Question history: Modified 10th edition
AACSB: Analytical Skills

109) Which of the following statements is <u>INCORRECT</u>?
A) Net exports equals exports minus imports.
B) The government sector balance equals net taxes minus government expenditures on goods and services.
C) Private sector balance equal private investment minus private saving.
D) The sum of government sector and private sector balances equals net exports.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

110) A country has a government sector deficit and a private sector surplus. If the government sector deficit increases, and the private sector surplus decreases, ________.
A) net exports decrease or remain constant
B) net exports increase
C) net exports increase, decrease, or remain constant
D) net exports decrease
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

111) If net exports is a negative number, the government sector must ________ if the private sector is in a ________.
A) run a surplus; surplus
B) equal zero; deficit
C) run a deficit; surplus
D) The statement errs because the accounts are not related.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

112) If $X - M$ = \$0 and the government sector has a deficit of \$250 billion, the private sector
A) has a deficit that equals \$0.
B) has a deficit that equals \$250 billion.
C) has a surplus that equals \$250 billion.
D) has a surplus that equals \$500 billion.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

113) If net exports is 100 and the private sector balance is 150, then the government sector balance is
A) -50.
B) 50.
C) 250.
D) 0.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

114) Suppose U.S. net exports are -$400 billion and the U.S. government sector surplus is $200 billion. Then in the private sector, saving minus investment equals
A) -$600 billion.
B) -$200 billion.
C) +$600 billion.
D) +$200 billion.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

115) If the government sector is running a deficit of $120 million and the private sector is running a surplus of $200 million, net exports equals a
A) $80 million surplus.
B) $320 million surplus.
C) $80 million deficit.
D) $320 million deficit.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

116) Hong Kong has imports of $1,130 billion and exports of $1,255 billion. Hong Kong definitely has ________.
A) negative net exports of $125 billion
B) positive net exports of $125 billion
C) a government budget surplus
D) Both answers B and C are correct.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

117) On the island country of Sunshine where the unit of currency is fish, net exports are 50 fish, saving is 250 fish, net taxes are 100 fish, and the government budget deficit is 175 fish. What is the value of investment?
A) 375 fish
B) -375 fish
C) 25 fish
D) -25 fish
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

118) On the island country of Sunshine where the unit of currency is fish, net exports are 50 fish, saving is 250 fish, net taxes are 100 fish, and the government budget deficit is 175 fish. The private sector has a ________.
A) deficit of 125 fish
B) surplus of 125 fish
C) deficit of 225 fish
D) surplus of 225 fish
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Component	Amount (billions of dollars)
Investment, *I*	700
Net taxes, *T*	1,300
Government expenditure, *G*	1,200
Exports, *X*	1,500
Imports, *M*	1,700

119) In the above table, the government sector balance is a
A) surplus of $200 billion.
B) deficit of $200 billion.
C) surplus of $100 billion.
D) deficit of $100 billion.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

120) In the above table, net exports equals a
A) surplus of $200 billion.
B) deficit of $200 billion.
C) surplus of $100 billion.
D) deficit of $100 billion.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

121) In the above table, the government sector balance is a ________ and net exports is a ________.
A) surplus of $100 billion; deficit of $200 billion
B) deficit of $100 billion; surplus of $200 billion
C) surplus of $100 billion; surplus of $200 billion
D) deficit of $100 billion; deficit of $200 billion
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

122) In the above table, the private sector has a
A) surplus of $300 billion.
B) deficit of $300 billion.
C) deficit of $200 billion.
D) deficit of $400 billion.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

123) In the above table, saving must be
A) -$300 billion.
B) $300 billion.
C) $400 billion.
D) -$400 billion.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of dollars
Exports of goods and services, *X*	500
Imports of goods and services, *M*	
Net taxes, *T*	750
Government expenditure, *G*	
Saving, *S*	1,000
Investment, *I*	

124) In the above table, suppose imports = $750 billion and government expenditures = $1,000 billion. Hence investment equals
A) -$500 billion.
B) $1,000 billion.
C) $500 billion.
D) $0.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

125) Using the data in the above table, suppose imports equals $250 billion and investment equals $1,000 billion. Hence government expenditure equals
A) $1,000 billion.
B) $750 billion.
C) $500 billion.
D) $250 billion.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

126) Using the data in the above table, if the private sector runs a surplus of $250 billion, imports will equal $1,000 billion if
A) government expenditure equals -$750 billion.
B) investment equals -$1000 billion.
C) government expenditure equals -$1000 billion.
D) the government sector runs a deficit of $750 billion.
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of dollars
Exports of goods and services, *X*	
Imports of goods and services, *M*	1,000
Net taxes, *T*	
Government expenditure, *G*	1,300
Saving, *S*	
Investment, *I*	650

127) Using the data in the above table, if exports = $1,150 billion and the private sector runs a surplus of $300 billion, the government sector will run
A) a surplus of $150 billion.
B) a surplus of $450 billion.
C) a deficit of $150 billion.
D) a deficit of $450 billion.
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

128) Using the data in the above table, if the government sector runs a deficit of $250 billion and net exports equal -$500 billion, then saving must equal
A) $450 billion.
B) $250 billion.
C) $1,350 billion.
D) $400 billion.
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

129) Using the data in the above table, if net exports = -$500 billion and the government balances its budget,
A) the private sector must balance its budget.
B) savings must equal $150 billion.
C) the private sector runs a surplus of $850 billion.
D) saving must equal $650 billion.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

130) Using the data in the above table, if saving equals $650 billion and exports are greater than imports,
A) the government sector must run a deficit.
B) net taxes will be greater than $1300 billion.
C) net taxes will be less than $650 billion.
D) government expenditures must increase.
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of dollars
Exports	234
Imports	277
Government expenditure	887
Net taxes	855
Investment	760
Saving	749

131) The above table gives data for the nation of Sueland. What is the value of net exports?
A) $43 billion
B) $234 billion
C) -$43 billion
D) $511 billion
Answer: C
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

132) The above table gives data for the nation of Sueland. What is the government sector balance?
A) $1,772 billion
B) $32 billion
C) -$43 billion
D) -$32 billion
Answer: D
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

133) The above table gives data for the nation of Sueland. What is the private sector balance?
A) $11 billion
B) -$11 billion
C) -$43 billion
D) $43 billion
Answer: B
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

Item	Billions of dollars
Imports of goods and services, *M*	275
Net taxes, *T*	300
Government expenditure, *G*	250
Savings, *S*	125
Investment, *I*	100

134) The table above gives some of the entries in the national income and product accounts. The government sector has a ________, and the private sector has a ________.
A) surplus of $50 billion; surplus of $25 billion
B) deficit of $50 billion; surplus of $25 billion
C) surplus of $50 billion; deficit of $25 billion
D) deficit of $50 billion; deficit of $25 billion
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

135) The table above gives some of the entries in the national income and product accounts. What is the value of exports?
A) $350 billion
B) $300 billion
C) -$25 billion
D) $25 billion
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Dollars
Exports	500
Imports	400
Government sector surplus	250
Private sector deficit	-150

136) The above table describes accounts for the country of Pacifica. Using this information, net exports for Pacifica equals
A) $100.
B) $900.
C) -$100.
D) $650.
Answer: A
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

137) In the United States, since 1981 which two of the following have almost always moved in the same direction?
A) net exports and the government sector balance
B) net exports and the private sector balance
C) the government sector balance and the private sector balance
D) none of the above
Answer: D
Topic: The Three Sector Balances
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

138) Which of the following is one of the balance of payments accounts?
A) government expenditure account
B) capital and financial account
C) reserve account
D) net borrowing account
Answer: B
Topic: Study Guide Question, Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

139) Suppose the United States initially has a trade deficit. Then U.S. firms increase their imports from Canada, financing that increase by borrowing from Canada. The current account deficit is now ________ and the capital and financial account surplus is now ________.
A) larger; larger
B) larger; smaller
C) smaller; larger
D) smaller; smaller
Answer: A
Topic: Study Guide Question, Balance of Payments Accounts
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

Component	Amount (billions of dollars)
Government expenditure, *G*	700
Net taxes, *T*	600
Investment, *I*	350
Savings, *S*	500

140) In the table above, what is the government's sector balance?
A) a deficit of $700 billion
B) a surplus of $600 billion
C) a deficit of $100 billion
D) $0
Answer: C
Topic: Study Guide Question, Net Export, Gov. Budget, Saving & Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

141) In the table above, what does the private sector surplus equal?
A) $500 billion
B) $350 billion
C) $150 billion
D) $0
Answer: C
Topic: Study Guide Question, Net Export, Gov. Budget, Saving & Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

142) In the table above, what do net exports equal?
A) a deficit of $700 billion
B) a deficit of $350 billion
C) a surplus of $50 billion
D) a surplus of $1,750 billion
Answer: C
Topic: Study Guide Question, Net Export, Gov. Budget, Saving & Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

5 News Based Questions

1) When the U.S. government buys aircraft from BAe, a British corporation, it pays for them using
A) euros.
B) pounds.
C) dollars.
D) foreign exchange rates.
Answer: B
Topic: Financing International Trade
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) In 2007, the U.S. sold $73 million of cigarettes to Iran. Iran paid for these cigarettes using
A) dollars.
B) rials, the Iranian currency.
C) euros.
D) pounds.
Answer: A
Topic: Financing International Trade
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

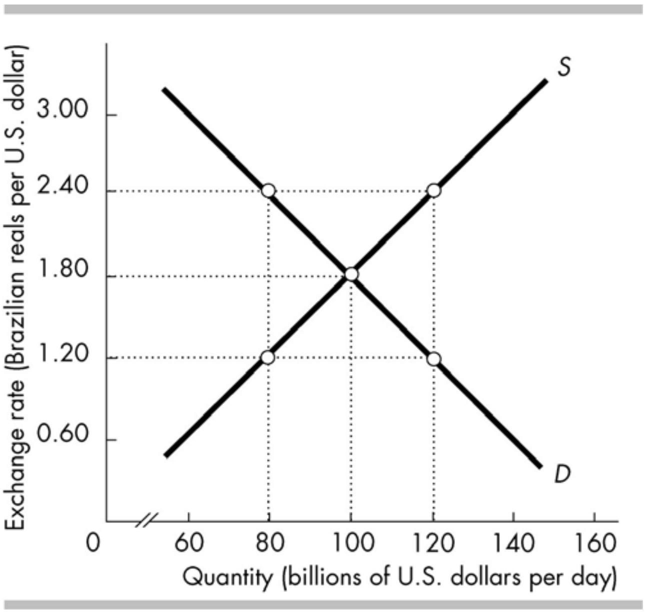
3) In July 2008, a British pound could buy $2. By October 2008, a pound could buy $1.55. Over the four months, the
A) pound depreciated against the dollar.
B) the real exchange rate did not change.
C) pound appreciated against the dollar.
D) the U.S. inflation rate increased.
Answer: A
Topic: The Exchange Rate, Currency Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) In June 2008, $1 bought 0.5 pounds and in October, $1 bought 0.65 pounds. As a result of this change, ________ between June and October.
A) the demand for dollars increased.
B) the dollar appreciated and the quantity of dollars demanded decreased.
C) the dollar depreciated and the quantity of dollars demanded decreased.
D) the demand for dollars decreased.
Answer: B
Topic: The Exchange Rate, Currency Appreciation
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

5) In June 2008, $1 bought 104 yen and in October, $1 bought 93 yen. This change means
A) U.S. exports became more expensive for Japanese buyers.
B) there will be a movement down along the demand curve for dollars.
C) there was an increase in the value in the dollar, relative to the yen.
D) the dollar appreciated relative to the yen.
Answer: B
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) In June 2008, the dollar bought 1.6 Brazilian reals and in October, the dollar bought 2.4 reals. This resulted in a
A) a movement upward along the supply curve for dollars.
B) a movement downward along the supply curve for dollars.
C) rightward shift in the supply curve for dollars.
D) leftward shift in the supply curve for dollars.
Answer: A
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) In June 2008, the dollar bought 1.6 Brazilian reals and in October, the dollar bought 2.4 reals. This resulted in a
A) a decrease in the quantity of dollars supplied.
B) an increase in the quantity of dollars supplied.
C) a rightward shift in the supply curve of dollars.
D) a depreciation of the dollar.
Answer: B
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking



8) The figure above shows the demand and supply of dollars in the foreign exchange market. The equilibrium in the market occurs at a price of ________ Brazilian reals per dollar and a quantity of ________ billion dollars.
A) 2.0 ; 100
B) 2.4; 120
C) 1.6; 100.
D) 100; 2.0
Answer: A
Topic: Foreign Exchange Market
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

9) The figure above shows the demand and supply of dollars in the foreign exchange market. At a price of 2.40 Brazilian reals per dollar,
A) there will be a shortage of dollars.
B) $40 billion dollars will be demanded.
C) $40 billion dollars will be supplied.
D) there will be a surplus of dollars.
Answer: D
Topic: Equilibrium Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

10) The figure above shows the demand and supply of dollars in the foreign exchange market. At a price of 1.20 Brazilian reals per dollar,
A) there will be a shortage of dollars.
B) $120 billion dollars will be supplied.
C) $40 billion dollars will be demanded.
D) there will be a surplus of dollars.
Answer: A
Topic: Equilibrium Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

11) As a result of the 2008-2009 financial crisis and the decrease in GDP in many European economies, we would expect
A) an increase in the demand for U.S. exports and a leftward shift in the demand curve for dollars.
B) a decrease in the demand for U.S. exports and a leftward shift in the demand curve for dollars.
C) a decrease in the demand for U.S. exports and a rightward shift in the demand curve for dollars.
D) a decrease in the demand for U.S. imports and a movement up along the demand curve for dollars.
Answer: B
Topic: The Law of Demand for Foreign Exchange, Exports
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

12) In October 2008, Iceland's central bank increased its lending rate to 18% in an "effort to prop up the country's frozen current and markets." (www.nytimes.com, October, 29, 2008)
As a result, the ________ curve for Icelandic krona shifted ________, holding all else the same.
A) supply; rightward
B) demand; rightward
C) demand; leftward
D) A and C are both correct.
Answer: B
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

13) In October 2008, Iceland's central bank increased its lending rate to 18% in an "effort to prop up the country's frozen currency and markets." (www.nytimes.com, October, 29, 2008)
As a result, the ________ and demand curve for Icelandic krona shifted ________, holding all else the same.
A) interest rate differential between U.S. and Icelandic interest rates increased; rightward
B) interest rate differential between U.S. and Icelandic interest rates decreased; leftward
C) dollar appreciated relative to the krona; rightward
D) value of U.S. exports to Iceland increased; leftward
Answer: A
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

14) In October 2008, Iceland's central bank increased its lending rate to 18% in an "effort to prop up the country's frozen current and markets." (www.nytimes.com, October, 29, 2008)
As a result, there was ________ , holding all else the same.
A) a movement upward along the supply curve for krona
B) a leftward shift in the supply curve for krona
C) a rightward shift in the supply curve for krona
D) an increase in the quantity supplied of krona
Answer: B
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

15) In late 2010 the National Bank of Australia offered a 4 percent interest rate on a savings account while Bank of America offered 2 percent. This difference means that
A) people expect the U.S. dollar to appreciate to 8 percent against the Australian dollar and interest rate parity to occur.
B) there will be a surplus of U.S. dollars in the foreign exchange market.
C) people expect the U.S. dollar to appreciate by 2 percent against the Australian dollar and interest rate parity to occur.
D) there will be a shortage of Australian dollars in the foreign exchange markets.
Answer: C
Topic: Interest Rate Parity
Skill: Analytical
Question history: Modified 10th edition
AACSB: Analytical Skills

16) On www.yodobashi.com, you can buy a Canon EOS camera for 298,000 yen. The same camera costs $2700 on www.calumetphoto.com. If the exchange rate is ________ yen per dollar, we can determine ________ for this camera.
A) 92; interest rate parity doesn't occur
B) 92; purchasing power parity occurs
C) 110; interest rate parity occurs
D) 110; purchasing power parity occurs
Answer: B
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

17) In 2009, Germany's capital account was -$135 million. This implies that
A) Germany invested more in other countries than those countries invested in Germany.
B) Germany's currency must have appreciated during 2009.
C) Germany imported more goods from its trading partners than it exported.
D) Germany's official settlements account in 2009 must have been positive.
Answer: A
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

18) In 2007, Japan reported that its overseas assets totalled more than $4.6 trillion. This implies that Japan
A) is debtor nation.
B) has a current account deficit.
C) has a capital account deficit.
D) is a creditor nation.
Answer: D
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) Over a month in late 2008, the Federal Reserve Bank reduced the interest rate by 1 percentage point. Given that the United States operates under a ________ exchange rate regimes, the *primary* purpose of these changes was ________ exchange rate of each currency.
A) flexible; not designed to influence
B) flexible; designed to influence
C) fixed; designed to influence
D) fixed; designed to influence
Answer: A
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Communication

6 Essay Questions

1) Give an example of currency depreciation and appreciation.
Answer: A currency depreciates when it becomes less valuable in the foreign exchange market. For instance, if the exchange rate changes from 130 yen per dollar to 110 yen per dollar, the dollar has depreciated. A currency appreciation is the exact opposite: A currency appreciates when it becomes less valuable in the foreign exchange market. For instance, if the exchange rate changes from 130 yen per dollar to 150 yen per dollar, the dollar has appreciated.
Topic: The Exchange Rate, Currency Appreciation and Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) In the foreign exchange market, what factor leads to a movement along the demand curve for dollars?
Answer: A change in the exchange rate leads to a movement along the demand curve for dollars.
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) In the foreign exchange market, how does the quantity of U.S. dollars demanded respond to a change in the U.S. exchange rate? Why is there this response?
Answer: If the U.S. exchange rate falls, the quantity of U.S. dollars demanded increases for two reasons. The first is the exports effect. If the exchange rate falls, then U.S. goods and services are cheaper in foreign nations. These nations increase the amount of U.S. exports they demand. As exports increase the quantity of dollars demanded increases so that the importing nations can pay for the exports. The second reason the quantity of U.S. dollars demanded increases is the expected profit effect. In general, the greater the expected profit from holding U.S. dollars, the greater is the quantity demanded of U.S. dollars. When the exchange rate falls, more people will believe that it will rise again in the future and so more people want to hold U.S. dollars. As a result, the quantity of U.S. dollars demanded increases.
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) In the foreign exchange market, how does each of the following influences affect the demand for dollars and the demand curve for dollars?
a) an increase in the exchange rate.
b) an increase in the U.S. interest rate.
c) a fall in the expected future exchange rate.
Answer:
a) The increase in the exchange rate decreases the quantity of dollars demanded and creates an upward movement along the demand curve for dollars.
b) An increase in the U.S. interest rate increases the demand for dollars and shifts the demand curve for dollars rightward.
c) A fall in the expected future exchange rate decreases the demand for dollars and shifts the demand curve for dollars leftward.
Topic: Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) Name three factors in the foreign exchange market that affect either the quantity of dollars demanded or the demand for dollars. Discuss whether the factor increases or decreases the number of dollars people want to hold.
Answer: Three factors are the exchange rate, the U.S. interest rate differential, and the expected future exchange rate. If the exchange rate rises, the quantity of dollars demanded decreases. If the U.S. interest rate differential is larger (either because the U.S. interest rate rose or because foreign interest rates fell) then the demand for dollars increases. And, if the expected future value of the exchange rate is higher, then the current demand for dollars increases.
Topic: Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) Explain the effect on the demand for dollars in the foreign exchange market of an increase in the U.S. interest rate differential.
Answer: As the U.S. interest rate differential increases, international investors can obtain a greater return by holding U.S. assets. Therefore these investors want to buy more U.S. assets, such as bonds. But in order to buy more U.S. assets, they need more dollars. Hence the increase in the U.S. interest rate differential leads to an increase in the demand for dollars in the foreign exchange market and so the demand curve for U.S. dollars shifts rightward.
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) In the foreign exchange market, how does a change in the expected future U.S. exchange rate affect the demand for dollars?
Answer: Changes in the expected future exchange rate change the demand for dollars. If the expected future exchange rate falls, the demand for dollars decreases and the demand curve shifts leftward because the expected profit from holding dollars decreases. If the expected future exchange rate rises, the demand for dollars increases and the demand curve shifts rightward because the expected profit from holding dollars increases.
Topic: Changes in the Demand for $, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

8) Why do people and firms in the United States supply dollars to the foreign exchange market?
Answer: People and firms supply dollars in order to obtain foreign currency with which to purchase foreign goods and services and/or foreign assets.
Topic: Supply of Foreign Exchange
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) In the foreign exchange market, how does a fall in the U.S. interest rate affect the supply of dollars?
Answer: The fall in the U.S. interest rate increases the supply of dollars as U.S. residents supply more dollars in order to obtain foreign currency with which to buy foreign assets that now have relatively higher interest rates.
Topic: Changes in the Supply of Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

10) In the foreign exchange market, how does a change in expected future U.S. exchange rate affect the supply of dollars?
Answer: Changes in the expected future exchange rate change the supply of dollars. If the expected future exchange rate falls, the supply of dollars increases and the supply curve shifts rightward because the expected profit from holding dollars decreases. If the expected future exchange rate rises, the supply of dollars decreases and the supply curve shifts leftward because the expected profit from holding dollars increases.
Topic: Changes in the Supply of $, Expected Future Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

11) "In the foreign exchange market, if the demand for the U.S. dollar increases, the U.S. dollar appreciates in value." Briefly explain whether the previous statement is correct or incorrect.
Answer: The statement is correct. The increase in the demand for dollars shifts the demand curve for dollars rightward and creates a shortage of dollars at the initial exchange rate. This shortage puts upward pressure on the exchange rate and so the exchange rate rises to its new equilibrium value.
Topic: Changes in the Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) What happens in the foreign exchange market if the U.S. interest rate increases? What is the effect on the exchange rate?
Answer: In the foreign exchange market, the increase in the U.S. interest rate increases the demand for dollars and the demand curve for dollars shifts rightward. The increase in the interest rate also decreases the supply of dollars and the supply curve of dollars shifts leftward. As a result, the exchange rate rises so that the dollar appreciates.
Topic: Changes in the Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) How will an increase in the expected future exchange rate affect the current supply and demand curves for dollars?
Answer: An increase in the expected future exchange rate increases the return from holding U.S. dollars. As a result, the demand for dollars increases and the demand curve shifts rightward while the supply of dollars decreases and the supply curve shifts leftward.
Topic: Change in the Demand and Supply of Dollars
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

14) What is purchasing power parity?
Answer: Purchasing power parity means "equal value of money," that is, the exchange rate adjusts so that one currency can buy the same amount of goods and services as another currency.
Topic: Purchasing Power Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

15) "Fluctuations in exchange rates, other things remaining the same, creates a situation in which money buys the same amount of goods and services in different currencies." What does the previous statement describe? Will these fluctuations occur in the short run or the long run?
Answer: The statement describes purchasing power parity, the proposition that money will buy the same amount of goods and services in different currencies. The effects of purchasing power parity will change the exchange rate in the long run. In the short run, deviations from purchasing power parity can occur.
Topic: Purchasing Power Parity
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

16) What role can the Fed play in the foreign exchange market?
Answer: The Federal Reserve can intervene in the foreign exchange market by (temporarily) selling or buying dollars. If the Fed sells dollars, it drives the exchange rate lower and if the Fed buys dollars, it drives the exchange rate higher. The Fed cannot buy dollars forever because it will run out of the foreign exchange it using to buy the dollars. And, the Fed likely will not want to sell dollars forever because it would accumulate ever increasing amounts of foreign exchange.
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

17) How does the Fed intervene in the foreign exchange market and what the effects are of the Fed's actions?
Answer: The Fed intervenes in the foreign exchange market and changes the value of the exchange rate by buying or selling dollars. If the Fed wants to raise the exchange rate and appreciate the dollar, the Fed will buy dollars. By buying dollars the Fed increases the demand for dollars and raises the exchange rate. If the Fed wants to lower the exchange rate and depreciate the dollar, the Fed will sell dollars. By selling dollars the Fed increases the supply of dollars and lowers the exchange rate.
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

18) If the Fed wants to lower the U.S. exchange rate, what action should it take in the foreign exchange market? Why does the action lower the exchange rate?
Answer: To lower the exchange rate, the Fed should sell dollars and buy foreign currency. By selling dollars, the Fed increases the supply of dollars, which lowers the U.S. exchange rate.
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) What are the three balance of payments accounts? Briefly describe them. What is the relationship among the three?
Answer: The three balance of payment accounts are the current account, the capital account, and the official settlements account. The current account records exports, imports, net interest, and net transfers. The capital account records foreign investment in the United States and U.S. investment abroad. Finally, the official settlements account shows changes in U.S. official reserves, the government holdings of foreign currency. The relationship is that the current account balance plus capital account balance plus official settlements account must sum to zero.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

20) "The current account records foreign investment in a nation minus investment abroad." Is the previous statement correct or incorrect?
Answer: The statement is incorrect. The current account equals exports minus imports plus net interest plus net transfers. The capital account records foreign investment in a nation minus investment abroad.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

21) What are the main components of the current account? What has been the recent U.S. experience with these items?
Answer: The current account records payments for the imported of goods and services and the receipts for exported of goods and services. These two components of the current account are by far the largest components. In addition to the value of imports and exports, the current account also includes the net interest income paid abroad and net transfers. Net interest income measures the interest payments both made and received which flow from previously purchased assets. Net transfers record such items as foreign aid payments.
Over recent years, the U.S. current account has been negative, that is, there has been a current account deficit. Over these years, the United States has experienced a perennial trade deficit, which means that the value of imports has exceeded the value of exports. The trade deficit has been the primary cause why the U.S. current account has been negative. Net interest income has been barely negative while net transfers are also negative and slightly larger in magnitude than net interest income.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

22) What balance of payment account records foreign investment between countries?
Answer: The capital account records foreign investment between countries. The U.S. capital account equals foreign investment in the United States minus U.S. investment abroad.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

23) How do the capital account and the current account differ?
Answer: The current account and the capital account differ in what is recorded in each. The current account records exports, imports, net interest, and net transfers. The capital account records foreign investment in the United States and U.S. investment abroad.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

24) Define official settlements account and U.S. official reserves. Discuss the differences between the two terms.
Answer: The official settlements account is the record of the change in a country's official reserves. U.S. official reserves are the U.S. government's holdings of foreign currency. If the U.S. official reserves increases, the official settlements account balance is negative. The reason the official settlements account decreases is that holding foreign money is similar to investing abroad insofar as both buying foreign money and buying foreign assets (that is, investing abroad) use (rather than acquire) U.S. dollars.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

25) If U.S. official reserves increase, is the official settlements account balance positive, negative, or unaffected?
Answer: If U.S. official reserves increase, the official settlements account balance is negative.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

26) "If the official settlements balance is zero, a current account surplus must equal the capital account deficit." Is the previous statement correct or incorrect? Briefly explain your answer.
Answer: The statement is correct. The sum of the current account balance plus the capital account balance plus the official settlements account must equal zero. If the official settlements account balance is zero, then the sum of the current account balance plus the capital account balance must equal zero. Therefore a current account surplus must be "balanced" by an equally-sized capital account deficit.
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

27) Looking at the U.S. balance of payments for the last two decades, how have the current account and the capital account changed?
Answer: Since the early 1980s and onward, the U.S. current account has been negative and sometimes quite large. The U.S. capital account has more or less mirrored the current account, only it has been positive rather than negative. Thus when the current account deficit is small, the capital account surplus is small and when the current account deficit is large, the capital account surplus is large.
Topic: Patterns and Trends in International Trade
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

28) Define net borrower, net lender, creditor nation, and debtor nation. Discuss the difference between a net borrower and a debtor nation.
Answer: A country that is borrowing more from the rest of the world than it is lending to the rest of the world is a net borrower. A country that is lending more to the rest of the world than it borrows from the rest of the world is a net lender. A country that during its entire history has borrowed more from the rest of the world than it has lent to the rest of the world is a debtor nation. A country that has invested more in the rest of the world than other countries have invested in it is a creditor nation. A net borrower is a country that is currently borrowing whereas a debtor nation has a stock of outstanding debt. Borrowing is a flow variable and the outstanding debt is a stock. Thus a net borrower could be a creditor nation that is currently borrowing or it could be a debtor nation that is currently borrowing and thereby increasing its debt.
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

29) What is the relationship between net borrower, net lender, debtor nation, and creditor nation?
Answer: If a nation is currently borrowing from the world more than it is lending to the world, the nation is a net borrower. If a nation is currently lending more to the world more than it is borrowing from the world, the nation is a net lender. If during its entire history a nation has borrowed more than it has lent, the nation is a debtor nation. If during its entire history a nation has lent more than it has borrowed, the nation is a creditor nation. The distinction between borrowing or lending and being a debtor or creditor deals is the distinction between a flow and a stock. A nation that is a net borrower is increasing its debt (or decreasing its assets). The net borrowing is the flow that adds to the stock of debt (or decreases the stock of assets). A nation that is a net lender is increasing its assets (or decreasing its debt). The net lending is the flow that adds to the stock of assets (or decreases the stock of debt).
Topic: Borrowing and Lending
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

30) When a nation has no funds to finance economic development, how can it acquire the needed funds? Is the country a net lender or a net borrower?
Answer: Funds for development can be borrowed from other nations. In this case, the borrowing nation is a net borrower in its capital account.
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

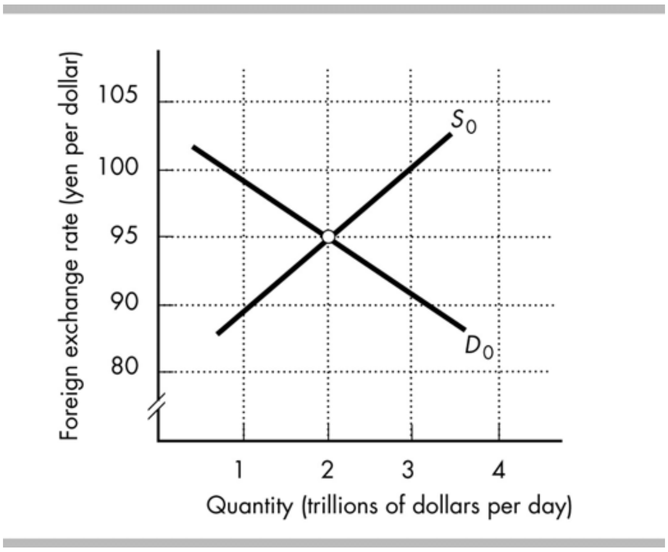
31) "Although the United States is running a large current account deficit, it is still ranked as a major international net lender." Is the previous statement correct or incorrect? Briefly explain your answer.
Answer: The statement is incorrect. Aside from changes in the official settlements account, any nation that is running a current account deficit must be paying for the excess of imports over exports by borrowing from abroad. The United States is no exception and with its large current account deficits, the United States is a large net borrower from abroad.
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

32) What is a "debtor nation?" Is the United States a debtor nation?
Answer: A debtor nation is a country that during its entire history has borrowed more from the rest of the world than it has lent to it. Although the United States was a creditor nation until the 1980s, its borrowing during the 1980s means that today the United States is a debtor nation.
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

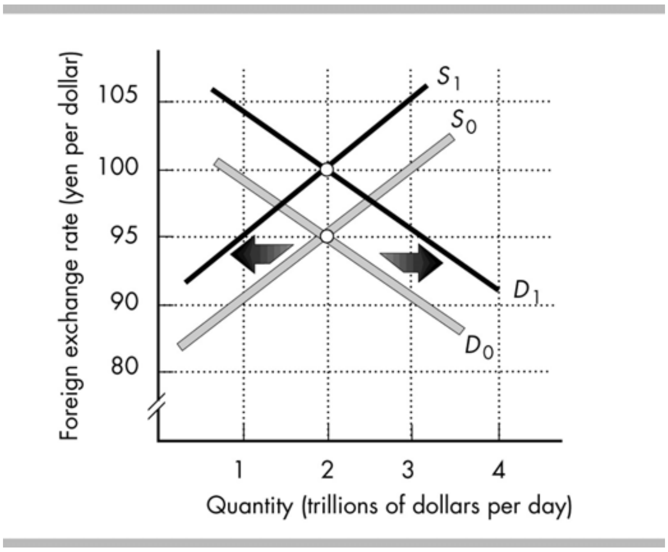
33) What is the relationship between net exports, the government sector surplus or deficit, and the private sector surplus or deficit?
Answer: The relationship is that net exports equals the government surplus or deficit plus the private sector surplus or deficit.
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

34) Saving is S, investment is I, net taxes is NT, government expenditure is G, exports is X, and imports is M. Using these symbols, what is the relationship among the saving, investment, net taxes, government expenditure, exports, and imports?
Answer: The relationship is that $(X - M) = (S - I) + (NT - G)$, or net exports equals the private sector balance plus the government sector balance.
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

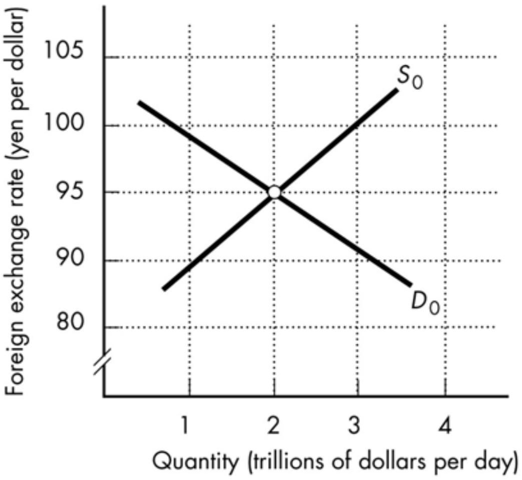
7 Numeric and Graphing Questions



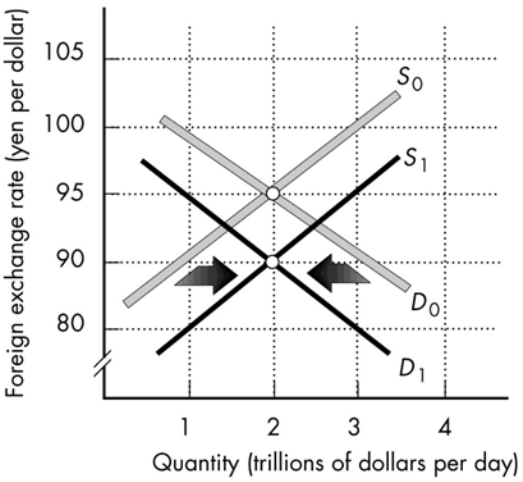
1) In the figure above, illustrate the effect of an increase in the U.S. interest rate. What is the effect on the exchange rate?
Answer:



The figure above shows the effect of the increase in the U.S. interest rate. The demand for dollars increases and the demand curve shifts rightward. The supply of dollars decreases and the supply curve shifts leftward. The equilibrium exchange rate rises, to 100 yen per dollar in the figure.
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills



2) The figure above illustrates the U.S. foreign exchange market. Illustrate how the exchange rate changes if the expected future exchange rate falls. Does the dollar appreciate or depreciate?
Answer:



The fall in the expected future exchange rate decreases the demand for dollars and increases the supply. The demand curve shifts leftward and the supply curve shifts rightward. As shown in the figure, the exchange rate falls so the dollar depreciates.
Topic: Changes in the Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

3) If imports are $1,200 billion and exports are $1,300 billion, while net interest income and net transfers are zero, what is the current account balance?
Answer: The current account balance equals exports minus imports, or $1,300 billion minus $1,200 billion, which is $100 billion.
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

4) During this year a country reports imports of $1,000 billion, exports of $1,100 billion, foreign investment in the country of $900 billion, investment abroad of $1,200 billion, net interest and net transfers of zero. What is the country's current account balance?
Answer: The current account balance is $100 billion.
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

5) If the current account balance is $235 billion and U.S. official reserves increased by $35 billion, what is the official settlements account balance and the capital account balance?
Answer: The official settlements account equals the negative of the change in official reserves, so the official settlements account balance is -$35 billion. Then, the sum of the current account balance plus the capital account balance plus the official settlements account balance equals zero, which means that the capital account balance must equal $200 billion.
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Amount (billions of dollars)
Imports of goods and services	1,400
Exports of goods and services	1,600
Net interest	0
Net transfers	0
Foreign investment in the United States	480
U.S. investment abroad	700

6) The above gives some of the balance of payments accounts of the United States in 2020.
a) What is the current account balance?
b) What is the capital account balance?
c) What is the official settlements account balance?
Answer:
a) The current account balance is $200 billion.
b) The capital account balance is -$220 billion.
c) The official settlements account balance is $20 billion.
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Amount (billions of dollars)
Investment	1,900
Saving	1,600
Government expenditure	1,000
Net taxes	1,700

7) The table above gives some of the accounts of the United States in 2020.
a) What is the private sector balance?
b) What is the government sector balance?
c) What is net exports?
Answer:
a) The private sector balance equals saving minus investment, or -$300 billion.
b) The government sector balance equals net taxes minus government expenditure, or $700 billion.
c) Net exports equals the sum of the private sector balance plus the government sector balance, so net exports equal $400 billion.
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

8) The United States has net exports of -$350 billion and the private sector balance is -$400 billion. What is the government sector balance?
Answer: The sum of the private sector balance plus the government sector balance equals net exports. Therefore -$350 billion = -$400 billion + government sector balance, so the government sector balance is $50 billion.
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

8 True or False

1) An exchange rate is the price of one country's currency in terms of another country's currency.
Answer: TRUE
Topic: The Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

2) "Currency appreciation" means the price of the currency is decreasing.
Answer: FALSE
Topic: The Exchange Rate, Currency Appreciation
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

3) If the exchange rate rises from 100 yen per dollar to 120 yen per dollar, the dollar has appreciated.
Answer: TRUE
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

4) If the exchange rate falls from 120 yen per dollar to 110 yen per dollar, the dollar has depreciated.
Answer: TRUE
Topic: The Exchange Rate, Currency Appreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

5) If the yen appreciates in value against the dollar, the dollar must have depreciated against the yen.
Answer: TRUE
Topic: The Exchange Rate, Currency Appreciation and Depreciation
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

6) The demand for one money is the supply of another money.
Answer: TRUE
Topic: The Exchange Rate
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

7) A rise in the exchange rate leads to a decrease in the quantity of dollars demanded.
Answer: TRUE
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

8) The lower the exchange rate, the cheaper are foreign-produced goods and services.
Answer: FALSE
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9) Other things remaining the same, the higher the current exchange rate, the larger is the expected profit from buying dollars.
Answer: FALSE
Topic: Law of Demand for Foreign Exchange
Skill: Conceptual
Question history: Modified 10th edition
AACSB: Reflective Thinking

10) In the foreign exchange market, a decrease in the exchange rate increases the quantity of dollars supplied.
Answer: FALSE
Topic: Law of Supply for Foreign Exchange
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

11) According to the law of supply in the foreign exchange market, when the U.S. exchange rate rises, the quantity of U.S. dollars supplied will decrease.
Answer: FALSE
Topic: Law of Supply for Foreign Exchange
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

12) An increase in the U.S. interest rate differential increases the demand for dollars.
Answer: TRUE
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

13) If the Fed raises the interest rate, in the foreign exchange market the demand for the U.S. dollar increases.
Answer: TRUE
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

14) If U.S. interest rates are rise relative to foreign interest rates, in the foreign exchange market the demand for U.S. dollars will decrease.
Answer: FALSE
Topic: Changes in the Demand for Dollars, Interest Rates
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

15) In the foreign exchange market, a decrease in the supply of dollars leads to an appreciation of the U.S. dollar.
Answer: TRUE
Topic: Changes in the Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

16) Purchasing power parity means that the expected exchange rate is such that the returns from investing in two nations are equal.
Answer: FALSE
Topic: Purchasing Power Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

17) Purchasing power parity means equal rates of return.
Answer: FALSE
Topic: Purchasing Power Parity
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

18) In the short run, a change in the nominal exchange rate brings an equivalent change in the real exchange rate.
Answer: TRUE
Topic: The Real Exchange Rate
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

19) The exchange rate can be influenced by a nation's central bank.
Answer: TRUE
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

20) In the foreign exchange market, if the demand for dollars permanently decreases, the Fed can maintain the exchange rate at its old equilibrium level indefinitely by buying dollars.
Answer: FALSE
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

21) When the demand for a currency permanently increases, that nation's central bank can maintain its fixed exchange rate indefinitely.
Answer: TRUE
Topic: The Fed in the Foreign Exchange Market
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

22) A country's balance of payment accounts include its government budget deficit or surplus.
Answer: FALSE
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

23) The current account records foreign investment in the United States minus U.S. investment abroad.
Answer: FALSE
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

24) The official settlements account records the change in official U.S. reserves.
Answer: TRUE
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

25) The sum of the current, capital and official settlements accounts is always zero.
Answer: TRUE
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

26) If the official settlements account is zero, whenever the United States has a current account deficit, it must also have a capital account deficit.
Answer: FALSE
Topic: Balance of Payments Accounts
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

27) Over the past decade, the United States has had a current account deficit and capital account deficit.
Answer: FALSE
Topic: Balance of Payments Accounts
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

28) In the market for international loans, most countries, including the United States, are net borrowers.
Answer: TRUE
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

29) The United States is a creditor nation.
Answer: FALSE
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

30) Currently, the United States is both a net borrower and a debtor nation.
Answer: TRUE
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Recognition
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

31) A net borrower country must also be a debtor nation.
Answer: FALSE
Topic: Borrowers and Lenders, Debtors and Creditors
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

32) If net exports increases, but neither government expenditure nor net taxes change, saving must increase.
Answer: TRUE
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Conceptual
Question history: Previous edition, Chapter 9
AACSB: Reflective Thinking

9 Extended Problems

1) The price of a computer in the United States is $1,000. The price of a car in Germany is 10,000 euros. The current exchange rate is 0.9 euros per dollar.
a) If a computer is exported from the United States to Germany with no barriers to trade, what will be the price of the computer in Germany?
b) If a car is imported to the United States from Germany with no barriers to trade, what will be the price of the car in the United States?
c) Suppose the dollar appreciates by 10 percent against the euro. How will the price of a computer exported from the United States change in Germany?
d) Suppose the dollar appreciates by 10 percent against the euro. How will the price of a car imported to the United States from Germany change in the United States?
Answer:
a) The price of an American computer in Germany is $1,000 × 0.9 euros per dollar, which is 900 euros.
b) The price of a German car in the United States is 10,000 euros/0.9 euros per dollar = $11,111.
c) The new exchange rate is 0.9 euros per dollar × 1.1 = 0.99 euros per dollar. So the new price of a U.S. computer in Germany is $1,000 × 0.99 euros per dollar = 990 euros. The price of a U.S. computer in Germany rises by 10 percent.
d) The new price of a German car in the United States is 10,000 euros/0.99 euros per dollar = $10,101. So the price of a German car in the United States falls by about 10 percent.
Topic: The Exchange Rate
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

2) Suppose that the price of a Big Mac is a good approximation of the price level in the country. A Big Mac costs £2 in London and \$3 in New York.
a) If purchasing power parity holds, what is the exchange rate between the U.S. dollar and the British pound?
b) If the current exchange rate is \$1.6 per pound, what is the dollar price of a Big Mac in London? What do you predict will happen to the exchange rate? Explain.
c) The exchange rate between the U.S. dollar and the Russian ruble is 30 rubles per dollar. If purchasing power parity holds, what is the price of a Big Mac in Moscow?
Answer:
a) If purchasing power parity holds, the dollar price of a Big Mac in London must be the same as that in New York. This is the case when the exchange rate is \$1.5 per pound. With this exchange rate, the dollar price of a Big Mac in London is £2 × 1.5 dollars per pound = \$3.
b) If the current exchange rate is \$1.6 per pound, the dollar price of a Big Mac in London is £2 × 1.6 dollars per pound, which is \$3.20. If the price of a Big Mac represents the price level in the country, British goods are relatively more expensive than American goods. The quantity of the U.K. imports demanded decreases in the United States and the quantity of U.S. exports demanded increases in the United Kingdom. The demand for dollars in the foreign exchange market increases and the demand for pounds decreases. As a result, the dollar appreciates against the pound until the purchasing-power-parity exchange rate is restored.
c) If purchasing power parity holds, the dollar price of a Big Mac in Moscow must be the same as in New York, that is, \$3. Given the ruble/dollar exchange rate, the price of a Big Mac in Moscow is \$3 × 30 rubles per dollar, which is 90 rubles.
Topic: Purchasing Power Parity
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of buns
Imports of goods and services	600
Exports of goods and services	700
Foreign investment in Exland	350
Exland's investment abroad	430
Increase in the official holdings of foreign currency	20

3) The citizens of Exland, whose currency is the bun, conduct the transactions outlined in the table above.
a) What is Exland's current account balance?
b) What is Exland's capital account balance?
c) What is Exland's official settlement balance?
d) What is Exland's net foreign borrowing?
Answer:
a) The current account balance equals exports minus imports: 700 - 600 = 100 billion buns.
b) The capital account balance equals foreign investment in Exland minus Exland's investment abroad: 350 - 430 = -80 billion buns
c) A country's official settlement balance is the change in its official reserves. If official reserves increase, the official settlement balance is negative. So Exland's official settlement balance is -20 billion buns.
d) A country's net foreign borrowing is the difference between its borrowing from the rest of the world and its lending to the rest of the world. Exland's foreign borrowing is the foreign investment in Exland (350 billion buns). Exland's foreign lending is its investment abroad (430 billion buns) plus the increase in the official holdings of foreign currency (20 billion buns). So Exland's net foreign borrowing is 350 - 430 - 20 = -100 billion buns which means the country is a net foreign lender.
Topic: Balance of Payments Accounts
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills

Item	Billions of bonts
GDP	320
Consumption expenditure	200
Government expenditure on goods and services	60
Investment	80
Exports of goods and services	40
Government budget deficit	25

4) The table above shows some data for Wiland, a country whose currency is the bont. The official settlement balance, net interest income, and net transfers from abroad are zero.
a) What is Wiland's imports of goods and services?
b) What is Wiland's current account balance?
c) What is Wiland's capital account balance?
d) What is Wiland's net taxes?
e) What is Wiland's private sector balance?
Answer:
a) The country's net exports are GDP minus consumption minus investment minus government purchases, which is 320 - 200 - 80 - 60 = -20 billion bonts. Net exports are the difference between imports and exports. Because Wiland's exports are 40 billion bonts and its net exports are -20 billion bonts, then it imports must equal 60 billion bonts.
b) Because net interest income and net transfers from abroad are zero, the current account balance equals net exports, so the current account balance is -20 billion bonts.
c) Because the official settlement balance is zero, the sum of the capital account balance and current account balance is zero, which means that the capital account balance is 20 billion bonts.
d) The government budget deficit is the difference between government purchases and net taxes, which means net taxes equal government purchases minus the budget deficit. So in Wiland, net taxes are 60 - 25, which is 35 billion bonts.
e) The private sector balance is saving minus investment. Saving is GDP minus net taxes minus consumption. In Wiland, saving is 320 - 35 - 200 = 85 billion bonts. So the country's private sector balance is 85 - 80 = 5 billion bonts, that is, a surplus of 5 billion bonts.
Topic: Net Exports, the Government Budget, Saving, and Investment
Skill: Analytical
Question history: Previous edition, Chapter 9
AACSB: Analytical Skills