Wilf Csaplar Jr. Economics 488(365) Homework #10 Due Wednesday 4/16?

Do not write your name on the assignment. Write your name only on the back of this sheet of paper and staple your answers on the front of this sheet of paper. Failure to follow these directions will cost you 1 point on the assignment.

Because this course has both a homework assignment and a test due during your last week in the course, the assignments must slowly begin moving to come due at the beginning of each week. Therefore, I propose that each assignment be due on the day of the week prior to the day of the previous assignment. Therefore, this assignment will be due Wednesday and the last one will be due on Tuesday. If any of those dates are poor, we can change them. Do we want to meet on Thursday at the normal time or Tuesday at 4:00? The advantage of changing the day is that the discussion of the material will occur before the assignment will be due.

This assignment covers chapter 20.

1) (15 points each) Draw the supply and demand for Egyptian Pounds (LE) priced in US$. For each part, illustrate a large drop in the demand for LE because of the drop in tourism. Explain what will happen to the exchange rate and what actions the government will be forced to do, if they are forced to do anything. Use a separate graph for each part.
A) Egypt has a fixed exchange rate with a narrow band.
B) Egypt has a crawling peg with a narrow band.
C) Egypt has an adjustable peg with a narrow band.

2) (20 points) Suppose that you are the monetary leader of a country has a fixed exchange rate with respect to the US$. The demand for your currency decreases. Illustrate that on the supply and demand diagram for your currency. What is your country forced to do? Why are you forced to do that? Why can't you do that forever? Suppose speculators realize that you cannot do it forever. What will then occur on the exchange market? Illustrate that on the curves and explain why that will occur. What problem is caused by this speculation?

3) (15 points) Many countries in southeast Asia have currencies tied to the Japanese Yen. Many OPEC countries have currencies pegged to the US$. Why would countries have a pegged exchange rate, and why would they choose those respective countries' currencies?

4) (20 points) Why must there be economic cooperation between countries when there is a fixed exchange rate?