

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 150 points (to be scaled up to 225 points) and is scheduled to take 75 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I can give SOME extra time but not much.

1) (8 points each) For TWO of the following events, do the double entry bookkeeping for the USA and **BRIEFLY** explain each entry.

- A) I buy \$1000 worth of shares of Toyota. (Toyota is a Japanese company.)
- B) An Italian spends \$3000 on vacation in West Virginia. (I have no idea why they would.)
- C) I bought a \$1500 German-made bicycle.
- D) Mexican-American citizens send \$2000 worth of clothing back to family members in Mexico

2) (8 points each) Use your answers to Question #1 to answer TWO of these questions.

BRIEFLY explain your answer and show all calculations. Only use the two parts you showed.

- A) What is the value of the current account? Is that a deficit or surplus?
- B) What is the value of the capital account? Is that a deficit or a surplus?
- C) What is the value of the goods and services account? Is that a deficit or a surplus?

3) (10 points) Answer EITHER Part A OR Part B.

- A) What is the economic reason both countries gain from trade?
- B) What is the slope of a PPF which has corn on the vertical axis and pears on the horizontal axis? Why is that true?

4) (14 points) Answer EITHER Part A OR Part B.

- A) Explain how you can reduce exchange rate risk using options. In your example, assume you need to have C\$1000 in three months.
- B) What is relative PPP? Why would we expect it to hold?

5) (14 points) Answer EITHER Part A OR Part B.

- A) If RP increases, then what will happen to M, D, and F? Explain your logic.
- B) Interest rates in Japan are lower than in the USA. Give two reasons why I might want to earn interest rate in Japan?

6) (20 points) Illustrate EITHER the event in Part A OR the event in Part B on the supply and demand for Egyptian Pound (LE). Which currency appreciates? Explain how you know which appreciated and why the curve(s) moved as drawn.

- A) Interest rates in the USA drop.
- B) The Egyptian GDP drops.

7) (30 points) Answer EITHER Part A OR Part B.

- A) Draw the supply and demand for American exports priced in euro. Put scales on both axes. Have the diagram correspond to an exchange rate of \$1.50/euro. Show how it moves if the exchange rate changes to \$3.00/euro. Explain why the curve(s) moved as drawn. Does this information give you points on the supply or the demand for euros? Why did you choose that?

Use this information to find two points on the supply/demand (which ever one you said you could get) diagram for euros. Explain how you got those two points.

B) Draw the supply and demand for American imports priced in British pounds. Put scales on both axes. Have the diagram correspond to an exchange rate of \$2.00/pound. Show how it moves if the exchange rate changes to \$4.00/pound. Explain why the curve(s) moved as drawn. Does this information give you points on the supply or the demand for pounds? Why did you choose that? Use this information to find two points on the supply/demand (which ever one you said you could get) diagram for pounds. Explain how you got those two points.

8) (30 points) Suppose that in the Gambia it takes 4 hours of labor to produce a hat and 12 hours of labor to produce a computer. In Macedonia, it takes 7 hours of labor to produce a hat and 14 hours of labor to produce a computer. Who has the absolute advantage in each good? Who has the comparative advantage in each good? Who will export which good and what will the price be? Draw the PPF/CPF for ONE of the two countries. Explain how you reached each conclusion and how you got the endpoints on the two graphs. How does your graph show that the country gains from trade?