

Do NOT write your name anywhere. (Canvas will tell me who turned in the exam.) Take pictures of your answers and use your own software or <https://pdfcandy.com/> to create a PDF for each answer which requires an upload. If it is large, resize it to A4. Upload that to Canvas. Upload each answer as a separate file with that question. Failure to follow directions will cost you one point.

You are not allowed to use your books, notes, the internet, or other people when taking this test. You can use the internet to access Canvas and to convert your answers to PDF files. Nothing else.

Failure to follow these directions will cost you 1 point. The test has 150 points (to be scaled up to 210 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 have it set up to only give you 2.5 hours.

If you run out of time or lose your internet connection, you can do a second submission. You do NOT have to redo the questions you already did. I will be able to see every submission. If you have problems, you can always contact me via Zoom or e-mail. If you use Zoom, open it in a new tab or window.

1) (10 points) Answer EITHER Part A OR Part B.

A) Explain why an increase in EA^* has a different effect upon the demand for domestic bonds, D , and the demand for foreign bonds, F .

B) Explain why an increase in RP^* has a different effect upon the demand for domestic bonds, D , and the demand for foreign bonds, F .

2) (12 points each) For TWO of the following events, determine the debit and the credit. Then determine what happens to the current account and the capital-financial account. You do not need to explain your answer because it is only 10 points.

A) You send \$2000 worth of N95 masks to Italy

B) Suppose you went to Costa Rica during spring break. Suppose you paid \$400 for a hotel room.

C) You sold \$10,000 worth of BP (British Petroleum) to a Brit to pay for next year's tuition.

3) (12 points) For EITHER foreign exchange swaps OR foreign exchange futures, state what it is and give an example of how it would be used to reduce risk.

4) (16 points) Answer EITHER Part A OR Part B.

A) Explain why relative PPP may not hold. Make sure you write the equation for relative PPP.

B) Explain why most of the time relative PPP holds when absolute PPP does not hold. You do NOT need to write either equation.

5) (18 points) Answer EITHER Part A OR Part B.

A) Draw the J-curve. State the Marshall-Lerner (M-L) condition. Explain how the M-L condition explains the shape of the J-curve.

B) Draw the supply and demand for the US\$ on the foreign exchange market such that the exchange rate is unstable. Prove that the equilibrium is unstable. Use the euro, €, as the other currency.

6) (18 points) Answer EITHER Part A OR Part B.

A) Draw the CIAP diagram. Explain why the CIAP line looks as drawn and why there is a band on the two sides of it. Is down/right of the lowest line an inflow of money or an outflow? Explain our logic.

B) In Chapter 15, there was a diagram with four panels. They showed what happened over time when the money supply had a one-time 10% increase. The graphs showed what happen to the money supply, the interest rates, the price level, and the exchange rate. Draw the graph for the exchange rate the way I defined the exchange rate. Explain why it takes its shape including why it overshoots.

7) (18 points) Draw the supply/demand for the US\$ on the foreign exchange market with the British pound, £, as the other currency. Illustrate EITHER an increase in our interest rates OR an increase in the British price level. Explain why the curve(s) moved as drawn. Which currency depreciated? Explain your logic.

8) (34 points) Answer EITHER Part A OR Part B. Like Questions #2 and #3 on Homework #11, these two are one word different.

A) Note that unlike the book, I am doing this question in terms of dollars, not the foreign currency. Draw the supply/demand for US imports with the price in US\$. Put a scale on the axes. Have the price go to \$20/unit and the quantity go to 1000 units. Draw the demand steep and have it cross supply at the price of \$12/unit and a quantity of 500. Suppose that the exchange rate there is £.5/\$. Now, suppose the exchange rate changes to £.6/\$. Illustrate the effects of the appreciation on the graph. Explain why you moved the curve you moved and not the other one. Also, explain why it moved as drawn including how you got two points on the new line. Given the data from that graph, draw two points on one line of the S/D for \$ on the foreign exchange market. Explain how you know whether it is the supply or the demand. Explain how you found the points.

B) Note that unlike the book, I am doing this question in terms of dollars, not the foreign currency. Draw the supply/demand for US exports with the price in US\$. Put a scale on the axes. Have the price go to \$20/unit and the quantity go to 1000 units. Draw the demand steep and have it cross supply at the price of \$12/unit and a quantity of 500. Suppose that the exchange rate there is £.5/\$. Now, suppose the exchange rate changes to £.6/\$. Illustrate the effects of the appreciation on the graph. Explain why you moved the curve you moved and not the other one. Also, explain why it moved as drawn including how you got two points on the new line. Given the data from that graph, draw two points on one line of the S/D for \$ on the foreign exchange market. Explain how you know whether it is the supply or the demand. Explain how you found the points.