# ECON3315: INTERNATIONAL ECONOMIC ISSUES – Fall 2016

## ASSIGNMENT 2

DUE Tuesday December 6th (in class or by 11.59pm if submitted on turnitin.com)

1. For each of the following identify in which part of the balance-of-payments accounts it appears (current account, capital account or financial account) and whether it is a credit or debit in the US's balance of payments:
   a. An American resident's sale of a share of Johnson & Johnson stock by transferring funds from a bank account
   b. An French woman's purchase of an airline ticket from United Airlines (a US airline company)
   c. The Swiss government's purchase of US Treasury bills in exchange for US$ reserves.
   d. A US importers purchase of Saki (rice wine)
   e. $50 million of foreign aid to Haiti
   f. A loan by an American bank to a Mexican company.

2. During the gold standard era, most currencies were tied to the price of gold. What is the exchange rate between US dollars and Norwegian krona if one dollar is convertible into 1/10th ounce of gold and one Swiss franc is convertible into 1/40th ounce of gold?

3. Given the foreign exchange rate table H1 published by the Federal Reserve (see http://www.federalreserve.gov/releases/h10/current/), calculate cross rates for the Monday in the table for:

   a) Mexican peso per Swedish krona
   b) Swiss franc per Euro
   c) New Zealand dollar per Canadian dollar
   d) Japanese yen per South African Rand
   e) Australian dollars per Chinese yuan

4. Write down the list of factors that determine the exchange rate. Compare and contrast the importance of these factors for developed vs developing countries.

5. Using the foreign exchange rate model for determining the foreign exchange rate based on the uncovered interest parity, but using (as in the chapter) the home country as the US and the foreign country as the euro area:
   a) Show what would happen to the exchange rate if the ECB decides to lower interest rates;
   b) Show what would happen to the exchange rate if the Federal Reserve decides to raise interest rates;
   c) Show what happens if there an announcement from the ECB that they will start on a new round of quantitative easing of monetary policy (thereby injecting more money into the European economy)
   d) What is the spot exchange rate if the interest rate in the US is 0.5%, the interest rate in the euro area is 0.1%, and the expected future exchange rate is 1 US dollar per euro?

6. What is the difference between uncovered and covered interest parity?

7. What are the limitations of the foreign exchange rate model for determining the foreign exchange rate based on uncovered interest parity?

Patrick Crowley, November 2016.