Chapter 19
The Foreign Exchange Market

■ Multiple Choice

1) The exchange rate is
(a) the price of one currency relative to gold.
(b) the value of a currency relative to inflation.
(c) the change in the value of money over time.
(d) the price of one currency relative to another.
(e) all of the above.
Answer: D
Question Status: New

2) Exchange rates are determined in
(a) the money market.
(b) the foreign exchange market.
(c) the stock market.
(d) the capital market.
(e) both (b) and (c) of the above.
Answer: B
Question Status: New

3) Although market trades are said to involve the buying and selling of currencies, most trades involve the buying and selling of
(a) bank deposits denominated in different currencies.
(b) SDRs.
(c) gold.
(d) ECUs.
Answer: A
Question Status: Previous Edition

4) The immediate (two-day) exchange of one currency for another is a
(a) forward transaction.
(b) spot transaction.
(c) money transaction.
(d) exchange transaction.
(e) daily transaction.
Answer: B
Question Status: New

5) An agreement to exchange dollar bank deposits for euro bank deposits in one month is a
(a) spot transaction.
(b) future transaction.
(c) forward transaction.
(d) monthly transaction.
(e) deposit transaction.
Answer: C
Question Status: New

6) Today 1 euro can be purchased for $1.10. This is the
(a) spot exchange rate.
(b) forward exchange rate.
(c) fixed exchange rate.
(d) money exchange rate.
(e) financial exchange rate.
Answer: A
Question Status: New

7) In an agreement to exchange dollars for euros in three months at a price of $0.90 per euro, the price is the
(a) spot exchange rate.
(b) money exchange rate.
(c) forward exchange rate.
(d) monthly exchange rate.
(e) fixed exchange rate.
Answer: C
Question Status: New

8) When the value of the British pound changes from $1.25 to $1.50, then
(a) the pound has appreciated and the dollar has appreciated.
(b) the pound has depreciated and the dollar has appreciated.
(c) the pound has appreciated and the dollar has depreciated.
(d) the pound has depreciated and the dollar has depreciated.
Answer: C
Question Status: Previous Edition

9) When the value of the British pound changes from $1.50 to $1.25, then
(a) the pound has appreciated and the dollar has appreciated.
(b) the pound has depreciated and the dollar has appreciated.
(c) the pound has appreciated and the dollar has depreciated.
(d) the pound has depreciated and the dollar has depreciated.
Answer: B
Question Status: Previous Edition

10) When the value of the dollar changes from 0.5 pounds to 0.75 pounds, then
(a) the pound has appreciated and the dollar has appreciated.
(b) the pound has depreciated and the dollar has appreciated.
(c) the pound has appreciated and the dollar has depreciated.
(d) the pound has depreciated and the dollar has depreciated.
Answer: B
Question Status: Revised

11) When the value of the dollar changes from 0.75 pounds to 0.5 pounds, then
(a) the pound has appreciated and the dollar has appreciated.
(b) the pound has depreciated and the dollar has appreciated.
(c) the pound has appreciated and the dollar has depreciated.
(d) the pound has depreciated and the dollar has depreciated.
Answer: C
Question Status: Revised

12) When the exchange rate for the Mexican peso changes from 9 pesos to the dollar to 10 pesos to the dollar, then
(a) the peso has appreciated and the dollar has appreciated.
(b) the peso has depreciated and the dollar has appreciated.
(c) the peso has appreciated and the dollar has depreciated.
(d) the peso has depreciated and the dollar has depreciated.
Answer: B
Question Status: Revised

13) When the exchange rate for the Mexican peso changes from 10 pesos to the dollar to 9 pesos to the dollar, then
(a) the peso has appreciated and the dollar has appreciated.
(b) the peso has depreciated and the dollar has appreciated.
(c) the peso has appreciated and the dollar has depreciated.
(d) the peso has depreciated and the dollar has depreciated.
Answer: C
Question Status: Previous Edition

14) In April 2000, one U.S. dollar traded on the foreign exchange market for about 7.2 French francs. Therefore, one French franc would have purchased about
(a) 4.10 U.S. dollars.
(b) 1.40 U.S. dollars.
(c) 0.41 U.S. dollars.
(d) 0.14 U.S. dollars.
Answer: D
Question Status: Previous Edition

15) In April 2000, one U.S. dollar traded on the foreign exchange market for about 44 Indian rupees. Thus, one Indian rupee would have purchased about

(a) 0.01 U.S. dollars.
(b) 0.02 U.S. dollars.
(c) 0.20 U.S. dollars.
(d) 2.00 U.S. dollars.

Answer: B
Question Status: Previous Edition

16) In April 2000, one U.S. dollar traded on the foreign exchange market for about 180 Spanish pesetas. Therefore, one Spanish peseta would have purchased about

(a) 0.005 U.S. dollars.
(b) 0.05 U.S. dollars.
(c) 0.50 U.S. dollars.
(d) 5.00 U.S. dollars.

Answer: A
Question Status: Previous Edition

17) In April 2000, one U.S. dollar traded on the foreign exchange market for about 1.47 Canadian dollars. Therefore, one Canadian dollar would have purchased about

(a) 2.30 U.S. dollars.
(b) 1.15 U.S. dollars.
(c) 0.67 U.S. dollars.
(d) 0.56 U.S. dollars.

Answer: C
Question Status: Previous Edition

18) At the beginning of 1980, the French franc was valued at 25 cents and in early 1988 it was valued at 17.5 cents. Thus, from 1980 to 1988, the dollar _____ and the franc _____.

(a) appreciated; appreciated
(b) appreciated; depreciated
(c) depreciated; depreciated
(d) depreciated; appreciated

Answer: B
Question Status: Previous Edition

19) If the dollar _____ from 1.0 European euros per dollar to 0.9 euros per dollar, the euro _____ from 1.0 dollar to 1.1 dollars per euro.

(a) appreciates; appreciates
(b) appreciates; depreciates
(c) depreciates; depreciates
(d) depreciates; appreciates

Answer: D
Question Status: Previous Edition

20) If the dollar _____ from 5 Mexican pesos per dollar to 10 pesos per dollar, the peso _____ from 20 cents to 10 cents per peso.

(a) appreciates; appreciates
(b) appreciates; depreciates
(c) depreciates; depreciates
(d) depreciates; appreciates

Answer: B
Question Status: Previous Edition

21) If the dollar appreciates from 5 French francs per dollar to 10 francs per dollar, the franc depreciates from _____ cents to _____ cents per franc.

(a) 20; 10
(b) 10; 20
(c) 10; 25
(d) 20; 25

Answer: A
Question Status: Revised

22) If the British pound appreciates from $0.50 to $0.75 per U.S. dollar, the dollar depreciates from _____ to _____ pounds per dollar.

(a) 2; 2.5
(b) 2; 1.33
(c) 2; 1.5
(d) 2; 1.25

Answer: B
Question Status: Previous Edition

23) If the Japanese yen appreciates from one cent to two cents per yen, the dollar depreciates from _____ to _____ yen per dollar.

(a) 100; 50
(b) 10; 5
(c) 5; 10
(d) 50; 100

Answer: A
Question Status: Revised

24) If the dollar appreciates from 1.5 Brazilian reals per dollar to 2.0 reals per dollar, the real depreciates from _____ to _____ dollars per real.

(a) $0.67; $0.50
(b) $0.33; $0.50
(c) $0.75; $0.50
(d) $0.50; $0.67
(e) $0.50; $0.75

Answer: A
Question Status: Previous Edition

25) If the relative price of the dollar changes from 1.5 Brazilian reals to 2.0 reals per dollar, the dollar is said to _____ and the real is said to _____.

(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; depreciate
(d) depreciate; appreciate

Answer: B
Question Status: Previous Edition

26) If the relative price of the dollar changes from 2.0 Brazilian reals to 1.5 reals per dollar, the dollar is said to _____ and the real is said to _____.

(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; depreciate
(d) depreciate; appreciate

Answer: D
Question Status: Previous Edition

27) If the exchange rate between the dollar and the euro changes from 1.0 to 1.1 euros per dollar, the

(a) euro appreciates and the dollar depreciates.
(b) dollar depreciates and the euro appreciates.
(c) euro depreciates and the dollar appreciates.
(d) dollar depreciates and the euro depreciates.

Answer: C
Question Status: Previous Edition

28) If the exchange rate between the dollar and the euro changes from 1.1 to 1.0 euros per dollar, the

(a) euro appreciates and the dollar appreciates.
(b) dollar depreciates and the euro appreciates.
(c) euro depreciates and the dollar appreciates.
(d) dollar depreciates and the euro depreciates.

Answer: B
Question Status: Revised

29) If the exchange rate between the dollar and the euro changes from 90 to 95 cents per euro, the

(a) euro appreciates and the dollar appreciates.
(b) dollar depreciates and the euro appreciates.
(c) euro depreciates and the dollar appreciates.
(d) dollar depreciates and the euro depreciates.

Answer: B
Question Status: Revised

30) If the exchange rate between the dollar and the euro changes from 99 to 97 cents per euro, the
(a) euro appreciates and the dollar appreciates.
(b) dollar depreciates and the euro appreciates.
(c) dollar depreciates and the euro depreciates.
(d) dollar appreciates and the euro depreciates.

Answer: D
Question Status: Revised

31) If the dollar price of a euro increases from $0.90 to $1.00, the euro
(a) depreciates from 1.11 euros per dollar to 1 euro per dollar.
(b) appreciates from 1.11 euros per dollar to 1 euro per dollar.
(c) depreciates from 1 euro per dollar to 1.11 euros per dollar.
(d) appreciates from 1 euro per dollar to 1.11 euros per dollar.
(e) appreciates from 0.90 euros per dollar to 1 euro per dollar.

Answer: B
Question Status: New

32) If the Swiss franc price of a dollar increases from 1.50 Swiss francs to 1.6 Swiss francs per dollar, the dollar
(a) appreciates from $0.67 per Swiss franc to $0.625 per Swiss franc.
(b) depreciates from $0.67 per Swiss franc to $0.625 per Swiss franc.
(c) appreciates from $0.625 per Swiss franc to $0.67 per Swiss franc.
(d) depreciates from $0.625 per Swiss franc to $0.67 per Swiss franc.
(e) appreciates from $1.50 to $1.60 per Swiss franc.

Answer: A
Question Status: New

33) When the exchange rate for the German mark changes from $0.50 to $0.30, then, holding everything else constant,
(a) the mark has appreciated and German cars sold in the United States become more expensive.
(b) the mark has appreciated and German cars sold in the United States become less expensive.
(c) the mark has depreciated and American wheat sold in Germany becomes more expensive.
(d) the mark has depreciated and American wheat sold in Germany becomes less expensive.

Answer: C
Question Status: Revised

34) If the dollar appreciates relative to the British pound,
(a) British dishes will become cheaper in the United States.
(b) American wheat will become cheaper in Great Britain.
(c) British dishes will become more expensive in the United States.
(d) no change will occur.

Answer: A
Question Status: Previous Edition

35) If the dollar depreciates relative to the British pound
(a) British dishes will become cheaper in the United States.
(b) American wheat will become more expensive in Great Britain.
(c) British dishes will become more expensive in the United States.
(d) both (b) and (c) will occur.
Answer: C
Question Status: Previous Edition

36) If the dollar depreciates relative to the British pound
(a) British dishes will become more expensive in the United States.
(b) American computers will become less expensive in Great Britain
(c) Swiss chocolate will become cheaper in the United States.
(d) both (a) and (b) will occur.
(e) both (b) and (c) will occur.
Answer: D
Question Status: Previous Edition

37) If the dollar depreciates relative to the Swiss franc
(a) Swiss chocolate will become cheaper in the United States.
(b) American computers will become more expensive in Switzerland.
(c) Swiss chocolate will become more expensive in the United States.
(d) Swiss computers will become cheaper in the United States.
Answer: C
Question Status: Previous Edition

38) If the dollar depreciates relative to the Swiss franc
(a) Swiss chocolate will become more expensive in the United States.
(b) American computers will become less expensive in Switzerland.
(c) Swiss chocolate will become cheaper in the United States.
(d) both (a) and (b) of the above.
Answer: D
Question Status: Previous Edition

39) If the dollar appreciates relative to the Swiss franc
(a) Swiss chocolate will become more expensive in the United States.
(b) American computers will become less expensive in Switzerland.
(c) Swiss chocolate will become cheaper in the United States.
(d) both (a) and (b) of the above.
Answer: C
Question Status: Previous Edition

40) All else constant, an appreciation of the Swiss franc causes
(a) Swiss watches sold in the United States to become more expensive.
(b) American computers sold in Switzerland to become more expensive.
(c) Swiss cheese sold in the United States to become cheaper.
(d) American automobiles sold in Switzerland to become cheaper.
(e) both (a) and (d) of the above are true.

Answer: E
Question Status: Study Guide

41) When a country's currency appreciates (rises in value relative to other currencies), the country's goods abroad become _____ expensive and foreign goods in that country become _____ expensive (holding domestic prices constant in the two countries).
(a) more; less
(b) more; more
(c) less; less
(d) less; more

Answer: A
Question Status: Previous Edition

42) When a country's currency depreciates, its goods abroad become _____ expensive while foreign goods in that country become _____ expensive.
(a) more; less
(b) more; more
(c) less; less
(d) less; more

Answer: D
Question Status: Previous Edition

43) According to the law of one price, if the price of Colombian coffee is 100 Colombian pesos per pound and the price of Brazilian coffee is 4 Brazilian reals per pound, then the exchange rate between the Colombian peso and the Brazilian reals is:
(a) 40 pesos per real.
(b) 100 pesos per real.
(c) 25 pesos per real.
(d) 0.4 pesos per real.
(e) none of the above.

Answer: C
Question Status: Previous Edition

44) The starting point for understanding how exchange rates are determined is a simple idea called _____, which states: if two countries produce an identical good, the price of the good should be the same throughout the world no matter which country produces it.

(a) Gresham's law
(b) the law of one price
(c) purchasing power parity
(d) arbitrage

Answer: B
Question Status: Previous Edition

45) The _____ states that exchange rates between any two currencies will adjust to reflect changes in the price levels of the two countries.

(a) theory of purchasing power parity
(b) law of one price
(c) theory of money neutrality
(d) quantity theory of money

Answer: A
Question Status: Previous Edition

46) The theory of PPP suggests that if one country's price level rises relative to another's, its currency should

(a) depreciate.
(b) appreciate.
(c) float.
(d) do none of the above.

Answer: A
Question Status: Previous Edition

47) The theory of PPP suggests that if one country's price level falls relative to another's, its currency should

(a) depreciate.
(b) appreciate.
(c) float.
(d) do none of the above.

Answer: B
Question Status: Previous Edition

48) The theory of PPP suggests that if one country's price level rises relative to another's, its currency should

(a) depreciate in the long run.
(b) appreciate in the long run.
(c) depreciate in the short run.
(d) do both (a) and (c) of the above.
(e) do both (b) and (c) of the above.

Answer: A
Question Status: Previous Edition

49) The theory of PPP suggests that if one country's price level falls relative to another's, its currency should
(a) depreciate in the long run.
(b) appreciate in the long run.
(c) appreciate in the short run.
(d) depreciate in the short run.
Answer: B
Question Status: Previous Edition

50) The theory of purchasing power parity cannot fully explain exchange rate movements because
(a) not all goods are identical in different countries.
(b) monetary policy differs across countries.
(c) some goods are not traded between countries.
(d) of both (a) and (c) of the above.
(e) of both (b) and (c) of the above.
Answer: D
Question Status: Previous Edition

51) The theory of purchasing power parity cannot fully explain exchange rate movements because
(a) all goods are identical even if produced in different countries.
(b) monetary policy differs across countries.
(c) some goods are not traded between countries.
(d) fiscal policy differs across countries.
Answer: C
Question Status: Previous Edition

52) The purchasing power parity may not fully explain exchange rate movements because
(a) different countries have differing monetary policies.
(b) of changes in the prices of goods and services not traded internationally.
(c) the domestic price level changes by more than the foreign price level.
(d) the foreign price level changes by more than the domestic price level.
(e) different countries have different inflation rates.
Answer: B
Question Status: Study Guide

53) The PPP conclusion that exchange rates are determined solely by changes in relative price levels
(a) rests on the assumption that all goods are identical in both countries.
(b) does not take into account that many goods and services (whose prices are included in a measure of a country's price level) are not traded across borders.
(c) is quite accurate as a long-run proposition.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: E
Question Status: Previous Edition

54) The PPP conclusion that exchange rates are determined solely by changes in relative price levels
(a) rests on the assumption that all goods are identical in both countries.
(b) does not take into account that many goods and services (whose prices are included in a measure of a country's price level) are not traded across borders.
(c) is certainly not accurate as a short-run proposition.
(d) all of the above.
(e) only (a) and (b) of the above.

Answer: D
Question Status: Previous Edition

55) The PPP conclusion that exchange rates are determined solely by changes in relative price levels
(a) rests on the assumption that all goods are identical in both countries.
(b) does not take into account that many goods and services (whose prices are included in a measure of a country's price level) are not traded across borders.
(c) does not appear to be accurate even as a long-run proposition.
(d) all of the above.
(e) only (a) and (b) of the above.

Answer: D
Question Status: Previous Edition

56) The theory of purchasing power parity states that exchange rates between any two currencies will adjust to reflect changes in
(a) the trade balances of the two countries.
(b) the current account balances of the two countries.
(c) fiscal policies of the two countries.
(d) the price levels of the two countries.

Answer: D
Question Status: Previous Edition

57) The theory of purchasing power parity states that exchange rates between any two currencies will adjust to reflect changes in
(a) the interest rates of the two countries.
(b) the current account balances of the two countries.
(c) the price levels of the two countries.
(d) monetary policies of the two countries.

Answer: C
Question Status: Previous Edition

58) The theory of purchasing power parity states that in the long run
(a) exchange rates adjust to changes in relative interest rates.
(b) exchange rates adjust to changes in relative productivity.
(c) exchange rates adjust to changes in relative price levels.
(d) none of the above.

Answer: C
Question Status: Previous Edition

59) In the long run, a rise in a country's price level (relative to the foreign price level) causes its currency to _____, while a fall in the country's relative price level causes its currency to _____.

(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; appreciate
(d) depreciate; depreciate

Answer: C
Question Status: Previous Edition

60) In the long run, a decline in a country's price level (relative to the foreign price level) causes its currency to _____, while a rise in the country's relative price level causes its currency to _____.

(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; appreciate
(d) depreciate; depreciate

Answer: B
Question Status: Revised

61) If the 2001 inflation rate in Canada is 4 percent, and the inflation rate in Mexico is 2 percent, then the theory of purchasing power parity predicts that, during 2001, the value of the Canadian dollar in terms of Mexican pesos will

(a) rise by 5 percent.
(b) rise by 2 percent.
(c) fall by 5 percent.
(d) fall by 2 percent.
(e) do none of the above.

Answer: D
Question Status: Previous Edition

62) According to the purchasing power parity theory, a rise in the United States price level of 5 percent, and a rise in the Mexican price level of 6 percent cause

(a) the dollar to appreciate 1 percent relative to the peso.
(b) the dollar to depreciate 1 percent relative to the peso.
(c) the dollar-peso exchange rate to remain unchanged.
(d) the dollar to appreciate 5 percent relative to the peso.
(e) the peso to depreciate 6 percent relative to the dollar.

Answer: A
Question Status: Study Guide

63) Higher tariffs and quotas cause a country's currency to _____ in the _____ run.

(a) depreciate; short
(b) appreciate; short
(c) depreciate; long
(d) appreciate; long

Answer: D
Question Status: Previous Edition

64) Lower tariffs and quotas cause a country's currency to _____ in the _____ run.
(a) depreciate; short
(b) appreciate; short
(c) depreciate; long
(d) appreciate; long
Answer: C
Question Status: Previous Edition

65) Anything that increases the demand for foreign goods relative to domestic goods tends to _____ the domestic currency because domestic goods will only continue to sell well if the value of the domestic currency is _____.
(a) depreciate; lower
(b) depreciate; higher
(c) appreciate; lower
(d) appreciate; higher
Answer: A
Question Status: Previous Edition

66) Increased demand for a country's _____ causes its currency to appreciate in the long run, while increased demand for _____ causes its currency to depreciate.
(a) imports; imports
(b) imports; exports
(c) exports; imports
(d) exports; exports
Answer: C
Question Status: Previous Edition

67) Increased demand for a country's exports causes its currency to _____ in the long run, while increased demand for imports causes its currency to _____.
(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; appreciate
(d) depreciate; depreciate
Answer: B
Question Status: Previous Edition

68) If a factor increases the demand for _____ goods relative to _____ goods, the domestic currency will appreciate.
(a) foreign; domestic
(b) foreign; foreign
(c) domestic; domestic
(d) domestic; foreign
Answer: D
Question Status: Previous Edition

69) If a factor decreases the demand for _____ goods relative to _____ goods, the domestic currency will depreciate.

(a) foreign; domestic
(b) foreign; foreign
(c) domestic; domestic
(d) domestic; foreign

Answer: D
Question Status: Previous Edition

70) An increase in productivity in a country will cause its currency to _____ because it can produce goods at a _____ price.

(a) depreciate; lower
(b) appreciate; lower
(c) depreciate; higher
(d) appreciate; higher
(e) appreciate; unchanged

Answer: B
Question Status: New

71) If a country experiences a _____ in productivity relative to other countries, its currency will _____ because the cost of producing goods _____.

(a) rise; appreciate; increases
(b) rise; depreciate; decreases
(c) decline; depreciate; increases
(d) decline; depreciate; decreases
(e) decline; appreciate; increases

Answer: C
Question Status: New

72) If, in retaliation for "unfair" trade practices, Congress imposes a 30 percent tariff on Japanese videocassette recorders, but at the same time, U.S. demand for Japanese goods increases, then, in the long run,

(a) the Japanese yen should appreciate relative to the dollar.
(b) the Japanese yen should depreciate relative to the dollar.
(c) the dollar should depreciate relative to the yen.
(d) it is not clear whether the dollar should appreciate or depreciate relative to the yen.

Answer: D
Question Status: Previous Edition

73) If Congress imposes a quota on imports of Japanese cars due to claims of "unfair" trade practices, and Japanese demand for American exports increases at the same time, the long-run result will be
(a) an appreciation of the yen relative to the dollar.
(b) a depreciation of the yen relative to the dollar.
(c) a depreciation of the dollar relative to the yen.
(d) uncertain, as it is not clear whether the yen should appreciate or depreciate.
(e) both (a) and (c) above.
Answer: B
Question Status: Study Guide

74) If the inflation rate in the United States is higher than that in Mexico and productivity is growing at a slower rate in the United States than in Mexico, then, in the long run,
(a) the peso should appreciate relative to the dollar.
(b) the peso should depreciate relative to the dollar.
(c) the dollar should depreciate relative to the peso.
(d) both (a) and (c) will occur.
(e) it is not clear whether the dollar should appreciate or depreciate relative to the peso.
Answer: D
Question Status: Previous Edition

75) If the inflation rate in the United States is higher than that in Mexico and productivity is growing at a slower rate in the United States than in Mexico, then, in the long run,
(a) the peso should appreciate relative to the dollar.
(b) the peso should depreciate relative to the dollar.
(c) the dollar should neither appreciate nor appreciate relative to the peso.
(d) we cannot know whether the dollar will appreciate or depreciate since these factors offset each other.
Answer: A
Question Status: Previous Edition

76) If the inflation rate in the United States is higher than that of Mexico and productivity is growing at a slower rate in the United States than it is in Mexico, in the long run,
(a) the peso should appreciate relative to the dollar.
(b) the peso should depreciate relative to the dollar.
(c) there should be no change in the peso price of dollars.
(d) it is not clear what will happen to the peso price of dollars.
Answer: A
Question Status: Revised

77) If the Brazilian demand for American exports rises at the same time that U.S. productivity rises relative to Brazilian productivity, then, in the long run,
(a) the Brazilian real should depreciate relative to the dollar.
(b) the Brazilian real should appreciate relative to the dollar.
(c) the dollar should depreciate relative to the Brazilian real.
(d) both (a) and (c) will occur.
(e) it is not clear whether the Brazilian real should appreciate or depreciate relative to the dollar.
Answer: A
Question Status: Previous Edition

78) If the Brazilian demand for American exports rises at the same time that U.S. productivity rises relative to Brazilian productivity, then, in the long run,
(a) the Brazilian real should appreciate relative to the dollar.
(b) the dollar depreciate relative to the Brazilian real.
(c) the dollar should appreciate relative to the Brazilian real.
(d) it is not clear whether the Brazilian real should appreciate or depreciate relative to the dollar.
Answer: C
Question Status: Previous Edition

79) The theory of asset demand suggests that the most important factor affecting the demand for domestic and foreign deposits is
(a) the level of trade and capital flows.
(b) the expected return on these assets relative to one another.
(c) the liquidity of these assets relative to one another.
(d) the riskiness of these assets relative to one another.
Answer: B
Question Status: Previous Edition

80) The theory of asset demand suggests that the most important factor affecting the demand for domestic and foreign deposits is the
(a) productivity of the domestic country relative to the foreign country.
(b) price level of the domestic country relative to the foreign country.
(c) preference for domestic goods relative to foreign goods.
(d) expected return on these assets relative to one another.
Answer: D
Question Status: Previous Edition

81) The _____ suggests that the most important factor affecting the demand for domestic and foreign deposits is the expected return on domestic assets relative to foreign assets.
(a) theory of asset demand
(b) law of one price
(c) interest parity condition
(d) theory of foreign capital mobility
Answer: A
Question Status: Previous Edition

82) The theory of asset demand suggests that the most important factor affecting the demand for domestic and foreign deposits is the _____ on these assets relative to one another.

(a) interest rate
(b) risk
(c) expected return
(d) liquidity

Answer: C
Question Status: Previous Edition

83) The condition that states that the domestic interest rate equals the foreign interest rate minus the expected appreciation of the domestic currency is called

(a) the purchasing power parity condition.
(b) the interest parity condition.
(c) money neutrality.
(d) the theory of foreign capital mobility.

Answer: B
Question Status: Previous Edition

84) As the relative expected return on dollar deposits increases, foreigners will want to hold more _____ deposits and less _____ deposits.

(a) foreign; foreign
(b) foreign; dollar
(c) dollar; foreign
(d) dollar; dollar

Answer: C
Question Status: Previous Edition

85) As the relative expected return on dollar deposits increases,

(a) foreigners will want to hold more dollar deposits and less foreign deposits.
(b) Americans will want to hold more dollar deposits and less foreign deposits.
(c) Americans will want to hold less dollar deposits and more foreign deposits.
(d) both (a) and (b) of the above.
(e) both (a) and (c) of the above.

Answer: D
Question Status: Previous Edition

86) As the relative expected return on dollar deposits increases,

(a) foreigners will want to hold fewer dollar deposits and more foreign deposits.
(b) Americans will want to hold more dollar deposits and less foreign deposits.
(c) Americans will want to hold fewer dollar deposits and more foreign deposits.
(d) Americans and foreigners will be indifferent towards holding dollar deposits or foreign deposits.

Answer: B
Question Status: Previous Edition

87) When Americans or foreigners expect the return on _____ deposits to be high relative to the return on _____ deposits, there is a higher demand for dollar deposits and a correspondingly lower demand for foreign deposits.

(a) dollar; dollar
(b) dollar; foreign
(c) foreign; dollar
(d) foreign; foreign

Answer: B
Question Status: Previous Edition

88) When Americans or foreigners expect the return on _____ deposits to be high relative to the return on _____ deposits, there is a _____ demand for dollar deposits.

(a) dollar; dollar; lower
(b) dollar; foreign; higher
(c) foreign; dollar; higher
(d) foreign; foreign; lower

Answer: B
Question Status: Revised

89) When Americans or foreigners expect the return on dollar deposits to be high relative to the return on foreign deposits, there is a _____demand for dollar deposits and a correspondingly _____ demand for foreign deposits.

(a) higher; higher
(b) higher; lower
(c) lower; higher
(d) lower; lower

Answer: B
Question Status: Previous Edition

90) When Francoise the Foreigner considers the expected return of dollar deposits in terms of foreign currency the expected return must be adjusted for

(a) any expected appreciation or depreciation of the dollar.
(b) any expected appreciation or depreciation of the foreign currency.
(c) both (a) and (b) of the above.
(d) neither (a) nor (b) of the above.

Answer: A
Question Status: Previous Edition

91) If the interest rate on euro-denominated assets is 7 percent and it is 5 percent on dollar-denominated assets, and if the dollar is expected to appreciate at a 4 percent rate, for Francois the Frenchman the expected rate of return on dollar-denominated assets is

(a) 11 percent.
(b) 9 percent.
(c) 5 percent.
(d) 3 percent.
(e) 1 percent.

Answer: B
Question Status: Previous Edition

92) If the interest rate is 7 percent on euro-denominated assets and 5 percent on dollar-denominated assets, and if the dollar is expected to appreciate at a 4 percent rate,

(a) euro-denominated assets have a higher expected return than dollar-denominated assets.
(b) the expected return on euro-denominated assets in dollars is 1 percent.
(c) the expected return on dollar-denominated assets in euros is 1 percent.
(d) the expected return on euro-denominated assets in dollars is 3 percent.
(e) the expected return on dollar-denominated assets in euros is 3 percent.

Answer: D
Question Status: Revised

93) If the interest rate is 13 percent on euro-denominated assets and 15 percent on peso-denominated assets, and if the euro is expected to appreciate at a 4 percent rate relative to the peso, then

(a) euro-denominated assets have a lower expected return than peso-denominated assets.
(b) the expected return on euro-denominated assets in pesos is 9 percent.
(c) the expected return on peso-denominated assets in euros is 9 percent.
(d) both (a) and (b) of the above will occur.
(e) none of the above will occur.

Answer: E
Question Status: Previous Edition

94) If the interest rate is 13 percent on euro-denominated assets and 15 percent on peso-denominated assets, and if the euro is expected to appreciate at a 4 percent rate relative to the peso, then

(a) euro-denominated assets have a higher expected return than peso-denominated assets.
(b) the expected return on euro-denominated assets in pesos is 9 percent.
(c) the expected return on peso-denominated assets in euros is 11 percent.
(d) both (a) and (b) of the above will occur.
(e) both (a) and (c) of the above will occur.

Answer: E
Question Status: Previous Edition

95) If the interest rate is 13 percent on euro-denominated assets and 15 percent on peso-denominated assets, and if the euro is expected to appreciate at a 4 percent rate relative to the peso, then
(a) euro-denominated assets have a higher expected return than peso-denominated assets.
(b) the expected return on euro-denominated assets in pesos is 9 percent.
(c) the expected return on peso-denominated assets in euros is 9 percent.
(d) both (a) and (b) of the above will occur.

Answer: A
Question Status: Previous Edition

96) If the interest rate on euro-denominated assets is 13 percent and it is 15 percent on peso-denominated assets, and if the euro is expected to appreciate at a 4 percent rate, for Manuel the Mexican the expected rate of return on euro-denominated assets is
(a) 19 percent.
(b) 17 percent.
(c) 13 percent.
(d) 11 percent.
(e) 9 percent.

Answer: B
Question Status: Previous Edition

97) If the interest rate on euro-denominated assets is 13 percent and it is 15 percent on peso-denominated assets, and if the euro is expected to appreciate at a 4% rate, for Francois the Frenchman the expected rate of return on peso-denominated assets is
(a) 19 percent.
(b) 17 percent.
(c) 15 percent.
(d) 11 percent.
(e) 9 percent.

Answer: D
Question Status: Previous Edition

98) With a 10 percent interest rate on dollar deposits, and an expected appreciation of 7 percent over the coming year, the expected return on dollar deposits in terms of the foreign currency is
(a) 3 percent.
(b) 10 percent.
(c) 13.5 percent.
(d) 17 percent.
(e) 24 percent.

Answer: D
Question Status: Study Guide

99) With a 10 percent interest rate on dollar deposits, and an expected appreciation of 7 percent over the coming year, the expected return on dollar deposits in terms of the dollar is
(a) 3 percent.
(b) 10 percent.
(c) 13.5 percent.
(d) 17 percent.
(e) 24 percent.
Answer: B
Question Status: Study Guide

100) The expected return on the dollar deposit in terms of foreign currency can be written as the _____ of the interest rate on dollar deposits and the expected appreciation of the dollar.
(a) product.
(b) ratio.
(c) sum.
(d) difference.
Answer: C
Question Status: Previous Edition

101) In a world with few impediments to capital mobility, the domestic interest rate equals the sum of the foreign interest rate and the expected depreciation of the domestic currency, a situation known as the
(a) interest parity condition.
(b) purchasing power parity condition.
(c) exchange rate parity condition.
(d) foreign asset parity condition.
Answer: A
Question Status: Previous Edition

102) According to the interest parity condition, if the domestic interest rate is
(a) above the foreign interest rate, then there is a positive expected appreciation of the foreign currency.
(b) above the foreign interest rate, then there is a negative expected appreciation of the foreign currency.
(c) below the foreign interest rate, then there is a positive expected appreciation of the foreign currency.
(d) below the foreign interest rate, then the interest parity condition is violated.
Answer: A
Question Status: Previous Edition

103) According to the interest parity condition, if the domestic interest rate is 12 percent and the foreign interest rate is 10 percent, then
(a) the expected appreciation of the foreign currency must be 4 percent.
(b) the expected appreciation of the foreign currency must be 2 percent.
(c) the expected depreciation of the foreign currency must be 2 percent.
(d) the expected depreciation of the foreign currency must be 4 percent.
Answer: B
Question Status: Previous Edition

104) According to the interest parity condition, if the domestic interest rate is 10 percent and the foreign interest rate is 12 percent, then
(a) the expected appreciation of the foreign currency must be 4 percent.
(b) the expected appreciation of the foreign currency must be 2 percent.
(c) the expected depreciation of the foreign currency must be 2 percent.
(d) the expected depreciation of the foreign currency must be 4 percent.

Answer: C
Question Status: Previous Edition

105) According to the interest parity condition, the domestic interest rate is equal to
(a) the foreign interest rate plus the expected appreciation of the domestic currency.
(b) the foreign interest rate less the expected appreciation of the domestic currency.
(c) the foreign interest rate less the expected depreciation of the domestic currency.
(d) the foreign interest rate less the expected depreciation of the domestic currency weighted by the domestic interest rate.

Answer: B
Question Status: Previous Edition

106) If the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on these deposits must also increase.
(b) the expected return on domestic deposits must decrease.
(c) the expected return on domestic deposits must increase.
(d) both (a) and (b) of the above.
(e) both (a) and (c) of the above.

Answer: A
Question Status: Revised

107) If the interest rate on foreign deposits decreases, holding everything else constant,
(a) the expected return on these deposits must also increase.
(b) the expected return on these deposits must decrease.
(c) the expected return on domestic deposits must increase.
(d) then both (a) and (b) of the above.
(e) then both (b) and (c) of the above.

Answer: B
Question Status: Revised

108) The expected return on dollar deposits in terms of dollars, R^D, is
(a) always the interest rate on dollar deposits, i^D, for any exchange rate.
(b) the interest rate on dollar deposits, i^D, only when $E_t > E^e_{t+1}$.
(c) the interest rate on dollar deposits, i^D, only when $E_t < E^e_{t+1}$.
(d) the interest rate on dollar deposits, i^D, only when $E_t = E^e_{t+1}$.

Answer: A
Question Status: Revised

109) In the foreign exchange market, a change in the current exchange rate
(a) results in a movement along the expected return schedule for foreign deposits.
(b) causes the expected return schedule for foreign deposits to shift to the right.
(c) causes the expected return schedule for foreign deposits to shift to the left.
(d) results in a movement along the expected return schedule for domestic deposits.

Answer: A
Question Status: Previous Edition

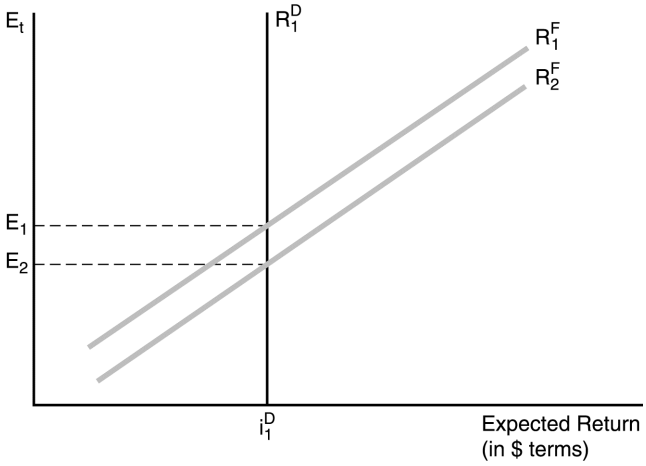


Figure 19-1

110) In Figure 19-1, at an exchange rate below E_2,
(a) the exchange rate is below equilibrium.
(b) the exchange rate will rise causing a greater expected depreciation of the dollar.
(c) the exchange rate will rise causing a greater expected appreciation of the foreign currency.
(d) all of the above.
(e) only (a) and (b) of the above.

Answer: D
Question Status: Previous Edition

111) In Figure 19-1, an exchange rate below E_2,
(a) the exchange rate is below equilibrium.
(b) the exchange rate will rise causing a greater expected appreciation of the dollar.
(c) the exchange rate will rise causing a greater expected depreciation of the foreign currency.
(d) only (a) and (b) of the above.

Answer: A
Question Status: Previous Edition

112) In Figure 19-1, an increase in the expected future exchange rate
(a) shifts the return on foreign deposits schedules from R_1^f to R_2^f, increasing the equilibrium exchange rate.
(b) shifts the return on foreign deposits schedules from R_1^f to R_2^f, reducing the equilibrium exchange rate.
(c) shifts the return on foreign deposits schedules from R_2^f to R_1^f, increasing the equilibrium exchange rate.
(d) shifts the return on foreign deposits schedules from R_2^f to R_1^f, reducing the equilibrium exchange rate.
(e) has no effect on the spot exchange rate.
Answer: C
Question Status: New

113) In Figure 19-1, factors that shift the return schedule on foreign deposits from R_1^f to R_2^f include
(a) a rise in the domestic interest rate.
(b) a fall in the foreign interest rate.
(c) expectations of higher domestic trade barriers.
(d) expectations of an increase in foreign productivity.
(e) all of the above.
Answer: D
Question Status: New

114) In Figure 19-1, the best explanation for the drop in the equilibrium exchange rate from E_1 to E_2 is
(a) a fall of domestic interest rates.
(b) expectations of a rise in the domestic price level relative to the foreign price level.
(c) fall of the foreign interest rate.
(d) expectations of higher domestic productivity.
(e) all of the above.
Answer: B
Question Status: New

115) In Figure 19-1, factors that increase the return on foreign deposits from R_1^f to R_2^f include
(a) an increase in the domestic price level relative to other countries.
(b) expectations of increased domestic import demand.
(c) expectations of increased foreign trade barriers.
(d) an increase in the foreign interest rate.
(e) all of the above.
Answer: E
Question Status: New

116) In Figure 19-1, an increase in the foreign interest rate
(a) shifts R^F from R_1^F to R_2^F, causing the domestic exchange rate to appreciate.
(b) shifts R^F from R_1^F to R_2^F, causing the domestic exchange rate to depreciate.
(c) shifts R^F from R_2^F to R_1^F, causing the domestic exchange rate to appreciate.
(d) shifts R^F from R_2^F to R_1^F, causing the domestic exchange rate to depreciate.
(e) has no effect on exchange rates.
Answer: B
Question Status: New

117) In Figure 19-1, a decrease in the foreign interest rate
(a) shifts R^F from R_1^F to R_2^F, causing the foreign exchange rate to appreciate.
(b) shifts R^F from R_1^F to R_2^F, causing the foreign exchange rate to depreciate.
(c) shifts R^F from R_2^F to R_1^F, causing the foreign exchange rate to appreciate.
(d) shifts R^F from R_2^F to R_1^F, causing the foreign exchange rate to depreciate.
(e) has no effect on exchange rates.
Answer: D
Question Status: New

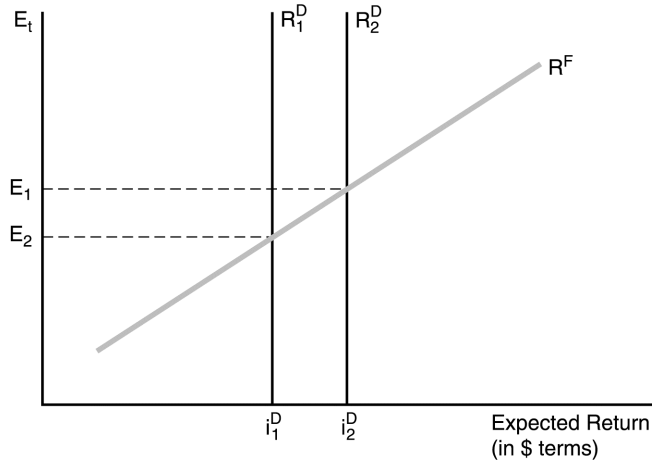


Figure 19-2

118) In Figure 19-2, the factor causing the domestic currency to appreciate is
(a) a rise in the domestic interest rate.
(b) a fall in the foreign interest rate.
(c) a rise in the expected future exchange rate.
(d) an expected fall in foreign productivity.
(e) all of the above.
Answer: A
Question Status: New

119) In Figure 19-2, a decrease in the domestic interest rate
(a) causes the domestic currency to appreciate.
(b) causes the domestic currency to depreciate.
(c) causes the expected future exchange rate to increase.
(d) causes the expected future exchange rate to decrease.
(e) causes both the current and expected future exchange rate to appreciate.

Answer: B
Question Status: New

120) In Figure 19-2, an increase in the domestic interest rate
(a) shifts R^D from R_1^D to R_2^D, causing the domestic exchange rate to appreciate.
(b) shifts R^D from R_1^D to R_2^D, causing the domestic exchange rate to depreciate.
(c) shifts R^D from R_2^D to R_1^D, causing the domestic exchange rate to appreciate.
(d) shifts R^D from R_2^D to R_1^D, causing the domestic exchange rate to depreciate.
(e) has no effect on exchange rates.

Answer: A
Question Status: New

121) In Figure 19-2, a decrease in the domestic interest rate
(a) shifts R^D from R_1^D to R_2^D, causing the domestic exchange rate to appreciate.
(b) shifts R^D from R_1^D to R_2^D, causing the domestic exchange rate to depreciate.
(c) shifts R^D from R_2^D to R_1^D, causing the domestic exchange rate to appreciate.
(d) shifts R^D from R_2^D to R_1^D, causing the domestic exchange rate to depreciate.
(e) has no effect on exchange rates.

Answer: D
Question Status: New

122) In the foreign exchange market, factors that shift the expected return schedule for foreign deposits include
(a) a change in the foreign interest rate.
(b) a change in the expected future exchange rate.
(c) a change in the current exchange rate.
(d) both (a) and (b) of the above.

Answer: D
Question Status: Previous Edition

123) In the foreign exchange market, factors that shift the expected return schedule for foreign deposits include
(a) a change in the foreign interest rate.
(b) a change in the expected future exchange rate.
(c) a change in the current exchange rate.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: E
Question Status: Previous Edition

124) In the foreign exchange market, factors that shift the expected return schedule for foreign deposits include
(a) a change in the domestic interest rate.
(b) a change in the expected future exchange rate.
(c) a change in the current exchange rate.
(d) only (a) and (b) of the above.
Answer: B
Question Status: Previous Edition

125) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the expected return schedule for foreign deposits shifts to the left.
(d) both (a) and (b) of the above occur.
(e) both (a) and (c) of the above occur.
Answer: D
Question Status: Previous Edition

126) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the expected return schedule for foreign deposits shifts to the left.
(d) both (a) and (c) of the above occur.
Answer: B
Question Status: Revised

127) In the foreign exchange market, if the interest rate on foreign deposits decreases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the expected return schedule for foreign deposits shifts to the right.
(d) both (a) and (b) of the above occur.
Answer: B
Question Status: Previous Edition

128) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the expected return schedule for domestic deposits shifts to the right.
(d) both (a) and (b) of the above occur.
Answer: A
Question Status: Previous Edition

129) An increase in the foreign interest rate shifts the R^F schedule to the _____ and causes the domestic currency to _____.
(a) right; depreciate
(b) right; appreciate
(c) left; depreciate
(d) left; appreciate
Answer: A
Question Status: Revised

130) A _____ in the foreign interest rate shifts the R^F schedule to the right and causes the domestic currency to _____.
(a) decline; depreciate
(b) decline; appreciate
(c) rise; depreciate
(d) rise; appreciate
Answer: C
Question Status: Revised

131) A _____ in the foreign interest rate shifts the R^F schedule to the _____ and causes the domestic currency to depreciate.
(a) decline; right
(b) decline; left
(c) rise; right
(d) rise; left
Answer: C
Question Status: Revised

132) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the expected return schedule for domestic deposits shifts to the right.
(d) both (a) and (b) of the above occur.
Answer: A
Question Status: Previous Edition

133) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the expected return schedule for foreign deposits shifts to the right.
(d) both (a) and (b) of the above occur.
(e) both (a) and (c) of the above occur.
Answer: D
Question Status: Previous Edition

134) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar depreciates.
(d) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

135) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the dollar depreciates.
(d) all of the above.
(e) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

136) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return on domestic deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar depreciates.
(d) the dollar appreciates.
Answer: C
Question Status: Previous Edition

137) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar depreciates.
(d) the foreign currency appreciates.
Answer: B
Question Status: Previous Edition

138) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the dollar depreciates.
(d) the foreign currency depreciates.
Answer: D
Question Status: Previous Edition

139) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return schedule for foreign deposits shifts to the right.
(b) the dollar depreciates.
(c) the foreign currency appreciates.
(d) all of the above.
Answer: D
Question Status: Previous Edition

140) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the expected return schedule for foreign deposits shifts to the right.
(b) the dollar depreciates.
(c) the foreign currency depreciates.
(d) both (a) and (b) of the above.
(e) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

141) In the foreign exchange market, if the interest rate on foreign deposits increases, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates
(d) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

142) An increase in the foreign interest rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to depreciate.
(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left
Answer: C
Question Status: Previous Edition

143) If the interest rate on foreign deposits increases, holding everything else constant, the expected return on these deposits must also increase. Thus, an increase in the foreign interest rate shifts the R^F schedule to the _____ and causes the domestic currency to _____.

(a) right; depreciate
(b) right; appreciate
(c) left; depreciate
(d) left; appreciate

Answer: A
Question Status: Revised

144) A decrease in the foreign interest rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to appreciate.

(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left

Answer: D
Question Status: Previous Edition

145) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,

(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar appreciates.
(d) all of the above.

Answer: D
Question Status: Previous Edition

146) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,

(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar appreciates.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.

Answer: E
Question Status: Previous Edition

147) In the foreign exchange market, if the interest rate on foreign deposits declines, holding everything else constant,

(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates
(d) both (a) and (c) of the above.

Answer: B
Question Status: Previous Edition

148) A decrease in i^F shifts the R^F schedule to the _____ and causes the domestic currency to _____.
(a) right; depreciate
(b) right; appreciate
(c) left; depreciate
(d) left, appreciate
Answer: D
Question Status: Revised

149) A _____ in i^F shifts the R^F schedule to the left and causes the domestic currency to _____.
(a) rise; depreciate
(b) rise; appreciate
(c) decline; depreciate
(d) decline; appreciate
Answer: D
Question Status: Revised

150) A _____ in i^F shifts the R^F schedule to the _____ and causes the domestic currency to appreciate.
(a) rise; left
(b) rise; right
(c) decline; left
(d) decline; right
Answer: C
Question Status: Revised

151) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the expected return schedule for foreign deposits shifts to the left.
(d) both (a) and (b) of the above occur.
(e) both (a) and (c) of the above occur.
Answer: C
Question Status: Previous Edition

152) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the expected return schedule for foreign deposits shifts to the right.
(d) both (a) and (b) of the above occur.
(e) both (a) and (c) of the above occur.
Answer: D
Question Status: Previous Edition

153) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the expected return schedule for domestic deposits shifts to the right.
(d) both (a) and (b) of the above occur.
Answer: A
Question Status: Previous Edition

154) A rise in the expected future exchange rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to appreciate.
(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left
Answer: D
Question Status: Previous Edition

155) A rise in the expected future exchange rate shifts the expected return on foreign deposits schedule to the _____ and causes an appreciation of the _____ currency.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: B
Question Status: Previous Edition

156) A _____ in the expected future exchange rate shifts the expected return on foreign deposits schedule to the _____ and causes an appreciation of the domestic currency.
(a) rise; left
(b) rise; right
(c) fall; left
(d) fall; right
Answer: A
Question Status: Previous Edition

157) A decline in the expected future exchange rate shifts the expected return on foreign deposits schedule to the _____ and causes an appreciation of the _____ currency.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: C
Question Status: Previous Edition

158) A _____ in the expected future exchange rate shifts the expected return on foreign deposits schedule to the right and causes an appreciation of the _____ currency.

(a) decline; foreign
(b) decline; domestic
(c) rise; foreign
(d) rise; domestic

Answer: A
Question Status: Previous Edition

159) An expected appreciation of the dollar causes the dollar to _____, and an expected depreciation of the dollar causes the dollar to _____.

(a) appreciate; appreciate
(b) appreciate; depreciate
(c) depreciate; appreciate
(d) depreciate; depreciate

Answer: B
Question Status: Previous Edition

160) A fall in the expected future exchange rate shifts R^F to the _____ and causes a depreciation of the _____ currency.

(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic

Answer: D
Question Status: Revised

161) A fall in the expected future exchange rate shifts R^F to the _____ and causes _____ of the domestic currency.

(a) left; a depreciation
(b) left; an appreciation
(c) right; a depreciation
(d) right; an appreciation

Answer: C
Question Status: Revised

162) A rise in the expected future exchange rate shifts R^F to the _____ and causes a depreciation of the _____ currency.

(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic

Answer: A
Question Status: Revised

163) A _____ in the expected future exchange rate shifts R^F to the _____ and causes a depreciation of the foreign currency.
(a) fall; left
(b) rise; left
(c) fall; right
(d) rise: right

Answer: B
Question Status: Revised

164) A fall in the expected future exchange rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to depreciate.
(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left

Answer: C
Question Status: Previous Edition

165) When the expected future exchange rate increases, the expected return schedule for foreign deposits shifts to the _____, and the exchange rate _____.
(a) right; appreciates
(b) right; depreciates
(c) left; appreciates
(d) left; depreciates
(e) right; remains constant

Answer: D
Question Status: Study Guide

166) A fall in the expected future exchange rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to _____.
(a) domestic; right; depreciate
(b) domestic; left; appreciate
(c) foreign; right; depreciate
(d) foreign; left; appreciate

Answer: C
Question Status: Previous Edition

167) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the dollar appreciates.
(d) both (a) and (c) of the above.

Answer: C
Question Status: Previous Edition

168) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar appreciates.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.
Answer: E
Question Status: Previous Edition

169) In the foreign exchange market, if the exchange rate is expected to increase in the future, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates.
(d) both (a) and (c) of the above.
Answer: B
Question Status: Previous Edition

170) In the foreign exchange market, if the exchange rate is expected to decline in the future, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates.
(d) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

171) In the foreign exchange market, if the exchange rate is expected to decrease in the future, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) both (b) and (c) of the above.
Answer: A
Question Status: Previous Edition

172) In the foreign exchange market, if the exchange rate is expected to decline in the future, holding everything else constant,
(a) the expected return on foreign deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the dollar appreciates.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.
Answer: B
Question Status: Revised

173) In the foreign exchange market, if the exchange rate is expected to decline in the future, holding everything else constant,
(a) the expected return schedule for foreign deposits shifts to the right.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) all of the above.
(e) both (a) and (c) of the above.
Answer: A
Question Status: Previous Edition

174) In the foreign exchange market, factors that shift the expected return schedule for domestic deposits include
(a) a change in the foreign interest rate.
(b) a change in the expected future exchange rate.
(c) a change in the current exchange rate.
(d) a change in the domestic interest rate.
Answer: D
Question Status: Previous Edition

175) In the foreign exchange market, factors that shift the expected return schedule for domestic deposits include
(a) a change in the domestic interest rate.
(b) a change in the expected future exchange rate.
(c) a change in the foreign interest rate.
(d) all of the above.
Answer: A
Question Status: Previous Edition

176) An increase in the domestic interest rate causes
(a) a shift in the expected return schedule for domestic deposits to the right.
(b) a shift in the expected return schedule for domestic deposits to the left.
(c) a shift in the expected return schedule for foreign deposits to the right.
(d) a shift in the expected return schedule for foreign deposits to the left.
(e) a shift to the expected return schedules for both domestic and foreign deposits to the left.
Answer: A
Question Status: Study Guide

177) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for domestic deposits shifts to the right.
(c) the expected return schedule for domestic deposits shifts to the left.
(d) both (a) and (b) of the above occur.
(e) both (a) and (c) of the above occur.
Answer: B
Question Status: Previous Edition

178) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return schedule for domestic deposits shifts to the left.
(b) the expected return schedule for domestic deposits shifts to the right.
(c) the expected return on foreign deposits increases.
(d) both (b) and (c) of the above occur.
Answer: B
Question Status: Previous Edition

179) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return on domestic deposits increases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the dollar depreciates.
(d) both (a) and (c) of the above.
Answer: A
Question Status: Previous Edition

180) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return on domestic deposits increases.
(b) the expected return schedule for domestic deposits shifts to the right.
(c) the dollar appreciates.
(d) all of the above.
Answer: D
Question Status: Previous Edition

181) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return on domestic deposits decreases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar depreciates.
(d) the dollar appreciates.
Answer: D
Question Status: Previous Edition

182) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for foreign deposits shifts to the left.
(c) the dollar depreciates.
(d) the foreign currency depreciates.
Answer: D
Question Status: Previous Edition

183) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the expected return schedule for domestic deposits shifts to the right.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) all of the above.
Answer: D
Question Status: Previous Edition

184) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates.
(d) both (a) and (c) of the above.
Answer: B
Question Status: Previous Edition

185) In the foreign exchange market, if the interest rate on domestic deposits increases, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) both (b) and (c) of the above.
Answer: D
Question Status: Previous Edition

186) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,
(a) the expected return on foreign deposits increases.
(b) the expected return schedule for domestic deposits shifts to the right.
(c) the expected return schedule for domestic deposits shifts to the left.
(d) the expected return on domestic deposits increases.
Answer: C
Question Status: Previous Edition

187) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,
(a) the expected return schedule for domestic deposits shifts to the left.
(b) the expected return schedule for domestic deposits shifts to the right.
(c) the expected return on foreign deposits increases.
(d) none of the above occur.
Answer: A
Question Status: Previous Edition

188) An increase in the domestic interest rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to appreciate.

(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left

Answer: A
Question Status: Previous Edition

189) An increase in the domestic interest rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to _____.

(a) domestic; right; appreciate
(b) domestic; left; depreciate
(c) foreign; right; appreciate
(d) foreign; left; depreciate

Answer: A
Question Status: Previous Edition

190) A rise in the domestic interest rate (i^D) shifts the expected return on domestic deposits to the _____ and causes an appreciation of the _____ currency.

(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic

Answer: D
Question Status: Previous Edition

191) A _____ in the domestic interest rate (i^D) shifts the expected return on domestic deposits to the _____ and causes an appreciation of the domestic currency.

(a) fall; left
(b) rise; left
(c) fall; right
(d) rise; right

Answer: D
Question Status: Previous Edition

192) A rise in i^D shifts the i^D schedule to the _____ and causes a depreciation of the _____ currency.

(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic

Answer: C
Question Status: Revised

193) A _____ in i^D shifts the i^D schedule to the _____ and causes a depreciation of the foreign currency.
(a) fall; left
(b) rise; left
(c) fall; right
(d) rise; right
Answer: D
Question Status: Revised

194) A fall in the domestic interest rate (i^D) shifts the expected return on domestic deposits to the _____ and causes an appreciation of the _____ currency.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: A
Question Status: Previous Edition

195) A _____ in the domestic interest rate (i^D) shifts the expected return on domestic deposits to the _____ and causes an appreciation of the foreign currency.
(a) fall; left
(b) rise; left
(c) fall; right
(d) rise; right
Answer: A
Question Status: Previous Edition

196) A fall in i^D shifts the R^D schedule to the _____ and causes a depreciation of the _____ currency.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: B
Question Status: Revised

197) A _____ in i^D shifts the R^D schedule to the _____ and causes a depreciation of the domestic currency.
(a) fall; left
(b) rise; left
(c) fall; right
(d) rise; right
Answer: A
Question Status: Revised

198) A decrease in the domestic interest rate shifts the expected return schedule for _____ deposits to the _____ and causes the domestic currency to depreciate.

(a) domestic; right
(b) domestic; left
(c) foreign; right
(d) foreign; left

Answer: B
Question Status: Previous Edition

199) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,

(a) the expected return on domestic deposits increases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the dollar depreciates.
(d) both (b) and (c) of the above.

Answer: D
Question Status: Previous Edition

200) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,

(a) the expected return on domestic deposits increases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the dollar appreciates.
(d) all of the above.

Answer: B
Question Status: Previous Edition

201) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,

(a) the expected return on domestic deposits decreases.
(b) the expected return schedule for domestic deposits shifts to the left.
(c) the dollar depreciates.
(d) all of the above.

Answer: D
Question Status: Revised

202) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,

(a) the expected return on domestic deposits increases.
(b) the expected return schedule for foreign deposits shifts to the right.
(c) the dollar depreciates.
(d) the foreign currency depreciates.

Answer: C
Question Status: Previous Edition

203) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,
(a) the expected return schedule for domestic deposits shifts to the left.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) all of the above.
Answer: A
Question Status: Previous Edition

204) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency appreciates.
(d) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

205) In the foreign exchange market, if the interest rate on domestic deposits declines, holding everything else constant,
(a) the dollar depreciates.
(b) the dollar appreciates.
(c) the foreign currency depreciates.
(d) both (b) and (c) of the above.
Answer: A
Question Status: Previous Edition

206) If the domestic real interest rate rises, R^D shifts _____ and the _____ currency appreciates.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: D
Question Status: Revised

207) If the domestic real interest rate _____, R^D shifts _____ and the domestic currency appreciates.
(a) rises; left
(b) rises; right
(c) falls; left
(d) falls; right
Answer: B
Question Status: Revised

208) If the domestic real interest rate falls, R^D shifts _____ and the _____ currency appreciates.
(a) left; foreign
(b) left; domestic
(c) right; foreign
(d) right; domestic
Answer: A
Question Status: Revised

209) If the domestic real interest rate _____, R^D shifts _____ and the foreign currency appreciates.
(a) rises; left
(b) rises; right
(c) falls; left
(d) falls; right
Answer: C
Question Status: Revised

210) If the domestic real interest rate rises, R^D shifts _____ and the domestic currency _____.
(a) left; depreciates
(b) left; appreciates
(c) right; depreciates
(d) right; appreciates
Answer: D
Question Status: Revised

211) If the domestic real interest rate _____, R^D shifts right and the domestic currency _____.
(a) rises; depreciates
(b) rises; appreciates
(c) falls; depreciates
(d) falls; appreciates
Answer: B
Question Status: Revised

212) If the domestic real interest rate falls, R^D shifts _____ and the domestic currency _____.
(a) left; depreciates
(b) left; appreciates
(c) right; depreciates
(d) right; appreciates
Answer: A
Question Status: Revised

213) If the domestic real interest rate _____, R^D shifts left and the domestic currency _____.
(a) rises; depreciates
(b) rises; appreciates
(c) falls; depreciates
(d) falls; appreciates
Answer: C
Question Status: Revised

214) If the domestic real interest rate rises, R^D shifts _____ and the foreign currency _____.
(a) left; depreciates
(b) left; appreciates
(c) right; depreciates
(d) right; appreciates
Answer: C
Question Status: Revised

215) If the domestic real interest rate _____, R^D shifts right and the foreign currency _____.
(a) rises; depreciates
(b) rises; appreciates
(c) falls; depreciates
(d) falls; appreciates
Answer: A
Question Status: Revised

216) If the domestic real interest rate falls, R^D shifts _____ and the foreign currency _____.
(a) left; depreciates
(b) left; appreciates
(c) right; depreciates
(d) right; appreciates
Answer: B
Question Status: Revised

217) If the domestic real interest rate _____, R^D shifts left and the foreign currency _____.
(a) rises; depreciates
(b) rises; appreciates
(c) falls; depreciates
(d) falls; appreciates
Answer: D
Question Status: Revised

218) When the domestic nominal interest rate rises because of an increase in expected inflation, the expected appreciation of the dollar declines, R^F shifts out _____ than R^D, and the exchange rate _____.
(a) less; falls
(b) less; rises
(c) more: falls
(d) more; rises
Answer: C
Question Status: Revised

219) When the domestic nominal interest rate rises because of an increase in expected inflation, the expected appreciation of the dollar declines, _____ shifts out more than _____, and the exchange rate declines.

(a) R^F; R^D
(b) R^F; R^F
(c) R^D; R^D
(d) R^D; R^F

Answer: A
Question Status: Revised

220) A decline of the domestic nominal interest rate due to a decrease in expected inflation, the expected appreciation of the dollar increases, R^F shifts in _____ R^D, and the exchange rate _____.

(a) less than; falls
(b) less than; rises
(c) more than; falls
(d) more than; rises
(e) by the same amount as, remains unchanged

Answer: D
Question Status: Study Guide

221) If the central bank decides to _____ the level of the money supply, the price level will rise in the long run, thereby reducing the expected future exchange rate resulting in a _____ shift of R^F.

(a) increase; rightward
(b) decrease; rightward
(c) increase; leftward
(d) decrease; leftward

Answer: A
Question Status: Revised

222) If the central bank decides to _____ the level of the money supply, the price level will fall in the long run, thereby increasing the expected future exchange rate resulting in a _____ shift of R^F.

(a) increase; rightward
(b) decrease; rightward
(c) increase; leftward
(d) decrease; leftward

Answer: D
Question Status: Revised

223) If the central bank decides to increase the level of the money supply, the price level will rise in the long run, thereby _____ the expected future exchange rate resulting in a _____ shift of R^F.

(a) increasing; rightward
(b) increasing; leftward
(c) decreasing; rightward
(d) decreasing; leftward

Answer: C
Question Status: Revised

224) If the central bank decides to reduce the level of the money supply, the price level will fall in the long run, thereby _____ the expected future exchange rate resulting in a _____ shift of R^F.
(a) increasing; rightward
(b) increasing; leftward
(c) decreasing; rightward
(d) decreasing; leftward

Answer: B
Question Status: Revised

225) If the central bank decides to increase the level of the money supply, the price level will rise in the long run, thereby reducing the expected future exchange rate resulting in a _____ shift of _____.
(a) leftward; R^F
(b) leftward; R^D
(c) rightward; R^F
(d) rightward; R^D

Answer: C
Question Status: Revised

226) If the central bank decides to reduce the level of the money supply, the price level will fall in the long run, thereby increasing the expected future exchange rate resulting in a _____ shift of _____.
(a) leftward; R^F
(b) leftward; R^D
(c) rightward; R^F
(d) rightward; R^D

Answer: A
Question Status: Revised

227) If the central bank decides to increase the level of the money supply, the higher money supply will lead to a higher real money supply in the short run,
(a) causing i^D to rise and the R^D schedule to shift to the left.
(b) causing i^D to rise and the R^D schedule to shift to the right.
(c) causing i^D to fall and the R^D schedule to shift to the left.
(d) causing i^D to fall and the R^D schedule to shift to the right.

Answer: C
Question Status: Revised

228) If the central bank decides to reduce the level of the money supply, the lower money supply will lead to a lower real money supply in the short run,
(a) causing i^D to rise and the R^D schedule to shift to the left.
(b) causing i^D to rise and the R^D schedule to shift to the right.
(c) causing i^D to fall and the R^D schedule to shift to the left.
(d) causing i^D to fall and the R^D schedule to shift to the right.

Answer: B
Question Status: Revised

229) A higher domestic money supply causes the domestic currency to
(a) depreciate in the short run.
(b) depreciate in the long run.
(c) appreciate in the short run.
(d) do both (a) and (b) of the above.
(e) do both (b) and (c) of the above.
Answer: D
Question Status: Previous Edition

230) A higher domestic money supply causes the domestic currency to
(a) depreciate in the short run.
(b) appreciate in the long run.
(c) appreciate in the short run.
(d) do both (a) and (b) of the above.
(e) do both (b) and (c) of the above.
Answer: A
Question Status: Previous Edition

231) A lower domestic money supply causes the domestic currency to
(a) depreciate in the short run.
(b) depreciate in the long run.
(c) appreciate in the short run.
(d) do both (a) and (b) of the above.
(e) do both (b) and (c) of the above.
Answer: C
Question Status: Previous Edition

232) A lower domestic money supply causes the domestic currency to
(a) depreciate in the short run.
(b) appreciate in the long run.
(c) appreciate in the short run.
(d) do both (a) and (b) of the above.
(e) do both (b) and (c) of the above.
Answer: E
Question Status: Previous Edition

233) Decreasing the domestic money supply causes the domestic currency to
(a) depreciate more in the short run than the long run.
(b) depreciate more in the long run than the short run.
(c) appreciate more in the short run than the long run.
(d) appreciate more in the long run than the short run.
(e) depreciate in the short run and appreciate in the long run.
Answer: C
Question Status: Study Guide

234) Which of the following cause a depreciation of the domestic currency?
(a) A higher domestic interest rate due to a higher expected inflation rate
(b) A rise in the domestic real interest rate
(c) An increase in the domestic money supply
(d) Both (a) and (c) of the above
(e) Both (b) and (c) of the above
Answer: D
Question Status: Previous Edition

235) Which of the following cause a depreciation of the domestic currency?
(a) A higher domestic interest rate due to a higher expected inflation rate
(b) A decline in the domestic real interest rate
(c) An increase in the domestic money supply
(d) All of the above
Answer: D
Question Status: Previous Edition

236) Which of the following cause a depreciation of the domestic currency?
(a) A higher domestic interest rate due to a higher expected inflation rate
(b) A decline in the domestic real interest rate
(c) A decrease in the domestic money supply
(d) Both (a) and (b) of the above
Answer: D
Question Status: Previous Edition

237) Which of the following cause a depreciation of the domestic currency?
(a) A lower domestic interest rate due to a lower expected inflation rate
(b) A decline in the domestic real interest rate
(c) A decrease in the domestic money supply
(d) All of the above
Answer: B
Question Status: Previous Edition

238) Which of the following cause an appreciation of the domestic currency?
(a) A higher domestic interest rate due to a higher expected inflation rate
(b) A rise in the domestic real interest rate
(c) An increase in the domestic money supply
(d) Both (a) and (c) of the above
(e) Both (b) and (c) of the above
Answer: B
Question Status: Previous Edition

239) Which of the following cause an appreciation of the domestic currency?
(a) A lower domestic interest rate due to a lower expected inflation rate
(b) A decline in the domestic real interest rate
(c) An increase in the domestic money supply
(d) All of the above

Answer: A
Question Status: Previous Edition

240) Which of the following cause an appreciation of the domestic currency?
(a) A higher domestic interest rate due to a higher expected inflation rate
(b) A decline in the domestic real interest rate
(c) A decrease in the domestic money supply
(d) Both (a) and (b) of the above

Answer: C
Question Status: Previous Edition

241) Which of the following cause an appreciation of the domestic currency?
(a) A lower domestic interest rate due to a lower expected inflation rate
(b) A decline in the domestic real interest rate
(c) A decrease in the domestic money supply
(d) Both (a) and (b) of the above
(e) Both (a) and (c) of the above

Answer: E
Question Status: Previous Edition

242) In the long run, a one-time percentage increase in the money supply is matched by the same one-time percentage rise in the price level,
(a) leaving unchanged the real money supply and all other economic variables such as interest rates. This proposition is called money neutrality.
(b) leaving unchanged the real money supply and the nominal exchange rate. This proposition is called money neutrality.
(c) leaving unchanged the real money supply and all other economic variables such as interest rates. This proposition is called money illusion.
(d) leaving unchanged the real money supply and the nominal exchange rate. This proposition is called money illusion.

Answer: A
Question Status: Previous Edition

243) Money neutrality means that in the long run the domestic interest rate and R^D remain unchanged, implying that the fall in the exchange rate is greater in the _____ run than in the _____ run, a phenomenon called exchange rate overshooting.
(a) short; short
(b) short; long
(c) long; short
(d) long; long

Answer: B
Question Status: Revised

244) Money neutrality means that in the _____ run the domestic interest rate and R_D remain unchanged, implying that the fall in the exchange rate is _____ in the short run than in the long run, a phenomenon called exchange rate overshooting.

(a) long; smaller
(b) long; greater
(c) short; smaller
(d) short; greater

Answer: B
Question Status: Revised

245) A higher domestic money supply causes the domestic currency to

(a) depreciate more in the short run than in the long run.
(b) depreciate more in the long run than in the short run.
(c) appreciate more in the short run than in the long run.
(d) appreciate more in the long run than in the short run.

Answer: A
Question Status: Previous Edition

246) A lower domestic money supply causes the domestic currency to

(a) depreciate more in the short run than in the long run.
(b) depreciate more in the long run than in the short run.
(c) appreciate more in the short run than in the long run.
(d) appreciate more in the long run than in the short run.

Answer: C
Question Status: Previous Edition

247) When the exchange rate falls by more in the short run than it does in the long run when the money supply increases, it is called

(a) exchange rate disequilibrium.
(b) exchange rate overshooting.
(c) the J-curve effect.
(d) none of the above.

Answer: B
Question Status: Previous Edition

248) When the exchange rate falls by more in the short run than it does in the long run when the money supply increases, it is called

(a) exchange rate disequilibrium.
(b) exchange rate sterilization.
(c) the J-curve effect.
(d) none of the above.

Answer: D
Question Status: Previous Edition

249) The weakness of the dollar in the late 1970s, and the strength of the dollar in the early 1980s can be explained by movements in
(a) real interest rates, but not nominal interest rates.
(b) nominal interest rates, but not real interest rates.
(c) relative price levels, but not real interest rates.
(d) none of the above.

Answer: A
Question Status: Previous Edition

250) Evidence from the United States during the period 1973–2002 indicates that the value of the dollar and the
(a) measure of the real interest rate rose and fell together.
(b) measure of the nominal interest rate rose and fell together.
(c) measure of the expected inflation rate rose and fell together.
(d) measure of the actual inflation rate rose and fell together.

Answer: A
Question Status: Revised

251) Evidence from the United States during the period 1973–2002 indicates that the value of the dollar and the
(a) measure of the real interest rate moved in opposite directions.
(b) measure of the real interest rate rose and fell together.
(c) measure of the nominal interest rate moved in opposite directions.
(d) measure of the nominal interest rate rose and fell together.

Answer: B
Question Status: Revised

252) Evidence from the United States during the period 1973–2002 indicates the correspondence between nominal interest rates and exchange rate movements is
(a) much closer than that between real interest rates and exchange rate movements.
(b) not nearly as close as that between government spending and exchange rate movements.
(c) not nearly as close as that between government deficits and exchange rate movements.
(d) not nearly as close as that between real interest rates and exchange rate movements.

Answer: D
Question Status: Revised

■ Essay Questions

1) Explain the law of one price and the theory of purchasing power parity. Why doesn't the purchasing power parity explain all exchange rate movements? What factors determine long-run exchange rates?

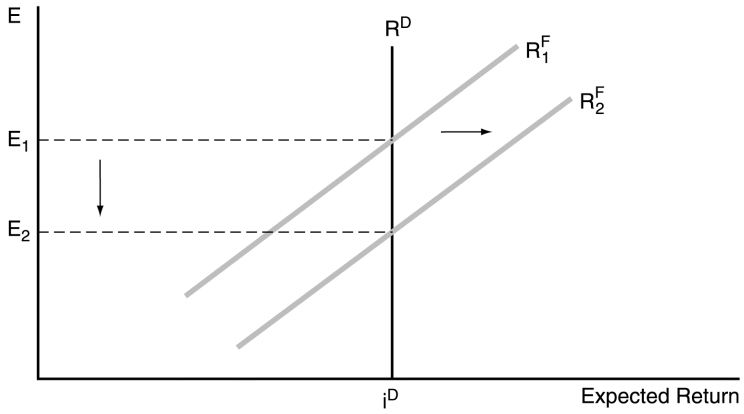
Answer: With no trade barriers and low transport costs, the law of one price states that the price of traded goods should be the same in all countries. The purchasing power parity theory extends the law of one price to total economies. PPP states that exchange rates should adjust to reflect changes in the price levels between two countries. PPP may fail to fully explain exchange rates because goods are not identical, and price levels include traded and nontraded goods and services. Long-run exchange rates are determined by domestic price level relative to foreign price levels, trade barriers, import and export demand, and productivity.

2) Explain the interest parity condition. What key assumption underlies this condition? What factors affect the returns on domestic and foreign deposits?

Answer: The interest parity condition states that returns on domestic and foreign deposits will be equal. The key assumption for this condition is capital mobility. The return on domestic deposits is equal to the domestic interest rate. The return on foreign deposits is equal to the foreign interest rate minus the expected rate of appreciation of the domestic currency.

3) Explain and show graphically the effect of a decrease in the expected future exchange rate on the equilibrium exchange rate.

Answer: A fall in the expected future exchange rate shifts R^F to the right, causing a depreciation of the domestic exchange rate. R^F shifts to the right, from R_1^F to R_2^F. The equilibrium exchange rate falls from E_1 to E_2.



4) Explain and show graphically the effect of a decrease in the domestic nominal interest rate due to a decrease in expected inflation on the equilibrium exchange rate.

Answer: The decrease in expected inflation lowers the domestic nominal interest rate, and increases expected dollar appreciation by more than the fall in the domestic interest rate. Thus, R^F shifts to the left by more than R^D, causing the domestic exchange rate to appreciate from E_1 to E_2.