EE452

Guidelines

Topic 1

Multiple Choice:

1. B

2. A

3. B

4. D

5. B

6. B

7. B

8. C

9. A

10. A

Essay Question:

POSSIBLE RESPONSE: The current account includes all debit and credit items like exports and imports of goods and services, income receipts and income payments, and gifts. In addition to the current account, the financial account and the changes in official international reserves are part of the balance of payments of a country. The current account balance must equal net foreign investment (the increase in the country's foreign financial assets minus the increase in the country's foreign financial liabilities). If a country has a current account deficit, then its net foreign investment is negative, and it is acting as a net borrower from the rest of the world.

The second meaning of the current account is associated with the national savings and investments. A country can either invest its national savings domestically or abroad. That means that the net foreign investment is the difference between national savings and domestic investments. A current account deficit means that a country's domestic investments exceed its savings.

The third view on the current account is as a difference between domestic product and national expenditure. From this viewpoint a deficit on the current account implies that the country buys more goods and services than it produces goods and services.

Topic 2

Multiple Choice:

1. A

2. B

3. D

4. B

5. C

6. D

7. A

8. D

9. D

10. A

Essay Question:

a. POSSIBLE RESPONSE: Tariffs and quotas placed by the U.S. on all imports into the country would decrease U.S. imports and thus decrease the demand for foreign currency. This, in turn, would lead to an appreciation of the dollar vis-à-vis other currencies.

b. POSSIBLE RESPONSE: By itself, decreased demand by foreign consumers for the U.S. exports would decrease demand for U.S. dollars and lead to a depreciation of the dollar vis-à-vis other currencies. By itself, an increased U.S. demand for import would increase demand for foreign currency, so, the foreign currency would appreciate and the dollar would depreciate. The two changes together therefore would depreciate the dollar.