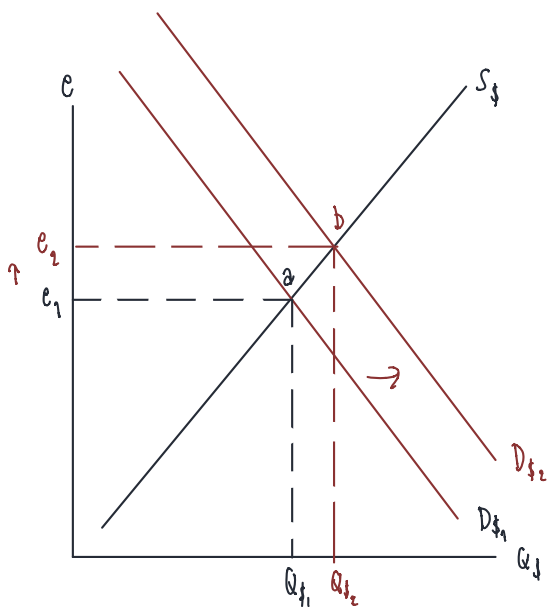


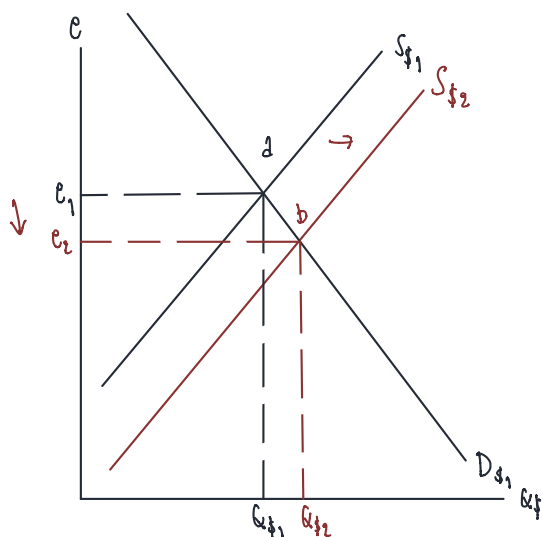
assignment 4

1.2



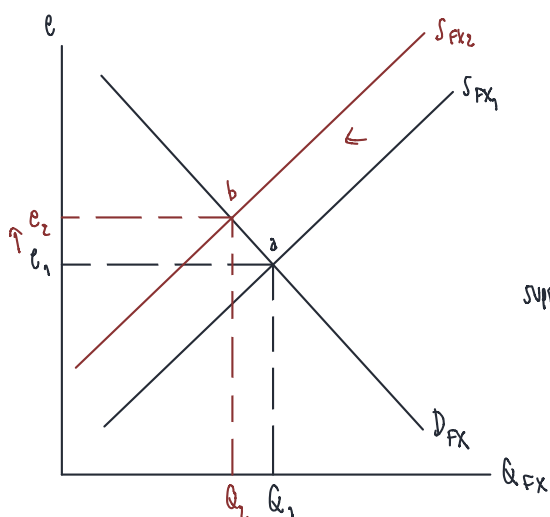
The demand for dollars increase and the demand curve will shift right from $D_{\$1}$ to $D_{\$2}$. At point e_1 , there is an excess demand for dollar which lead to e increase from e_1 to e_2 . The US dollar will be appreciate and Thai baht will be depreciate.

1.4

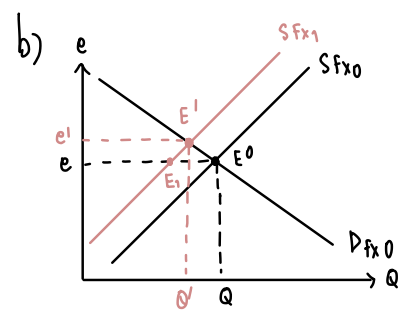


A positive improvement in production technology of Thailand causes a decrease in domestic price. The demand for Thai goods raise so, the export will be increase. The supply of dollars will raise and then shift right from $S_{\$1}$ to $S_{\$2}$. At point e_1 , there is an excess supply of dollar. e will be fall. The dollar will depreciate and Thai baht will be appreciate.

2a)



When S&P decide to downgrade the credit rating of Thai economy. It will cause Thai credit ability to invest falling down and lead to hesitation of foreigners to exchange US dollar into Thai baht. Hence, supply curve will shift left from S_{FX1} to S_{FX2} . At point e_1 , there is an excess demand. e will rise from e_1 to e_2 . It can implies that when exchange rate increases, foreigner will supply USD because Thai products are cheaper relative to others. However, domestic people will demand to hold less USD as it is more expensive since THB depreciation, foreign goods become more expensive.

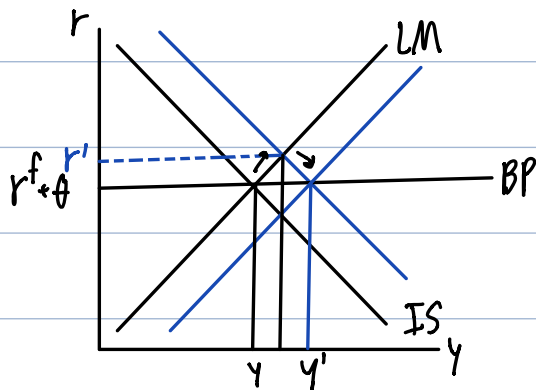


From question a, Thai Baht depreciates and Thailand faces excess demand. Hence, central bank needs to supply forex reserve. As a result, supply for forex will shift back at E_0 (equilibrium).

c) When central bank supply forex reserve, it decreases forex reserve in Thailand, currency in circulation also falls, and leads to rise in interest rate. Therefore, government needs to increase their asset by stimulating people to buy more government bond.

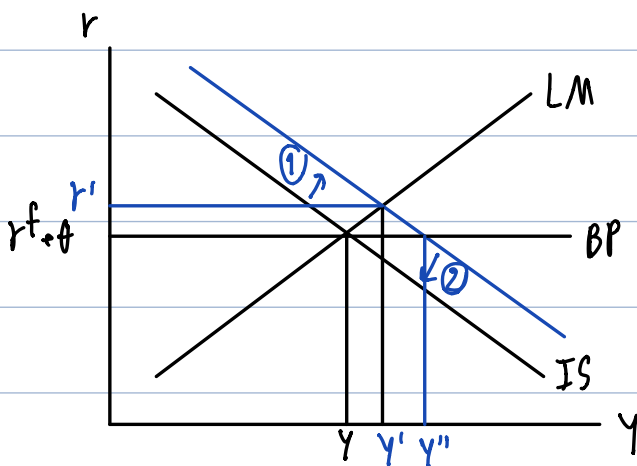
3.2) 3.2) An increase in government spending.

(fixed exchange)



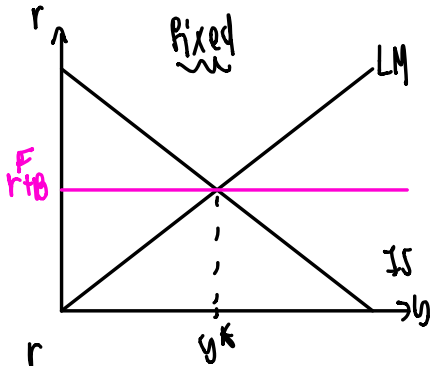
As government spending increase ($G \uparrow$). It makes IS shift to the left. result in increase in interest (r) that would attract huge capital inflow to the country. So, central bank need to print a lot of Baht as an exchange for high demand of baht. As M_s increase $r \downarrow$ unit it goes back at $r^f + \theta$. As a result that $r \downarrow$, it makes consumption & investment increase. That generate even higher level of output.

An increase in government spending (flexible exchange)

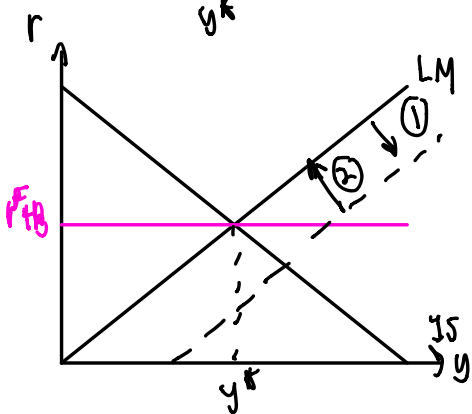


Under flexible exchange rate, after government spending increase, IS shift to the left as a consequence. Interest increase from $r^f + \theta$ to r' , and GDP of country increase from y to y' . After a big inflow of capital. It would cause baht appreciate. It would cause country to export less which gradually shift IS back to $r^f + \theta$. Due to a decrease in $r \downarrow$, It makes investment and consumption increase even further from the first shift (y' to y'').

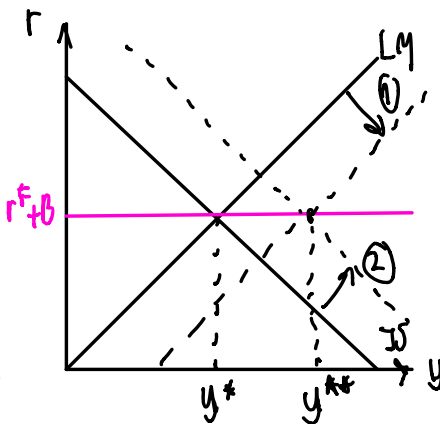
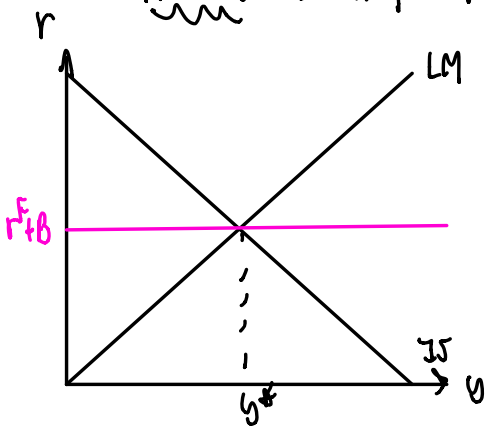
3.4) Thai credit rate have been improved means investors want to invest more in Thailand \rightarrow demand for Thai baht more \rightarrow LM shift to the



right. This causes interest rate to decrease, and dropping in interest rate will decrease the capital inflow. As capital account decrease. Central bank try to reduce the domestic money supply in order to shift LM back to the original point. So, the central bank sell the dollar in hand to increase the current account.



Flexible exchange rate case



Increase in money demand cause LM to shift to the right and cause the interest rate to decrease. Under the flexible exchange rate, low interest rate cause Thai baht to depreciate. When Thai baht depreciate the

increase in export and decrease in import. This because foreign products are now relative higher than domestic products. Lower interest rate will increasing the aggregate expenditure. Firm borrow and invest more. This cause the IS shift to the right. In open economy economic will getting better because y will increase from y^* to y^{**}