

Chapter 6 – Open Economy Macroeconomics

Question 1

A source of supply of foreign exchange is

- Donations given
- Imports
- Exports
- Gifts

Answer:

Exports

Question 2

A source of demand for foreign exchange is

- The brokerage of goods and services
- Smuggle of goods and services
- Export of goods and services
- Import of goods and services

Answer:

Import of goods and services

Question 3

What is the flexible exchange rate?

Answer:

The flexible exchange rate is a type of rate which is ascertained by the demand and supply of distinct currencies in the foreign market.

Question 4

Provide two examples and explain why there is a rise in demand for foreign currency when its price decreases.

Answer:

When the price of foreign currency decreases, imports get cheaper in price. Hence, more demand for foreign exchange by the importers. Tourism is promoted abroad as it becomes cheaper. Hence, the demand for foreign currency increases.

Question 5

What determines the flow of foreign exchange into the nation?

Answer:

Below mentioned are the factors that contribute to the flow of foreign exchange into the nation:

- Trading of domestic commodities by the foreigners
- FDI and portfolio investment in their home nation
- Purchase of foreign exchange

Question 6

What is the foreign exchange and foreign exchange rate?

Answer:

Foreign exchange is referred to as the conversion of a currency into another at a specific rate. The conversion rate for the currencies are fluctuating as the rate of exchange is influenced by the factors of demand and supply.

The foreign exchange rate is referred to as the rate of exchange at which one currency will be exchanged for another currency. It shows the relative value of a currency in comparison to another currency.

Question 7

What is meant by the appreciation of currencies?

Answer:

Appreciation of currencies refers to the increase in the exchange value of the currency when it is compared with other nation.

Question 8

Point out the merit of the fixed exchange rate.

- None
- Ensures the supply of the fixed exchange rate
- Ensures demand for the fixed exchange rate
- Ensures stability for the fixed exchange rate

Answer:

Ensures stability for the fixed exchange rate

Question 9

Point out a demerit of the fixed exchange rate.

- Promotes the objectives of free markets
- Ensures the supply of the fixed exchange rate
- None
- Contradicts the objectives of free markets

Answer:

Contradicts the objectives of free markets

Question 10

Distinguish between the autonomous and accommodating transaction of the balance of payment account.

Answer:

Autonomous transactions take place for a few economic contemplations such as profits, and such financial transactions are independent of the state of balance of payment. Accommodating transactions are undertaken to cover the surplus or deficit in the balance of payments.