

## **Real Exchange Rate Questions**

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1. Suppose the relative supply of domestic goods increases. Show and explain the effect on the real exchange rate.
2. Suppose the relative demand for domestic goods falls. Show and explain the effect on the real exchange rate.
3. Suppose the domestic money supply increases relative to the foreign one. Show and explain the effect on the real exchange rate.
4. Suppose the foreign money supply increases relative to the domestic one. Show and explain the effect on the real exchange rate.
5. Explain why we often look at the real exchange rate instead of the nominal exchange rate alone.
6. How does the real exchange rate overcome some of the problems with PPP?
7. If PPP holds, what does the real exchange rate equal?
8. Suppose you observe an increase in the real exchange rate.
  - a. What are some of the possible causes of this?
  - b. If you learn that interest rates have been falling while the real exchange rate is rising, what is the most likely cause of the real exchange rate's rise?
9. In recent years, the US has been running an increasingly large trade deficit with China. What should have been happening to our real exchange rate with China?

## **General Theory of Exchange Rate Determination**

10. Write the general theory's exchange rate equation.
11. What is the effect on the exchange rate of a relative increase in the level of the domestic money supply? Explain your answer fully.
12. What is the effect on the exchange rate of a relative increase in the growth rate of the domestic money supply? Explain your answer fully.
13. What is the effect on the exchange rate of a relative increase in the demand for domestic products? Explain your answer fully.
14. What is the effect on the exchange rate of a relative increase in the supply of domestic products? Explain your answer fully.

