EC 349
International Finance
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Department of Economics
Wilfrid Laurier University
Fall 2008

# Assignment 4 (REQUIRED)

*<u>Submisson Deadline and Location: Nov 13 in Class</u>*

Total Marks: 30

## Part A True/ False/ Uncertain Questions 10 Marks

*Explain why the following statements are True, False, or Uncertain according to economic principles. Use diagrams and / or numerical examples where appropriate. Unsupported answers will receive no marks. It is the explanation that is important.*

**A1. [10 Marks]**

In an open economy IS-LM model, a permanent increase in domestic government purchases leads to an increase in domestic equilibrium interest rate and output, and results into a depreciation of domestic currency against foreign currency in the short run. [Diagrams required]

**Part B** **Analytical Questions** **20 Marks**

**B1. [20 marks]**

Consider the model of output and exchange rate determination (the AA-DD model) we have studied in class. Suppose the economy begins at its long-run level with output at its full-employment level.

Compare and contrast the short-run effects of the temporary policies by the home government listed below on home output, the home current account, and the nominal exchange rate under a floating exchange rate regime to the effects on these variables under a fixed exchange rate regime.

Use AA-DD-XX diagrams to support your answers.

**I.** An increase in the home money supply.
**II.** A decrease in the home government taxes.