

2007 NATIONAL ECONOMICS CHALLENGE
NCEE/Goldman Sachs Foundation

Round III – International/Current Events
Regional Competition, Adam Smith Division

Please select the one best answer.

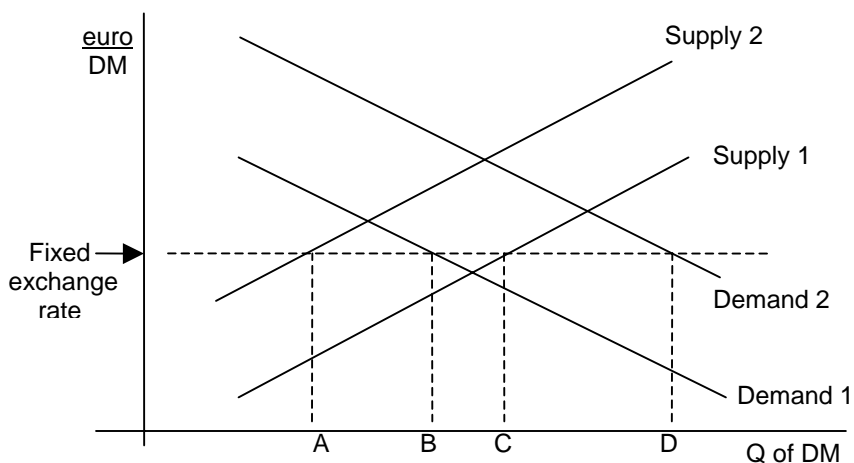
1. Suppose the current exchange rate between U.S. dollars and euros is $\$1.25 = 1$ euro. You expect the exchange rate one year from now to be $\$1 = 1$ euro. You are considering purchasing a 1-year bond in the United States with an interest rate of 4 percent. You have the alternative of purchasing a 1-year German bond of the same risk. You must pay for the German bond in euros. What must the interest rate on the German bond be to make you indifferent between purchasing the U.S. bond and the German bond?
 - A. 1 percent
 - B. 3 percent
 - C. 21 percent
 - D. 25 percent
 - E. 30 percent

2. Which is true of the U.S. balance of payments account?
 - A. The current account includes the balance of trade and the capital account includes the balance of services.
 - B. The current account includes the balance of services and the financial account includes the purchase and sale of foreign assets.
 - C. The current account is the sum of all payments to foreigners and the capital account is the sum of all payments from foreigners to the United States.
 - D. The current account is the sum of all payments from foreigners to the United States and the capital account is the sum of all payments to foreigners.
 - E. The current account represents the flow of current financial capital in a year, and the financial account represents the accumulated stock of the financial capital.

3. According to the National Bureau of Economic Research, when did the last three U.S. recessions begin?
 - A. July 1981; July 1990; March 2001
 - B. April 1985; January 1991; March 2001
 - C. November 1983; March 1993; February 2001
 - D. June 1984; October 1992; February 2001
 - E. December 1982; May 1989; February 2001

4. What are the likely long-run consequences of a country increasing its tariffs on all goods and services it imports?
 - A. Increase in both imports and exports
 - B. Decrease in imports but exports will remain unchanged
 - C. Decrease in both imports and exports
 - D. Decrease in imports and an increase in exports
 - E. Unlike the short-term, no significant long-term consequences

5. After the initial establishment of the euro as the currency of many countries in the European Union, these countries' original currencies were fixed to the euro. The following graph depicts a fictional exchange rate market between euros and German marks during this period. It includes two potential equilibriums relating to Demand 1 and Supply 1, and to Demand 2 and Supply 2.



- If at this certain point in time the mark was found to be *undervalued* at the fixed exchange rate, which policy would the central banks undertake to keep the exchange rate fixed?
- Purchase AD amount of marks
 - Supply AD amount of marks
 - Purchase BC amount of marks
 - Supply BC amount of marks
 - No action would be necessary; supply and demand will adjust to lead back to the fixed exchange rate
6. Consider the market for Yen with Yen on the horizontal (Q) axis and \$/Yen on the vertical (P) axis. The initial equilibrium has the exchange rate at $\$0.01 = 1$ Yen. Japanese consumers decide to buy more U.S. goods. This will cause the supply in this market to _____, causing the dollar to _____ with respect to the Yen. This change in the \$/Yen exchange rate should lead U.S. consumers to buy _____ Japanese goods.
- decrease; depreciate; less
 - decrease; appreciate; more
 - increase; depreciate; less
 - increase; appreciate; more
 - increase; depreciate; less

7. Which best describes the infant industry argument?
- A. Trade restrictions should be removed to increase exports and therefore increase the demand for new domestic industries.
 - B. Trade restrictions should be removed to allow an inflow of foreign capital goods and labor for new domestic industries to acquire.
 - C. Trade restrictions should be removed to allow established domestic industries to export and compete with newly formed foreign industries.
 - D. Trade restrictions should be implemented to protect new domestic industries from foreign competition.
 - E. Trade restrictions should be implemented to protect established domestic industries from competition from newly industrialized foreign competition.
8. Within which range of values was the U.S. capacity utilization rate at the trough of the last U.S. recession?
- A. 55 to 69%
 - B. 70 to 74%
 - C. 75 to 79%
 - D. 80 to 84%
 - E. 85 to 89%
9. During which year did the FOMC last decide to decrease the target federal funds rate?
- A. 2007
 - B. 2006
 - C. 2005
 - D. 2004
 - E. 2003
10. Recent newspaper stories and cable-news shows have discussed the “subprime” problem. Which best explains the “subprime” problem?
- A. Some riskier homeowners are defaulting on their mortgages
 - B. U.S. exchange rates are approaching below optimal levels increasing the U.S. trade deficit
 - C. Banks are offering their best customers loans at rates below the prime rate of interest
 - D. The Federal Reserve has lowered interest rates below a level which allows banks to cover lending costs
 - E. U.S. interest rates could potentially drop below optimal levels relative to trading partners’ interest rates increasing the U.S. trade deficit
11. Which best explains purchasing power parity?
- A. Over a long period of time, interest rates will adjust to equate exchange rates among trading nations.
 - B. Over a long period of time, prices will adjust to equate saving rates among trading nations.
 - C. Over a long period of time, exchange rates will adjust to equate prices among trading nations.
 - D. Over a long period of time, exchange rates will adjust to equate borrowing costs among trading nations.
 - E. Over a long period of time, trade deficits will adjust to equate prices among trading nations.

12. Recently, which correctly identifies U.S. trading partners with regard to whom the U.S has had a trade surplus, and with whom the U.S has had a trade deficit?

<u>Trade Surplus</u>	<u>Trade Deficit</u>
A. Japan, Canada	Singapore, Hong Kong
B. Mexico, Hong Kong	Canada, Singapore
C. Canada, Singapore	Mexico, Hong Kong
D. Mexico, China	Hong Kong, Japan
E. Singapore, Hong Kong	Canada, Mexico

13. Which company was dropped from the 30-company Dow Jones Industrial Average in 2004 but returned in 2005?

- A. Ford
 B. AT&T
 C. Wal-Mart
 D. Microsoft
 E. McDonalds

14. Consider the production possibilities frontiers for Country A and Country B for the production of textiles and boats in one week with the same amount of resources.

	<u>Production Possibilities</u>					
	Country A			Country B		
Textiles	100	0	Textiles	50	0	
Boats	0	100	Boats	0	75	

Which country should export textiles, and what is a reasonable terms of trade?

<u>Exporter of textiles</u>	<u>Terms of trade</u>
A. Country A	4 textiles for 5 boats
B. Country A	5 textiles for 4 boats
C. Country B	4 textiles for 5 boats
D. Country B	5 textiles for 4 boats
E. Country B	5 textiles for 7 boats

15. Which country's attempt to keep its currency pegged to the U.S. dollar was one of the initial causes of the "Asian flu" crisis beginning in of the late 1990s?

- A. Japan
 B. China
 C. Thailand
 D. Singapore
 E. Taiwan