

2007 NATIONAL ECONOMICS CHALLENGE
NCEE/Goldman Sachs Foundation

Round III – International/Current Events
Regional Competition, David Ricardo Division

Please select the one best answer.

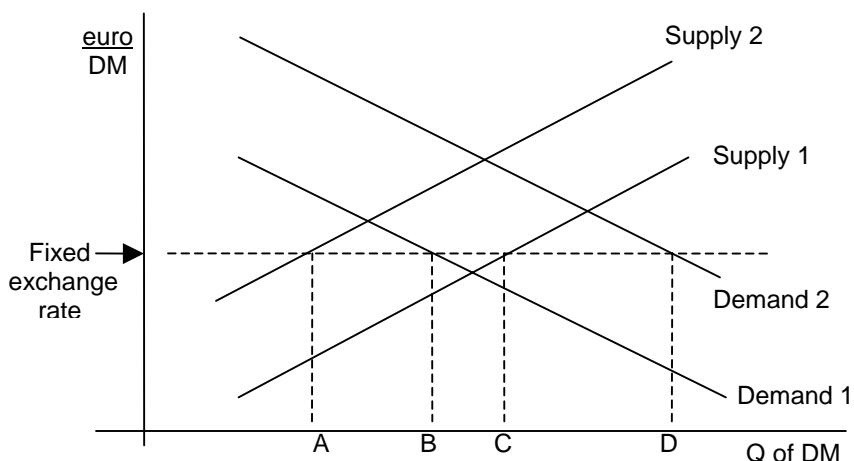
1. Which has been a characteristic of fixed exchange rate systems?
 - A. The value of a currency is fixed to a certain amount of gold.
 - B. The value of a currency is determined by supply and demand.
 - C. If performed correctly, a country's trade balance should equal zero.
 - D. They have freed central banks to respond to fluctuations in the economy.
 - E. There is less certainty regarding how much a foreign financial asset will be worth in the future.

2. In the U.S. balance of payments account for 2006, which had the largest absolute value?
 - A. Exports of goods
 - B. Imports of goods
 - C. Exports of services
 - D. Imports of services
 - E. Balance on current account

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. 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

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. Suppose the prices of goods and services are rising faster in Canada than in the United States. What would the purchasing power parity theory predict?
- The inflation rate will slow in Canada and increase in the United States.
 - The U.S. dollar will appreciate relative to the Canadian dollar.
 - The Canadian dollar will appreciate relative to the U.S. dollar.
 - The central banks of both countries will buy U.S. dollars.
 - The central banks of both countries will buy Canadian dollars.
7. During which U.S. President's tenure was there a substantial and somewhat sustained (three years in a row) Federal budget surplus?
- Jimmy Carter
 - Ronald Reagan
 - George H.W. Bush
 - Bill Clinton
 - George W. Bush

8. Within which range of values was the U.S. capacity utilization rate at the trough of the last U.S. recession?
- 55 to 69%
 - 70 to 74%
 - 75 to 79%
 - 80 to 84%
 - 85 to 89%
9. Which correctly matches the countries with their currencies?
- | | <u>India</u> | <u>Hong Kong</u> | <u>England</u> | <u>Australia</u> |
|----|--------------|------------------|----------------|------------------|
| A. | rupee | dollar | pound | dollar |
| B. | dollar | yuan | euro | dinar |
| C. | pound | won | pound | peso |
| D. | dinar | yuan | euro | dollar |
| E. | yuan | dollar | pound | peso |
10. Recent newspaper stories and cable-news shows have discussed the “subprime” problem. Which best explains the “subprime” problem?
- Some riskier homeowners are defaulting on their mortgages
 - U.S. exchange rates are approaching below optimal levels increasing the U.S. trade deficit
 - Banks are offering their best customers loans at rates below the prime rate of interest
 - The Federal Reserve has lowered interest rates below a level which allows banks to cover lending costs
 - U.S. interest rates could potentially drop below optimal levels relative to trading partners’ interest rates increasing the U.S. trade deficit
11. Which company was dropped from the 30-company Dow Jones Industrial Average in 2004 but returned in 2005?
- Ford
 - AT&T
 - Wal-Mart
 - Microsoft
 - McDonalds
12. 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?
- Japan
 - China
 - Thailand
 - Singapore
 - Taiwan

13. Which is true of the U.S. balance of payments account?
- The current account includes the balance of trade and the capital account includes the balance of services.
 - The current account includes the balance of services and the financial account includes the purchase and sale of foreign assets.
 - 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.
 - 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.
 - 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.
14. Which assures that the exchange rate between the U.S. dollar and the euro will be the same in New York, Tokyo and London?
- fiscal policy
 - arbitrageurs
 - central banks
 - adjustments in price levels
 - adjustments in interest rates
15. 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 |