Past-paper walk-through

Exchange rates ▪ 11.2

eXercise

Questions in this set

- 9708/31 N25 Q27 ▪ 1 mark
- 9708/31 N25 Q28 ▪ 1 mark
- 9708/31 N25 Q30 ▪ 1 mark
- 9708/32 N25 Q25 ▪ 1 mark
- 9708/32 N25 Q27 ▪ 1 mark
- 9708/33 N25 Q20 ▪ 1 mark
- 9708/33 N25 Q25 ▪ 1 mark

Question 27

9708/31 N25 ▪ Q27 ▪ 1 mark

27 What occurs in a monetary union?

A Countries have the same currency.

B Countries use the same fiscal policy.

C Countries have the same domestic rates of sales tax.

D The government budget in each country is balanced.

Solution 27

Answer: **A**

Why

- A monetary union means member countries share a single currency and a single monetary policy.
- So interest rates are set centrally for all of them.
- Fiscal policy and sales tax rates remain national, which is why members can diverge.

Question 28

9708/31 N25 ▪ Q28 ▪ 1 mark

28 What is the main role of the World Bank?

A to ensure that exchange rate systems are working efficiently

B to help countries enter international markets where trade barriers exist

C to offer short-term assistance to countries with balance of payments problems

D to provide low-interest loans to developing countries for infrastructure projects

Solution 28

Answer: **D**

Why

- The World Bank lends for long-term development projects in poorer countries.
- The IMF is the body concerned with exchange rates and short-term balance of payments support.
- The WTO handles trade barriers, so those are not the World Bank's role.

Question 30

9708/31 N25 ▪ Q30 ▪ 1 mark

30 As a member of the European Union, Greece must trade at the same exchange rate, tied to the euro, as stronger economies such as Germany. Greece has a persistent balance of payments deficit.

How would changing to a floating exchange rate help Greece?

A Exchange rates will be less volatile which encourages international investment.

B Its currency should be less open to attacks by international speculators.

C Its currency would be allowed to depreciate which will make its exports more competitive.

D The value of its exports and imports will automatically balance.

Solution 30

Answer: **C**

Why

- Sharing a currency with a stronger economy means Greece cannot devalue to restore competitiveness.
- Its exports stay expensive, so the current account deficit persists.
- The only remaining route is internal devaluation – cutting domestic costs and wages.

Question 25

9708/32 N25 ▪ Q25 ▪ 1 mark

25 What is a trade-weighted exchange rate?

A the price of one currency against a basket of other currencies

B the price of one currency in terms of another

C the price of one currency in terms of its real purchasing power

D the price of one currency being determined by state intervention

Solution 25

Answer: **A**

Why

- A trade-weighted rate averages a currency against several others.
- Each is weighted by how important that trading partner is.
- So it measures the currency against a *basket*, not against a single other currency.

Question 27

9708/32 N25 ▪ Q27 ▪ 1 mark

27 What is a protectionist policy a government may use to reduce the deficit on the balance of payments of the current account?

A revaluation of the exchange rate

B increase in the rate of income tax

C increase in the rate of interest

D introduction of import quotas

Solution 27

Answer: **D**

Why

- Protectionism restricts imports directly.
- So tariffs, quotas, embargoes and subsidies to domestic producers all count.
- Revaluing the exchange rate would make imports *cheaper*, which works the wrong way.

Question 20

9708/33 N25 ▪ Q20 ▪ 1 mark

20 Which macroeconomic policy is most likely to be used as a long-run means of reducing inflationary pressures?

A exchange rate policy

B fiscal policy

C supply-side policy

D monetary policy

Solution 20

Answer: **C**

Why

- Inflation is reduced in the long run by expanding productive capacity.
- Supply-side policy does exactly that, so higher demand no longer bids up prices.
- Monetary and fiscal policy work on demand, which is a shorter-run remedy.

Question 25

9708/33 N25 ▪ Q25 ▪ 1 mark

25 A central bank officially lowers the price of its currency relative to an agreed rate in terms of other currencies.

What type of central bank policy is this?

A appreciation

B depreciation

C devaluation

D revaluation

Solution 25

Answer: **C**

Why

- Lowering the official value of a currency within a fixed or managed system is a devaluation.
- Depreciation is the same movement but under a *floating* rate, driven by the market.
- So a deliberate official reduction is a devaluation.