

6 Balance of payments and exchange rates – Part 1

Name: _____ Class: _____ Date: _____

Vocabulary

Write each word three times.

English	Write it 3 times (English)		
balance of payments	_____	_____	_____
current account	_____	_____	_____
exchange rate	_____	_____	_____
appreciates	_____	_____	_____
depreciates	_____	_____	_____

Recall

Countries trade and exchange currencies:

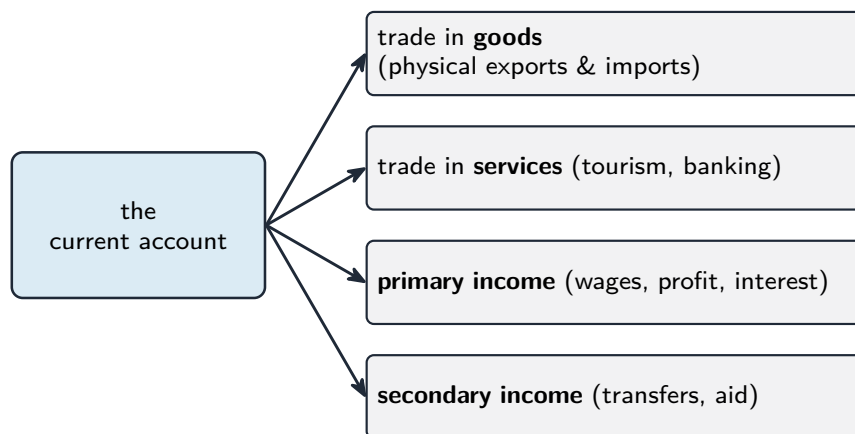
- A country buys imports and sells exports.
- To buy foreign goods you need foreign money.
- Exchange rates change – sometimes a currency is “strong”, sometimes “weak”.

This sheet links up trade balances and exchange rates. Each idea has a worked example.

New ideas

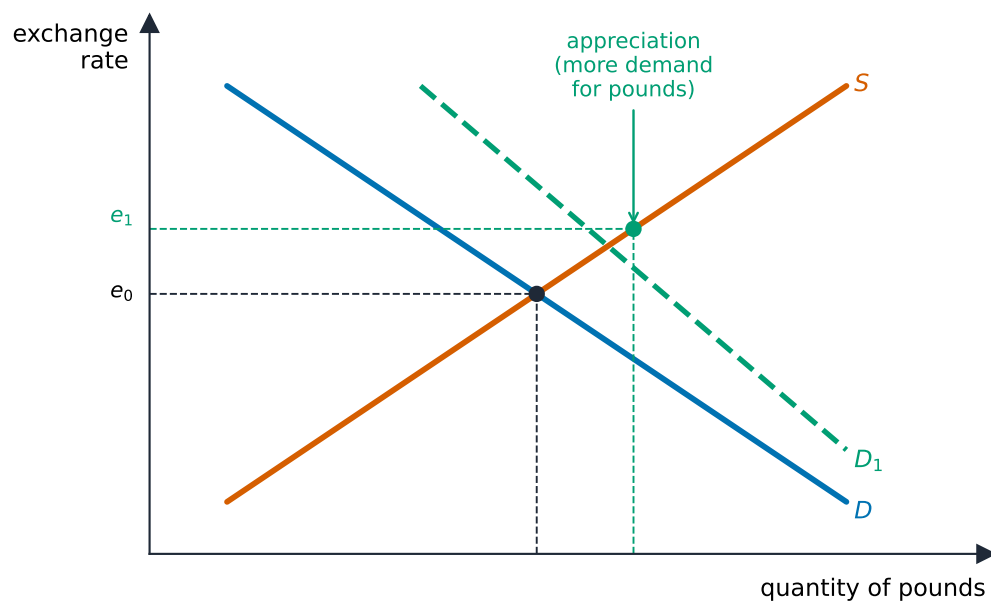
■ 1 The balance of payments

The **balance of payments** records a country's transactions with the rest of the world. Its **current account** tracks trade in goods and services (exports minus imports).



■ 2 Exchange rates

An **exchange rate** is the price of one currency in terms of another. A currency **appreciates** when it gains value and **depreciates** when it loses value.



■ 3 Two sides of one change

Every exchange-rate change has two sides.

Worked example. If $\$1 = \text{€}0.90$, then $\text{€}1 = \frac{1}{0.90} \approx \1.11 . If the dollar then rises to $\$1 = \text{€}1.00$, the dollar has **appreciated** and the euro has **depreciated** – the same event seen from each side.

■ 4 What moves exchange rates

A currency **appreciates** when demand for it rises – for example, higher domestic interest rates attract foreign investment, raising demand for the currency.

Watch out: an appreciation of one currency is always a depreciation of the other. Always track **which** currency you are describing.

Practice

Try these in order. The methods are all above.

2.1 State what the current account records. [2]

2.2 State the difference between a currency appreciating and depreciating. [2]

2.3 If $\$1 = \text{€}0.80$, how many dollars is $\text{€}1$ worth? [2]

2.4 The dollar changes from $\$1 = \text{€}0.80$ to $\$1 = \text{€}0.90$. State whether the dollar has appreciated or depreciated. [2]

2.5 State one reason a currency might appreciate. [1]
