Lecture: 8 Floating Rate, Currency Boards & Currency Basket Systems

Model Questions

1. Identify these pairs by putting the letter of the synonym in the blank provided (Term Means essentially the same as)

   a. appreciation --------
   b. supply of foreign currency --------
   c. law of one price --------
   d. dirty float --------
   e. floating exchange rate --------
   f. devaluation --------
   g. demand for domestic currency --------
   h. pegged exchange rate --------
   i. revaluation --------
   j. fixed exchange rate --------
   k. managed float --------
   l. depreciation --------
   m. purchasing power parity --------
   n. flexible exchange rate --------

2. Under a gold standard, countries should

   a) keep the supply of their domestic money constant.
   b) keep the supply of their domestic money fixed in proportion to their gold holdings.
   c) keep the supply of foreign exchange less than their domestic money supply.
   d) restrict the demand for foreign goods.
   e) outlaw speculation.

3. Under a fixed exchange standard, if the domestic demand for foreign exchange increases

   a) the central monetary authority must meet the demand out of its reserves.
   b) the central monetary authority must increase the supply of domestic money.
   c) the fixed exchange standard will breakdown.
   d) inflation will increase.
   e) the domestic currency must be devalued.
4. The Bretton Woods exchange rate system was an example of a
   a) target zone.
   b) managed float.
   c) pure gold standard.
   d) modified gold standard.
   e) floating exchange rate system

5. Which of the following is NOT one of the determinants of the gains of adopting a single currency?
   a) A well-synchronized business cycle involving all member countries
   b) The possibility of factors of production to freely move across borders
   c) The willingness and ability of member countries to design policies to address regional imbalances that may develop
   d) Widening the common market by allowing other countries to join
   e) None of the above.

6. The biggest disadvantage of a fixed exchange rate is the
   a) increased probability of high inflation.
   b) tradeoff between supporting the exchange rate and adjusting the trade balance.
   c) tradeoff between supporting the exchange rate and maintaining full employment.
   d) increased probability of a trade deficit.
   e) tradeoff between supporting the exchange rate and maintaining a balanced budget.

7. Write, in brief, pros & cons of fixed and completely flexible exchange rate regimes.

8. How the Managed Floating exchange rate regime overcome the difficulties of completely flexible exchange rate regime.

9. Discuss the advantages and disadvantages of Currency Boards System?

10. How can a Currency Basket Exchange rate regime be created? What are the advantages of currency basket regime over the flexible exchange rate regime?

11. Briefly outlines the historical developments of exchange rate regime in case of India.