

INTERNATIONAL ECONOMICS

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Exchange Rate Concepts and Types (Nominal, Real, Effective, NEER, REER)

1. The nominal exchange rate refers to:
 - A) The exchange rate adjusted for inflation
 - B) The current market price of one currency in terms of another
 - C) The exchange rate fixed by the government
 - D) The rate determined by trade balance

Answer: B

2. The real exchange rate is calculated by adjusting the nominal rate for:
 - A) Interest rate differentials
 - B) Inflation differentials between countries
 - C) Tariff differences
 - D) Fiscal policy

Answer: B

3. If domestic inflation rises relative to foreign inflation, the real exchange rate will:

- A) Appreciate
- B) Depreciate
- C) Remain constant
- D) Become unstable

Answer: B

4. The effective exchange rate measures:

- A) The average nominal exchange rate of a country against a basket of currencies
- B) The exchange rate against a single dominant currency
- C) Domestic purchasing power
- D) The long-term inflation rate

Answer: A

5. NEER stands for:

- A) Nominal Effective Exchange Rate
- B) Net Effective Exchange Rate
- C) National Exchange Efficiency Ratio
- D) Normal Equilibrium Exchange Rate

Answer: A

6. A rise in NEER indicates:

- A) Appreciation of domestic currency
- B) Depreciation of domestic currency
- C) A rise in inflation
- D) No change in purchasing power

Answer: A

7. REER stands for:

- A) Real Export Exchange Rate
- B) Real Effective Exchange Rate
- C) Revised Exchange Equalization Rate
- D) Relative Exchange Efficiency Ratio

Answer: B

8. A higher REER usually implies that domestic goods have become:

- A) More competitive
- B) Less competitive
- C) Cheaper abroad
- D) More in demand

Answer: B

9. When REER increases, it means the domestic currency has:

- A) Depreciated in real terms
- B) Appreciated in real terms
- C) Remained constant
- D) Lost global relevance

Answer: B

10. If NEER is constant but REER increases, this suggests:

- A) Domestic inflation exceeds foreign inflation
- B) Foreign inflation exceeds domestic inflation
- C) Both are equal
- D) Exchange rate policy is neutral

Answer: A

Fixed Exchange Rate System

11. In a fixed exchange rate system, the value of a currency is:

- A) Determined solely by market forces
- B) Constantly changing
- C) Pegged to another currency or basket of currencies
- D) Linked to gold standard only

Answer: C

12. Under fixed exchange rates, the central bank must:

- A) Do nothing
- B) Intervene to maintain the peg
- C) Allow appreciation freely
- D) Allow depreciation freely

Answer: B

13. The main merit of fixed exchange rates is:

- A) Exchange rate volatility
- B) Stability in international payments
- C) Promotes speculative trading
- D) Causes inflation

Answer: B

14. A devaluation refers to:

- A) Increase in value of domestic currency in a fixed system
- B) Reduction in value of domestic currency in a fixed system
- C) Market-driven depreciation
- D) Appreciation in floating rates

Answer: B

15. Fixed exchange rates promote:

- A) Predictability in trade
- B) Domestic price instability
- C) Arbitrary currency fluctuations
- D) High inflation rates

Answer: A

16. A major demerit of fixed exchange rates is:

- A) Encourages exports
- B) Limits monetary policy flexibility
- C) Reduces international confidence
- D) Leads to stable balance of payments

Answer: B

17. To defend a fixed exchange rate, a country may:

- A) Buy or sell foreign currency reserves
- B) Increase tariffs
- C) Decrease exports
- D) Ban imports

Answer: A

18. The Bretton Woods system operated on:

- A) Flexible exchange rates
- B) Gold standard with fixed parities
- C) Managed floating
- D) Free market determination

Answer: B

19. Under the gold exchange standard, currencies were pegged to:

- A) Silver
- B) Dollar or gold
- C) Basket of commodities
- D) Real exchange rate

Answer: B

20. Fixed exchange rates are also known as:

- A) Pegged rates
- B) Floating rates
- C) Flexible rates
- D) Market rates

Answer: A

Flexible (Floating) Exchange Rate System

21. In a flexible exchange rate system, the rate is determined by:

- A) Government policy
- B) Central bank interventions
- C) Market demand and supply of foreign currency
- D) Gold reserves

Answer: C

22. One major advantage of flexible exchange rates is:

- A) Reduced speculation
- B) Automatic balance of payments adjustment
- C) Fixed inflation rate
- D) No trade fluctuations

Answer: B

23. A depreciation of local currency leads to:

- A) Reduction of exports
- B) Increase in imports
- C) Encouragement of exports
- D) None of the above

Answer: C

24. Flexible exchange rates allow countries to:

- A) Retain independent monetary policies
- B) Lose control over inflation
- C) Fix interest rates permanently
- D) Keep stable parity always

Answer: A

25. A key disadvantage of floating exchange rates is:

- A) Volatility
- B) Trade stability
- C) Elimination of speculation
- D) Automatic equilibrium

Answer: A

26. Under flexible rates, speculation tends to:

- A) Eliminate fluctuations
- B) Cause frequent fluctuations
- C) Reduce liquidity
- D) Fix the rate

Answer: B

27. Flexible exchange rates are preferred when:

- A) The economy faces constant shocks
- B) Inflation is fixed
- C) Central bank cannot intervene
- D) Exports are insignificant

Answer: A

28. Floating rates can lead to:

- A) Exchange rate predictability
- B) Exchange rate uncertainty
- C) Elimination of deficits
- D) Fixed inflation

Answer: B

29. Managed floating exchange rate means:

- A) No intervention at all
- B) Periodic intervention by monetary authority
- C) Fixed parity
- D) Gold-based valuation

Answer: B

30. The foreign exchange market determines exchange rates in a:

- A) Fixed regime
- B) Flexible regime
- C) Pegged regime
- D) Regulated system only

Answer: B

Relative Merits and Demerits

31. Fixed rates ensure:

- A) Monetary independence
- B) Exchange rate stability
- C) High exchange volatility
- D) Free capital flows

Answer: B

32. Flexible rates ensure:

- A) Price stability
- B) Automatic adjustment to external shocks
- C) Rigid controls
- D) Balance-of-payments imbalances

Answer: B

33. Under fixed rates, speculative attacks are:

- A) Unlikely
- B) Common during disequilibrium
- C) Nonexistent
- D) Easy to manage

Answer: B

34. Inflation control is easier under:

- A) Fixed rate
- B) Flexible rate
- C) Gold standard
- D) Dual system

Answer: A

35. The Mundell-Fleming model suggests that under fixed rates, monetary policy is:

- A) Fully effective
- B) Ineffective
- C) Neutral
- D) Inflationary

Answer: B

36. Under flexible rates, fiscal policy effectiveness is:

- A) Higher
- B) Lower
- C) Unchanged
- D) Irrelevant

Answer: A

37. In a fixed regime, balance of payments disequilibrium is corrected by:

- A) Currency adjustments
- B) Reserve movements
- C) Price movements
- D) Tariff adjustments

Answer: B

38. Flexible exchange rates act as:

- A) Shock absorbers
- B) Policy constraints
- C) Fixed anchors
- D) Monetary rigidities

Answer: A

39. A country aiming for external stability prefers:

- A) Fixed rate
- B) Floating rate
- C) Hybrid system
- D) Inflation targeting

Answer: A

40. Volatility in flexible rates can discourage:

- A) Trade and investment
- B) Policy reforms
- C) Domestic production
- D) Inflation control

Answer: A

Hybrid or Intermediate Systems

41. A hybrid exchange rate combines elements of:

- A) Gold and silver standard
- B) Fixed and flexible systems
- C) Fiscal and monetary policy
- D) Controlled and unregulated markets

Answer: B

42. Managed floating is also known as:

- A) Dirty float
- B) Soft peg
- C) Crawling peg
- D) None of these

Answer: A

43. A crawling peg system involves:

- A) Fixed parity for long term
- B) Gradual, continuous adjustments
- C) No correction mechanism
- D) Random fluctuations

Answer: B

44. The adjustable peg system allows:

- A) Free market determination
- B) Periodic changes in fixed rate
- C) No central bank involvement
- D) Fixed gold parity only

Answer: B

45. Hybrid exchange rates seek to achieve:

- A) Both stability and flexibility
- B) Only currency speculation
- C) Complete control of trade
- D) Elimination of reserves

Answer: A

46. In a managed float, central banks:

- A) Never intervene
- B) Intervene occasionally to guide the rate
- C) Fix the rate permanently
- D) Set gold parity

Answer: B

47. The Exchange Rate Mechanism (ERM) of the EU was an example of:

- A) Pure floating system
- B) Fixed peg
- C) Hybrid exchange rate system
- D) Commodity-based system

Answer: C

48. In a currency board system, the domestic money supply is:

- A) Unrelated to reserves
- B) Fully backed by foreign currency
- C) Randomly adjusted
- D) Controlled by inflation rate

Answer: B

49. A band or target zone arrangement means:

- A) Currency can fluctuate within narrow limits
- B) Exchange rate is fully fixed
- C) Exchange rate is market-determined only
- D) No intervention is allowed

Answer: A

50. Hybrid systems are favored by developing economies because they:

- A) Provide both flexibility and stability
- B) Eliminate trade cycles
- C) Restrict monetary freedom
- D) Follow gold price determination

Answer: A

THANK YOU