Fiscal & Financial System in Japan A / International Finance

Fall 2012

Final Exam

13:30 - 14:30 Dec 18, 2012

- This is a closed book exam.
- Please write clearly. Poor handwriting will be ignored.
- You can withdraw anytime during the exam provided that you are sure you finished the exam. No class after exam.
- For answers and comments on the exam, visit my website: `http://www1.meijigakuin.ac.jp/~iwamura/`

Multiple-Choice Questions(5 points for each question)

1. If people throughout the world like to use a country ' s currency for international transactions, and view the issuing country as relatively stable so assets denominated in its currency are viewed as especially desirable, then that country will tend to experience:
   (a) balance of trade surpluses and capital account deficits.
   (b) relatively high rates of inflation and unemployment.
   (c) balance of trade deficits and capital account surpluses.
   (d) surpluses in the budget of its national government.

2. Which one of the following statements is the most accurate?
   (a) a decrease in the money supply lowers the interest rate, while an increase in the money supply raises the interest rate, given the price level and output.
   (b) an increase in the money supply lowers the interest rate, while a fall in the money supply raises the interest rate, given the price level.
   (c) an increase in the money supply lowers the interest rate, while a fall in the money supply raises the interest rate, given the output level.
   (d) an increase in the money supply lowers the interest rate, while a fall in the money supply raises the interest rate, given the price level and output.
   (e) None of the above.

3. Which of the following statements is the most accurate?

   (a) Given the price level, when the Japan's nominal money stock rises, the yen interest rate declines and the yen appreciates against the dollar.

   (b) Given the GDP, when the Japan's nominal money stock rises, the yen interest rate declines and the yen appreciates agains the dollar.

   (c) Given the price level and GDP, when the Japan's nominal money stock decreases, the yen interest rate declines and the yen depreciates against the dollar.

   (d) Given the price level and GDP, when the Japan's nominal money stock rises, the yen interest rate declines and the yen appreciates against the dollar.

   (e) Given the price level and GDP, when the Japan's nominal money stock rises, the yen interest rate declines and the yen depreciates against the dollar.

4. Given the Japan's price level and GDP,

   (a) an increase in the Japan's nominal money stock causes the yen to appreciate against the dollar, but it does not disturb the US money market equilibrium.

   (b) an increase in the Japan's nominal money stock causes the yen to depreciate against the dollar, and it creates the excess supply of the dollar in the US money market equilibrium.

   (c) an increase in the Japan's nominal money stock causes the yen to depreciate against the dollar, and it creates the excess demand of the dollar in the US money market equilibrium.

   (d) an increase in the Japan's nominal money stock causes the yen to depreciate against the dollar, but it does not disturb the US money market equilibrium.

   (e) None of the above statements is true.

5. Which of the following statements is most accurate?

   (a) In general, consumption demand rises by less than disposable income.

   (b) In general, consumption demand rises by more than disposable income.

   (c) In general, consumption demand rises by the same amount as disposable income rises.

6. In the short run, a rise in the exchange rate, i.e. currency depreciation,

   (a) raises aggregate demand and raises output

   (b) raises aggregate demand and lowers output

   (c) raises aggregated demand and does not affect output

   (d) lowers aggregate demand and raises output

   (e) lowers aggregate demand and lowers output

7. Using the DD-AA framework, which one of the following statements is the most accurate?

   (a) Only monetary policy can raise the equilibrium GDP in the short run.
   (b) Only fiscal policy can raise the equilibrium GDP in the short run.
   (c) Only both monetary and fiscal policies can raise the equilibrium GDP in the short run.
   (d) Neither policy is capable of raising the equilibrium GDP in the short run.
   (e) Monetary policy by itself or fiscal policy by itself can raise the equilibrium GDP in the short run.

8. In the short run, a temporary increase in the nominal stock of money

   (a) shifts the AA curve to the right, increases output and depreciates the currency.
   (b) shifts the AA curve to the left, increases output and depreciates the currency.
   (c) shifts the AA curve to the left, decreases output and depreciates the currency.
   (d) shifts the AA curve to the left, increases output and appreciates the currency.
   (e) shifts the AA curve to the right, increases output and appreciates the currency.

9. When output falls and the currency appreciates, which of the following is the most likely cause behind?

   (a) A rise in the dollar interest rate
   (b) A fall in the US GDP
   (c) A fall in investment demand
   (d) A fall in the nominal money stock
   (e) A depreciation in the expected future yen

10. Which of the following are true in terms of the trade balance?

   (a) Monetary expansion increases the trade balance.
   (b) Monetary expansion decreases the trade balance.
   (c) Fiscal expansion increases the trade balance.
   (d) Fiscal expansion decreases the trade balance.
   (e) Both A and D.

Essay Questions

1. Suppose that you borrow 100,000 yen for 5 years and repay it by making the *same yearly payment* every year until the maturity.

   (a) Set up an equation that calculates the interest rate of this *fixed-payment loan*, denoting the interest rate and the yearly payment by i and C respectively. (5 points)

   (b) Given the interest rate of the loan, the equation determines the amount of yearly payment C. Now suppose that another fixed-payment loan *with the same interest rate but a maturity of 10 years* is offered. Denoting the yearly payment by C', verify that the total payment of the 10-year loan is larger than that of the 5-year loan, though $C' < C$. (10 points)

2. Explain how the AA schedule is derived. (15 points)

3. Using the DD-AA framework, answer the follwing questions.

   (a) Explain how an increase in government demand affects the country's equilibrium GDP and exchange rate. (10 points)

   (b) Explain how the interest rate and the current account are affected. (10 points)