

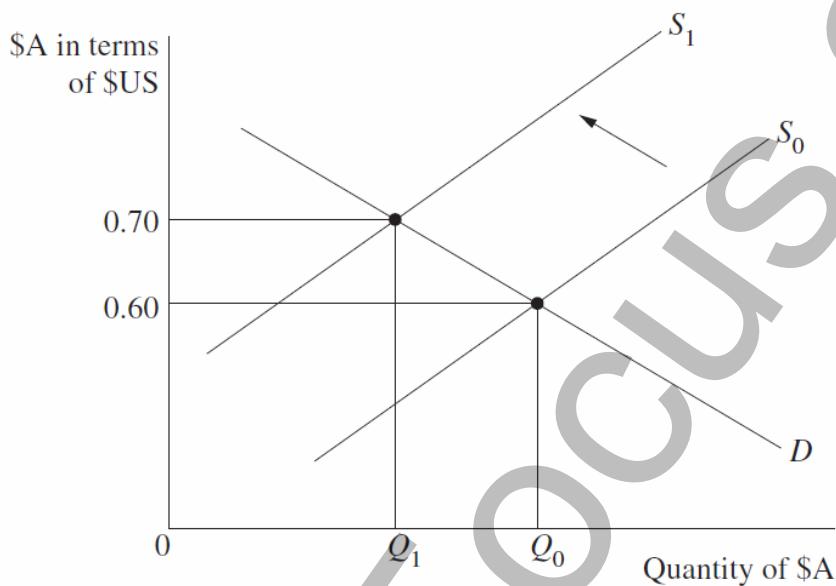
## Exchange rates – Past HSC questions 2011-2007

### ***Marking guide and notes from marking centre included***

**6** Which of the following combinations is most likely to reduce Australia's export volumes?

- (A) The Australian dollar depreciates and there is a recession in the US economy.
- (B) The Australian dollar appreciates and there is a recession in the US economy.
- (C) The Australian dollar depreciates and there is an expansion in the US economy.
- (D) The Australian dollar appreciates and there is an expansion in the US economy.

**10** The graph shows the demand for and supply of Australian dollars.



Which of the following is the most likely reason for the shift in the supply curve from S<sub>0</sub> to S<sub>1</sub>?

- (A) An increase in foreign imports into Australia
- (B) An increase in foreign financial investment in Australia
- (C) A reduction in the net income deficit on the current account
- (D) A decline in the international competitiveness of Australian firms

**11** What is the most likely impact of a rise in the level of Australia's interest rates relative to overseas interest rates?

- (A) An increase in foreign investment in Australia and a depreciation of the \$A
- (B) An increase in foreign investment in Australia and an appreciation of the \$A
- (C) A decrease in foreign investment in Australia and a depreciation of the \$A
- (D) A decrease in foreign investment in Australia and an appreciation of the \$A

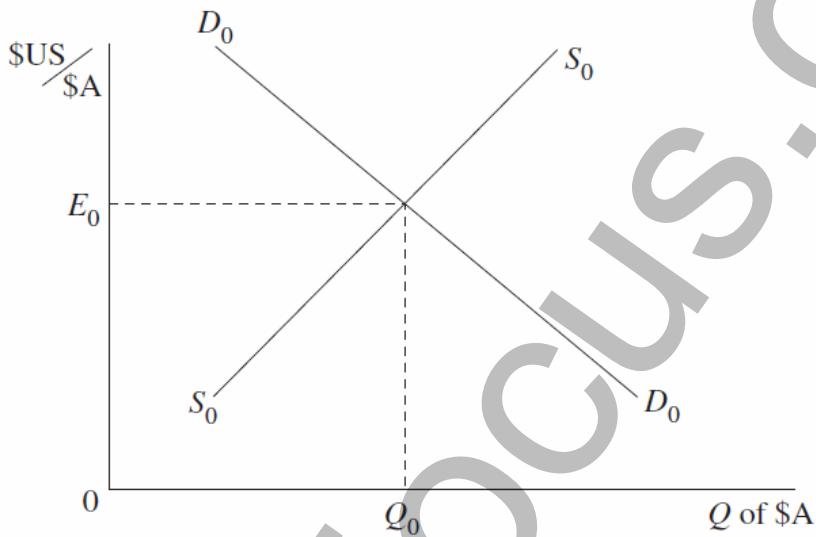
16 Which scenario best demonstrates the benefits of a fixed exchange rate system?

- (A) A country experiencing a recession fixes its currency to that of a country in which interest rates are low.
- (B) A country experiencing a boom fixes its currency to that of a country experiencing a recession.
- (C) A country experiencing a recession fixes its exchange rate above the equilibrium rate.
- (D) A country experiencing a boom fixes its exchange rate below the equilibrium rate.

**Question 24** (10 marks)

(a) The graph shows the market for \$A in terms of \$US.

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The market is initially in equilibrium at an exchange rate  $E_0$  and a quantity of \$A at  $Q_0$ .

On the diagram, draw the new equilibrium which results if there is a reduced demand for foreign assets by Australian investors. Label the new equilibrium exchange rate and quantity,  $E_1$  and  $Q_1$ .

**Question 24 (continued)**

(b) The table shows the value of Australia's currency against Country A and Country B, under a floating exchange rate. 3

Year	Country A Currency units/\$A	Country B Currency units/\$A
1	0.90	0.70
2	0.80	0.75
3	0.70	0.80

Briefly explain the trends in Australia's exchange rate with Country A and Country B.

**Question 24 (b)**

Criteria	Marks
<ul style="list-style-type: none"> <li>Clearly and concisely provides a possible reason/s for the trends in Australia's exchange rate with Country A and Country B</li> </ul>	3
<ul style="list-style-type: none"> <li>Sketches in general terms a possible reason for the trends in Australia's exchange rate with Country A and Country B</li> </ul>	
<p>OR</p> <ul style="list-style-type: none"> <li>Clearly and concisely provides a possible reason for the trends in Australia's exchange rate with EITHER Country A or Country B</li> </ul>	2
<ul style="list-style-type: none"> <li>Correctly identifies the trend in Australia's exchange rate with Country A and Country B</li> </ul>	1

### Question 24

a. In better responses, candidates clearly drew a shift of the supply curve to the left, indicating a decrease in the supply of the Australian dollar and clearly plotted points E1Q1 on the diagram provided.

In weaker responses, however, candidates either did not correctly draw the new supply curve with the new equilibrium point, inaccurately plotted price and quantity P1 and Q1, resorted to various random guesses with the supply and demand curves, or did not attempt to answer this question at all.

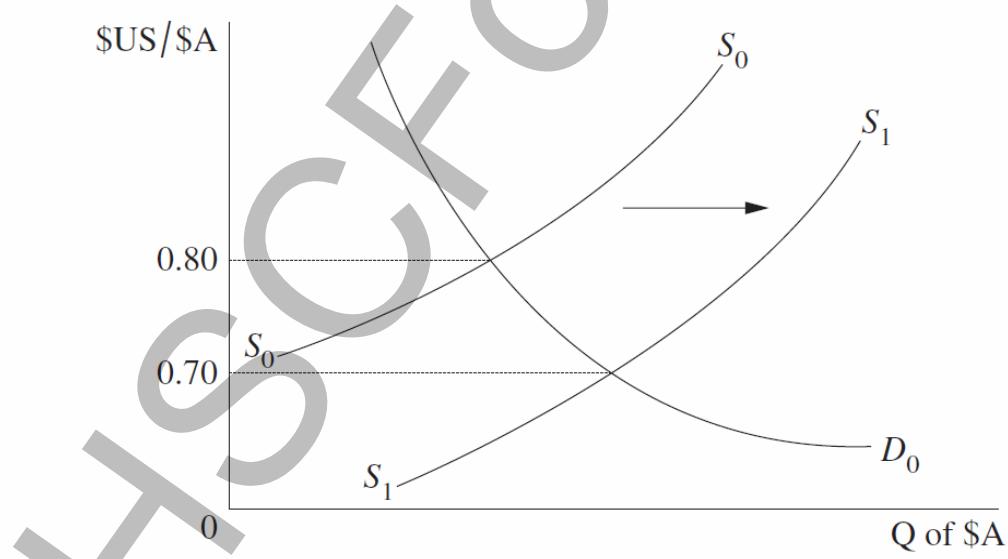
b. In better responses, candidates demonstrated a clear understanding of the trends and were able to briefly and concisely explain possible reasons for these and for Australia's exchange rate. These reasons included such things as foreign investment levels, protection levels, global financial crisis (GFC), exports and imports, and so on. They clearly articulated their responses by using appropriate terminology to communicate in a sophisticated manner the processes involved in the appreciation and depreciation of exchange rates.

In weaker responses, however, candidates only identified the trends and were confused in terms of reading/interpreting the stimulus material provided. Moreover, in these responses, candidates neglected to explain what could possibly be behind these trends and, as a result, presented fairly elementary and/or sketchy answers.

11 What is the most likely impact of an appreciation of the Australian dollar?

- (A) Lower import prices and an increase in net foreign debt
- (B) Higher export prices and a deterioration of the terms of trade
- (C) An improvement in the current account deficit and an increase in inflation
- (D) A decrease in capital inflows and a decline in international competitiveness

17 The graph shows the demand and supply for Australian dollars (\$A).



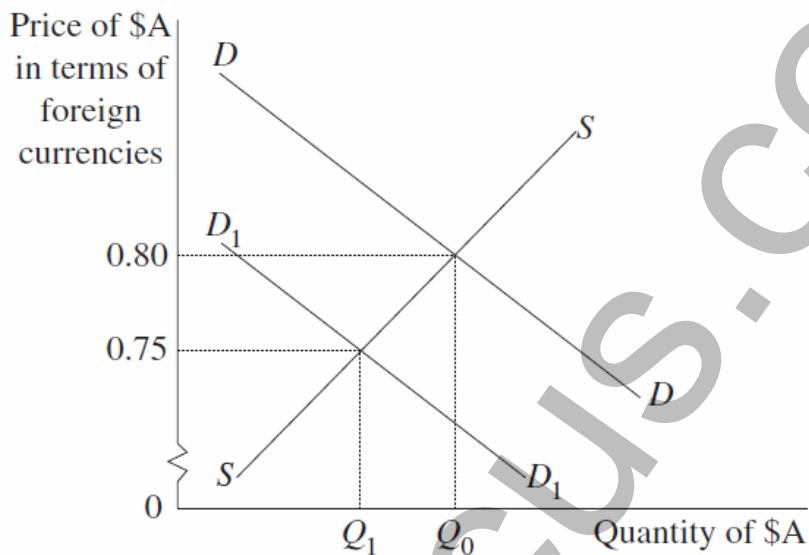
Which of the following would cause the supply curve to shift from  $S_0$  to  $S_1$ ?

- (A) Increased demand for foreign assets by Australians
- (B) Decreased demand for foreign imports by Australians
- (C) Decreased demand for Australian assets by foreigners
- (D) Increased demand for Australian exports by foreigners

10 Which of the following may cause an appreciation of the Australian dollar?

- (A) Australia's interest rates increase relative to overseas interest rates.
- (B) Australian investors purchase a foreign owned firm.
- (C) World commodity prices decrease.
- (D) Imports into Australia increase.

11 The diagram shows the demand for and supply of Australian dollars.



Other things being equal, what would be the effects of a movement of the demand curve for Australian dollars from  $DD$  to  $D_1D_1$ ?

- (A) Australia's international competitiveness would decrease and capital inflow would be encouraged as domestic assets are less expensive.
- (B) Australia's international competitiveness would decrease and capital outflow would be encouraged as domestic assets are more expensive.
- (C) Australia's international competitiveness would increase and capital inflow would be encouraged as domestic assets are less expensive.
- (D) Australia's international competitiveness would increase and capital outflow would be encouraged as domestic assets are more expensive.

16 If a major trading partner of Australia experienced a significant appreciation of its currency, what would be the likely effect in Australia?

- (A) International competitiveness with this country would decline.
- (B) Imported inflation from this country would decline.
- (C) Imports from this country would be less expensive.
- (D) Terms of trade with this country would decline.