1. Balance of payments (BOP) accounts provide us with a variety of measures of international activity.

   a. BOP accounts are maintained according to the rules of double entry bookkeeping; all transactions are recorded as debits or credits. What is the general rule for determining whether a transaction is a debit or credit in a country’s BOP? Provide examples of debit transactions for the current account, financial account, and international reserves sections of the balance of payments. (Note: you do not need to identify currency amounts, simply indicate a type of transaction that provides the appropriate example.)

   b. What does the current account balance (CAB) measure? If a country has a current account deficit, what does that mean for that country?

   c. Assuming that net exports are approximately equal to the CAB, use GNP accounting formulae to show the relationship between the CAB and national savings and investment. Given this formula, demonstrate how movements in either or both of these variables could lead to a CAB deficit.

   d. What does the official settlements balance (OSB) (or overall balance) measure? If a country has an OSB surplus, what does that mean for that country?

2. Consider the information presented below (all values are in US$):

<table>
<thead>
<tr>
<th>Country</th>
<th>Spot Exchange Rate</th>
<th>30 day Forward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>.50</td>
<td>.49</td>
</tr>
<tr>
<td>Canada</td>
<td>.75</td>
<td>.76</td>
</tr>
</tbody>
</table>

   a. Let $B$ denote the spot exchange rate and $B_f$ denote the 1 month forward rate. Derive the formula that shows how $B_f$ is determined in the foreign exchange market and how its value is related to $B$. Under what conditions in the real world is this formula most likely to hold true?

   b. Based on the information provided above, where (among the United States, Australia or Canada) are one month interest rates the highest? Lowest?

   c. Suppose that uncovered interest rate parity holds. What is the formula for this condition? Use the formula to determine market beliefs about the future behavior of the Australian dollar and the Canadian dollar. Under what conditions in the real world is this formula most likely to hold?

   d. Given the information, what is the Australian dollar price of 1 Canadian dollar?

3. Compare and contrast the operation of the classic gold standard with that of the Bretton Woods system. What elements of the former were responsible for its relatively better performance as an international monetary standard? Discuss how the rules and operation of the Bretton Woods system evolved over time in response to perceived problems with its performance.

5. How are the economic policies of one country transmitted internationally? Under what conditions does this transmission suggest a need for international policy coordination? Do countries engage in such coordination? What is the evidence on the success of coordination?

6. Write an essay on purchasing power parity (PPP). Your essay should include a discussion of the various versions of the theory; the role PPP plays in theories of exchange rate behavior; empirical evidence on PPP; and the relationship between PPP and measures of the real exchange rate.

7. Compare and contrast the long run and short run effects of contractionary monetary policy under fixed vs. flexible exchange rates. OR Compare and contrast the long run and short run effects of expansionary fiscal policy under fixed vs. flexible exchange rates. In either case, be sure to discuss the role that the degree of international capital mobility plays in your answer.

8. Beginning from its basics, develop an algebraic formula for the monetary approach to exchange rates. Use this model to predict the impact of each of the following events on a country’s exchange rate:
   a. a rise in the foreign interest rate, \( i^* \)
   b. a fall in home output, \( Y \)
   c. a fall in the domestic money supply, \( M^s \)
   Explain in a sentence or two why the model predicts these changes (i.e. what are the economic forces leading to these changes?).

9. Suppose that a Big Mac costs $2.50 in New York and SF 15 in Zurich. Suppose further that the spot exchange rate on that day is SF 5 = $1. Calculate the purchasing power parity exchange rate between the Swiss franc and the dollar. Based on your calculation is the SF overvalued or undervalued? Explain. Suppose now that a Big Mac costs £1.25 in London while the spot exchange rate is £.40 = $1. Is the pound overvalued or undervalued? Explain. Is the Big Mac a good basis for PPP calculations? Why or why not?

10. Write an essay on the present international monetary system. Identify the major institutions and discuss their roles in this system. Describe the major strong points of the current system. What are its weaknesses? Provide a short description of two proposals for reform of the system.