

Economics

Section II

40 marks

Attempt Questions 21–24

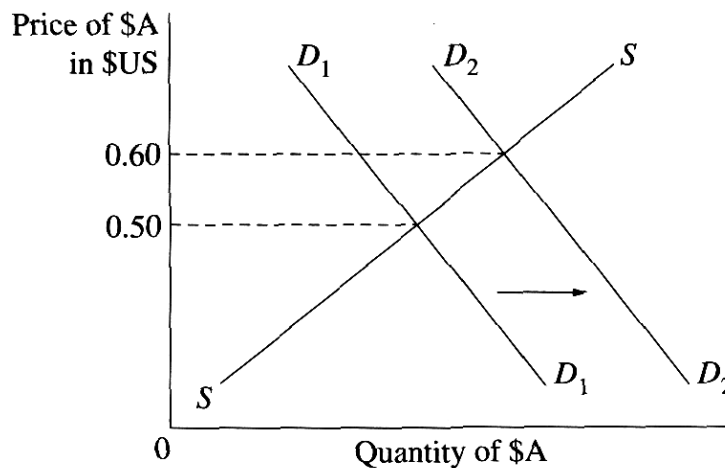
Allow about 1 hour and 15 minutes for this section

Answer the questions in the spaces provided.

Marks

Question 21 (10 marks)

The diagram shows information about the demand and supply of Australian dollars (\$) in terms of United States dollars (\$US). Both countries have flexible exchange rates.



- (a) State the economic term given to the movement of the exchange rate of the \$A from \$US0.50 to \$US0.60. 1

.....Appreciation.....

- (b) Outline TWO causes of an increase in demand for \$A. 2

.....One cause for an increase in the demand for Australian dollar could be an increase in the demand for exports by foreigners. The other cause could be the increase in foreign investment of foreigners into Australia.....

Question 21 continues on page 10

Question 21 (continued)

- (c) Briefly explain how the Reserve Bank could intervene in the foreign exchange market to influence the exchange rate of the \$A. 3

The reserve Bank through its actions of domestic market operations can influence the exchange rate of the Australian Dollar. Through increasing interest rates by the ~~put~~ selling of government securities it encourages overseas savings to enter the market increasing demand of \$A and raising the \$A. Conversely the RBA may purchase G.S.'s and reduce the interest rate will have the opposite effect and reduce demand for overseas savings causing a capital outflow.

- (d) Discuss TWO economic benefits to Australia of an appreciation of the \$A. 4

One economic benefit of an increase in the value of the Australian dollar is that our income from exports will increase as the goods cost more for overseas companies to purchase, leading to increased revenue which will ~~improve our balance of trade~~ and reduce the CAD.

Another economic benefit of an increase in the value of the Australian dollar is that it will lead to greater economic growth as increases in the value of the Australian currency indicate to market speculators that the economy is growing causing and increase in the purchase of \$A.

End of Question 21