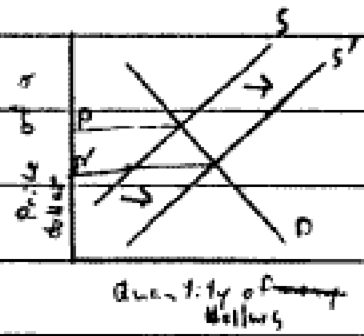
2MAC CC

Write in the box the number of the question you are answering on this page as it is designated in the examination.

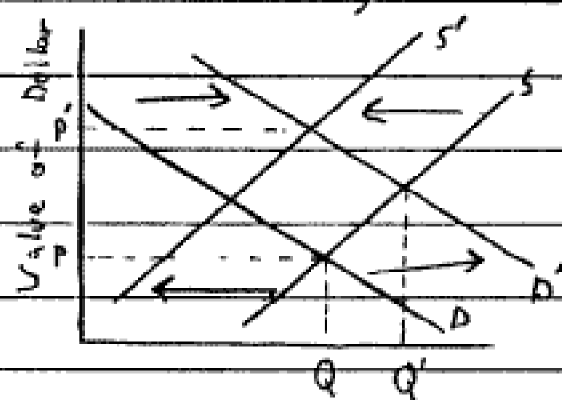
Question 2

2a) i) An increase in U.S. demand for French good will cause Americans to purchase francs with dollars. American purchases of francs will flood the international market with dollars, which is an increase in supply.

ii) The increased suply of dollars will cause the supply curve to shift from S to S′ and the price of a dollar to fall from P to P′.



b) i) An increase in real US interest rates will cause French investors to desire US dollars and the demand curve for dollars to shift right. ~~Against a constant~~ At the same time U.S. investors will be purchasing securities and the supply of dollars will be reduced (shift left) The graph illustrates how price will increase from P to P′ as demand shifts from D to D′ and supply from S to S′.



ii) As a direct result of the increase in rates dollars available in the market will increase from Q to Q′ (see graph with part i) but the final quanity of dollars, is unpredictable.