Practice problems

1. Explain what a Reserve Currency Standard is and describe some of its characteristics in the context of the Bretton Woods system.

2. Explain the concept of “original sin” as developed by Barry Eichengreen and Ricardo Hausmann.

3. On April 5th, 2011 this statement was written in the Economist:

“If you’re a country competing with Chinese exporters, you don’t much care whether Chinese manufacturing wages are rising or the currency is appreciating; both make production in your country look more attractive.”

Explain this paragraph using terms, such as nominal exchange rates, inflation, real exchange rate and making the necessary connections among them.

4. On April 7th, 2011 the Economist reported that

“Usually emerging markets welcome foreign capital....But the recent surge has them worried, partly because of its speed and fears of an equally rapid reversal. The IMF reckons that gross inflows have risen to 6% of emerging-world GDP in about a quarter of the time taken for a similar spike before the crisis. Policymakers also fear that this flood of capital could lead to asset-price bubbles and overvalued currencies. Many have implemented measures to stem the tide, from Brazil’s tax on portfolio inflows to Peru’s higher charge on non-residents’ purchases of central-bank paper”...

   i. Explain why “usually emerging markets welcome foreign capital”
   ii. Why are Brazil and Peru imposing capital controls? Are capital controls usually endorsed by the IMF policies?

5. Explain why one of the arguments pro floating exchange rates is that they act as automatic stabilizers
6. You are an economic advisor to the government of China in 2008. The country has a current account surplus and is facing inflationary pressures.

i. Show the location of the Chinese economy on II-XX diagram

ii. What would be your advice on how the authorities should move the yuan’s exchange rate?

7. Explain why default crises in developing countries are likely to be accompanied by balance of payments crises and bank runs.

8. Choose a country from South America and explain what reforms were pursued and what happened with its economy after the 1980s “debt crisis”.

9. What would be some of the lessons drawn from the developing country crises of 80s and 90s?