

SIMON FRASER UNIVERSITY
Department of Economics

Econ 345
International Finance

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PROBLEM SET 2
(Due November 19)

The following questions are short answer. 25 points each.

1. Recent US monetary policy has been the subject of a lot of criticism in other countries. For example, Brazil, which has a relatively flexible exchange rate against the US dollar, has complained, and so has China, which has a fixed exchange rate.

Use the DD-AA model to compare and contrast the effects of recent US monetary expansion on China and Brazil. Why are they upset? How do the effects differ in the two countries? What could they do in response?

2. Now that Obama has been re-elected, all eyes are on the so-called ‘fiscal cliff’, which represents an automatic US fiscal contraction (ie, higher taxes, lower spending) which will take place in January unless Congress acts.

Use the DD-AA model to compare and contrast how a US fiscal contraction will affect Canada and China (remember, China has a fixed exchange rate to the dollar, while Canada floats).