SIMON FRASER UNIVERSITY
Department of Economics

Econ 305 — Prof. Kasa
Intermediate Macroeconomic Theory — Fall 2015

PROBLEM SET 4
(Due December 3)

1. (25 points). Some people argue that China should let its exchange rate float more freely against the US dollar. Others argue that the peg has served China well, and it would be mistake to let the RMB float. Use the Keynesian Mundell-Fleming model discussed in class to evaluate the pros and cons of allowing greater exchange rate flexibility. Under what conditions would greater exchange rate flexibility be good for China, and under what conditions would it be bad. Use graphs to illustrate your answer.

2. (25 points). Many people are currently wondering when the USA will raise its short-term interest rate. Use the Keynesian Mundell-Fleming model to predict the consequences for Canada of an increase in US interest rates. Use graphs to illustrate your answer. Will it be good or bad for Canada? Why? (Remember, Canada has a flexible exchange rate with the USA).