

SIMON FRASER UNIVERSITY
Department of Economics

Econ 345
International Finance

Prof. Kasa
Spring 2016

PROBLEM SET 2 - Due March 17

1. (25 points). In the previous problem set you read an article describing the recent loss of foreign exchange reserves in China. Use the DD-AA model to explain why anticipations of higher US interest rates might have contributed to this. How will this loss of foreign exchange reserves affect Chinese output and employment? Why might China want to 'sterilize' its loss of foreign exchange reserves? How would it do so? How could you tell if it was? What information would you look at?
2. (25 points). Suppose Donald Trump gets elected. Nobody knows what this would mean. For the sake of argument, let's suppose that given the uncertainty, it increases the 'risk premium' on US dollar assets. Use the DD-AA model to describe the effects of an increased US dollar risk premium on the US economy. How would this affect Canada?