EC208  Question Set 2

Dr. Ozan Hatipoglu

1) Explain how a country is forced to import inflation under a fixed exchange regime.

2) Prove the following proposition using graphs: "According to the monetary model, with given nominal money stocks and real incomes, a rise in the domestic interest rates relative to those in the foreign country will be associated with a depreciation in the domestic currency"

3) Explain the process and the aim of sterilization under fixed exchange rate regime using the monetary model. Why is it a dubious process?

4) The following information is given about the total number of goods sold and their prices for the country of Developistan

<table>
<thead>
<tr>
<th>Year</th>
<th>X</th>
<th>Y</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>20 of X at $0.20</td>
<td>15 of Y at $0.30</td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>22 of X at $0.15</td>
<td>14 of Y at $0.45</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>25 of X at $0.22</td>
<td>14 of Y at $0.45</td>
<td></td>
</tr>
</tbody>
</table>

What's the yearly inflation measured between 2004 and 2005 based on the year 2003

i) according to GDP deflator?

ii) according to CPI, assuming the basket consists of X and Y?

Note: You should first create a GDP deflator index and a Consumer Price index.

5) A conservative Central Bank is one whose primary goal is to prevent inflation. The European Central Bank (ECB) is such a central bank
What conflicts might arise if the US inflation is higher than Europe and ECB is under pressure to protect competitiveness?

6) What’s the effect of an increase in money supply on output if there is perfect foresight in labor markets?

7) Write a program in excel which calculates the money’s worth based on a given CPI or GDP deflator between 1994-2003. Create a column of Wholesale Price Index deflator using data from http://www.treasury.gov.tr/yayin/hazineistatistikleri/1-8.xls. Your program should be able to answer a question like what’s your 1000 Lira in 1994 is worth in 2000? So columns labeled referring to the ”amount of money” ”initial year” and ”final year” as input columns and an answer column should be provided. Submit your file to openmac208@yahoo.com.