

Exchange rates workbook.

Unit one

Measurement of relative exchange rates:

- to other individual currencies
- Trade Weighted Index

These videos will help:

- [What are exchange rates](#) video
- [Introduction to exchange rates](#) video

Read section 5.1 of your textbook – Introduction (to exchange rates). Answer the following questions.

1. What is an exchange rate?
2. Why are exchange rates important in international trade?
3. What is the current value of the Australian dollar? How does this compare to the value of the dollar five years ago? Ten years ago? (Use the internet for this).
4. Watch the [following video about the Trade Weighted Index](#). You should also have a look at the relevant section of your textbook (around p.133).
 - i.) What is the TWI?
 - ii.) What is the purpose of the TWI? (Think about the kind of 'picture' it provides about the value of the \$A.)
 - iii.) How is the TWI determined? How are different currencies given weights in Australia's TWI?
 - iv.) Explain how this situation could be possible: *the Australian dollar depreciates against the US dollar but Australia's TWI appreciates.*
 - v.) Explain why the TWI is considered a 'better' measure of the strength of the \$A than traditional cross-rates. Use complete sentences. *This is a typical HSC question, so answer this properly as if it was worth three marks.*

Unit two

Determination of exchange rates including fixed, flexible and managed rates

For this unit, please look at the following sources:

- [How are exchange rates determined](#) video
- [Fixed versus floating exchange rates](#) video (*very useful in floating vs fixed*)
- Section 5.2 of your text
- Section 5.4 of your text

1. Floating exchange rates

Describe how this operates.

Draw an accurately labelled graph that demonstrates this method of determining exchange rates.

2. Fixed exchange rates

Describe how this operates.

Draw an accurately labelled graph that demonstrates this method of determining exchange rates.

3. Managed exchange rates

Describe, in general terms, how this operates.

4. Answer the following question: *Outline an advantage of moving from a fixed exchange rate to a floating exchange rate system.*

Unit three

Changes in exchange rates – appreciation/depreciation

In economics, you must be able to accurately draw a currency appreciation and depreciation.

Watch the following videos. Draw/briefly explain the graphs below.

- [Currency appreciation](#) video
- [Currency depreciation](#) video

Unit four

Factors affecting the demand for and supply of Australian dollars

The following videos will help you with the content you need:

- [Factors affecting the demand for \\$A](#) video
- [Factors affecting the supply of \\$A](#) video

Factor affecting demand for the \$A	How does this factor affect the value of the \$A? Discuss the process.
The level of Australian interest rates relative to global interest rates (interest rate differentials)	
Investment opportunities in Australia	
Actions of speculators/expectations of an appreciation in the \$A	
Demand for Australia's exports (X)	
Factor affecting supply of the \$A	How does this factor affect the value of the \$A? Discuss the process.
Financial flows leaving Australia	
Actions of speculators/expectations of a depreciation in the \$A	
Australia's demand for imports (M)	

Unit five

The influence of the Reserve Bank of Australia on exchange rates

From this unit, it is very important that you can discuss how the RBA acts to try and influence the level of the \$A.

- The key video to watch for this content is [here](#).
- You should also consult your textbook and the relevant section is 5.3.

1. Explain what is meant by the RBA 'dirtying the float'. Discuss, in detail, HOW the RBA would dirty the float to appreciate or depreciate the \$A.

2. Explain what is meant by the RBA undertaking 'indirect intervention'. Discuss, in detail, HOW the RBA would use indirect intervention to appreciate or depreciate the \$A.

3. Explain the following statement from the video: "Australia's exchange rates are generally allowed to float cleanly."

Unit six

The effects of fluctuations in exchange rates on the Australian economy

The key content for this section is:

- [Economic impact of currency appreciation and depreciation](#) video
- 'The effects of a change in the exchange rate' section in the text (around pp. 140-141; focus on the positive and negative effects)

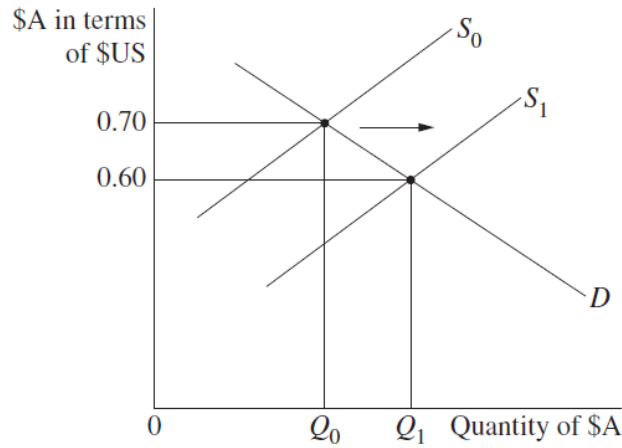
1. Define the 'valuation effect'. Give an example of how it might operate.
2. Discuss, in detail, **THREE** positives of an appreciation of the \$A.
3. Discuss, in detail, **THREE** negatives of an appreciation of the \$A.
4. Discuss, in detail, **THREE** positives of a depreciation of the \$A.
5. Discuss, in detail, **THREE** negatives of a depreciation of the \$A.

Practice exchange rate questions

2019 HSC

Question 21 (10 marks)

The diagram shows movements in the Australian dollar against the US dollar.



- (a) Outline a reason for the change in supply of the Australian dollar as shown in the diagram. 2

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- (b) Explain why Australia's exchange rate against the US dollar might NOT move in the same direction as Australia's Trade Weighted Index. 3

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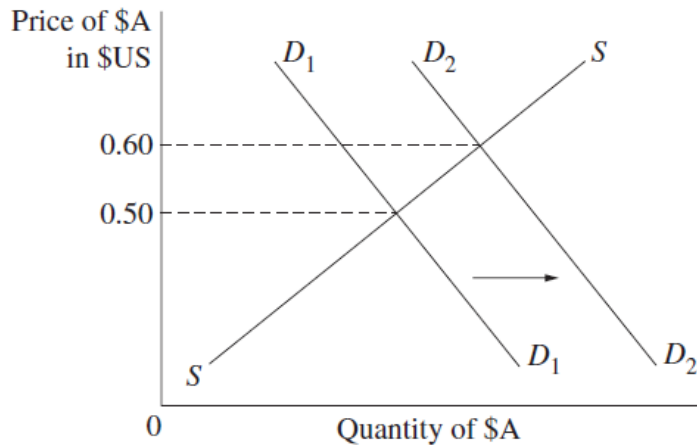
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Question 21 (10 marks)

The diagram shows information about the demand and supply of Australian dollars (\$) in terms of United States dollars (\$US). Both countries have flexible exchange rates.



- (a) State the economic term given to the movement of the exchange rate of the \$A from \$US0.50 to \$US0.60. 1

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- (b) Outline TWO causes of an increase in demand for \$A. 2

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