CHAPTER-6 | Open Economy Macroeconomics

QUIZ PART-01

1. **Foreign exchange refers to:**
   A. Only US dollars
   B. Domestic currency of a country
   C. All currencies other than domestic currency
   D. Only European currencies (C)

Explanation : Foreign exchange includes all currencies of the rest of the world except the domestic currency (e.g., USD, AUD in India).

2. **Foreign exchange rate is defined as:**
   A. The value of gold in a country
   B. The interest rate on foreign loans
   C. The rate at which one currency is exchanged for another
   D. The cost of international trade (C)

Explanation: It is the rate at which one currency can be exchanged for another, e.g., 1 USD = 85.83 INR.

3. **In a fixed exchange rate system, the exchange rate is:**
   A. Determined by demand and supply of foreign currency
   B. Fixed by the government or central bank
   C. Constantly fluctuating with trade
   D. Determined by exporters and importers (B)

Explanation: Fixed exchange rates are pegged and maintained by the government or central bank, not market forces.

4. **The process of pegging involves:**
   A. Buying foreign currency when its value falls and selling when it rises
   B. Buying foreign currency when its value rises and selling when it falls
   C. Keeping currency value unchanged by taxing imports
   D. Fixing currency in terms of domestic goods (B)

Explanation : Pegging means the central bank buys foreign exchange when its value rises and sells when it falls to stabilize exchange rates.

5. **Under the Gold Standard System, exchange rates were fixed by:**
   A. Central banks in terms of gold
   B. Governments in terms of imports
   C. Exporters and importers
   D. International Monetary Fund (A)

Explanation: Under this system, each currency's value was fixed in terms of gold, and central banks were ready to buy/sell gold at fixed prices.

6. **The Bretton Woods System pegged all currencies to:**
   A. Gold directly
   B. The British Pound
   C. The US Dollar
   D. Special Drawing Rights (SDRs) (C)

Explanation: Under Bretton Woods, currencies were pegged to the US Dollar, which was convertible into gold.

7. **Which of the following is an advantage of fixed exchange rates?**
   A. No need for foreign reserves
   B. Complete freedom from government control
   C. Stability in currency value, encouraging trade and investment
   D. Large fluctuations in exchange rates (C)

Explanation: Fixed exchange rates ensure stability, promoting trade, investment, and coordination of macroeconomic policies.

8. **A major disadvantage of fixed exchange rates is:**
   A. Excessive fluctuations in exchange rates
   B. No need to maintain foreign reserves
   C. Constant need to maintain foreign reserves
   D. Freedom from economic shocks (C)

Explanation: Maintaining stability under fixed rates requires large foreign reserves, reducing flexibility in crises.

9. **Flexible exchange rates are also called:**
   A. Dirty Floating
   B. Pegged Exchange Rates
   C. Floating or Free Exchange Rates
   D. Parity Exchange Rates (C)

Explanation: Flexible exchange rates, determined by demand and supply without government intervention, are called free or floating exchange rates.

10. **Managed floating exchange rate system is also called:**
   A. Clean Float
   B. Pegged Float
   C. Dirty Floating
   D. Gold Standard (C)

Explanation : Managed floating combines fixed and flexible systems, where central banks intervene to reduce fluctuations—known as dirty floating.

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