CHAPTER-6 | Open Economy Macroeconomics

QUIZ PART-04

1. **Balance of Trade (BOT) refers to:**
   A. Trade in goods and services together
   B. Difference between exports and imports of goods only
   C. Record of visible and invisible items
   D. All transfers from abroad (B)

Explanation : BOT measures the difference between exports and imports of visible goods only.

2. **Current Account Balance includes:**
   A. Only exports of goods
   B. Goods, services, and unilateral transfers
   C. Only imports of goods
   D. Only capital flows (B)

Explanation: Current account balance records trade in goods, trade in services, and unilateral transfers such as remittances.

3. **Official reserve transactions are conducted by:**
   A. Commercial banks
   B. Central bank
   C. Households
   D. Private firms (B)

Explanation: Official reserve transactions are undertaken by the central bank to manage foreign exchange reserves and balance of payments deficits.

4. **The real exchange rate is more relevant than the nominal rate when buying goods because it:**
   A. Excludes inflation effects
   B. Shows actual prices without exchange rates
   C. Reflects relative prices of goods adjusted for exchange rates
   D. Is fixed permanently by the government (C)

Explanation : The real exchange rate adjusts nominal rates for relative prices, showing purchasing power between domestic and foreign goods.

5. **Under the Gold Standard, a country with a trade deficit experienced:**
   A. Increase in gold reserves and inflation
   B. Decrease in gold reserves and deflation
   C. No effect on reserves
   D. Rise in exports and inflation (B)

Explanation: Trade deficit reduced gold reserves, contracting money supply and leading to deflation, which encouraged exports and reduced imports.

6. **In a flexible exchange rate regime, the exchange rate is determined by:**
   A. Central bank interventions
   B. Market forces of demand and supply
   C. Gold reserves
   D. Government decree (B)

Explanation: Flexible exchange rates fluctuate freely, determined by demand and supply of foreign exchange without government intervention.

7. **Devaluation differs from depreciation because:**
   A. Devaluation is market-led, depreciation is government-led
   B. Devaluation is government-led, depreciation is market-driven
   C. Both occur only in flexible regimes
   D. Both are identical terms (B)

Explanation: Devaluation is a deliberate act under a fixed regime, while depreciation results from market forces under a flexible regime.

8. **In a managed floating system, the central bank intervenes to:**
   A. Permanently fix exchange rates
   B. Restrict fluctuations by buying and selling foreign currency
   C. Abolish foreign reserves
   D. Eliminate international trade (B)

Explanation: Central banks intervene to restrict fluctuations in exchange rates and maintain reserves in managed floating systems.

9. **Demand for domestic goods differs from domestic demand for goods because:**
   A. Both mean the same
   B. Domestic demand includes foreign goods, while demand for domestic goods includes foreign demand too
   C. Demand for domestic goods excludes exports
   D. Domestic demand is limited to exports (B)

Explanation: Domestic demand includes all goods demanded within the country (domestic + foreign), while demand for domestic goods also includes foreign demand for them.

10. **Which of the following is an example of an invisible item in the Balance of Payments?**
    A. Export of machinery
    B. Import of petroleum
    C. Shipping and banking services
    D. Sale of gold reserves (C)

Explanation : Invisible items include services like shipping, insurance, banking, and tourism, which do not involve physical goods but affect BOP.