Practice Assessment — Task 3: Exchange Rates & Foreign Investment (Data Interpretation / Short Answer)

This practice task mirrors **Task 3** in the course assessment outline: a data-interpretation/calculation and short-answer paper on exchange rates and on foreign investment. Ten multiple-choice items, then two data/short-answer questions in parts. Recommended time: 50 minutes (40 marks).

Section One — Multiple choice (10 marks)

1. The Australian exchange rate is the price of:

A. Australian goods in foreign markets
B. the Australian dollar in terms of another currency
C. imports in Australian dollars
D. Australian exports in foreign currency

2. An appreciation of the $A occurs when:

A. the supply of $A increases
B. the demand for $A increases
C. Australian interest rates fall relative to overseas
D. commodity prices fall

3. The trade weighted index (TWI) measures the $A against:

A. the US dollar only
B. a basket of major trading partners' currencies, trade-weighted
C. the price of gold
D. the consumer price index

4. An appreciation of the $A will tend to:

A. make exports cheaper and imports dearer

B. make exports dearer and imports cheaper

C. have no effect on trade

D. increase the international competitiveness of exporters

5. Foreign direct investment is distinguished from portfolio investment by:

A. being recorded in the current account

B. establishing a lasting interest and influence in an enterprise

C. always being short-term

D. not appearing in the balance of payments

6. Foreign investment inflows are recorded in the:

A. trade balance

B. net primary income account

C. capital and financial account

D. net secondary income account

7. A rise in Australian interest rates relative to the rest of the world will most likely cause the $A to:

A. depreciate, as capital flows out

B. appreciate, as capital flows in

C. remain unchanged

D. leave the TWI unaffected

8. A cost of foreign investment in Australia is:

A. increased access to capital and technology

B. a future stream of income payable to foreign investors

C. higher domestic employment

D. greater productive capacity

9. If Australia's foreign liabilities exceed its foreign assets, Australia is a:

A. net creditor

B. net debtor

C. closed economy

D. balanced economy

10. A depreciation of the $A would be expected to:

A. worsen the trade balance immediately and permanently

B. improve export competitiveness over time

C. reduce the value of export receipts in $A

D. lower the price of imported goods

Section Two — Question 11: Exchange rates (15 marks)

Stimulus. Over a six-month period the $A moved from US$0.66 to US$0.72, against a background of rising iron-ore prices and a widening gap between Australian and US interest rates.

11(a). State whether the $A appreciated or depreciated, and calculate the percentage change. Show your working. ______________

11(b). Using a demand and supply diagram for the $A, explain how the rise in iron-ore prices contributed to this movement. (5 marks)

11(c). Explain how this movement in the exchange rate would affect Australian exporters and importers. (6 marks)

Section Two — Question 12: Foreign investment (15 marks)

12(a). Distinguish between foreign direct investment and portfolio investment. (4 marks)

12(b). Explain the link between foreign investment and the current account balance. (5 marks)

12(c). Evaluate one benefit and one cost of foreign investment for the Australian economy. (6 marks)

Marking guide (teacher)

Section One: 1 B, 2 B, 3 B, 4 B, 5 B, 6 C, 7 B, 8 B, 9 B, 10 B.

11(a): Appreciated; $\%\Delta = (0.72 - 0.66)/0.66 \times 100 \approx 9.1\%$. **11(b):** higher iron-ore prices raise export revenue and demand for $A to buy Australian commodities → demand curve for $A shifts right → new higher equilibrium exchange rate; award for a correctly labelled D/S-for-$A diagram. **11(c):** exporters — $A dearer, exports less competitive, lower foreign demand/receipts (3); importers — imports cheaper in $A, greater purchasing power, higher import volumes (3).

12(a): FDI = lasting interest/influence (≥10% voting power), more stable (2); portfolio = financial assets without control, more liquid/volatile (2). **12(b):** investment inflow recorded in the financial account funds a current account deficit; servicing it (interest/dividends) creates a net primary income outflow that widens the CAD over time (up to 5). **12(c):** benefit — access to capital/technology, jobs, capacity (3); cost — income outflows, foreign ownership/control, volatility of portfolio flows (3); reward an evaluative judgement.