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1. Double counting refers to the inclusion of the same benefits or costs more than once in the calculations of different measures like GNP, gross domestic product (GDP) etc. The reason for including only the value of final goods and services in GNP, as stated in the question, is to avoid the problem of double counting. Double counting will not occur if intermediate imports are subtracted, and intermediate exported goods are added to GNP accounts. Consider the sale of U.S. steel to Toyota and to General Motors. The steel sold to General Motors should not be included in GNP since the value of that steel is subsumed in the cars produced in the United States. The value of the steel sold to Toyota will not enter the national income accounts in a more finished state since the value of the Toyota goes towards Japanese GNP. The value of the steel should be subtracted from GNP in Japan since U.S. factors of production receive payment for it

2. Equation 2 can be written as  $CA = (Sp - I) + (T - G)$ . Higher U.S. barriers to imports may have little or no impact upon private savings, investment, and the budget deficit. If there were no effect on these variables, then the current account would not improve with the imposition of tariffs or quotas. It is possible to tell stories in which the effect on the current account goes either way. For example, investment could rise in industries protected by the tariff, worsening the current account. (Indeed, tariffs are sometimes justified by the alleged need to give ailing industries a chance to modernize their plant and equipment.) On the other hand, investment might fall in industries that face a higher cost of imported intermediate goods as a result of the tariff. In general, permanent and temporary tariffs have different effects. The point of the question is that a prediction of the manner in which policies affect the current account requires a general-equilibrium, macroeconomic analysis

**3. (a) The purchase of the German stock is a debit in the**

U.S. financial account. There is a corresponding credit in the U.S. financial account when the American pays with a check on his Swiss bank account because his claims on Switzerland fall by the amount of the check. This is a case in which an American trades one foreign asset for another.

(b) Again, there is a U.S. financial account debit as a result of the purchase of a German stock by an American. The corresponding credit in this case occurs when the German seller deposits the U.S. check in its German bank and that bank lends the money to a

German importer (in which case the credit will be in the U.S. current account) or to an individual or corporation that purchases a U.S. asset

(in which case the credit will be in the U.S. financial account).

Ultimately, there will be some action

taken by the bank which results in a credit in the U.S. balance of payments.

(c) The foreign exchange intervention by the French government involves the sale of a U.S. asset, the dollars it holds in the United States, and thus represents a