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The models developed in this chapter are designed to analyze the economic effects of exchange rates on the international economy. The models incorporate the relationships between exchange rates and economic indicators, such as trade balances and inflation rates. The models are based on the assumption that exchange rates are determined by supply and demand forces in the foreign exchange market. The models are also designed to incorporate the effects of monetary and fiscal policies on the exchange rate.

The results of the models are presented in the following graphs. The graphs show the relationships between exchange rates and economic indicators over time. The models indicate that exchange rates have a significant impact on economic performance. The graphs also show that monetary policies can be used to influence exchange rates and economic conditions.

In conclusion, the models developed in this chapter provide a framework for analyzing the economic effects of exchange rates. The models are designed to be used by policymakers and economists to make informed decisions about monetary and fiscal policies. The models also provide insights into the macroeconomic implications of exchange rate changes.
Equations (2.1) and (2.4) are the unit cost equations for exportables and non-exportables respectively. Unit costs depend on labour, (w) and capital, (q) costs and inputs from other sectors.

Equations (2.2) and (2.5) are the demand for labour functions while (2.3) and (2.6) are the supply functions for the two sectors. Equation (2.7) is the market clearing equation for non-exportables.

Equation (2.8) is the definition of the consumer price index (CPI) denoted p in the model.

Three revealed facts about the Australian economy are encapsulated in ROTE. First, real wages are fixed above the market clearing rate and in this short run model of operation the second supply of labour. Second, imports are not a close substitute for domestic output in an inflationary environment where imposing import tariffs is an inefficient means of raising importable output. The largest increase in output resulting from a 25 per cent across the board tariff increase is only 1.7 per cent. (Dixon, Permanenter, Brunet and Vincent, 1982, p.43). Third, exportables are a very small element in domestic consumption expenditures.

The logic of the BOT model is very simple. In its short run mode of operation the second capital stock is fixed. The rents on the fixed capital equipment, p^n and p^n are a function of p^n.

(2.9) \[ p^n = 1.7 + 0.16, P^{m} + 0.03 p + 0.41 p^{n} + 0.38 p^{m} + 2.16 a \]

(2.10) \[ a = \frac{1}{p^n} \]

(2.11) \[ a = \frac{1}{p^{m}} \]

(2.12) \[ a = \frac{1}{p^{n}} \]

(2.13) \[ a = \frac{1}{p^{m}} \]

Recall that all variables are defined in terms of percentage changes. If exportables prices fall by 15 percent approximately the terms of trade decline experienced by Australia between 1981 and 1983 ROTE predicts that p^n will fall by 7 percent leading to a rise in the relative price of non-exportables to exportables of some 8 percent. Thus the ROTE model predicts an appreciation of the real exchange rate with a decline in the terms of trade.

\( p^n, q^n, p^m, p^n \) and \( P^{m} \). The price of exportables (p^n) is exogenous as are real wages (w) and real absorption (a). All variables, which are defined in terms of percentage changes, and parameter values are set out in full in appendix table 1.
II. A Numerical Example: CRT Model

In Appendix A, Table 2 displays the results for both models, showing the coefficients for each variable included in the model. The CRT model includes two variables, while the BOTE model includes three. The coefficients are similar in magnitude but differ in sign for some variables. The CRT model suggests that the impact of the variable on the outcome is positive, whereas the BOTE model indicates a negative relationship.

The CRT model provides a more straightforward interpretation of the results, as it includes fewer variables. The BOTE model, on the other hand, is more complex and may require additional analysis to understand the full implications of the coefficients.

In conclusion, the CRT model is a more intuitive and straightforward approach for analyzing the relationship between variables. However, the BOTE model offers a more comprehensive view of the data, allowing for a deeper understanding of the underlying dynamics.
The equations of the three good, two-facet model are as follows:

E1) \( qX + sW = \beta X \) (1.4)
E2) \( qX + sW + eW = \beta X \) (1.4)
E3) \( qX + sW - sXW = \beta X \) (1.4)

Income and Price Changes:

E4) \( \frac{\partial E1}{\partial X} = \frac{\partial E2}{\partial W} = \frac{\partial E3}{\partial s} \)

The log-linear model is then estimated by including the equation above as an additional constraint in the TSL model with the mean of the stocks constraint in place.

The log-linear model can only capture the effects of income changes, while the ordered probit model used two separate models to capture the effects of the two facets. The ordered probit model is estimated using a two-step procedure, where the first step estimates the ordered probit model for the two facets, and the second step estimates the choice model for each facet.
dispar. If the peso remains high the assumption that domestic consumption models in a close
relationship. The critical aspect of the model is that domestic consumption and the peso are
imperfectly symmetric across the bilateral trade model. The peso has a consistent behavior that
influences the model's predictions. The peso's behavior is captured by the model of the exchange
rate. The peso's movement affects the equilibrium between the terms of trade and the real
exchange rate.

A Simpler Version

The peso is no longer considered a variable in the model. The peso is assumed to be fixed and
constant. The model is simplified and the terms of trade are no longer a factor in the model.

In this section a more general model is presented to the more simplified version of the notes.

The Exchange Rate Model

The exchange rate model in the 1980s is considered. The exchange rate is the common factor in
the model. The exchange rate is determined by two factors: the terms of trade and the relative
interest rates. The terms of trade are determined by the relative prices of exports and imports.
The relative interest rates are determined by the interest rate differential between the two
countries. The exchange rate is determined by the interaction of these two factors.

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is determined by the interaction of these two factors. The exchange rate is determined by the
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and the relative interest rates. The exchange rate is determined by the interaction of these
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exchange rate is determined by the relative prices of exports and imports. The relative prices
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determined by the interaction of these two factors.
The influence of the open economy on the domestic economy is reflected in the model assumptions that domestic variables in the open economy are determined by international factors. The model assumes that domestic production is driven by foreign demand, which is assumed to be exogenous. The model also assumes that the domestic economy is subject to international price shocks, which affect the prices of goods and services. The model further assumes that the domestic economy is subject to international interest rates, which affect the cost of borrowing and lending.

The model is a simple extension of the closed economy model, which assumes that the economy is isolated from the rest of the world. In the closed economy model, the standard Keynesian assumptions of the circular flow of income and the multiplier effect hold. In the open economy model, these assumptions are modified to account for the influence of international factors.

The model is a useful tool for understanding the effects of international trade and finance on the domestic economy. It can be used to analyze the effects of changes in foreign demand, foreign interest rates, and foreign prices on the domestic economy. The model can also be used to analyze the effects of domestic policies, such as fiscal and monetary policies, on the domestic economy.
The second question posed regarding the model is whether the implications and restrictions are consistent with the data. The answers to these questions depend on the model chosen to represent the relationship between the variables. The model chosen must be consistent with the data and the theory of exchange rates. The model chosen must also be consistent with the economic theory of exchange rates.

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate</td>
<td>-0.2</td>
<td>0.05</td>
<td>-0.06</td>
<td>-0.07</td>
<td>-0.08</td>
<td>-0.09</td>
<td>-0.09</td>
<td>-0.08</td>
<td>-0.07</td>
<td>-0.06</td>
</tr>
<tr>
<td>Rate</td>
<td>0.15</td>
<td>0.20</td>
<td>0.25</td>
<td>0.30</td>
<td>0.35</td>
<td>0.40</td>
<td>0.45</td>
<td>0.50</td>
<td>0.55</td>
<td>0.60</td>
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</tbody>
</table>

The table above shows the exchange rate data for the years 1973 to 1982. The exchange rate is defined as the price of one unit of a foreign currency expressed in terms of a domestic currency. The exchange rate is an important determinant of international trade and investment.

The second question posed regarding the model is whether the implications and restrictions are consistent with the data. The model chosen must be consistent with the data and the theory of exchange rates. The model chosen must also be consistent with the economic theory of exchange rates.
### Table 1: Exchange Rate and the Terms of Trade

<table>
<thead>
<tr>
<th>Exchange Rate</th>
<th>Terms of Trade</th>
</tr>
</thead>
<tbody>
<tr>
<td>100</td>
<td>50</td>
</tr>
<tr>
<td>200</td>
<td>70</td>
</tr>
<tr>
<td>300</td>
<td>90</td>
</tr>
<tr>
<td>400</td>
<td>110</td>
</tr>
<tr>
<td>500</td>
<td>130</td>
</tr>
</tbody>
</table>

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In the long run, a country's exchange rate is determined by the relative prices of its exports and imports. The terms of trade are an indicator of the relative price levels of a country's exports and imports. A country with an export price advantage has a positive terms of trade, and vice versa. The exchange rate reflects the terms of trade in the long run, as countries adjust their currencies to balance trade flows.
models is the complete consequences for the real exchange rate of changes in the terms of trade.

The conclusion is derived from the analysis of these numerical simulations.

References and/or footnotes (1997).

A fall in the terms of trade tends to increase the real exchange rate by reducing the balance of payments. The empirical results show that the effect of a fall in the terms of trade is larger than the effect of a fall in the real interest rate on the exchange rate. The model is estimated using a panel data set of 15 countries from 1960 to 1988, with a focus on the exchange rate and real interest rate. The results indicate that the model captures the data well, with the exchange rate being determined by the balance of payments and the real interest rate.

The second conclusion is that the model provides a valuable tool for the analysis of real exchange rate movements.

VI. Summary and Conclusions

The model is an important contribution to the literature on real exchange rates. It provides a framework for analyzing the determinants of real exchange rates and for assessing the implications of policy changes. The model is estimated using a panel data set of 15 countries from 1960 to 1988, with a focus on the exchange rate and real interest rate. The results indicate that the model captures the data well, with the exchange rate being determined by the balance of payments and the real interest rate.

The model is an important contribution to the literature on real exchange rates. It provides a framework for analyzing the determinants of real exchange rates and for assessing the implications of policy changes. The model is estimated using a panel data set of 15 countries from 1960 to 1988, with a focus on the exchange rate and real interest rate. The results indicate that the model captures the data well, with the exchange rate being determined by the balance of payments and the real interest rate.
changes in Australia’s terms of trade

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### Appendix Table 1

<table>
<thead>
<tr>
<th>Parameter Values</th>
<th>Notation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer goods, $T_m = 0.28$</td>
<td>$\theta_m = 0.25$</td>
</tr>
<tr>
<td>Indirect input, $T_{in} = 0.19$</td>
<td>$\theta_m = 0.25$</td>
</tr>
</tbody>
</table>

### Appendix Table 2

<table>
<thead>
<tr>
<th>Parameter Values</th>
<th>Notation</th>
</tr>
</thead>
<tbody>
<tr>
<td>$C_{in}$</td>
<td>$W$</td>
</tr>
<tr>
<td>$C_{out}$</td>
<td>$W$</td>
</tr>
<tr>
<td>$I_{in}$</td>
<td>$W$</td>
</tr>
<tr>
<td>$I_{out}$</td>
<td>$W$</td>
</tr>
</tbody>
</table>

### Diagram

- **Source:** Diagram et al. (1982, p. 117)
- **Note:** Redrawn from the original diagrams for clear presentation.