

World Saving and Investment Questions

Assume that the economy is open and that the world interest rate is determined on the world market instead of in the domestic economy. Use a two-country model with initial current accounts equal to zero. Use world saving - investment diagrams to answer the questions below.

1. How does an increase in domestic wealth affect the world equilibrium interest rate and the domestic current account?
2. How does an equal increase in current domestic taxes and government spending affect the world equilibrium interest rate and the domestic current account?
3. How does an increase in domestic total factor productivity affect the world equilibrium interest rate and the domestic current account?