

Past-paper walk-through

Real Interest Rates and International Capital Flows ■ 6.6

eXercise

Questions in this set

- 2026 Q1
- 2025 Set 2 Q1
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- 2022 Set 1 Q3
- 2021 Set 1 Q1
- 2021 Set 1 Q2
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Reading the mark scheme

- **B1** a mark that stands on its own – the point is either made or not.
- **M1** a *method* mark: the right approach, even if the number is wrong.
- **A1** an *answer* mark, and it usually needs its M mark first.
- **C1** a working mark on the way to the answer.
- **//** separates answers the examiner accepts equally.
- **ecf** = error carried forward: a later part is marked on your own earlier answer.
- **owtte** = “or words to that effect” – the wording need not match.

Question 1

2026 ■ Q1

The economy of Micanapy is in short-run equilibrium and is experiencing an inflationary gap.

(a)(i) Draw a correctly labeled graph of the aggregate demand, short-run aggregate supply, and long-run aggregate supply curves for Micanapy, and show each of the following.

The current equilibrium real output and price level, labeled Y_1 and PL_1 , respectively.

(a)(ii) Draw a correctly labeled graph of the aggregate demand, short-run aggregate supply, and long-run aggregate supply curves for Micanapy, and show each of the following.

The full-employment real output, labeled Y_F .

Question 1

2026 ■ Q1

The economy of Micanapy is in short-run equilibrium and is experiencing an inflationary gap.

(b) Assume that policymakers take no action to close the inflationary gap. Explain how Micanapy's economy will self-adjust to full employment in the long run.

Question 1

2026 ■ Q1

The economy of Micanapy is in short-run equilibrium and is experiencing an inflationary gap.

(c)(i) Suppose instead that Micanapy's central bank is considering using monetary policy to close the inflationary gap in the short run. The banking system in Micanapy has limited reserves.

Identify a specific open-market operation that the central bank of Micanapy would implement to close the inflationary gap in the short run.

(c)(ii) Draw a correctly labeled graph of the money market in Micanapy, and show the effect of the open-market operation identified in part C (i) on the nominal interest rate.

Question 1

2026 ■ Q1

The economy of Micanapy is in short-run equilibrium and is experiencing an inflationary gap.

(d)(i) Based solely on the interest rate change shown on your graph in part C (ii), will each of the following increase, decrease, or remain the same in the short run?

International financial capital flows into Micanapy. Explain.

(d)(ii) Based solely on the interest rate change shown on your graph in part C (ii), will each of the following increase, decrease, or remain the same in the short run?

The price of previously issued bonds in Micanapy.

(d)(iii) Based solely on the interest rate change shown on your graph in part C (ii), will each of the following increase, decrease, or remain the same in the short run?

Private domestic investment spending in Micanapy.

Question 1

2026 ■ Q1

The economy of Micanapy is in short-run equilibrium and is experiencing an inflationary gap.

(e) Based solely on the change in private domestic investment spending identified in part D (iii), will the unemployment rate in Micanapy increase, decrease, or remain the same in the short run? Explain.

Question 1

2025 Set 2 ■ Q1

Assume that the economy of Barrikos is in short-run equilibrium, with its economic data summarized in the table provided. The government budget is balanced, and the capital and financial account (CFA) balance is zero.

Cyclical unemployment rate	6%
Natural unemployment rate	4%
Structural unemployment rate	1%
Actual inflation rate	3%
Expected inflation rate	5%

Question 1

(a) What is the numerical value of the actual unemployment rate in Barrikos?

Question 1

Cyclical unemployment rate	6%
Natural unemployment rate	4%
Structural unemployment rate	1%
Actual inflation rate	3%
Expected inflation rate	5%