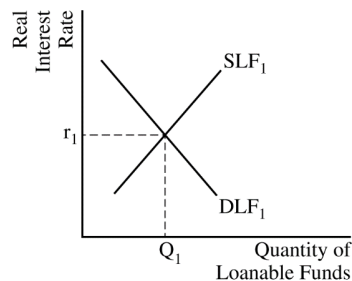


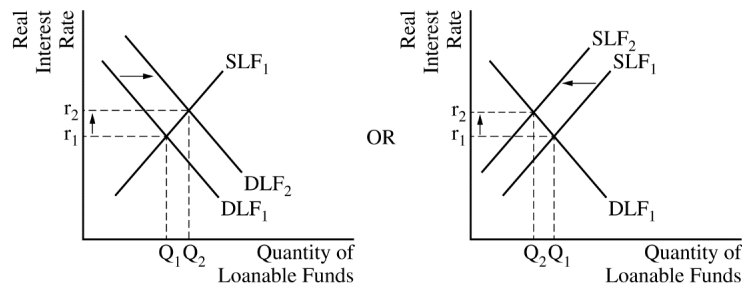
Question 2: Short**5 points**

(a) State that the country could implement one of the following fiscal policy actions: increase government spending, increase transfer payments, or decrease taxes. **1 point**

(b) Draw a correctly labeled graph of the loanable funds market. **1 point**



For the second point, the graph must show a rightward shift in the demand for loanable funds curve (or a leftward shift in the supply of loanable funds curve), resulting in an increase in the equilibrium real interest rate. **1 point**

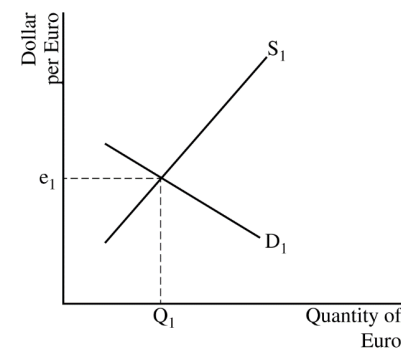
**Total for part (b) 2 points**

(c) (i) State that net exports will decrease and explain that the increase in the real interest rate will increase the demand for the country's currency, which will cause the country's currency to appreciate and make domestic goods relatively more expensive than foreign goods, thereby decreasing exports. **1 point**

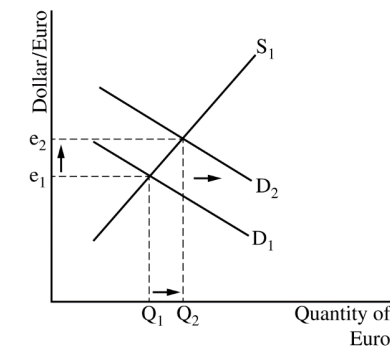
(ii) State that the stock of physical capital will decrease and explain that the increase in the real interest rate will discourage investment spending in physical capital. **1 point**

Total for part (c) 2 points**Total for question 2 5 points****Question 2****5 points (1 + 2 + 2)****(a) 1 point**

- One point is earned for stating that the U.S. current account will be in deficit and for explaining that an increase in the U.S. real GDP increases the U.S.'s demand for European goods and services, which increases imports.

(b) 2 points

- One point is earned for drawing a correctly labeled graph of the foreign exchange market for the euro.



- One point is earned for shifting the demand curve for the euro to the right and showing an increase in the value of the euro relative to the U.S. dollar.

2019 SCORING GUIDELINES**Question 2 (continued)****(c) 2 points**

- One point is earned for stating that the demand for the dollar will decrease and for explaining that capital flows from the European Union to the U.S. will decrease.
- One point is earned for stating that the dollar will depreciate.