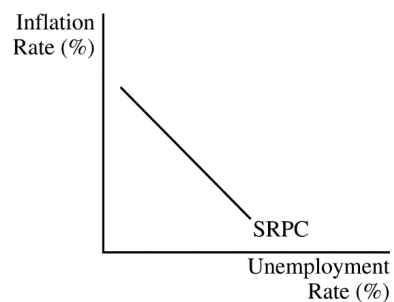
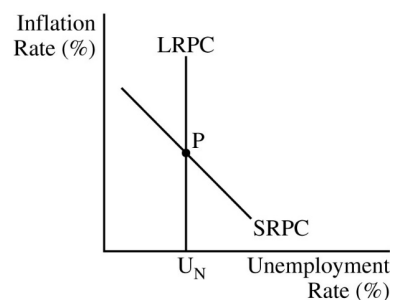
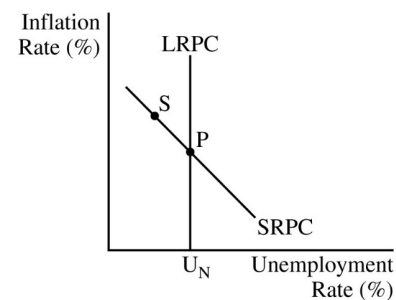


Question 1: Long**10 points****A** Draw a correctly labeled graph of the short-run Phillips curve (SRPC). **1 point**

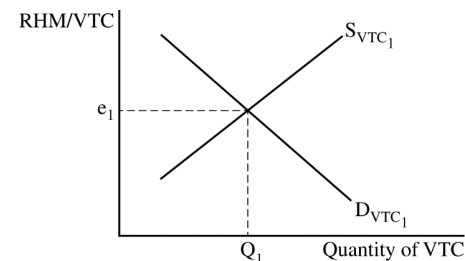
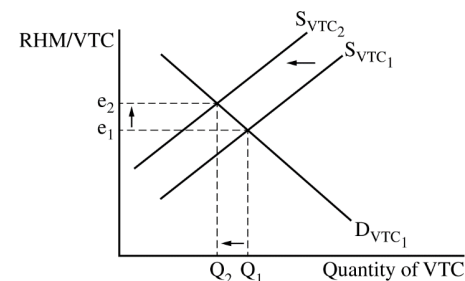
Point 1

Point 2 The graph must include a correctly labeled long-run Phillips curve (LRPC) and show a point labeled P at the intersection of the short-run and long-run Phillips curves. **1 point**Point 3 **B (i)** State that real output will increase and explain that the new residential construction projects increase investment spending, which increases aggregate demand. **1 point****(ii)** On the graph from part A, show a point labeled S on the SRPC to the left of point P. **1 point**

Point 4

**C** Draw a correctly labeled graph of the foreign exchange market for the Vortanian crown. **1 point**

Point 5

Point 6 The graph must show a leftward shift in the supply curve of the Vortanian crown, resulting in an appreciation of the Vortanian crown. **1 point****D** State that Vortania's net exports will decrease. **1 point**

Point 7

Point 8 **E (i)** State that the capital and financial account (CFA) balance in Vortania will move into surplus and explain that the current account (CA) moved into deficit and the balance of payments must balance (CA+CFA=0). **1 point****(ii)** State that employment in Vortania will decrease. **1 point**

Point 9

Point 10 **F** State that the central bank of Vortania would sell Vortanian crowns in the foreign exchange market and explain that the increased supply of the Vortanian crown will cause it to depreciate. **1 point**

Question 2: Short**5 points**

- (a) Calculate real GDP in Louland in year 2 as 900,000 and show your work. **1 point**

$$\text{Real GDP} = \frac{\text{Nominal GDP}}{\text{GDP Deflator}} \times 100 = \frac{1,035,000}{115} \times 100 = 900,000$$

- (b) State that the demand for money would increase and the nominal interest rate would increase. **1 point**

- (c) State that the standard of living of the average citizen in Louland decreased from year 1 to year 2 and explain that the real GDP per capita in year 1 was 800 and the real GDP per capita in year 2 was 750. **1 point**

- (d) State that the inflation rate from year 1 to year 2 was 15%. **1 point**

- (e) State that real wages decreased and explain that nominal wages increased by less than the inflation rate ($10\% < 15\%$). **1 point**

Total for question 2 5 points**Question 2: Short****5 points**

- (a) Calculate the nominal GDP in Maltrose in year 2 as \$210 and show your work. **1 point**

$$\text{Nominal GDP}_{\text{Year 2}} = (\$13 \times 10) + (\$4 \times 20) = \$210$$

- (b) Calculate the GDP deflator in Maltrose in year 2 as 105 and show your work. **1 point**

$$\text{GDP Deflator}_{\text{Year 2}} = \frac{\text{Nominal GDP}_{\text{Year 2}}}{\text{Real GDP}_{\text{Year 2}}} \times 100 = \frac{\$210}{(\$10 \times 10) + (\$5 \times 20)} \times 100 = 105$$

- (c) State that the inflation rate from year 1 to year 2 was 5%. **1 point**

- (d) (i) State that people living on a fixed income were worse off. **1 point**

- (ii) State that borrowers with fixed-interest-rate loans were better off because the real value of their debt decreased by more than they expected or because the real interest rate was lower than expected. **1 point**

Total for part (d) 2 points**Total for question 2 5 points**