

MACROECONOMICS

Section II

Total Time—60 minutes

Reading Period—10 minutes

Writing Period—50 minutes

Directions: You are advised to spend the first 10 minutes reading all of the questions and planning your answers. You will then have 50 minutes to answer all three of the following questions. You may begin writing your responses before the reading period is over. It is suggested that you spend approximately half your time on the first question and divide the remaining time equally between the next two questions. Include correctly labeled diagrams, if useful or required, in explaining your answers. A correctly labeled diagram must have all axes and curves clearly labeled and must show directional changes. Use a pen with black or dark blue ink.

1. Assume that the United States economy is currently in a short-run equilibrium with the actual unemployment rate above the natural rate of unemployment.
 - (b) Assuming no policy actions are taken, will the short-run Phillips curve shift to the right (upward), shift to the left (downward), or remain the same in the long run? Explain.
 - (c) If the Federal Reserve Bank wants to lower unemployment, what expansionary open-market operation should it use?
 - (d) How will the open-market operation you identified in part (c) affect each of the following?
 - (i) Federal funds rate. Explain.
 - (ii) Real interest rate in the short run.
 - (e) Given your answer in part (d)(ii), what is the effect on real gross domestic product (GDP) in the short run? Explain.
 - (f) Japan and the United States are major trading partners. Indicate how the change in real GDP you identified in part (e) will affect the demand for the Japanese yen in the foreign exchange market.