AP® Macroeconomics
2003 Sample Student Responses

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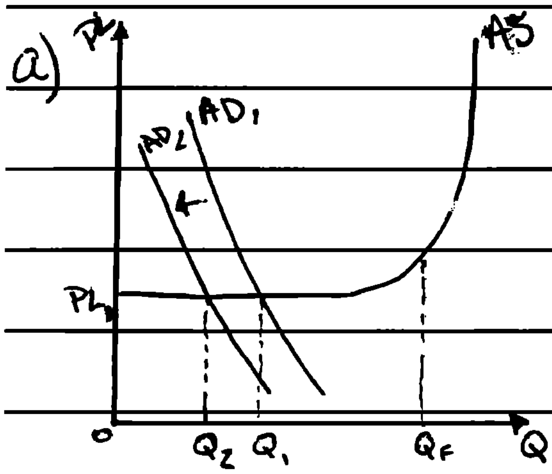
1MACLA1

Write in the box the number of the question you are answering on this page as it is designated in the examination.

1

a)

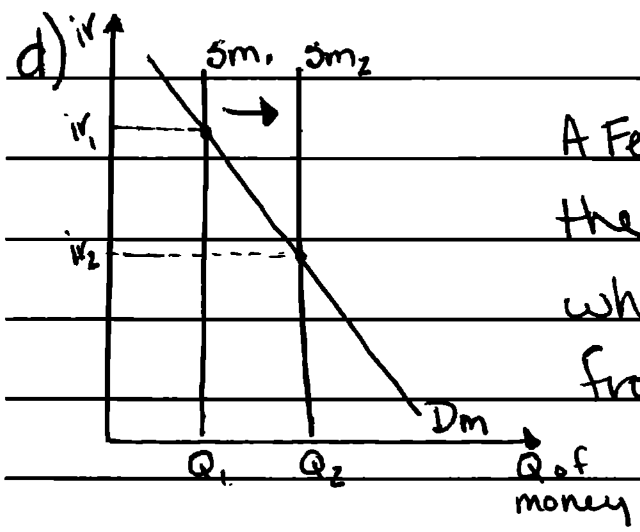


The full employment output is at Q_F. Because of the recession, the economy is operating at Q_1 PL_1.

b) The decrease in spending will shift Aggregate demand from AD_1 to AD_2. This lowers the level of output to Q_2. However, since the economy is operating in the horizontal range, there will be no change in price level.

c) The unemployment rate will increase in the short run. There will be a decrease in AD, thereby decreasing the quantity of output. Firms will then need fewer workers to produce goods and people will loose jobs

d)



A Fed purchase of bonds will increase the money supply (from Sm_1 to Sm_2) which lowers the interest rate from ir_1 to ir_2. The lower interest rate will result in a greater

1MACLA2

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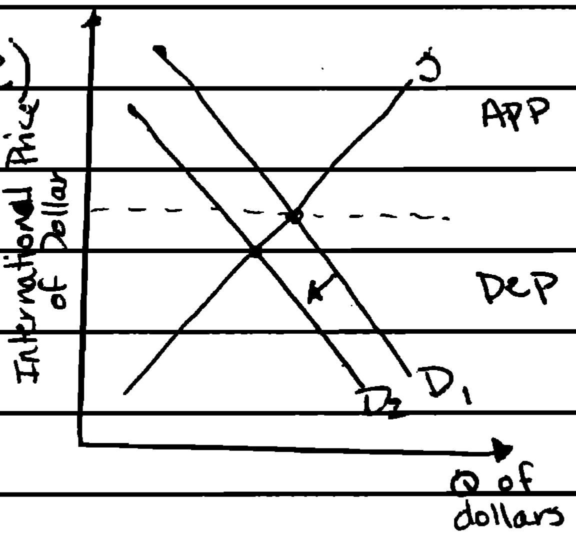
quantity of funds invested. This shifts aggregate demand to the right, increasing output and price level (in the intermediate range).

e)



An decrease in the interest rate will ~~the~~ discourage foreign investors from investing in the US. As a result, the demand for the dollar decreases. the dollar depreciates. Exports will increase because it is now relatively less expensive for foreign countries to by US goods. Imports will decrease because it is now relatively more expensive for the US to buy foreign goods.

1MACLD1

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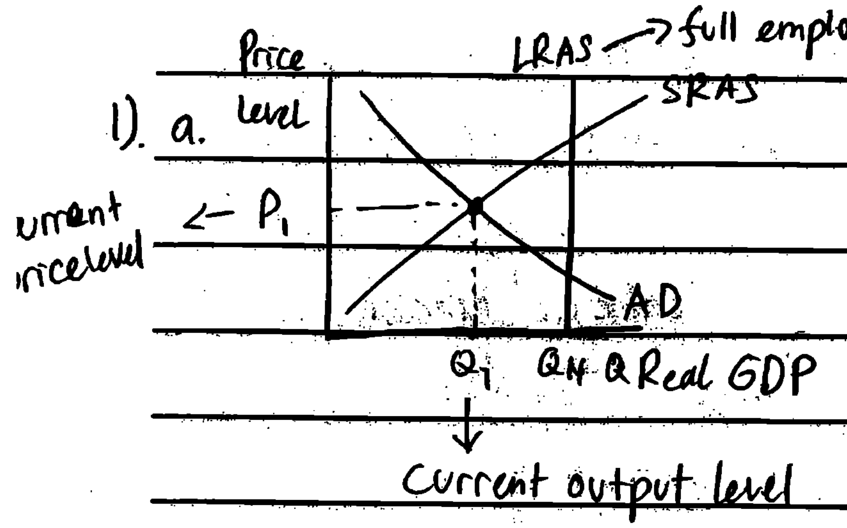
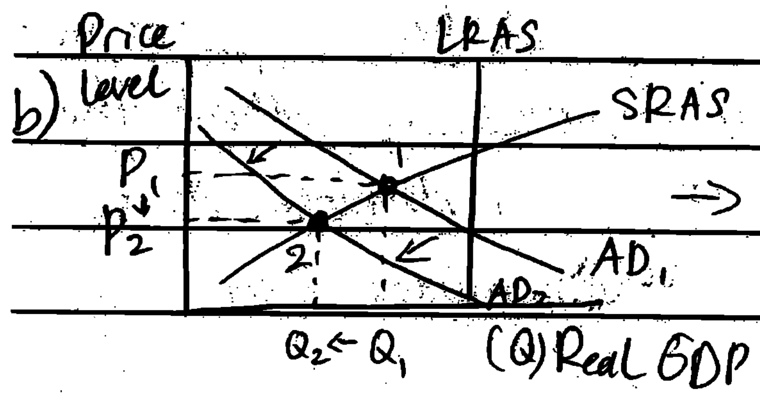
1 (one)

1). a.



Based on the graph, full-employment output (i) is shown by the vertical line of LRAS (Long-run ~~Aggregae~~ Aggregate supply), current output level (ii) is shown by Quantity of RGDP(1) (Q_1) and current price level is shown by P_1.

b)



→ The economy will move from point 1 to point 2.

A major ~~deerease~~ decrease in government spending result in a decrease of AD (Aggregate Demand). Aggregate demand will shift Leftward from AD_1 to AD_2. (i) As a result of this decrease, the level of out put will also decrease. SRAS will move downward from point Q_1 to point Q_2. (ii) A Decrease in AD will also decrease the price level. Price level will move downward from point P_1 to P_2.

c). The decrease in government spending will increase the unemployment rate. This is because less employees or workers is needed to produce lower level RGDP. Since there is a decrease in level of ~~oup~~ output, more workers or employees will be laid off from the working industries and less people will be hired, this factor will increase the ~~a~~ unemployment rate.

1 MACLD2

MACLD2

1. (one)

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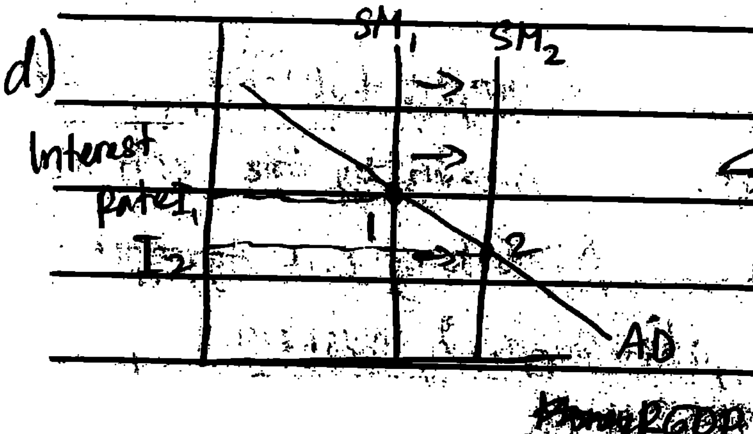
d)

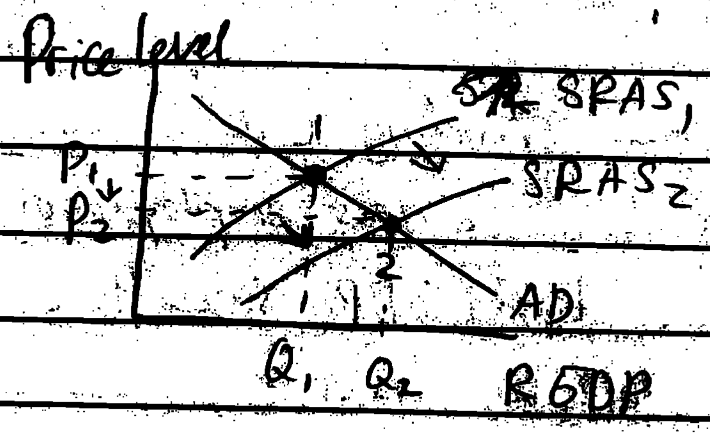
(i)



→ Interest rate decrease

When the Fed purchase bonds, the money supply will be increased. this is because more money will be available in the market. When supply of money is increasing without the change of demand, the interest rate will decrease. As seen in the graph, Interest rate will move downward from point 1 (I_1) to point 2 (I_2).

(ii) An Increase in money supply results a decrease in interest rate. A decrease in interest rate will entice investment. Investment will increase, which also results in an increase in output (output will increase). When output is increasing without a change in demand, the price level will go down. Shown by the graph.



1 MACD3

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1. (one)

e) A decrease in interest rate means ~~a dep~~ the value of dollars depreciate. It will be cheaper for foreign currency to buy dollars. This means that U.S. goods will cost cheaper than foreign goods. As a result, U.S. exports will increase; it is because more foreigner will be able ~~to~~ and willing to buy U.S. goods (because it is cheaper) and U.S. imports will decrease; it is because foreign goods will become more expensive for U.S. market to buy, people will buy less foreign goods.