Unit 4 Progress Check: FRQ

Name

1. 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. If the question prompts you to "Calculate," you must show how you arrived at your final answer.

Commercial banks in Country A hold no excess reserves. The required reserve ratio is 0.1. The central bank of Country A has become concerned about a steep decline in investment spending.

(a) Calculate the simple money multiplier. Show your work.

(b) Identify an open market operation that Country A's central bank is likely to implement to address the decline in investment spending.

(c) Draw a correctly labeled graph of the money market and show the effect of the central bank's policy identified in part (b) on the nominal interest rate.

(d) Explain the effect of the change in part (c) on aggregate demand in the short run.

Please respond on separate paper, following directions from your teacher.

2. 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. If the question prompts you to "Calculate," you must show how you arrived at your final answer.

A national newspaper's headline reads "Business Confidence Reaches Highest Level in 5 Years."

(a) Draw a correctly labeled graph of the loanable funds market, and show the effect of high business confidence on the equilibrium real interest rate.

(b) Assume the government increases its spending on capital projects and infrastructure. Would financing the increased government spending by borrowing result in a higher, a lower, or the same equilibrium real interest rate? Explain.

(c) How will the increase in government spending financed by borrowing affect national savings?

(d) If the expected inflation rate decreases to zero, will the nominal interest rate be greater than, less than, or equal to the real interest rate? Explain.

Unit 4 Progress Check: FRQ

Please respond on separate paper, following directions from your teacher.