

2006 AP[®] MACROECONOMICS FREE-RESPONSE QUESTIONS

2. Interest rates are important in explaining economic activity.
- (a) Using a correctly labeled graph of the money market, show how an increase in the income level will affect the nominal interest rate in the short run.
 - (b) Using a correctly labeled graph of the loanable funds market, show how a decision by households to increase saving for retirement will affect the real market interest rate in the short run.
 - (c) Suppose that the nominal interest rate has been 6 percent with no expected inflation. If inflation is now expected to be 2 percent, determine the value of each of the following.
 - (i) The new nominal interest rate
 - (ii) The new real interest rate
3. The unemployment rate is an important indicator of the health of the United States economy.
- (a) Assume that with the economy at full employment, the government implements an expansionary fiscal policy. How does the actual unemployment rate at the new short-run equilibrium compare with the natural rate of unemployment?
 - (b) Assume that a significant number of workers are involuntarily changed from full-time to part-time employment. Explain how this will affect the number of people who are officially classified as unemployed.
 - (c) Assume that the government reduces the level of unemployment compensation.
 - (i) Explain how this affects the natural rate of unemployment.
 - (ii) Using a correctly labeled graph, show how this affects the long-run Phillips curve.

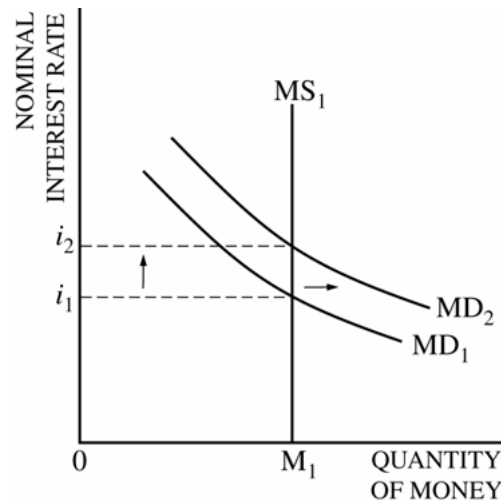
STOP

END OF EXAM

**AP[®] MACROECONOMICS
2006 SCORING GUIDELINES**

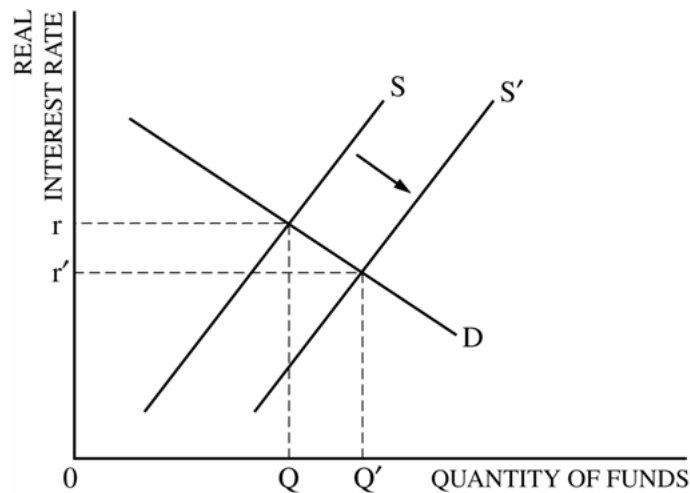
Question 2

8 points (3 + 3 + 2)



(a) 3 points:

- One point is earned for a correctly labeled graph.
- One point is earned for showing a rightward shift of the money demand curve.
- One point is earned for showing that the nominal interest rate is increasing.



(b) 3 points:

- One point is earned for a correctly labeled graph.
- One point is earned for showing a rightward shift of the supply curve for loanable funds.
- One point is earned for showing that the real interest rate is decreasing.

(c) 2 points:

- One point is earned for indicating that the nominal interest rate is 8 percent.
- One point is earned for indicating that the real interest rate is 6 percent.