2. The United States and South Africa are trading partners with flexible exchange rates, and the United States current account balance with South Africa is zero.

(a) Assume real income in the United States increases while real income in South Africa remains the same. Will United States net exports increase, decrease, or remain unchanged? Explain.

(b) Based on your answer to part (a), what will happen to each of the following?

(i) The capital and financial account balance in the United States
(ii) Actual unemployment in South Africa in the short run. Explain.

(c) The currency of the United States is the dollar (USD), and the currency of South Africa is the rand (ZAR). Draw a correctly labeled graph of the foreign exchange market for the rand and show the effect of the increase in real income in the United States on the international value of the rand.

Begin your response to this question at the top of a new page in the separate Free Response booklet and fill in the appropriate circle at the top of each page to indicate the question number.

GO ON TO THE NEXT PAGE.

3. Assume that the economy of country Zen is in long-run macroeconomic equilibrium.

(a) Draw a correctly labeled graph of the aggregate demand, short-run aggregate supply, and long-run aggregate supply curves, and show each of the following.

(i) The current equilibrium real output and price level, labeled Y_1 and PL_1, respectively
(ii) The full-employment output, labeled Y_F

(b) On your graph in part (a), show the short-run effect of an increase in consumer confidence. Label the new equilibrium real output Y_2 and the new equilibrium price level PL_2.

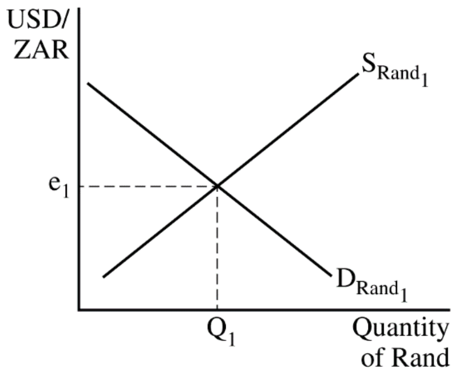
(c) Assume that the banking system in Zen has ample reserves. Suppose that the central bank's goal is to maintain a stable price level at PL_1. Based on the change in the price level shown in part (b), identify one specific monetary policy action the central bank would take to achieve its goal.

(d) Based on the monetary policy action identified in part (c), will real output increase, decrease, or stay the same in the short run? Explain.

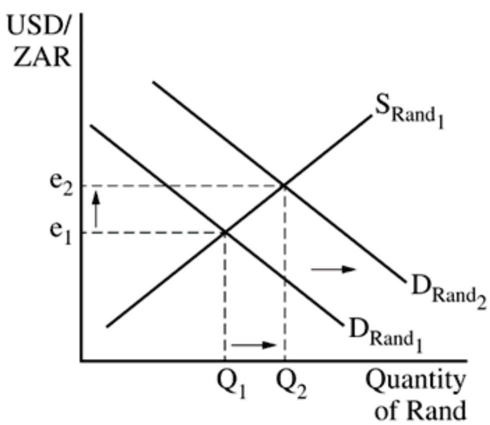
Begin your response to this question at the top of a new page in the separate Free Response booklet and fill in the appropriate circle at the top of each page to indicate the question number.

Question 2: Short — 5 points

(a)	State that United States net exports will decrease and explain that the demand for goods from South Africa will increase, which increases United States imports.	**1 point**
(b) (i)	State that the capital and financial account balance in the United States will move into surplus.	**1 point**
(ii)	State that actual unemployment in South Africa will decrease in the short run and explain that South African exports will increase, which will increase aggregate demand and real GDP in South Africa.	**1 point**
	Total for part (b)	**2 points**
(c)	Draw a correctly labeled graph of the foreign exchange market for the rand.	**1 point**



For the second point, the graph must show a rightward shift in the demand curve for the rand, resulting in an appreciation of the rand. **1 point**



Total for part (c) — **2 points**

Total for question 2 — **5 points**