1. Assume that the economy of Barrikos is in short-run equilibrium, with its economic data summarized in the table provided. The government budget is balanced, and the capital and financial account (CFA) balance is zero.

Cyclical unemployment rate	6%
Natural unemployment rate	4%
Structural unemployment rate	1%
Actual inflation rate	3%
Expected inflation rate	5%

A. What is the numerical value of the actual unemployment rate in Barrikos?

B. Using the relevant numerical values, draw a correctly labeled graph of the short-run and long-run Phillips curves for Barrikos. Indicate the current short-run equilibrium with a point labeled X. Plot the relevant numerical values on the graph.

C. Based on your graph in part B, identify one specific fiscal policy action that the government of Barrikos would take to move the economy toward long-run equilibrium.

D. Assume that the fiscal policy action identified in part C is implemented.

i. Will the government budget in Barrikos move into surplus, move into deficit, or remain balanced? Explain.

ii. Assume there is no change in inflationary expectations. On your graph in part B, show a possible new short-run equilibrium point, labeled Z, that would result from the fiscal policy action identified in part C.

iii. Draw a correctly labeled graph of the loanable funds market, and show the effect of the fiscal policy action identified in part C on the real interest rate.

E. Barrikos has an open economy and a flexible exchange rate. Based solely on the change in the real interest rate in Barrikos shown on your graph in part D (iii), will Barrikos' capital and financial account (CFA) balance move into surplus, move into deficit, or remain the same? Explain.

F. Based on the change in Barrikos' capital and financial account (CFA) balance identified in part E, what will happen to the international value of Barrikos' currency? Explain.

2. Assume the economy of Jenland is in short-run equilibrium at a real output level above full-employment real output.

A. The banking system in Jenland has ample reserves. Identify a specific monetary policy action that the central bank of Jenland would implement to return the economy to full employment in the short run.

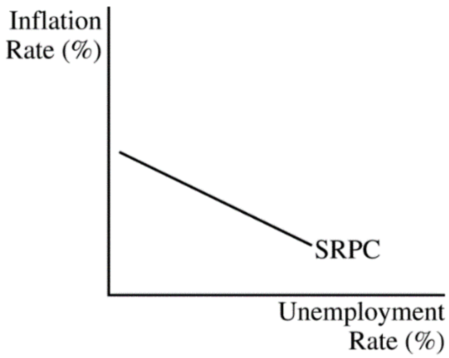
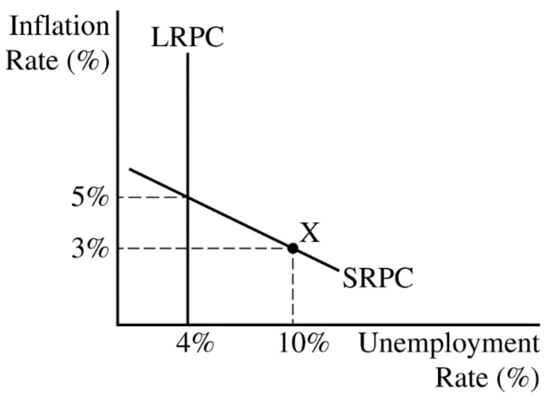
B. Draw a correctly labeled graph of the reserve market for Jenland, and show the effect of the central bank's action identified in part A on the policy rate.

C. Based on the change in the interest rate shown on your graph in part B, will each of the following increase, decrease, or remain the same in Jenland in the short run?

i. The price of previously issued bonds

ii. The price level. Explain.

Question 1: Long — 10 points

A Point 1	State that the actual unemployment rate is 10%.	**1 point**
B Point 2	Draw a correctly labeled graph of the short-run Phillips curve (SRPC).  	**1 point**
Point 3	The graph must include a vertical long-run Phillips curve (LRPC) at the natural rate of unemployment (4%), the expected inflation rate (5%) at the intersection of the SRPC and the LRPC, and a point labeled X on the SRPC to the right of the LRPC at the actual unemployment rate (10%) and the actual inflation rate (3%).  	**1 point**
C Point 4	State an increase in government spending, a decrease in taxes, or an increase in transfer payments.	**1 point**