

FRQ 12: THE LAST ONE

1. Assume that a country's economy is in equilibrium.

(a) Using a correctly labeled aggregate demand and aggregate supply graph, show how an increase in the price of oil, an important natural resource, will affect the following in the short run.

- (i) Real output
- (ii) Price level

(b) Using a correctly labeled graph, show how the increase in the price of oil affects the short-run Phillips curve.

(c) Assume that the central bank of the country responds to the higher price of oil by increasing the money supply.

(i) Explain the process by which the increase in the money supply will affect the aggregate demand in the short run.

(ii) Indicate how the increase in the money supply will affect real output and the price level.

(d) Now assume that instead of using monetary policy in response to the oil price increase, the government reduces business taxes, which results in lower production costs. Using a new correctly labeled graph, show the effect of the reduction in business taxes on the following.

- (i) Real output
- (ii) Price level

2. Due to an international financial crisis, Canada experiences a significant inflow of funds from other countries. Explain the effect that this inflow of funds will have on the following.

- (a) The international value of the Canadian dollar.
- (b) Canadian net exports
- (c) The real interest rate in Canada
- (d) The level of investment in Canada

<i>Country</i>	<i>Units of Cloth per worker per day</i>	<i>Units of Food per worker per day</i>
Newland	10	2
Beeland	10	1

3. The table above gives the production alternatives of two nations that are producing cloth and food, using equal amounts of resources.

- (a)
 - (i) Calculate the opportunity cost of producing a unit of cloth in Newland.
 - (ii) Calculate the opportunity cost of producing a unit of food in Beeland.
- (b)
 - (i) Which nation has the comparative advantage in cloth production?
 - (ii) Which nation has the comparative advantage in food production?
- (c) Now assume that the productivity of Beeland's workers triples for each good.
 - (i) Which country has a comparative advantage in food production?
 - (ii) Explain how you determined your answer.