
2. Replicate table 29-1 in Hubbard and O’Brien for Turkey for 2009. (The table entries will not be exactly the same.) What do you learn?

3. Write a paragraph (or two) explaining in your own words what affects the values of floating exchange rates. Then write another paragraph using your reasoning to explain why the euro is currently losing value against the dollar.

4. Think about the following model where aggregate supply is given by

\[ Y = 250 + 25P, \]

the components of aggregate demand are

\[ C = 159 + 0.6DI - 25P \]
\[ G = 800 \]
\[ T = 10 \]
\[ I = 175 - 20i + 0.3Y \]
\[ NX = 100 - 0.1Y + 0.5e, \]
where NX is net exports and e is the exchange rate (domestic currency per foreign currency), the money market is characterized by

\[
\begin{align*}
MS &= 100 \\
MD &= 200 - 20i + 0.2Y,
\end{align*}
\]

and the foreign exchange value of the domestic currency is given by

\[e = 350 - 20i.\]

(a) Interpret the model. Why does NX depend negatively on Y and positively on e? Why does e depend negatively on i? Why does I depend negatively on i and positively on Y?

(b) Solve model for the equilibrium values of P, Y, I, i, NX and e.

(c) How much does the AD curve shift to right (the horizontal shift in AD) if G increases by one unit?

(d) How much would AD shift (again the horizontal shift) in response to a unit increase in G if this were a closed economy (NX=0 at all times)? How much would it shift if the economy were open to trade (NX=100-0.1Y+0.5e) but the exchange rate was fixed at some given level (say at e=50)? Interpret your findings. What do you learn about the effectiveness of fiscal policy in open/closed economies and under fixed/floating exchange rates?