1. Suppose the price of a given type of compact disk is $15 in Madison and is 1500 yen in Tokyo. According to PPP theory, what does this imply for the equilibrium nominal exchange rate?

2. Suppose that it costs the equivalent of $1.00 to ship a compact disk from Madison to Tokyo or vice versa. In this case, what does the economic logic behind the theory of PPP imply for the nominal exchange rate given the compact disk prices in question 1?

3. Describe how a reduction in the nominal exchange rate affects the IS/LM equilibrium.

4. How is it possible C+I+G to exceed the level of output produced in the United States? Does the US get something for nothing when this happens?