

Do not write your name on the assignment. Write your name only on the back of this sheet of paper and staple your answers on the front of this sheet of paper. Failure to follow these directions will cost you 1 point on the assignment.

1) (20 points each) Illustrate the following events on the AD/LRAS/SRAS diagram. Explain why the curve(s) moved as drawn. State what happens to inflation and GDP in both the long and short run. Do each part on a separate graph.

- A) Canada's GDP increases.
- B) Income taxes go up.
- C) Technology improves.

2) (10 points) Explain why the following statement is wrong. "When the price level goes up, that means that all prices increase on average. People cannot afford to buy as much when all prices go up, so they buy less. That is why the AD curve slopes down."

3) (15 points) Why does Say's law imply that the LRAS is vertical?

4) (15 points) Why should desired savings equal desired investment?