Wilfrid W. Csaplar Jr. Principles of Macroeconomics
Review Sheet for Exam 3, Review Sheet for the final, and non-graded assignment #8A

This review sheet is intended to cover everything that could be on the exam. However, it is possible that I may have inadvertently overlooked something. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones on the homework assignments, and possibly a few definition questions. I am more likely to ask questions that make you use definitions rather than have you recite them. I may take a question from the book.

I will hold the optional review session for this test will be on Wednesday 11/19 at 8:45 in 109 Old Main. (I have not reserved the room yet, but I should be able to get it.) The review sessions for the two parts of the final will probably be held on Monday, 12/8 and Wednesday, 12/10 respectively.

Chapter 13:
What is fiscal policy? What should the government do with taxes and spending if there is an inflationary gap or a recessionary gap? Show those actions on the LRAS/SRAS/AD diagram. What are the drawbacks of doing fiscal policy, for example, crowding out investment and lags? Why are these problems? What is the Laffer Curve and why does it matter? What is Ricardian Equivalence and why should it hold? Note that Ricardian Equivalence, the size of crowding out and lags are often debated among economists. What are automatic stabilizers? What determines the size of the government deficit/surplus? How does a deficit differ from the debt? Ignore the appendix.

Chapter 14:
Why should money be a good medium of exchange, unit of account, store of value, and standard of deferred payment? What is meant by liquidity? What backs our money? Know what is in M1, M2, and M3. You only have to know the items in them that the book mentions, and M3 is M2 plus large time deposits. (There are other parts of M2 and M3 that the book leaves out.) Know the properties of each item in them. Know what happens when we move money between them. Hints: Do not forget that M1 is in M2 and M2 is in M3. Unless you are making a loan, then M3 doesn't change. What is financial intermediation? What are adverse selection and moral hazard? Do not worry about what each organization in Table 14-2 does. Ignore pages 333 - 336. What is the Federal Reserve? What does it do? What are its tools? How do they affect the money supply? (That is covered in more detail in chapters 15 and 16.)

Chapter 15:
What are reserves? How do we calculate required reserves? It's 10% of checkable deposits, a.k.a., demand deposits. What goes on each side of the balance sheet of a bank? What are open market operations and how do they affect the balance sheet of the bank? Ignore the balance sheet of the Fed. How does the money supply change? What is the reason the money can grow 10 times the original bond purchase? What is the formula for the money multiplier? Why is it too large? How does the discount rate affect the money multiplier? Note that if I ask about "the multiplier" it is the autonomous expenditure multiplier I will be referring to. If I mean the money multiplier, then I will specify it. What does the FDIC do? How does moral hazard affect the FDIC?

Chapter 16:
What determines the demand for money? What are transaction, precautionary, and asset demand for money? Be able to move the MS and MD curves. Ignore the S/D for bonds. Illustrate the effects of monetary policy on LRAS/SRAS/AD diagram. Understand why MV=PY. Understand why monetarists do not like monetary policy. (This is the lags from chapter 13 again, but they are of different lengths than they were there.) Why can't the Fed choose to set both interest rates and the money supply?

Review Sheet for the two parts of the final.

The second half of the final will be just like the first half of the final for the last two semesters. It will be the same except you will have different numbers. I would use a Keynesian, but not extreme Keynesian, approach to solve the problem because it is easier to solve problems in a Keynesian world. (That does not mean that Keynes is right.) Chapter 17, up to page 405 will be helpful.

The first part of the final will be held the last day of class. It will cover the material that is not directly covered by the second half of the final. For example, I will not ask you to show an increase in the money supply on the LRAS/SRAS/AD diagram. Anything on any review sheet that is not explicitly covered in part 2 of the final is fair game. For example, question #1 below would not be on the first half of the final, but the other questions could be on the first half of the final.

When I write the final, I look to see what I did not ask about, and what were the major topics. I write questions about those topics. (Obviously, opportunity costs and supply/demand will be on the first half of the final.) I try to get the questions evenly distributed from all the tests. However, the second half of the final covers much of the material for test 3 and some from test 2. Therefore, most of the material for the first half of the final will be on material from test 1, with some questions from the other material covered.

Non-graded assignment #8A to be covered with assignment #8.

1) (30 points) Illustrate the effects of the Fed's purchase of bonds on the LRAS/SRAS/AD and MS/MD diagrams. Explain why the curves moved as drawn.

2) (15 points each) Illustrate the following events on separate MS/MD diagrams. Explain the movement(s) of the curve(s). Use M1 for the money supply.
A) Credit cards become more common.
B) Stocks are predicted to make more money.

3) (20 points) Explain why the money multiplier is 10. Is the real-world money multiplier greater than, less than, or equal to 10? Why?

4) (20 points) Explain why moral hazard is a problem for the FDIC.