

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. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to follow these directions will cost you 1 point on the assignment.

1) (20 points) There are two key assumptions in the classical model which lead to the conclusion that the LRAS curve is the same as the SRAS curve. State those assumptions and explain how they give that result.

2) (15 points) Explain why $S = I$ is a logical assumption.

3) (20 points) Draw the Keynesian SRAS curve and explain why it takes that shape.

4A) (25 points) Prior to the great depression, most economists were classical economists. Use the classical SRAS/AD diagram to explain why they felt changing government spending would not affect the economy.

4B) (20 points) When the government borrows, that reduces the savings available to be borrowed. Show that on the S/I diagram. Explain why the curve(s) moved as drawn. (Your answers to Parts A and B show why the US Government cut spending at the beginning of the great depression.)