

Place your name on the back of this sheet of paper and nowhere else. Staple your answers on the front of this sheet of paper. Failure to follow these directions will cost you 1 point. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to type it will cost you 10 points. If you use double-sided printing or print on the back of scrap paper, I will give you one additional point.

- 1) (25 points) Draw the LRAS/SRAS/AD diagram for an economy in a recessionary gap. Explain how you know it is a recessionary gap. Illustrate what happens if the economy is left alone. Explain why the curve(s) moved as drawn. What happens to GDP and inflation?
- 2) (25 points) Draw the LRAS/SRAS/AD diagram for an economy in an inflationary gap. Explain how you know it is an inflationary gap. What should the government do during such times? Why? Illustrate what that government action would do to the graph. Explain why the curve(s) moved as drawn. What happens to GDP and inflation?
- 3) (15 points) Some people say that because of Ricardian Equivalence, the Bush/Obama stimulus package will not have an effect upon the economy. Explain their logic.
- 4) (15 points) I feel that crowding out is a major problem with a large government deficit/debt. What is it, and why is it so harmful to the economy?
- 5) (20 points) What are the “lags” in policy and why might they mean counter-cyclical fiscal policy may be counter productive?