Wilf Csaplar Jr. Economics 162 Homework #8 Due Friday 11/5

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 45° diagram, a.k.a. Keynesian Cross diagram. Illustrate an increase in government spending. Explain why the curve(s) moved as drawn. Given your diagram, what is the size of the government spending multiplier? Explain how you reached that conclusion.

2) (15 points) When calculating the government spending multiplier, we made several assumptions. For example, we assumed no income tax. How would relaxing that assumption affect the size of the multiplier? Explain your logic.

3) (5 points) Suppose the MPC is .80. Given our simple form of the government spending multiplier, how much would GDP increase if the government spent $1000? Explain how you reached that conclusion.

4) (20 points each) For each of the following, explain what the term means and how it would affect the size of the government spending multiplier.
A) Crowding out
B) Direct expenditure offset

5) (15 points) What are the automatic stabilizers? Why do they have that name? I.e., how do they stabilize the economy?