

Place your name on the back of this sheet of paper and nowhere else. Staple your answers face up 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.

Note that unlike past years, I am covering Chapter 12 before Chapter 10.

- 1) (25 points) Draw the Keynesian Cross, a.k.a.  $45^\circ$  diagram. Illustrate an increase in government spending. Explain why the curve(s) moved as drawn. What happens to GDP? Given your diagram, what is the size of the government spending multiplier? Explain how you reached that conclusion.
- 2) (20 points) Draw the Keynesian Cross, a.k.a.  $45^\circ$  diagram. Illustrate an increase in marginal propensity to consume. Explain why the curve(s) moved as drawn. What happens to GDP?
- 3) (20 points) Draw the Keynesian Cross, a.k.a.  $45^\circ$  diagram. Illustrate an increase in the interest rate. Explain why the curve(s) moved as drawn. What happens to GDP?
- 4) (10 points) How can an increase in government spending of \$100 cause GDP to increase by more than \$100?
- 5) (15 points) In class we estimated that the government spending multiplier was 10. We made some assumptions. What did we assume about net exports? If we relax that assumption, what happens to the size of the multiplier? Explain your logic.
- 6) (10 points) If a person's consumption is given by  $C = 500 + .9(Y-T)$  and that person has an after-tax income of \$20,000.00, then how much is their average propensity to consume? Show all work and briefly explain what you did.