

Write your name on the cover of the test booklet and nowhere else. Failure to follow these directions will cost you 1 point. The test has 100 points (to be scaled up to 160 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 14-point question should take 7 minutes. I can give some extra time, but not much because of the class which follows yours.

1) (12 points) Answer EITHER Part A OR Part B.

A) Why do movements in the production possibilities frontier (production possibilities curve) cause movements of the long-run aggregate supply curve?

B) Why do movements of the long-run aggregate supply curve cause movements of the short-run aggregate supply curve?

2) (12 points) Answer EITHER Part A OR Part B.

A) Prior to our invasion of Iraq, it was basically a closed economy. Now it is an open economy. Based solely on that information, will Iraq grow slower or faster now than it did in the past? Explain your logic.

B) The war in Iraq has destroyed a large amount of capital and the near anarchy has been a discouragement to companies who might want to invest in Iraq. Given just this information, do you think Iraq will grow faster or slower in the future? Explain your logic.

3) (14 points) For EITHER the aggregate demand curve, OR the Keynesian short-run aggregate supply curve, draw the curve and explain why it takes that shape.

4) (14 points) Answer EITHER Part A OR Part B.

A) What are two negative effects of growth of per capita real GDP? Explain how economic growth causes those problems.

B) Suppose the consumption function is given by $C = 50 + 0.9Y$. (There are no taxes.) If a person has \$1000 worth of income, then what is that person's MPC, MPS, APC, and APS? Show all work, or explain how you got the numbers if no work is done.

5) (20 points) Answer EITHER Part A OR Part B.

A) Illustrate an increase in the value of the US\$ on SRAS/AD/LRAS diagram for the USA. Explain why the curves moved as drawn. What is the net effect upon the price level and GDP? What is the economic reason for that net effect?

B) Both the book and the review sheet say that a sales tax will not affect the SRAS/LRAS/AD diagram in the same manner as an income tax. Illustrate both taxes on the same diagram and explain why the effects are different.

6) (28 points) Illustrate EITHER the event in Part A OR the event in Part B on both the SRAS/LRAS/AD diagram and the Keynesian Cross (45°) diagram. Use the **same event for both graphs** and explain why the curves moved as drawn. What happens to GDP and the price level? What are the economic reasons for the changes in GDP and the price level?

A) The marginal propensity to consume increases.

B) Interest rates increase.