

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. 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 10-point question should take 5 minutes. I cannot give extra time because of the class which follows yours.

1) (10 points) Answer EITHER Part A OR Part B.

A) We say that economic growth is good. However, it may not be. Other than pollution, explain a problem caused by economic growth and how growth causes it.

B) What can the government do to get real GDP per capita to grow? Explain how that action will have the desired effects.

2) (10 points) Answer EITHER Part A OR Part B.

A) If the consumption function is given by $C = 100 + 0.9Y$ and the person earns \$10,000, then what are his MPC, MPS, APC, and APS? Do the same for a woman earning \$20,000.

B) Even though our model says the marginal propensity to consume is the same for all income groups, it does not say that the average propensity to consume is the same for all income groups. What does it predict about the average propensity to consume and what is the economic reason for predicting that?

3) (12 points) For EITHER the Keynesian SRAS curve OR the AD curve, draw the curve and explain why it takes that shape.

4) (12 points) For EITHER *limiting protectionism* OR *letting creative destruction run its course*, explain why that will help the economy develop.

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

A) Draw an SRAS/LRAS/AD diagram for a country in a recessionary gap. State how you see the recessionary gap on the diagram. Illustrate what will happen to automatically correct the problem, assuming the government does nothing. Explain why the curve(s) moved as drawn. What happens to the variables on the axes?

B) Draw an SRAS/LRAS/AD diagram for a country in equilibrium. Illustrate a *negative supply shock*. Explain what a *negative supply shock* is and why it moved those curves as drawn. What happens to the variables on the axes?

6) (36 points) Answer EITHER Part A OR Part B.

A) Illustrate a decrease in the marginal propensity to consume on BOTH the SRAS/LRAS/AD diagram and the Keynesian Cross, a.k.a. the 45° diagram. Explain why the curve(s) moved as drawn. What happens to the level of GDP and the price level? Explain the economic reason for the change.

B) Illustrate an improvement in technology on BOTH the SRAS/LRAS/AD diagram and the Keynesian Cross, a.k.a. the 45° diagram. Explain why the curve(s) moved as drawn. What happens to the level of GDP and the price level? Explain the economic reason for the change.