

Do not put your name anywhere on the assignment, other than on the back of this sheet of paper. 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 do double-sided printing or print on the back of scrap paper, I will give you one additional point.

Note that if I do not specify which SRAS curve to use, use the “modern” one.

1) (20 points each) Illustrate the following events on the LRAS/SRAS/AD diagram. Explain why the curve(s) moved as drawn. What happens to GDP and the price level?

- A) The government spends even more on the war.
- B) A new technology allows firms to produce more.
- C) The price of oil increases.

2) (15 points) Draw the “modern” SRAS curve. Explain why it takes its shape, including explaining why the two sections are called the “Keynesian” and “Classical” sections.

3) (25 points) Do you think that the Keynesian or Classical model makes the more realistic assumptions for the US economy? Explain your logic. Zimbabwe’s official inflation rate is now 1700% (and some think it is actually double that) and its GDP is almost stagnate. Which model is more realistic for that economy? Explain your logic.