

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 some students have a class after your class.

1) (10 points) For EITHER *creative destruction* OR *limiting protectionism*, how does that promote economic growth?

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

A) Why does an increase in government spending of \$1000 cause GDP to increase by much more than that? Explain your logic.

B) Which is larger, the MPC or the APC? Explain your logic.

3) (10 points) Answer EITHER Part A OR Part B.

A) What is wrong with this statement, "When the price level increases, people cannot afford to buy as much, so there is less demanded. That is why AD slopes down."?

B) What is the real reason the AD curve slopes down?

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

A) Explain two reasons why real GDP per capita may not be a good measure of how well off the economy is.

B) What are two negative aspects of economic growth? Explain how economic growth causes them.

5) (16 points) Answer EITHER Part A OR Part B.

A) Draw an SRAS/LRAS/AD diagram in an inflationary gap. Show how the curve(s) will move if the government does nothing. Explain how you know there is an inflationary gap and why the curve(s) moved as drawn.

B) Draw an SRAS/LRAS/AD diagram at full employment. Given an example of a positive supply shock and illustrate it on the diagram. Explain why the curve(s) moved as drawn.

6) (40 points) Answer EITHER Part A OR Part B.

A) Draw an SRAS/LRAS/AD diagram and a Keynesian Cross, a.k.a. 45° diagram, for an economy in at full employment. Suppose the minimum wage increase also causes all wages to increase. Illustrate that on both diagrams and explain why the curves moved as drawn. What happens to the GDP and to the price level?

B) Draw an SRAS/LRAS/AD diagram and a Keynesian Cross, a.k.a. 45° diagram, for an economy at full employment. Illustrate an increase in the MPC. Explain why the curves moved as drawn. What happens to the GDP and to the price level?