

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

The review session will be Sunday at a time to be determined, in the normal room (I hope).  
You will be given a pair of equations and asked to explain one of them.

Chapter 6: What causes economic growth? How do we measure  $A$ ? For the Solow Growth Model, be able to draw the per-worker production function. Understand what moves it. How do we find  $k_G$  (the “golden rule” capital-labor ratio),  $k_{\max}$  (the maximum capital-labor ratio), and  $k^*$  (the equilibrium capital-labor ratio)? Why is the latter at the point where  $sf(k)$  crosses  $(n+d)k$ ? What moves those two lines? Why does the economy automatically move towards  $k^*$  and why is that not necessarily at  $k_G$ ? Understand the economic reasons for the changes in  $k$  that the diagram predicts. For endogenous growth theory, understand why they assume  $Y=AK$  and why  $\Delta Y/Y = sA - d$ . What government policies affect “ $s$ ,” “ $A$ ,” and “ $d$ ”? (Nothing the government does really affects  $d$ .) Why do they have those effects? (They can be seen on pages 238 - 240.) For this chapter, it is crucial that you remember the differences between small and CAPITAL letters. Remember that small letters are rates, ratios, or fractions. Do NOT use them interchangeably with capital letters.

Chapter 7: What are the three functions of money? What are in  $M1$ ,  $M2$ , and  $M3$ ? Why do we have more than one definition of money? How does the central bank affect the money supply? What determines which type of assets you want? (Expected return, risk, and liquidity) What determines the demand for money? (Price level, real income, interest rates, wealth, and the properties of other assets.) The summary on page 257 should be a big help. What is the quantity theory of money? Why should the velocity of money be constant? Why hasn't  $M1$ 's velocity been constant? Why is the inflation rate dependent upon the growth of money and the growth of GDP

Chapter 8: What do the following terms mean: aggregate economic activity, expansions, boom, contraction, recession, depression, peak, trough, business cycle, comovement, recurrent but not periodic, and persistent? Why have business cycles become longer and less severe since World War II? Why are some economists uncertain about that statement? What determines if a variable is procyclical, countercyclical, or acyclical? What are lagging, leading, and coincident variables? If I gave you a variable, you should be able to determine which type of variable it is and the economic reason for that. Understand why the SRAS/LRAS/AD diagram takes its shape and what moves them. I mentioned two reasons for AD Curve's slope. One of the reasons is the one from Chapter 9 when the AD Curve is derived from the IS/LM/FE diagram.

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This is the non-graded Assignment #7A that will be gone over with Assignment #7.

1) (15 points each) For each of these variables, determine if the variable moves pro-cyclically, counter-cyclically, or a-cyclically. Then determine if it is a leading, lagging, or coincident variable. Explain your logic.

- A) Duration of unemployment.
- B) Stock prices

2) (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) Government spending increases
- B) Population increases.
- C) The price of oil increases.

3) (10 points) Explain the AD curve takes its shape.