

Place your name on the back of this sheet of paper and nowhere else. 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 use double-sided printing or print on the back of scrap paper, I will give you one additional point.

1) (20 points) On the diagram with policies on the axes and plotting internal balance and external balance, explain why the IB curve slopes up. Explain why being up/left of both curves is labeled “unemployment, surplus.”

2) (10 points) Why is it false to say “the AD curve slopes down because at higher prices, we cannot afford to buy as much.”

3) (20 points each) Illustrate the following events on the SRAS/LRAS/AD diagram for a closed economy. Explain why the curve(s) moved as drawn. What happens to prices and GDP?

A) Government spending increases.

B) Money supply increases.

C) The price of oil increases.

4) (10 points) Why does this the SRAS curve take its shape?