Wilf Csaplar Jr.   Economics 162   Homework #7   **Due Friday 4/3**

Place your name on the back of this sheet of paper and nowhere else. Staple your answers face up 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) Draw the Keynesian Cross, a.k.a. 45° diagram. Illustrate the effects of an increase in government spending. Explain why the curve(s) moved as drawn. What happens to the equilibrium level of GDP? <u>Given your diagram</u>, what is your estimate for the value of the government spending multiplier? Explain your logic and show all work.

2) (15 points each) For each of the following, explain what we assumed about that variable when we estimated the government spending multiplier. If we relaxed that assumption, what happens to the size of the government spending multiplier? Explain your logic. Answer each part in separate paragraphs.
A) income tax revenue
B) prices

3) (20 points) Draw the SRAS/LRAS/AD diagram with the SRAS which slopes up. Illustrate the effects of an increase in government spending. Explain why the curve(s) moved as drawn. What happens to the price level and real GDP?

4) (20 points) Draw the SRAS/LRAS/AD diagram with the SRAS which slopes up. Illustrate the effects of an improvement in technology. Explain why the curve(s) moved as drawn. What happens to the price level and real GDP?

5) (10 points) What is wrong with this logic? "When prices go up, people cannot afford to buy as much. That is why AD slopes down."