

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 10 points. 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) (35 points) Explain what is meant by *crowding out*. Why does it make counter-cyclical fiscal policy less effective? Use an SRAS/LRAS/AD diagram with an economy starting in a recessionary gap to explain your logic. Is it occurring now? Explain your logic.

2) (20 points) What is meant by *Ricardian Equivalence*? Explain why it would make counter-cyclical fiscal policy ineffective. Like all macroeconomic theories, sometimes it accurately describes the economy but at other times it does not. Do you believe the theory holds most of the time or not? Explain your logic.

3) (20 points) What are the *automatic stabilizers*? Explain why they are called that and how they stabilize the economy.

4) (25 points) What are the *lags* in fiscal policy. Use an appropriate graph to explain why they may mean you do not want to do counter-cyclical fiscal policy.