Wilfrid W. Csaplar Jr., Ph.D. Economics 202 Exam #3 2023/11/16

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 150 points (to be scaled up to 210 points) and is scheduled to take 75 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I will give some extra time, but not much.

1) (10 points) Answer EITHER Part A OR Part B.
A) Give an example of one of the “automatic stabilizers”. Explain why it has that name.
B) Give an example of a “supply shock”. Explain why it has that name.

2) (12 points) For EITHER the “Key for Development” in Part A OR the “Key for Development” in Part B, state what that means. Explain how that helps a country to develop.
A) Creative destruction
B) Enforcing property rights.

3) (14 points) For EITHER the problem in Part A OR the problem in Part B, explain why that my make counter-cyclical fiscal policy either less effective, ineffective, or counterproductive. Do you feel it is a strong argument? Explain your logic.
A) lags
B) crowding out

4) (14 points) For EITHER the problem in Part A OR the problem in Part B, explain how the debt could cause that problem. Then tell me which debt, gross public debt, net public debt, or Paul O’Neill’s debt, is most likely to cause that problem. Explain your logic.
A) It limits what the government can spend in the future.
B) It causes problems for our foreign policy.

5) (16 points) For EITHER the event in Part A OR the event in Part B, illustrate the effects of that on the 45° (Keynesian Cross) diagram. Explain why the curve(s) moved as drawn. What happened to GDP?
A) Congress spends more.
B) The MPC decreases.

6) (18 points) For EITHER the event in Part A OR the event in Part B, illustrate the effects of that on the LRAS/SRAS/AD diagram. Explain why the curve(s) moved as drawn. What happens to GDP, inflation, and the unemployment rate in the USA?
A) An earthquake destroys a large number of buildings.
B) The government increases the income tax rate.

7) (18 points) Answer EITHER Part A OR Part B.
A) Suppose the government’s tax revenue is T = .2Y, the government spending is \$800, and government transfers are TR = 700 - .1Y. If GDP is \$6000, then how much is the budget deficit or surplus? If the full employment GDP is \$4000, how much is the full-employment deficit or surplus? For both parts show all work and conclude your answers with either, “The deficit is...” or “The surplus is...” Is the government doing good fiscal policy? Explain your logic.
B) The current unemployment rate in the USA is 3.9%. The most recent government budget deficit is

5.4% of GDP. Is the full-employment deficit larger or smaller than the actual deficit? Explain your logic. The two schools of thought have different ideas on what the full-employment budget should be now. What are do the two schools say about whether it should be balanced, a surplus, or a deficit? Explain your logic.
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8) (18 points) Answer EITHER Part A OR Part B.
A) Draw the SRAS/LRAS/AD diagram showing a recessionary gap. Explain how the economy would get back to equilibrium if there was <u>no</u> government action. Explain why the curve(s) moved as drawn. What happens to GDP, inflation, and the unemployment rate? Remember, the government does nothing.
B) Draw the SRAS/LRAS/AD diagram starting at full employment. Illustrate the effects of an increase in the price of electricity. Explain why the curve(s) moved as drawn. What happens to GDP, inflation, and the unemployment rate?

9) (30 points) For EITHER the event in Part A OR the event in Part B, illustrate the even on both the LRAS/SRAS/AD diagram and the 45° (Keynesian Cross) diagram. Explain why the curves moved as drawn. What happens to GDP, inflation, and the unemployment rate in the USA?
A) Interest rates increase (JP Morgan/Chase has increased them a lot since 2020.)
B) The OECD predicted that the Canadian GDP would fall in 2023. Draw the diagram for the USA if the prediction comes true.