

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 100 points (to be scaled up to 160 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I cannot give extra time because some students have a class after your class.

1) (12 points) Answer EITHER Part A OR Part B.

A) We estimated that the government spending multiplier is 10. However, we assumed that there is no income tax. What would happen to the size of the multiplier if there was an income tax?

B) If your income is \$1000 and your consumption function is given by $C = 30 + 0.9Y$, then how much are your MPC and APC? Show all work and briefly explain what you did.

2) (12 points) Answer EITHER Part A OR Part B.

A) Why is savings important for economic growth?

B) Why does the Classical SRAS Curve look as we drew it? (The Classical section of the Modern SRAS Curve takes its shape for the same reason.)

3) (12 points) Answer EITHER Part A OR Part B.

A) What is meant by *limiting protectionism* and how does that help a country develop?

B) What are two problems caused by faster GDP growth? Explain how faster GDP growth causes them.

4) (18 points) Answer EITHER Part A OR Part B.

A) Illustrate an increase in marginal propensity to consume on the 45° , aka Keynesian Cross, diagram. Explain why the curve(s) moved as drawn. What happens to GDP?

B) Illustrate an increase in the value of the dollar on the foreign exchange market on the 45° , aka Keynesian Cross, diagram. Explain why the curve(s) moved as drawn. What happens to GDP?

5) (20 points) Answer EITHER Part A OR Part B.

A) According to a UN document I have, the Democratic Republic of Congo's real GDP per capita using PPP is \$281. Why is that probably underestimating the output of the country? Give at least two reasons. What is meant by "using PPP"?

B) Each year, Johan typically does all his own landscaping and yard work. He spends \$200 per year on mulch for his flower beds, \$225 per year on flowers and plants, \$50 on fertilizer for his lawn, and \$245 on gasoline and lawn mow maintenance. It takes him 100 hours to do all this work each year. If he could earn \$10/hour at work, what is the total cost of his yard work? How much does he contribute to GDP each year? Show all work and briefly explain your answers to each part.

6) (22 points) Answer EITHER Part A OR Part B.

A) Illustrate an decrease in the income tax rate on the SRAS/AD/LRAS diagram. Explain why the curve(s) moved as drawn. What happens to inflation and GDP?

B) Illustrate an increase in the price of gasoline on the SRAS/AD/LRAS diagram. Explain why the curve(s) moved as drawn. What happens to inflation and GDP?