

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) When we calculated the government spending multiplier using algebra, we got 10. However, when we used the graph to calculate it, we got numbers ranging from 1.5 to 3. Why are they so different?

B) Why is saving important for economic growth.

2) (14 points) Answer EITHER Part A OR Part B.

A) Suppose you save \$10 now and it averages earning 5% per year. How much will you have in 28 years? How much will you have in 42 years? Show all calculations. (Hint, the calculations are quite simple.) Why is the second number a lot more than the first number?

B) How do patents help the economy to grow? Explain your logic.

3) (14 points) Answer EITHER Part A OR Part B.

A) When going from NI to PI, we added or subtracted several things. What are TWO things we added or subtracted. Explain why we added or subtracted them.

B) In the equation for calculating GDP, what is X? It is something minus something. What is added and what is subtracted? Explain why we add and subtract those two items.

4) (14 points) For EITHER creative destruction OR limiting protectionism, explain how that helps the government to develop.

5) (14 points) Answer EITHER Part A OR Part B.

A) In class we estimated that the government spending multiplier was 10. We made some assumptions. What did we assume about the price level? If we relax that assumption, what happens to the size of the multiplier? Explain your logic.

B) If a person's consumption is given by $C = 2000 + .8(Y-T)$ and that person has an after-tax income of \$20,000, then how much is their average propensity to consume, average propensity to save, marginal propensity to consume, and marginal propensity to save? Show all work and briefly explain what you did. If there is no work, state how you found it.

6) (16 points) Answer EITHER Part A OR Part B.

A) Draw the Keynesian Cross, a.k.a. 45° diagram. Illustrate the effects of a decrease in the income tax rate. Explain why the curve(s) moved as drawn.

B) Draw the Keynesian Cross, a.k.a. 45° diagram for the USA. Illustrate the effects of a decrease in Canada's GDP. Explain why the curve(s) moved as drawn.

7) (16 points) Answer EITHER Part A OR Part B.

A) Draw the LRAS/AD diagram. Illustrate the effects of an improvement in technology. Explain why the curve(s) moved as drawn. What happens to real GDP and the price level?

B) Explain TWO of the three reasons why the AD curve slopes down.