

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

**The review session for the first half of the final will be at a time to be determined, probably 12/6.**

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### **Review Sheet for the two parts of the final.**

The two parts of the final will be in the same order as the last few years. **The second half of the final** will be just like the second half of the final for the last semester. (However, I may slightly change the manner which I assign points or improve the wording.) If I were you, I would use a Keynesian, but not extreme Keynesian, approach to solve the problem because it is easier to solve problems in a Keynesian world. (That does not mean that Keynes is right, just easier to deal with.) For the second half of the final, you will probably want to practice showing policy on the SRAS/LRAS/AD diagram, 45° diagram, and the MS/MD diagram **at the same time**. Make sure that GDP goes the same direction in the two diagrams with it on the X-axis. **The second half of the final is open book and notebook.**

**The first part of the final** will be held during the last class. It will cover the material that is not directly covered by the second half of the final. For example, I will not ask you to show an increase in the money supply on the LRAS/SRAS/AD diagram. Anything on any review sheet that is not explicitly covered in Part 2 of the Final is fair game. This part of the final is closed book and closed notes, just like all other tests. Obviously, the material since Exam #4 will be on the first half of the final.

When I write the final, I look to see what I did not ask about, and what were the major topics. I write questions about those topics. (Obviously, opportunity costs and supply/demand will be on the first half of the final.) I try to get the questions evenly distributed from all the tests. However, the second half of the final covers much of the material for Tests #3 and #4 and after #4. Therefore, much of the material for the first half of the final will be on material from Tests #1 and #2, with some questions from each of the other tests' material.

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In the past, some of this material was on Exam #4, so you may want to look at old Exam #4.

Chapter 15: Why should money be a good **medium of exchange, unit of account, store of value, and standard of deferred payment**? What is meant by **liquidity**? What backs our money? Know what is in **M1** and **M2**, but not **M3**. You only have to know the items in them that the book mentions. (There are other parts of **M2** and **M3** that the book leaves out.) Know the properties of each item in them. Know what happens when we move money between them. *Hints: Do not forget that M1 is in M2. Unless you are taking a loan, then M2 doesn't change.* What is **financial intermediation**? What are **adverse selection** and **moral hazard** and why are they a problem? Do not worry about what each organization in Table 15-2 does. What is the **Federal Reserve**? What does it do? What are its tools? How do they affect the money supply? (That is covered in more detail in Chapter 16 after the test.) The

map of the Federal Reserve Districts incorrectly has us in the Richmond District. We are in the Cleveland District. Do not worry about the balance sheets or the money multiplier. What is the **FDIC**? How does it result in moral hazard and adverse selection? Ignore the rest of the chapter.

Chapter 16: What determines the demand for money? What are transaction, precautionary, and asset demand for money? Be able to move the **MS** and **MD** curves. Ignore the S/D for bonds. Illustrate the effects of **monetary policy** on LRAS/SRAS/AD diagram. Understand why **MV=PY**. Understand why **monetarists** do not like monetary policy. (This is the lags from Chapter 13 again, but they are of different lengths than they were there.) Why can't the Fed choose to set both interest rates and the money supply?

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This is the non-graded Assignment #9A that will be reviewed on 12/6.

- 1) (40 points) Illustrate the results of the Fed buying bonds on the LRAS/SRAS/AD diagram and on the MD/MS diagram. Explain why the curves moved as drawn. What happened to GDP, interest rates, and the price level?
- 2) (20 points) Use the supply and demand for money to explain why no central bank can control both interest rates and the money supply. (Of interest, if the central bank wants to control the exchange rate, then it cannot control either the interest rates or the money supply.)
- 3) (20 points) Use the SRAS/LRAS/AD diagram to explain the neutrality of money.
- 4) (20 points) Illustrate the effects of an increase in the GDP on the MS/MD diagram. Explain why the curve(s) moved as drawn. What happens to the quantity of money and the interest rate?