

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) (15 points) My sister e-mailed a question. She wrote, “Massachusetts has a question on adding a tax for anyone over 1 million income. I was wondering what affects that might have on economy.” You will want to think about one of two things. First, how much revenue will it bring in? Second, how will people respond? You only need to answer one of those questions and explain how you reached your conclusion. You should note, most people in Massachusetts live in the metropolitan Boston area. All of them live within a two hour drive of New Hampshire, and most live less than an hour from New Hampshire. A large percentage of the rest of the people in the state are also within an hour drive of New Hampshire. I found the following information online: New Hampshire has no tax on earned income, and their 5% tax on interest and dividends is being phased out.

<https://www.revenue.nh.gov/assistance/tax-overview.htm#interest>

2) (20 points) Draw the SRAS/LRAS/AD diagram. Illustrate the effects of the recent increases in oil prices. Explain why the curve(s) moved as drawn. What happens to real GDP, inflation, and the unemployment rate?

3) (25 points) Draw the SRAS/LRAS/AD diagram starting with high unemployment. State how you know the unemployment rate is high. Illustrate the effects of the economy’s self correction mechanism. Explain why the curve(s) moved as drawn. What happens to real GDP, inflation, and the unemployment rate?

4) (25 points) The most recent unemployment numbers for the USA, has the unemployment rate at 3.5%. Draw the SRAS/LRAS/AD diagram which corresponds to that unemployment rate. Explain how your graph shows that unemployment rate. What is the best fiscal policy? Illustrate those effects on the graph. Explain why the curve(s) moved as drawn. What happens to real GDP, inflation, and the unemployment rate. <https://www.bls.gov/news.release/pdf/empsit.pdf>

5) (15 points) Counter-cyclical fiscal policy, especially expansionary, **may** not work. One of the reasons it may not work is Ricardian Equivalence. Explain how that may preventing it from working. Do you believe that is what happens normally? Explain your logic.