

Write your name on the cover of the test booklet and nowhere else. 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 14-point question should take 7 minutes. I cannot give extra time because there are classes after yours.

1) (10 points) Answer EITHER the question in Part A OR the question in Part B.

A) Why have the business cycles become less severe since World War II?

B) Define co-movement and explain why it is important to business cycles.

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

A) In this case, you will give two explanations for the same curve. When written in different forms, there are different explanations. Explain $r = \alpha_{IS} - \beta_{IS}Y$. Only explain Y. Also explain it as

$Y = \alpha_{IS} - \beta_{IS}r$. Explain only r.

B) Explain $r = \alpha_{LM} - \left(\frac{1}{l_r}\right)\left(\frac{M}{P}\right) + \beta_{LM}Y$. Only explain M, P, and Y.

3) (14 points) For EITHER the curve in Part A OR the curve in Part B, draw that curve. Explain why it takes the shape.

A) The LM curve.

B) Aggregate demand.

4) (16 points) Answer EITHER Part A OR Part B.

A) Illustrate an increase in the liquidity of non-monetary assets on the real money supply/demand diagram. Explain why the curve(s) moved as drawn.

B) Draw the LRAS/SRAS/AD diagram. Illustrate how the curves will move if the US\$ gains value on the foreign exchange market. Explain why the curve(s) moved as drawn.

5) (16 points) For EITHER the variable in Part A OR the variable in Part B, explain the economic theory as to whether it is pro-cyclical, counter-cyclical, or a-cyclical. Explain the economic theory as to whether it is leading, coincident, or lagging.

A) Stock prices

B) Real wage

6) (28 points) Answer EITHER Part A OR Part B.

A) Use the real money supply/demand diagram and the SRAS/LRAS/AD diagram to prove that the only variable affected in the long-run by a money supply increase is the price level.

B) Use the IS/LM/FE diagram to derive the AD curve.

7) (54 points) Illustrate EITHER the event in Part A OR the event in Part B on the IS/LM/FE diagram, SRAS/LRAS/AD diagram, and the real money supply/demand diagram. Use the SAME event in all THREE graphs. Explain why the curve(s) moved as drawn. Only worry about the short-run events. You can draw the SRAS curve with a slight upward slope.

A) The wealth of the country increases.

B) There is an improvement in technology.