

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) (10 points) Answer EITHER Part A OR Part B.

- A) The press has made many in the past month like, "The food shortages in most of the world, especially wheat, have been caused by the increased use of corn-based ethanol in the USA." Explain the economic reasoning.
- B) Use economic reasoning to explain why you should not "pull and all-nighter" the night before an exam.

2) (10 points) Answer ONE of the following three parts. Yes, that is ONE out of three.

- A) Explain how economic growth can be bad for a country.
- B) Why is savings important for economic growth?
- C) How can limiting protectionism help the economy grow faster?

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

- A) Draw a PPF (PPC) for capital goods (new machines) versus consumption goods. Use it to explain why we would have to consume less now if we wanted to have a larger GDP in the future.
- B) Draw the supply and demand for a good which causes a positive externality. Explain how your graph shows a positive externality and explain why we do not produce the optimal amount of the good. **Do NOT worry about trying to solve the problem.**

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

- A) People have predicted that the price of rice will be higher next year. Illustrate the effect of that prediction on the supply and demand for rice. Explain why the curve(s) moved as drawn. What happens to the quantity sold and the price?
- B) Draw the supply and demand diagram for college educations. Illustrate what happens when salaries of professors increase. Explain why the curve(s) moved as drawn. What happens to the price and quantity sold?

5) (16 points) Answer EITHER Part A OR Part B.

- A) Illustrate an increase in the amount of labor on the SRAS/LRAS/AD diagram. Explain why the curve(s) moved as drawn. What happens to prices and GDP?
- B) Illustrate an increase in the marginal propensity to consume on the Keynesian cross, a.k.a. 45° diagram. Explain why the curve(s) moved as drawn.

6) (16 points) Answer ONE of the following three parts. Yes, that is ONE out of three.

- A) In the second part of the final, we will assume that direct expenditure offsets do not occur. What are they? Why is that an important assumption?
- B) If $MV=PY$, then explain why some economists feel the only long-run effect of an increase in the money supply is greater inflation? (Ignore this argument in the second part of the final.)
- C) Use a diagram to explain why lags could cause either monetary or fiscal policy to have undesirable effects. Make sure you explain what the lags are.

7) (18 points) Answer EITHER Part A OR Part B.

- A) What is the problem facing Social Security? How would raising the retirement age reduce the problem? Would you use that to solve the problem? Explain your logic.
- B) What is meant by the expenditure method of calculating GDP? What is meant by the value added method of calculating GDP? Why should they give the same answer?