

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 170 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) Explain EITHER the equation in Part A OR the equation in Part B.

A)  $r = \alpha_{LM} - (1/\ell_r)(M/P) + \beta_{LM} Y$  Explain only the (M/P) and Y.

B)  $M^d/P = \ell_0 + \ell_Y Y - \ell_r(i)$ . Explain only Y and i.

2) (12 points) For ONE of the following, determine if it is a-cyclical, pro-cyclical, or counter-cyclical. Also determine if it is a leading, lagging, or roughly coincident variable. Explain your logic.

A) Nominal interest rates

B) Productivity of labor

C) Inventory investment

D) Consumer debt

3) (12 points) Answer EITHER Part A OR Part B.

A) Why does the AD Curve slope downward?

B) Why is it hard to tell when a recession ended?

4) (18 points) Answer EITHER Part A OR Part B.

A) Draw the LRAS/SRAS/AD diagram for an economy with an unemployment rate which is too low. Explain how you know it is too low. Illustrate what happens over time and explain why the curve(s) moved over time.

B) Draw the IS/LM/FE diagram. Illustrate the effects of an increase in prices. Explain why the curve(s) moved as drawn.

5) (48 points) Answer EITHER Part A OR Part B.

A) Draw the LRAS/SRAS/AD, IS/LM/FE, and the real MS/real MD diagrams. Illustrate the effects of the government increasing government spending. Explain why the curves moved as drawn. What happens to GDP, inflation, unemployment rate, and the interest rate? State how you reached those conclusions. Assume Ricardian Equivalence does not exist.

B) Draw the LRAS/SRAS/AD, IS/LM/FE, and the real MS/real MD diagrams. Illustrate the effects of the Federal Reserve buying more bonds on the open market. Explain why the curves moved as drawn. What happens to GDP, inflation, unemployment rate, and the interest rate? State how you reached those conclusions.