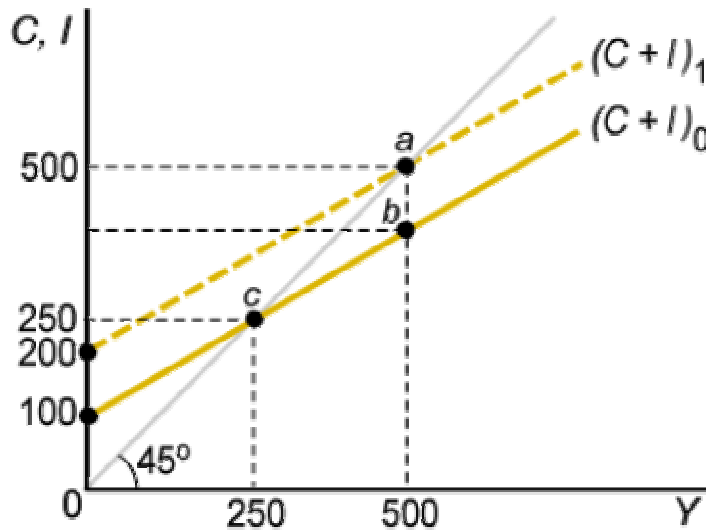


Final Exam

Time: 90 minutes (11:00 -13:00)

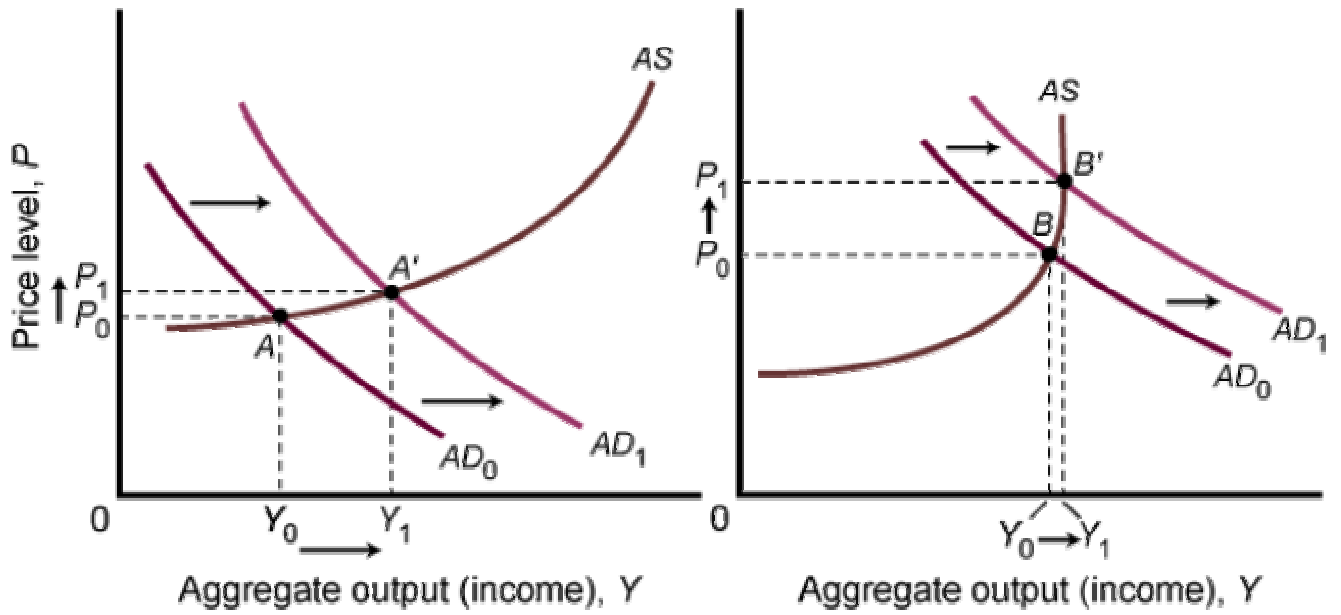
Part A. Multiple Choice Questions (3 points each)

1. Refer to the graph below. What is the value of the marginal propensity to save (MPS)?



- a. 1.5
 - b. 1.66
 - c. 0.4
 - d. 0.6
2. If input prices changed at exactly the same rate as output prices, then
- a. The aggregate demand curve would be vertical
 - b. The aggregate supply curve would be vertical
 - c. The aggregate demand curve would be horizontal
 - d. Aggregate supply would always equal aggregate demand
3. If the Central Bank wants to decrease the money supply, it will:
- a. Buy government securities in the open market
 - b. Buy gold
 - c. Increase the reserve requirement
 - d. Decrease the discount rate

4. Refer to the graphs below. Expansionary policy works better when the economy looks more like:

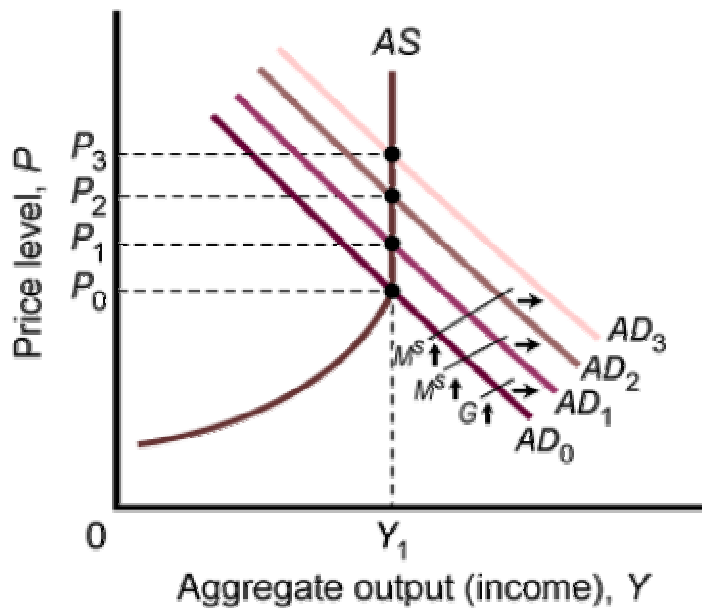


- a. the graph on the left
- b. the graph on the right
- c. either graph
- d. neither graph

5. Fill in the blanks. When income goes up, the demand for money _____ and the interest rate _____.

- a. rises; rises
- b. falls; falls
- c. rises; falls
- d. falls; rises

6. Refer to the graph below. Which of the terms below *best* describes the problem illustrated



by this graph?

- a. Stagflation
- b. Hyperinflation
- c. Stagnation
- d. Cost-push inflation

7. Which of the following is an expression for the budget surplus?

- a. $T - Y$
- b. $C + I + G$
- c. $T - G$
- d. $C + S + T$

8. Which of the following is most likely to cause an increase (shift to the right) in both the long-run and short-run aggregate supply curves?

- a. an increase in the size of the national debt
- b. an increase in marginal tax rates
- c. a decline in the economy's rate of capital formation
- d. an increase in labor productivity

9. Assuming that G , T , and M^s remain the same, the impact of an increase in the price level on the economy can be described as follows:

- a) $\uparrow P \rightarrow \downarrow M^d \rightarrow \uparrow r \rightarrow \downarrow I \rightarrow \downarrow AE$
- b) $\uparrow P \rightarrow \uparrow M^d \rightarrow \uparrow r \rightarrow \downarrow I \rightarrow \downarrow AE$
- c) $\uparrow P \rightarrow \downarrow M^d \rightarrow \downarrow r \rightarrow \uparrow I \rightarrow \uparrow AE$
- d) $\uparrow P \rightarrow \uparrow M^d \rightarrow \uparrow r \rightarrow \uparrow I \rightarrow \uparrow AE$

10. The effect of *contractionary monetary policy* is as follows:

- a) $\downarrow M^s \rightarrow r \downarrow \rightarrow I \uparrow \rightarrow Y \downarrow \rightarrow M^d \uparrow$
- b) $\downarrow M^s \rightarrow r \uparrow \rightarrow I \downarrow \rightarrow Y \downarrow \rightarrow M^d \uparrow$
- c) $\downarrow M^s \rightarrow r \uparrow \rightarrow I \downarrow \rightarrow Y \downarrow \rightarrow M^d \downarrow$
- d) $\downarrow M^s \rightarrow r \uparrow \rightarrow I \downarrow \rightarrow Y \uparrow \rightarrow M^d \uparrow$

Part B. Problems and Essay Questions

1. (20 points) Assume an economy with only two goods in a two period framework.

	2005		2006	
	Quantity	Price	Quantity	Price
Good A	1000	12 YTL	1500	8 YTL
Good B	2000	10YTL	2000	12 YTL

a. What is nominal GDP in 2005?

b. What is nominal GDP in 2006?

c. What is the real GDP growth rate from 2005 to 2006?

d. What is the GDP deflator (change in overall price levels) if the base year is 2005?

2. Suppose that the government of Lumpland is enjoying a budget surplus with fixed government expenditures of $G = 200$ and fixed taxes of $T = 100$. Assume that the consumers of Lumpland behave according to the following consumption function: $C = 100 + 0.75(Y-T)$. Suppose further that investment spending is fixed at 200.

a. (5 points) Calculate the equilibrium level of GDP. (Hint: At equilibrium $GDP = Y = AE = C + I + G$)

b. (5 points) Calculate the equilibrium levels of Consumption (C) and Saving (S).

c. (5 points) Assume that the Congress of Lumpland increases taxes by 100 to a new fixed level of 200. Recalculate the equilibrium level of GDP either by using the tax multiplier or by using $Y = AE$ equation.

d. (5 points) What are the new equilibrium levels of Consumption (C) and Saving (S).

e. (10 points) Draw the AE graph and show the effect of the tax hike. Label the both axes, show where the AE curve intersects the y-axis and the 45-degree line both at the old and at the new equilibrium.

3. (20 points) By using AS and AD curves to illustrate your points, discuss the impacts of the following events on the price level and on equilibrium GDP (Y) in the short-run

a. A tax cut holding government purchases constant with economy operating at near full capacity

b. An increase in the money supply during a period of high unemployment and excess industrial capacity

Bonus (5 points): Who is the former chairman of FED (i.e. US Central Bank)?