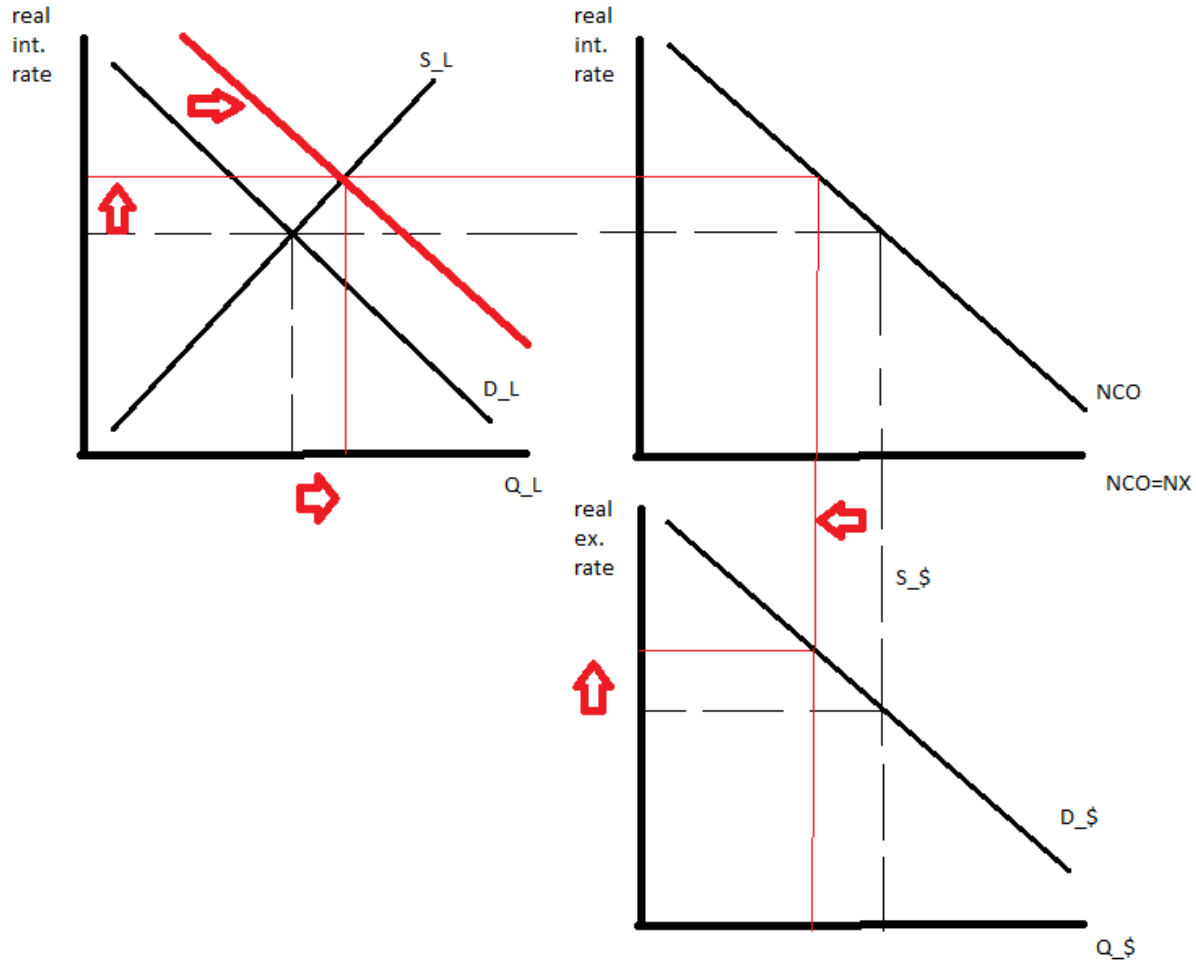
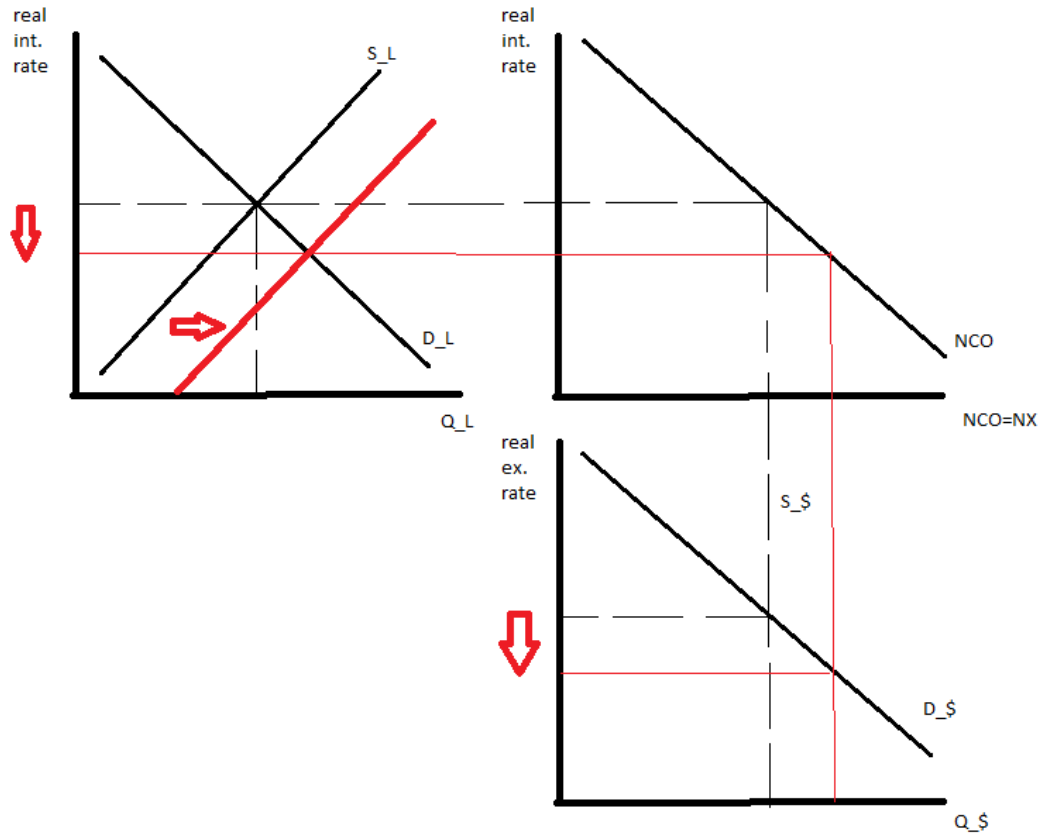
1. The increase in the SRAS curve can happen due to an increase in A, K, L, HC, N or an *expected* increase in those productive factors. A would probably reduce the expectation of N and decrease SRAS. B sounds pretty good. C would likely reduce L and shift in the SRAS. D would be occur with a decrease in Y and an increase in P (which is the exact opposite of what is given in the graph). (B)

2. Now we see stagflation as we move from the SR equilibrium to the LR equilibrium. P increases and Y decreases. (C)

3. Hooray graphs! (A)

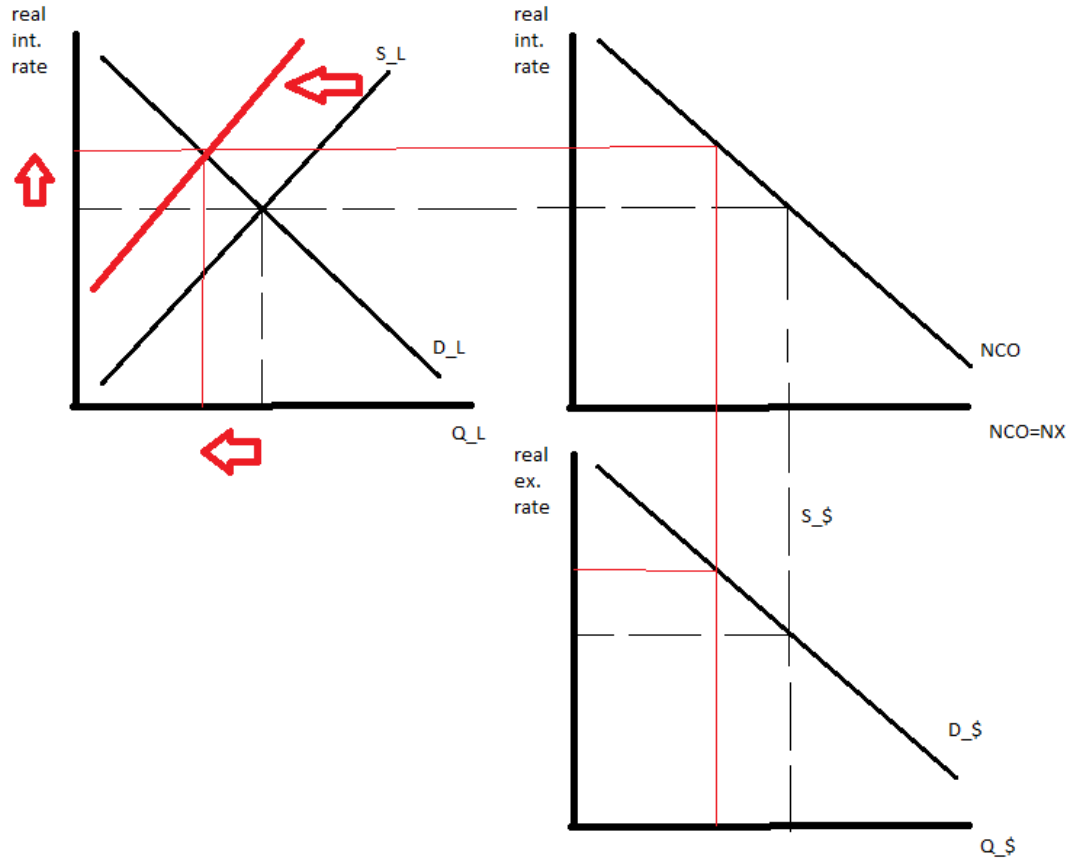


4. Oh fun! Another graph! To make NX go up we must have the real interest rate fall. First, imposing an import quota would merely increase the demand for $. That would impact the real exchange rate but not NX=NCO. To make NX=NCO increase we need the real interest rate to fall. A decrease in the budget deficit would increase the S_L and thus lower the real interest rate. (B)

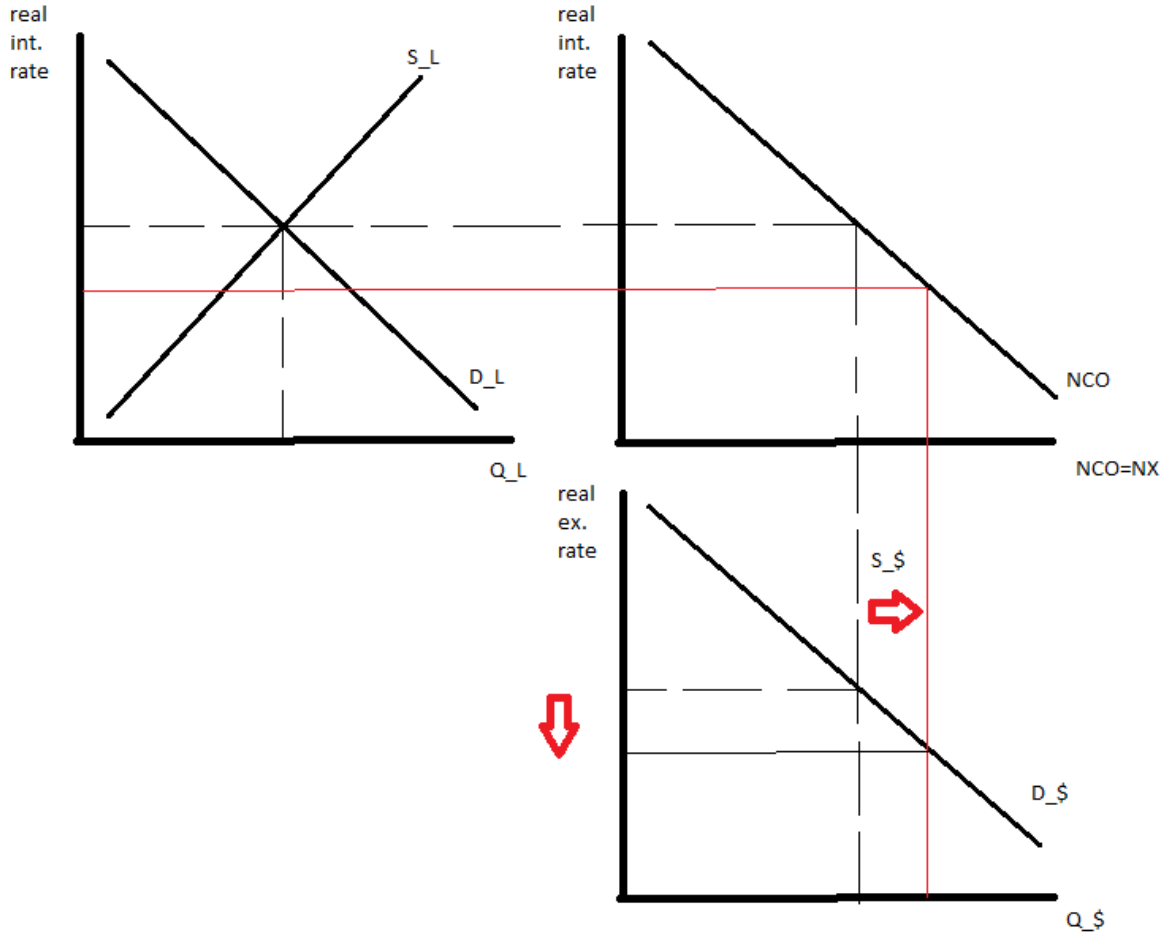


5. The technical definition of a recession (B)

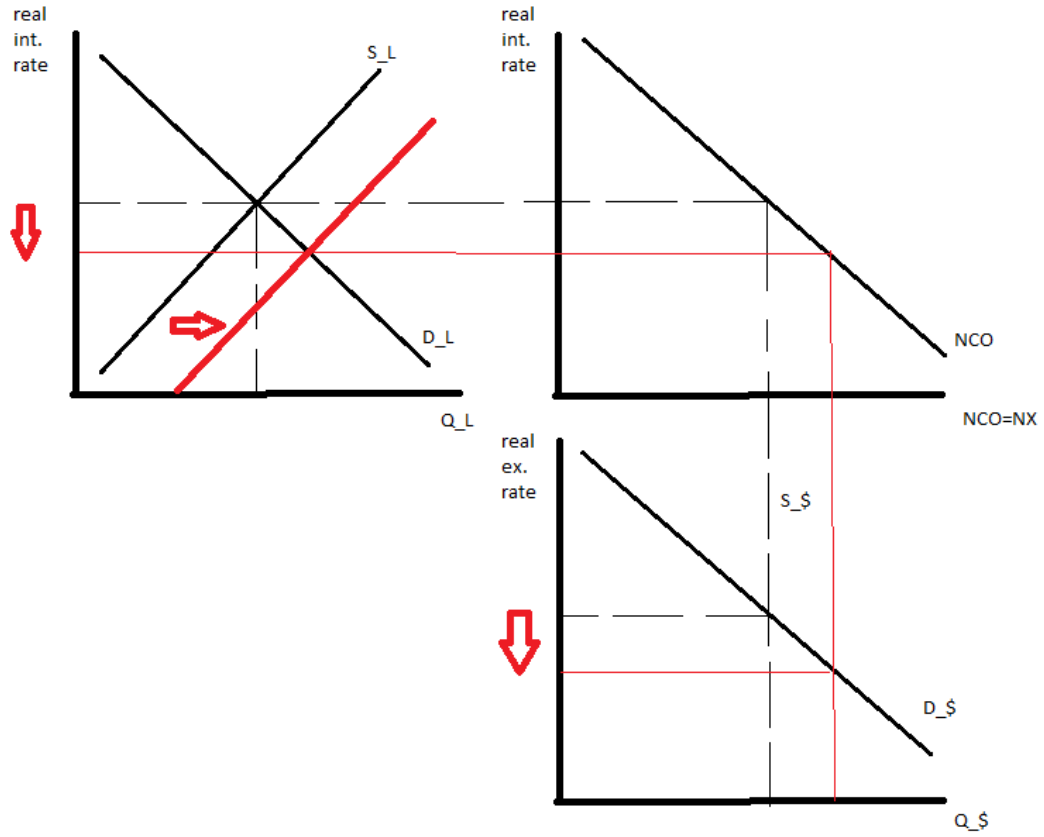
6. Graphs, again! (D)



7. You've got to be kidding, right? Another graph?(A)

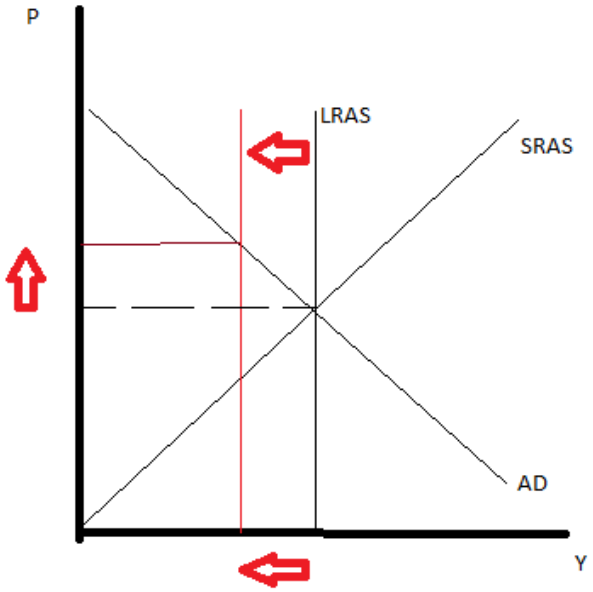


8. Have a look at the graph for #7. NX and NCO goes up. (C)
9. Investment is highly correlated with GP growth. C, G and NX aren't as cyclical. (C)
10. If the country increases its budget deficit then the Supply of loanable funds decreases. GRAPH TIME! In fact, have a look at the graph for #6. (B)
11. A and C move the AD curve outwards while B moves the AD curve inwards. (D)
12. Graph TIME! (B)



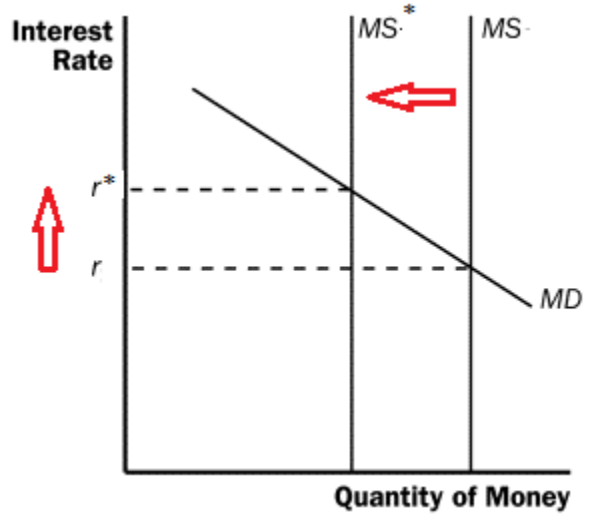
13. The very definition of PPP. Yeah, you know me! (B)
14. NCO = Net Capital Outflows which represents the US Dollars heading overseas to buy portfolio assets and physical assets (foreign direct investment). This is the Supply of $ as shown in the open economy macroeconomic model. (B)

15. Hmmm… stagflation means stagnant economic growth (or a recession) and an increase in the price level. You can graph all four options (which would be fun) but the correct answer is below. (D)



16. Wait, isn't this just the graph for #12? Yes, it is! Here's the thing… the open economy macroeconomic model has four lines that can either increase or decrease. That's only eight possible outcomes. (D)

17. First, the money supply falls as we move from MS to MS*. The interest rate increases which means that Investment would likely fall and the AD curve shifts inwards. (D)

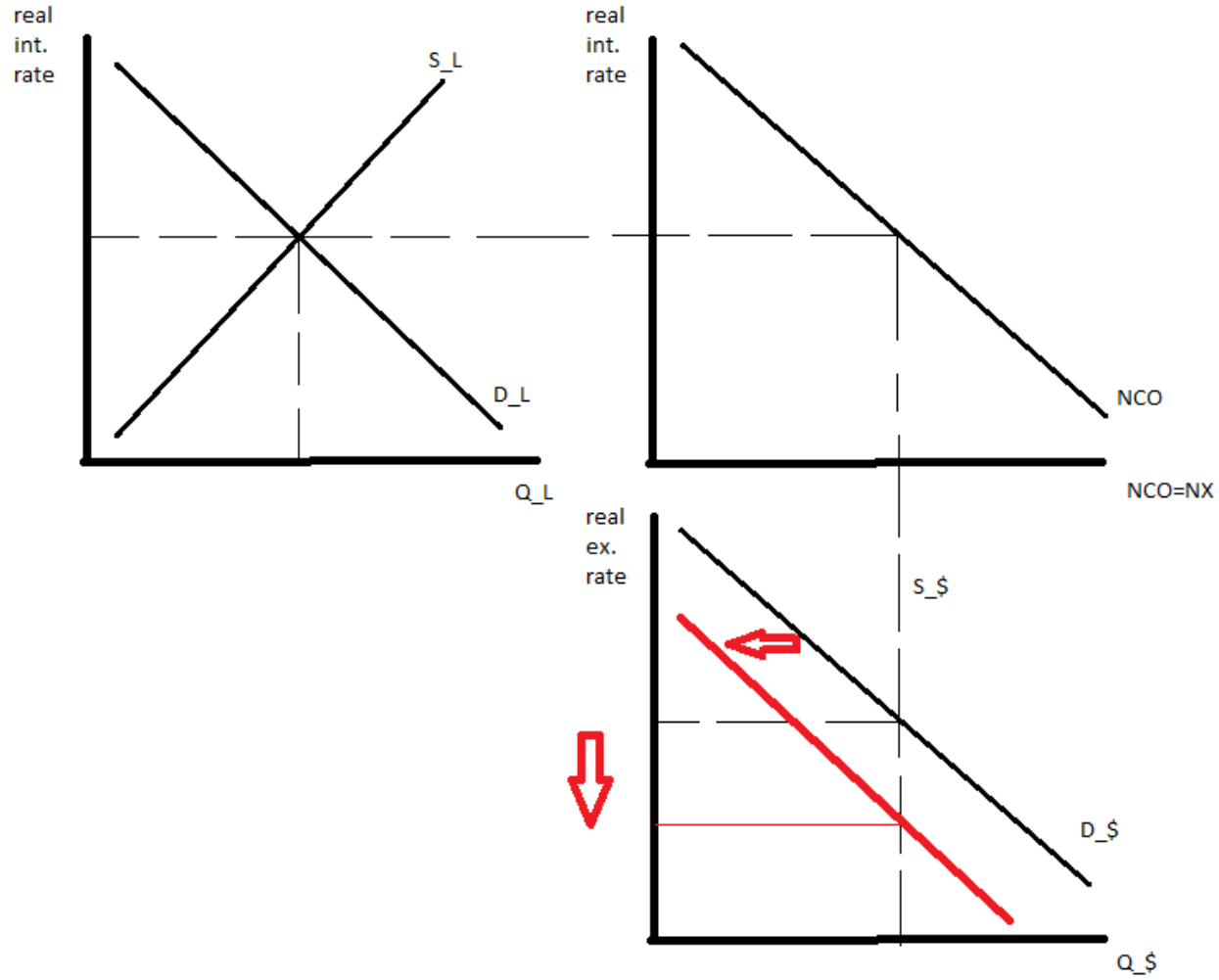


18. A decline in net exports would shift the AD curve inwards. To stabilize the economy the Fed would want to shift the AD curve back outwards by increasing the money supply. To increase the money supply the Fed needs to lower interest rates which is possible by buying bonds or lowering the fed funds rate and discount rate. (B)

19. A is the opposite of true. B sounds pretty good because investment is highly correlated with GDP growth. C isn't true because recessions are typically associated with DECLINES in GDP not just subpar growth. D is also the opposite of true. (B)

20. A would be more associated with a movement from b to a. B isn't true either; if the AD curve shifts from AD1 to AD2 then the short run equilibrium is at point b but the long run equilibrium is at the intersection of the AD curve and the LRAS. C is correct; a decrease in money supply (monetary policy), an increase in taxes (fiscal policy) or a decrease in gov't spending (fiscal policy) would cause the inward shift in the AD.

21. If the interest rate increase then you can make a higher return by keeping money in the bank instead of holding cash. So the opportunity cost of holding cash is greater when the interest rate goes up. As people hold less cash the quantity of money demanded falls. (B)
22. From notes. The exact definition. (B)
23. A is associated with net exports so its included in the demand for dollars. Both B and C are associated with net capital outflows not the demand for dollars. (A)
24. Exactly how to shift out the demand for dollars (A)
25. To get LR economic growth we need the LRAS to shift outwards. A and B would shift out the AD curve but only C would shift out the LRAS as investment leads to more capital equipment. (C)
26. Phew, I was worried we were done graphing. (D)



27. From the quantity theory of money we know that changes in the money supply only impact nominal variables not real variables. Output and unemployment rates are real but prices are nominal. (A)
28. I'm playing change the word to make the statement true. See the underlined word to find out what changed.
A.An increase in the money supply causes the interest rate to decrease so that aggregate demand shifts <u>right.</u>
B. <u>A decrease</u> in stock prices reduces consumption spending so that aggregate demand shifts left.
C. An increase in the price level causes the real exchange rate to rise <u>and the rest of this statement is garbage</u>.
D. All GOOD.
(D)
29. This one should be easy. Changes in AD can impact both output and P. (D)

30. This one is not easy. More teller machines means that shoeleather costs will fall and people will hold less cash and more money will be held at the bank. If there's more money in the bank then it gets multiplied by the money multiplier effect so that money supply increases. The increase in the money supply also increases AD. (B)