



# Macroeconomics Unit 3 Study Guide

## National Income and Price Determination

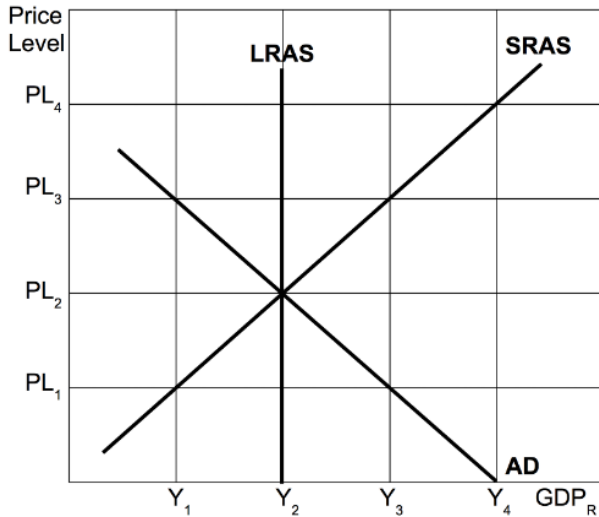
Topic 3.1- Aggregate Demand (AD) ▶	Topic 3.2- Multipliers ▶																																									
1. What is the difference between a market demand curve and the aggregate demand curve?  2. What three concepts explain why aggregate demand is downward sloping?  3. What are the shifters of aggregate demand?	1. What is the multiplier effect?  2. Define marginal propensity to consume (MPC).  3. Define marginal propensity to save (MPS).  4. Equation for the simple spending multiplier.  5. Equation for the tax multiplier.  6. <i>Fill in the blanks below:</i>																																									
Topic 3.3- Short-run Aggregate Supply (SRAS) ▶	1. Why is short-run aggregate supply upward sloping?  2. What are the shifters of short-run aggregate supply?																																									
Topic 3.4- Long-run Aggregate Supply (LRAS) ▶	1. Why is long-run aggregate supply vertical?																																									
	<table border="1"> <thead> <tr> <th>Initial Change</th> <th>Initial Amount</th> <th>MPC</th> <th>Maximum Change</th> <th>Initial Change</th> </tr> </thead> <tbody> <tr> <td>↓ G</td> <td>\$30 billion</td> <td></td> <td>↓\$60 billion</td> <td>↓ G</td> </tr> <tr> <td>↑ C</td> <td></td> <td>.9</td> <td>↑\$200 billion</td> <td>↑ C</td> </tr> <tr> <td>↓ Taxes</td> <td>\$10 billion</td> <td>.8</td> <td></td> <td>↓ Taxes</td> </tr> <tr> <td>↑ I</td> <td></td> <td>.75</td> <td>↑\$80 billion</td> <td>↑ I</td> </tr> <tr> <td>↑ M</td> <td>\$10 billion</td> <td>.9</td> <td></td> <td>↑ M</td> </tr> <tr> <td>↑ X</td> <td>\$10 billion</td> <td></td> <td>↑\$50 billion</td> <td>↑ X</td> </tr> <tr> <td>↑ Transfer Payments</td> <td>\$20 billion</td> <td>.9</td> <td></td> <td>↑ Transfer Payments</td> </tr> </tbody> </table>		Initial Change	Initial Amount	MPC	Maximum Change	Initial Change	↓ G	\$30 billion		↓\$60 billion	↓ G	↑ C		.9	↑\$200 billion	↑ C	↓ Taxes	\$10 billion	.8		↓ Taxes	↑ I		.75	↑\$80 billion	↑ I	↑ M	\$10 billion	.9		↑ M	↑ X	\$10 billion		↑\$50 billion	↑ X	↑ Transfer Payments	\$20 billion	.9		↑ Transfer Payments
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Topic 3.5- Equilibrium in the AD-AS Model ▶																																										
1. Draw an economy with a negative output gap	2. Draw an economy at full employment	3. Draw an economy with a positive output gap																																								



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### Topic 3.6- Changes in the AD-AS Model in the Short Run ▶



Use the graph to the right to answer the following questions (assume that each event takes places independently)

1. What is the short-run equilibrium price level and output?
2. Identify the short-run equilibrium price level and output if consumption increased?
3. Identify the short-run equilibrium price level and output after a negative supply shock?
4. What happens to output and unemployment if investment falls?
5. Use the graph to explain the difference between demand-pull and costs-push inflation.

6. What is a negative supply shock?

7. What is a positive supply shock?

8. Define stagflation.

9. Define deflation.

10. What is autonomous consumption?

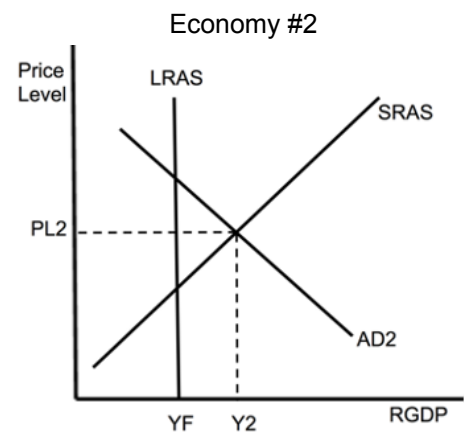
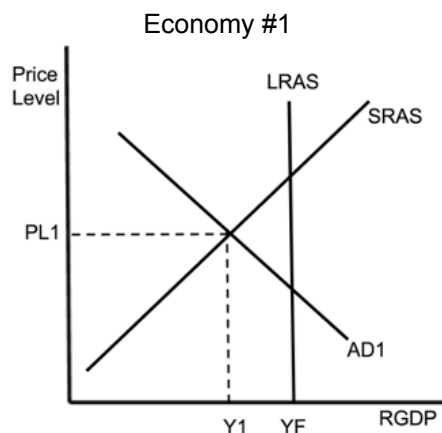
11. What is disposable income?

### Topic 3.7- Long-run Self-Adjustment ▶

1. Explain how the economy self-adjusts in the long run when there is a negative output gap.

2. Explain how the economy self-adjusts in the long run when there is a positive output gap.

3. Assuming wages and resource prices are flexible, show how each economy below will self-adjust in the long run.



4. Assume instead that Economy #2 experiences economic growth. What happens to LRAS and output?

5. Does the natural rate of unemployment increase, decrease, or stay the same when the LRAS shifts right?



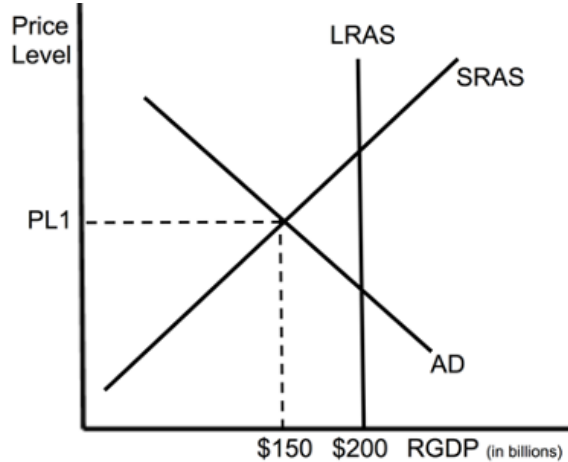
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### Topic 3.8- Fiscal Policy ▶

- |  |   |
|--|---|
| 1. Define expansionary fiscal policy.<br><br>2. Define contractionary fiscal policy. | 3. Explain why an increase in government spending will lead to more total spending than a decrease in taxes by the same amount. |
|--|---|

Use the graph to answer the questions to the right. Assume wages and resource prices are flexible.



4. Is there a recessionary gap or inflationary gap?
5. What happens to price level and output in the long run if no policy action is taken?
6. Assume instead that the government decides to use fiscal policy. Identify two policies that could close the gap.
7. If the MPC is .5, what is the least amount of government spending that could close the gap?
8. If the MPC is .5, what is the least amount the government could cut taxes to close the gap?

### Topic 3.9- Automatic Stabilizers

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|--|--|
| 1. Define discretionary fiscal policy.<br><br>2. Define non-discretionary fiscal policy.<br><br>3. Identify three different examples of automatic stabilizers. | 9. Assume instead that the MPC is .9. What is the least amount of government spending that could close the gap?<br><br>10. Would an increase in private savings increase or decrease the effectiveness of fiscal policy?<br><br>11. Why are there lags when the government uses discretionary fiscal policy? |
|--|--|

### Unit Review

- True or False:*
1. An increase in expected inflation will decrease the short-run aggregate supply.
  2. An increase in interest rates will increase investment and aggregate demand.
  3. The spending multiplier is weaker than the tax multiplier.
  4. Fiscal policy includes government spending and taxation.
  5. If the MPS is .2 the tax multiplier is 4.
  6. When the MPC increases, the spending multiplier decreases.
  7. Jacob Clifford is very attractive.

Scenario	Change in AD or AS	↑ or ↓
8. Government uses expansionary fiscal policy		
9. No policy when there is a recession		
10. Government increases taxes on consumers		
11. There is a decrease in imports		
12. Positive output gap. Government takes no policy		