Instructions: There are two sections in this exam. Section A is compulsory. You have to choose two questions from a total of four in section B and answer them. Time allotted for the exam is one hour. This is a closed book/notes exam. Please show the details of your work if you wish to receive partial credit. Remember that the length of your answer is not a substitute for clarity. Only exams written in ink will be re-graded on request. Please do not forget to write your name on the answer booklet. Good luck!

Answers for Section A

1. D
2. C
3. C
4. C
5. C
6. A
7. A
8. A (But also give credit for answering B, as there may be some confusion regarding the exact meaning of the statements)
9. A
10. D
11. E
12. B
13. A
14. C
15. D
Answers for Section B

1. (a). \( C = 1 + 0.9(Y - 40) \)
   
   (Both 1 and 40 are in billion $: the answer is taken to be fully correct if it is either in the above form, even if the billion has not been written. Of course, writing the billion would make it exactly precise!)

(b). Equilibrium expenditure decreases by $100 billion (- $100 billion is also an acceptable answer. No points to be deducted if the dollar & billion are missing. If the answer is incorrect, but the student has put down the formula \( \Delta Y^* = (1/1-MPC) \Delta G \), then only 1 point is to be deducted).

(c). \( 1/(1-MPC) \) = 10 (Just 10 is also acceptable. If that is incorrect, then the formula needs to be there to earn 3 points).

(d). \(-MPC/(1-MPC) = -9 \) (Again, the correct answer earns full points. If that is incorrect, then the formula needs to be there to earn 3 points).

2. (a). The quantity of RGDP demanded goes up. The aggregate demand curve shifts rightward (or out/outward).

(b).

![Diagram of Aggregate Demand Shift](image)

Labeling each axis carries \( \frac{1}{2} \) a point each. Drawing AE 0 & AE 1 correctly carry \( \frac{1}{2} \) appoint each (there is no penalty for not labeling them as exactly AE0 & AE1, but there needs to be some indication that these are AE curves, and an upward shift has occurred. If there is no such indication, then \( \frac{1}{2} \) a point is to be deducted). Drawing the 45 degree line carries 1 point. Labeling points A & B correctly carry \( \frac{1}{2} \) a point each (it is also permissible to drop perpendiculars from the two points of intersection to the horizontal axis and label those points on the axis as A & B respectively).

(c). More than.

(d). No, it increases less. (Just answering ‘no’ earns 1 point)

(e). It would not. RGDP would remain at its potential level (constant/fixed).

(Any variation of this answer earns full points).

3. (a). Money is a commodity that acts as: A means of payment, a medium of exchange, a unit of account, and a store of value. (Important: mentioning any three of these four will earn the student the full 4 points).

(b). M1 increases by $1000. M2 remains unchanged.
(c). (i). Aggregate demand increases.
(ii). The price level rises & RGDP increases in the short run.
(iii). In the long run RGDP returns to potential level (it is also acceptable to say that in the long run RGDP remains constant at the potential level). Price level rises compared to the initial level by the same percentage as the percentage increase in money supply (as the Quantity theory holds in the long run for this economy).
(Any variation of the answer is ok: it is important to say that RGDP remains fixed, or at its potential level in the long run, and that price level increases. If the fact that percentage change in money supply & percentage change in price level is equal is not mentioned, then 1 point should be deducted).

4. (a). $1200
(b). $1200
(c). $(1 - \text{reserve ratio}) \times 1200 = 0.9 \times 1200 = 1080$ (if the final answer is not correct, then the formula needs to be there to earn partial credit of 2 points).
(d). $1200 + 0.9 \times 1200 + (0.9 \times 0.9) \times 1200 = 1200 + 1080 + 972 = $3252
(There could have been a possible confusion regarding the wording of this question, so if a student has answered either $0.9 \times 1200 + (0.9 \times 0.9) \times 1200 = 1080 + 972 = $2052$, or $1200 + 0.9 \times 1200 = 1200 + 1080 = $2280$ then give full credit also).
(e). $\left(\frac{1}{\text{reserve ratio}}\right) \times 1200 = 10 \times 1200 = $12000$ (in case the final answer is incorrect, the formula needs to be there to earn partial credit of 2 points)