

Econ. 1A. Quiz 11 (take home) Due: **in the beginning of final exam.**

Note:

- 1. Write your answer on other pieces of paper. Don't write on this text.**
- 2. Turn in your answer in the beginning of Final exam.**
- 3. Read our textbook, my note on AS-AD curve, and the two-page lecture note which I distribute in the last class of this semester.**

The AS-AD model is a powerful tool for understanding both economic fluctuations and the way economic policy can fight adverse shocks.

*Please use AD, AS, LRAS and UR line to answer the following question **verbally and graphically.***

- U.S. unemployment rate (UR) = 7.3% in Oct. 2013. On AS-AD-LRAS-UR graph show the macroeconomic equilibrium in U.S. in Oct.2013. Please show equilibrium Y , P , Y_p , UR and NUR explicitly. [4]
- Explain verbally and graphically what is inflationary gap? What is recessionary gap? [4]
- Is U.S.in Oct, 2013 facing a recessionary gap or inflationary gap? Explain your answer. [2]
- If US faces a recessionary gap, which type of **fiscal policy** would move this economy to full employment equilibrium (potential output)? What are some examples of such policies? Also show your answer graphically. State **the cause** and **the effect** explicitly. [6]
- In his radio address two years ago, President Obama claims

Government has to start living within its means, just like families do. We have to cut the spending (government purchase, G) we can't afford so we can put the economy on sounder footing, and (move back to full employment, i.e., $Y = Y_p$ and $UR = NUR$).

Based on U.S. economy in Oct. 2013, show the effect of Obama's proposal on equilibrium of Y , P , UR graphically. Also state **the cause** and **the effect** explicitly. [8]