INSTRUCTIONS:

1. Answer ONLY the specified number of questions from the options provided in each section. Do not answer more than the required number of questions. Each section takes one hour.
2. Your answers must be on the paper provided. No more than one answer per page. Do not answer two questions on the same sheet of paper.
3. If you use more than one sheet of paper for a question, write "Page 1 of 2" and "Page 2 of 2."
4. Write ONLY on one side of each sheet. Use only pen. Answers in pencil will be disqualified.
5. Write **------ END -----** at the end of each answer.
6. Write your exam identification number in the upper right-hand corner of each sheet of paper.
7. Write the question number in the upper right-hand corner of each sheet of paper.

Section 2: Macroeconomics and Monetary Theory—Answer One Question.

2A. (Econ 202) Answer all of the following parts completely. Be specific.

a) Draw a *dynamic* aggregate demand-aggregate supply (AD-AS) diagram correctly identifying both axes and all the curves.
b) In one sentence, describe what is the difference between the static and the dynamic version of the AD-AS model (noting that one is static and one is dynamic is NOT a correct answer).
c) What explains the slope of the aggregate demand curve in the AS-AD model?
d) What factors do each of the following schools emphasize regarding shifts in the demand curve:
   a. Pre Keynesian, Classical economists?
   b. Orthodox Keynesian economists?
   c. Real business cycle economists?

e) What are the difference and/or similarities between how Monetarist economists and New Classical economists would describe the short-run in change in output due to an aggregate demand shock?

f) Show on a diagram similar to the one you drew for part (a) how a negative shock to aggregate demand would affect the curves in both the short-run and long run.

g) Use the aggregate demand-aggregate supply model to portray what causes a recession according to real business cycle theory.

h) What theory of expectations does real business cycle theory depend upon? Identify and explain.

2B. (Econ 235) Answer all of the following parts completely. Be specific.

a) Does the Federal Reserve (Fed) actually control interest rates? If so, to what extent?
b) What is the short-run impact of an expansionary monetary policy on interest rates? What is this effect called, and why does it occur? Depict this short-run impact on a diagram of the loanable-funds market. Assume you are starting with a constant money stock and that the Fed engages in a one-shot increase in the money stock.
c) After the new money circulates throughout the economy, what happens to interest rates? What is this effect called, and why does it occur? Depict this impact on a diagram of the loanable-funds market.
d) Now assume that the Fed continues expanding the money stock at a constant rate. What is the impact on nominal interest rates? What is the impact on real interest rates? What is this effect called, and why does it occur? (You do not need to graph it.)
e) Why does the difference between short-term and long-term effects of monetary policy that you have described in parts (b), (c,) and (d) create problems for a monetary policy that targets interest rates?
f) Give the equation for the Taylor Rule. Clearly identify all variables and coefficients in the equation. What macroeconomic variables does the Taylor Rule try to stabilize? How does the Taylor Rule deal with the problems you described in part (e)?

(over)