Econ 331 - Study Guide for Test 2:

Chapter 8:
- the "who" of a policy (fiscal versus monetary);
- the "what" of a policy (monetary: OMO, FFR, AD-side of the economy)
- the "why" of a policy (long versus short run);
- the "when" of a policy;
- the "how" of a policy (example of a monetary policy: T-bills, banks reserves, MS);
- how a policy works (example of a monetary policy);
- the development of a policy (the works of a policy in reverse);

Chapter 9:
- $AD = C + I + G + NX$
- Unplanned inventory ($UI = Y - AD$, $UI > 0$, $UI < 0$);
- simple economy (no G, no NX), the consumption function;
- marginal propensity to consume, marginal propensity to save;
- budget constraint: $Y = C + S$;
- disposable income: $YD = Y - TA + TR$;
- $\bar{A}$ (and all the components of it);
- the expression for AD;
- the AD function and its graph (the vertical intercept; the slope), the current equilibrium;
- the multiplier effect (explanation, how to calculate the multiplier effect);
- how the multiplier effect changes if MPC changes;
- graphical representation of the multiplier effect;
- the consumption function with taxes and transfer payments;
- the updated AD function: the new expression and the graph for the AD function (different slope, why?);
- taxes and the multiplier (changes in the multiplier due to changes in tax rates);
- fiscal policy and its effect on AD function (graph) and the multiplier effect;
- difference between increase G and TR (different impact on Y – why?);
- **know how to do all the questions from HW2**;
- budget surplus versus budget deficit and full-employment budget surplus;

Chapter 10:
- investment spending function (the expression, all the components), what does it tell us?
- the slope of the function;
- derivation of the IS curve (four (4) graphs);
- what does the slope of the IS depend on?
- shifting the IS curve (to the right, to the left);
- the money market (the demand for liquidity function with all its components, its slope; the real supply of money and its slope);
- derivation of the LM curve (two (2) graphs);
- shifting LM (to the left, to the right);
- the complete IS-LM diagram;
- what is LM? what is IS?
- the equilibrium point in the IS-LM framework – what happens to the equilibrium when IS shifts? when LM shifts?

- derivation of the AD curve (two graphs);
- shifting of the AD curve (to the right, to the left);
- **know how to do all the questions from HW3**;

Chapter 11:
- monetary policy – which market/s it affects, the major tool used;
- expansionary monetary policy (explanation, IS-LM framework shift);
- contractionary monetary policy (explanation, IS-LM framework shift);
- transmission mechanism;
- the liquidity trap (the IS-LM framework showing the specific condition of the LM curve, explanation, other type of the liquidity trap);
- unorthodox monetary policy (latest financial crisis);
- the classical case for the LM curve (why we call it "classical case");
- fiscal policy: expansionary, contractionary (explanations, graphs);
- crowding out (explanation, the IS-LM framework);
- two extreme cases for the crowding out (flat LM, vertical LM – explanations, graphs);
- accommodating monetary policy (when, what does it mean?).