



AP[®] Macroeconomics 2002 Sample Student Responses Form B

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Write in the box the number of the question you are answering on this page as it is designated in the examination.

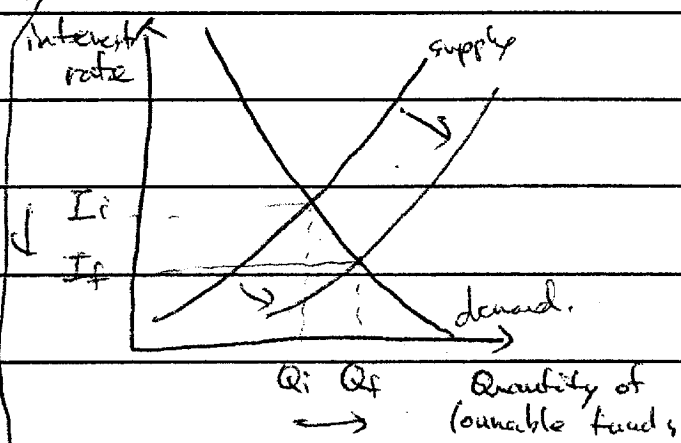
Question 2

2. a) By replacing income tax with national sales tax, the government is transferring the weight of taxes from ~~investment~~ ^{savings} to consumption.

i) There will be less consumption.

ii) There will be more ~~investment~~, National saving (Investment)

b) (loanable funds market)



i) Increases in savings ~~lowers~~ ~~the~~ increases the supply of loanable funds which decrease interest rates.

ii) Investment increases.

c) As investment ~~rise~~ increases, more capital accumulates resulting in a larger long-run economic growth.

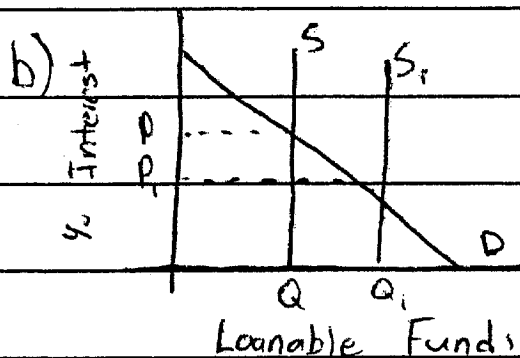
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2

a) i. There is an indeterminate effect on consumption.

This is because although disposable income increases the price of goods does so as well. Therefore, an individual may divert more money to savings instead of consumption.

ii. National saving increases as lower taxes mean more disposable income. Although the Mean Propensity to Save might remain constant there is a larger value of disp. income to save which would increase national savings.



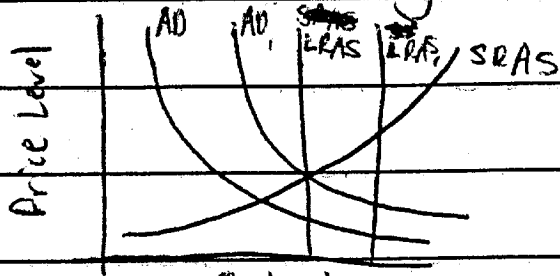
As the supply of money increases due to more disposable income, S shifts to the right to S_1 .

i. Due to this increase, the ~~investment~~ interest rate decreases from P to P_1 . Due to Fisher's law the real interest rate will decrease as well.

ii. Investment will increase as there is more chance that the investor will get a higher return, as compared to keeping the money in the bank with a low interest rate.

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c) In the long run:



In the long run AD will shift to the right to AD₁, as investment is a part of aggregate demand. However, Long Run Aggregate Supply will shift to the right from LRAS to LRAS₁, as companies invest more money in capital goods. These goods expand the potential of the country to produce goods and ^{therefore} shift LRAS to the right.