Problem 1. The difference between the short run and the long run is that

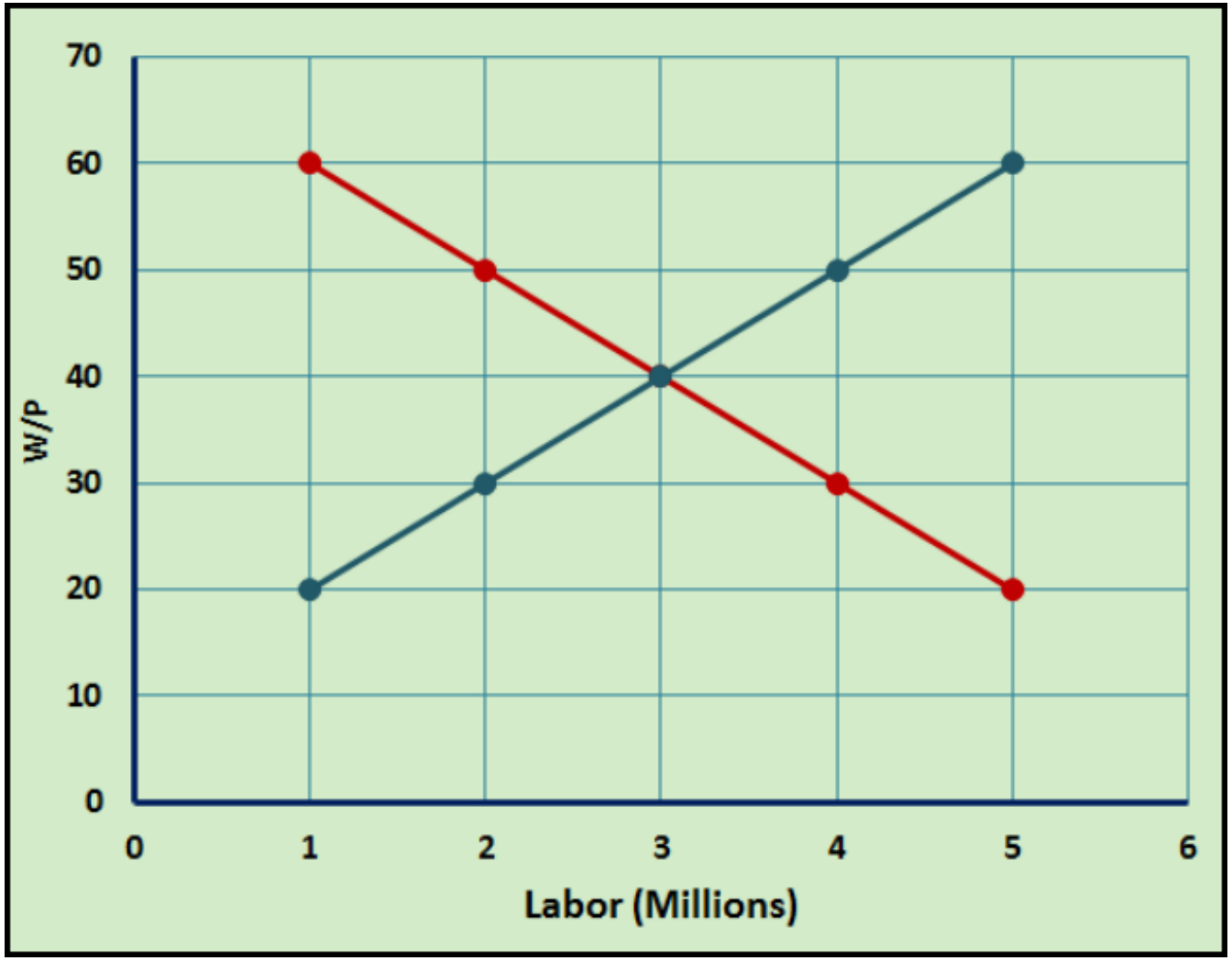
(a) in the short run, wages and prices are rigid or "sticky"; whereas they are fully flexible in the long run.

(b) in the short run, the labor market always in equilibrium; whereas in the long run it might not be.

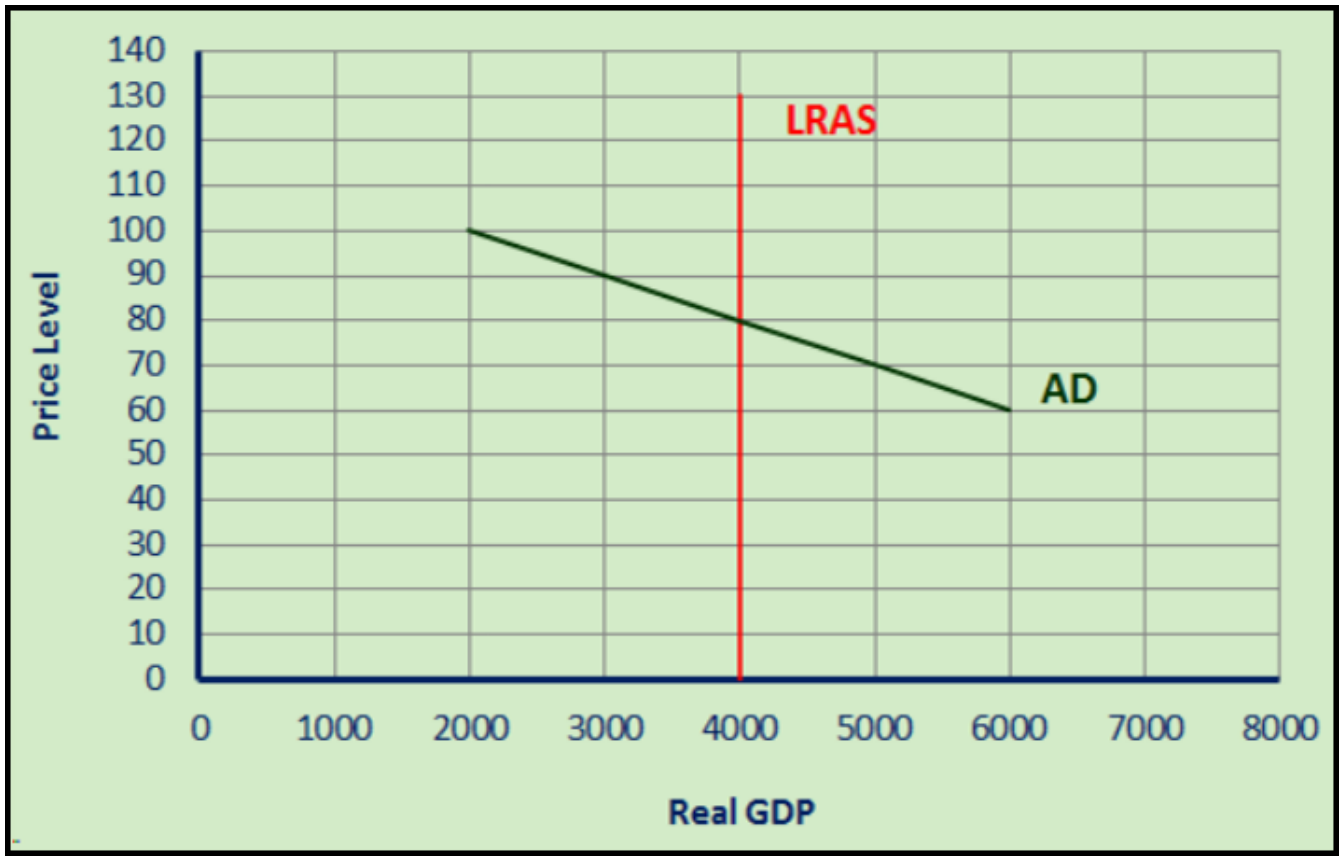
(c) in the short run, the Federal Reserve targets the demand for loanable funds; whereas in the long run, they target supply of loanable funds.

(d) in the long run, we're all dead.

Problem 2. Wages and prices are fully flexible. Currently $P = 1000$. If the price level increases by 5%, the nominal wage will change to what?



Problem 3. Suppose the MPC is 0.75. Currently $Y = 4000$, $C = 1500$, $I = 1500$, $G = 1000$, and $EX - IM = 0$. Suppose that the government increases its purchases by 1000 units. What will be the new long-run equilibrium price level and real GDP? How much private spending will be crowded out?



Problem 4. $MPC = 0.75$. Suppose government engages in a balanced-budget increase of government purchases by 1000. What's the new equilibrium price level and real GDP?