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Spring 2006, Intermediate Macroeconomics, section 2

ECON 219 Quiz III

General recommendations:

- Read questions thoroughly.
- Please respond on this copy.
- You have 20 minutes.
- Work individually.
- There are two pages.
- Good luck!

Your name:

1. Circle the appropriate answer on each of the following items. Circle multiple items if necessary:

   (a) The marginal propensity to consume is: 1) less than one; 2) equal to one; 3) more than one; 4) we cannot say.

   (b) In a static model, shocks to total factor productivity, z, are a good explanation of the business cycle because: 1) of the welfare theorems; 2) the US government is following supply-side economic policy; 3) the model matches many stylized facts; 4) prices are countercyclical.

   (c) A permanent shock to income implies: 1) a smaller change in consumption; 2) a same-sized change to consumption; 3) a larger change in consumption, 4) we cannot tell.

   (d) Consumption demand is decreasing in the interest rate because: 1) all households want to consume less as they face a negative income shocks; 2) savings become more atractive; 3) the price of future consumption goes up; 4) consumption is a normal good.

2. Explain as completely as possible what happens to current consumption for a borrower when current income go up.

3. Explain what happens to current consumption for a borrower when future income goes up.

4. In the static model with the production possibilities frontier, explain why consumption fluctuates more than output in the face of government expense shocks.

5. In the dynamic model, why does consumption fluctuate less than output?

Bonus question: In class, we made the distinction between an economy with credit markets and an economy without credit markets. Suppose now that credit markets are incomplete: households can lend, but not borrow. How could this be possible?