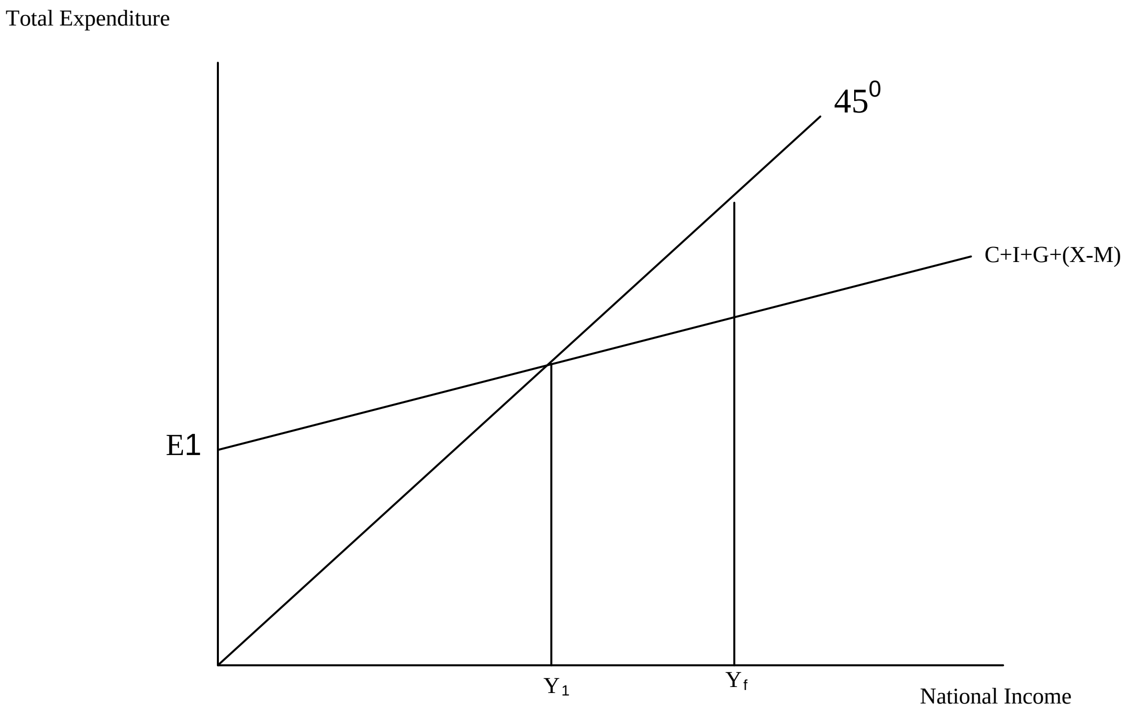
Chapter 33

1. A manufacturer of component parts for the automobile industry finds that stocks are building up each week. What does this tell you about the difference between planned and actual investment in this business?

2. Look at the diagram below which current equilibrium in the economy.



a. Comment on the position of the economy at this equilibrium point.
b. What would Keynesians argue should be done if the economy was in such a position?
c. What is the relevance to policy of the slope of the expenditure line?

In the diagram below, the economy is in equilibrium where the expenditure line E1 cuts the 45 degree line.

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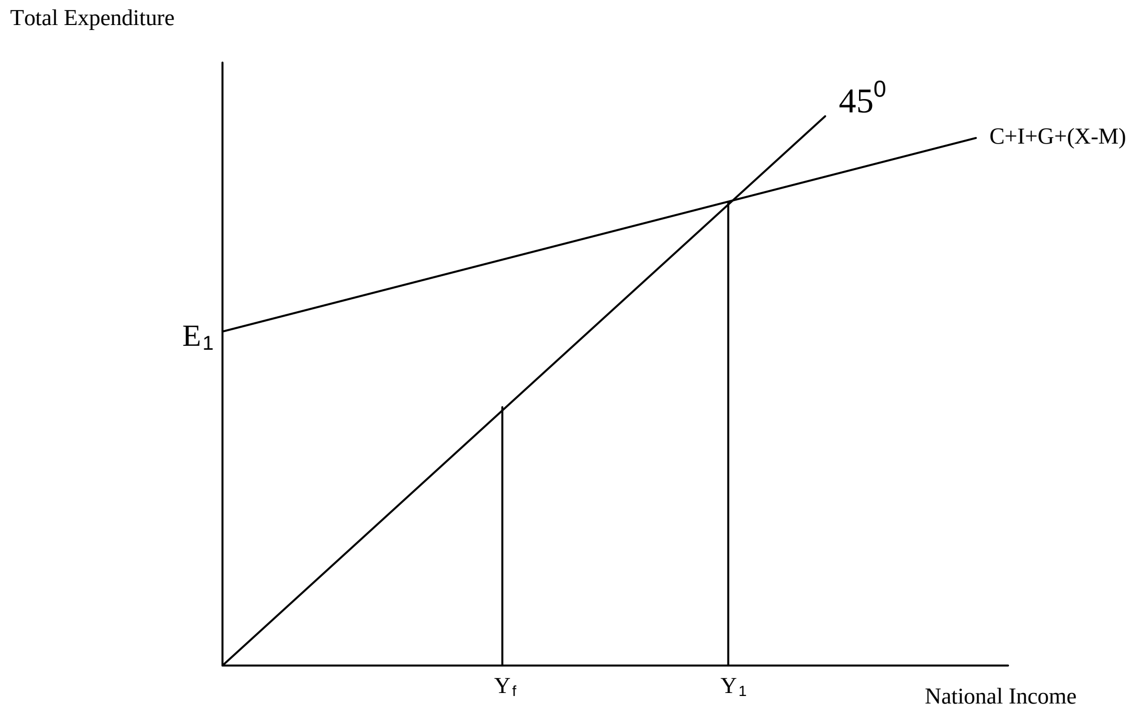

3.

a. What is the situation in the economy at this equilibrium point?

b. What policy option would Keynesians suggest in this situation?

4. There is a rise in autonomous expenditure of €8 billion. Calculate the value of the multiplier and hence the change in national income assuming a closed economy if the marginal propensity to save is:

a. 0.1

b. 0.45

c. 0.3

d. 0.2

e. 0.25

5. In each of the cases for the MPS in question 4 above, what difference to the change in national income would occur if the economy was open and

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the marginal propensity to import was 0.1?

6.

a. Assume the economy is in equilibrium at an interest rate i_e and a level of national income Y_e. The government chooses to institute a dramatic cut in public spending. Use an IS-LM diagram to show what is likely to happen to the interest rate and the level of national income.

b. How different would the analysis presented in 6a. above if the central bank in this country had a policy of maintaining inflation at a constant rate.

7. Assume the money supply is held constant but the price levels falls. What happens to the supply of real money balances and the LM curve as a result? What would happen to the aggregate demand curve in this situation?

8. The financial crisis led to record low interest rates in countries around the world. However, critics argued that low interest rates would not necessarily help to pull economies out of recession. Why? Explain.

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