ECO 120: Global Macroeconomics **Name:**
Practice Exam 3

1. Suppose Everything-Is-A-Nail Hammer Company produces hammers. Under current market conditions, no matter how many hammers the company decides to produce, they will be able to sell hammers for $10 each. The table below illustrates how many hammers it can produce per week with various levels of employment.

Hours of Labor	0	40	80	120	160	200
Quantity of Hammers	0	100	180	240	280	300

   (a) (7 points) Plot the demand curve for labor.

   (b) (7 points) Suppose the equilibrium wage in the economy is $10 per hour. How many hours of labor will Everything-Is-A-Nail hire each week?

   (c) (7 points) Suppose weak demand for hammers causes the price of hammers to drop to $5 each. Will there be a change in the labor demand curve? If so, draw the original and new labor demand curves. Will there be a movement along the curve, or a shift in the curve?

2. Consider the following government policies. Use the productivity curve to describe and illustrate whether or not each can positively influence the *long-run* level of output per worker.

   (a) (7 points) While balancing the government budget (zero government savings), the government provides financial support for building infrastructure, such as roads, railways, buildings, etc.

   (b) (7 points) While balancing the government budget, the government increases its financial support for long-term unemployed people.

   (c) (7 points) While balancing the government budget, the government increases its funding for research and development into new technologies.

   (d) (7 points) While balancing the government budget, the government increases its funding for state universities.

3. (7 points) Suppose in a country the marginal propensity to consume 95% and imports are unaffected by disposable income or real GDP. Suppose firms expect the economy to dip into a more severe recession in upcoming months. Expecting this to happen, investment in the economy decreases by $50 billion. What is the change in real GDP?

4. (7 points) Suppose the marginal propensity to consume is 95% and the marginal propensity to import is 15%. The economy is in a recession: real GDP is $9 trillion, and at full employment real GDP would be $10 trillion. The president decides to increase government spending to solve the problem. How much should government spending be increased by?

5. (7 points) Suppose the marginal propensity to consume is 95% and the marginal propensity to import is 15%. Suppose a drop in income in European countries causes a decrease in demand for U.S. exports of $10 billion. What is the change in real GDP?

6. Suppose the government is deciding whether to impose new tariffs and quotas on traded goods, which is estimated to reduce the marginal propensity to import from 20% to 10%. Suppose the marginal propensity to save is 5%.

   (a) (7 points) If the government wanted to stimulate the economy by increasing spending by $50 billion, under which scenario for trade restrictions would the government be more effective? What would be the change in real GDP in this case?

   (b) (7 points) Suppose the government decides to go forward with the increase in tariffs and quotas. In response, other governments do the same which causes exports to decrease by $50 billion. What effect is this going to have on real GDP? Would the impact have been different if there was the same decrease in exports, but without the tariffs and quotas?

7. What was your opportunity cost to studying for this exam?