ECO 305: Intermediate Macroeconomics
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Fall 2011, Final Exam

1. Economic growth is the principle source for improving the standard of living for people over time. We have learned three models to explain economic growth. Identify each model, and answer the following questions for each:

   (a) Explain the assumptions behind each model.

   (b) Identify what variables are constant in the long-run (if any) and what variables grow in the long-run.

   (c) Explain the conclusions of the model.

   (d) Identify the strengths of the model. That is, which conclusions or implications are realistic? You may include in your answer when these conclusions were realistic, or for what types of countries these conclusions are realistic.

   (e) Identify the weaknesses of the model. That is, which conclusions or implications are not realistic? Explain as you do in part (d).

   (f) Identify a government policy that can cause output per worker to increase in the long run. Use the model to explain why your government policy suggestion is effective.

   Learning Objectives for Problem 1:
   LO1: Students will be able to understand theories for determinants of economic growth, including the impact macroeconomic policies may have on economic growth.
   LO6: Students will be able to accomplish these objectives above using quantitative skills and graphical models of the macroeconomy.

2. Suppose an economy with fully flexible wages is originally in a full employment equilibrium. Suppose public policy makers debate a new plan for funding Medicare and Medicaid that causes consumers to expect higher taxes in the future. In the present, policy makers are only debating and they have not yet taken any actions. Describe and illustrate the general equilibrium effects of on employment, real wage, production, real interest rate, investment, consumption, and the price level.

   Learning Objectives for Problem 2:
   LO2: Students will understand how supply and demand decisions are made in markets for factors of production, and the implications for equilibrium in these markets.
   LO3: Students will understand how supply and demand decisions are made in markets for goods and services, and the implications for equilibrium in this market.
   LO6: Students will be able to accomplish these objectives above using quantitative skills and graphical models of the macroeconomy.

3. Suppose an economy is currently experiencing positive unemployment.

   (a) Use a dynamic general equilibrium economy with sticky wages do describe and illustrate this situation. Clearly explain the part of the model that implies an unemployment problem. Describe how equilibrium real GDP compares to the equilibrium level of real GDP that would occur with fully flexible wages.

   (b) Redraw your answer for part (a). Suggest a fiscal policy that can reduce unemployment and increase real GDP. Describe and illustrate the general equilibrium effects of your policy suggestion on employment, unemployment, real wage, production, real interest rate, investment, consumption, and the price level.

   (c) Redraw your answer for part (a). Suggest a monetary policy that can reduce unemployment and increase real GDP. Describe and illustrate the general equilibrium effects of your policy suggestion on employment, unemployment, real wage, production, real interest rate, investment, consumption, and the price level.

   Learning Objectives for Problem 3:
   LO2: Students will understand how supply and demand decisions are made in markets for factors of production, and the implications for equilibrium in these markets.
   LO3: Students will understand how supply and demand decisions are made in markets for goods and services, and the implications for equilibrium in this market.
   LO4: Students will be able to explain various theories for business cycle fluctuations and be able to prescribe and evaluate policy responses.
   LO5: Students will be able to understand the determinants of the demand and supply for money and be able to evaluate the impact changes in the market for money have on the economy as a whole.
   LO6: Students will be able to accomplish these objectives above using quantitative skills and graphical models of the macroeconomy.