

SIMON FRASER UNIVERSITY
Department of Economics

Econ 305
Intermediate Macroeconomic Theory

Prof. Kasa
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MIDTERM EXAM

Answer the following questions True, False, or Uncertain. Briefly explain your answers. No credit without explanation. (8 points each).

1. Tax cuts decrease national saving.
2. The unemployment rate is zero when the labor market clears.
3. In the Solow model, an increase in the savings rate increases the economy's growth rate.
4. Productivity increases cause current account surpluses.
5. Faster money growth causes inflation to increase.

The following questions are short answer. Briefly explain your answer. Clarity will be rewarded.

6. (20 points). Suppose the (per capita) production function is $y = \sqrt{k}$. Also suppose the savings rate, s , is 16%, the population growth rate, n , is 3%, and the depreciation rate, δ , is 5%. (There is no technological progress, i.e., $g = 0$). (a) Calculate the economy's steady-state capital/labor ratio and income per capita. (b) Is this economy above or below the Golden Rule?
7. (20 points). On the planet Vulcan, the velocity of money is constant. Real GDP grows by 4% per year, the money supply grows by 10% per year, and the nominal interest rate is 9%. What is the real interest rate?
8. (20 points). Compare and contrast how 'closed economies' and 'small open economies' respond to a fiscal expansion. Use graphs if you want.