ECO 120: Macroeconomics **Your Name:** ____________________

In-class Exercise

Keynesian Model **Section (Circle One): 2:15-3:40 PM 3:55-5:20 PM**

Directions: Work in groups of up to four people and answer the following questions. All papers will be collected, but only one member's paper will be randomly selected and graded and all members of the group will receive the same grade.

By signing below, you agree that the following work represents the efforts of everyone in the group, and you are willing to accept as your own grade for the group project the grade earned from this representation of your group's work.

____________________	____________________	__________
Signature Group Member 1	Print Name	Date
____________________	____________________	__________
Signature Group Member 2	Print Name	Date
____________________	____________________	__________
Signature Group Member 3	Print Name	Date
____________________	____________________	__________
Signature Group Member 4	Print Name	Date

1. Suppose that when consumers earn an additional dollar of income, they typically spend \$0.67 domestically and the rest is saved or spent on imported goods. Suppose businesses' economic outlook improves, leading to an increase in investment demand equal to \$150. Compute the immediate change in real GDP in the United States.

2. Suppose there is a Federal tax rebate that totals \$100bn for U.S. consumers, in which each full-time working American receives a check for \$500. Suppose the typical person puts \$100 of this money towards their savings accounts or paying towards existing debts. They spend the rest of this, including approximately \$50 on imported goods. Compute the immediate change in real GDP.

3. Suppose the Chinese Yuan appreciates against the U.S. dollar. Suppose if income were to increase by \$1, savings would rise by \$0.05 and imports would rise by \$0.20.

   (a) All other things remaining the same, will U.S. exports to China increase, decrease, or stay the same? Will U.S. imports from China increase, decrease or stay the same. Explain.

   (b) Suppose in response to the appreciation of the Yuan, the initial change in U.S. exports is \$10 billion and the initial change in U.S. imports is \$15 billion (you should know whether each of these is an increase or decrease). What will be the impact on real GDP?

4. What happens to the multiplier if the marginal propensity to save increases from 5% to 10% (assume MPM=0). Which MPS gives the government greater power to influence GDP? Does this imply that the government should persuade people not to save? Think about this question in terms of the expenditure model and past models with a long-run outlook.

5. Suppose in a closed economy, the marginal propensity to save is 5%. Suppose the economy decides to remove its trade barriers and freely allow imports and exports. As a consequence the marginal propensity to import becomes 20%.

   (a) How does this effect the expenditure multiplier?

   (b) How does this change affect the ability of the government to fix recessions?

   (c) How does this affect the stability of GDP in the face of changes in aggregate expenditures?

   (d) Is opening up the economy a good thing or a bad thing? Explain.