

EC 103–003

Problem Set 3

Prof. Santetti

Spring 2023

INSTRUCTIONS: Carefully read all problems.

Your answers must be **handwritten**, scanned (you may use a phone app such as *CamScanner*), and submitted in a single PDF file with your *first name* (mine would be `marcio.pdf`). You can convert images to PDF format [here](#). Also, you can merge different PDF files [here](#).

Submit your files via [theSpring](#). In case you experience any issues, email them to msantetti@skidmore.edu.

Assignment due April 19, before class.

Points Possible: 30

PLEASE WRITE SO I CAN READ IT.

- You have 2 weeks to complete this assignment. See our [course syllabus](#) for late submissions policies.
- Be honest. Don't cheat.
- As a Skidmore student, always recall your votes of academic integrity, and the [Honor Code](#) you have abided by:

"I hereby accept membership in the Skidmore College community and, with full realization of the responsibilities inherent in membership, do agree to adhere to honesty and integrity in all relationships, to be considerate of the rights of others, and to abide by the college regulations."

Have fun!

Problem 1

Answer the following short questions:

- (a) If a country is running a balance of trade *deficit*, will its current account be in deficit? Explain. (2 points)
- (b) When someone sends 500 U.S. dollars to a family member in Australia, will this transaction show up on the U.S. Balance of Payments' *financial* account or *current* account? Explain. (2 points)
- (c) Will the following be *suppliers* or *demanders* of U.S. dollars in foreign exchange markets? (2 points)
- A U.S. tourist in Latin America.
 - A German foreign exchange trader who believes that the dollar exchange rate will fall.
 - A U.S. foreign exchange trader who believes that the dollar exchange rate will fall.
 - A Costa Rican tourist in the United States.
- (d) State whether the following will show up on the Balance of Payments' *current* account or the *financial* account: (2 points)
- IBM's exports of computers to Japan.
 - IBM's hiring of a British merchant bank as a consultant.
 - A foreign national living in the United States repatriates money.
 - Ford Motor Company's profit in Hungary.
 - Ford Motor Company uses that Hungarian profit to build a new plant in Hungary.
- (e) Using this [Link](#), you will visualize the current account balance of the Vietnamese economy. Is Vietnam a *creditor* or *debtor* nation? Explain. (2 points)

Problem 2

Suppose you are given the following information regarding country YYZ:

- Aggregate consumption: $C = 350 + 0.6Y$
- Planned investment: $I = \$150$
- Aggregate expenditures definition: $AE = C + I$
- In equilibrium, aggregate income (Y) must be equal to aggregate expenditures (AE).

Answer the following questions. (If you **do not** show your calculations, you will be given **no credit**.)

- (a) What is YYZ's marginal propensity to consume? (2 points)
- (b) What is YYZ's marginal propensity to save? (2 points)
- (c) Show the expression (equation) for YYZ's aggregate expenditures function. (2 points)
- (d) What is the equilibrium level of income for YYZ? (2 points)
- (e) Now, suppose that the level of planned investment increases to $I' = \$200$ in the following year. What is the new equilibrium level of income for YYZ? (2 points)
- (f) Given your answers to parts (d) and (e), what is the size of YYZ's multiplier? To get full credit, you must show its value in two different ways. (2 points)

Problem 3

By reading the U.S. FED's official statement on its **latest monetary policy decisions**, answer the following questions:

- (a) What is the FED's long-run target rate of inflation? (2 points)
- (b) What is the FED's latest decision on its interest rate instrument, the federal funds rate? (2 points)
- (c) In order to achieve this target interest rate, will the FED increase its *buying* or *selling* of US Government Treasuries? (2 points)
- (d) Based on your answer to part (c), does this measure *increase* or *decrease* the amount of money circulating in the economy for aggregate expenditures (i.e., consumption and investment)? Explain your answer; otherwise, you won't receive full credit. (2 points)