MBA201B Macroeconomics in the Global Economy

Spring 2024

Practice Final Exam

Indicate the correct answer(s) and use the "box" below to explain your reasoning. If you answer the question correctly, we will not look at the box, but if you make any mistake, we will look at the box content to potentially award partial credit.

1. Suppose the US economy is experiencing a recession and the FED wants to stimulate aggregate demand. To do this, the FED targets a lower Federal Funds Rate. Which kind of conventional open market operation will help the FED comply with its objective?

   a. Sell government securities to commercial banks.
   b. Purchase government securities from commercial banks.
   c. Increase reserve requirements applied to commercial banks.
   d. Increase the interest rate on reserves held by commercial banks at the FED.

2. According to the quantity theory of money, which annual money growth rate should the Central Bank target to obtain a constant 2% annual inflation rate if money velocity is constant and nominal output grows by 3.5% per year?

   a. 1.5%
   b. 3.5%
   c. 5.5%
   d. None of the above

3. Which of the following events does not contribute to 2019 US GDP accounting?

   a. Mary purchases 1 pound of avocados produced in California in 2019.
   b. Chrysler produces 200 cars that remain unsold in 2019.
   c. Chrysler sells 200 cars in 2019 that were produced in 2018.
   d. 100,000 copies of *The Lord of the Rings* are printed and sold in 2019.

4. Suppose a new general-purpose technology is discovered and commercialized. Such technology, if adopted, makes all firms in the economy more productive, and does not affect the saving behavior of citizens. According to the saving-investment framework, what will happen to the real interest rate in equilibrium?
   a. It will remain constant.
   b. It will increase.
   c. It will decrease.
   d. The impact on the real interest rates is ambiguous.

5. In response to the invasion of Ukraine by Russia, the German government has decided to increase government spending for defense purposes. Using the IS-MP and AD-IA-LR frameworks, what do you think it will happen to US long-run output, inflation, and real interest rate?
   a. Long-run output is the same, inflation is the same, the real interest rate is higher.
   b. Long-run output is higher, inflation is the same, the real interest rate is higher.
   c. Long-run output is the same, inflation is higher, the real interest rate is higher.
   d. Nothing changes in the long run.

6. Suppose that Western Europe is a closed economy, except that it imports natural gas from Russia. A war occurring between Russia and Ukraine temporarily increases energy prices in Western Europe. In turn, prices of all goods temporarily increase. What happens to the Western European economy, according to the IS-MP framework?
   a. As prices increase, the ECB does not respond, demand for goods decreases (the IS curve shifts to the left), and the Western European economy experiences a recession.
   b. As prices increase, the ECB decreases real interest rates to stimulate demand for goods (the MP curve shifts to the right), and the Western European economy experiences an expansion.
   c. As prices increase, the ECB raises real interest rates to fight inflation (the MP curve shifts to the left), and the Western European economy experiences a recession.
   d. As prices increase, demand for goods decreases (the IS curve shifts to the left), the ECB decreases real interest rates to stimulate demand for goods (the MP curve shifts to the right), and output is unaffected.

7. The end of the pandemic makes US firms much more confident about the state of the economy, and many of them decide to invest more. At the same time, the President announces a large infrastructure plan for the country, which increases government spending. According to the IS-MP and AD-IA-LR frameworks for a closed economy, how does the FED react?
   a. The FED decreases the real interest rate, purchasing government securities to commercial banks.
   b. The FED increases the real interest rate, selling government securities to commercial banks.
   c. The FED keeps the real interest rate constant.
   d. The FED starts a massive program of quantitative easing.

8. Which one of the following statements about the IS-MP and AD-IA-LR frameworks are not correct? Select all that apply.

    a. If the CB raises the real interest rate because output is higher than its natural level, the MP curve shifts to the left.
    b. An increase in consumers' confidence shifts the IS curve and the AD curve to the right.
    c. A tax cut shifts the IS curve to the right and the AD curve to the left.
    d. If the CB decreases the real interest rate for any level of output, the IS curve shifts to the left and the AD curve shifts to the right.

9. Bribeland is a small open economy with a relatively unstable governments living in a world of fixed exchange rates. A new change in government triggers a temporary increase in the risk premium required by financial markets for holding domestic assets. What happens to Bribeland's economy?

    a. The increase in the risk premium puts selling pressure on domestic assets and currency, the CB is forced to increase interest rates to maintain exchange rate stability, and Bribeland experiences a recession.
    b. The increase in the risk premium puts selling pressure on domestic assets and currency, the currency depreciates, net exports increase, and Bribeland experiences an expansion.
    c. The increase in the risk premium makes domestic assets and currency more attractive, the currency appreciates, net exports decrease, and Bribeland experiences a recession.
    d. The increase in the risk premium makes domestic assets and currency more attractive, the CB is forces to decrease interest rates to maintain exchange rate stability, and Bribeland experiences an expansion.

10. Panama's currency (i.e., the Balboa) is pegged to the US dollar. Suppose the US experiences a sudden recession, and the FED responds by decreasing interest rates, r^*. What happens to Panama's economy?

    a. The decrease in r^* makes the US dollar less attractive than the Balboa. This event puts selling pressures on the US dollar, which depreciates relative to the Balboa. Panama's net exports decrease, and the economy experiences a recession.
    b. The decrease in r^* makes the US dollar less attractive than the Balboa. The CB of Panama is forced to decrease the real interest rate to maintain exchange rate stability, and Panama experiences an expansion.
    c. The decrease in r^* makes the US dollar more attractive than the Balboa. The US dollar appreciates relative to the Balboa as a result, Panama's net exports increase, and the economy experiences an expansion.
    d. The decrease in r^* makes the US dollar more attractive than the Balboa. The CB of Panama is forced to increase the interest rates to maintain exchange rate stability, and Panama experiences a recession.

11. “The fiscal multiplier of a government spending (i.e., the increase in real output given an increase in government spending) is higher...” Select all that apply.

    a. In a closed economy relative to an open economy living in a world of flexible exchange rates.
    b. In an open economy living in a world of fixed exchange rates relative to an open economy living in a world of flexible exchange rate.
    c. In an open economy living in a world of flexible exchange rates relative to closed economy.
    d. In an open economy living in a world of fixed exchange rates relative to a closed economy.

12. “Monetary policy as a stabilization tool of the domestic economy is more effective...” Select all that apply.

    a. In a closed economy relative to an open economy living in a world of fixed exchange rates.
    b. In an open economy living in a world of fixed exchange rates relative to an open economy living in a world of flexible exchange rate.
    c. In an open economy living in a world of flexible exchange rates relative to an open economy living in a world of fixed exchange rates.
    d. In an open economy living in a world of fixed exchange rates relative to a closed economy.

13. Your company wants you to provide insight on the investment environment in Zambia before entering the market. You download a dataset that reports that return to capital (i.e., marginal revenue product of capital, or MRPK) across firms. You explore the data, and report back that you see a large dispersion of the return to capital across firms and that state-owned firms tend to have a lower return to capital. You make the following conclusions and report them to your board (circle all that apply):
    a. Firms in Zambia find it difficult to expand because of constraints on the labor market.
    b. Private firms are at an advantage in Zambia as they face lower capital costs than state-owned firms.
    c. Resources are likely misallocated as capital is not flowing from firms with low return to capital to firms with high return to capital.
    d. Your firm will likely find it more costly to borrow than its state-owned competitors.

14. The population in Japan is older than the population Korea. What effect do you think this will have on the labor force participation (LFP) rate?
    a. The LFP rate will be higher in Japan
    b. The LFP rate will be higher in Korea
    c. The LFP in both countries will be high in both countries
    d. There is not enough information to tell

15. On average, the population in Japan is older than the population Korea. What effect do you think this will have on the unemployment rate?
    a. The unemployment rate will be higher in Japan
    b. The unemployment rate will be higher in Korea
    c. The unemployment rate will be the same in both countries.
    d. There is not enough information to tell.

16. This question asks you to use the supply and demand model we used to study low-wage immigration to study the gender wage gap. Consider the labor market for women. Suppose a new policy mandates universal paid family leave and childcare. You expect this will increase the supply of women in the labor market, but will also likely make firms more productive as talented women enter the labor force. You expect (select all that apply)
    a. Wages for women to rise.
    b. Employment of women to fall.
    c. Wages for women to rise, so long as the increase in labor demand for women is sufficiently large to offset the increase in supply.
    d. Employment of women to rise.

17. This question asks you to use the supply and demand model of the labor market to consider labor market trends following the pandemic's outbreak in April 2020. Suppose the labor market is initially in equilibrium, and for simplicity assume that COVID-19 reduced the demand for labor while leaving the supply of labor unchanged. (This is unrealistic, but is a simple way of saying demand fell more than supply.) Assume that wages are sticky in the short-run, that is they do not change from their previous equilibrium level. What do you expect to happen to wages and unemployment in April 2020?
    a. Wages and unemployment rise.
    b. Wages are unchanged and unemployment falls.
    c. Wages are unchanged and unemployment rises.
    d. Wages and unemployment are unchanged.

18. Next, we apply the same model to consider labor market trends during the recovery from the pandemic in 2021. Suppose that the labor market is initially in equilibrium (a different one than the previous question), and that labor demand from firms begins to rise as the economy recovers. Consider the medium- to long-run trends in the recovery (i.e., wages are no longer sticky, but freely adjust to equilibrate the labor market). Which of the following do you expect to be true (select all that apply)
    a. Wages will fall and employment will rise.
    b. Wages and employment will rise.
    c. The increase in wages will be lower if government policies cause individuals to be more willing to work at any particular wage rate.
    d. Wages will be unchanged, but employment will rise.

19. Higher migration costs would likely _____ the rate of frictional unemployment.
    a. Have no impact on
    b. Increase
    c. Decrease
    d. There is not enough information to tell.

20. Suppose the UK loses its trade deal with the EU. Select all that apply.
    a. This will be represented by movement along the labor demand curve as wages fall.
    b. Labor demand will shift in as UK firms sell less goods abroad.
    c. If wages are rigid, then unemployment will likely rise.
    d. Wages are likely to fall.

21. The factors most responsible for forecasts of the U.S. government debt spiraling out of control in the next half century are the projected to be:
    a. Slowdowns in the rates of technological change and human capital growth.
    b. A decrease in high-skilled domestic workers and the increase in immigration of low-skilled workers into the United States.
    c. Aging of the U.S. population and rising health care costs.
    d. An increase in international competition and the outsourcing of U.S. jobs.

22. Angola's government is highly indebted and there are concerns regarding the ability of the government to service its debt obligations. Which policies would you recommend reducing the debt-to-GDP ratio (select all that apply)
    a. Reduce corruption, improve education and infrastructure, and improve the property rights and contracting system.
    b. Reduce taxes.
    c. Reduce government expenditures in a way that doesn't too adversely affect economic growth.
    d. Print money to finance spending instead of issuing debt.

23. A couple of years after graduating from Haas, you go to work for a startup based in Southeast Asia. The country you are based in raises tariffs on imports from a neighbor, and you are asked in a meeting whether you think the country will benefit from the policy. You tell your colleague you would need to know the following piece of data to know if there was a possibility of the country "winning" from the policy:
    a. Tariff revenue received by the government.
    b. The change in profits of domestic producers.
    c. The change in prices received by exporters to the country.
    d. The change in the trade balance between the two countries.

24. You read that global real interest rates are on the rise due to changes in inflationary trends and increases in global risk factors. What effect do you expect to happen to the debt sustainability of countries, in particular emerging market economies?
    a. Increase debt sustainability.
    b. Reduce debt sustainability.
    c. No effect on debt sustainability
    d. There is not enough information to tell.

25. Choose the two correct statements about carbon tax and cap-and-trade among the following ones.
    a. A carbon tax sets the price of carbon emissions and allows the market to determine the quantity of emissions reductions.
    b. Cap-and-trade sets the price of emissions and allows the market to determine the quantity of emissions reductions.
    c. A carbon tax sets the quantity of emissions and allows the market to determine the price through an exchange where firms can trade permits to emit carbon.
    d. Cap-and-trade sets the quantity of emissions and allows the market to determine the price through an exchange where firms can trade permits to emit carbon.