KING'S UNIVERSITY COLLEGE

Economics 020 - Review Questions

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1. Describe the first and second round effects of an increase in government expenditure.

2. Describe the first and second round effects of an increase in the money supply (i.e. an expansionary monetary policy).

3. What would happen in the following scenario? Economy A and B are identical except that an 1% change of interest rate results in 0.1 billion change in interest sensitive expenditure in economy A but 10 billion change in the economy B.

a) In which country is fiscal policy more effective? (A or B)Why?
b) In which country is monetary policy more effective? Why?
c) What about the crowding effect of fiscal policy in each economy.
d) Which economy would you say is likely to be Keynesian and which monetarist?

4.

Inflation (percent per year)	Unemployment (percent)
12	4
11	5
10	6
9	7
8	8
7	9

(a) The above table illustrates a short-run Phillips curve for the country of Ruritania. If the expected rate of inflation is 10 percent, and the rate of inflation unexpectedly rises to 12 percent, what is the unemployment rate?
(b) If the expected rate of inflation is 10 percent, and the rate of inflation unexpectedly falls to 8 percent, what is the unemployment rate?
(c) If the expected rate of inflation is 10 percent, and the rate of inflation unexpectedly rises to 12 percent and stays there for some period of time, what will be the rate of expected inflation and the unemployment rate?
(d) If the expected rate of inflation is 10 percent, what is the natural rate of unemployment for this country?

5. If the level of GDP is $400 million and the price level is 200 and the velocity of money is 20:

(a) What is the initial level of the quantity of money?

(b) If the quantity of money rises by 20 %, what is the new quantity of money

(c) What is the new price level?

(d) What is the new level of GDP?

6. Assume that we have a perfectly flexible exchange rate (i.e., no intervention by the Bank of Canada to influence the exchange rate). Moreover, assume the exchange rate is defined as the value of the Canadian dollar (i.e., US $ per Canadian $). With the use of a demand and supply diagram for the market for Canadian dollars, determine the impact on the demand curve, the supply curve and the equilibrium exchange rate if:

(a)the international community expects the Canadian dollar to depreciate in the near term.

(b) the Bank of Canada decides to slow the rate of inflation by reducing the rate of growth of the domestic money supply.