Universidade Nova de Lisboa

Law School

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Midterm Macroeconomics

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I (40%)

Please comment on the veracity of the following statements:

a) The computation of the GDP in the expenditure approach is the sum of the gross value added in the different sectors of activity.
False, the sum of gross value added across sectors leads to GDP in the production approach, not the expenditure approach.

b) The real growth rate of a variable is always smaller than its nominal growth rate.
False, if prices decrease (negative growth rate) the real growth rate becomes larger than the nominal one.

c) Fiscal balances and external balances tend to have opposing signs.
False, given the fundamental identity of macroeconomics (S-I)+(T-G)=(X-M), the "twin deficits" tend to exist.

d) Public consumption is an expenditure aggregate whose value is imputed by total public expenditure.
False, public consumption is inputed as public expenditure with goods and services and and wages of civil servants

II (30%)

In the context of the simple Keysian model, consider an economy characterized by the following values for desired expenditure aggregates:

C=10+0.5*Y

I=5

G=3

X-M=2

$AD = C+I+G+X-T$
$= 10+0.5Y+5+3+2$
$Y=AD$
$Y=20+\frac{1}{2}Y$
$Y=\frac{1}{1-\frac{1}{2}}[20]=40$

a) What is the equilibrium income level in this economy?
Y*=1/(1-0.5)*[10+5+3+2]=40

b) What is the effect of a unitary reduction in autonomous consumption, resulting from more pessimism of households?
Change Y*=1/(1-0.5)*(-1)=-2

$\Delta Y^* = \frac{1}{1-\frac{1}{2}}\Delta\bar{C} \Leftrightarrow \Delta Y^* = 2.(-1)$
$= -2$

c) Can this situation be counteracted by policy authorities? Justify.

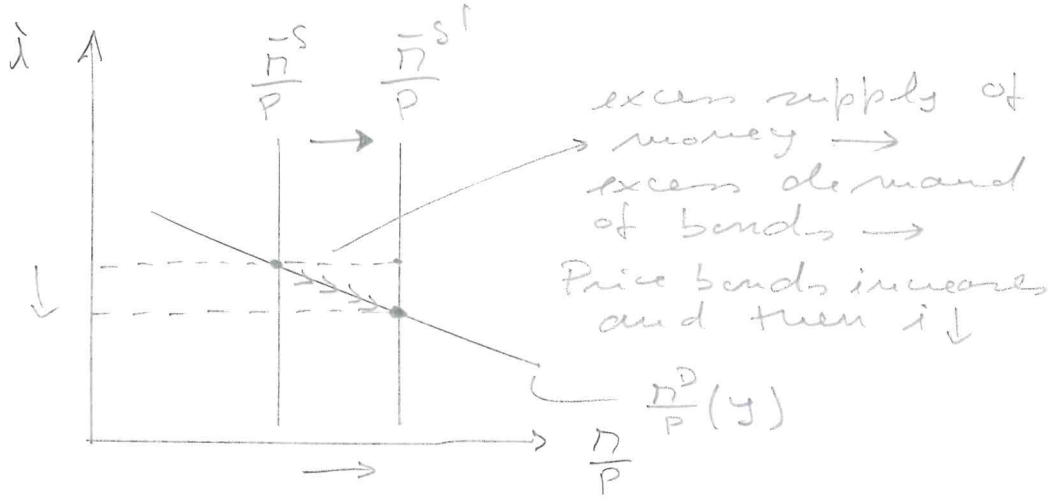
Yes, an increase of public expenditure by 1 would compensate the negative shock on the consumers

III (30%)

Money is a fundamental part of the functioning of any economy.

a) How is Money defined?
Money is an asset that fulfils three tasks simultaneously: unit of account, reserve of value and being widely accepted as a means of payment.

b) What is the impact in the Money market of an increase in the nominal Money supply? Explain the adjustment mechanism.



c) What is the impact of an increase in the nominal Money supply on economic activity? (in the short-run)?

[AT THE TIME OF TEST - IS/LM GRAPHS WERE NOT GIVEN]

[i ↓ promotes I ↑ ⇒ expansion in economic activity → feedback because Y ↑ expands money demand which increases i partially.