

MOCK EXAM
Prof. Paolo Paesani

INSTRUCTIONS

1. This is a **closed book exam**. You are not allowed to consult any materials or other sources of information (including notebooks, laptops, dictionaries, mobile phones) during the exam. Please ensure that there are no materials on your person when you are seated. If any materials or devices are found on you after you are seated, this constitutes cheating and you will be excluded from the exam.
2. **Bring your own calculator;**
3. You have one hour to complete your exam;
4. Use the sheets provided by the invigilator to write your answers;
5. Write your student number on the top of EACH SHEET that you are handing to the supervisor;
6. Please remember that it is your responsibility to make sure that your writing is LEGIBLE and the sheets that you hand in are sufficiently tidy and clear. Illegible work will be excluded for obvious reasons.

Exercise on inflation and growth (20% of final grade)

	Qa	Pa	Qb	Pb
2015	100	10	100	5
2016	100	12	120	6

1. Use the following data and the Laspeyres formula to compute the inflation rate and the growth rate between 2015 and 2016.
2. Based on your answer to the previous question complete the following sentence and show the formula on which you base your answer

“The fact that between 2015 and 2016 the inflation rate was equal to ... per cent, implies that – on average – real interest rates were ... than nominal interest rates. *Ceteris paribus*, this is ... for creditors and ... for debtors and contributes to ... aggregate investment, GDP and employment”.

Fill in the blanks (10% of final grade)

Complete the following sentence and show the formulas on which you base your answer

1. “*Ceteris paribus*, a rise in government purchases causes the government budget deficit to, aggregate demand to ..., GDP to and employment to ... at least in the short-run. One possible remedy to the in the government budget deficit is to ... government transfers and / or Taxation”.

True/False (10% of final grade)

State whether the following statement is True or False and provide a short motivation.

2. “*Ceteris paribus*, a rise in foreign prices causes aggregate demand and GDP to fall and unemployment to rise at least in the short-run”.

Open question (60% of final grade)

3. Use the IS-MP-IA and the model of the competitive labour market to discuss the impact of a rise in the marginal propensity to consume in the short and the long-run. In doing so, address the following issues
- a. What is the marginal propensity to consume and how does it enter the IS-MP-IA model?
 - b. On the assumption that the economy starts at full employment, how does a rise in the marginal propensity to consume affect real GDP and inflation in the short-run and why?
 - c. What happens to interest rates, aggregate investment and employment in the transition from the short to the long run and why?
 - d. Based on your answer to d, is it possible that the long-run aggregate supply function shifts and if so in which direction and why?
 - e. Complete the following sentence and motivate it “On the assumption that bank loans are pro-cyclical, the rise in the marginal propensity to consume leads them to This has a ... impact on money supply and can ... the economy”.
 - f. Based on your answers to the previous questions, what is the business impact of a rise in the marginal propensity to consume? Discuss likely impact on costs, revenues and profits.