Name: _____

Cosumnes River College
Principles of Macroeconomics
Problem Set 4
Due March 8, 2017

Spring 2017   Prof. Dowell

Instructions: Write the answers clearly and concisely on these sheets in the spaces provided. Do not attach extra sheets.

1.   a.   Write out the equation for the consumption function in algebraic form and identify each component.

b.   Assume a consumption function that takes on the following algebraic form: $C = \$100 + .8Y^D$. Assume that $Y = \$1,200$ and $T = \$200$. What is the level of consumption?

c.   Suppose the slope of the consumption function is 0.75 and there was an increase in income of $100. Calculate the increase in consumption.


2.   Compare and contrast the MPC and the MPS. Also explain what these two figures must always add up to.

3.   Critically evaluate the following statement. "People can spend more than their income by borrowing   therefore the sum of the MPC and the MPS could actually be greater than one.

4. Assume a consumption function of the form $C = 200 + .8Y$. Derive the saving function and write out the algebraic representation.

5. Draw a graph of the consumption function and determine the MPC and the level of autonomous consumption given the following data.

Year	Disposable Income	Consumer Spending
2011	$1,500	$1,200
2012	1,800	1,440
2013	2,100	1,680
2014	2,400	1,920
2015	2,700	2,160
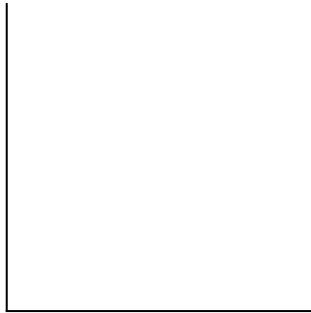
6. For each of the following, state the effect on the consumption function and explain why:

   a. An increase in the nominal value of stocks and real estate

   b. An increase in the price level

   c. An increase in expected future real wealth

7. Explain why permanent tax cuts are likely to lead to bigger increases in consumer spending than temporary tax cuts.

8. Suppose the price of imported goods goes down. What happens to Consumption, Imports and Net Exports?

9. Suppose you are given the following:

$$C = \omega/P + 0.75(Y - T)$$
$$\omega = 200$$
$$P = 4$$
$$Y = 2{,}000$$
$$T = 500$$

   a. Solve for C.

   b. Suppose that net taxes (T) increase to 1,000. Solve for the new level of consumption.

   c. Suppose now that P falls to 2. Solve for the new level of consumption.