

Econ 102- Principles of Macroeconomics
Discussion Section Handout #5

Announcement:

Homework is due on March 9th no later than 5pm.

Key concepts:

Rule of 70, determinants of long-run economic growth, potential real GDP, savings and investment, loanable funds market

Examples:

1. Consider the following data for a closed economy;
Y=\$14 trillion
C=\$7 trillion
I=\$3 trillion
TR=\$1 trillion
T=\$3 trillion

Use the data to calculate the following;
 - a. Private saving
 - b. Public saving
 - c. Government purchases
 - d. Suppose the government purchases increase from the level of the answer for (c). If the values of Y and C are unchanged, what must happen to the values of S and I?

2. i is the real interest rate(%) and L is the quantity of loanable funds(trillion dollars). Demand for loanable funds is $L^D = 12 - i$ and supply for loanable funds is $L^S = 0.5i$. Answer the following questions.
 - a. What is the equilibrium in the loanable funds market?
 - b. If government purchases decrease by 3 trillion, what happens to the equilibrium? What happens to saving and investment?
 - c. Suppose there is no inflation. If 5% of inflation is expected in the near future, what happens to the equilibrium? And to the nominal interest rate?