

Macroeconomics – Homework 3

Due to 28.4.2015, at the beginning of the lecture

You can work in two

1. In Table below are data for the price of Big Macs in several countries. The U.S. price of a Big Mac is \$3.57.

Country	Price of a Big Mac	Predicted Exchange Rate	Actual Exchange Rate
Chile	1,750 pesos	_____ pesos/\$	549 pesos/\$
Hungary	720 forint	_____ forints/\$	199 forints/\$
Czech Republic	67.9 korunas	_____ korunas/\$	18.7 korunas/\$
Brazil	8.03 real	_____ real/\$	2.00 real/\$
Canada	3.89 C\$	_____ C\$/\$	1.16 C\$/\$

- a. For each country compute the predicted exchange rate of the local currency per U.S. dollar.
 - b. According to purchasing-power parity, what is the predicted exchange rate between Hungarian forint and Canadian dollar? What is the actual exchange rate?
 - c. How well does the theory of purchasing-power parity explain exchanges rates?
2. Over the past decade, some of Chinese saving has been used to finance American investment. That is, the Chinese have been buying American capital assets. Answer the following questions in words and with a diagram.
 - a. If the Chinese decided they no longer wanted to buy U.S. assets, what would happen in the U.S. market for loanable funds? In particular, what would happen to U.S. interest rates, U.S. saving, and U.S. investment?
 - b. What would happen in the market for foreign-currency exchange? In particular, what would happen to the value of the dollar and the U.S. trade balance?
 3. The economy begins in long-run equilibrium. Then one day, the president appoints a new chairman of the Federal Reserve. This new chairman is well-known for his view that inflation is not a major problem of an economy.
 - a. How would this news affect the price level that people would expect to prevail?
 - b. How would this change in the expected price level affect the nominal wage that workers and firms agree to in their new labor contracts?
 - c. How would this change in the nominal wage affect the profitability of producing goods and services at any given price level?
 - d. How does this change in profitability affect the short-run aggregate-supply curve?
 - e. If aggregate demand is held constant, how does this shift in the aggregate-supply curve affect the price level and the quantity of output produced?