First Quiz

- Consider the following model

$C=100+0.8\ Y_d$

$G=100$, $I=120$, $X=60$,

$T= 0.2\ Y$, $IM= 0.15\ Y$

  - Find the equilibrium national income in two ways
  - Show it graphically

1- What is the relationship between the MPC and the slope of the AE curve?

2- "If the income tax rate is high enough, the multiplier can be negative." Is the previous statement correct or incorrect?

3- What is the relationship between the slope of the aggregate expenditure curve and the multiplier?

Answers

1-Answer: If there are no imports or income taxes, then the slope of the *AE* curve equals the *MPC*. If there are imports and income taxes, then the slope of the *AE* curve is less than the *MPC*. In either case, an increase in the *MPC* increases the slope of the *AE* curve.

2- Answer: The statement is incorrect. The higher the income tax rate, the smaller the multiplier, but the multiplier always remains positive.

3- Answer: The multiplier equals 1/(1 - slope of the *AE* curve) . This result does not change regardless of the existence or absence of imports or income taxes.