Problem Set #4
ECON 4020, Prof. DeBacker
Due Wednesday, April 1, 5 p.m.

NOTE: You are encouraged to work on this problem set in a group of up to four members. When finished, each group should turn in one copy of the problem set directly to me or to the departmental office on the fifth floor of Brooks Hall. A completed problem set should list the names of the group members who worked on the assignment. As noted in the syllabus, no late assignments will be graded.

1. Chapter 11, Problems and Applications (6 points): #1, #3, #7
2. Chapter 12, Problems and Applications (6 points): #1, #3, #7
3. Chapter 14, Problems and Applications (2 points): #2
4. Chapter 14, “Made up problem”- Stabilization policy and its limitations (5 points):
   (a) Define the inside lag and the outside lag.
   (b) Which type of lag is longer for monetary policy? Which type is longer for fiscal policy?
   (c) What types of advancements or institutional changes might shorten each type of lag?
5. Chapter 15, “Made up problem”- the Stimulus Package (6 points):
   (a) Using the classical model of Chapter 3, what is the effect of the “stimulus package” in the long run?
   (b) Using the Solow growth model of Chapter 7, how do the long run effects described in the previous question affect the steady state capital stock and steady state output?
   (c) If, previous to the increase in government spending and decrease in taxes, the steady state capital stock were below the Golden Rule capital stock, what would the “stimulus package” do to consumption in the long run?
   (d) Using the IS-LM model, describe the short run effects of the “stimulus package”.
   (e) Given what you know about the effects of increasing the budget deficit (both in the short-run and the long-run), if you were a member of Congress, would you have voted to approve the “stimulus package”? Why or why not?