

ECO 407 – L0101

Competing Views in Macroeconomic Theory and Policy

Term Test

Instructions:

- The total time for this test is 1 hour and 45 minutes.
- Answer TWO of the following THREE questions in essay form.
- Each Question is worth one-half of the total grade.
- No aids allowed.
- Answer each question in a separate booklet.
- Please write legibly. If I can't read your handwriting, I can't award you any marks!

1. Critically comment on the following two statements:
 - a. "Some economists argue that investment is determined by savings. At the same time, they consider savings to be an increasing function of the rate of interest. Therefore, it must be concluded that an increase in the rate of interest will increase investment."
 - b. "Orthodox economists consider that an economy's output is a decreasing function of the real wage rate. To the contrary, heterodox economists argue that an increase in real wages might result into an increase in overall aggregate output."
2. Critically comment on the following statement: "Fiscal austerity has emerged from the debate on the euro crisis as the main strategy to restore growth and employment. According to this view, reducing public debts reduces interest rates and injects confidence in the private sector, freeing the basic instincts to invest and consume."
3. Critically comment on the following statement: "All of today's developed countries have become rich through free-market policies, especially through free trade with the rest of the world. As David Ricardo demonstrated almost two centuries ago, specialization and trade based on the principle of comparative advantages makes all countries better off. Therefore, developing countries should fully embrace free-trade policies in order to close the income-gap with developed countries."