

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 100 points (to be scaled up to 150 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I cannot give extra time because some students have a class after your class.

1) (12 points) Answer EITHER Part A OR Part B.

A) Suppose nominal interest rate is 10%, the tax rate is 30%, and the inflation rate is 8%. What is the real after-tax interest rate? Show all work.

B) Suppose the inflation rate is 20%. What is the value of the inflation tax? Show all work. What is the economic interpretation of that number?

2) (14 points) Answer EITHER Part A OR Part B.

A) What is a *public good*? Why should the government provide it?

B) What is the difference between *current* and *recurrent* expenditures? Which play a bigger role in making it difficult for the government to cut its taxes?

3) (14 points) For EITHER the policy in Part A OR the policy in Part B, explain why it is important for the developed countries to use that type of policy. I will give 1 bonus point if you can guess what rank, out of the 21 countries, the USA was in 2005 for that policy. The countries are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, UK, and the USA.

A) Migration, capturing the extent to which policies ease or hinder migration (particularly of unskilled rather than skilled workers) from poor to rich countries.

B) Security, including financial contributions to peacekeeping operations, naval operations that secure international shipping lanes, and penalties for certain arms exports.

4) (20 points) Answer EITHER Part A OR Part B.

A) Suppose you are a leader of a very poor developing country. Which type of tax would you rely on the most for tax revenue? Explain BOTH an advantage of that type of tax AND a disadvantage of ONE of the other taxes.

B) SOEs often run deficits. Why is this the case? Why do governments continue to have them if they just cost the government more money?

5) (20 points) Answer EITHER Part A OR Part B.

A) What is beneficial about having interest rate ceilings? What is detrimental about them? Explain how interest rate ceilings causes those problems.

B) What is the advantage of having a relatively high reserve requirement like Russia's 20%? What problem can that cause? Explain how it causes that problem.

6) (20 points) Answer EITHER Part A OR Part B.

A) The IMF puts conditions of loans. What type of conditions do they put? Are they a good idea?

B) Which of the three views about the effects of aid upon the economy do you feel is the strongest? Explain their arguments and why you feel it is a strong argument.