

EE312 (1/2020): Ch.8 Two-Period Model, the Consumption-Savings Decision

Quiz 7 :You have 10 minutes.

PART 1. (20 marks) Short Answer. Answer each question in the space provided.

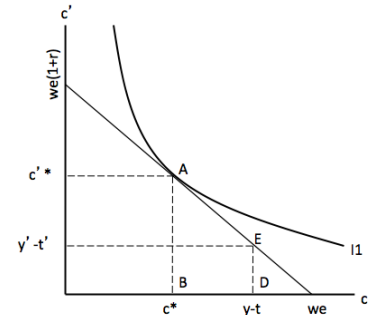
1. Write down consumer's life time budget constraint. Interpret its meaning.

.....

PART 2. (80 marks) Multiple choices. Please choose the correct answer by **circling one** letter only. [In case there is no correct choice provided, please write down the correct answer. The mark will be given only if there is a mistake in that question.]

1. Consider the figure below. Which of the following is **wrong**?

- (a) This consumer lends out in the credit market by $(y - t) - c^*$
- (b) This consumer will save by $|BD|$
- (c) The future consumption is **not** equal to $(y' - t')$.
- (d) The distance between $(y' - t')$ and c'^* is **not** equal to $(1 + r)|BD|$
- (e) The future consumption is equal to $(y' - t') + (1 + r)(y - t - c)$



*Note that $|BD|$ is the distance between point B and point D.

• **Let vertical axis is future consumption and horizontal axis is current consumption.**

- 2. If current output (y) **increases**, budget line will shift by Δy .
 - a. vertically upward b. vertically downward c. horizontally to the right d. horizontally to the left
- 3. If future output (y') **decreases**, budget line will shift by $\Delta y'$.
 - a. vertically upward b. vertically downward c. horizontally to the right d. horizontally to the left
- 4. If there is an **increase in current income**, current consumption will, future consumption will and saving will
 - a. increase, decrease, increase b. increase, increase, increase
 - c. increase, increase, decrease d. It depends on whether the consumer is a lender or borrower.
- 5. Suppose the consumer is a **lender**. Substitution effect is **greater than** income effect. If there is an **increase in interest rate**, **current consumption** will, **future consumption** will and **saving** will
 - a. increase, increase, increase b. decrease, increase, increase
 - c. decrease, increase, decrease d. else, specify
- 6. Suppose the consumer is a **borrower**. Substitution effect is **equal to** income effect. If there is an increase in interest rate, **current consumption** will and saving will
 - a. decrease, remain constant b. increase, increase
 - c. decrease, increase d. else, specify
- 7. An **increase** in the real interest rate (r) causes **future consumption** to become and **current consumption** becomes
 - a. cheaper, more expensive b. cheaper, cheaper
 - c. more expensive, cheaper d. else, specify
- 8. The effect of **the government's tax cut** on consumption depends on whether the cut is temporary or permanent.
 - **If temporary**, the increase in **current consumption** will be ; most of the increased income is
 - **If permanent**, the increase in **current consumption** will be
 - a. large, consumed, small b. large, saved, large
 - c. small, saved, large d. else, specify

EE312 (1/2020): Ch.8 Two-Period Model, the Consumption-Savings Decision

Quiz 1 :You have 10 minutes.

PART 1. (20 marks) Short Answer. Answer each question in the space provided.

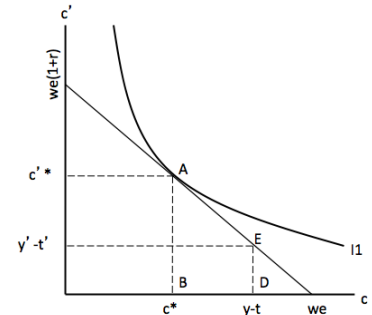
1. Write down consumer's life time budget constraint. Interpret its meaning.

.....

PART 2. (80 marks) Multiple choices. Please choose the correct answer by **circling one** letter only. [In case there is no correct choice provided, please write down the correct answer. The mark will be given only if there is a mistake in that question.]

1. Consider the figure below. Which of the following is **wrong**?

- (a) This consumer lends out in the credit market by $(y - t) - c^*$
- (b) This consumer will save by $|BD|$
- (c) The future consumption is equal to $(y' - t') + (1 + r)(y - t - c)$
- (d) The distance between $(y' - t')$ and c^* is equal to $(1 + r)|BD|$
- (e) The future consumption is equal to $(y' - t')$.



*Note that $|BD|$ is the distance between point B and point D.

• **Let vertical axis is future consumption and horizontal axis is current consumption.**

- 2. If current output (y) **decreases**, budget line will shift by Δy .
 - a. vertically upward b. vertically downward c. horizontally to the right d. horizontally to the left
- 3. If future output (y') **increases**, budget line will shift by $\Delta y'$.
 - a. vertically upward b. vertically downward c. horizontally to the right d. horizontally to the left
- 4. If there is an **increase in current income**, current consumption will, future consumption will and saving will
 - a. increase, increase, decrease b. increase, decrease, increase
 - c. increase, increase, increase d. It depends on whether the consumer is a lender or borrower.
- 5. Suppose the consumer is a **lender**. Substitution effect is **greater than** income effect. If there is an **increase in interest rate**, **current consumption** will, **future consumption** will and **saving** will
 - a. increase, increase, increase b. decrease, increase, decrease
 - c. decrease, increase, increase d. else, specify
- 6. Suppose the consumer is a **borrower**. Substitution effect is **lower than** income effect. If there is an increase in interest rate, **current consumption** will and saving will
 - a. decrease, remain constant b. decrease, increase
 - c. increase, increase d. else, specify
- 7. An **increase** in the real interest rate (r) causes **current consumption** to become and **future consumption** becomes
 - a. cheaper, more expensive b. cheaper, cheaper
 - c. more expensive, cheaper d. else, specify
- 8. The effect of **the government's tax cut** on consumption depends on whether the cut is temporary or permanent.
 - **If permanent**, the increase in **current consumption** will be
 - **If temporary**, the increase in **current consumption** will be ; most of the increased income is
 - a. large, small, consumed b. large, small, saved
 - c. small, large, saved d. else, specify

EE312 (1/2020): Ch.8 Two-Period Model, the Consumption-Savings Decision

Quiz 1 :You have 10 minutes.

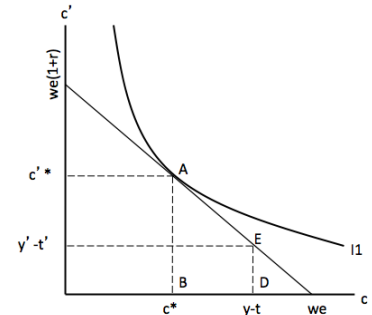
PART 1. (20 marks) Short Answer. Answer each question in the space provided.

1. Write down consumer's life time budget constraint. Interpret its meaning.

.....

PART 2. (80 marks) Multiple choices. Please choose the correct answer by **circling one** letter only.[In case there is no correct choice provided, please write down the correct answer. The mark will be given only if there is a mistake in that question.]

1. Consider the figure below. Which of the following is **wrong**?
 - (a) This consumer lends out in the credit market by $(y - t) - c^*$
 - (b) This consumer will save by $|BD|$
 - (c) The future consumption is **not** equal to $(y' - t') + (1+r)(y - t - c)$
 - (d) The distance between $(y' - t')$ and c^* is equal to $(1+r)|BD|$
 - (e) The future consumption is **not** equal to $(y'-t')$.



* Note that $|BD|$ is the distance between point B and point D.

• **Let vertical axis is future consumption and horizontal axis is current consumption.**

2. If future output (y') **increases**, budget line will shift by $\Delta y'$.
 - a. horizontally to the right
 - b. horizontally to the left
 - c. vertically upward
 - d. vertically downward
3. If current output (y) **decreases**, budget line will shift by Δy .
 - a. horizontally to the right
 - b. horizontally to the left
 - c. vertically upward
 - d. vertically downward
4. Suppose the consumer is a **lender**. Substitution effect is **greater than** income effect. If there is an **increase in interest rate**, **current consumption** will, **future consumption** will and **saving** will
 - a. increase, increase, increase
 - b. decrease, increase, decrease
 - c. decrease, increase, increase
 - d. else, specify
5. If there is an **increase in current income**, current consumption will, future consumption will and saving will
 - a. increase, increase, increase
 - b. increase, increase, decrease
 - c. increase, decrease, increase
 - d. It depends on whether the consumer is a lender or borrower.
6. Suppose the consumer is a **borrower**. Substitution effect is **equal to** income effect. If there is an increase in interest rate, **current consumption** will and saving will
 - a. decrease, increase
 - b. decrease, decrease
 - c. increase, remain constant
 - d. else, specify
7. An **increase** in the real interest rate (r) causes **future consumption** to become and **current consumption** becomes
 - a. cheaper, more expensive
 - b. cheaper, cheaper
 - c. more expensive, cheaper
 - d. else, specify
8. The effect of **the government's tax cut** on consumption depends on whether the cut is temporary or permanent.
 - **If temporary**, the increase in **current consumption** will be ; most of the increased income is
 - **If permanent**, the increase in **current consumption** will be
 - a. small, saved, large
 - b. large, small, consumed
 - c. large, consumed, small
 - d. else, specify

EE312 (1/2020): Ch.8 Two-Period Model, the Consumption-Savings Decision

Quiz 1 :You have 10 minutes.

PART 1. (20 marks) Short Answer. Answer each question in the space provided.

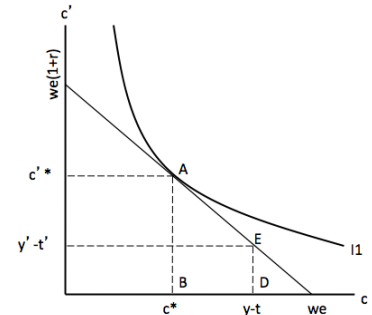
1. Write down consumer's life time budget constraint. Interpret its meaning.

.....

PART 2. (80 marks) Multiple choices. Please choose the correct answer by **circling one** letter only. [In case there is no correct choice provided, please write down the correct answer. The mark will be given only if there is a mistake in that question.]

1. Consider the figure below. Which of the following is **wrong**?

- (a) This consumer lends out in the credit market by $(y - t) - c^*$
- (b) This consumer will save by $|BD|$
- (c) The future consumption is **not** equal to $(y' - t') + (1 + r)(y - t - c)$
- (d) The distance between $(y' - t')$ and c^* is equal to $(1 + r)|BD|$
- (e) The future consumption is equal to $(y' - t')$.



* Note that $|BD|$ is the distance between point B and point D.

• **Let vertical axis is future consumption and horizontal axis is current consumption.**

- 2. If current output (y) **increases**, budget line will shift by Δy .
 - a. horizontally to the right
 - b. horizontally to the left
 - c. vertically upward
 - d. vertically downward
- 3. If future output (y') **decreases**, budget line will shift by $\Delta y'$.
 - a. horizontally to the right
 - b. horizontally to the left
 - c. vertically upward
 - d. vertically downward
- 4. An **increase** in the real interest rate (r) causes **current consumption** to become and **future consumption** becomes
 - a. cheaper, more expensive
 - b. cheaper, cheaper
 - c. more expensive, cheaper
 - d. else, specify
- 5. Suppose the consumer is a **lender**. Substitution effect is **greater than** income effect. If there is an **increase in interest rate**, **current consumption** will, **future consumption** will and **saving** will
 - a. increase, increase, increase
 - b. decrease, increase, increase
 - c. decrease, increase, decrease
 - d. else, specify
- 6. If there is an **increase in current income**, current consumption will, saving will and future consumption will
 - a. increase, increase, increase
 - b. increase, increase, decrease
 - c. increase, decrease, increase
 - d. It depends on whether the consumer is a lender or borrower.
- 7. Suppose the consumer is a **borrower**. Substitution effect is **equal to** income effect. If there is an increase in interest rate, **current consumption** will, saving will
 - a. decrease, remain constant
 - b. decrease, increase
 - c. decrease, decrease
 - d. else, specify
- 8. The effect of **the government's tax cut** on consumption depends on whether the cut is temporary or permanent.
 - **If permanent**, the increase in **current consumption** will be
 - **If temporary**, the increase in **current consumption** will be ; most of the increased income is
 - a. large, small, consumed
 - b. large, small, saved
 - c. small, large, saved
 - d. else, specify