

Economics 1012A
Introduction to Macroeconomics
Fall 2008
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Second Midterm Examination
October 17, 2008

Answer all of the following questions by selecting the most appropriate answer on your bubble sheet. Be sure to read each question carefully. Each question is worth 2 points (100 points total) and will count as 20 per cent of your final course grade.

NOTE: The use of calculators and electronic translators is prohibited.

1. If prices rose by 5% and real output fell by 8%, nominal output
 - A) rose by 3%.
 - B) rose by 13%.
 - C) fell by 3%.
 - D) fell by 13%.

2. One reason expectations of inflation are important from a macroeconomic point of view is that people
 - A) tend to raise prices and wages more when they do not expect inflation.
 - B) tend to raise prices and wages more when they expect inflation.
 - C) do not seem to notice increases in the cost-of-living that were not anticipated.
 - D) seem to notice increases in the cost-of-living more when those increases were anticipated.

3. Institutionalists argue that
 - A) the liberty of individuals takes precedence over social goals.
 - B) social assistance and other social programs are unnecessary.
 - C) the government should not promote the establishment of new institutions or interfere with existing institutions.
 - D) economic analysis cannot be conducted without considering institutions.

4. If country of 270 million people has a total income of \$8 trillion, its per capita income is about
 - A) \$29.70.
 - B) \$29,700.
 - C) \$33.75.
 - D) \$33,750.

5. Inflationary expectations are important because widespread changes in inflationary expectations affect
 - A) the distribution of income.
 - B) relative prices.
 - C) actual inflation.
 - D) unexpected inflation.

6. Supporters of efficiency wage theory argue that all of the following are reasons why firms might pay wages higher than necessary to attract workers EXCEPT:
 - A) discourage shirking by workers by raising the cost of being fired.
 - B) because they are forced to by law.
 - C) increase the quality of the applicant pool.
 - D) improve worker moral.

7. Which of the following statements *best* characterizes the Classical view of business cycles?
 - A) Fluctuations in business activity occur in regular and predictable patterns.
 - B) Fluctuations in business activity are to be expected and should be accepted just as changes in the seasons are accepted.
 - C) Expansions and recessions are symptoms of underlying problems and should be addressed by macroeconomic policy.
 - D) The appropriate macroeconomic policy can eliminate fluctuations in business activity.

8. Policies that affect aggregate expenditures are
 - A) most relevant to the short-run business cycle framework.
 - B) most relevant to the long-run growth framework.
 - C) relevant to either the short-run business cycle or long-run growth frameworks.
 - D) relevant to neither the short-run business cycle nor long-run growth frameworks.

9. If you are looking for an early indication of future consumer price inflation, you would want to look at the
 - A) price level.
 - B) CPI.
 - C) GDP deflator.
 - D) raw materials price index.

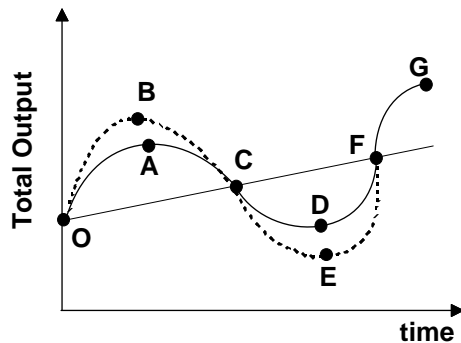
10. The natural rate of unemployment is defined as the
 - A) highest sustainable rate of unemployment achievable under existing conditions.
 - B) unemployment rate that coincides with a stable inflation rate.
 - C) unemployment rate at which there is no cyclical or structural unemployment.
 - D) the rate of unemployment that should exist according to policy makers.

11. Issues of growth are generally considered in
 - A) the short-run framework.
 - B) the long-run framework.
 - C) both the short-run and the long-run frameworks.
 - D) neither the short-run nor the long-run frameworks.

12. The business cycle consists of several stages or phases. Which is the accurate sequence?
 - A) Recession, peak, expansion, trough.
 - B) Recession, peak, trough, expansion.
 - C) Recession, expansion, peak, trough.
 - D) Recession, trough, expansion, peak.

13. Per capita real output is a
 - A) better measure of personal material consumption than real GDP.
 - B) worse measure of personal material consumption than real GDP.
 - C) better measure of the physical environment than real GDP.
 - D) worse measure of the physical environment than real GDP.

Use the following to answer question 14:



14. Refer to the graph above. An expansion occurs when the economy moves from point
 - A) O to point C.
 - B) O to point F.
 - C) D to point G.
 - D) C to point D.

15. In the late 1990s, the economy was experiencing a prolonged expansion and the unemployment rate fell to near 4 percent. Companies had a hard time finding workers. What type of unemployment was declining during this period?
 - A) Cyclical unemployment.
 - B) Full unemployment.
 - C) Structural unemployment.
 - D) Frictional unemployment.

16. If prices rose by 5% and nominal output rose by 8%, real output
- A) rose by 3%.
 - B) rose by 13%.
 - C) fell by 3%.
 - D) fell by 13%.
17. Changes in the institutional structure of the Canadian economy following the Great Depression
- A) reduced fluctuations in Canadian output.
 - B) increased fluctuations in Canadian output.
 - C) eliminated fluctuations in Canadian output.
 - D) had no effect on fluctuations in Canadian output.
18. Which of the following is NOT a measurement problem with the Consumer Price Index?
- A) Substitution bias.
 - B) Quality improvement bias.
 - C) Quality decline bias.
 - D) New product bias.
19. According to the national income accounting identity,
- A) the value of output equals income only when profits are zero.
 - B) the value of output always equals income because whenever something is produced, somebody receives an income for producing it.
 - C) the value of output equals income only when saving equals zero.
 - D) the value of output does not equal income.
20. GDP is \$7 trillion. If consumption is \$3.5 trillion, investment is \$1.4 trillion, and government purchases are \$2.1 trillion, then
- A) exports are equal to imports.
 - B) exports exceed imports.
 - C) imports exceed exports.
 - D) net exports cannot be determined from the available information.
21. Which of the following is the most volatile component of GDP?
- A) Consumption.
 - B) Investment.
 - C) Government expenditure.
 - D) Net exports.

22. GDP is the
- A) total market value of all final goods and services produced in an economy in a one-year period.
 - B) total market value of all goods and services produced in an economy in a one-year period.
 - C) total market value of all final goods and services produced by a country's citizens in a one-year period.
 - D) sum of all final goods and services produced in an economy in a one-year period.
23. In defining GDP, an example of a final good or service is
- A) a CD player purchased at a retail store by a consumer.
 - B) vegetables purchased by local restaurants to make soup.
 - C) iron ore purchased by a steel corporation.
 - D) pension benefits.
24. If depreciation does not occur, then
- A) net domestic product exceeds gross domestic product.
 - B) net domestic product equals gross domestic product.
 - C) net domestic product is less than gross domestic product.
 - D) net domestic product cannot be defined.
25. Using the expenditure approach, gross domestic product equals
- A) gross national product.
 - B) gross national product minus net exports.
 - C) the sum of consumption, investment, and government expenditures.
 - D) the sum of consumption, investment, government expenditures, and net exports.
26. Personal consumption expenditures consist of
- A) household and individual purchases of services and durable and nondurable goods.
 - B) foreign investments in Canada.
 - C) foreign plus domestic investments.
 - D) domestic investments.
27. The reason economists include only the value of final goods and services when they calculate GDP is that intermediate goods
- A) do not create value added.
 - B) do not add to economic welfare.
 - C) have no social value.
 - D) would be double counted otherwise.

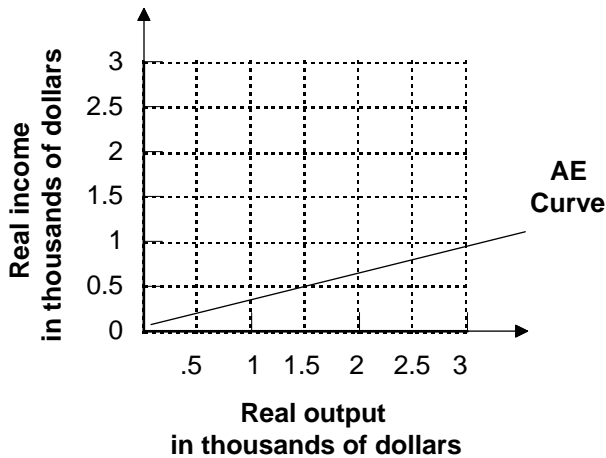
28. If economic activity increases, it follows that economic welfare
- A) increases as more goods and services become available.
 - B) decreases as more resources are depleted.
 - C) does not change since it does not depend on the level of economic activity.
 - D) may increase, decrease, or remain unchanged, depending on the nature of the increase in economic activity.
29. The movement of expenditures and factor payments through the economy is called
- A) net national product.
 - B) national income.
 - C) gross domestic product.
 - D) the circular flow.
30. If a woman divorces her house spouse (who has been cleaning the house) and hires him to continue cleaning her house for \$20,000 per year, GDP will
- A) remain constant.
 - B) increase by \$20,000 per year.
 - C) decrease by \$20,000 per year.
 - D) remain unchanged.
31. The slope of the AE curve that represents the equation $AE = 500 + 0.3Y$ equals
- A) 0.7.
 - B) 0.3.
 - C) 1.33.
 - D) 3.33.
32. According to the expenditures function, what happens to expenditures as income rises?
- A) They stay the same.
 - B) They decrease.
 - C) They increase by the same amount as income.
 - D) They increase by less than the increase in income.
33. The multiplier equation shows the relationship between
- A) autonomous expenditures and savings.
 - B) autonomous expenditures and government spending.
 - C) autonomous expenditures and the equilibrium income level.
 - D) investment spending and savings.
34. Which of the following statements is TRUE?
- A) The greater is the marginal propensity to save, the smaller is the multiplier.
 - B) The greater is the marginal propensity to consume, the smaller is the multiplier.
 - C) The greater is the marginal propensity to save, the greater is the marginal propensity to consume.
 - D) The greater is the marginal propensity to consume, the smaller is equilibrium income.

Use the following to answer question 35:

Income	Expenditures
\$ 0	\$ 500
1,000	1,167
1,500	1,500
2,000	1,833
2,500	2,167

35. In the table above, the marginal propensity to consume is
- A) \$500.
 - B) \$1,500.
 - C) 0.167.
 - D) 0.667.
36. The multiplier effect implies that
- A) investors respond to changes in interest rates.
 - B) the economy is in a recession.
 - C) a change in autonomous purchases will cause aggregate income to change by a larger amount.
 - D) consumers respond to a price change.

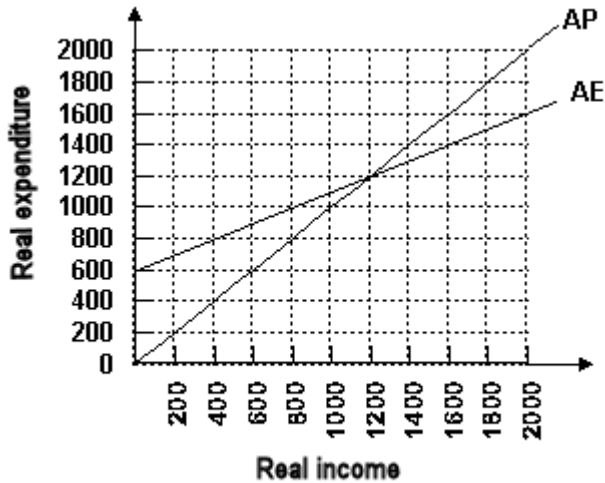
Use the following to answer question 37:



37. Refer to the graph above. The *mpc* equals
- A) 0.
 - B) 1/3.
 - C) 2/3.
 - D) 3.

38. The multiplier effect would *not* occur if
- the marginal propensity to consume equalled 1.
 - all expenditures were induced expenditures.
 - all expenditures were autonomous expenditures.
 - changes in saving did not affect the level of investment.

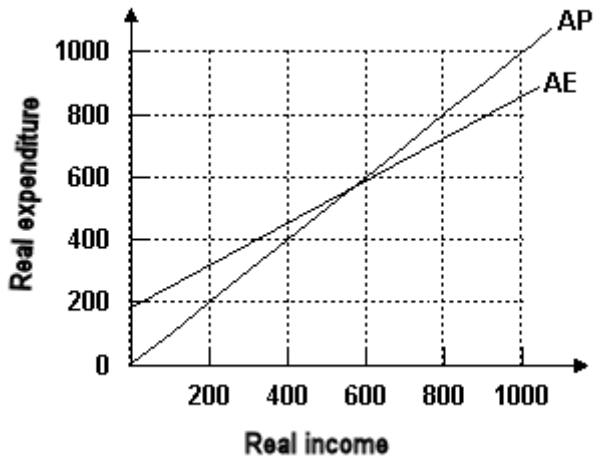
Use the following to answer question 39:



39. Refer to the graph above. Which of the following expenditures function is depicted?
- $AE = \$600 + .5Y$.
 - $AE = .5Y$.
 - $AE = \$600$.
 - $AE = \$600Y/.5$.
40. According to the paradox of thrift, the more people save,
- the lower the price level will be.
 - the higher the price level will be.
 - the lower equilibrium income will be.
 - the higher equilibrium income will be.
41. Suppose autonomous expenditures equal 500 and the *mpc* is 0.9. Now suppose the *mpc* falls to 0.8. Using the multiplier equation, we know that equilibrium income will
- decrease by 50.
 - increase by 450.
 - decrease by 450.
 - decrease by 2,500.

42. In a aggregate expenditure model, if the mpc is 0.75 and autonomous investment increased by \$20 billion, equilibrium income would increase by
- A) \$20 billion.
 - B) \$40 billion.
 - C) \$80 billion.
 - D) \$120 billion.

Use the following to answer question 43:



43. Refer to the graph above. If autonomous expenditures were to change to \$300, equilibrium real income would be
- A) greater than \$600.
 - B) \$600.
 - C) less than \$600.
 - D) indeterminate.
44. If the marginal propensity to consume is 0.9 and a decline in household wealth reduces autonomous expenditures by \$75 billion, equilibrium real GDP will
- A) increase by \$300 billion.
 - B) increase by \$750 billion.
 - C) decrease by \$750 billion.
 - D) decrease by \$500 billion.
45. The phenomenon of individuals attempting to save more but in doing so spending less and causing income to decrease is called
- A) the multiplier effect.
 - B) the paradox of thrift.
 - C) the liquidity trap.
 - D) the saving dilemma.

46. Given $AE = 6000 + 0.5Y$, equilibrium income will be
- A) \$3,000.
 - B) \$4,000.
 - C) \$8,000.
 - D) \$12,000.
47. Keynesian economists think that
- A) government policies do not affect economic activity.
 - B) government can implement policy proposals that can positively impact the economy.
 - C) most government policies would probably make things worse.
 - D) the economy ought to be left to market forces.
48. If prices are flexible,
- A) an increase in autonomous expenditures will decrease the price level.
 - B) a decrease in autonomous expenditures will increase the price level.
 - C) an increase in autonomous expenditures will increase the price level.
 - D) a change in autonomous expenditures will have no change in the price level.

Use the following to answer question 49:

Income	Expenditures
\$ 0	\$1,000
1,000	1,800
2,000	2,600
3,000	3,400
4,000	4,200
5,000	5,000

49. In the table above, if income rises from \$300 to \$400, autonomous expenditures
- A) remain equal to \$1,000.
 - B) remain equal to \$300.
 - C) rise by \$50.
 - D) rise to \$100.
50. As the marginal propensity to consume rises, the multiplier
- A) decreases.
 - B) remains constant.
 - C) increases.
 - D) changes unpredictably.

Answer Key

1. C
2. B
3. D
4. B
5. C
6. B
7. B
8. D
9. D
10. B
11. B
12. D
13. A
14. C
15. A
16. A
17. A
18. C
19. B
20. A
21. B
22. A
23. A
24. B
25. D
26. A
27. D
28. D
29. D
30. B
31. B
32. D
33. C
34. A
35. D
36. C
37. B
38. C
39. A
40. C
41. D
42. C
43. A
44. C

- 45. B
- 46. D
- 47. B
- 48. C
- 49. A
- 50. C