

ANSWER KEY

Economics 1012B
Introduction to Macroeconomics
Spring 2006
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Final Examination
April 21, 2006

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 (200 points total) and will count as 40 per cent of your final course grade. You have 120 minutes to complete this examination.

NOTE: The use of calculators is prohibited.

1. Economics is the study of

- A) the best way of training business students to be good managers who will make profits for the firms they will work for when they graduate.
- B) how to make money on the stock market.
- C) how individuals, firms, and governments make optimal choices from among a set of alternatives when facing no constraints.
- D) how individuals, firms, and governments make optimal choices from among a set of alternatives when facing scarce resources.

Ans: D

2. You bought one share of McDonalds stock for \$10, one share of Coca-Cola for \$15, and one share of Pepto-Bismol for \$20. Currently, each stock is priced at \$15 per share. Assuming no tax problems and that you cannot predict the price of either in the future, if you needed \$15, which stock would you sell?

- A) McDonalds. B) Coca-Cola. C) Pepto-Bismol. D) It doesn't matter which one you sell.

Ans: D

3. Economic reasoning would argue that there

- A) is an opportunity cost to everything.
- B) is an opportunity cost to most things.
- C) is an opportunity cost to only economic things.
- D) is an opportunity cost to nothing.

Ans: A

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4. Economics is a branch of
A) the natural sciences. B) the social sciences. C) political science. D) philosophy.

Ans: B

5. "Price controls are bad for the economy and should not be used" is an example of
A) positive economics. C) the science of economics.
B) normative economics. D) Marshallian economics.

Ans: B

6. Which of the following statements about market economies is *false*?
A) It is based on private property and the market.
B) It does not need a rationing mechanism.
C) It gives private property rights to individuals.
D) It relies on market forces to coordinate economic activity.

Ans: B

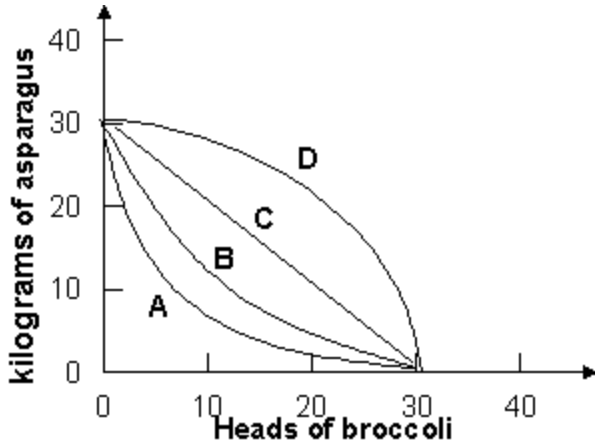
7. Investment in capital goods is one way to increase the standard of living in the future. Investment in capital goods, however, means that we must forgo consumption today. One of the tradeoffs facing an economy is between consumption today and consumption in the future. The following table presents such a trade off. Which of the following statements based upon the table is TRUE?

Current consumption	Future consumption
800	100
750	260
650	340
600	380
550	400

- A) The opportunity cost of increasing current consumption from 750 to 800 is greater than the opportunity cost of increasing current consumption from 550 to 600.
B) The opportunity cost of increasing future consumption from 100 to 260 is greater than the opportunity cost of increasing future consumption from 380 to 400.
C) The opportunity cost of increasing current consumption by 50 is the same whether you start at 550 or start at 750 consumption units.
D) The opportunity cost of increasing future consumption by 50 is the same whether you start at 260 or 340.
E) None of the above.

Ans: A

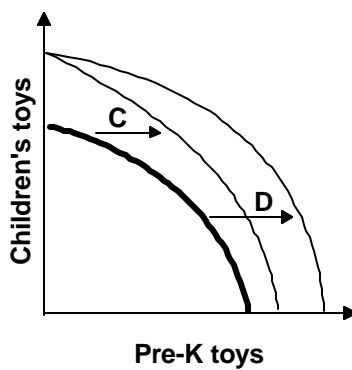
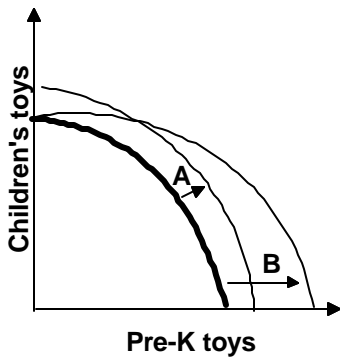
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8. Refer to the graph above. Given the following production possibility table for growing broccoli and asparagus in a 320 square-metre garden in one season, the relevant production possibility curve is

Broccoli	Asparagus
30	0
25	11
20	18
15	23
10	26
5	28
0	30

A) A B) B C) C D) D
 Ans: D



9. Refer to the graphs above. Which shift explains what would happen to the production possibility curve if improved technologies increased the production of pre-kindergarten (Pre-K) toys by 25% and the production of children's toys by 50%?
 A) A. B) B. C) C. D) D.
 Ans: C

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10. The principle of increasing marginal opportunity holds in which of the following cases?
A) All inputs are equally adaptable to the production of all goods.
B) The production possibility curve is a downward sloping straight line.
C) All inputs are not equally adaptable to the production of all goods.
D) Each input can be used to produce more than one good.

Ans: C

11. Under feudalism, serfdom was maintained primarily through
A) market forces. B) tradition. C) supply and demand. D) the church.

Ans: B

12. Profit is
A) the same as cost.
B) the same as revenue.
C) what's left over from total revenue after all of the appropriate costs have been subtracted.
D) what's left over from total cost after all of the appropriate revenues have been subtracted.

Ans: C

13. Which group has ultimate control over the economy?
A) Business. B) Households. C) Multinationals. D) Government.

Ans: B

14. Corporate advertising
A) may reinforce consumer sovereignty. C) cannot affect consumer sovereignty.
B) may undermine consumer sovereignty. D) makes consumer sovereignty meaningless.

Ans: B

15. Suppose the price of a banjo in Canada is \$60 and the exchange rate between the dollar and the British pound is \$1.5 per pound. In the absence of transportation costs and taxes, a British resident who wished to buy a Canadian banjo would have to pay
A) 20 pounds. B) 40 pounds. C) 90 pounds. D) 120 pounds.

Ans: B

16. All of the following would be expected to cause the supply of wool to decrease *except*
A) a decrease in the price of wool.
B) a decrease in the number of wool producers.
C) an increase in the cost of raising sheep.
D) an increase in wages paid to workers in the wool industry.

Ans: A

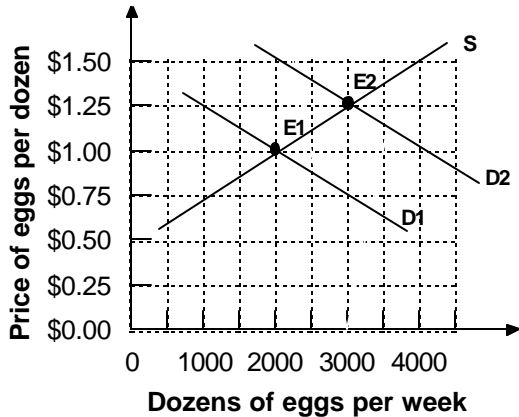
17. The more the current price exceeds the equilibrium price
A) the greater the resulting shortage will be. C) the greater the resulting surplus will be.
B) the smaller the resulting shortage will be. D) the smaller the resulting surplus will be.

Ans: C

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18. If there are many more substitutes for good A than for good B
- A) the demand curve for good A will likely be flatter.
 - B) the demand curve for good B will likely be flatter.
 - C) you can't say anything about the likely relative flatness of the demand curves.
 - D) the demand curve for good B will likely shift out further.

Ans: A



19. Refer to the graph above. The figure shows the demand and supply curves for eggs and shows two equilibrium points, E1 and E2. Suppose the prevailing price of a dozen eggs is \$1.25 and the demand curve is given by D1. Which of the following would result?
- A) A surplus of 2000 dozen eggs per week.
 - B) A shortage of 2000 dozen eggs per week.
 - C) A surplus of 3000 dozen eggs per week.
 - D) A tendency for the price of eggs to increase.

Ans: A

20. Suppose a recent and widely circulated medical article reports new benefits of exercise. Simultaneously, the price of the parts needed to make bikes falls. What is the likely effect on the equilibrium price and quantity of exercise bikes sold?
- A) Price of exercise bikes decreases and quantity sold remains the same.
 - B) Price of exercise bikes increases and quantity sold also increases.
 - C) Price of exercise bikes remains the same and quantity sold increases.
 - D) The change in price is ambiguous, but the quantity sold increases.

Ans: D

21. Which of the following problems is *not* one of the central concerns of macroeconomics?
- A) Product pricing.
 - B) Growth.
 - C) Business cycles.
 - D) Unemployment.

Ans: A

22. Fluctuations around the long-term growth rate are called
- A) recessions.
 - B) depressions.
 - C) expansions.
 - D) business cycles.

Ans: D

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23. The unemployment rate that coincides with a stable inflation rate is
- A) zero.
 - B) called the natural rate of unemployment.
 - C) called the optimal rate of unemployment.
 - D) unknown.
- Ans: B
24. Given that teenage workers have a greater tendency to become unemployed, an increase in the proportion of the labour force aged 16 to 19 would tend to
- A) reduce both the actual unemployment rate and the target unemployment rate.
 - B) reduce the actual unemployment rate, but increase the target unemployment rate.
 - C) increase the actual unemployment rate, but reduce the target unemployment rate.
 - D) increase both the actual unemployment rate and the target unemployment rate.
- Ans: D
25. According to Okun's rule of thumb, an increase in the rate of unemployment from 6 percent to 8 percent would be expected to cause income in the economy to
- A) fall by 4 percent.
 - B) rise by 4 percent.
 - C) fall by 2 percent.
 - D) rise by 2 percent.
- Ans: A
26. If prices have risen by 5% in one year, real output
- A) must have risen by 5% in that same year.
 - B) must have risen by less than 5% in that same year.
 - C) must have risen by more than 5% in that same year.
 - D) may have changed by any amount in that same year.
- Ans: D
27. The value of intermediate goods is
- A) included in both GDP and GNI.
 - B) included in GDP but not GNI.
 - C) included in GNI but not GDI.
 - D) excluded from both GDP and GNI.
- Ans: D
28. Value added by individuals and business in a nation in a year equals
- A) the value of intermediate products.
 - B) the value of investment goods.
 - C) total profits.
 - D) GDP.
- Ans: D

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	In billions of dollars
Consumption	3,600
Investment	800
Transfer payments	750
Government expenditures	1,000
Exports	650
Imports	450
Net foreign factor income	-30

29. Calculate GDP using the table above.

A) 5,570. B) 5,600. C) 6,050. D) 6,320.

Ans: B

30. If you know that a meal costing \$40 in Canada would cost \$2 in Bangladesh and that this is representative of the relative prices of most goods, you also know that

- A) purchasing power parity would decrease comparative GDP for Bangladesh.
- B) purchasing power parity would decrease comparative GDP for Canada.
- C) GDP using market prices would overstate the value of output for Bangladesh.
- D) GDP using market prices would understate the value of output for Canada.

Ans: B

31. Suppose Botswana doubles its income in 6 years while South Africa doubles its income in 9 years. According to the Rule of 72, the growth rate in Botswana is

- A) 3 percentage points higher than the growth rate in South Africa.
- B) 4 percentage points higher than the growth rate in South Africa.
- C) 8 percentage points higher than the growth rate in South Africa.
- D) 12 percentage points higher than the growth rate in South Africa.

Ans: B

32. Per capita growth

- A) occurs when the population is growing.
- B) occurs when output is growing.
- C) occurs when there is an increase in goods and services per person.
- D) improves the distribution of income.

Ans: C

33. Suppose the quantities of labour, land, and capital each increase by 10 percent and output also increases by 10 percent. In that case, returns to scale are

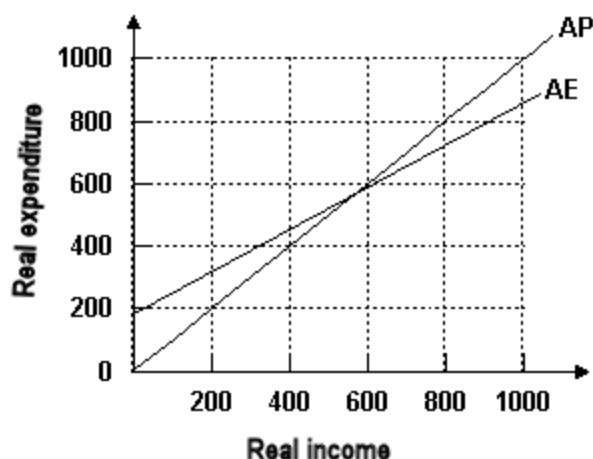
- A) decreasing. B) constant. C) increasing. D) not defined since more than one input is changing.

Ans: B

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34. If the skills of labour are continually increasing
- A) increasing returns to scale will be present.
 - B) employment will eventually decline.
 - C) increases in physical capital may not exhibit diminishing marginal productivity.
 - D) growth in per capita income will decline.
- Ans: C
35. Learning by doing implies that
- A) greater experience increases efficiency.
 - B) greater experience increases production costs.
 - C) diminishing marginal productivity occurs more rapidly.
 - D) patents are more valuable.
- Ans: A
36. Which of the following policies is most likely to promote per capita growth?
- A) An income tax.
 - B) A cap on interest rates for saving accounts.
 - C) A policy that discourages foreign investment.
 - D) A consumption tax.
- Ans: D
37. Expenditures that would exist at an income level of zero are called
- A) endogenous expenditures.
 - B) aggregate expenditures.
 - C) induced expenditures.
 - D) autonomous expenditures.
- Ans: D
38. If a family's expenditures increase from \$25,000 to \$30,000 per year when its income increases from \$30,000 to \$37,500, its autonomous expenditures
- A) do not change.
 - B) equal \$5,000.
 - C) increase by \$7,500.
 - D) change by an amount that cannot be determined without more information.
- Ans: A
39. The *mps* is larger, other things equal, when
- A) the multiplier is larger.
 - B) the multiplier is smaller.
 - C) the *mpc* is larger.
 - D) the economy is in equilibrium.
- Ans: B

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40. Refer to the graph above. If the mpc were to change to $1/3$, equilibrium real income would be
A) greater than \$600. B) \$600. C) less than \$600. D) indeterminate.

Ans: C

41. Because of political unrest in South Korea, investment declines by 40. If the mpc is 0.75, income would likely decline by
A) 30. B) 53.33. C) 120. D) 160.

Ans: D

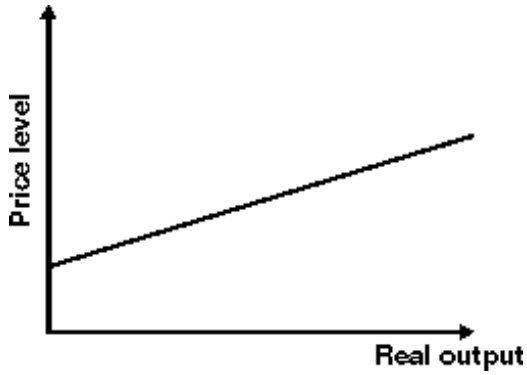
42. All of the following statements about the AS/AD model are true *except*
A) on the vertical axis is the price of all goods.
B) on the horizontal axis is the aggregate output level.
C) the model depends on the concept of opportunity cost.
D) it can incorporate both Keynesian and Classical views of the economy.

Ans: C

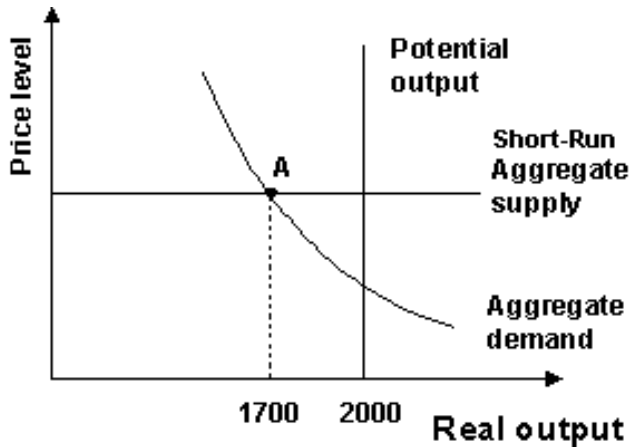
43. A rise in foreign income will most likely cause
A) a reduction in Canadian exports, so the Canadian aggregate demand curve shifts left.
B) a reduction in Canadian exports, so the Canadian aggregate demand curve shifts right.
C) an increase in Canadian exports, so the Canadian aggregate demand curve shifts left.
D) an increase in Canadian exports, so the Canadian aggregate demand curve shifts right.

Ans: D

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44. Refer to the graph above. The curve in the graph is called
 A) an aggregate demand curve. C) a potential output curve.
 B) a short-run aggregate supply curve. D) a supply curve.
 Ans: B
45. The SAS curve is most likely to shift up if
 A) productivity rises but wages fall. C) productivity falls but wages rise.
 B) both productivity and wages rise. D) both productivity and wages fall.
 Ans: C
46. If aggregate demand is less than potential output, eventually the short-run aggregate supply curve will shift
 A) left and eliminate the recessionary gap. C) left and eliminate the inflationary gap.
 B) right and eliminate the recessionary gap. D) right and eliminate the inflationary gap.
 Ans: B
47. A cut in defence spending is an example of
 A) an expansionary monetary policy. C) an expansionary fiscal policy.
 B) a contractionary monetary policy. D) a contractionary fiscal policy.
 Ans: D



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48. Refer to the graph above. If the economy in the graph is at point A, the most appropriate fiscal policy would be

- A) an increase in the income tax rate.
- B) a decrease in transfer payments.
- C) an increase in government spending.
- D) a reduction of the exchange rate.

Ans: C

49. Printing money

- A) is the most desirable way to finance a deficit.
- B) is superior to issuing bonds because it does not affect the debt.
- C) is inferior to issuing bonds because it creates more inflation.
- D) cannot be used to finance a deficit.

Ans: C

50. The budget deficit that would exist even if the economy were at potential income is called a

- A) passive deficit.
- B) real deficit.
- C) structural deficit.
- D) nominal deficit.

Ans: C

51. Which of the following is *not* one of the functions of money?

- A) Medium of exchange.
- B) Unit of account.
- C) Standard of economic well-being.
- D) Store of wealth.

Ans: C

52. An asset can be a store of value

- A) only if it is liquid.
- B) only if it is not liquid.
- C) whether it is liquid or not.
- D) only if it is also a medium of exchange.

Ans: C

53. If the Bank of Canada issued too little money, money's relative price would

- A) fall, and the money price of goods would rise.
- B) rise, and the money price of goods would fall.
- C) fall, and the money price of goods would fall.
- D) rise, and the money price of goods would rise.

Ans: B

54. Your cheque is as good as money as long as

- A) the Bank of Canada accepts it.
- B) people accept it.
- C) you replace it with currency within a stated period of time.
- D) you have an interest-bearing chequing account.

Ans: B

55. Fisher's version of the quantity theory predicts that an increase in the quantity of money will

- A) increase the transaction velocity of money.
- B) increase the price level.
- C) increase the Cambridge k .
- D) decrease the price level.

Ans: B

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56. If $M = 6,000$, $P = 1.2$, and $Y = 5,000$, what is the value of k ?

- A) 2. B) 1.4. C) 1. D) 9.2.

Ans: C

57. Which of the following is the best example of a real effect?

- A) An increase in the quantity of money increases real GDP.
B) An increase in the quantity of money increases nominal GDP.
C) An increase in the quantity of money increases the price level.
D) An increase in the quantity of money decreases nominal GDP.

Ans: A

58. The transactions demand for money

- A) is positively related to nominal income. C) is negatively related to the price level.
B) is negatively related to nominal income. D) is negatively related to real GDP.

Ans: A

59. The precautionary demand for money

- A) is money that is needed to undertake purchases of goods and services.
B) is money needed to meet unforeseen expenses.
C) considers how much money is held in a portfolio of assets.
D) is negatively related to the price level.

Ans: B

60. Suppose that in January newly issued government t-bills had a price of \$975, but in July of the same year, newly issued government t-bills with the same maturity and face value had a price of \$950. From this we can conclude that

- A) the yield on the January bonds was higher.
B) the yield on the July bonds was higher.
C) we need information on the nominal rate of interest before we can say what happened to yields.
D) we need information on the real rate of interest before we can say what happened to yields.

Ans: B

61. Which of the following money demand functions is consistent with the Keynesian approach to money demand?

- A) $\frac{M_d}{P} = 1000 + 0.7Y + 2000i$ C) $\frac{M_d}{P} = 1000 - 0.7Y + 2000i$
B) $\frac{M_d}{P} = 1000 + 0.7Y - 2000i$ D) $\frac{M_d}{P} = 1000 - 0.7Y - 2000i$

Ans: B

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62. All of the following are true, EXECPT:

- A) the steeper the money demand curve, the flatter the AD curve.
- B) the steeper the investment schedule, the flatter the AD curve.
- C) the greater the investment multiplier, the flatter is the AD curve.
- D) the more sensitive money demand in the aggregate is to the rate of interest, the flatter the money demand curve.

Ans: B

63. Which of the following is true?

- A) The steeper the money demand curve, the flatter the AD curve.
- B) The steeper the investment schedule, the flatter the AD curve.
- C) The greater the investment multiplier, the steeper the AD curve.
- D) The more sensitive money demand in the aggregate is to the rate of interest, the steeper the money demand curve.

Ans: A

64. Which of the following is NOT likely to be the result of a decrease in interest rates?

- A) An increase in investment.
- B) An increase in money demand.
- C) A decrease in investment.
- D) An increase in Canadian exports.

Ans: C

65. An increase in interest rates increases

- A) consumption spending.
- B) money demand.
- C) investment.
- D) the value of the Canadian dollar.

Ans: D

66. Money neutrality implies that

- A) changes in the money supply will have real effects.
- B) an increase in the money supply will cause investment to increase.
- C) changes in the money supply will only cause the price level to change by the same proportion.
- D) changes in the money supply will only cause consumption spending to change by the same proportion.

Ans: C

67. The empirical evidence the textbook presents suggests that the following is NOT true:

- A) Money neutrality does not hold for Canada.
- B) Money demand is strongly associated with the CPI.
- C) Money demand is not very sensitive to the rate of interest.
- D) Money demand is strongly related to income.

Ans: A

ANSWER KEY

68. The empirical evidence the textbook presents suggests that the following is NOT true:

- A) Money neutrality holds for Canada.
- B) Money demand is strongly associated with the CPI.
- C) Money demand is not very sensitive to the rate of interest.
- D) Money demand is only weakly related to income.

Ans: D

69. Liquidity preference refers to

- A) the choice between holding bonds and money.
- B) the choice between holding cash and keeping money in a bank account.
- C) the need to hold money to meet any unforeseen expenses.
- D) the need to hold money to make transactions.

Ans: A

70. The normal rate of interest is

- A) the rate of interest the economy will return to under normal conditions.
- B) the real rate of interest plus the rate of inflation.
- C) the rate of interest that equates money demand and money supply.
- D) the rate of interest for savings accounts.

Ans: A

71. The velocity of money is

- A) the average number of months a dollar is held before being spent.
- B) the average number of times each dollar is spent each year.
- C) constant.
- D) inversely related to output.

Ans: B

72. If the money supply is 500 and the velocity is 6, then real GDP

- A) is 83.33.
- B) is 500.
- C) is 3,000.
- D) cannot be determined.

Ans: D

73. Which of the following is likely to be the result of an increase in interest rates?

- A) An increase in investment.
- B) An increase in money demand.
- C) A decrease in investment.
- D) An increase in Canadian exports.

Ans: C

74. Monetary policy *directly* affects all of the following EXCEPT

- A) the money supply.
- B) the banking system.
- C) the availability of credit.
- D) the budget deficit.

Ans: D

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75. Monetary policy affects
A) only inflation. B) only output. C) both inflation and output. D) neither inflation nor output.
Ans: C
76. In the SAS/AD model (when prices are fixed), monetary policy has the GREATEST effect on *real output* when
A) both the AD and SAS curves shift. C) only the SAS curve shifts.
B) only the AD curve shifts. D) neither the SAS nor the AD curves shift.
Ans: B
77. A monetary policy that affects nominal income but *not* real income must result in the shift of
A) both the AD and SAS curves. C) only the SAS curve.
B) only the AD curve. D) neither the SAS curve nor the AD curve.
Ans: A
78. An expansionary monetary policy that affects the price level but not real output, must result in the shift of
A) both the AD and SAS curves. C) only the SAS curve.
B) only the AD curve. D) neither the SAS curve nor the AD curve.
Ans: A
79. If the economy is in the Keynesian range, an expansionary monetary policy
A) increases both nominal and real income. C) increases nominal income but not real income.
B) increases real income but not nominal income. D) doesn't increase real or nominal income.
Ans: A
80. If the economy is in the Classical range, a contractionary monetary policy
A) decreases both nominal and real income. C) decreases nominal income but not real income.
B) decreases real income but not nominal income. D) doesn't decrease real or nominal income.
Ans: C
81. If prices are inflexible, monetary policy
A) affects both nominal and real income. C) affects nominal income but not real income.
B) affects real income but not nominal income. D) doesn't affect real or nominal income.
Ans: A

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82. If a contractionary monetary policy reduces nominal income but not real income, it must be true that prices

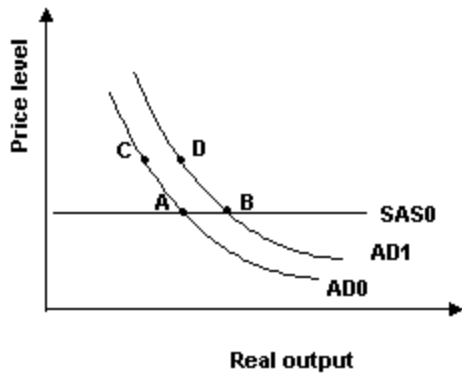
- A) are perfectly flexible.
- B) are at least partially flexible.
- C) are completely inflexible.
- D) have not fully adjusted to the change in aggregate demand.

Ans: A

83. If nominal income increases by 4 percent and the price level increases by 3 percent, real income must

- A) increase by 7 percent.
- B) increase by 1 percent.
- C) decrease by 1 percent.
- D) decrease by 7 percent.

Ans: B



84. Refer to the graph above. Suppose the economy is initially at A but then the Bank of Canada adopts an expansionary monetary policy. If the economy is in the Classical range, the new equilibrium will be at

- A) A.
- B) B.
- C) C.
- D) D.

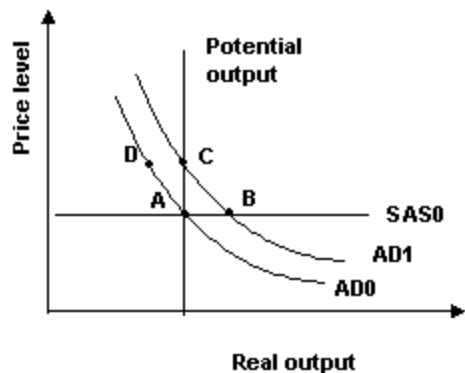
Ans: D

85. Refer to the graph above. Suppose the economy is initially at A but the Bank of Canada adopts an expansionary monetary policy. If prices are neither perfectly flexible nor rigidly fixed, the new equilibrium will

- A) be at B.
- B) be at C.
- C) be at D.
- D) not be at B, C, or D.

Ans: D

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86. Refer to the graph above. Suppose the economy is initially at A but then the Bank of Canada adopts an expansionary monetary policy that shifts the AD curve to AD1. In the long run, this policy will cause the economy to move to point

- A) A. B) B. C) C. D) D.

Ans: C

87. Which of the following statements about the Bank of Canada is false?

- A) The Bank of Canada is a Crown corporation.
B) The Governor of the Bank is appointed by the Prime Minister from among the elected members of the House of Commons.
C) The Board of Directors of the Bank are nonspecialists in monetary economics who have little influence over the direction of monetary policy.
D) The Bank acts as the government's banker.

Ans: B

88. Supporters of the current structure of the Bank of Canada argue that

- A) the Governor of the Bank needs to be insulated from electoral politics and that the current structure achieves this.
B) effectively the Minister of Finance already controls the day-to-day operations of the Bank of Canada.
C) the Bank has a long history of implementing effective countercyclical policies without government interference.
D) price stability should not be achieved in the short run at the expense of the unemployed.

Ans: A

89. Actual decisions about monetary policy are made by

- A) the Chairman of Treasury Board.
B) the Prime Minister.
C) the Minister of Industry, Trade, and Commerce.
D) the Governor of the Bank of Canada in consultation with senior staff.

Ans: D

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90. Chartered banks with a deficit position in the clearing and settlement of the Large Value Transfer System typically cover their deficit with
- A) loans on the overnight market from CPA members who have a surplus in the Large Value Transfer System for that day.
 - B) loans on the overnight market from the Bank of Canada.
 - C) a withdrawal from their accounts at the Bank of Canada.
 - D) the sale of highly liquid treasury bills.

Ans: A

91. Many interest rates are related to the overnight financing rate through
- A) the open market operations of the Bank of Canada.
 - B) the term structure of interest rates.
 - C) the fixed relation between the prime rate and the overnight rate.
 - D) cash management operations.

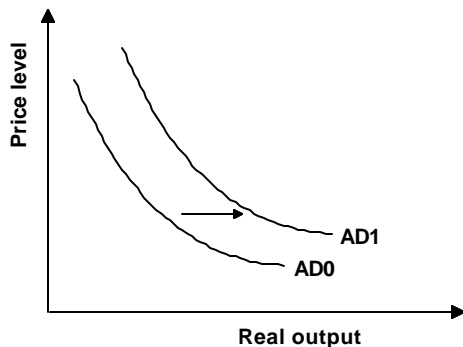
Ans: B

92. If the Bank of Canada wanted to restrain aggregate demand, it could
- A) raise the target range for the overnight financing rate, thereby reducing interest rates throughout the economy.
 - B) raise the target range for the overnight financing rate, thereby increasing interest rates throughout the economy.
 - C) lower the target range for the overnight financing rate, thereby reducing interest rates throughout the economy.
 - D) lower the target range for the overnight financing rate, thereby increasing interest rates throughout the economy.

Ans: B

93. When the Bank of Canada reduces the bank rate, this sends a signal to banks that the Bank of Canada wants
- A) the money supply to expand.
 - B) the money supply to contract.
 - C) the overnight financing rate to increase.
 - D) banks to increase their desired reserve ratio.

Ans: A



ANSWER KEY

94. Refer to the graph above. The Bank of Canada expects an undesired change in aggregate demand from AD0 to AD1 this year. To offset that change, the Bank of Canada should
- A) engage in open market purchases of bonds.
 - B) raise the bank rate.
 - C) lower the bank rate.
 - D) lower the overnight financing rate.
- Ans: B
95. If the Bank of Canada buys securities through its open market operations, the money supply will
- A) decrease.
 - B) remain the same.
 - C) increase.
 - D) increase or decrease depending on the bank rate.
- Ans: C
96. If the Bank of Canada sells government bonds, you might expect
- A) a decrease in interest rates.
 - B) an increase in interest rates.
 - C) an increase in the money supply.
 - D) a fall in the bank rate.
- Ans: B
97. Bank of Canada sales of government bonds _____ bank reserves and _____ the money supply.
- A) increase, increase
 - B) decrease, decrease
 - C) decrease, increase
 - D) increase, decrease
- Ans: B
98. Which of the following monetary policies raises aggregate demand and output?
- A) An open market sale of government securities.
 - B) An open market purchase of government securities.
 - C) An increase in the bank rate.
 - D) An increase in the overnight financing rate.
- Ans: B
99. Countercyclical monetary policy in the AS/AD model involves
- A) a contractionary monetary policy throughout the business cycle.
 - B) an expansionary monetary policy throughout the business cycle.
 - C) a contractionary monetary policy during boom periods and expansionary monetary policy during recession.
 - D) a contractionary monetary policy during recession and expansionary monetary policy during boom periods.
- Ans: C

ANSWER KEY

100. In 1996, the lead sentence in a *Wall Street Journal* article read, "Tight job markets, rising wages, and the economy's continued strength put more pressure on the Federal Reserve (the American central bank) to raise short-term interest rates." If the Federal Reserve responded to this pressure, it would
- A) raise interest rates to increase investment spending and lower real output, thus reversing the economy's strength.
 - B) raise interest rates to decrease investment spending and lower real output, thus reversing the economy's strength.
 - C) lower interest rates to increase investment spending and raise real output, thus adding to the economy's strength.
 - D) lower interest rates to decrease investment spending and raise real output, thus adding to the economy's strength.
- Ans: B

Have a great summer!