

McGill University

Faculty of Arts

Department of Economics

Macroeconomic Analysis and Applications

Economics 209B (Section 02)

Final Examination

Version 1

Examiner: Prof. Alex G. Vicas
Associate Examiner: Prof. R. Rowley

Thursday, April 14, 2005
9:00-12:00

INSTRUCTIONS

There are 123 questions on the 30 pages following this one. Answer all questions on the scantron card provided.

- You may use any calculators. You may use a language dictionary.
- You will be given 0.81 points for every question answered correctly, and zero points for questions not answered or not answered correctly.
- Verify that you have entered correctly your name, examination version number, and student number on the scantron card. If the computer fails to read your student number or version number, you will not receive a grade for this exam.
- If you find that more than one choice is correct, make a judgment about which choice provides the best answer. The way you exercise this option to make a choice is part of the grading process...

WARNING: The Examination Security Monitor Program detects pairs of students with unusually similar answer patterns on multiple-choice exams. Data generated by this program can be used as admissible evidence, either to initiate or corroborate an investigation or a charge of cheating under Section 16 of the Code of Student Conduct and Disciplinary Procedures.

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

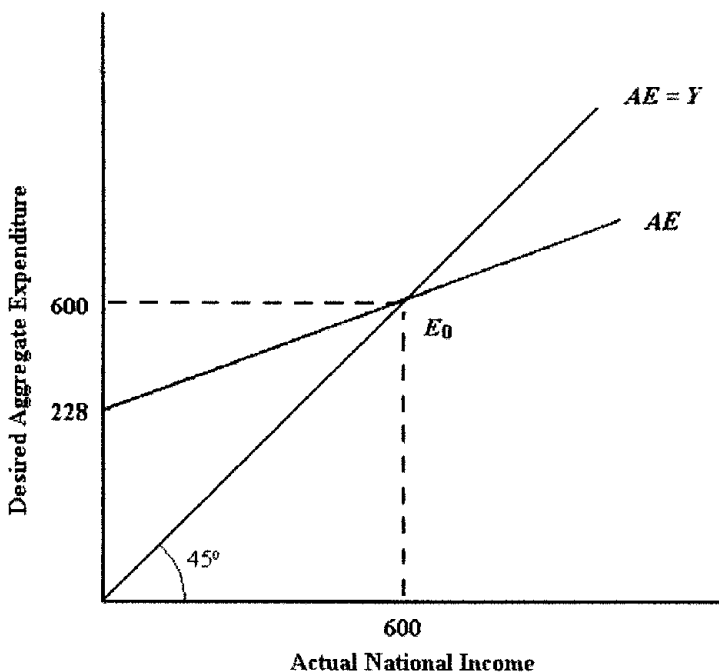


FIGURE 22-1

- 1) In Figure 22-1, the slope of the AE curve (z) is approximately 1) _____
 - A) 0.50.
 - B) 0.62.
 - C) 1.00.
 - D) 1.50.
 - E) 2.63.

- 2) We have the following macro model: $C = 120 + 0.86Y$, $I = 300$, $G = 520$, $T = 0$, $X = 180$, $IM = 0.12Y$. 2) _____
 The vertical intercept of the AE curve is _____.
 - A) 120.0
 - B) 420.0
 - C) 600.0
 - D) 828.8
 - E) 1 120.0

- 3) An upward shift in the net export function can be caused by 3) _____
 - A) an increase in domestic national income.
 - B) an increase in foreign national income.
 - C) a decrease in the exchange rate.
 - D) a decrease in foreign prices.
 - E) an increase in domestic prices.

- 4) If net exports is greater than zero an economy is 4) _____
 - A) accumulating foreign assets.
 - B) depleting foreign assets.
 - C) not investing.
 - D) taxes must equal government expenditure.
 - E) not saving.

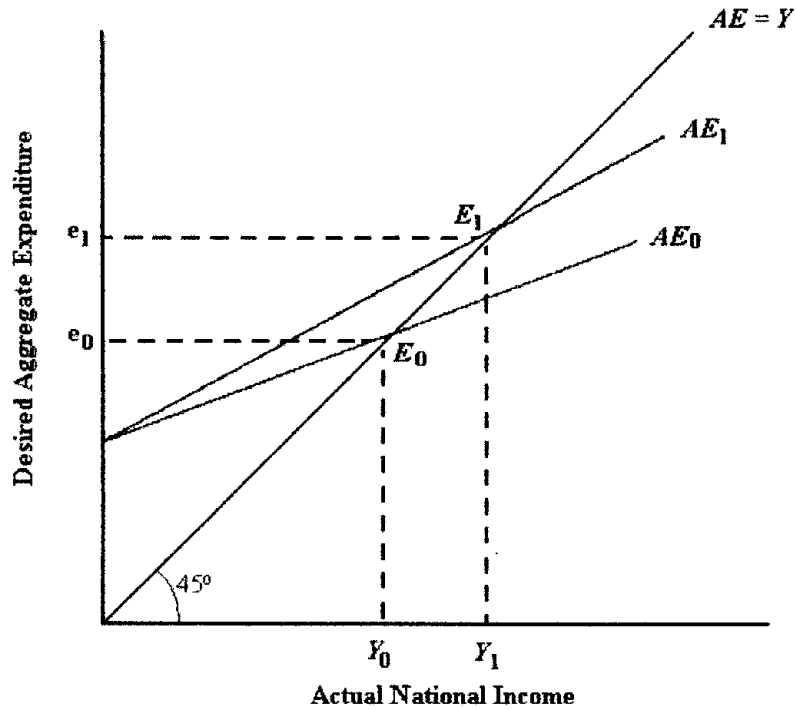


FIGURE 22-2

- 5) Using Figure 22-2, the rotation from AE_1 to AE_0 causes the value of the marginal propensity to spend to _____ and the multiplier to multiplier to _____. 5) _____
- A) fall, rise
 - B) fall; fall
 - C) rise; fall
 - D) remain the same; fall
 - E) rise; rise
- 6) Using Figure 22-2, the rotation from AE_0 to AE_1 is caused by 6) _____
- A) lower government spending.
 - B) lower tax rates.
 - C) higher tax rates.
 - D) a balanced budget.
 - F) higher government spending.
- 7) Using Figure 22-2, the rotation from AE_1 to AE_0 is caused by 7) _____
- A) a balanced budget.
 - B) higher tax rates.
 - C) lower government spending.
 - D) lower tax rates.
 - E) higher government spending.

- 8) In an open economy with government, a decrease in the equilibrium level of income could be caused by 8) _____
- A) an increase in government spending.
 - B) a decrease in taxes at all levels of income.
 - C) a decrease in desired consumption at all levels of income.
 - D) a decrease in the desired level of imports at all levels of income.
 - E) a decrease in the desired level of saving at all levels of income.
- 9) Over the intermediate (middle) range of the short run *AS* curve, a rightward shift of the *AD* curve will result in 9) _____
- A) a decrease in output and an increase in prices.
 - B) a decrease in both output and prices.
 - C) an increase in output but not prices.
 - D) an increase in both output and prices.
 - E) an increase in prices but not output.
- 10) An increase in national income associated with a shift in the *AD* curve to the right could result from a rise in 10) _____
- A) savings.
 - B) imports.
 - C) government transfer payments to households.
 - D) income-tax rates.
 - E) prices.
- 11) The price level and desired aggregate expenditure are connected to each other in a relationship that is 11) _____
- A) direct in some circumstances and inverse in others.
 - B) direct and proportional.
 - C) direct and exponential.
 - D) inverse and proportional.
 - E) direct and nonproportional.
- 12) A rightward shift in the short run *AS* curve implies that 12) _____
- A) at any given price level, a higher level of national output will be supplied.
 - B) the same national output will be produced, but only at a higher price level.
 - C) there is a decrease in aggregate supply.
 - D) there is a demand shock.
 - E) at any given price level, a lower level of national output will be supplied.

- 13) Assuming a constant price level, an increase in autonomous consumption will cause the *AE* curve to shift 13) _____
- A) downward and the *AD* curve shifting to the left.
 - B) downward and the *AD* curve shifting to the right.
 - C) upward and a movement to the right along the *AD* curve.
 - D) upward and the *AD* curve shifting to the left.
 - E) upward and the *AD* curve shifting to the right.
- 14) If the short run *AS* is very steep (almost vertical) then an increase in aggregate demand, will result in 14) _____
- A) almost no change in prices but a large increase in real GDP.
 - B) an increase in the price level with almost no change in real GDP.
 - C) a decrease in real GDP and a very small decrease in the price level.
 - D) a decrease in the price level and a very small decrease in real GDP.
 - E) an equal increase the price level and in real GDP.
- 15) If the short run *AS* curve is very steep (almost vertical) and the *AD* curve shifts to the left, the result is 15) _____
- A) an increase in the price level and a decrease in national income.
 - B) no change in either price level or output.
 - C) a decrease in the price level with almost no change in national income.
 - D) a decrease in the price level and an increase in national income.
 - E) both an increase in price level and national income.
- 16) In the short run, the aggregate supply curve has a positive slope because, as the price level rises, business firms will 16) _____
- A) accumulate inventories.
 - B) produce the same output, but at higher prices.
 - C) be compensated for the extra costs incurred to produce more output.
 - D) experience rising factor prices.
 - E) produce less in response to falling profits.
- 17) A rise in the domestic price level 17) _____
- A) makes domestic goods more attractive to foreigners.
 - B) raises the real burden of repaying a fixed money value debt.
 - C) makes foreign goods less attractive to domestic residents.
 - D) lowers the real value of all assets denominated in money units.
 - E) causes a decrease in saving.
- 18) Unit wage costs will rise if 18) _____
- A) wages rise.
 - B) the government reduces payroll taxes.
 - C) there is a rise in the price of oil.
 - D) wage and price controls are in effect.
 - E) wage increases exceed productivity increases.

- 19) An increase in aggregate demand (a positive demand shock) will cause
- A) a movement of the equilibrium point to the right along the short run *AS* curve.
 - B) the price level and real national income to both decrease.
 - C) a shift in the short run *AS* curve.
 - D) a decrease in one or more of the components of desired aggregate expenditure.
 - E) the unemployment rate to rise.

19) _____

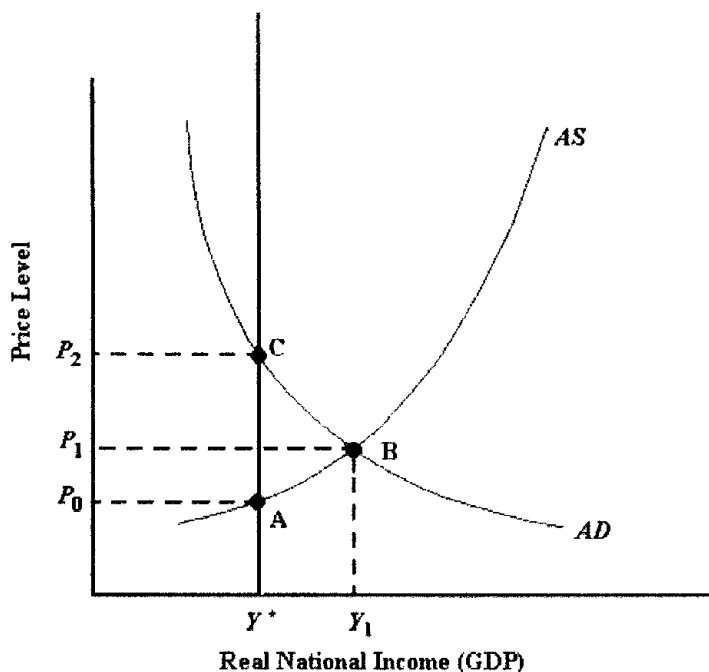


FIGURE 24-2

- 20) Referring to Figure 24-2, where the economy is in equilibrium at Y_1 , if wages are sticky the government could use fiscal policy to close the gap by
- A) an increase in government spending.
 - B) an increase in current interest rates.
 - C) a decrease in government spending.
 - D) an increase in personal and corporate income taxes.
 - E) a decrease in government spending and an increase in taxes.
- 21) Suppose that the short run *AS* curve is relatively steep. If the *AD* curve shifts to the left, then the price level will _____ and national output will _____.
- A) increase slightly; significantly decrease
 - B) fall sharply; decrease slightly.
 - C) fall sharply; will not change.
 - D) increase slightly; significantly increase
 - E) increase sharply; increase slightly

20) _____

21) _____

- 22) Progressive income taxes in Canada can be considered to be automatic stabilizers because tax _____
- A) taxes are changed through discretionary fiscal policy to create surpluses in recessions.
 - B) rates and revenues increase when income increases, thereby offsetting some of the increase in aggregate demand.
 - C) revenues decrease when income increases, thereby intensifying the increase in aggregate demand.
 - D) taxes are changed through discretionary fiscal policy to keep the budget balanced.
 - E) rate structures can be changed when the Minister of Finance brings down a new budget.
- 23) The Phillips curve describes the relationship between _____
- A) aggregate demand and the price level.
 - B) the money supply and interest rates.
 - C) unemployment and the interest rate.
 - D) aggregate expenditure and aggregate demand.
 - E) the rate of change of wages and output.
- 24) If the natural rate of unemployment is 6 per cent, and the current rate of unemployment is 6 per cent, then the economy is currently _____
- A) producing real GDP that is greater than full-employment output and there is a recessionary gap.
 - B) producing real GDP that is less than full-employment output and the general price level will increase.
 - C) producing real GDP that is less than full-employment output and there is an inflationary gap.
 - D) producing real GDP that is less than full-employment output and there is a recessionary gap.
 - E) at full employment output and there is no output gap.

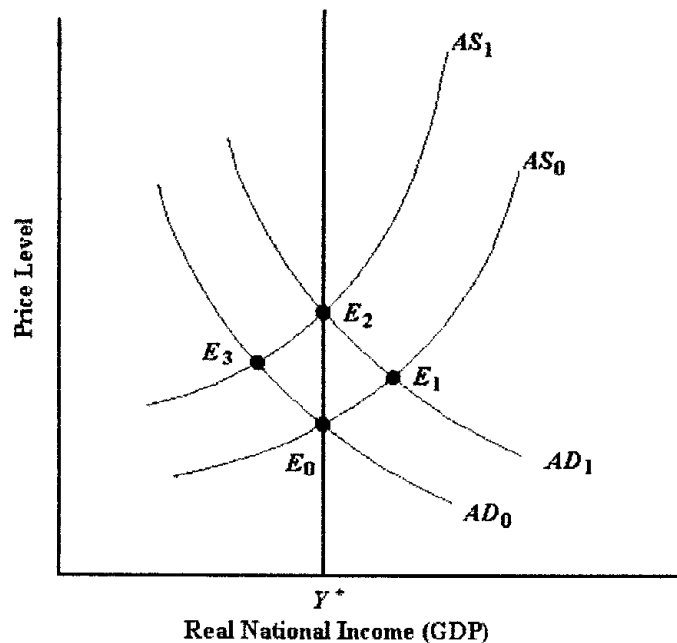


FIGURE 24-3

- 25) In Figure 24-3, the economy cannot be in equilibrium at E_1 , in the long run, because the _____ 25) _____
- A) AD_1 curve will shift back to the original position due to a fall in current consumption.
 - B) AS will shift to the left due to an increase in wages.
 - C) AD_1 curve will shift back to the original position AD_0 due to an increase in the price level.
 - D) AS will shift to the right due to a decrease in the price level.
 - E) AS will shift to the left due to an increase in the price level.
- 26) Given current limitations, fiscal policy as a macroeconomic stabilizer is more defensible the _____ the output gap being suffered, an argument supporting _____. 26) _____
- A) larger; gross tuning
 - B) larger; crowding out
 - C) smaller; fine tuning
 - D) larger; fine tuning
 - E) smaller; crowding out
- 27) The "paradox of thrift" is that in a recession the understandable tendency of worried people to _____ savings causes a _____ recession. 27) _____
- A) decrease, more severe
 - B) decrease; less severe
 - C) increase; shorter
 - D) increase; less severe
 - E) increase; more severe

- 28) Since output in the long run is determined by the position of the Y^* curve, the only role of the AD curve is to determine the price level. This is true because the _____
- A) long run Y^* curve is vertical.
 - B) long run Y^* curve is horizontal.
 - C) aggregate demand curve is horizontal.
 - D) short run aggregate supply curve, AS is upward sloping.
 - E) aggregate demand curve is vertical.

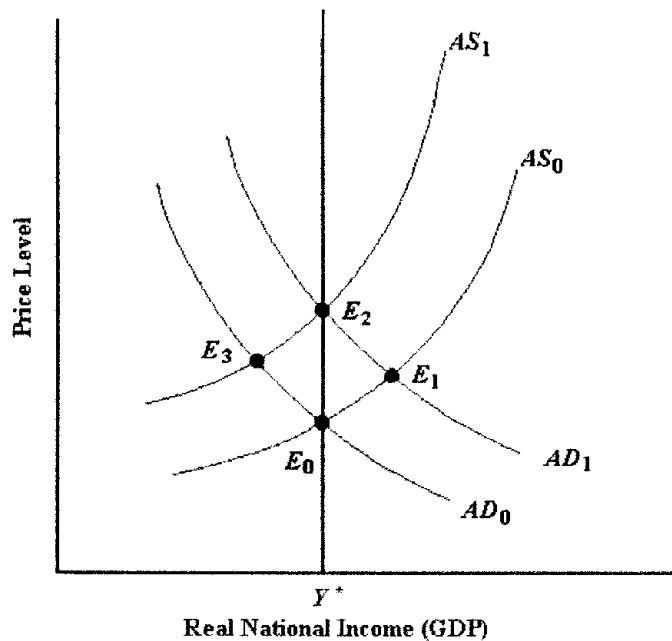


FIGURE 24-3

- 29) In Figure 24-3, if the economy is currently in equilibrium at E_3 , the concept of asymmetrical behaviour of the short run AS curve proves that _____
- A) the price level is constant regardless of the level of equilibrium income.
 - B) a decrease in the price level will induce a rightward shift of AS .
 - C) the economy will attain potential output faster, if there is no intervention by the government.
 - D) the return of the economy to potential output can be slow and long drawn out and sometimes may not be possible without government intervention.
 - E) the economy will never return to potential output.
- 30) Some economists argue that in the long run monetary policy has no effect on _____
- A) nominal interest rates.
 - B) nominal GDP.
 - C) the inflation rate.
 - D) the unemployment rate.
 - E) the price level.

- 31) Increases in long run growth and potential GDP may be caused by a (an) 31) _____
- A) decrease in factor productivity.
 - B) decrease in factor utilization rates.
 - C) increase in interest rates.
 - D) increase in the unemployment rate.
 - E) increase in savings in the short run.
- 32) In the long run, interest rates will fall as the economy goes into a recession because 32) _____
- A) aggregate demand decreases, causing increases in unemployment and national savings.
 - B) increased savings by households leads to a hoarding of cash.
 - C) unions increase the pressure for higher wages to compensate for rising unemployment.
 - D) aggregate demand increases, causing a decrease in unemployment and an increase in national savings.
 - E) reduced factor utilization rates cause lower inflation which lowers interest rates.
- 33) Increases in long run growth and potential GDP may be caused by a (an) 33) _____
- A) decrease in savings in the short run.
 - B) increased availability of key inputs to production such as oil supplies or the size of the labour force.
 - C) decrease in factor productivity.
 - D) increases in the prices of factors of production such as wages or interest rates.
 - E) decrease in factor utilization rates.
- 34) In the short run the source of a change in real GDP and a shift of the aggregate supply could be caused by an increase in 34) _____
- A) the amount of employed labour.
 - B) the productivity of capital.
 - C) the amount of land (natural resources) available to the economy.
 - D) the prices of factors of production.
 - E) all of the above
- 35) A former Governor of the Bank of Canada argued that interest rates must rise in times of inflation in order to bring them down again. This apparent contradiction illustrates that 35) _____
- A) the governor of the Bank of Canada is typically a patronage appointment with little formal training or knowledge of economic theory.
 - B) interest rates move in cycles and therefore tend to rise before they fall.
 - C) higher interest rates promote savings which increases the supply of funds for lending and other things constant, drives the "price" of borrowing down.
 - D) higher interest rates in the short run put downward pressure on inflation which in turn, lowers demand for borrowed funds decreasing interest rates in the long run.
 - E) what goes up must come down.

- 36) An important implication of changes in the prices for factors of production is that they cause 36) _____
- A) short-run changes to birth rates that lead to changes to the long-run growth rate of potential national income.
 - B) short-run changes to factor utilization rates but have little impact on long-run growth in potential national income.
 - C) short-run changes to factor utilization rates and are therefore the primary cause of changes to changes in the long-run growth rate of potential national income.
 - D) long-run changes to the birth rate that lead to unpredictable changes to the productivity of factors.
 - E) long-run changes to factor utilization rates and are therefore the primary cause of changes to changes in the long-run productivity of factors.
- 37) On the basis of theory and empirical evidence, most economists believe that changes in fiscal policy 37) _____ have
- A) major effects on the incentive to save in the short run.
 - B) effects on real GDP and factor utilization in the short run but are not effective in changing potential GDP in the long run.
 - C) powerful effects on real GDP and factor prices both in the short run and in the long run.
 - D) no effect on factor utilization in the short run or on factor prices in the long run.
 - E) effects in changing potential GDP in the long run but have little impact on short run real GDP.
- 38) When an economist is exploring how and economy can move from recession to potential GDP the 38) _____ emphasis is on the
- A) long run, to explore the existence of an inflationary gap.
 - B) long run, to compare actual GDP is greater than potential GDP.
 - C) short run, to explain why actual GDP has to be equal to potential GDP.
 - D) long run, to explain why wage rates have a tendency to rise.
 - E) short run, as to explain why actual GDP is less than potential GDP.
- 39) A factor payment that is the very important in determining production costs and the long run price 39) _____ level in the economy as a whole is the
- A) wages paid to workers.
 - B) rents paid for the use of land.
 - C) indirect taxes paid on value-added.
 - D) profits paid to the entrepreneurs.
 - E) the interest rate.
- 40) An increase in the rate of savings will lead to 40) _____
- A) an immediate increase in national income, but may cause a drop in national income in the long run.
 - B) a reduction in consumption and therefore to both a short-run and a long-run decrease in national income.
 - C) a short-run increase in national income, but to a decrease in economic growth.
 - D) no change in the growth rate in either the short run or the long run.
 - E) a short-run reduction in national income, but to an increase in economic growth.

- 41) Embodied technical change can be illustrated by better methods of 41) _____
- A) property law that make more clear the ownership of technology.
 - B) managerial control, such as just-in-time inventory control.
 - C) strengthening and lightening structures, such as the use of new alloys.
 - D) development of social infrastructure like transportation systems and public health care.
 - E) education that teach a wider portion of the labour force basic numeracy.
- 42) A decrease in government taxes, everything else constant, will cause a (an) 42) _____
- A) equal decrease in private investment.
 - B) increase in national saving.
 - C) equal increase in private consumption.
 - D) decrease in national saving.
 - E) increase in the growth rate.
- 43) New endogenous growth theories 43) _____
- A) assume that the growth rate of technology is exogenous.
 - B) incorporate factors such as central-bank behaviour.
 - C) ignore the role of technology.
 - D) assume that the rate of growth of the economy is equal to the rate of population growth.
 - E) stress the role of knowledge and learning in the economy's rate of growth.
- 44) The traditional Neoclassical growth model assumes that with a given state of technology, 44) _____
- A) increases in the use of a single factor bring increasing returns.
 - B) increases in the use of single factor bring diminishing returns.
 - C) increases in the use of a single factor result in constant returns.
 - D) increases in GDP are possible only if all factors are increased at an equal rate.
 - E) the return from successive units of a single factor increases over time.
- 45) An aggregate production function exhibits increasing returns to investment when a 45) _____
- A) each additional unit of investment is more productive than the previous unit.
 - B) no change in capital produces a one percent increase in output.
 - C) a one percent increase in capital produces no change in output.
 - D) each additional unit of investment increased the number of jobs by more than one percent.
 - E) a one percent decrease in capital produces an increase in the marginal product of capital.

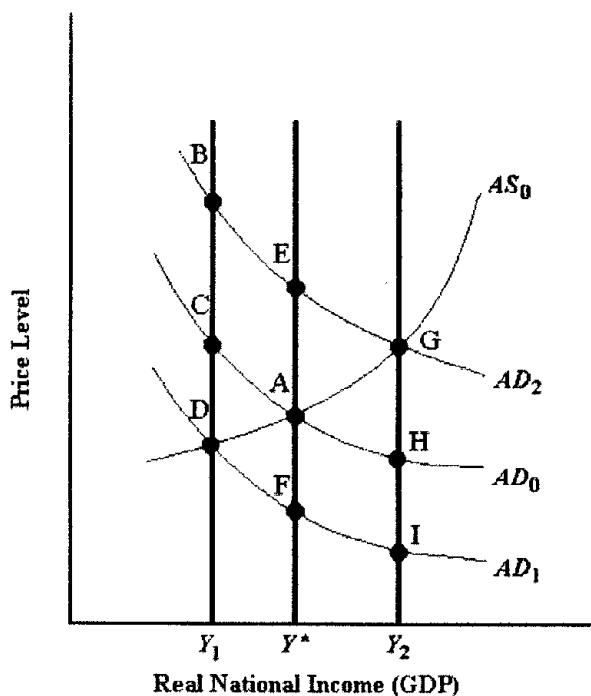


FIGURE 26-1

- 46) Starting from an initial equilibrium at point A in Figure 26-1, a decrease in the savings rate of an economy will lead to a new short-run equilibrium at point _____. 46) _____
- A) D B) E C) F D) G E) H
- 47) Which of the following is consistent with the predictions of Gresham's law? 47) _____
- A) An increase in the money supply will be followed by inflation.
- B) increased circulation of U.S. coin *in Canada* during periods when the Canadian dollar is worth significantly less than the U.S. dollar.
- C) Debasement of a metallic money will be followed by inflation.
- D) The disappearance of U.S. coins circulating *in Canada* during periods when the Canadian dollar is worth less than the U.S. dollar.
- E) Increases in the money supply led to the hyperinflation of the 1920s in Germany.
- 48) Following a new deposit of \$10 000, a chartered bank will find itself having 48) _____
- A) no excess reserves if there is no reserve requirement.
- B) \$1 000 of excess cash reserves if the desired reserve ratio is 10 percent.
- C) \$2 000 of excess cash reserves if the desired reserve ratio is 2 percent.
- D) \$9 000 of excess cash reserves if the desired reserve ratio is 10 percent.
- E) \$98 000 of excess cash reserves if the desired reserve ratio is 2 percent.

- 49) Canadians use Canadian dollars to purchase goods and services because they have confidence that the dollar 49) _____
- A) is fully convertible into gold.
 - B) is accepted by foreigners as more valuable and stable than their own currency.
 - C) is fully convertible into American dollars at a set par value.
 - D) is fully backed by the British pound sterling.
 - E) will be accepted in the future.
- 50) The largest element of the money supply in Canada today is 50) _____
- A) gold.
 - B) the debt of the federal government.
 - C) paper money.
 - D) bank deposits.
 - E) coins.
- 51) Suppose you found a \$100 bill under your grandmother's mattress and the banking system has a cash drain of 5 percent. If the desired reserve ratio in the banking system is 20 percent and all excess reserves were lent out, the new deposit of \$100 would lead to an expansion of the money supply of 51) _____
- A) \$20. B) \$25. C) \$200. D) \$400. E) \$500.
- 52) Suppose a student deposits a \$200 cheque that she received from her parents in a local bank. This transaction alone would 52) _____
- A) decrease the money supply by \$1000 if the desired reserve ratio was 20 percent.
 - B) not change the money supply.
 - C) increase the money supply by \$1000 if the desired reserve ratio was 20 percent.
 - D) increase the money supply by an indeterminate amount.
 - E) decrease the money supply.
- 53) The largest component of the assets of the Bank of Canada is 53) _____
- A) Government of Canada Deposits.
 - B) loans to private individuals.
 - C) Government of Canada securities.
 - D) advances to chartered banks.
 - E) notes and coins in circulation.
- 54) In the event of a sudden loss in confidence in the ability of the chartered banks to redeem deposits, the Bank of Canada would typically 54) _____
- A) impose severe financial penalties on the chartered banks by charging them interest at higher than the bank rate.
 - B) take over the operation of any banks in severe difficulties.
 - C) lend reserves to the chartered banks.
 - D) offer to sell government bonds to the chartered banks.
 - E) suspend operation of the banking system until the panic subsided.

- 55) Gresham's law comes into effect when an economy has two types of money (e.g., gold and silver coins) that are both legal tender but have different nonmonetary values and
- A) the value of the coins is in the same ratio as is their nonmonetary value.
 - B) the lower-valued coin is taken out of circulation.
 - C) people refuse to use the coins of lesser value.
 - D) people use the higher valued coins for exchange and the lower valued for savings..
 - E) the higher-valued coin is taken out of circulation.

55) _____

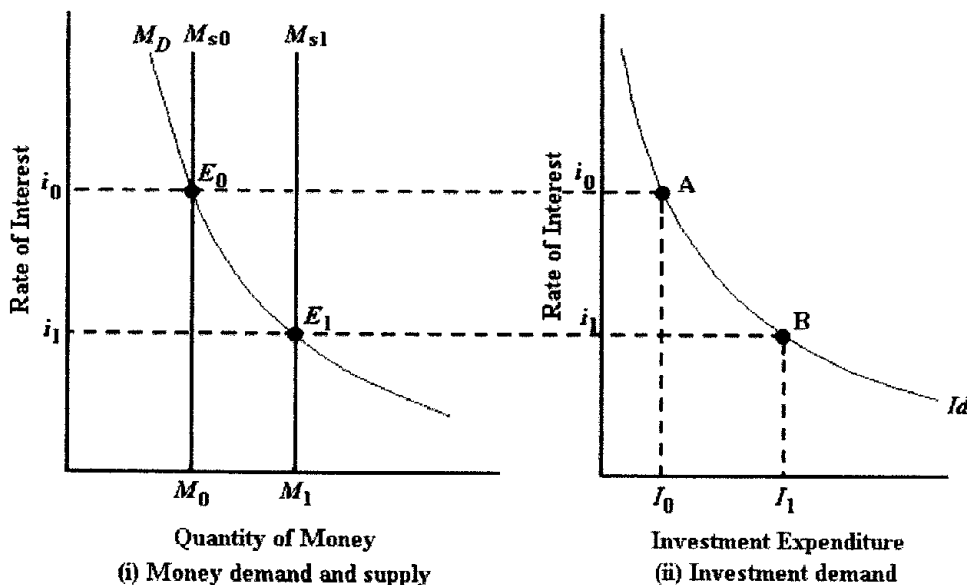


FIGURE 28-3

- 56) Refer to Figure 28-3. The fall in the interest rate from i_0 to i_1 is caused by
- A) an increase in the money supply, leading to the purchase of bonds by economic agents.
 - B) an increase in the demand for money due to a higher price level.
 - C) an increase in the demand for money due to a higher real GDP.
 - D) a decrease in the demand for money occasioned by a lower real GDP.
 - E) a decrease in the money supply, leading to the sale of bonds by economic agents.
- 57) If the Bank of Canada reduces the money supply, other things equal, we can expect the aggregate expenditure curve to shift
- A) upward shift and the aggregate demand to shift left.
 - B) downward and the aggregate demand to shift to the right.
 - C) upward and the aggregate demand to shift to the right.
 - D) downward and the aggregate demand to shift left.
 - E) downward but the aggregate demand will remain unchanged.

56) _____

57) _____

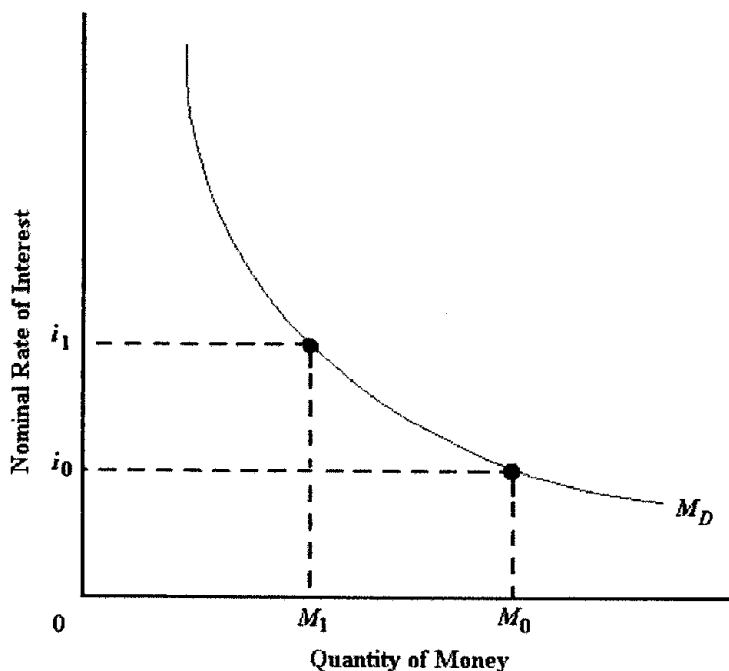


FIGURE 28-1

58) Referring to Figure 28-1, a rightward shift of the LP curve is caused by

- A) an increase in the rate of interest.
- B) a decrease in the price level.
- C) an increase in either the price level or the real GDP.
- D) a decrease in the real GDP.
- E) a decrease in the rate of interest.

58) _____

59) In determining the negative slope of the AD curve, a rise in the price level causes the transactions demand for money to

- A) increase, shifting the M_D curve downward, lowering the interest rate and decreasing desired investment, causing the AE curve to shift downward.
- B) decrease, shifting the M_D curve upward, raising the interest rate and increasing desired investment, causing the AE curve to shift upward.
- C) decrease, shifting the M_D curve downward, lowering the interest rate and increasing desired investment, causing the AE curve to shift upward.
- D) increase, shifting the M_D curve upward, raising the interest rate and decreasing desired investment, causing the AE curve to shift downward.
- E) increase, shifting the M_D curve upward, raising the interest rate and decreasing desired investment, causing the AE curve to shift upward.

59) _____

- 60) The real demand for money is 60) _____
- A) equal to the amount of currency circulating in the economy.
 - B) the nominal demand for money divided by the price level.
 - C) the nominal demand for money multiplied by the price level.
 - D) equal to the supply of money at all times.
 - E) equal to the nominal demand for money as long as inflation is fully anticipated.
- 61) Which of the following represents viewpoints of classical economists? 61) _____
- A) The economy is composed of the real sector and the monetary sector, and the latter does not affect the former.
 - B) The allocation of resources is determined by the money supply.
 - C) Relative prices are determined by the money supply.
 - D) Inflation is unimportant, because it has no effect on the real sector of the economy.
 - E) The distribution of income is determined by the money supply.
- 62) If the Bank Rate decreases during a contraction of real GDP, then the Bank of Canada 62) _____
- A) must have caused the change, because only the Bank of Canada can influence interest rates.
 - B) must have been decreasing the money supply.
 - C) must have left the money supply constant.
 - D) must have been increasing the money supply.
 - E) may not have caused the change, because the demand for money decreases during recessions.
- 63) To increase the level of desired investment, the Bank of Canada could 63) _____
- A) reduce its spending.
 - B) buy securities in the open market.
 - C) reduce the reserves of the commercial banks.
 - D) transfer government accounts from the commercial banks to the Bank of Canada.
 - E) raise the bank rate.
- 64) If the Bank of Canada has engaged in *Inflation Targeting*, it would react to a negative supply shock 64) _____
by
- A) switching Government of Canada accounts out of the commercial banks.
 - B) buying bonds from the open market.
 - C) by changing its target variable from inflation to real GDP.
 - D) raising the bank rate.
 - E) with a contractionary monetary policy.
- 65) If investment spending responds to a decrease in interest rates, this will result in 65) _____
- A) a graph of aggregate expenditures that is a vertical straight line.
 - B) aggregate expenditures rising when the supply of money decreases.
 - C) an increase in aggregate expenditures.
 - D) banks having no excess reserves.
 - E) a decrease in aggregate expenditures.

- 66) If the Bank of Canada chooses the over night lending rate as the policy variable, then the money supply will 66) _____
- A) contract when real GDP is greater than Y^* .
 - B) grow at a steady rate.
 - C) grow at a higher rate than the long run core inflation rate.
 - D) grow more slowly in booms and more rapidly in recessions.
 - E) expand when real GDP is greater than Y^* .
- 67) If the Bank of Canada buys \$100 of government bonds from the nonbank private sector, the desired reserve ratio is 10 percent, and the commercial banks have no excess reserves, this open-market sale will enable the commercial banks to 67) _____
- A) increase reserves by \$90, deposits by \$100, and make no change on loans.
 - B) reduce reserves by \$100, loans by \$900, and deposits by \$1 000.
 - C) reduce reserves by \$100, loans by \$1,000, and deposits by \$1 000.
 - D) increase reserves by \$100, loans by \$900, and deposits by \$1 000.
 - E) reduce reserves by \$90, loans by \$90, and deposits by \$100.
- 68) Assume that an economy is currently in long-run equilibrium at its potential output and that it is subjected to a positive demand shock. When the economy moves back to producing its potential level of national income, the price level will be 68) _____
- A) equal to what it was originally before the demand shock.
 - B) lower than it was in short-run equilibrium and the lower than it was originally.
 - C) lower than it was in the short-run equilibrium but higher than it was originally.
 - D) higher than it was in the short-run equilibrium and higher than it was originally.
 - E) higher than it was in the short-run equilibrium but lower than it was originally.
- 69) The theory of "rational expectations" suggests that a monetary policy designed to stabilize the economy will fail unless 69) _____
- A) the Bank of Canada always validates an inflationary gap.
 - B) any change in the money supply is fully anticipated.
 - C) labor unions agree to no increase in wage contracts.
 - D) the government is operating with a balanced budget.
 - E) any change in the money supply is unexpected.
- 70) A rightward shift of the *AD* curve accompanied by a rightward shift of the *AS* curve should 70) _____
- A) reduce GDP but have an uncertain effect on the price level.
 - B) reduce the price level but have an uncertain effect on GDP.
 - C) reduce both the price level and GDP.
 - D) increase the price level but have an uncertain effect on GDP.
 - E) increase GDP but have an uncertain effect on the price level.

- 71) If the economy is faced with continued supply shocks, such as annual wage increases for union workers, and there is no monetary validation, we can expect 71) _____
- A) an inflationary gap.
 - B) rising unemployment until the wage increases cease, or are offset by other wage decreases.
 - C) a shrinking output gap.
 - D) a one-time rise in the price level.
 - E) peace in labour-management relations.
- 72) According to the acceleration hypothesis, the inflation rate will accelerate when output is held 72) _____
- A) at the NAIRU.
 - B) at the natural rate.at potential level.
 - C) below potential level.
 - D) at the level where unemployment is at the natural rate.
 - E) above potential level.
- 73) Which of the following would be expected to cause a permanent increase in the inflation rate as opposed to a , once and for all, rise in the price level 73) _____
- A) the imposition of a new sales tax.
 - B) a new payroll tax that raises unit wage costs.
 - C) persistent expectations of continued inflation.
 - D) the sudden doubling of a key raw materials price.
 - E) an early frost that damages the agricultural harvest.
- 74) New Classical theories of the labour market assume that labour markets 74) _____
- A) are always clear.
 - B) should be regulated to produce an efficient wage rate.
 - C) will always provide a subsistence wage.
 - D) are inefficient.
 - E) have asymmetrically rigid wages.
- 75) Full employment means that there exists 75) _____
- A) no job vacancies at the time.
 - B) only involuntary unemployment.
 - C) an unemployment rate of less than 5 percent.
 - D) only structural and/or frictional unemployment.
 - E) a measured unemployment rate of zero.
- 76) During a recession, the unemployment rate _____ the NAIRU. 76) _____
- A) falls toward
 - B) is equal to
 - C) rises above
 - D) rises toward but never exceeds
 - E) falls below

- 77) An example of hysteresis in a labour market is 77) _____
- A) when a negative supply shock persists.
 - B) when a negative demand shock persists.
 - C) a group of new entrants to the labour market have difficulty finding jobs, and as a result have a higher rate of unemployment throughout their working lives.
 - D) unemployment which arises due to the effects of a policy, such as a minimum wage.
 - E) a group of new entrants to the labour market has a high rate of unemployment due to technological change.
- 78) According to macroeconomic theory, other things constant, when changes in technology cause some industries to decline and other industries to expand it results in 78) _____
- A) an increase in NAIRU.
 - B) an increase in frictional unemployment.
 - C) a decrease in cyclical unemployment.
 - D) a decrease in NAIRU.
 - E) an increase in structural unemployment.
- 79) According to New Classical theories of unemployment, if the unemployment rate exceeds NAIRU, wages will 79) _____
- A) decrease and the labour force will increase.
 - B) increase and the labour force will decrease.
 - C) remain unchanged but the labour force will decrease until wages are in equilibrium.
 - D) increase and the labour force will increase.
 - E) decrease and the labour force will decrease.
- 80) Suppose the real interest rate equals the rate of growth of real GDP. In this case, the government's debt-to-GDP ratio will rise only if 80) _____
- A) there is a primary budget deficit.
 - B) the debt-to-GDP ratio is already high.
 - C) the primary budget surplus exceeds the overall budget surplus.
 - D) there is an overall budget deficit.
 - E) the real interest rate is high.
- 81) In a closed economy, if the government deficit drives up interest rates 81) _____
- A) government borrowing cannot push up interest rates.
 - B) the money supply will increase.
 - C) credit will become less expensive.
 - D) some private investment expenditure will be crowded out.
 - E) private expenditure would be expected to increase.

- 82) The annual primary budget deficit is equal to the 82) _____
- A) accumulation of government borrowing.
 - B) excess of government expenditure over tax revenues in a given fiscal year.
 - C) total amount of government spending on program expenses, personnel, and capital outlays.
 - D) decrease in the stock of government debt during the course of a year.
 - E) excess of current revenue over current expenditure.
- 83) Since government saving is equal to the government's budget surplus, we can say that 83) _____
- A) national saving is equal to private saving minus the government budget deficit.
 - B) national saving is equal to private saving plus the government budget deficit.
 - C) the government budget deficit is equal to the sum of government saving and private saving.
 - D) national saving is equal to private saving.
 - E) none of the above
- 84) An annually balanced budget, with no surplus or deficit, is difficult to achieve as a policy goal because 84) _____
- A) a significant portion of the government's budget is beyond the short term control of the federal government.
 - B) tax revenues automatically rise during economic booms and fall during recessions.
 - C) transfer payments rise during recessions and fall during economic booms.
 - D) government has little control over interest rate charges on its debt during a fiscal year.
 - E) all of the above are reasons why a balanced budget is difficult to achieve.

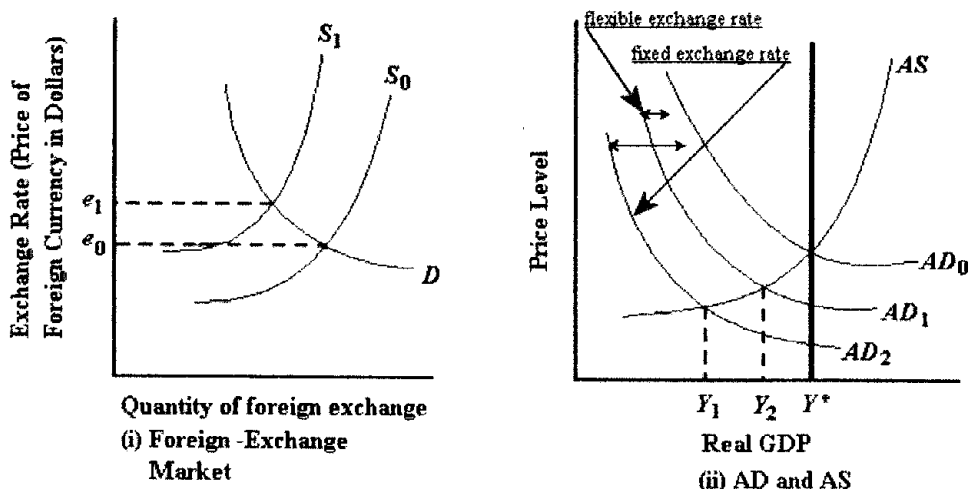


FIGURE 35-4

- 85) Referring to Figure 35-4, an increase in the world's demand for Canadian exports (assuming fixed exchange rates) will shift _____ 85) _____
- A) both the supply curve from (S_1 to S_0) and the aggregate demand curve from AD_2 to AD_1 .
 - B) both the supply curve from (S_0 to S_1) and aggregate demand curve from AD_0 to AD_1 .
 - C) both the supply curve from (S_0 to S_1) and the aggregate demand curve from AD_0 to AD_2 .
 - D) the aggregate demand curve to AD_1 only.
 - E) the aggregate demand curve to AD_2 only.
- 86) High Canadian interest rates lead to _____ 86) _____
- A) appreciation of the European currency.
 - B) depreciation of the Canadian dollar.
 - C) appreciation of the Canadian dollar.
 - D) financial capital outflows.
 - E) a decreased external value of the Canadian dollar.
- 87) If the Canadian dollar appreciates, there will be a _____ in the demand for foreign imports, and the number of dollars offered in the foreign-exchange market will _____. 87) _____
- A) fall; fall
 - B) rise; fall
 - C) fall; rise
 - D) rise; rise
 - E) fall; remain constant
- 88) The aggregate demand curve, 'AD' relates the _____ 88) _____
- A) aggregate expenditure to real national income.
 - B) price level to desired consumption.
 - C) aggregate expenditure to aggregate supply.
 - D) aggregate supply to real national income.
 - E) price level to equilibrium real national income.

- 89) Over the horizontal range of the short run *AS*, a leftward shift of the *AD* curve will result in
- A) an increase in prices and no change in real GDP.
 - B) an increase in both real GDP and prices.
 - C) an increase in real GDP and no change in prices.
 - D) a decrease in both real GDP and prices.
 - E) a decrease in real GDP but no change in prices.

89) _____

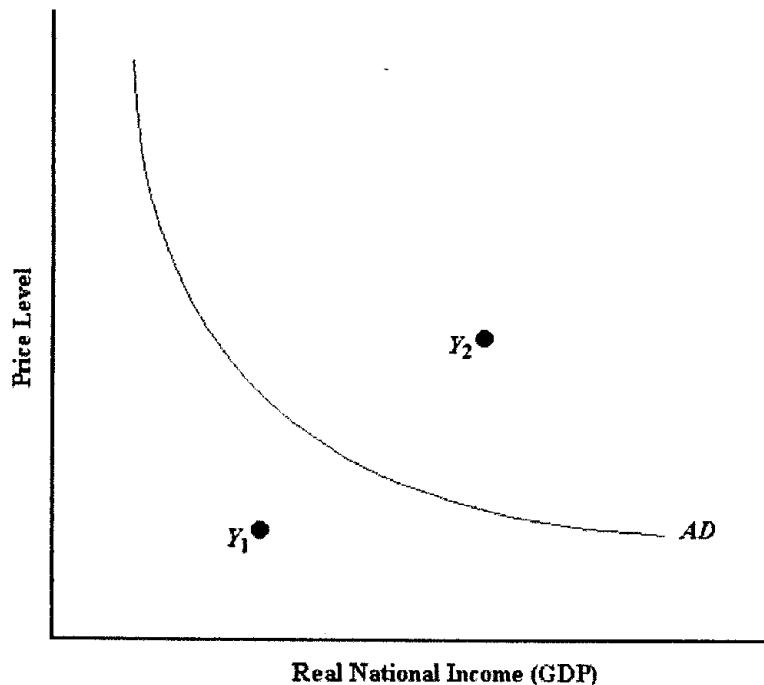


FIGURE 23-1

- 90) In Figure 23-1, at point Y_2 the
- A) corresponding point on the aggregate expenditure curve is on the 45-degree line.
 - B) corresponding point on the aggregate expenditure function is above the 45-degree line.
 - C) output and the price level will tend to fall.
 - D) economy national income is in short-run equilibrium.
 - E) desired aggregate expenditure is greater than national income.
- 91) A rise in the amount of desired consumption, investment, government spending, or net export expenditure associated with each level of national income shifts the *AE* curve
- A) down and shifts the *AD* curve to the right.
 - B) up and shifts the *AD* curve to the right.
 - C) down but no movement of the *AD* curve.
 - D) up and shifts the *AD* curve to the left.
 - E) down and shifts the *AD* curve to left.

90) _____

91) _____

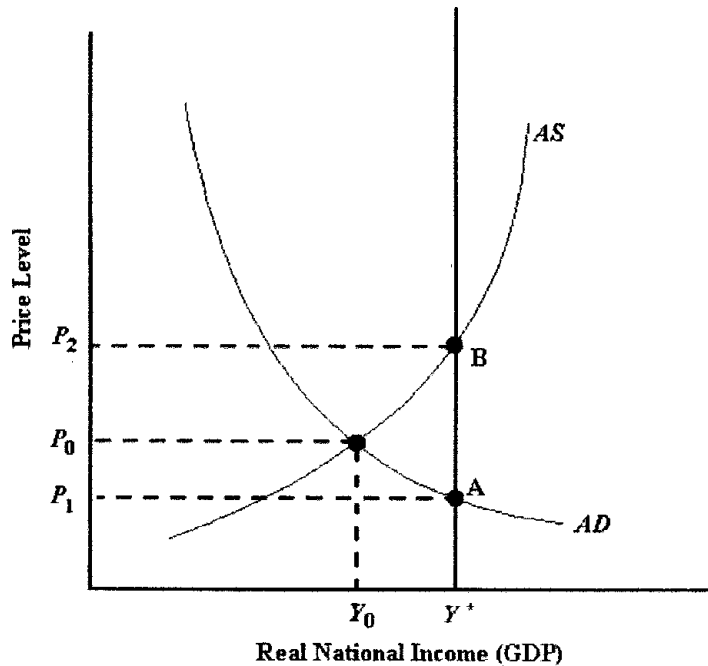


FIGURE 24-1

- 92) If the economy in Figure 24-1 is currently producing Y_0 level of output and wages are sticky downward, then the 92) _____
- A) economy will only move gradually toward point A as wages slowly adjust.
 - B) economy will eventually move to point B.
 - C) AD curve will eventually shift to the right and return the economy to full employment level of output.
 - D) economy will quickly move to point A.
 - E) level of output will decrease below Y_0 .
- 93) An inflationary output gap occurs when 93) _____
- A) potential GDP exceeds actual GDP.
 - B) actual GDP exceeds potential GDP.
 - C) nominal GDP exceeds real GDP.
 - D) demand for labour services is very low.
 - E) equilibrium national income is below potential national income.
- 94) Mechanisms of automatic adjustment during a recessionary gap include 94) _____
- A) declining wages.
 - B) increasing taxes.
 - C) increasing imports.
 - D) declining government spending.
 - E) increasing prices.

- 95) When real GDP is below potential output, the _____
A) AD curve shifts to the left rapidly.
B) AD curve shifts to the right very rapidly.
C) AS curve shifts to the right very rapidly.
D) AS curve shifts to the right only very slowly.
E) AS curve shifts to the left fairly rapidly.
- 96) In the long run, increases in the growth rate and potential GDP are possible only if there is _____
A) no government interference with the market system.
B) an increase in the general price level.
C) a continuous growth in the rate of savings relative to income.
D) an increase in the unemployment rate.
E) a growth in the resource base available to the economy or a continuous growth in factor productivity.
- 97) M2 is defined as currency in circulation plus _____
A) term deposits, money market funds and demand loans.
B) term deposits and money market funds.
C) term deposits, money market funds and personal savings accounts.
D) demand deposits and savings accounts.
E) demand deposits, savings deposits and non-personal notice deposits.
- 98) Near money refers to _____
A) cheques on demand deposits.
B) assets that fulfill the temporary store-of-value function but not the medium-of-exchange function.
C) financial assets whose capital values are too unstable for them to be classified as money.
D) money substitutes such as credit cards.
E) assets that fulfill the medium-of-exchange function but not the store of value function.
- 99) A rise in the price level will _____
A) increase the value of money.
B) decrease the purchasing power of money.
C) stabilize the value of money.
D) has no effect on the value of money
E) increase the purchasing power of money.

- 100) The opportunity cost of holding money is 100) _____
- A) inversely related to the rate of interest and not related to the extra interest that could have been earned had the money been used to buy bonds.
 - B) the extra interest that could have been earned had the money been used to buy bonds.
 - C) positively related to the rate of interest and the extra interest that could have been earned had the money been used to buy bonds.
 - D) inversely related to the rate of interest and the extra interest that could have been earned had the money been used to buy bonds.
 - E) positively related to the rate of interest and not related to the extra interest that could have been earned had the money been used to buy bonds.
- 101) The term "demand for money" usually refers to the 101) _____
- A) aggregate demand for cash and demand deposits in the economy.
 - B) sum of all desired assets, including cash, bond, and real property.
 - C) average person's desire to hold cash.
 - D) sum of all desired holdings of cash.
 - E) cash and deposits actually held by firms.
- 102) An increase in the money supply will lead to the largest increase in aggregate demand if the economy has an 102) _____
- A) inelastic demand for money and an inelastic investment demand function
 - B) inelastic demand for money and an elastic investment demand function
 - C) elastic demand for money and an inelastic investment demand function
 - D) elastic demand for money and an elastic investment demand function
 - E) none of the above
- 103) The Bank of Canada's purchases and sales of government securities represent 103) _____
- A) reserve requirements.
 - B) increases and decreases in government expenditure.
 - C) margin requirements.
 - D) open-market operations.
 - E) the setting of the bank rate.
- 104) The Bank of Canada uses monetary policy to control undesirable fluctuations in real GDP, among other methods, by 104) _____
- A) controlling government spending.
 - B) controlling business investment expenditures directly.
 - C) influencing the money supply which affects the interest rate and hence, the marginal propensity to consume.
 - D) influencing the money supply which affects the interest rate and hence, consumption and investment.
 - E) all of the above

- 105) A 2 percent per year rate of growth of the money supply accompanied by a growth in the demand for money of 3 percent would be considered 105) _____
- A) a contractionary monetary policy.
 - B) a neutral monetary policy.
 - C) targeting the overnight lending rate.
 - D) targeting the exchange rate.
 - E) an expansionary monetary policy.
- 106) According to the "forward-looking" version of the expectations hypothesis 106) _____
- A) individuals make the best possible use of available information to form their expectations of future behaviour of policy-makers.
 - B) discretionary monetary and fiscal policy designed to stabilize the economy are effective only in the short run.
 - C) individuals are unable to anticipate the future actions of economic policy-makers.
 - D) individuals' expectations change very slowly.
 - E) individuals base their expectations of future events only on past experience.
- 107) Assume that there is an inflationary gap and that the Bank of Canada holds the money supply constant. This scenario will lead to 107) _____
- A) an increase in wages and an upward shift of the AS curve.
 - B) the emergence of a recessionary gap.
 - C) a permanent decrease in output.
 - D) a wage-price spiral.
 - E) reduced transactions demand for money, an increase in the price of bonds, and a lower rate of interest.
- 108) One reason that economists are interested in the stocks of unemployed as opposed to the gross flows in the labour force is that examining the stocks 108) _____
- A) by themselves provides a good estimate of the duration of unemployment.
 - B) provides a better indication of the total number of people unemployed at any one time.
 - C) gives a better picture of the amount of activity in the labour market.
 - D) increases the emphasis on the new entrants and retirements of people moving into and out of the labour force.
 - E) gives a better estimate of NAIRU.
- 109) Most economists believe that a budget balanced over the business cycle 109) _____
- A) is a worthy idea but requires accurate forecasting and definition of the business cycle.
 - B) is the same as an annually balanced budget.
 - C) would stabilize the economy and produce an annual budget balance of zero.
 - D) is absolutely necessary for prudent management of the economy.
 - E) would be pro-cyclical.

110) An increase in the income-tax rate _____ the marginal propensity to spend and thus _____ the multiplier. 110) _____

- A) lowers; raises
- B) raises; lowers
- C) no change; raises
- D) lowers; lowers
- E) raises; raises

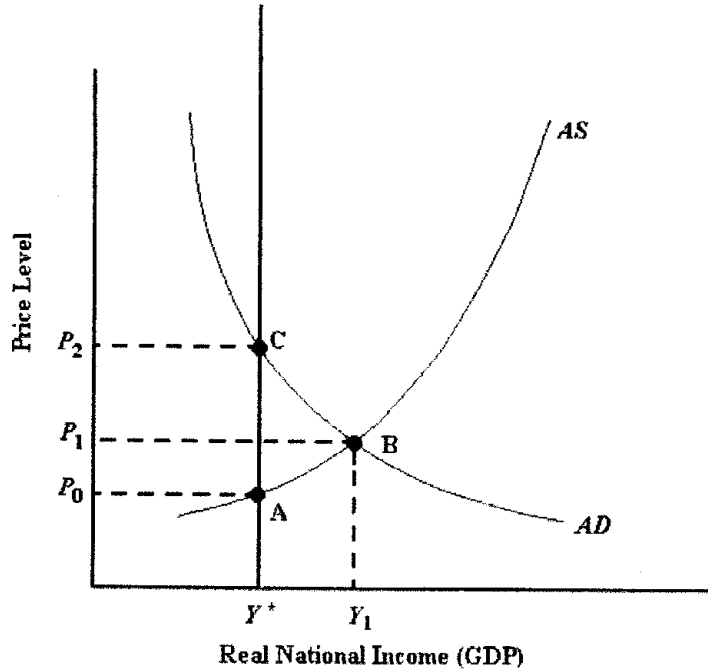


FIGURE 24-2

111) Referring to Figure 24-2, where the economy is in equilibrium at Y_1 , if wages are sticky the government could use fiscal policy to close the gap by 111) _____

- A) a decrease in government spending with taxes constant.
- B) an increase in current interest rates.
- C) a decrease in government spending and an increase in taxes.
- D) a decrease in personal and corporate income taxes.
- E) an increase in personal and corporate income taxes.

112) In the short run, national income is primarily determined by 112) _____

- A) changes in the capital stock.
- B) aggregate supply.
- C) changes in investment.
- D) changes in the factor productivity.
- E) aggregate demand.

- 113) An example of the acquisition of human capital would best be shown by a 113) _____
- A) worker communicates more quickly and accurately with suppliers because of upgrades to communications software.
 - B) worker receives new machinery enabling him/her to do the amount of work that was formerly done by two workers.
 - C) worker takes a training course that increases his/her productivity.
 - D) government-sponsored program increases the amount of investment available per worker.
 - E) chip manufacturer introduces a new faster processor for micro-computing.
- 114) If the economy is currently in monetary equilibrium, an increase in the money supply will 114) _____
- A) lead to a movement down the money demand curve to a lower rate of interest.
 - B) not change the equilibrium conditions.
 - C) cause an increase in the demand for money, leading to a lower rate of interest.
 - D) cause a reduction in the demand for money, leading to a higher rate of interest.
 - E) cause an excess demand for money and a decrease in the rate of interest.
- 115) Compared to rational expectations, backward-looking expectations adjust more _____ and are _____ prone to repetition of an expectational error. 115) _____
- A) quickly; less
 - B) slowly; less
 - C) quickly; more
 - D) slowly; more
- 116) The normal turnover of labour and the usual time it takes to find a satisfactory job opening causes _____ unemployment to persist even at potential GDP. 116) _____
- A) involuntary
 - B) actual unemployment greater than NAIRU
 - C) cyclical
 - D) frictional
 - E) structural
- 117) It is argued that government deficits may provide net benefits to future generations because 117) _____
- A) building an up-to-date infrastructure lowers costs for future generations.
 - B) capital budgeting could be used to minimize undesirable redistributions of income between generations.
 - C) investments into infrastructure with a higher rate of return than the cost of borrowing money makes good business sense.
 - D) spending on health care, education and similar things as a result of the deficit can be considered a socially responsible investment.
 - E) all of the above
- 118) If the Canadian exchange rate on the British pound sterling is \$2.80, then 118) _____
- A) one dollar exchanges for 0.280 pounds.
 - B) one pound exchanges for 0.28 dollars.
 - C) one dollar exchanges for 0.357 pounds.
 - D) one pound exchanges for 2.40 dollars.
 - E) one dollar exchanges for 1.40 pounds.

- 119) A one-time demand shock, that causes the equilibrium output to be higher than the potential output, will
- A) allow a stable expansion of real income over time.
 - B) be negated in the long run, through the self-adjustment mechanism.
 - C) result in a price level lower than that preceding the demand shock.
 - D) set off a endless cycle of price rises and increases in unemployment.
 - E) always reverse itself.

119) _____

- 120) An aggregate production function exhibits constant returns to scale when a one percent increase in labour input
- A) along with a one percent increase in capital produces one percent more output.
 - B) along with a one percent increase in capital produces the same amount of output.
 - C) produces a one percent increase in output.
 - D) along with a one percent decrease in capital produces the same amount of output.
 - E) induces a one percent increase in capital input.

120) _____

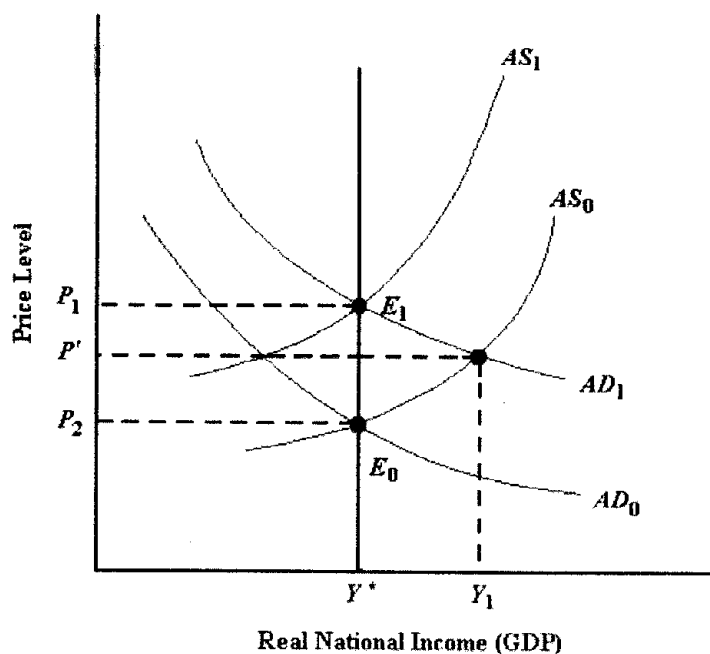


FIGURE 28-4

- 121) Refer to Figure 28-4. The frustration of the adjustment mechanism, which results in the movement of the economy from E_0 to E_2 , is explained by the fact that
- A) net exports have risen unexpectedly.
 - B) the personal consumption has increased due to an increase in wealth.
 - C) money supply increases as fast as the price level.
 - D) money supply is held constant when the price level increases.
 - E) new inventions have led to a spurt of investment activity.

121) _____

122) The bank rate is the

122) _____

- A) primary method used by the Bank of Canada to control the money supply.
- B) same as a margin requirement.
- C) interest rate that commercial banks charge their best customers.
- D) interest rate at which the Bank of Canada will lend funds to commercial banks whose reserves are temporarily below the required level.
- E) interest rate at which the Bank of Canada will lend funds to the Canadian government.

123) Expectational inflation theory explains

123) _____

- A) than an AS curve can shift upward purely as a result of decision makers' expectations.
- B) that expectations of inflation are formed based purely on calculations of trade unions.
- C) the appropriate policy for eliminating expectational inflation is to increase aggregate demand.
- D) that inflation is always and everywhere the result of short run increases in the money supply.
- E) the original cause of inflation.