

Last Name: \_\_\_\_\_

First Name: \_\_\_\_\_

Student ID #: \_\_\_\_\_

Grade	MC	
	P1	
	P2	
	Total	

## Midterm Exam #2

ECON 105-D200: Principles of Macroeconomics  
Prof. Krauth, Spring 2013

Please put away all materials except for pens or pencils and a non-programmable, non-graphing, non-communicating calculator. Communication with classmates *for any purpose* is forbidden. You can lose up to 5 points on this exam for failure to follow instructions, including failure to put your name and student number on your exam and bubble sheets. Raise your hand if you have any questions or needs. You do not need to “show your work”; all I care about is your answer to the question. Good luck!

### Multiple choice (40 questions - 2 points each)

- Suppose that a lobster in Nova Scotia costs \$10 and the same type of lobster in New Brunswick costs \$30. How could people make a profit in the situation?
  - by buying lobsters in Nova Scotia and selling them in New Brunswick, which would increase the price of lobster in New Brunswick
  - by buying lobsters in Nova Scotia and selling them in New Brunswick, which would decrease the price of lobster in New Brunswick
  - by buying lobsters in New Brunswick and selling them in Nova Scotia, which would increase the price of lobster in New Brunswick
  - by buying lobsters in New Brunswick and selling them in Nova Scotia, which would decrease the price of lobster in New Brunswick
- In 2007 Freedonia had a population of 2,700 and real GDP of about \$1,080,000. In 2006 it had a population of 2,500 and real GDP of about \$1,000,000. What was the approximate growth rate of real GDP per person in Freedonia between 2006 and 2007?
  - 0 percent
  - 2.5 percent
  - 5 percent
  - 7.5 percent
- In a market economy, when do we know that a resource has become scarcer?
  - when its price rises relative to other prices
  - when it is nonrenewable and some of it is used
  - when substitutes exist
  - when there are no substitutes

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4. Which of the following would NOT be considered physical capital?
  - a. a new factory building
  - b. a computer used to help Mercury Delivery Service keep track of their orders
  - c. on-the-job training
  - d. a desk used in an accountant's office
  
5. Which of the following is an important fact about population growth?
  - a. There are no substantial differences between rates of growth in population among countries.
  - b. In developed countries, population tends to grow slower than in developing countries.
  - c. Higher rate of growth in population implies higher productivity.
  - d. Economists generally believe that a country that increases its population growth rate will increase its economic growth rate.
  
6. Real GDP per person is \$25,000 in Aquilonia, \$10,000 in Nemedra, \$15,000 in Shem, and \$20,000 in Zexa. Saving per person is \$2,000 in all three countries. Other things equal, what would we expect?
  - a. All four countries will grow at the same rate.
  - b. Aquilonia will grow the fastest.
  - c. Nemedra will grow the fastest.
  - d. Shem will grow the fastest.
  
7. Which of the following is generally an opportunity cost of investment in human capital?
  - a. future job security
  - b. forgone wages during the years of school
  - c. increased earning potential
  - d. the costs of living during the years of school
  
8. Drug companies can usually obtain patents on new drugs. Patents turn new ideas into which of the following goods?
  - a. private goods, which increase the incentive to engage in research
  - b. private goods, which decrease the incentive to engage in research
  - c. public goods, which increase the incentive to engage in research
  - d. public goods, which decrease the incentive to engage in research
  
9. Lucy wants to start her own psychiatric practice, but her expenditures exceed her income. Which of the following best describes Lucy?
  - a. She is a saver who demands money from the financial system.
  - b. She is a saver who supplies money to the financial system.
  - c. She is a borrower who demands money from the financial system.
  - d. She is a borrower who supplies money to the financial system.

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10. Suppose Microsoft sells a bond. What is the company doing?
  - a. borrowing directly from the public
  - b. borrowing indirectly from the public
  - c. lending directly to the public
  - d. lending indirectly to the public
  
11. If Huedepool Beer runs into financial difficulty, how are bondholders and shareholders paid?
  - a. Shareholders are paid before bondholders.
  - b. Shareholders are paid after bondholders.
  - c. Shareholders and bondholders are paid proportional shares of the company's assets.
  - d. Shareholders receive all the company's assets.
  
12. Suppose that the government finds a major defect in one of a company's products and demands that it be taken off the market. Which of the following would we expect?
  - a. The supply of the stock and the price will both rise.
  - b. The supply of the stock and the price will both fall.
  - c. The demand for the stock and the price will both rise.
  - d. The demand for the stock and the price will both fall.
  
13. In a closed economy, how does national saving compare with investment?
  - a. National saving is usually greater than investment.
  - b. National saving is equal to investment.
  - c. National saving is usually less than investment because of the leakage of taxes.
  - d. National saving is usually less than investment.
  
14. Suppose that in a closed economy GDP is equal to 15,000, taxes are equal to 2500, consumption equals 7500, and government expenditures equal 3000. What is public saving?
  - a. -600
  - b. -500
  - c. 500
  - d. 600
  
15. The country of Aquilonia does not trade with any other country. Its GDP is \$30 billion. Its government purchases \$5 billion worth of goods and services each year, collects \$7 billion in taxes, and provides \$3 billion in transfer payments to households. Private saving in Aquilonia is \$5 billion. What is consumption?
  - a. \$18 billion
  - b. \$21 billion
  - c. \$13 billion
  - d. There is not enough information to answer the question.

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16. The Eye of Horus Incense Company has \$10 million in cash, which it has accumulated from retained earnings. It was planning to use the money to build a new factory. Recently, the rate of interest has increased. How does this fact influence the company's decision?
- a. The increase in the rate of interest should not influence the decision to build the factory because the Eye of Horus doesn't have to borrow any money.
  - b. The increase in the rate of interest should not influence the decision to build the factory because its shareholders are expecting a new factory.
  - c. The increase in the rate of interest should make it more likely that the Eye of Horus will build the factory because a higher interest rate will make the factory more valuable.
  - d. The increase in the rate of interest should make it less likely that the Eye of Horus will build the factory because the opportunity cost of the \$10 million is now higher.

17. Suppose the market for loanable funds is in equilibrium. Using the table below, what is the quantity of funds demanded?

GDP	\$100 billion
Consumption	\$65 billion
Taxes minus Transfers	\$15 billion
Government Purchases	\$20 billion

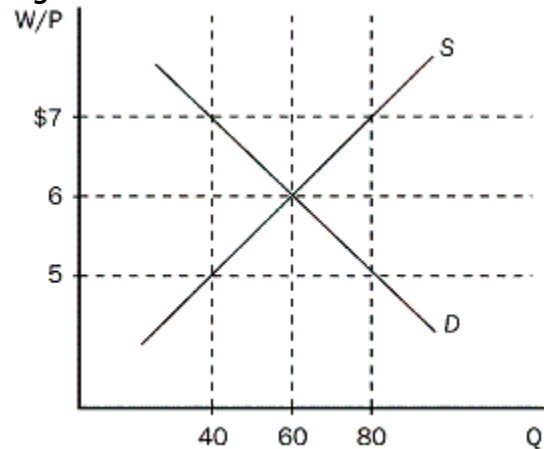
- a. \$25 billion
  - b. \$20 billion
  - c. \$15 billion
  - d. \$10 billion
18. Suppose that the government were to replace the income tax with a consumption tax. What would happen to the interest rate and investment, respectively?
- a. increase and increase
  - b. decrease and decrease
  - c. increase and decrease
  - d. decrease and increase
19. What does the labour-force participation rate measure?
- a. the percentage of the total adult population that is in the labour force
  - b. the percentage of the total adult population that is employed
  - c. the percentage of the labour force that is employed
  - d. the percentage of the labour force that is either employed or unemployed

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20. In 2000 in Japan, based on concepts similar to those used to compute Canadian employment statistics, the unemployment rate was about 4.8 percent, the labour force participation rate was about 62 percent, and the adult population was about 108 million. How many people were employed?
- about 52 million
  - about 64 million
  - about 67 million
  - about 103 million
21. Since World War II, which of the following has happened to the labour-force participation rate?
- It has increased for both men and women.
  - It increased for women and decreased for men.
  - It has decreased for both men and women.
  - It decreased for women and increased for men.
22. Suppose that some people are counted as unemployed when, to maintain unemployment compensation, they search for work only at places where they are unlikely to be hired. If these individuals were counted as out of the labour force instead of as unemployed, how would the labour statistics change?
- The unemployment rate and the labour-force participation rate would be higher.
  - The unemployment rate and the labour-force participation rate would be lower.
  - The unemployment rate would be lower and the labour-force participation rate would be higher.
  - The unemployment rate would be higher and the labour-force participation rate would be lower.
23. Suppose that consumers decide to buy more computers and fewer typewriters. As a result, computer companies expand production while typewriter companies lay off workers. What is this an example of?
- structural unemployment created by efficiency wages
  - cyclical unemployment created by a recession
  - frictional unemployment created by a sectoral shift in demand
  - frictional unemployment created by a sectoral shift in supply

Use the graph below to answer the following questions.

**Figure 1**



24. **Refer to Figure 1.** If the minimum wage is \$5 or \$6, what is the number of people unemployed, respectively?
- 40 and 0
  - 20 and 20
  - 40 and 20
  - 0 and 0
25. **Refer to Figure 1.** If the minimum wage rose from \$6 to \$7, what would happen to unemployment?
- It would rise by 40.
  - It would rise by 20.
  - It would fall by 20.
  - It would fall by 40.
26. When Arnold uses dollars to record his income and expenses, how is he using money?
- as a unit of account
  - as a means of payment
  - as a store of value
  - as a medium of exchange
27. Who owns the Bank of Canada?
- private individuals
  - the Queen
  - the commercial banks
  - the federal government of Canada

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28. If the reserve ratio is 15 percent and currency holdings are zero, by how much will an additional \$1000 of reserves increase the money supply?
- \$1176
  - \$1275
  - \$5667
  - \$6667
29. Which of the following lists contains only actions that increase the money supply?
- raise the bank rate; make open market purchases
  - raise the bank rate; make open market sales
  - lower the bank rate; make open market purchases
  - lower the bank rate; make open market sales
30. Suppose the reserve ratio is 10 percent, and currency holdings are zero. Suppose the Bank of Canada sells \$10 million of bonds to the public. Which of the following best describes the effects of this open market operation?
- Bank reserves increase by \$1 million, and the money supply eventually increases by \$10 million.
  - Bank reserves increase by \$10 million, and the money supply eventually increases by \$100 million.
  - Bank reserves decrease by \$1 million, and the money supply eventually increases by \$10 million.
  - Bank reserves decrease by \$10 million, and the money supply eventually decreases by \$100 million.
31. How can the Bank of Canada directly protect a bank during a bank run?
- by increasing reserve requirements
  - by selling government bonds to the bank
  - by lending reserves to the bank
  - by penalizing the bank in trouble
32. When does the supply of money increase?
- when the value of money increases
  - when the price level decreases
  - when the Bank of Canada makes open-market purchases
  - when the Bank of Canada increases the bank rate
33. What does the principle of monetary neutrality imply?
- An increase in the money supply will increase real GDP and the price level.
  - An increase in the money supply will increase real GDP, but not the price level.
  - An increase in the money supply will increase the price level, but not real GDP.
  - An increase in the money supply will increase neither the price level nor real GDP.

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34. According to the quantity equation, if  $P = 15$ ,  $Y = 10$ , and  $M = 20$ , what is  $V$ ?
- 30
  - 15
  - 7.5
  - 7
35. Suppose that the Government of Canada unexpectedly decided to pay off its debt by printing new money. Which of the following would happen?
- People who held money would feel richer.
  - Prices would fall.
  - People who lent money at a fixed interest rate would feel richer.
  - People who borrowed money at a fixed interest rate would feel richer.
36. Since 1992, which of the following has the Bank of Canada done?
- It has announced that it was targeting the money supply growth of 2 percent.
  - It has announced a target rate of inflation of 2 percent.
  - It has announced an inflation target close to 4 percent.
  - It has announced its objective of maintaining a stable rate of economic growth of 2 percent.
37. Which of the following does net capital outflow measure?
- an imbalance between a country's income and expenditure
  - an imbalance between a country's investment and saving
  - an imbalance between a country's sale of goods and services abroad and buying of foreign goods and services
  - an imbalance between a country's sale of domestic assets abroad and domestic purchase of foreign assets
38. Suppose Canada sells chocolate to the United States. Which of the following correctly identifies the effects of this transaction?
- U.S. net exports increase, and U.S. net capital outflow increases.
  - U.S. net exports increase, and U.S. net capital outflow decreases.
  - U.S. net exports decrease, and U.S. net capital outflow increases.
  - U.S. net exports decrease, and U.S. net capital outflow decreases.
39. A Canadian firm buys sardines from Morocco and pays for them with Canadian dollars. Which of the following correctly identifies the effects of this transaction?
- Canadian net exports increase, and Canadian net capital outflow increases.
  - Canadian net exports increase, and Canadian net capital outflow decreases.
  - Canadian net exports decrease, and Canadian net capital outflow increases.
  - Canadian net exports decrease, and Canadian net capital outflow decreases.



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- e. Under policy (b) what will be the money growth rate in Canada?
  
  - f. Under policy (b) what will be the growth rate in Canada's nominal exchange rate, (i.e., the value of the Canadian dollar in US dollars)?
  
  - g. In the real world, inflation is never entirely stable, and purchasing power parity does not exactly hold. Suppose that the U.S. inflation rate is actually highly variable and unpredictable. Describe one advantage of policy (a) over policy (b) given this situation.
  
  - h. Describe one advantage of policy (b) over policy (a) given the situation described in part (g) of this question.
2. **(5 points)** *Of the factors affecting long-run economic growth discussed in this course, identify the one you think is the most important in explaining persistent income differences between rich and poor countries? Explain (in no more than three sentences) why you think it is the most important.*

## Midterm Exam #2 Answer Key (blue)

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### Multiple choice

1. B
2. A
3. A
4. C
5. B
6. C
7. B
8. A
9. C
10. A
11. B
12. D
13. B
14. B
15. B
16. D
17. C
18. D
19. A
20. B
21. B
22. B
23. C
24. D
25. A
26. A
27. D
28. D
29. C
30. D
31. C
32. C

- 33. C
- 34. C
- 35. D
- 36. B
- 37. D
- 38. D
- 39. D
- 40. D

## Short answer

1. **(15 points).**
  - a. 5%
  - b. 9%
  - c. 0%
  - d. 2%
  - e. 6%
  - f. 3%
  - g. In policy (a), instability in U.S. inflation will not cause instability in the nominal exchange rate and in policy (b) it will. So Canadian households and businesses engaged in international trade will experience less uncertainty over relative prices.
  - h. In policy (b), instability in US inflation will not cause instability in domestic prices, and in policy (a) it will. So Canadian individuals and households engaged in domestic trade will experience less uncertainty over relative prices.
2. **(5 points)** There are many correct answers to this question. My main concern was making sure you actually referred to a factor we discussed in this course, and making sure you provided a reasonably sensible explanation.