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# CARLETON UNIVERSITY

**FINAL  
EXAMINATION**  
April 2013

**DURATION: 2.5 HOURS**

No. of Students: 1350

**Department Name & Course Number:** ECON 1000/ECON 1002 A, B, C, D, V  
**Course Instructor(s):** N. Rowe, C. Kyeremeh, G. Kowalski, T. Joseph, M. Francis

<b>AUTHORIZED MEMORANDA</b>	None
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Students **MUST** count the number of pages in this examination question paper before beginning to write, and report any discrepancy to a proctor. This question paper has Seven (7) pages.

This examination paper **MAY** be taken from the examination room.

In addition to this question paper, students require: two (2) examination booklets      yes  no   
a Scantron sheet      yes  no

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## PLEASE READ ALL INSTRUCTIONS CAREFULLY

**Note:** This examination has three (3) sections.

**PART A: MULTIPLE CHOICE (20 questions, 2 marks each). Answer ALL questions. Detach answer sheet from examination paper and hand in answer sheet with exam booklets. USE BLOCK CAPITAL LETTERS. (Total 40 Marks).**

**PART B: SHORTER QUESTIONS: Answer any FIVE (5) of the questions. Each question is worth 8 marks. Answer in main exam booklet. (Total 40 Marks)**

**PART C: LONGER QUESTIONS: Answer any ONE (1) of the questions. Each question is worth 20 marks. Answer in extra exam booklet (Total 20 Marks)**

**Please note:** Answer parts B & C in separate exam booklets!

**Part A: Multiple Choice. USE ANSWER SHEET PROVIDED**

*Identify the choice that best completes the statement or answers the question.*

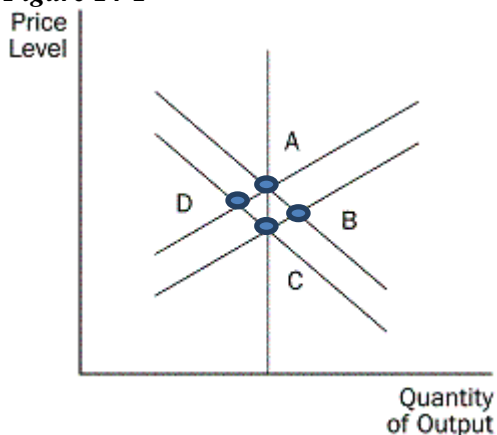
1. Which of the following best defines a transfer payment?
  - a. government spending on imported goods
  - b. money that Canadian citizens working abroad send back to their families in Canada
  - c. payments to governments, other than taxes
  - d. a form of government spending that is not made in exchange for a currently produced good or service
2. Suppose that Nova Scotia produces cheese and fish. In 2010, 20 units of cheese are sold at \$5 each and 8 units of fish are sold at \$50 each. In 2006, the base year, the price of cheese was \$10 per unit, and the price of fish was \$75 per unit. What can we conclude?
  - a. Nominal GDP is \$500, real GDP is \$800, and the GDP deflator is 62.5
  - b. Nominal GDP is \$500, real GDP is \$800, and the GDP deflator is 160
  - c. Nominal GDP is \$800, real GDP is \$500, and the GDP deflator is 160
  - d. Nominal GDP is \$800, real GDP is \$500, and the GDP deflator is 62.5
3. What does the “substitution bias” in the consumer price index refer to?
  - a. substitution of new goods for old goods in the purchases of consumers
  - b. substitution of quality for quantity in consumer purchases over time
  - c. the fact that consumers substitute toward goods that have become relatively less expensive
  - d. substitution of new prices for old prices in the basket of goods from one year to the next
4. The price of imported athletic shoes produced by a Canadian company operating in Thailand increases. By itself, what effect will this change have on the Canadian GDP deflator and CPI?
  - a. The GDP deflator and the CPI will both increase.
  - b. The GDP deflator will increase, and the CPI will be unaffected.
  - c. The GDP deflator and the CPI will both be unaffected.
  - d. The GDP deflator will be unaffected, and the CPI will increase.
5. In terms of riskiness, how do long-term bonds and short-term bonds compare?
  - a. Short-term bonds are more risky and so pay higher interest.
  - b. Short-term bonds are less risky and so pay lower interest.
  - c. Short-term bonds are less risky and so pay higher interest.
  - d. Short-term bonds have about the same degree of risk and so pay about the same interest.
6. Henry buys a bond issued by Ralston Purina, which uses the funds to buy new machinery for one of its factories. Who is investing and who is saving?
  - a. Henry and Ralston Purina are both investing.
  - b. Henry and Ralston Purina are both saving.
  - c. Henry is investing; Ralston Purina is saving.
  - d. Henry is saving; Ralston Purina is investing.
7. How is Latoya, a homemaker who works as a volunteer at the local Red Cross and is currently not looking for a job, counted?
  - a. as employed and in the labour force
  - b. as unemployed and in the labour force
  - c. as unemployed and not in the labour force
  - d. as not in the labour force

8. Which of the following is included in the M2 definition of the money supply?
  - a. credit cards
  - b. term deposits
  - c. corporate bonds
  - d. foreign currency accounts
  
9. Which of the following is not a tool of monetary policy?
  - a. open market operations
  - b. reserve requirements
  - c. changing the overnight rate of interest
  - d. increasing the deficit
  
10. According to the quantity equation, if  $P = 15$ ,  $Y = 10$ , and  $M = 20$ , what is  $V$ ?
  - a. 30
  - b. 15
  - c. 7.5
  - d. 7
  
11. The country of Freedonia has a GDP of \$4000, consumption of \$1800, and government purchases of \$500. Which of the following does this situation imply?
  - a. Investment is equal to  $-\$1700$ .
  - b. Investment plus net capital outflow is equal to \$1700.
  - c. Investment plus net exports is equal to \$2300.
  - d. Saving is equal to \$2200.
  
12. According to purchasing-power parity theory, if a McDonald's Big Mac cost U.S.\$2.50 in the United States and 5 euros in France, what should the nominal exchange rate be?
  - a. 2 euros per U.S. dollar
  - b. 1 euro per U.S. dollar
  - c. 1/2 euro per U.S. dollar
  - d. 1/4 euro per U.S. dollar
  
13. If a country went from a government budget deficit to a surplus, which of the following best predicts the consequences?
  - a. National savings would increase, shifting the supply of loanable funds right.
  - b. National savings would increase, shifting the supply of loanable funds left.
  - c. National savings would decrease, shifting the demand for loanable funds right.
  - d. National savings would decrease, shifting the demand for loanable funds left.
  
14. When Mexico suffered from capital flight in 1994, what happened to Mexico's real interest rate and the peso?
  - a. The real interest rate fell and the peso appreciated.
  - b. The real interest rate fell and the peso depreciated.
  - c. The real interest rate rose and the peso appreciated.
  - d. The real interest rate rose and the peso depreciated.
  
15. What happens when the Canadian dollar appreciates?
  - a. Net exports increase, and aggregate demand shifts right.
  - b. Net exports increase, and aggregate demand shifts left.
  - c. Net exports decrease, and aggregate demand shifts right.
  - d. Net exports decrease, and aggregate demand shifts left.

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Consider the exhibit below for the following questions.

**Figure 14-1**



16. **Refer to Figure 14-1.** If the economy starts at A and there is a fall in aggregate demand, what happens to the economy in the long run?
  - a. It moves back to A.
  - b. It moves to B.
  - c. It moves to C.
  - d. It moves to D.
  
17. According to liquidity preference theory, what is the opportunity cost of holding money?
  - a. the interest rate on bonds
  - b. the inflation rate
  - c. the cost of converting bonds to a medium of exchange
  - d. the difference between the inflation rate and the interest rate on bonds
  
18. How do tax cuts and government expenditure affect aggregate demand?
  - a. Both shift aggregate demand right.
  - b. Both shift aggregate demand left.
  - c. Tax cuts shift aggregate demand right; government expenditure shifts aggregate demand left.
  - d. Tax cuts shift aggregate demand left; government expenditure shifts aggregate demand right.
  
19. In the long run, which of the following will happen if the Bank of Canada increases the rate at which it increases the money supply?
  - a. Inflation will be higher.
  - b. Unemployment will be lower.
  - c. Real GDP will be higher.
  - d. Unemployment will be higher.
  
20. In the short run, an unexpected increase in the money supply will cause:
  - a. Price level to rise and unemployment to rise
  - b. Price level to rise and unemployment to fall
  - c. Price level to fall and unemployment to rise
  - d. Price level to fall and unemployment to fall

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## **Part B.**

Short Answer. Answer ANY FIVE questions. 8 marks each. Use the main booklet.

1. a) According to the Loanable Funds theory, what might cause an increase in the rate of interest?  
b) According to the Liquidity Preference theory, what might cause an increase in the rate of interest?  
c) Which theory works best in the short run, and which theory works best in the long run? Explain.
2. Some countries seem to have permanently higher rates of unemployment than other countries. Briefly explain two theories that might explain why.
3. a) Explain the theory of Purchasing Power Parity.  
b) According to Purchasing Power Parity, what would happen to the Canadian exchange rate and/or price level if the US price level increased by 10%?  
c) Explain the circumstances under which Purchasing Power Parity would be likely to be true or likely to be false.
4. Explain how an increase in the savings rate would affect a country's present standard of living, and future standard of living. Would an increase in the savings rate permanently or only temporarily affect the growth rate? Explain.
5. Suppose the Canadian government persuades Canadians to "Buy Canadian". Explain how this policy would affect the real exchange rate, exports, and imports.
6. Suppose the Bank of Canada wanted to increase the money supply. Explain how it would do this, and explain the role of commercial banks in this process.
7. a) Explain the Quantity Theory of Money.  
b) According to the Quantity Theory, explain what would happen if the Bank of Canada increased the growth rate of the money supply.  
c) Is the Quantity Theory more likely to be true in the short run or in the long run? Explain.
8. Give three different examples where a country's GDP would increase but the standard of living would decrease.
9. Use the Phillips Curve to explain what would happen, in the short run, and in the long run, if the Bank of Canada increased the target rate of inflation from 2% to 10%.

### Part C.

Long Answer: Answer ANY ONE question. 20 marks. Use the additional booklet.

1. Use the AD/AS model, for a **closed** economy, to explain the effects of an increase in Government expenditure. Use a diagram or diagrams as part of your answer. Explain how and why it will affect AD, AS, Consumption, Investment, the rate of interest, and the price level. Explain both the short run effects and the long run effects.
2. Use the AD/AS model, for a small **open** economy, to explain the effects of an increase in the money supply. Use a diagram or diagrams as part of your answer. Explain how and why it will affect net exports, real income, the real exchange rate, and the price level. Explain both the short run effects and the long run effects.
3. Suppose there is an increase in saving in the rest of the world. Explain how this will affect Canada. In particular, explain how this will affect the Canadian rate of interest, Canadian saving and investment, net capital outflow, net exports, and the real exchange rate. Use a diagram or diagrams as part of your answer.

