

ECO 2142 – MACROECONOMICS THEORY I  
Midterm exam #1, October 22, 2014

LAST NAME \_\_\_\_\_ FIRST NAME \_\_\_\_\_

STUDENT ID \_\_\_\_\_

*Instructions:*

1. The exam lasts 1 hour and 15mins.
2. The exam is worth 100 points in total: 2.5 points for each question.
3. Write your answers in the blanks below. You won't get credit for circled answers.
4. There is no need to explain your answers.
5. Good luck!

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

Suppose production and prices of pizzas and calzones in 1997 and 2013 are as follows:

Year	Quantity of pizzas	Price of pizzas	Quantity of calzones	Price of calzones
2003	25	\$5	25	\$5
2013	100	\$10	50	\$10

1. What are the values of nominal GDP for 2003 and 2013, respectively?
  - A) A **\$250; \$1,500.**
  - B) \$250; \$750.
  - C) \$500; \$750.
  - D) \$500; \$1,500.
  - E) None of the answers is correct.
  
2. Assume that 2003 is the base year. What are the values of real GDP for 2003 and 2013, respectively?
  - A) \$500; \$750.
  - B) \$250; \$1,500.
  - C) **\$250; \$750.**
  - D) \$500; \$1,500.
  - E) None of the answers is correct.
  
3. The profits from a French owned company in Canada are included in Canadian \_\_\_\_\_ and French \_\_\_\_\_.
  - A) **GDP; GNP.**
  - B) GDP; GDP.
  - C) GNP; GDP.
  - D) GNP; GNP.
  - E) All of the above answers
  
4. Policy makers can become concerned if the unemployment rate is too low because:
  - A) output will increase.
  - B) output will decrease.
  - C) an exchange rate crisis might occur.

- D) inflation might increase  
E) They may win the elections
5. Which of the following conditions must be satisfied in a closed economy?  
A) There is NO government  
B) Private saving equals investment.  
C) There is no government spending or taxes.  
D) Exports equal imports.  
E) Total saving equals investment.
6. Equilibrium in the goods market requires that:  
A) Equilibrium in the market of all the goods  
B) production equals income.  
C) production equals demand.  
D) consumption equals saving.  
E) government spending equals taxes minus transfers.
7. An increase in the marginal propensity to consume from .5 to .7 will cause:  
A) the ZZ line to become steeper and a given change in government spending (G) to have a smaller effect on output.  
B) the ZZ line to become flatter and a given change in government spending (G) to have a smaller effect on output.  
C) the ZZ line to become steeper and a given change in government spending (G) to have a larger effect on output.  
D) the ZZ line to become flatter and a given change in government spending (G) to have a larger effect on output.  
E) None of the above.
8. A rise in investment confidence is shown by  
A) An upward shift in the ZZ curve.  
B) A downward shift in the 45-degree line.  
C) A steeper ZZ curve without any shifts.  
D) A flatter ZZ curve without any shifts.  
E) A flatter ZZ curve and also an upward shift.
9. The higher the MPS, the \_\_\_\_ is the ZZ curve, and the \_\_\_\_ is the fluctuation in the short run GDP.  
A) Flatter; smaller  
B) Flatter; larger  
C) Steeper; smaller  
D) Steeper; larger  
E) The fluctuation in short run GDP is not related to the size of the MPS.
10. Let the goods market multiplier to be equal to 10. Suppose some private firms have gone into bankruptcy because of the stock market crash. If the losses in investment expenditures due to these bankruptcies are equal to \$25,000,000, then the change in GDP would be equal to:  
A) 0  
B) \$250,000,000.  
C) \$500,000,000.  
D) -\$250,000,000.  
E) -\$500,000,000.
11. In the  $Y=Z$  model, if  $Y < Z$ , then unplanned inventory would \_\_\_\_ and the price level would \_\_\_\_.  
A) Increase; increase.  
B) Increase; decrease.  
C) Increase; stay constant.  
D) Decrease; increase.  
E) Decrease; stay constant.
12. Based on the information presented below, the equation representing the consumption for the economy is \_\_\_\_ and the equilibrium level of GDP is \_\_\_\_\_. There is no government and this is a closed economy.

GDP (Y)	Consumption (C)	Saving (S)	Investment (I)
\$0	\$60	\$-60	\$100
100	120	-20	100
200	180	20	100

300	240	60	100
400	300	100	100
500	360	140	100

- A)  $C = 40 + 0.75Y$ ; \$450.
- B)  $C = -60 + 0.8Y$ ; 500.
- C)  $C = 60 + 0.6Y$ ; \$400.
- D)  $C = 60 + 0.4Y$ ; \$400.
- E) None of the answers is correct.

13. Consider this quote from Person A: " I am working full-time right now, and I have the money to buy a \$13,000 car. However, I feel uncomfortable because we do not know if we would have a general election soon, and what kind of economic policies the new party would introduce. I am going to wait and see how things turn out before I buy my bike." This statement captures
- A. Person A's Marginal Propensity to Consume or spending habit.
  - B. Person A's Marginal Propensity to Save or saving habit.
  - C. Used cars' demand function
  - D. Person A's consumer confidence.
  - E. None of the above.
14. The government wants to spend more money on building low-income housing. If it wants the spending to have maximum effect on economic growth, which of the following saving equations would it prefer to see?
- A)  $S = -30 + 0.4(Y-T)$ .
  - B)  $S = -80 + 0.8(Y-T)$ .
  - C)  $S = -90 + 0.7(Y-T)$ .
  - D)  $S = -140 + 0.6(Y-T)$ .
  - E)  $S = -60 + 0.5(Y-T)$ .

A simplified economy is specified as below.

I. Goods market, all values of C, I, G are in billions of C\$:

Consumption expenditure:	$C = 200 + 0.8(Y-T)$	Lump-sum constant taxes:	$T = 300$
Investment expenditure:	$I = 1054$		
Government expenditure:	$G = 300$		

15. What is the equilibrium Y?
- A) 5,850.
  - B) 6,620.
  - C) 6,570.
  - D) 7,000.
  - E) 8,310.
16. What is the equilibrium consumption expenditure?
- A) 5,216.
  - B) 5,774.
  - C) 6,213.
  - D) 6,450.
  - E) 7,250.
17. What is the value of the goods market multiplier?
- A) 2.5.
  - B) 4.
  - C) 5.
  - D) 6.67.
  - E) 8.
18. Greece has recently introduced austerity plans into its economy in an effort to reign in its government debts by cutting government expenditure on education, health care and the hiring of public servants. Which of the following observation(s) will lessen the negative impact of these spending cuts on the Greece's GDP?
- A) Their tax rate is very low.

- B) Their marginal propensity to save is very low.  
 C) Their crowding-in or crowding-out effect is very weak.  
 D) Their marginal propensity to consume is very low.  
 E) All of the answers are correct.
19. The banking system finds that its desired reserve ratio is 8% (or 0.08), and it is \$100 million short of reserves. If it is unable to obtain any additional reserves, it must decrease its money supply by  
 A) \$1,250 million.  
 B) \$100 million.  
 C) \$1,000 million.  
 D) \$1,600 million.  
 E) None of the answers is correct.
20. If the public decides to hold more cash as a percentage of their deposit balances, the money market multiplier will be \_\_\_\_\_, and for a given monetary base, the money supply is \_\_\_\_\_.  
 A) Larger; larger  
 B) Larger; smaller  
 C) Smaller; larger  
 D) Smaller; constant  
 E) Smaller; smaller
21. An excess demand for money will cause bond prices to \_\_, interest rates to\_\_ and investment expenditure to \_\_\_\_.  
 A) Rise; fall; rise  
 B) Fall; fall; fall  
 C) Fall; fall; rise  
 D) Fall; rise; fall  
 E) Rise; fall; fall
22. Which of the following is a characteristic of "bonds"?  
 A) can be used for transactions  
 B) pay zero interest  
 C) are sold for a price that varies inversely with the interest rate  
 D) are more liquid than cash  
 E) can only be issued by the government
23. Which of the following could NOT be a component of money?  
 A) saving account deposits  
 B) paper currency held by the nonbank public  
 C) chequable deposits  
 D) a deposit where a debit card can be used to withdraw funds  
 E) paper currency and coins held by the public
24. The money demand curve will shift to the left when which of the following events occurs?  
 A) a reduction in the interest rate  
 B) an open market purchase of bonds by the central bank  
 C) an increase in the interest rate  
 D) an open market sale of bonds by the central bank  
 E) a decrease in income
25. A central bank can control which component(s) of the money market?  
 A) Desired reserve ratio.  
 B) Currency or cash drain ratio.  
 C) Only A and B.  
 D) A, B and C can be controlled.  
 E) Monetary base.
26. Which of the following are a component of the money supply?  
 A) chequable deposits  
 B) stocks  
 C) bonds  
 D) saving deposits  
 E) mortgages

27. Suppose a bond offers to pay \$1000 in one year and currently has a 25% interest rate. Given this information, we know that the bond's price must be:
- A) \$140.00.
  - B) \$250.
  - C) \$583.33.
  - D) \$750.00.
  - E) \$800.00.
28. In an economy in which individuals hold both currency and chequable deposits, if the reserve ratio is 10% and people hold 40% of their money in the form of currency, the money multiplier is equal to:
- A) 1.66.
  - B) 2.17.
  - C) 10.
  - D) 2.5.
  - E) 0.46.
29. An increase in the minimum wage will cause:
- A) an increase in the natural rate of unemployment.
  - B) an increase in the equilibrium real wage.
  - C) a reduction in the equilibrium real wage.
  - D) a decrease in the natural rate of unemployment.
  - E) no change in the natural rate of unemployment.
30. As the unemployment rate rises:
- A) the proportion of the unemployed finding a job increases.
  - B) the separation rate decreases.
  - C) the young and unskilled experience larger-than-average increases in unemployment.
  - D) the young and skilled experience larger-than-average increases in unemployment.
  - E) the young and unskilled experience lower-than-average increases in unemployment.
31. An individual is considered unemployed if he or she:
- A) works full-time in a family business, but is not paid.
  - B) works only part-time.
  - C) is not working and is not looking for work.
  - D) is retired and is not looking for work.
  - E) is not working and is looking for work.
32. Efficiency wage theory suggests that:
- A) unskilled workers will have a lower turnover rate than skilled workers.
  - B) workers will be paid more than their reservation wage.
  - C) firms will be more resistant to wage increases as the labour market tightens.
  - D) the government can only set tax rates so high before people will prefer not to work.
  - E) productivity might drop if the wage rate is too high.
33. In the wage-setting relation, the nominal wage falls when:
- A) the price level falls.
  - B) the minimum wage increases.
  - C) the unemployment rate falls.
  - D) unemployment benefits increase.
  - E) the price level rises.
34. Based on price setting behaviour, we know that an increase in the unemployment rate will cause:
- A) a reduction in the real wage.
  - B) no change in the real wage.
  - C) an increase in the real wage.
  - D) an upward shift of the PS curve.
  - E) a downward shift of the PS curve.
35. Suppose the economy experiences a population growth that is translated in more workers with jobs and increase in competition in the goods market. In this case, we would expect to observe:
- A) an upward shift in the WS curve and a downward shift in the PS curve.

- B) a downward shift in the WS curve and a downward shift in the PS curve.
- C) a downward shift in the PS curve and an upward shift in the WS curve.
- D) an upward shift in the PS curve and an downward shift in the WS curve.
- E) a movement along the WS curve and an upward shift in the PS curve.

Suppose that the following equations describe an economy:

$C = 170 + 0.60Y_D$	$MS = 735; P = 1$	$T = 200$
$I = 100 - 4i$	$M^d = 0.75Y - 6i$	$G = 350$

36. The equation for equilibrium in the goods market is:
- A)  $Y = 1250 + 10i$ .
  - B)  $Y = 980 + 8i$ .
  - C)  $Y = 980 - 8i$ .
  - D)  $Y = 1250 - 10i$ .
  - E)  $Y = 1250 + 8i$ .
37. The equation for equilibrium in the financial markets:
- A)  $Y = 1250 + 10i$ .
  - B)  $Y = 980 + 8i$ .
  - C)  $Y = 980 - 8i$ .
  - D)  $Y = 1250 - 10i$ .
  - E)  $Y = 1250 + 8i$ .
38. The equilibrium level of output (Y), the interest rate (i), investment (I) and consumption (C) are, respectively:
- A)  $Y = 1200; i = 15; I = 40; C = 710$ .
  - B)  $Y = 1100; i = 5; I = 40; C = 700$ .
  - C)  $Y = 1100; i = 15; I = 40; C = 710$ .
  - D)  $Y = 1200; i = 15; I = 20; C = 710$ .
  - E)  $Y = 1000; i = 10; I = 40; C = 600$ .
39. Suppose that the Bank of Canada sought to achieve the equilibrium level of output  $Y = 1140$  through expansionary monetary policy alone. By how much would the Bank of Canada have to increase the money supply?
- A) 23
  - B) 72
  - C) 44
  - D) 38
  - E) 54
40. Suppose that G increases by 36 to 386. The new IS curve is given by:
- A)  $Y = 1340 - 8i$ .
  - B)  $Y = 1340 - 10i$ .
  - C)  $Y = 1340 + 10i$ .
  - D)  $Y = 1250 - 10i$ .
  - E)  $Y = 1250 + 8i$ .