

CONCORDIA UNIVERSITY
Department of Economics

ECON 203

SAMPLE MIDTERM EXAMINATION WITH ANSWERS

Multiple Choice Questions (2 marks each).

1. Gross domestic product (GDP) equals the _____ of final _____ produced within a country during a given period of time.
 - A) market value; goods
 - B) market value; services
 - C) market value; goods and services**
 - D) quantity; goods

2. The CPI is a measure of the:
 - A) real wage.
 - B) price of a specific good or service.
 - C) rate of inflation.
 - D) average level of prices relative to prices in the base year.**

3. Who of the following would be counted as unemployed by Statistics Canada?
 - A) A person with a part-time job.
 - B) A person with a full-time job.
 - C) A person employed or unemployed but actively looking for a job.**
 - D) A person willing to work who had not looked for a job in two months.

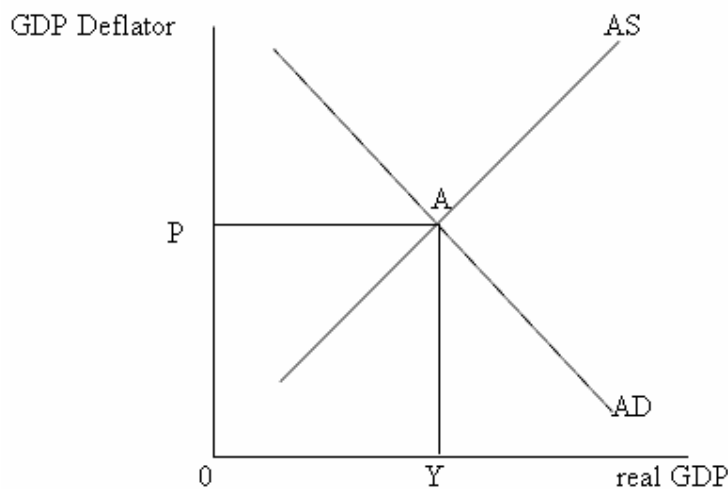
4. Your full-time accountant retires, so you hire a part-time accounting student at a much lower wage. As a result, GNP will:
 - A) rise.
 - B) remain unchanged.
 - C) fall.**
 - D) none of the above.

5. Three equivalent ways to measure GDP are total _____, total _____, and total

- _____.
- A) profits; production; saving
 - B) expenditure; income; profits
 - C) investment; consumption; saving
 - D) production; income; expenditure**
6. Nominal GDP measures the value of current:
- A) output at current prices.**
 - B) output when prices are held constant.
 - C) income received by households.
 - D) investment spending by firms.
7. Indicate below which is a good example of an intermediate good:
- A) nuts and bolts.
 - B) electricity generation.
 - C) steel supplied to a car manufacturer.**
 - D) a lathe.
8. _____ is a use of national income that _____ the flow of expenditures.
- A) investment, reduces
 - B) saving, increases
 - C) saving, reduces**
 - D) investment, does not affect
9. Net domestic income includes all the following except:
- A) small business income.
 - B) depreciation.**
 - C) net interest.
 - D) company profits.
10. If nominal GDP increases at a rate of 10 per cent per year while the GDP deflator increases at 8 per cent per year, then:
- A) real GDP remains constant.
 - B) real GDP rises by 10 per cent.
 - C) real GDP falls by 8 per cent.
 - D) real GDP rises by 2 per cent.**

Use the following to answer the question:

Figure 5.1 The AD/AS model for the year 2006



11. Refer to Figure 5.1. If the GDP deflator has a base year value of $P = 1.0$ then the following are correct except:
- A) real GDP in the year 2006 is OY .
 - B) nominal GDP in the year 2006 is the area $OY \times OP$.
 - C) **nominal and real GDP will be the same in every year.**
 - D) the GDP deflator in the year 2006 is OP .
12. The aggregate demand curve is:
- A) vertical if full employment exists.
 - B) horizontal when there is considerable unemployment in the economy.
 - C) **downsloping because of the interest-rate, wealth or real balances, and foreign trade effects.**
 - D) downsloping because production costs decrease as real output increases.
13. A fall in the Canadian price level will cause foreigners to
- A) **substitute Canadian goods for foreign goods.**
 - B) substitute foreign goods for Canadian goods.
 - C) buy more foreign goods.
 - D) buy fewer Canadian goods.
14. The substitution effect suggests that an increase in the Canadian price level relative to other countries will:
- A) increase the amount of Canadian real output purchased.
 - B) **increase Canadian imports and decrease Canadian exports.**

- C) increase both Canadian imports and Canadian exports.
 - D) decrease both Canadian imports and Canadian exports.
15. The short-run aggregate supply curve is upsloping because:
- A) of the interest-rate effect.
 - B) higher price levels create incentives to expand output when resource prices remain constant.**
 - C) of the net export effect.
 - D) higher price levels create an expectation among producers of still higher price levels.
16. A downward shift in the aggregate supply curve might best be explained by:
- A) an increase in business taxes.
 - B) a decrease in productivity.
 - C) an increase in nominal wages.
 - D) a decrease in the price of imported resources.**
17. The potential output curve shows the output level an economy can produce when
- A) firms adjust quantity rather than price.
 - B) capital is fully employed.
 - C) labour is fully employed.
 - D) both capital and labour are fully employed.**
18. In Canada during the recessions of the early 1980's and 1990's:
- A) Actual real GDP was greater than potential GDP.
 - B) Actual real GDP and potential GDP were equal.
 - C) Actual real GDP was less than potential GDP.**
 - D) potential GDP decline while actual GDP increased.
19. If the economy suffers from a recessionary gap:
- A) AD is stronger than required for equilibrium at potential output.
 - B) AD and AS intersect at potential output.
 - C) AS falls short of potential output.
 - D) AD is weaker than required for equilibrium at potential output.**

20. According to Okun's law, if growth in actual GDP exceeds growth in potential GDP
- A) unemployment rates will increase
 - B) employment will fall
 - C) the natural unemployment rate will increase
 - D) **the unemployment rate will fall**
21. In the short run with fixed wages and prices:
- A) **equilibrium real GDP is determined by aggregate demand.**
 - B) equilibrium real GDP is determined by aggregate supply.
 - C) labour and the productive capacity of firms are always fully employed.
 - D) equilibrium real GDP is a fixed amount and will not change.
22. All of the following statements about the consumption function are false except:
- A) the consumption function describes the relationship between aggregate consumption and the price level.
 - B) **the consumption function describes the relationship between aggregate consumption and the level of national income.**
 - C) the consumption function describes all equilibrium levels of income where aggregate saving and investment are equal.
 - D) the consumption function is not generally used in macroeconomics because consumption is only a relatively small part of aggregate income.
23. Other things constant, an increase in households' willingness to save more at every level of income will cause:
- A) the consumption function to become flatter because the MPC rises.
 - B) **the consumption function to make a downward parallel shift.**
 - C) the consumption function to remain stationary but the saving function to shift upward.
 - D) the consumption function to become steeper because the MPC declines.
24. As used in the income-expenditure diagram in macroeconomics, the 45 degree line:
- A) **shows all the points at which spending and real income are equal.**
 - B) contains only a consumption component.
 - C) represents consumption plus planned investment.
 - D) shows those income levels where the marginal propensity to save is 1.

Use the following to answer the next 3 questions:

The letters Y, C, S, and I represent GDP, consumption, saving, and investment respectively.

GDP (Y)	Consumption (C)	Investment (I)
\$0	\$60	\$30
100	120	40
200	180	50
300	240	60
400	300	70
500	360	80

25. Refer to the table above. The equation representing the investment schedule for the above economy is:
- A) $I = 0.3Y$.
 - B) $I = 80 - 0.3Y$.
 - C) $I = 30 + 0.1Y$.**
 - D) $I = I_0 = 30$.
26. Refer to the table above. The aggregate expenditure schedule in the above economy is:
- A) $AE = 90 + 0.4Y$.
 - B) $90 + 0.7Y$.**
 - C) $90 - 0.2Y$.
 - D) None of the above.
27. Refer to the table above. The equilibrium level of real GDP in the above economy is:
- A) 225.
 - B) 400.
 - C) 300.**
 - D) 500.
28. If firms experience an unplanned reduction in their inventories of \$75 billion, then:
- A) planned inventories will rise by \$75 billion.
 - B) planned inventories do not change.
 - C) firms have underestimated aggregate spending by \$75 billion.**

- D) aggregate spending is at its equilibrium level.
29. If national income is \$1500 billion and the level of planned spending by households and businesses is \$1575 billion, then we can say that:
- A) there will be an accumulation of inventories and output will rise.
 - B) there will be an accumulation of inventories and output will fall.
 - C) there will be an unplanned reduction in inventories and output will fall.
 - D) there will be an unplanned reduction in inventories and output will rise.**

Use the following to answer the next 3 questions:

Where I is planned investment, S is saving, and Y is gross domestic product (GDP).

$$I = I_0 = 80 \quad (6.3)$$

$$S = -80 + .4Y \quad (6.4)$$

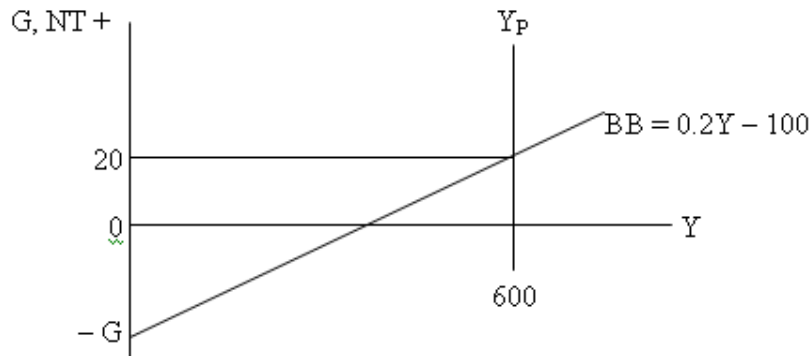
30. Refer to equations (6.3) and (6.4). The equilibrium GDP will be:
- A) \$160.
 - B) \$400.**
 - C) \$360.
 - D) \$480.
31. Refer to equations (6.3) and (6.4). In equilibrium consumption will be:
- A) \$400.
 - B) \$280.
 - C) \$320.**
 - D) \$360.
32. Refer to equations (6.3) and (6.4). In equilibrium saving will be:
- A) \$40.
 - B) \$120.
 - C) \$60.
 - D) \$80.**
33. Suppose that national income is initially at its equilibrium level when desired investment falls. We would expect:
- A) a fall in national income, but not by as much as the fall in desired investment.

- B) no change in national income even though desired investment spending falls.
 - C) an increase in national income by an amount equal to the reduction in investment spending.
 - D) **a fall in national income by some multiple of the fall in desired investment spending.**
34. The principle of the multiplier states that:
- A) **any increase in spending that causes the aggregate expenditure line to shift will result in a larger increase in national income.**
 - B) in the long run, the aggregate expenditure line becomes relatively flat as the economy approaches full employment.
 - C) any increase in national income will result in a larger increase in aggregate spending.
 - D) for any given increase in income, there will be a less than proportional increase in consumer spending.
35. In a diagram illustrating the savings and investment functions for a closed economy with no government, an increase in saving at every level of income will:
- A) shift the investment function up and increase equilibrium income.
 - B) increase the slope of the savings function and lower equilibrium income.
 - C) **leave the level of investment and saving unchanged but lower the equilibrium income.**
 - D) change the slope of the investment function but leave equilibrium income unchanged.
36. In a simple economy, with government spending but without any taxes, an equilibrium income occurs when:
- A) actual savings equals actual investment plus government spending.
 - B) **unintended inventory changes are zero.**
 - C) planned saving equals actual saving.
 - D) planned saving equals actual investment plus government spending.
37. If the MPC is .8 and the government increases spending by \$100 million, then we would expect the result to be:
- A) **an increase in real GDP of \$500 million.**
 - B) a reduction in equilibrium real GDP of \$80 million.
 - C) an increase in equilibrium real GDP of \$100 million.
 - D) no change in equilibrium real GDP.
38. If the MPC is .75, the net tax rate is 0.2 and the government increases spending

- by \$100 million, then we would expect the result to be:
- A) an increase in real GDP of \$400 million.
 - B) a reduction in equilibrium real GDP of \$100 million.
 - C) an increase in equilibrium real GDP of \$250 million.**
 - D) no change in equilibrium real GDP.
39. Which of the following best completes this statement: "Once we include a proportional income tax in the model of aggregate expenditure and equilibrium real GDP....:"
- A) individual incomes are higher than they would be without the taxes.
 - B) the marginal propensity to consume out of disposable income rises as a result of the tax.
 - C) the multiplier is lower than it would be without the taxes.**
 - D) the government must also be spending on goods and services.
40. One of the important underlying tenets of the balanced budget multiplier model is that:
- A) a change in taxes by the government causes households to change the composition of stock of wealth and will not affect aggregate demand.
 - B) for any increase in taxes, households will finance some of their increased tax liability out of savings.**
 - C) a change in fiscal policy changes aggregate demand and this causes a multiple change in aggregate income and output.
 - D) any increase in government spending and taxes will have essentially no effect on aggregate employment and income.
41. Suppose that the government increases its spending by 10 per cent and also increases taxes by 10 per cent. We would expect this to:
- A) essentially have no effect on the level of national income.
 - B) have a contractionary effect on national income.
 - C) decrease the marginal propensity to save out of each extra pound of income.
 - D) have an expansionary effect on national income.**
42. The structural budget balance shows what the budget balance would be if _____ is at _____.
- A) actual spending, planned spending
 - B) output, potential output**
 - C) actual tax revenue, forecast tax revenue
 - D) forecast consumers' expenditure, actual consumers' expenditure

Use the following to answer the next 3 questions:

Figure 7.6: A Government budget function



43. Refer to Figure 7.6. All figures are in billions of dollars. If the potential GDP is \$600 billion while the actual GDP is \$400 billion, the actual budget balance is:

- A) a deficit of \$200 billion.
- B) a surplus of \$60 billion.
- C) a surplus of \$40 billion.
- D) a deficit of \$20 billion.**

44. Refer to Figure 7.6. All figures are in billions of dollars. If the full-employment GDP is \$600 billion while the actual GDP is \$400 billion, the structural budget balance is

- A) + \$40 billion.
- B) zero.
- C) - \$ 60 billion.
- D) + \$20 billion.**

45. Refer to Figure 7.6. All figures are in billions of dollars. If the potential GDP is \$600 billion while the actual GDP is \$400 billion, the reduction in the budget balance caused by recessionary gap is:

- A) \$40 billion.**
- B) \$20 billion.
- C) zero.
- D) \$60 billion.

46. The progressive income tax and unemployment compensation are examples of:

- A) full-employment budgeting.
- B) automatic stabilizers.**
- C) monetary policy.
- D) a balanced budget multiplier.

47. Assume the government runs budget surplus. The result is:
- A) an increase in the total of outstanding government bonds.
 - B) the paradox of thrift.
 - C) a decrease in the public debt.**
 - D) the money-fund effect.
48. _____ export expenditure increases equilibrium output and a _____ MPZ reduces output.
- A) higher, lower
 - B) higher, higher**
 - C) lower, lower
 - D) lower, higher
49. Other things equal, if \$100 billion of government purchases (G) is added to aggregate expenditure (C + I + XN), GDP will:
- A) increase by \$100 billion.
 - B) increase by less than \$100 billion.
 - C) increase by more than \$100 billion.**
 - D) fall by \$100 billion.

Use the following to answer the next question:

Consumption: $C = 40 + .8Y$

Investment $I = 40$

Exports $X = 20$

Imports $Z = 30$

50. The equilibrium level of real GDP (=Y) in the economy is:

- A) \$200.
- B) \$245.
- C) \$320.
- D) \$350.**