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Student # _____

**LAKEHEAD UNIVERSITY
APRIL TEST - MACROECONOMICS**

**Economics 1100 YD
Principles of Economics**

**Sergio Buonocore
April 16, 2009
6:00 – 8:00 pm
UC 1017**

DURATION: 2 hours

Non-Programmable Calculators allowed.

THIS EXAMINATION MAY NOT BE TAKEN FROM THE EXAMINATION ROOM

You MUST count the number of pages in this examination paper BEFORE beginning to write. Report any discrepancy immediately to the professor.

This is page 1 of 15 pages

Multiple Choice

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

- _____ 1. Money
 - a. is more efficient than barter.
 - b. makes trades easier.
 - c. allows greater specialization.
 - d. All of the above are correct.
- _____ 2. When Arnold use dollars to record his income and expenses, he is using money as a
 - a. unit of account.
 - b. means of payment.
 - c. store of value.
 - d. medium of exchange.
- _____ 3. Which list ranks assets from most to least liquid?
 - a. currency, fine art, stocks
 - b. currency, stocks, fine art
 - c. fine art, currency, stocks
 - d. fine art, stocks, currency
- _____ 4. Current Canadian currency is
 - a. fiat money with intrinsic value.
 - b. fiat money with no intrinsic value.
 - c. commodity money with intrinsic value.
 - d. commodity money with no intrinsic value.
 - e. None of the above are correct.
- _____ 5. M1 includes
 - a. currency.
 - b. demand deposits.
 - c. travelers' checks.
 - d. foreign currency accounts
 - e. both a and b.
- _____ 6. Credit cards are
 - a. used as a method of payment.
 - b. part of the M1 money supply.
 - c. a method of deferring payment.
 - d. a unit of account.
- _____ 7. The agency responsible for regulating the money supply in Canada is
 - a. the Comptroller of the Currency.
 - b. the U.S. Treasury.
 - c. the Bank of Canada.
 - d. the TD Bank.
 - e. the Canadian Payments Association.
- _____ 8. Who owns Bank of Canada?
 - a. Private individuals
 - b. The Queen
 - c. The commercial banks
 - d. The federal government of Canada

- _____ 9. The Board of Directors at Bank of Canada
- a. is chaired by the Governor of the Bank of Canada.
 - b. are appointed by the prime minister.
 - c. has eleven members.
 - d. All of the above are correct.
- _____ 10. Which of the following statements about Bank of Canada is incorrect?
- a. The members of the Board of Directors are appointed by the Governor General.
 - b. The Bank of Canada makes monetary policy.
 - c. The gold standard does not apply in Canada anymore.
 - d. The Bank of Canada regulates chartered banks.
- _____ 11. In a 100-percent-reserve banking system,
- a. banks can create money by issuing currency.
 - b. banks can create money by lending out reserves.
 - c. the Bank of Canada can increase the money supply with open market sales.
 - d. banks hold as many reserves as they hold deposits.
 - e. banks hold no reserves.
- _____ 12. Suppose a bank has \$10,000 in deposits and \$7,000 in loans. It has a reserve ratio of
- a. 3 percent.
 - b. 7 percent.
 - c. 30 percent.
 - d. 70 percent.
 - e. None of the above are correct.
- _____ 13. If you deposit \$100 into a demand deposit at a bank, this action by itself
- a. does not change the money supply.
 - b. increases the money supply.
 - c. decreases the money supply.
 - d. has an indeterminate effect on the money supply.
- _____ 14. Under a fractional reserve banking system, banks
- a. hold more reserves than deposits.
 - b. generally lend out a majority of the funds deposited.
 - c. cause the money supply to fall by lending out reserves.
 - d. All of the above are correct.
- _____ 15. If the reserve ratio is 7 percent and a bank receives a new deposit of \$300, it
- a. must increase required reserves by \$21.
 - b. will initially see reserves increase by \$279.
 - c. will be able to make new loans up to a maximum of \$279.
 - d. Both a and c are correct.
 - e. None of the above is true.
- _____ 16. A central bank raised the reserve requirement ratio from 10 percent to 12 percent. Other things the same this should have
- a. increased both the money multiplier and the money supply.
 - b. decreased both the money multiplier and the money supply.
 - c. increased the money multiplier and decreased the money supply.
 - d. decreased the money multiplier and increased the money supply.

Use the balance sheet for the following questions.

Table 29-2

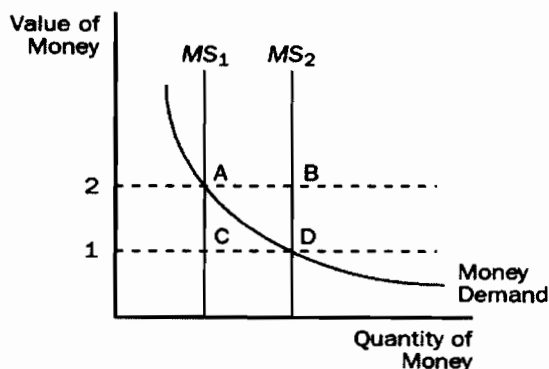
<u>First Bank of Mason City</u>			
Assets		Liabilities	
Required Reserves	\$20.00	Deposits	\$100.00
Loans	\$80.00		

- _____ 17. **Refer to Table 29-2.** The reserve ratio is
- 0 percent.
 - 20 percent.
 - 80 percent.
 - 100 percent.
- _____ 18. **Refer to Table 29-2.** If \$1,000 is deposited into the First Bank of Mason City,
- total reserves will initially increase by \$200.
 - liabilities will decrease by \$1,000.
 - assets will increase by \$1,000.
 - required reserves will increase by \$800.
- _____ 19. **Refer to Table 29-2.** If \$400 is deposited into the First Bank of Mason City,
- the bank will be able to make additional loans totaling \$320.
 - excess reserves initially increase by \$320.
 - required reserves initially increase by \$80.
 - All of the above are true.
- _____ 20. If a bank uses \$100 of reserves to make a new loan when the reserve ratio is 20 percent, this action by itself initially makes the money supply
- and wealth increase by \$100.
 - and wealth decrease by \$100.
 - increase by \$100 while wealth does not change.
 - decrease by \$100 while wealth decreases by \$100.
- _____ 21. As the reserve ratio increases, the money multiplier
- increases.
 - does not change.
 - decreases.
 - could do any of the above.
- _____ 22. If the central bank in some country lowered the reserve ratio, the money multiplier
- would increase.
 - would not change.
 - would decrease.
 - could do any of the above.
- _____ 23. At one time, the country of Aquilonia had no banks, but had currency of \$10 million. Then a banking system was established with a reserve requirement of 20 percent. The people of Aquilonia deposited half of their currency into the banking system. If banks do not hold excess reserves, what is Aquilonia's money supply now?
- \$10 million
 - \$12 million
 - \$25 million
 - \$30 million

- _____ 24. Which list contains only actions that increase the money supply?
- make open market purchases, raise the reserve requirement ratio
 - make open market purchases, lower the reserve requirement ratio
 - make open market sales, raise the reserve requirement ratio
 - make open market sales, lower the reserve requirement ratio
- _____ 25. The Bank of Canada's policy decisions have an important influence on
- both the rate of inflation and the level of employment in the short run.
 - the rate of inflation in the long run and the level of employment in the short run.
 - the rate of inflation in the short run and the level of employment in the long run.
 - both the rate of inflation and the level of employment in both the short run and the long run.
- _____ 26. When the value of money rises, the number of dollars needed to buy a representative basket of goods
- increases, and so the price level rises.
 - increases, and so the price level falls.
 - decreases, and so the price level rises.
 - decreases, and so the price level falls.
- _____ 27. As the price level decreases, the value of money
- increases, so people want to hold more of it.
 - increases, so people want to hold less of it.
 - decreases, so people want to hold more of it.
 - decreases, so people want to hold less of it.
- _____ 28. In the fourteenth century, the Western African Emperor Kankan Musa traveled to Cairo where he gave away much gold, which was in use as a medium of exchange. We would predict that this increase in gold
- raised both the price level and the value of gold in Cairo.
 - raised the price level, but decreased the value of gold in Cairo.
 - lowered the price level, but increased the value of gold in Cairo.
 - lowered both the price level and the value of gold in Cairo.
- _____ 29. In the 1970s in response to recessions caused by an increase in the price of oil, the central banks in many countries increased the money supply. The central banks might have done this by
- selling bonds on the open market, which would have raised the value of money.
 - purchasing bonds on the open market, which would have raised the value of money.
 - selling bonds on the open market, which would have raised the value of money.
 - purchasing bonds on the open market, which would have lowered the value of money.
- _____ 30. When the money market is depicted in a diagram with the value of money on the vertical axis, if the price level is above the equilibrium level, there is a
- shortage, so the price level will rise.
 - shortage, so the price level will fall.
 - surplus, so the price level will rise.
 - surplus, so the price level will fall.
 - black market solution.

Use the figure below for the following questions.

Figure 30-1



31. **Refer to Figure 30-1.** If the money supply is MS_2 and the value of money is 2,
 - a. the value of money is less than its equilibrium level.
 - b. the price level is higher than its equilibrium level.
 - c. money demand is greater than the money supply.
 - d. the money supply is greater than money demand.
 - e. None of the above are correct.
32. **Refer to Figure 30-1.** If the money supply is MS_2 and the value of money is 2, there is excess
 - a. demand equal to the distance between A and C.
 - b. demand equal to the distance between A and B.
 - c. supply equal to the distance between A and C.
 - d. supply equal to the distance between A and B.
33. **Refer to Figure 30-1.** When the money supply curve shifts from MS_1 to MS_2 ,
 - a. the demand for goods and services decreases.
 - b. the economy's ability to produce goods and services increases.
 - c. the equilibrium price level increases.
 - d. the equilibrium value of money increases.
 - e. None of the above are correct.
34. **Refer to Figure 30-1.** When the money supply curve shifts from MS_1 to MS_2 ,
 - a. the equilibrium value of money decreases.
 - b. the equilibrium price level decreases.
 - c. the supply of money has decreased.
 - d. the demand for goods and services will decrease.
35. **Refer to Figure 30-1.** If the current money supply is located at MS_1 ,
 - a. there is no excess supply or excess demand if the value of money is 2.
 - b. the equilibrium is at point C.
 - c. there is an excess supply of money if the value of money is 1.
 - d. All of the above are correct.

- ____ 36. Your boss gives you an increase in the number of dollars you earn per hour. This increase in pay makes
- a. your nominal wage increase. If your nominal wage rose by a greater percentage than the price level, then your real wage also increased.
 - b. your nominal wage increase. If your nominal wage rose by a greater percentage than the price level, then your real wage decreased.
 - c. your real wage increase. If your real wage rose by a greater percentage than the price level, then your nominal wage also increased.
 - d. your real wage decrease. If your real wage rose by a greater percentage than the price level, then your nominal wage decreased.
 - e. None of the above are correct.
- ____ 37. The classical dichotomy refers to the idea that the supply of money
- a. is irrelevant for understanding the determinants of nominal and real variables.
 - b. determines nominal variables, but not real variables.
 - c. determines real variables, but not nominal variables.
 - d. is a determinant of both real and nominal variables.
- ____ 38. The principle of monetary neutrality implies that an increase in the money supply will
- a. increase real GDP and the price level.
 - b. increase real GDP, but not the price level.
 - c. increase the price level, but not real GDP.
 - d. increase neither the price level nor real GDP.
 - e. None of the above are correct.
- ____ 39. The velocity of money is
- a. the rate at which the central bank puts money into the economy.
 - b. the same thing as the long-term growth rate of the money supply.
 - c. the money supply divided by nominal GDP.
 - d. the average number of times per year a dollar is spent.
- ____ 40. Velocity is computed as
- a. $(P \times Y)/M$.
 - b. $(P \times M)/Y$.
 - c. $(Y \times M)/P$.
 - d. $(Y \times M)/V$.
- ____ 41. According to the quantity equation, if $P = 15$, $Y = 10$, $M = 20$, then $V =$
- a. 30
 - b. 15
 - c. 7.5
 - d. 7
 - e. 4
- ____ 42. If velocity and output were nearly constant,
- a. the inflation rate would be much higher than the money supply growth rate.
 - b. the inflation rate would be about the same as the money supply growth rate.
 - c. the inflation rate would be much lower than the money supply growth rate.
 - d. any of the above would be possible.
- ____ 43. The money supply in Freedonia is \$200 billion. Nominal GDP is \$800 billion and real GDP is \$400 billion. Assuming that velocity is stable, if real GDP grows by 10 percent this year, and if the money supply does not change this year, then
- a. the inflation rate will be zero.
 - b. nominal GDP will grow by 10 percent.
 - c. nominal GDP will stay the same.
 - d. none of the above are correct.

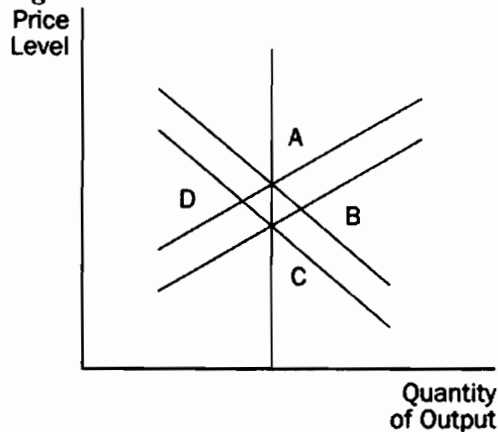
- _____ 44. If money is neutral and velocity is stable, an increase in the money supply creates a proportional increase in
- real output.
 - nominal output.
 - the price level.
 - Both b and c are correct.
- _____ 45. The nominal interest rate is 5 percent and the inflation rate is 2 percent. What is the real interest rate?
- 7percent.
 - 6 percent.
 - 5 percent.
 - 3 percent.
 - 3 percent.
- _____ 46. If a country had deflation,
- the nominal interest rate would be greater than the real interest rate.
 - the real interest rate would be greater than the nominal interest rate.
 - the real interest rate would equal the nominal interest rate.
 - None of the above are necessarily correct.
- _____ 47. If the money supply growth rate permanently increased from 4 percent to 12 percent, we would expect that
- inflation would increase by 8 percent, and the nominal interest rate would increase by less than 10 percent.
 - the inflation rate would increase by less than 8 percent, and the nominal interest rate would increase by 8 percent.
 - both the inflation rate and the nominal interest rate would increase by 8 percent.
 - both the inflation rate and the nominal interest rate would increase by less than 8 percent.
 - both the inflation rate and the nominal interest rate would decrease by more than 8 percent.
- _____ 48. The cost of changing price tags and price listings is known as
- inflation-induced tax distortions.
 - relative-price variability costs.
 - shoeleather costs.
 - menu costs.
- _____ 49. Given a nominal interest rate of 7 percent, in which case would you earn the lowest after-tax real rate of interest?
- Inflation is 4 percent; the tax rate is 25 percent.
 - Inflation is 3 percent; the tax rate is 20 percent.
 - Inflation is 2 percent; the tax rate is 15 percent.
 - Inflation is 1 percent; the tax rate is 10 percent
 - The after-tax real interest rate is the same for all of the above.
- _____ 50. When deciding how much to save, people care most about
- after-tax nominal interest rates.
 - after-tax real interest rates.
 - before-tax real interest rates.
 - before-tax nominal interest rates.
- _____ 51. Which of the following explains why production rises in most years?
- increases in the labour force
 - increases in the capital stock
 - increases in technology
 - All of the above are correct.

- _____ 52. A short period of falling incomes and rising unemployment is called a
- depression.
 - recession.
 - expansion.
 - business cycle.
- _____ 53. During a recession the economy experiences
- rising employment and income.
 - rising employment and falling income.
 - rising income and falling employment.
 - falling employment and income.
 - falling employment and rising income.
- _____ 54. The decrease in real GDP during a recession is
- mostly a decrease in investment spending.
 - mostly a decrease in consumption spending.
 - about equally divided between consumption and investment spending.
 - sometimes mostly a decrease in consumption and sometimes mostly a decrease in investment.
- _____ 55. Real GDP
- is the dollar value of all goods produced by the citizens of an economy within a given time measured in current year prices.
 - measures economic activity and income.
 - is used primarily to measure long-run trends in the economy.
 - All of the above are correct.
- _____ 56. Which part of real GDP fluctuates most over the course of the business cycle?
- consumption
 - government expenditures
 - investment
 - net exports
- _____ 57. The overall price level is measured by
- the price of some particular commodity or service.
 - the rate of inflation.
 - the CPI.
 - the GDP deflator.
 - either the CPI or the GDP deflator.
- _____ 58. The aggregate demand curve
- slopes downward for the same reasons that market demand curves slope downward.
 - is vertical in the long run.
 - shows an inverse relation between the price level and the quantity of all goods and services demanded.
 - All of the above are correct.
- _____ 59. Which of the following is included in the aggregate demand for goods and services?
- consumption demand
 - investment demand
 - net exports
 - All of the above are correct.

- ___ 60. The aggregate quantity of goods demanded increases if
- real wealth falls.
 - the interest rate rises.
 - the dollar depreciates.
 - None of the above is correct.
- ___ 61. An increase in the price level induces people to hold
- less money, so they lend less, and the interest rate rises.
 - less money, so they lend more, and the interest rate falls.
 - more money, so they lend more, and the interest rate falls.
 - more money, so they lend less, and the interest rate rises.
- ___ 62. When the dollar appreciates, Canadian
- exports decrease, while imports increase.
 - exports and imports decrease.
 - exports and imports increase.
 - exports increase, while imports decrease.
- ___ 63. The aggregate demand curve slopes
- downward because higher prices cause the exchange rate to depreciate.
 - downward because higher prices cause real wealth to decrease and interest rates to increase.
 - upward because higher prices cause people to increase their production.
 - upward because higher prices cause real wealth to increase and interest rates to decrease.
- ___ 64. If people want to save more for retirement
- or if the government raises taxes, aggregate demand shifts right.
 - or if the government raises taxes, aggregate demand shifts left.
 - aggregate demand shifts right. If the government raises taxes, aggregate demand shifts left.
 - aggregate demand shifts left. If the government raises taxes, aggregate demand shifts right.
 - None of the above are correct.
- ___ 65. The aggregate supply curve is upward sloping rather than vertical in
- the short and long run.
 - neither the short nor long run.
 - the long run, but not the short run.
 - the short run, but not the long run.
- ___ 66. The sticky wage theory of the short-run aggregate supply curve says that when prices fall unexpectedly, the real wage
- rises, so employment rises.
 - rises, so employment falls.
 - falls, so employment rises.
 - falls, so employment falls.
- ___ 67. Which of the following shifts both short-run and long-run aggregate supply right?
- an increase in the actual price level
 - an increase in the expected price level
 - an increase in the capital stock
 - None of the above is correct.
- ___ 68. Which of the following shift short-run aggregate supply left?
- an increase in price expectations
 - an increase in the price level
 - a decrease in the money supply
 - a decrease in the price of oil

Consider the exhibit below for the following questions.

Figure 33-1

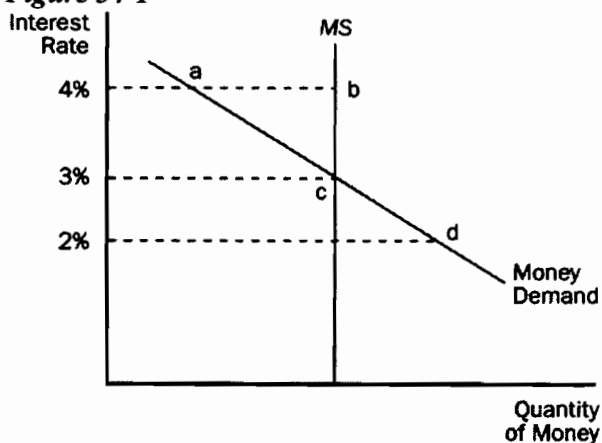


69. Refer to Figure 33-1. An increase in the money supply would move the economy from C to
- B in the short run and the long run.
 - D in the short run and the long run.
 - B in the short run and A in the long run.
 - D in the short run and C in the long run.
70. Refer to Figure 33-1. An increase the money supply would move the economy from C to
- A in the long run.
 - B in the long run.
 - return to C in the long run.
 - D in the long run.
71. Refer to Figure 33-1. If the economy is at A and there is a fall in aggregate demand, in the short run the economy
- stays at A.
 - moves to B.
 - moves to C.
 - moves to D.
72. Refer to Figure 33-1. If the economy starts at A and there is a fall in aggregate demand, the economy moves
- back to A in the long run.
 - to B in the long run.
 - to C in the long run.
 - to D in the long run.
73. Refer to Figure 33-1. If the economy starts at A and moves to D, the economy moves
- to A in the long run.
 - to B in the long run.
 - to C in the long run.
 - back to D in the long run.
74. Refer to Figure 33-1. The economy would be moving to long-run equilibrium if it started at
- A and moved to B.
 - C and moved to B.
 - D and moved to C.
 - None of the above is correct.

- ____ 75. **Refer to Figure 33-1.** An adverse shift in aggregate supply would move the economy from
- A to B.
 - C to D.
 - B to A.
 - D to C.
- ____ 76. **Refer to Figure 33-1.** In the short run, a favourable shift in aggregate supply would move the economy from
- A to B.
 - B to C.
 - C to D.
 - D to A.
- ____ 77. Fiscal policy affects the economy
- only in the short run.
 - only in the long run.
 - in both the short and long run.
 - in neither the short nor long run.
- ____ 78. Which of the following is *not* a response that would result from a decrease in the price level and so help to explain the slope of the aggregate demand curve?
- When interest rates fall, Sleepwell Hotels decides to build some new hotels.
 - The exchange rate falls, so French restaurants in Paris buy more Iowa pork.
 - Janet feels wealthier because of the price drop and so she decides to remodel her bathroom.
 - With prices down and wages fixed by contract, Gatekeeper Computers decides to lay off workers.
 - None of the above are correct.
- ____ 79. Liquidity preference refers directly to Keynes' theory concerning
- the effects of changes in money demand and supply on interest rates.
 - the effects of changes in money demand and supply on exchange rates.
 - the effects of wealth on expenditures.
 - the difference between temporary and permanent changes in income.
 - None of the above are correct.
- ____ 80. According to liquidity preference theory, the money supply curve would shift if Bank of Canada
- engaged in open-market transactions.
 - changed the bank rate.
 - changed the reserve requirement.
 - did any of the above.
- ____ 81. According to the theory of liquidity preference, which variable adjusts to balance the supply and demand for money?
- interest rate
 - money supply
 - quantity of output
 - price level
 - the velocity of circulation

For the following questions, consult the diagram below:

Figure 34-1



82. Refer to Figure 34-1. If the current interest rate is 2 percent,
- there is excess money supply.
 - people will sell more bonds, which drives interest rates up.
 - as the money market moves to equilibrium, people will buy more goods.
 - All of the above are correct.
83. Refer to Figure 34-1. There is excess money demand at an interest rate of
- 2 percent.
 - 3 percent.
 - 4 percent.
 - None of the above are correct.
84. Refer to Figure 34-1. At an interest rate of 4 percent there is excess
- money demand equal to the distance between a and b.
 - money demand equal to the distance between b and c.
 - money supply equal to the distance between b and a.
 - money supply equal to the distance between c and b.
85. Refer to Figure 34-1. Which of the following is correct?
- If the interest rate is 4 percent, there is excess money demand, and the interest rate will fall.
 - If the interest rate is 3 percent, there is excess money supply, and the interest rate will rise.
 - If the interest rate is 4 percent, the demand for goods will rise when the money market is in its new equilibrium.
 - None of the above is correct.
86. If there is excess money demand, people will
- deposit more into interest-bearing accounts, and the interest rate will fall.
 - deposit more into interest-bearing accounts, and the interest rate will rise.
 - withdraw money from interest-bearing accounts, and the interest rate will fall.
 - withdraw money from interest-bearing accounts, and the interest rate will rise.
87. Which of the following shifts money demand to the right?
- an increase in the price level
 - a decrease in the price level
 - an increase in the interest rate
 - a decrease in the interest rate

- ____ 88. According to liquidity preference theory, an increase in the price level shifts the
- money demand curve right so the interest rate increases.
 - money demand curve right so the interest rate decreases.
 - money demand curve left so the interest rate decreases.
 - money demand curve left so the interest rate increases.
- ____ 89. According to liquidity preference theory, people will demand fewer goods and services if the price level
- or interest rate increase.
 - or interest rate decrease.
 - increases or the interest rate decreases.
 - decreases or the interest rate increases.
- ____ 90. Which of the following shifts aggregate demand to the left?
- an increase in the price level
 - an increase in the money supply
 - a decrease in the price level
 - a decrease in the money supply
- ____ 91. If a central bank targets the interest rate,
- it can then set the money supply at whatever value it wants.
 - it must increase the money supply if the interest rate is above its target.
 - it must decrease the money supply if the interest rate is above its target.
 - None of the above is correct.
- ____ 92. If the stock market booms,
- aggregate demand increases, which Bank of Canada could offset by increasing the money supply.
 - aggregate supply increases, which Bank of Canada could offset by increasing the money supply.
 - aggregate demand increases, which Bank of Canada could offset by decreasing the money supply.
 - aggregate supply increases, which Bank of Canada could offset by decreasing the money supply.
 - None of the above are correct.
- ____ 93. When Bank of Canada decreases the money supply we expect
- interest rates and stock prices to rise.
 - interest rates and stock prices to fall.
 - interest rates to rise and stock prices to fall.
 - interest rates to fall and stock prices to rise.
- ____ 94. The multiplier effect is the multiplied impact on
- the money supply of a given increase in government purchases.
 - tax revenues of a given increase in government purchases.
 - investment of a given increase in interest rates.
 - aggregate demand of a given increase in government purchases.
- ____ 95. The government purchases multiplier is defined as
- MPC .
 - $1 - MPC$.
 - $1/MPC$.
 - $1/(1 - MPC)$.

- ____ 96. If the $MPC = .9$, then the government purchases multiplier is about
- a. 0.10
 - b. 1
 - c. 1.11
 - d. 9
 - e. 10
- ____ 97. If the MPC is 0, the multiplier is
- a. 0.
 - b. 1.
 - c. infinite.
 - d. None of the above is correct.
- ____ 98. The reduction in demand that results when a fiscal expansion raises the interest rate is called the
- a. multiplier effect.
 - b. crowding-out effect.
 - c. accelerator effect.
 - d. Riccardian equivalence effect.
 - e. Fisher effect.
- ____ 99. An increase in government purchases is likely to
- a. decrease interest rates.
 - b. result in a net decrease in aggregate demand.
 - c. crowd out investment spending by business.
 - d. decrease money demand.
- ____ 100. Suppose that the MPC is .50 and there is no investment accelerator or crowding- out effects. If government expenditures increase \$20 billion, aggregate demand
- a. shifts right \$20 billion.
 - b. shifts right \$25 billion.
 - c. shifts right \$40 billion.
 - d. None of the above is correct.