Name:____________________________ Student #______________________

LAKEHEAD UNIVERSITY
APRIL TEST - MACROECONOMICS

Economics 1100 YA
Principles of Economics

Sergio Buonocore
April 12, 2011
6:00 – 8:00 pm
GYM ROWS: L M N O S T U V W X Y

DURATION: 2 hours

Non-Programmable Calculators allowed.

THIS EXAMINATION <u>MAY NOT</u> 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 16 pages

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

____ 1. Barter
  a. requires a double-coincidence of wants.
  b. is less efficient than money.
  c. is the trading of goods for goods.
  d. All of the above are correct.

____ 2. Which of the following is a store of value?
  a. currency
  b. federal government bonds
  c. fine art
  d. All of the above are correct.

____ 3. Which of the following best illustrates the medium of exchange function of money?
  a. You keep some money hidden in your shoe.
  b. You keep track of the value of your assets in terms of currency.
  c. You pay for your double latte using currency.
  d. None of the above is correct.

____ 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. 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.

____ 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 Bank of Canada does all except which of the following?
  a. control the supply of money
  b. control the value of money
  c. make loans to individuals
  d. regulate the banking system
  e. It does all of the above.

____ 8. Who owns Bank of Canada?
  a. Private individuals
  b. The Queen
  c. The commercial banks
  d. The federal government of Canada

____ 9. On a bank's T-account,
a. both deposits and reserves are assets.
b. both deposits and reserves are liabilities.
c. deposits are assets, reserves are liabilities.
d. reserves are assets, deposits are liabilities.

____ 10. Suppose that the reserve ratio is 5 percent and that a bank has $3,000 in deposits. Its required reserves are
a. $150.
b. $50.
c. $1,500.
d. $500.
e. $3,000.

____ 11. 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.

____ 12. 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.

Table 29-4

The following information pertains to the Bank of Edmonton.

Assets:		Liabilities:	
Reserves	$100	Deposits	$1,000
Loans	$900		

____ 13. **Refer to Table 29-4.** If the Bank of Edmonton has loaned out all the money it wants given its deposits, then its reserve ratio is
a. 1%
b. 5%
c. 10%
d. 15%
e. 20%

____ 14. **Refer to Table 29-4.** Assume that the Bank of Edmonton is holding the required percent of deposits as reserves. Also, assume all other banks hold only the required percent of deposits as reserves, and that people hold only deposits and no currency. What is the money multiplier?
a. 1
b. 5
c. 10
d. 15
e. 20

____ 15. **Refer to Table 29-4.**If the Bank of Canada requires banks to hold 5 percent of deposits as reserves, how much in excess reserves does the Bank of Edmonton now hold?
a. $5
b. $25
c. $50
d. $55
e. $75

____ 16. **Refer to Table 29-4.** Assume that all other banks hold only the required 5 percent of deposits as reserves and people hold only deposits and no currency. If the Bank of Edmonton decides to hold exactly 5 percent reserves, by how much would the economy's money supply increase?
a. $500
b. $1,000
c. $1,500
d. $2,000
e. $2,500

____ 17. If the central bank in some country lowered the reserve ratio, the money multiplier
a. would increase.
b. would not change.
c. would decrease.
d. could do any of the above.

____ 18. The banking system has $10 million in reserves, the reserve requirement is 20 percent, and there are no excess reserves. The public holds $10 million in cash. Then bankers decide that it is prudent to hold some excess reserves, and so begin to hold 25 percent of deposits in the form of reserves. At the same time, the public decides to withdraw $5 million in currency from the banking system. Other things the same, these actions will cause the money supply to
a. change forms, but not size.
b. fall by $10 million.
c. fall by $25 million.
d. fall by $35 million.

____ 19. Which list contains only actions that decrease the money supply?
a. lower the bank rate, raise the reserve requirement ratio
b. lower the bank rate, lower the reserve requirement ratio
c. raise the bank rate, raise the reserve requirement ratio
d. raise the bank rate, lower the reserve requirement ratio

____ 20. Which of the following is false?
a. A central bank indirectly controls the money supply.
b. Banks determine the reserve requirement.
c. Banks can create money in a fractional reserve banking system.
d. A central bank can control the level of reserves in the banking system.

____ 21. Inflation can be measured by the
a. change in the consumer price index.
b. percentage change in the consumer price index.
c. percentage change in the price of a specific commodity.
d. change in the price of a specific commodity.

____ 22. The quantity theory of money
- a. is a fairly recent addition to economic theory.
- b. can explain both moderate and hyperinflations.
- c. argues that inflation is caused by too little money in the economy.
- d. All of the above are correct.

____ 23. Economists all agree that
- a. neither high inflation nor moderate inflation is very costly.
- b. both high and moderate inflation are quite costly.
- c. high inflation is costly, but disagree about the costs of moderate inflation.
- d. moderate inflation is as costly as high inflation.

____ 24. The supply of money is determined by
- a. the price level.
- b. the Ministry of Finance.
- c. the Bank of Canada.
- d. the demand for money.
- e. the Treasury Board of Canada.

____ 25. As the price level decreases, the value of money
- a. increases, so people want to hold more of it.
- b. increases, so people want to hold less of it.
- c. decreases, so people want to hold more of it.
- d. decreases, so people want to hold less of it.

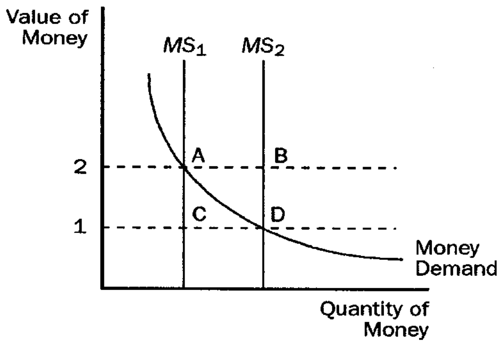
____ 26. When the money market is depicted in a diagram with the value of money on the vertical axis, the value of money increases if
- a. either money demand or money supply shifts right.
- b. either money demand or money supply shifts left.
- c. money demand shifts right or money supply shifts left.
- d. money demand shifts left or money supply shifts right.

____ 27. When the money market is depicted in a diagram with the value of money on the vertical axis, if the money supply is increased, then in the long run the price level
- a. and the quantity of money demanded increases.
- b. increases, but the quantity of money demanded decreases.
- c. decreases, but the quantity of money demanded increases.
- d. and the quantity of money demanded decreases.
- e. None of the above are correct.

____ 28. A decrease in the money supply creates an excess
- a. supply of money that is eliminated by rising prices.
- b. supply of money that is eliminated by falling prices.
- c. demand for money that is eliminated by rising prices.
- d. demand for money that is eliminated by falling prices.

Use the figure below for the following questions.

Figure 30-1



____ 29. **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.

____ 30. **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.

____ 31. **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.

____ 32. **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.

____ 33. **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.

____ 34. Real GDP measures

a. the total quantity of final goods and services produced.
b. the dollar value of the economy's output of final goods and services.
c. the total income received from producing final goods and services at current prices.
d. All of the above are correct.

____ 35. The price level is a

a. relative variable.
b. actual variable.
c. real variable.
d. nominal variable.
e. endogenous variable.

____ 36. According to the classical dichotomy, which of the following is influenced by monetary factors?

a. real GDP
b. unemployment
c. nominal interest rates
d. the real wage rate.
e. All of the above are correct.

____ 37. Monetary neutrality implies that an increase in the quantity of money will

a. increase employment.
b. increase the price level.
c. increase the incentive to save.
d. not affect the price level.

____ 38. 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.

____ 39. Based on the quantity equation, if $M = 125$, $V = 4$, and $Y = 200$, then $P =$

a. 0.5.
b. 1
c. 1.5
d. 2
e. 2.5

____ 40. According to the quantity equation if $P = 4$ and $Y = 800$, which of the following pairs could M and V be?

a. 800, 4
b. 600, 3
c. 400, 2
d. 200, 1

____ 41. Which of the following explains why production rises in most years?

a. increases in the labour force
b. increases in the capital stock
c. increases in technology
d. All of the above are correct.

____ 42. During a recession the economy experiences

a. rising employment and income.
b. rising employment and falling income.
c. rising income and falling employment.
d. falling employment and income.
e. falling employment and rising income.

____ 43. Business cycles
- a. are explained mostly by fluctuations in consumption.
- b. no longer are very important due to government policy.
- c. are fluctuations in real GDP and related variables over time.
- d. are easily predicted by competent economists.
- e. None of the above are correct.

____ 44. The decrease in real GDP during a recession is
- a. mostly a decrease in investment spending.
- b. mostly a decrease in consumption spending.
- c. about equally divided between consumption and investment spending.
- d. sometimes mostly a decrease in consumption and sometimes mostly a decrease in investment.

____ 45. Real GDP
- a. moves in the same direction as unemployment.
- b. is not adjusted for inflation.
- c. also measures income.
- d. All of the above are correct.

____ 46. Which of the following is incorrect concerning the long run?
- a. Higher money supply growth leads to higher output growth.
- b. An unemployment rate of zero is unobtainable.
- c. Per-capita real GDP depends on productivity.
- d. An increase in the money supply raises the price level.
- e. None of the above are correct.

____ 47. According to classical economic theory, changes in the money supply affect
- a. real GDP.
- b. real interest rates.
- c. the price level.
- d. All of the above are correct.

____ 48. The model of aggregate demand and aggregate supply explains the relationship between
- a. the price and quantity of a particular good.
- b. unemployment and output.
- c. wages and employment.
- d. real GDP and the price level.

____ 49. Which of the following adjusts to bring aggregate supply and demand into balance?
- a. the price level
- b. the real rate of interest
- c. the money supply
- d. technology
- e. the real exchange rate

____ 50. Which of the following is included in the aggregate demand for goods and services?
- a. consumption demand
- b. investment demand
- c. net exports
- d. All of the above are correct.

____ 51. The downward slope of the aggregate demand curve shows that an increase in the
a. money supply causes the aggregate quantity of goods and services demanded to increase.
b. money supply causes the aggregate quantity of goods and services demanded to decrease.
c. price level causes the aggregate quantity of goods and services demanded to increase.
d. price level causes the aggregate quantity of goods and services demanded to decrease.

____ 52. *Ceteris paribus,* as the price level falls, a country's real exchange rate
a. and interest rates rise.
b. and interest rates fall.
c. fall and interest rates rise.
d. rise and interest rates fall.

____ 53. A decrease in the price level makes the dollars people hold worth
a. more, so they spend more.
b. more, so they spend less.
c. less, so they spend more.
d. less, so they spend less.

____ 54. People will spend more if real wealth
a. and interest rates rise.
b. rises and interest rates fall.
c. falls and interest rates rise.
d. and interest rates fall.

____ 55. The aggregate quantity of goods demanded decreases if
a. real wealth falls.
b. the interest rate rises.
c. the dollar appreciates.
d. All of the above are correct.

____ 56. When the dollar depreciates, each dollar buys
a. more foreign currency, and so buys more foreign goods.
b. more foreign currency, and so buys fewer foreign goods.
c. less foreign currency, and so buys more foreign goods.
d. less foreign currency, and so buys fewer foreign goods.

____ 57. Suppose a stock market boom makes people feel wealthier. The increase in wealth would cause people to desire
a. increased consumption, which shifts the aggregate demand curve right.
b. increased consumption, which shifts the aggregate demand curve left.
c. decreased consumption, which shifts the aggregate demand curve right.
d. decreased consumption, which shifts the aggregate demand curve left.

____ 58. When taxes decrease, consumption increases as shown by
a. a movement to the right along a given aggregate demand curve.
b. shifting aggregate demand to the right.
c. shifting aggregate supply to the right.
d. None of the above is correct.

____ 59. When taxes decrease, consumption
a. increases, so aggregate demand shifts right.
b. increases, so aggregate supply shifts right.
c. decreases, so aggregate demand shifts left.
d. decreases, so aggregate supply shifts left.

____ 60. Which of the following shifts aggregate demand to the left?
a. an increase in the price level
b. a decrease in the money supply
c. an increase in net exports
d. an investment tax credit

____ 61. When the government spends more, the initial effect is that
a. aggregate demand shifts right.
b. aggregate demand shifts left.
c. aggregate supply shifts right.
d. aggregate supply shifts left.
e. a movement along the aggregate demand curve occurs.

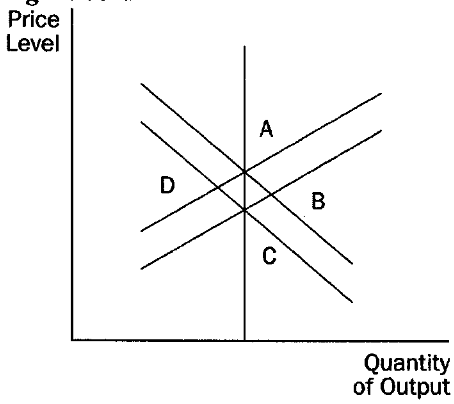
____ 62. If people want to save more for retirement
a. or if the government raises taxes, aggregate demand shifts right.
b. or if the government raises taxes, aggregate demand shifts left.
c. aggregate demand shifts right. If the government raises taxes, aggregate demand shifts left.
d. aggregate demand shifts left. If the government raises taxes, aggregate demand shifts right.
e. None of the above are correct.

____ 63. The aggregate supply curve is vertical in
a. the short and long run.
b. neither the short nor long run.
c. the long run, but not the short run.
d. the short run, but not the long run.

____ 64. The long-run aggregate supply curve shifts right if
a. immigration from abroad increases.
b. the capital stock increases.
c. technology advances.
d. All of the above are correct.

Consider the exhibit below for the following questions.

Figure 33-1



____ 65. **Refer to Figure 33-1**. An increase in the money supply would move the economy from C to
a. B in the short run and the long run.
b. D in the short run and the long run.
c. B in the short run and A in the long run.
d. D in the short run and C in the long run.

____ 66. **Refer to Figure 33-1**. An increase the money supply would move the economy from C to
a. A in the long run.
b. B in the long run.
c. return to C in the long run.
d. D in the long run.

____ 67. **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
a. stays at A.
b. moves to B.
c. moves to C.
d. moves to D.

____ 68. **Refer to Figure 33-1**. If the economy starts at A and there is a fall in aggregate demand, the economy moves
a. back to A in the long run.
b. to B in the long run.
c. to C in the long run.
d. to D in the long run.

____ 69. **Refer to Figure 33-1**. If the economy starts at A and moves to D, the economy moves
a. to A in the long run.
b. to B in the long run.
c. to C in the long run.
d. back to D in the long run.

____ 70. **Refer to Figure 33-1**. The economy would be moving to long-run equilibrium if it started at
a. A and moved to B.
b. C and moved to B.
c. D and moved to C.
d. None of the above is correct.

____ 71. **Refer to Figure 33-1**. An adverse shift in aggregate supply would move the economy from
a. A to B.
b. C to D.
c. B to A.
d. D to C.

____ 72. **Refer to Figure 33-1**. In the short run, a favourable shift in aggregate supply would move the economy from
a. A to B.
b. B to C.
c. C to D.
d. D to A.

____ 73. Which of the following reasons for the downward slope of the aggregate demand curve would likely be more important for a small closed economy?
a. the wealth effect
b. the interest-rate effect
c. the exchange-rate effect
d. the real-wage effect
e. the Ricardian equivalence effect.

____ 74. Liquidity preference refers directly to Keynes' theory concerning
a. the effects of changes in money demand and supply on interest rates.
b. the effects of changes in money demand and supply on exchange rates.
c. the effects of wealth on expenditures.
d. the difference between temporary and permanent changes in income.
e. None of the above are correct.

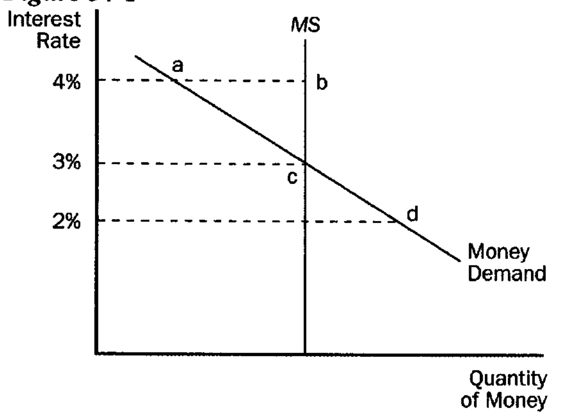
____ 75. If expected inflation is constant, then when the nominal interest rate increases, the real interest rate
a. increases by more than the change in the nominal interest rate.
b. increases by the change in the nominal interest rate.
c. decreases by the change in the nominal interest rate.
d. decreases by more than the change in the nominal interest rate.
e. It is impossible to predict what will happen to the real interest rate.

____ 76. According to liquidity preference theory, the money supply curve would shift if Bank of Canada
a. engaged in open-market transactions.
b. changed the bank rate.
c. changed the reserve requirement.
d. did any of the above.

____ 77. The opportunity cost of holding money
a. decreases when the interest rate increases, so people desire to hold more of it.
b. decreases when the interest rate increases, so people desire to hold less of it.
c. increases when the interest rate increases, so people desire to hold more of it.
d. increases when the interest rate increases, so people desire to hold less of it.

For the following questions, consult the diagram below:

Figure 34-1



____ 78. **Refer to Figure 34-1.** If the current interest rate is 2 percent,
a. there is excess money supply.
b. people will sell more bonds, which drives interest rates up.
c. as the money market moves to equilibrium, people will buy more goods.
d. All of the above are correct.

____ 79. **Refer to Figure 34-1.** There is excess money demand at an interest rate of
a. 2 percent.
b. 3 percent.
c. 4 percent.
d. None of the above are correct.

____ 80. **Refer to Figure 34-1.** At an interest rate of 4 percent there is excess
a. money demand equal to the distance between a and b.
b. money demand equal to the distance between b and c.
c. money supply equal to the distance between b and a.
d. money supply equal to the distance between c and b.

____ 81. **Refer to Figure 34-1.** Which of the following is correct?
a. If the interest rate is 4 percent, there is excess money demand, and the interest rate will fall.
b. If the interest rate is 3 percent, there is excess money supply, and the interest rate will rise.
c. If the interest rate is 4 percent, the demand for goods will rise when the money market is in its new equilibrium.
d. None of the above is correct.

____ 82. The effects of the interest rate in the short run are usually best shown using
a. either liquidity preference theory or classical theory.
b. neither liquidity preference theory or classical theory.
c. only liquidity preference theory.
d. only classical theory.

____ 83. According to liquidity preference theory, an increase in the price level shifts the
   a. money demand curve right so the interest rate increases.
   b. money demand curve right so the interest rate decreases.
   c. money demand curve left so the interest rate decreases.
   d. money demand curve left so the interest rate increases.

____ 84. Which of the following shifts aggregate demand right?
   a. The price level rises.
   b. The price level falls.
   c. The money supply falls.
   d. None of the above is correct.

____ 85. Assume that the *MPC* is 0.80. The multiplier is
   a. .20
   b. .25
   c. 5.
   d. 8
   e. None of the above are correct.

____ 86. Assuming multiplier but no crowding-out or investment-accelerator effects, a $300 billion increase in government expenditures shifts aggregate
   a. demand right by more than $300 billion.
   b. demand right by less than $300 billion.
   c. demand right by exactly $300 billion
   d. supply left by more than $300 billion.
   e. supply left by less than $300 billion.

____ 87. If the Bank of Canada allows the exchange rate to vary freely, an expansionary fiscal policy
   a. causes a large and permanent rightward shift of the AD curve.
   b. causes a large and permanent leftward shift of the AD curve.
   c. has no permanent effect on the position of the AD curve, but causes interest rates to permanently increase.
   d. has no permanent effect on either the position of the AD curve or the interest rate.

____ 88. When the government reduces taxes, which of the following decreases?
   a. consumption
   b. take-home pay
   c. household saving
   d. None of the above is correct.

____ 89. In the long run,
   a. the natural rate of unemployment depends primarily on the level of aggregate demand.
   b. inflation depends primarily upon the money supply growth rate.
   c. there is a tradeoff between the inflation rate and the natural rate of unemployment.
   d. All of the above are correct.

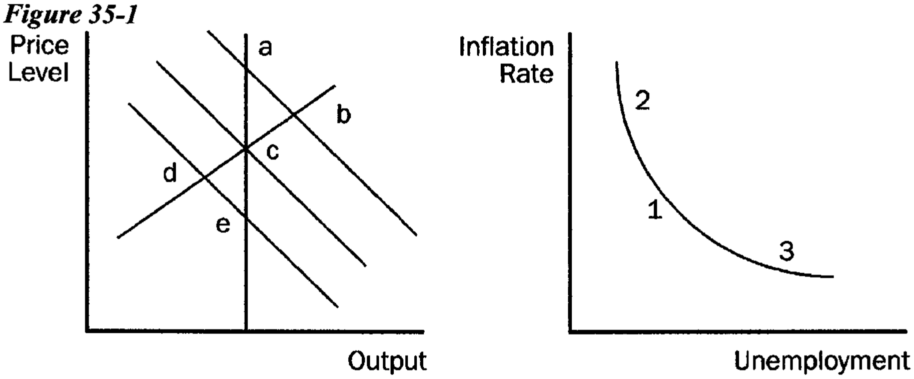
____ 90. If policymakers expand aggregate demand, inflation
   a. falls, but unemployment rises.
   b. and unemployment fall.
   c. and unemployment rise.
   d. rises, but unemployment falls.

____ 91. Suppose that a central bank increases the money supply. According to the Phillips curve this should make
a. prices, output, and employment rise.
b. prices and output rise, employment fall.
c. prices rise and output and employment fall.
d. prices fall, output, and employment rise.

____ 92. To move to a point on the Phillips curve where unemployment is lower,
a. inflation must fall.
b. the government could cut taxes.
c. the Bank of Canada could decrease the money supply.
d. None of the above is correct.

Use the pair of diagrams below to answer the following questions.

Figure 35-1



____ 93. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, an increase in the money supply growth rate moves the economy to
a. a and 1.
b. b and 2.
c. c and 3.
d. None of the above is correct.

____ 94. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, an increase in government expenditures moves the economy to
a. b and 2.
b. b and 3.
c. d and 3.
d. None of the above is correct.

____ 95. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, a decrease in taxes moves the economy to
a. d and 2.
b. d and 3.
c. back to c and 1.
d. None of the above is correct.

____ 96. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, a decrease in aggregate demand moves the economy to
a. a and 2.
b. d and 3.
c. e and 3.
d. None of the above is correct.

____ 97. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, a decrease in the money supply growth rate moves the economy to
a. e and 1.
b. d and 2.
c. d and 3.
d. None of the above is correct.

____ 98. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, a decrease in government expenditures moves the economy to
a. d and 2
b. d and 3.
c. e and 3.
d. None of the above is correct.

____ 99. **Refer to Figure 35-1**. If the economy starts at c and 1, then in the short run, an increase in taxes moves the economy to
a. b and 2.
b. d and 3.
c. e and 2.
d. None of the above is correct.

____ 100. In the long run, 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. All of the above are correct.