

Instructions: Please fill in your name and student number on every page of the exam questionnaire and on the NCS sheet. Use the NCS sheet to answer the Multiple Choice questions. This exam has 10 pages—check that this copy has all of them. Good luck!

Multiple-Choice Questions (82 points—2 points per question)

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

1. If GDP rises,
 - a. **income and expenditure must both rise.**
 - b. income and expenditure must both fall.
 - c. income must rise, but expenditure may rise or fall.
 - d. expenditure must rise, but income may rise or fall.

2. To compute GDP we
 - a. simply sum the number of final goods and services.
 - b. sum the cost of producing final goods and services.
 - c. use weights determined by a survey regarding how much people value different sorts of goods and services to compute GDP as a weighted average.
 - d. **sum the market values of final goods and services.**

3. Over time people have come to rely more on market-produced goods and less on goods that they produce for themselves. For example people eat at restaurants relatively more and prepare their own meals at home relatively less. By itself this change would
 - a. make GDP fall over time.
 - b. not make any change in GDP over time.
 - c. **make GDP rise over time.**
 - d. change GDP, but in an uncertain direction.

4. In computing GDP, investment is spending on
 - a. stocks, bonds, and other financial assets.
 - b. real estate and financial assets.
 - c. **new capital equipment, inventories, and structures, including new housing.**
 - d. capital equipment, inventories, and structures, excluding household purchases of new housing.

5. A firm produces consumer goods and adds some to inventory in the third quarter. In the fourth quarter the firm sells the goods at a retail outlet which leaves their inventory diminished. As a result of these actions, what component(s) of real GDP change in the fourth quarter?
 - a. only investment and it decreases.
 - b. only consumption and it increases.
 - c. Investment decreases and consumption increases.
 - d. **None of the above is correct.**

6. Welfare payments are
 - a. included in GDP because they represent payment for work performed in the past.
 - b. included in GDP because they represent potential consumption.
 - c. **excluded from GDP because they do not represent** current government purchases of goods and services.
 - d. excluded from GDP because they are not private pensions.

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7. If in a given year an economy has consumption of \$3000, investment of \$2000, government purchases of \$1500, exports of \$500, imports of \$600, taxes of \$1200, transfer payments of \$400, and depreciation of \$300, then GDP will equal
- a. \$6400.
 - b. \$7000.
 - c. \$7600.
 - d. \$8900.
 - e. \$9500.
8. Suppose that Nova Scotia produces cheese and fish. In 2002, 20 units of cheese are sold at \$5 each, and 8 units of fish are sold at \$50 each. In 2001, the base year, the price of cheese was \$10 per unit, and the price of fish was \$75 per unit.
- a. Nominal 2002 GDP is \$800, real 2002 GDP is \$500, and the GDP deflator is 160.
 - b. Nominal 2002 GDP is \$500, real 2002 GDP is \$800, and the GDP deflator is 160.
 - c. Nominal 2002 GDP is \$500, real 2002 GDP is \$800, and the GDP deflator is 62.5.
 - d. Nominal 2002 GDP is \$800, real 2002 GDP is \$500, and the GDP deflator is 62.5.
9. If a small country has current nominal GDP of \$25 billion and the GDP deflator is 125, what is real GDP?
- a. \$312.5 billion
 - b. \$207.5 billion
 - c. \$31.25 billion
 - d. \$20 billion
10. If a country reported a nominal GDP of 85 billion in 2002 and 100 billion in 2001 and reported a GDP deflator of 100 in 2002 and of 105 in 2001, then from 2001 to 2002 real output
- a. and prices both rose. 850 m
 - b. rose and prices fell.
 - c. fell and prices rose. 952 m
 - d. and prices both fell.
11. The term "inflation" is used to describe a situation in which
- a. the overall level of prices in the economy is increasing.
 - b. incomes in the economy are increasing.
 - c. stock-market prices are rising.
 - d. the economy is growing rapidly.
12. What is the basket of goods used to construct the CPI?
- a. a random sample of all goods and services produced in the economy
 - b. the goods and services typically bought by consumers, according to Statistics Canada surveys
 - c. goods and services weighted by the ratio of expenditures on them relative to the consumption component of GDP
 - d. the least and the most expensive goods and services in each major category of consumer expenditures

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13. In 2015, OPEC succeeds in raising world oil prices by 300 percent. This price increase causes inventors to look at alternative sources of fuel for internal-combustion engines. A hydrogen-powered engine is developed which is cheaper to operate than gasoline engines. Which problem in the construction of the CPI does this situation represent?
- substitution bias and introduction of new goods
 - introduction of new goods and unmeasured quality change
 - unmeasured quality change and new goods.
 - income bias and substitution bias
14. If the prices of Australian-made shoes imported into Canada increase,
- both the GDP deflator and the consumer price index will increase.
 - neither the GDP deflator nor the consumer price index will increase.
 - the GDP deflator will increase but the consumer price index will not increase.
 - the consumer price index will increase, but the GDP deflator will not increase.
15. You know that a candy bar cost five cents in 1962. You also know the CPI for 1962 and the CPI for today. Which of the following would you use to compute the price of the candy bar in today's prices?
- five cents \times (1962 CPI/ today's CPI)
 - five cents \times (1962 CPI/(today's CPI - 1962 CPI))
 - five cents \times (today's CPI/1962 CPI)
 - five cents \times today's CPI - five cents \times 1962 CPI.
16. Indexation refers to:
- a process of adjusting the nominal interest rate so that it is equal to the real interest rate.
 - using a law or contract to automatically correct a dollar amount for the effects of inflation.
 - using a price index to deflate dollar values.
 - an adjustment made by Statistics Canada to the CPI so that the index is in line with the GDP deflator.
17. If the nominal interest rate is 10 percent, the tax rate on interest income is 30 percent and the expected inflation rate is 4 percent then after a year a person will be left with
- 10 percent more dollars which will purchase 6 percent more goods.
 - 10 percent more dollars which will purchase 3 percent more goods.
 - 7 percent more dollars which will purchase 6 percent more goods.
 - 7 percent more dollars which will purchase 3 percent more goods.
 - 6 percent more dollars which will purchase 6 percent more goods.
18. Ms. Smith borrowed \$1000 from her bank for one year at an interest rate of 10 percent per year. During that year the price level went up by 15 percent. Which of the following statements is correct?
- Ms. Smith will repay the bank fewer dollars than she initially borrowed.
 - Ms. Smith's repayment will give the bank less purchasing power than it originally loaned her.
 - Ms. Smith's repayment will give the bank greater purchasing power than it originally loaned her.
 - Ms. Smith's repayment will give the bank the same purchasing power that it originally loaned her.

19. Which of the following is true?
- Although levels of real GDP per person vary substantially from country to country, the growth rate of real GDP per person is similar across countries.
 - Productivity is not closely linked to government policies.
 - The level of real GDP per person is a good gauge of economic prosperity, and the growth rate of real GDP per person is a good gauge of economic progress.
 - Productivity may be measured by the growth rate of real GDP per person.
20. The average amount of goods and services produced from each hour of a worker's time is called
- per capita GDP
 - per capita GNP
 - productivity
 - human capital
21. Which of the following is correct?
- Countries with the highest growth rates over the last 100 years are the ones that had the highest level of real GDP 100 years ago.
 - Most countries have had little fluctuation around their average growth rates during the past 100 years.
 - The ranking of countries by income changes substantially over time.
 - Over the last 100 years, Japan had the highest real GDP growth rate, and now has the highest real GDP per person.
22. In 2002 real GDP in Oceania was 561.0 billion and the population was 2.2 million. In 2001 real GDP was 500.0 billion and the population was 2.0 million. What was the approximate growth rate of real GDP per person?
- 12 percent
 - 10 percent
 - 4 percent
 - 2 percent
23. Which of the following would not be considered physical capital?
- a new factory building
 - a computer used to help Mercury Delivery Service keep track of their orders
 - on-the-job training
 - a desk used in an accountant's office
24. The behaviour of market prices over time show that natural resources
- are a limit to economic growth.
 - are unrelated to economic growth.
 - are not a limit to economic growth.
 - are the major determinant of productivity.
25. Suppose that real GDP grew more in Country A than in Country B last year.
- Country A must have a higher standard of living than country B.
 - Country A's productivity must have grown faster than country B's.
 - Both of the above are correct.
 - None of the above are correct.

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26. Across countries, investment and growth rates are
- negatively related.
 - positively related.
 - negatively related for rich countries, but positively related for poor countries.
 - positively related for rich countries, but negatively related for poor countries.
27. Real GDP per person is \$21,000 in Aquilonia, \$15,000 in Nemedra and \$6,000 in Shem. Saving per person is \$2,000 in all three countries. Other things equal, we would expect that
- all three countries will grow at the same rate.
 - Aquilonia will grow the fastest.
 - Nemedra will grow the fastest.
 - Shem will grow the fastest.
28. Investment from abroad
- is a way for poor countries to learn the state-of-the-art technologies developed and used in richer countries.
 - is viewed by economists as a way to increase growth.
 - often requires removing restrictions that governments have imposed on foreign ownership of domestic capital.
 - All of the above are correct.
29. The President of a developing country proposes that his country needs to help domestic firms by imposing trade restrictions.
- These are outward-oriented policies and most economists believe they would have beneficial effects on growth.
 - These are outward-oriented policies and most economists believe they would have adverse effects on growth.
 - These are inward-oriented policies and most economists believe they would have beneficial effects on growth.
 - These are inward-oriented policies and most economists believe they would have adverse effects on growth.
30. Senator Noitall says that in order to help poor countries develop, Canada should: 1. Prevent Canadian corporations from investing in poor countries because they take profits that the poor countries should have; 2. Not import goods from poor countries that use child labour; 3. Work to promote political stability in poor countries; and 4. Reduce poor countries' reliance on market forces in their economies. How many of these ideas are likely to help poor countries grow?
- 1
 - 2
 - 3
 - 4
31. Which of the following people purchased the correct asset to meet their objective?
- Michelle wanted to be a part owner of Mamma Rosa's Pizza, so she purchased a bond issued by Mamma Rosa's Pizza.
 - Tim wanted a high return, even if it meant taking some risk, so he purchased stock issued by Specific Electric instead of bonds issued by Specific Electric.
 - Jennifer wanted to buy equity in Honda, so she purchased bonds sold by Honda.
 - All of the above are correct.

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32. Which of the following is a financial intermediary?
- a. a mutual fund
 - b. the stock market
 - c. a U.S. government bond
 - d. None of the above are correct.
33. In a closed economy, national saving equals
- a. investment.
 - b. income minus the sum of consumption and government expenditures.
 - c. private saving plus public saving.
 - d. All of the above are correct.
34. The country of Nemedra does not trade with any other country. Its GDP is \$20 billion. Its government collects \$4 billion in taxes and pays out \$3 billion to households in the form of transfer payments. Consumption equals \$15 billion and investment equals \$2 billion. What is public saving in Nemedra, and what is the value of the goods and services purchased by the government of Nemedra?
- a. -\$2 billion and \$3 billion
 - b. \$1 billion and \$3 billion
 - c. -\$1 billion and \$4 billion
 - d. There is not enough information to answer the question.
35. The Eye of Horus incense company has \$10 million in cash which it has accumulated from retained earnings. It was planning to use the money to build a new factory. Recently, the rate of interest has increased. The increase in the rate of interest should
- a. not influence the decision to build the factory because The Eye of Horus doesn't have to borrow any money.
 - b. not influence the decision to build the factory because its stockholders are expecting a new factory.
 - c. make it more likely that The Eye of Horus will build the factory because a higher interest rate will make the factory more valuable.
 - d. make it less likely that The Eye of Horus will build the factory because the opportunity cost of the \$10 million is now higher.
36. The slope of the supply of loanable funds curve represents the
- a. positive relation between the real interest rate and investment.
 - b. positive relation between the real interest rate and saving.
 - c. negative relation between the real interest rate and investment.
 - d. negative relation between the real interest rate and saving.
37. In 1995, MP Bill Gatt proposed that the income tax be replaced with a consumption tax. If his program had been passed, then today it is likely that the equilibrium interest rate
- a. and quantity of loanable funds would be lower.
 - b. and quantity of loanable funds would be higher.
 - c. would be higher and the equilibrium quantity of loanable funds would be lower.
 - d. would be lower and the equilibrium quantity of loanable funds would be higher.

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38. If the government currently has a budget deficit,
- it does not necessarily have a debt.
 - the debt is increasing.
 - government expenditures are greater than taxes.
 - All of the above are correct.
39. Other things the same, a government budget deficit
- increases both private saving and national saving.
 - increases public saving but reduces national saving.
 - reduces both public and national saving.
 - reduces private saving, but increases national saving.
40. Which of the following is incorrect?
- If GDP is rising faster than debt, the government is, in some sense, living within its means.
 - The ratio of debt to GDP in Canada has always been less than one.
 - Debts during wars may distribute the burden of fighting the war more evenly across generations.
 - All of the above
41. All other things equal, what is the impact of a sudden increase in interest rates on the price of (existing) bonds and stocks?
- Both the price of bonds and the price of stocks increase.
 - The price of bonds increases and the price of stocks decreases.
 - The price of bonds decreases and the price of stocks increases.
 - Both the price of bonds and the price of stocks decrease.

Short-Answer Questions (18 points)
Answer in the space provided.

42. (4 points) In a simple economy, people produce and consume only two goods, food and clothing. Assume the base year for the GDP deflator and the CPI is 2008. Show your calculations in answering the questions below.

| | Year 2008 | | | Year 2009 | | |
|----------|-----------|-------------------------|----------------------------------|-----------|-------------------------|----------------------------------|
| | Price | Production (# of units) | Average Consumption (# of units) | Price | Production (# of units) | Average Consumption (# of units) |
| Food | \$4 | 150 | 50 | \$5 | 100 | 50 |
| Clothing | \$10 | 0 | 30 | \$12 | 20 | 30 |

a. What is nominal GDP for 2009?

$$\begin{array}{r} 200 \\ 300 \\ \hline 500 \end{array}$$

$$\begin{array}{r} 500 \\ 260 \\ \hline 760 \end{array}$$

$$\begin{array}{r} 200 \\ 390 \\ \hline 640 \end{array}$$

f

$$\$500 + \$260 = \$760$$

b. What is real GDP for 2009?

f

$$\$100 + \$200 = \$600$$

c. What is the CPI for 2009?

f

$$\begin{array}{l} 2009 \text{ basket} \rightarrow (640) \\ 2008 \text{ basket} \rightarrow (500) \end{array} \times 100 = 128$$

d. What is the CPI inflation rate for 2009?

f

$$\left(\frac{128 - 100}{100} \right) \times 100 = 28\%$$

43. (5 points) Answer the questions below about Canada's recent productivity performance. Your answer may be in point form.

- a. What has been Canada's productivity performance in recent years (relative to that of the U.S. for example)?

Canada's productivity performance relative to U.S. is poor. For the following reasons

- Not enough research done in Canada
- Brain drain to U.S. (Canadian moving to U.S. for higher pay)
- Not as much trade agreement.

- b. What are the implications of that in terms of competitiveness and standard of living?

- Canada standard of living does not compare to U.S. std of living
- no innovation thus less investors. → less incentive to invest → lose to other country & U.S.
- in the long-run cannot compete to country with economic growth.
- will eventually seek more investment from abroad in order to compete → may lead to a lot of FDI thus profit leaves Canada.

- b. Provide some elements of explanation for that performance.

- taxes prevent those from getting more income/reward.
- take advantage of free health care, research benefits, education & bring info to foreign countries