

CONCORDIA UNIVERSITY
Department of Economics

ECON 203

MIDTERM EXAMINATION WITH ANSWERS

Multiple Choice Questions (2 marks each).

1. If the MPC is 0.8 and government levies a net tax rate of 0.3 then the MPC out of national income (Y) becomes;
A) **0.56.**
B) 0.24.
C) 0.5.
D) 0.6.
2. Other things constant, if the government imposes a net tax equal to $NT = tY$ we would expect:
A) a movement down and along the aggregate expenditure curve.
B) **a decrease in the slope of the aggregate expenditure curve.**
C) an increase in the slope the aggregate expenditure curve.
D) an upward shift of the aggregate expenditure curve.
3. All of the following would be included in a list of the government's automatic stabilizers except:
A) unemployment compensation.
B) **education opportunity grants for low income households.**
C) personal income taxes.
D) taxes on business income.
4. A government budget deficit is financed mainly by borrowing from the public by:
A) printing money.
B) raising taxes.
C) borrowing overseas.
D) **selling bonds.**
5. If the Canadian economy is producing above its potential income, all of the following are likely to happen except:
A) **production will continue to increase.**
B) there will be a shortage of labour and raw materials.
C) prices will rise.
D) inventories will decline.
6. A \$1 increase in government spending will have a larger impact upon national income than a \$1 cut in taxes since:
A) the government prints the dollar it spends.
B) **not all of a tax cut is spent.**
C) when taxes are cut, so too is government spending.
D) taxes are an injection into the system.

Use the following to answer the next 3 questions:

$$\text{Consumption } C = 25 + 0.8(Y - NT)$$

$$\text{Investment } I = 75$$

$$\text{Government expenditure } G = 70$$

$$\text{Exports } X = 30$$

$$\text{Imports } Z = 0.14Y$$

$$\text{Net taxes } NT = 0.2Y$$

7. The multiplier for this economy:
- A) is 4.
 - B) is 2.**
 - C) is 3.
 - D) is 2.33.
8. The equilibrium level of GDP for this economy is:
- A) \$200.
 - B) \$530.
 - C) \$400.**
 - D) \$415.
9. If government wanted to raise the equilibrium GDP to \$450, it could:
- A) raise G by \$50 and not change NT
 - B) raise G by \$25 and not change NT.**
 - C) raise G by \$30 or reduce NT by \$40.
 - D) raise both G and NT by \$25.
10. All of the following are components of investment except:
- A) increases in plant and equipment.
 - B) inventory expansion.
 - C) residential housing construction.
 - D) purchases of stocks and bonds.**
11. All the following are correct except:
- A) Gross Investment = Net Investment + Depreciation.
 - B) GNP = gross domestic product + net factor income from abroad.
 - C) NDI = GDP - net indirect taxes + capital consumption.**
 - D) aggregate spending = $C + I + G + NX = GDP$.
12. If potential output exceeds short run equilibrium output, eventually:
- A) input prices will rise and output will fall.
 - B) both input prices and output will rise.
 - C) input prices will fall and output will rise.**
 - D) both input prices and output will fall.
13. According to the consumption function, as real disposable income increases:
- A) consumption will rise by the same amount as the increase in disposable income.
 - B) both consumption and saving will rise.**
 - C) consumption falls but saving rises.
 - D) consumption rises but saving falls.
14. If nominal GDP increases by 10 percent from one year to the next but real GDP is unchanged then:
- A) Factor costs have increased by 10 percent but net indirect tax rates have not changed.
 - B) Factor costs have not changed but net indirect tax rates have increased by 10 percent.
 - C) The GDP deflator has increased by 10 percent.
 - D) All the above.**
15. The aggregate supply curve is:
- A) upward sloping because costs of production increase as real output increases.**
 - B) horizontal because producers sell their output at fixed prices.
 - C) downward sloping because lower prices call for higher output to maintain revenues.
 - D) vertical because the economy's output is fixed in the short run.

16. Other things being equal, a reorganization of the OPEC cartel to permit it to increase world oil prices by 70 percent would most likely have which effect?
- A) It would shift the aggregate demand curve right.
 - B) It would shift the aggregate supply curve right.
 - C) It would shift the aggregate supply curve up.**
 - D) It would shift the aggregate demand curve right and the aggregate supply curve up.
17. Intermediate goods are:
- A) partly finished goods.**
 - B) goods in transit.
 - C) goods that can only be used with other goods.
 - D) types of money.
18. A balanced increase in the government's expenditure and tax revenue will:
- A) lead to higher equilibrium GDP.**
 - B) have no effect on equilibrium real GDP.
 - C) reduce equilibrium real GDP.
 - D) have an unpredictable effect on equilibrium real GDP.
19. Government may be able to increase equilibrium real GDP and reduce the unemployment rate by:
- A) increasing government purchases and keeping taxes the same.
 - B) cutting taxes.
 - C) increasing both purchases and taxes by the same amount.
 - D) all of the above.**
20. An inflationary gap is characterized by:
- A) constant prices.
 - B) AD greater than AS at potential real GDP.**
 - C) falling prices.
 - D) amount by which price level should increase to increase the total output level.
21. Empirical evidence for Canada suggests that if actual GDP grows by 2 percent a year and potential GDP grows by 3 percent a year:
- A) the unemployment rate will be unchanged.
 - B) the unemployment rate will fall by 1 percentage point.
 - C) the unemployment rate will rise by ½ of one percentage point.**
 - D) the economy will experience an inflationary gap.
22. Other things equal, serious recessions in Canada's trading partners will:
- A) have no perceptible impact on the Canadian economy.
 - B) cause inflation in the Canadian economy.
 - C) depress real output and employment in the Canadian economy.**
 - D) stimulate real output and employment in the Canadian economy.
23. Double counting can be avoided when computing GDP by:
- A) simply deducting a double-counting factor from the GDP estimates.
 - B) adding the value of only the intermediate (non-final) goods and services produced.
 - C) adding only the value contributed by firms at each stage of production.**
 - D) including the value of all output produced in the economy.

Use the following to answer the next 2 questions:

In the absence of a government sector, household consumption expenditure is as follows:

National Income	Consumption
\$200	\$205

225	225
250	245
275	265
300	285

24. The marginal propensity to consume is:
- A) 0.25.
 - B) 0.75.
 - C) 0.20.
 - D) 0.80.**
25. At the \$200 level of national income:
- A) the marginal propensity to save is $2\frac{1}{2}$ percent.
 - B) dissaving is \$5.**
 - C) the average propensity to save is .20.
 - D) the average propensity to consume is .80.
26. If net exports are positive:
- A) the equilibrium GDP must be greater than potential GDP.
 - B) imports must exceed exports.
 - C) aggregate expenditures are greater at each level of GDP than when net exports are zero or negative.**
 - D) some other component of aggregate expenditures must be negative.
27. According to short run macroeconomic analysis, once an economy attains an aggregate equilibrium:
- A) there will be no unemployment in the economy.
 - B) investment must be zero.
 - C) consumption will be equal to or greater than income.
 - D) there may or may not be unemployment.**
28. All the following statements are correct except:
- A) if double counting is not avoided, the GDP measurement will be too high.
 - B) GDP includes all market and non-market values of goods and services produced during a given time period.**
 - C) since GDP includes only the value of currently produced goods, second-hand transactions are not included in GDP.
 - D) GDP measures the market value of final goods and services produced in a country during a given time period.
29. In an economy without government or international trade (a) the marginal propensity to consume is 0.75, (b) consumption equals income at \$120 billion, and (c) the level of investment is \$40 billion. What is the equilibrium level of income?
- A) \$280 billion.**
 - B) \$320 billion.
 - C) \$262 billion.
 - D) \$198 billion.

Use the following to answer the next 3 questions:

The following information is consumption and investment data for a closed economy. Figures are in billions of dollars.

$$C = 60 + .6Y \quad (6.1)$$

$$I = I_0 = 30 \quad (6.2)$$

30. Refer to equations (6.1) and (6.2). The equilibrium level of income (Y) is:
- A) 360.
 - B) 225.**
 - C) 200.
 - D) 135.
31. Refer to equations (6.1) and (6.2). In equilibrium the level of consumption spending will be:
- A) 170.
 - B) 270.
 - C) 160.
 - D) 195.**
32. Refer to equations (6.1) and (6.2) In equilibrium the level of saving will be:
- A) 30.**
 - B) 26.
 - C) 25.
 - D) 60.
33. Suppose that nominal wages fall and productivity rises in a particular economy. Other things equal, the aggregate:
- A) demand curve will shift leftward.
 - B) supply curve will shift rightward.**
 - C) supply curve will shift leftward.
 - D) expenditures curve will shift downward.
34. The potential output line shows:
- A) that maximum sustainable output that can be produced from the existing set of inputs.**
 - B) the maximum output that can be produced based on existing aggregate demand.
 - C) the maximum sustainable output that can be produced at the current price level.
 - D) the maximum output that can be produced when markets are quantity adjusting.
35. For firms in the economy, a build-up of unwanted inventories:
- A) means that consumers are saving more than businesses want to invest.**
 - B) never occurs in a closed, private economy.
 - C) indicates a lack of confidence by consumers.
 - D) will result in the level of income rising.
36. In the economy of Outlandia nominal GDP grew by 8% last year and the GDP deflator increased from 130 to 136.5. As a result:
- A) real GDP declined by 1.5%.
 - B) real GDP increased by 14.5%.
 - C) real GDP was unchanged.
 - D) real GDP increased by 3%.**
37. Planned investment equals planned saving:
- A) at all levels of GDP.
 - B) at all below-equilibrium levels of GDP.
 - C) at all above-equilibrium levels of GDP.
 - D) only at the equilibrium GDP.**
38. If the MPC for the closed economy with no government is 0.8, the:
- A) MPS is $1/0.8$.
 - B) the multiplier is 5.**
 - C) the multiplier is 8.
 - D) the MPS is 0.4.
39. If the structural budget balance is deficit of about \$100 billion and the actual budget balance is a deficit of about \$150 billion, it can be concluded that there is:
- A) built-in stability.

- B) **a increased deficit caused by a recession.**
 C) an expansionary fiscal policy.
 D) a contractionary fiscal policy.
40. If the slope of the AE function is 0.75 and investment increases by \$3 billion, the equilibrium GDP will:
- A) increase by about \$10 billion.
 B) increase by \$3 billion.
 C) decrease by \$9 billion.
 D) **increase by \$12 billion.**
41. The interest-rate effect suggests that:
- A) a decrease in the supply of money will increase interest rates and reduce interest-sensitive consumption and investment spending.
 B) an increase in the price level will increase the demand for money, reduce interest rates, and decrease consumption and investment spending.
 C) **an increase in the price level will increase the demand for money, increase interest rates, and decrease consumption and investment spending.**
 D) an increase in the price level will decrease the demand for money, reduce interest rates, and increase consumption and investment spending.
42. Which one of the following would not shift the aggregate demand curve?
- A) **a change in the price level.**
 B) depreciation of the international value of the dollar.
 C) a decline in the interest rate at each possible price level.
 D) an increase in personal income tax rates.
43. The numerical value of the multiplier will be smaller the:
- A) higher the level of the AE function.
 B) **larger the slope of the saving function.**
 C) larger the slope of the AE function.
 D) smaller the slope of the AE function.
44. The increase in equilibrium income which results from an increase in investment spending would be greater the:
- A) **smaller the MPS.**
 B) larger the MPZ.
 C) larger the MPS.
 D) smaller the MPC
45. An effective expansionary fiscal policy will:
- A) reduce a cyclical deficit, but necessarily increase the total (actual) deficit.
 B) reduce a structural deficit.
 C) **increase the structural deficit but reduce the cyclical deficit.**
 D) always result in a balanced budget once full-employment is achieved.
46. The CPI in year one was 145. The CPI in year two was 151. The rate of inflation between years one and two was _____ percent.
- A) 4.0
 B) **4.1**
 C) 4.5
 D) 5.1
47. Assume the slope of the AE function is $\frac{2}{3}$. If investment spending increases by \$2 billion, the equilibrium level of GDP will increase by:

- A) \$3 billion.
 - B) \$2/3 billion.
 - C) \$6 billion.**
 - D) \$2 billion.
48. If the slope of the AE function was 0.8, from the MPC, before taxes, and government introduced net taxes $NT = 0.2Y$, the slope of AE would be:
- A) 1.0.
 - B) 0.6.
 - C) 0.64.**
 - D) 1.6.
49. If the labour force in Utopia grows by 7 per cent and employment grows by 5 percent unemployment rate will:
- A) increase by about 2 percent.**
 - B) remain unchanged.
 - C) fall by about 2 percent.
 - D) rise by about 12 percent.
50. The simple circular flow model shows that:
- A) firms hire the factors from households and produce the output consumed by households.
 - B) households provide the factors to firms and buy the output produced by firms.
 - C) the source of household income is the producing sector and the source of firms' revenue is household spending.
 - D) all of the above are correct.**