

MACROECONOMICS

Section I

Time—70 minutes

60 Questions

Directions: Each of the questions or incomplete statements below is followed by five suggested answers or completions. Select the one that is best in each case and then fill in the corresponding circle on the answer sheet.

1. A country's government runs a budget deficit when which of the following occurs in a given year?
 - (A) The amount of new loans to developing nations exceeds the amount of loans paid off by developing nations.
 - (B) Government spending exceeds tax revenues.
 - (C) The debt owed to foreigners exceeds the debt owed to the country's citizens.
 - (D) The amount borrowed exceeds the interest payment on the national debt.
 - (E) Interest payments on the national debt exceed spending on goods and services.
2. A high marginal propensity to consume implies which of the following?
 - (A) A small change in consumption when income changes
 - (B) A high savings rate
 - (C) A high marginal tax rate
 - (D) An equilibrium level of income near full employment
 - (E) A low marginal propensity to save
3. The transaction demand for money is very closely associated with money's use as a
 - (A) store of value
 - (B) standard unit of account
 - (C) measure of value
 - (D) medium of exchange
 - (E) standard of deferred payment
4. Unlike a market economy, a command economy uses
 - (A) more centralized planning in economic decision making
 - (B) consumer sovereignty to make production decisions
 - (C) its resources more efficiently
 - (D) price signals in economic decision making
 - (E) the popular vote in making resource allocation decisions
5. The value of a country's currency will tend to appreciate if
 - (A) demand for the country's exports increases
 - (B) the country's money supply increases
 - (C) the country's citizens increase their travel abroad
 - (D) domestic interest rates decrease
 - (E) tariffs on the country's imports decrease
6. Which of the following best illustrates an improvement in a country's standard of living?
 - (A) An increase in real per capita gross domestic product
 - (B) An increase in nominal per capita gross domestic product
 - (C) Price stability
 - (D) A balanced budget
 - (E) An increase in the consumer price index

7. Hyperinflation is typically caused by
- (A) high tax rates that discourage work effort
 - (B) continuous expansion of the money supply to finance government budget deficits
 - (C) trade surpluses that are caused by strong protectionist policies
 - (D) bad harvests that lead to widespread shortages
 - (E) a large decline in corporate profits that leads to a decrease in production
8. All of the following changes will shift the investment demand curve to the right EXCEPT
- (A) a decrease in the corporate income tax rate
 - (B) an increase in the productivity of new capital goods
 - (C) an increase in the real interest rate
 - (D) an increase in corporate profits
 - (E) an increase in real gross domestic product
9. The official unemployment rate understates the unemployment level in the economy because the official unemployment rate
- (A) ignores the duration of unemployment
 - (B) ignores underemployed and discouraged workers
 - (C) includes jobs created by the underground economy
 - (D) excludes all unemployed teenagers
 - (E) excludes frictionally unemployed workers
10. If a reduction in aggregate supply is followed by an increase in aggregate demand, which of the following will definitely occur?
- (A) Output will increase.
 - (B) Output will decrease.
 - (C) Output will not change.
 - (D) The price level will increase.
 - (E) The price level will decrease.
11. Which of the following combinations of changes in government spending and taxes is necessarily expansionary?
- | <u>Government
Spending</u> | <u>Taxes</u> |
|--------------------------------|--------------|
| (A) Increase | Increase |
| (B) Increase | Decrease |
| (C) Decrease | Not change |
| (D) Decrease | Increase |
| (E) Decrease | Decrease |
12. The amount of money that the public wants to hold in the form of cash will
- (A) be unaffected by any change in interest rates or the price level
 - (B) increase if interest rates increase
 - (C) decrease if interest rates increase
 - (D) increase if the price level decreases
 - (E) decrease if the price level remains constant
13. For an economy consisting of households and businesses only, which of the following is consistent with the circular flow of income and production?
- (A) Households are producers of goods and services and consumers of resources.
 - (B) Households are users of resources, and businesses are sources of saving.
 - (C) Households are suppliers of resources and consumers of goods and services.
 - (D) Businesses are users of taxes, and households are sources of taxes.
 - (E) Businesses are suppliers of resources and consumers of goods and services.
14. With an increase in the real interest rate, consumption and real gross domestic product will most likely change in which of the following ways?
- | <u>Consumption</u> | <u>Real Gross
Domestic Product</u> |
|--------------------|--|
| (A) Increase | Increase |
| (B) Increase | Decrease |
| (C) Decrease | Increase |
| (D) Decrease | Decrease |
| (E) No change | Increase |

15. According to the short-run Phillips curve, lower inflation rates are associated with

- (A) higher unemployment rates
- (B) higher government spending
- (C) larger budget deficits
- (D) greater labor-force participation rates
- (E) smaller labor-force participation rates

16. Which of the following will lead to a decrease in a nation's money supply?

- (A) A decrease in income tax rates
- (B) A decrease in the discount rate
- (C) An open market purchase of government securities by the central bank
- (D) An increase in reserve requirements
- (E) An increase in government expenditures on goods and services

17. An increase in which of the following would cause the aggregate demand curve to shift to the left?

- (A) Consumer optimism
- (B) Population
- (C) Cost of resources
- (D) Income taxes
- (E) Net exports

18. Which of the following changes in the supply of and the demand for a good will definitely result in a decrease in both the equilibrium price and quantity of the good?

<u>Supply</u>	<u>Demand</u>
(A) Increase	Increase
(B) Increase	No change
(C) No change	Decrease
(D) Decrease	Increase
(E) Decrease	Decrease

BANK A

<u>Assets</u>		<u>Liabilities</u>	
Actual reserves	\$1,000	Demand deposits	\$5,000
Loans	\$4,000		

BANK B

<u>Assets</u>		<u>Liabilities</u>	
Actual reserves	\$ 100	Demand deposits	\$ 600
Loans	\$ 500		

BANK C

<u>Assets</u>		<u>Liabilities</u>	
Actual reserves	\$ 10	Demand deposits	\$ 100
Loans	\$ 90		

19. Based on the balance sheets above for three different banks, which of the following is true, if the reserve requirement is 10 percent?
- (A) Bank A has no excess reserves.
 - (B) Bank B has no excess reserves.
 - (C) Bank B can increase its loans by \$500.
 - (D) Bank B can increase its loans by \$40.
 - (E) Bank C has excess reserves.

20. Which of the following will most likely lead to a decrease in inflationary expectations?
- (A) A decrease in the marginal propensity to save
 - (B) A decrease in imports
 - (C) A decrease in the money supply
 - (D) An increase in the government budget deficit
 - (E) An increase in the prices of raw materials

21. With an upward-sloping short-run aggregate supply curve, an increase in government expenditure will most likely
- (A) reduce the price level
 - (B) reduce the level of nominal gross domestic product
 - (C) increase real gross domestic product
 - (D) shift the short-run aggregate supply curve to the right
 - (E) shift both the aggregate demand curve and the long-run aggregate supply curve to the left

22. Which of the following are the most likely short-run effects of an increase in government expenditures?

<u>Unemployment Rate</u>	<u>Inflation Rate</u>	<u>Real Gross Domestic Product</u>
(A) Increase	Increase	Increase
(B) Increase	Increase	Decrease
(C) Decrease	Increase	Increase
(D) Decrease	Decrease	Increase
(E) No change	Decrease	Increase

23. In the short run, an expansionary monetary policy would most likely result in which of the following changes in the price level and real gross domestic product (GDP) ?

<u>Price Level</u>	<u>Real GDP</u>
(A) Decrease	Increase
(B) No change	Decrease
(C) Increase	No change
(D) Increase	Decrease
(E) Increase	Increase

24. A reduction in inflation can best be achieved by which of the following combinations of fiscal and monetary policy?

<u>Fiscal Policy</u>	<u>Monetary Policy</u>
(A) Increase taxes	Sell government bonds
(B) Decrease taxes	Buy government bonds
(C) Decrease taxes	Lower margin requirements
(D) Decrease government spending	Lower discount rate
(E) Increase government spending	Raise discount rate

25. Which of the following is likely to occur following the depreciation of the United States dollar?

- (A) United States imports will increase.
- (B) United States exports will increase.
- (C) Demand for the United States dollar will decrease.
- (D) United States demand for foreign currencies will increase.
- (E) United States goods will become more expensive in foreign markets.

26. The table below shows the production alternatives of Country A and Country B for producing computers and cars with equal amounts of resources that are fully and efficiently employed.

<u>Country</u>	<u>Computers</u>	<u>Cars</u>
A	24	0
	0	12
B	45	0
	0	15

Which of the following is true according to the data in the table?

- (A) Country A has an absolute and comparative advantage in the production of computers.
- (B) Country B has an absolute and comparative advantage in the production of computers.
- (C) Country B should import computers and export cars.
- (D) Since Country B has an absolute advantage in the production of both goods, it will not trade with Country A.
- (E) Neither country can benefit from trade.

27. Which of the following individuals is considered officially unemployed?
- (A) Chris, who has not worked for more than three years and has given up looking for work
 - (B) Kim, who is going to school full-time and is waiting until graduation before looking for a job
 - (C) Pat, who recently left a job to look for a different job in another town
 - (D) Leslie, who retired after turning 65 only five months ago
 - (E) Lee, who is working 20 hours per week and is seeking full-time employment
28. An increase in net investment leads to faster economic growth because capital per worker and output per worker will change in which of the following ways?
- | <u>Capital
per Worker</u> | <u>Output
per Worker</u> |
|-------------------------------|------------------------------|
| (A) Increase | Increase |
| (B) Increase | Decrease |
| (C) No change | Increase |
| (D) Decrease | Increase |
| (E) Decrease | Decrease |
29. If a country's economy is operating below the full-employment level of output at a very low inflation rate, the central bank of the country is most likely to
- (A) pursue an expansionary monetary policy because it is required to do so by law whenever output is below the full-employment level
 - (B) pursue an expansionary fiscal policy because it is required to do so by law whenever output is below the full-employment level
 - (C) lower the discount rate and buy bonds on the open market to generate an increase in output
 - (D) lower the required reserve ratio and sell bonds on the open market to generate an increase in output
 - (E) raise the discount rate and lower the required reserve ratio to generate an increase in output
30. Assume that an economy is currently in long-run equilibrium and the short-run aggregate supply curve is upward sloping. An adverse supply shock, such as a drought, will most likely cause which of the following to the economy in the short run?
- (A) A decrease in the price level and a decrease in the nominal wage
 - (B) A decrease in the price level and an increase in the nominal wage
 - (C) An increase in the price level and an increase in the nominal wage
 - (D) An increase in the price level and an increase in the real wage
 - (E) An increase in the price level and a decrease in the real wage
31. If Country Alpha has been experiencing a higher inflation rate than Country Beta over the past decade, which of the following is true?
- (A) Alpha's currency will have appreciated relative to Beta's currency.
 - (B) Alpha's currency will have depreciated relative to Beta's currency.
 - (C) Alpha will have had lower nominal interest rates than Beta.
 - (D) Alpha will have had slower growth in the money supply than Beta.
 - (E) Alpha's economy will have grown at a faster rate than Beta's.

	National Economic Figures (billions of dollars)
Consumption	\$ 3,000
Government purchases of goods and services	1,000
Gross private domestic investment	700
Depreciation	300
Exports	300
Imports	500
Indirect business taxes	0

32. Based on the economic figures in the table above, what is the value of gross domestic product, in billions of dollars?

- (A) \$4,500
- (B) \$4,700
- (C) \$4,900
- (D) \$5,150
- (E) \$5,950

33. Which of the following best explains the increase in national income that results from equal increases in government spending and taxes?

- (A) Consumers do not reduce their spending by the full amount of the tax increase.
- (B) The government purchases some goods that consumers would have purchased on their own anyway.
- (C) Consumers believe all tax cuts are transitory.
- (D) The increase in government spending causes a decrease in investment.
- (E) Consumers are aware of tax increases but not of increases in government spending.

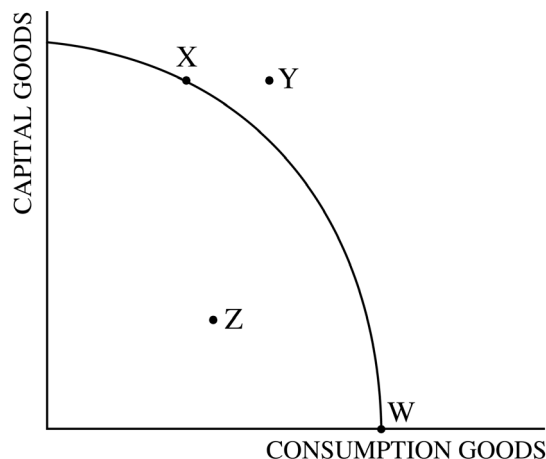
34. Which of the following statements is true of unanticipated inflation?

- (A) It decreases the economic well-being of all members of society proportionately.
- (B) It decreases the economic well-being of all members of society equally.
- (C) It increases the economic well-being of net creditors.
- (D) It increases the economic well-being of net debtors.
- (E) It increases the economic well-being of workers with long-term labor contracts.

35. A simultaneous increase in inflation and unemployment could be explained by an increase in which of the following?

- (A) Consumer spending
- (B) The money supply
- (C) Labor productivity
- (D) Investment spending
- (E) Inflationary expectations

36. A country can have an increased surplus in its balance of trade as a result of
- (A) an increase in domestic inflation
 - (B) declining imports and rising exports
 - (C) higher tariffs imposed by its trading partners
 - (D) an increase in capital inflow
 - (E) an appreciating currency
37. Policies intended to reduce demand-pull inflation are most likely to increase which of the following in the short run?
- (A) Gross domestic product
 - (B) The labor force participation rate
 - (C) The price level
 - (D) Unemployment
 - (E) Wage levels
38. An increase in the government budget deficit is most likely to result in an increase in which of the following?
- (A) The marginal propensity to consume
 - (B) Exports
 - (C) The real interest rate
 - (D) The money supply
 - (E) The simple multiplier
39. An increase in which of the following would be most likely to increase long-run growth?
- (A) Pension payments
 - (B) Unemployment compensations
 - (C) Subsidies to businesses for purchases of capital goods
 - (D) Tariffs on imported capital goods
 - (E) Tariffs on imported oil
40. A commercial bank's ability to create money depends on which of the following?
- (A) The existence of a central bank
 - (B) A fractional reserve banking system
 - (C) Gold or silver reserves backing up the currency
 - (D) A large national debt
 - (E) The existence of both checking accounts and savings accounts
41. The consumer price index (CPI) is designed to measure changes in the
- (A) spending patterns of urban consumers only
 - (B) spending patterns of all consumers
 - (C) wholesale price of manufactured goods
 - (D) prices of all goods and services produced in an economy
 - (E) cost of a select market basket of goods and services
42. A barter economy is different from a money economy in that a barter economy
- (A) encourages specialization and division of labor
 - (B) involves higher costs for each transaction
 - (C) eliminates the need for a double coincidence of wants
 - (D) has only a few assets that serve as a medium of exchange
 - (E) promotes market exchanges
43. In the short run, which of the following would occur to bond prices and interest rates if a central bank bought bonds through open-market operations?
- | <u>Bond Prices</u> | <u>Interest Rates</u> |
|--------------------|-----------------------|
| (A) No change | Increase |
| (B) Increase | Increase |
| (C) Increase | Decrease |
| (D) Decrease | Increase |
| (E) Decrease | Decrease |
44. Suppose that in an economy with lump-sum taxes and no international trade, autonomous investment spending increases by \$2 million. If the marginal propensity to consume is 0.75, equilibrium gross domestic product will change by a maximum of
- (A) \$0.5 million
 - (B) \$1.5 million
 - (C) \$2.0 million
 - (D) \$8.0 million
 - (E) \$15.0 million



45. The diagram above shows the production possibilities curve for an economy that produces only consumption and capital goods. All of the following statements about this economy are true EXCEPT:
- (A) Producing at point Z results in the underutilization of resources.
 - (B) The combination represented by point Y is unattainable, given the scarcity of resources.
 - (C) Resources are fully utilized at points W and X.
 - (D) Producing at point X will result in greater economic growth than will producing at point W.
 - (E) Point X represents the most efficient combination of the two goods that can be produced by this economy.

46. Assume that the required reserve ratio is 10 percent, banks keep no excess reserves, and borrowers deposit all loans made by banks. Suppose you have saved \$100 in cash at home and decide to deposit it in your checking account. As a result of your deposit, the money supply can increase by a maximum of
- (A) \$800
 - (B) \$900
 - (C) \$1,000
 - (D) \$1,100
 - (E) \$1,200
47. Which of the following would be the initial impact on an economy if wages were to increase more than worker productivity?
- (A) There would be no initial impact, since neither the aggregate supply curve nor the aggregate demand curve would shift.
 - (B) Employment would increase, causing a rightward shift in the aggregate demand curve.
 - (C) The price level would increase, resulting in excess aggregate supply.
 - (D) The short-run aggregate supply curve would shift to the left, increasing the price level.
 - (E) The aggregate demand curve would shift to the left, increasing the price level.
48. Under a flexible exchange-rate system, the Indian rupee will appreciate against the Japanese yen when
- (A) India's inflation rate exceeds Japan's
 - (B) India has a trade deficit with Japan
 - (C) Japan's economy enters a recession, but India's does not
 - (D) Japan's money supply decreases while India's money supply increases
 - (E) real interest rates in India increase relative to those in Japan

49. Which of the following occurs as investment becomes more responsive to changes in the interest rate?
- (A) Monetary policy becomes more effective at changing real gross domestic product.
 - (B) Fiscal policy becomes more effective at changing real gross domestic product.
 - (C) Monetary policy becomes more effective at changing interest rates.
 - (D) Fiscal policy becomes more effective at changing interest rates.
 - (E) There is no change in the effectiveness of either monetary or fiscal policy.
50. If two nations specialize according to the law of comparative advantage and then trade with each other, which of the following would be true?
- (A) A smaller number of goods would be available in each trading nation.
 - (B) Total world production of goods would decrease.
 - (C) Everyone within each nation would be better off.
 - (D) Each nation would increase its consumption possibilities.
 - (E) One nation would gain at the expense of the other nation.
51. The shifting of a country's production possibilities curve to the right will most likely cause
- (A) net exports to decline
 - (B) inflation to increase
 - (C) the aggregate demand curve to shift to the left
 - (D) the long-run aggregate supply curve to shift to the left
 - (E) the long-run aggregate supply curve to shift to the right
52. One explanation for the downward slope of the aggregate demand curve is that when the price level increases, which of the following will decrease?
- (A) Real value of assets
 - (B) Prices of foreign goods
 - (C) Prices of substitute goods
 - (D) Expectations of future prices
 - (E) Government deficit
53. Which of the following is true about changes in tax rates, changes in the level of government expenditures, and changes in the money supply?
- (A) They are automatic stabilizers.
 - (B) They are tools of discretionary fiscal policy.
 - (C) They have different lag times between implementation of a policy and its effects on aggregate demand.
 - (D) They are favored equally by both classical and Keynesian economists to fine-tune the economy.
 - (E) All are controlled by the Federal Reserve system.
54. An increase in which of the following would LEAST likely increase labor productivity?
- (A) Physical capital
 - (B) Human capital
 - (C) Technological improvements
 - (D) Educational achievement
 - (E) The labor force
55. Tariffs are different from assigned import quotas in that tariffs will
- (A) restrict imports
 - (B) increase the price of imported goods
 - (C) benefit domestic consumers of imported goods
 - (D) hurt domestic producers of goods facing import competition
 - (E) generate additional revenue for the domestic government

56. In the narrowest definition of money, M1, savings accounts are excluded because they are
- not a medium of exchange
 - not insured by federal deposit insurance
 - available from financial institutions other than banks
 - a store of purchasing power
 - interest-paying accounts
57. For which of the following sets of unemployment and inflation rates will a central bank be most reluctant to increase the rate of growth in the money supply?
- | | <u>Unemployment Rate</u> | <u>Inflation Rate</u> |
|-----|--------------------------|-----------------------|
| (A) | 10% | 2% |
| (B) | 10% | 5% |
| (C) | 10% | 10% |
| (D) | 5% | 5% |
| (E) | 5% | 10% |
58. Assume that Jane's marginal propensity to consume equals 0.8, and that in 2004 Jane spent \$36,000 from her disposable income of \$40,000. If her disposable income in 2005 increased to \$50,000, her consumption spending increased by
- \$4,000
 - \$8,000
 - \$9,000
 - \$10,000
 - \$14,000
59. Advocates of a monetary rule recommend increasing the money supply at a rate that is equal to the rate of increase in which of the following?
- Price level
 - Unemployment rate
 - Level of exports
 - Level of imports
 - Long-run real gross domestic product
60. If economic agents perfectly anticipate policy changes and if all prices, including wages, are completely flexible, which of the following will be true in the long run?
- The price level will be constant.
 - There will be no trade-off between inflation and unemployment.
 - The unemployment rate will be less than the natural rate of unemployment.
 - The unemployment rate will be greater than the natural rate of unemployment.
 - Changes in the money supply will not lead to changes in the price level.

END OF SECTION I

**IF YOU FINISH BEFORE TIME IS CALLED, YOU MAY
CHECK YOUR WORK ON THIS SECTION.**

DO NOT GO ON TO SECTION II UNTIL YOU ARE TOLD TO DO SO.

MAKE SURE YOU HAVE DONE THE FOLLOWING.

- **PLACED YOUR AP NUMBER LABEL ON YOUR ANSWER SHEET**
- **WRITTEN AND GRIDDED YOUR AP NUMBER CORRECTLY ON YOUR ANSWER SHEET**
- **TAKEN THE AP EXAM LABEL FROM THE FRONT OF THIS BOOKLET AND PLACED IT ON YOUR ANSWER SHEET**