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**ECON 212 – Principles of Economics II**

**Problem Set 1**

**LONG QUESTIONS:**

**1)** Suppose that a very simple economy produces only the following three final goods and services: pizzas, clothes, and haircut. Information on population, nominal prices and total output for each good and services in the years 2010 and 2020 is given below.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **2010**  Population: 60 million | | **2020**  Population: 80 million | |
|  | **Per unit price ($)** | **Output (in millions)** | **Per unit price ($)** | **Output (in millions)** |
| **Pizzas** | 4.00 | 10 | 5.00 | 12 |
| **Clothes** | 10.00 | 5 | 12.00 | 5 |
| **Haircut** | 6.00 | 2 | 8.00 | 4 |

1. Calculate nominal GDP for 2010.

Nominal GDP for 2010= ($4+x10 million) +($10x5 million) +($6x2 million) =**102 million $**

**b)** Calculate nominal GDP for 2020.

Nominal GDP for 2020= ($5x12 million) +($12x5 million) +($8x4 million) =**152 million $**

1. Calculate real GDP for 2010 and 2020 if the base year is 2010.

Real GDP for 2010= ($4+x10 million) +($10x5 million) +($6x2 million) =**102 million $**

Real GDP for 2020= ($4+x12 million) +($10x5 million) +($6x4 million) = **122 million $**

1. Calculate the growth rate of real GDP (using 2010 $).

Growth Rate of Real GDP= (122 million-102 million)/102 million=**% 19.6**

1. Has the standard of living increased or decreased since 2010?

**Since Real GDP per capita has decreased, the standard of living has also decreased.**

**2)** What is the difference between the Long Run and Short Run frameworks?

**The short-run is a period of time in which the quantity of at least one input is fixed and the quantities of the other inputs can be varied. The long-run is a period of time in which the quantities of all inputs can be varied.**

**3)** What is unemployment rate?

**The unemployment rate is the percent of the labor force that is unemployed.**

**4)** What is target rate of unemployment?

**The target rate of unemployment is the lowest sustainable rate of unemployment that policymakers believe is achievable.**

**5)** How is the target rate of unemployment related to potential output?

**Potential output is the output that would materialize at the target rate of unemployment and the optimum capacity utilization rate.**

**MULTIPLE CHOICE QUESTIONS:**

**1)** During a business cycle expansion, total production \_\_\_\_\_\_\_\_ and total employment \_\_\_\_\_\_\_\_.**(A)**

**A) increases, increases**

B) decreases, increases

C) increases, decreases

D) decreases, decrease

**2)** Gross domestic product is calculated by summing up **(C)**

A) the total quantity of goods and services in the economy.

B) the total market value of goods and services in the economy.

**C) the total market value of final goods and services produced in the economy during a period of time.**

D) the total quantity of goods and services produced in the economy during a period of time.

**3)** In the circular flow model, the value of total production for an economy \_\_\_\_\_\_\_\_ the value of total**(D)**

expenditures on final goods and services.

A) is greater than

B) is less than

C) may be greater than or less than

**D) equals**

**4)** The purchase by a foreign government of an airplane produced in the United States is included in U.S.**(B)**

A) investment expenditures.

**B) net exports.**

C) government purchases.

D) consumption expenditures.

Consider the table below showing three stages of production of an automobile.

|  |  |  |  |
| --- | --- | --- | --- |
| **Stage of Production** | **Seller** | **Buyer** | **Price** |
| **1** | Steel mill | Auto manufacturer | $12,000 |
| **2** | Auto manufacturer | Auto dealer | $22,000 |
| **3** | Auto dealer | Consumer | $30,000 |

**5)** Refer to table above. The value added by the automobile dealer equals **(A)**

**A) $8,000.**

B) $10,000.

C) $22,000.

D) $30,000.

**6)** Refer to table above. The value of each automobile in gross domestic product equals **(D)**

A) $8,000.

B) $10,000.

C) $22,000.

**D) $30,000.**

**7)** Legalizing all forms of illegal activities**(D)**

A) reduces GDP and the size of the underground economy.

B) increases GDP and increases the size of the underground economy.

C) reduces GDP and increases the size of the underground economy.

**D) increases GDP and reduces the size of the underground economy.**

**8)** Nominal GDP is GDP in a given year **(C)**

A) valued in the prices of the base year.

B) adjusted for anticipated inflation.

**C) valued in the prices of that year.**

D) adjusted for inflation.

**9)** Real GDP is GDP in a given year **(B)**

A) adjusted only for anticipated inflation.

**B) valued in the prices of the base year.**

C) adjusted only for unanticipated inflation.

D) valued in the prices of that year.

**10)** The GDP deflator is a measure of the **(A)**

**A) average level of prices of final goods and services in the economy.**

B) average level of prices of intermediate goods and services in the economy.

C) total production of the economy unadjusted for inflation.

D) total production of the economy adjusted for inflation.

**11)** Which one is the definition of structural unemployment? **(A)**

**A) unemployment caused by the institutional structure of an economy or by economic**

**restructuring making some skills obsolete**

B) unemployment that occurs during recessions and depressions.

C) The percentage of people in the economy who are both able to and looking for work but who

cannot find jobs

D) Unemployment caused by people entering the job market and people quitting a job just long

enough to look for and find another one

**12)** The term business cycle refers to the **(C)**

A) short-term ups and downs in the price level.

B) long-term trends in the price level.

**C) short-term ups and downs in the level of economic activity.**

D) long-term trends in the level of economic activity.

**13)** The labor force equals the number of people **(A)**

**A) employed plus unemployed.**

B) employed.

C) unemployed.

D) in the working-age population.

**14)** Cyclical unemployment is the result of **(D)**

A) the ups and downs in inflation.

B) a persistent mismatch between the skills and characteristics of workers and the

requirements of the jobs.

C) the search process of matching workers with jobs.

**D) a slowdown in the economy.**

**15)** In calculating GDP: **(C)**

A) both exports and imports are added

B) neither exports nor imports are added

**C) exports are added and imports are subtracted**

D) imports are added and exports are subtracted

**16)** What is value added? **(B)**

A) Value added refers to goods that are produced by one firm for use in further processing by

another firm.

**B) Value added is the difference between the value of goods as they leave a stage of production and**

**the cost of the goods as they entered that stage.**

C) Value added is data collected and published by the government describing the various

components of national income and output in the economy.

D) Value added refers to goods and services produced for final use.

**17)** An Italian company opens a pasta company in the U.S. The profits from this pasta company

are included in **(C)**

A) both U.S. and Italian GNP.

B) both U.S. and Italian GDP.

**C) U.S. GDP and Italian GNP.**

D) U.S. GNP and Italian GDP.

**18)** Double counting can be avoided by **(B)**

A) including the value of intermediate goods in the current year.

**B) not counting the value of intermediate goods in GDP.**

C) including the value of intermediate goods in the GNP but not in the GDP.

D) including the value of intermediate goods in the production year but not in the selling

year of those goods.

**19)** Which of the following is included in both the U.S. GDP and GNP? **(B)**

A) The value of all cars produced by Ford in Mexico.

**B) The value of all cars produced by General Motors in the U.S.**

C) The value of all cars produced by Toyota in the U.S.

D) The value of cars produced by Nissan in Japan and the U.S.

**20)** Depreciation is **(C)**

A) the decrease in the overall price level.

B) the additional capital stock in a year.

**C) the amount of used up machinery in a year.**

D) the amount of decline in business inventories.