

Name: _____

Student #: _____

QUEEN'S UNIVERSITY AT KINGSTON

FACULTY OF ARTS AND SCIENCE

Department of Economics

ECONOMICS 110B

Final Examination

Econ 110B Sections 001 & 002 – Prof Ian Cromb

April 19, 2018

INSTRUCTIONS TO STUDENTS:

This examination is 3 HOURS in length.

There are 6 sections to this examination.

This exam is printed on both sides of the page.

Mark your selections in PENCIL on the Answer Sheet. Fill in the appropriate rectangle completely, but stay within its limits. There is only one correct answer for each question; multiple answers will be marked as incorrect. If you make changes, be sure to erase completely.

Before you begin the exam please record your **Student Number, Name, and Test Form A** in the appropriate sections of the Answer Sheet. For detailed instructions on filling in this information see the back of this page.

The following aids are allowed:

Casio FX-991 calculator

PLEASE NOTE:

Proctors are unable to respond to queries about the interpretation of exam questions.

Do your best to answer exam questions as written.

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Before You Begin the Exam:

1. Write your Student # under "**I.D. Number**" on the Answer Sheet and fill in the appropriate rectangle below each number. See example below.
2. Print your **Last Name** followed by first name in the appropriate space, and fill in the appropriate rectangle under each letter. (If your name is too long to fit in the spaces provided, please enter as many letters as you can.) See example below.
3. Under "**Test Form**", fill in "A". See example below.

The image shows a template for a standardized test answer sheet. At the top left is a grid for the "I.D. NUMBER" (Student ID) with rows for numbers 0-9 and columns for digits 0-9. In the center is a large rectangular area with the instruction "DO NOT MARK IN THIS AREA" printed in bold capital letters. To the right of this central area are two vertical columns: "TEST FORM" and "EXAM NUMBER", each containing four options (A, B, C, D or 0, 1, 2, 3). Below the central area is a section for "LAST NAME" and "FIRST NAME", each with a grid of letters A-I and a row of boxes for marking. The last name "GIDDIE" and first name "ABBIE" are written in the grids. To the right of these names is a column labeled "CODE" with boxes for marking.

Part A [40 marks]

This section consists of 40 questions that survey the course material.

Answer all 40 questions; each question is worth 1 mark.

The diagram below shows the marginal benefit and marginal cost of a public good. This economy has 3 individuals, A, B and C. The diagram shows the MB for each individual and a summation of their marginal benefits.

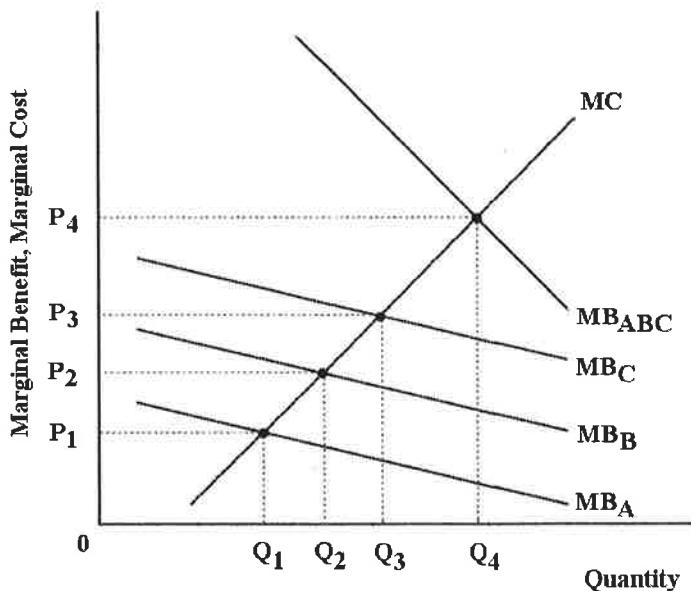


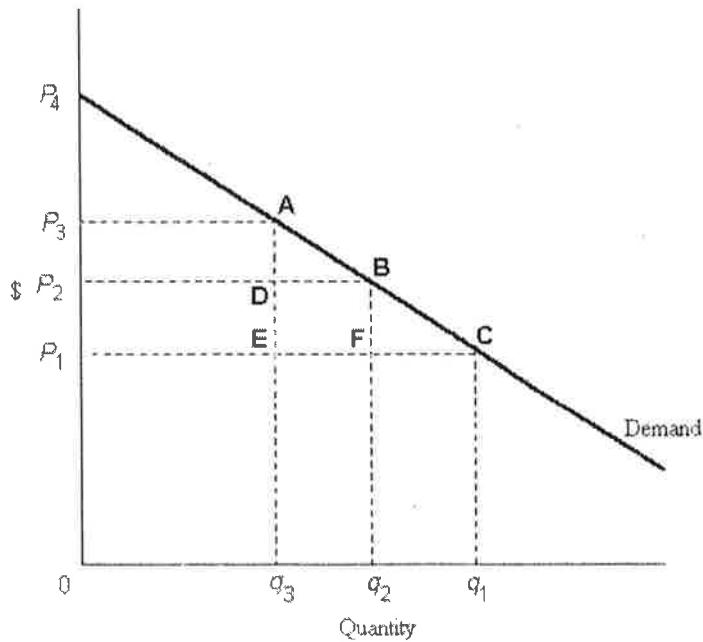
FIGURE 16-4

- 1) Refer to Figure 16-4. The curve MB_{ABC} is derived by
 - A) a vertical summation of the marginal benefits of all individuals at each level of output.
 - B) observation of the consumption of public goods at a price of zero.
 - C) observation of the consumption of public goods at the optimal price.
 - D) a horizontal summation of the marginal benefits of all individuals at each given price level.
 - E) determining the private marginal cost of the public good.

- 2) Refer to Figure 16-4. What is the optimal quantity of this public good to provide?

A) 0	B) Q_1	C) Q_2	D) Q_3
E) Q_4			

- 3) Suppose taxes are levied in the following way. No individual pays any taxes on the first \$10 000 of their income. And for every dollar earned above this amount, all individuals pay 20% in taxes. This income-tax system is
 - A) regressive.
 - B) progressive.
 - C) indexed.
 - D) proportional.
 - E) an accurate description of the Canadian system.

**FIGURE 18-3**

- 4) Refer to Figure 18-3. Suppose that supply is perfectly elastic and the price of this good is initially P_1 . If an excise tax raises the price from P_1 to P_2 , the direct burden of the tax is
- the area DEFB.
 - the area P_1FBP_2 .
 - the area P_1CBP_4 .
 - the area BFC.
 - zero.
- 5) Refer to Figure 18-3. Suppose that supply is perfectly elastic and the price of this good is initially P_1 . If an excise tax raises the price from P_1 to P_2 , the excess burden (deadweight loss) of the tax is
- the area DEFB.
 - the area P_1FBP_2 .
 - the area P_1CBP_4 .
 - the area BFC.
 - zero.
- 6) Suppose Honest Rob's Used Cars buys a used car for \$2000 and resells it for \$3000. The result of Honest Rob's transactions is to
- decrease the value of national income by \$3000.
 - decrease the value of national income by \$1000.
 - leave the value of national income unchanged.
 - increase the value of national income by \$1000.
 - increase the value of national income by \$3000.

7) If 27 million people are employed and 3 million people are unemployed, what is the unemployment rate?

- A) 11%
- B) 89%
- C) 10%
- D) 90%
- E) Not able to determine from the information provided

8) Suppose that a price index for a certain basket of goods and services has a value of 150 in 2015 and a value of 156 in 2016. This index suggests that the cost of the market basket of goods and services

- A) was 4% higher in 2016 than in 2015.
- B) was 6% lower in 2016 than in 2015.
- C) was 6% higher in 2016 than in 2015.
- D) was 156% higher in 2016 than in 2015.
- E) was approximately the same in 2016 and 2015.

9) Consider Canada's national accounts. An example of a transfer payment is

- A) government payments of salaries to schoolteachers.
- B) government spending on military equipment.
- C) pensions paid from the Canada Pension Plan.
- D) private firms' payments of dividends.
- E) government payments of salaries to Members of Parliament.

The table below shows total output for an economy over 2 years.

2015	Price	Quantity
Good A	\$1.00	100 units
Good B	\$2.00	200 units
2016	Price	Quantity
Good A	\$2.00	120 units
Good B	\$3.00	200 units

TABLE 20-5

10) Refer to Table 20-5. If 2015 is the base year, then real GDP in 2016 was

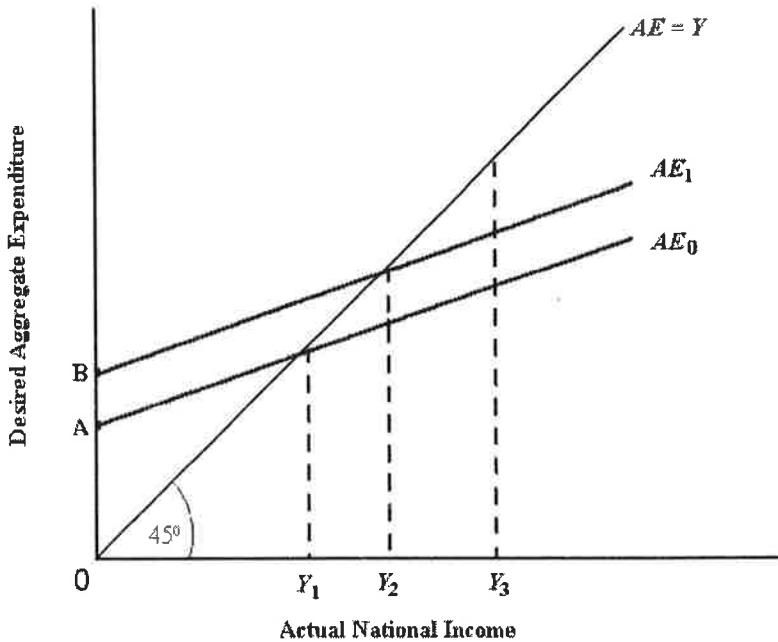
- A) \$500.
- B) \$520.
- C) \$700.
- D) \$840.
- E) \$1040.

11) One major reason that GDP is an inaccurate measure of the "quality of life" is that

- A) people frequently buy things they do not want.
- B) it does not include the value of leisure.
- C) it is statistically very inaccurate.
- D) it cannot be adjusted for changes in prices.
- E) it includes net exports.

12) Suppose disposable income for an entire economy rises from \$400 billion to \$440 billion and desired consumption rises from \$350 billion to \$380 billion. We can conclude that the marginal propensity to consume for this economy is

- A) 0.65.
- B) 0.75.
- C) 0.80.
- D) 0.90.
- E) 1.33.

**FIGURE 21-3**

- 13) Refer to Figure 21-3. If national income is Y_3 and the aggregate expenditure function is AE_1 ,
- the economy is in equilibrium.
 - there is unintended inventory accumulation and income will rise.
 - there is unintended inventory accumulation and income will fall.
 - there is unintended inventory decumulation and income will rise.
 - there is unintended inventory decumulation and income will fall.
- 14) Consider a simple macro model with demand-determined output. In such a model, the larger is the marginal propensity to spend, the
- flatter is AE and the smaller is the multiplier.
 - flatter is AE and the larger is the multiplier.
 - steeper is AE and the smaller is the multiplier.
 - steeper is AE and the larger is the multiplier.
 - greater is investment as a percentage of GDP.
- 15) When determining the AE function for an open economy with government, it is generally assumed that as real national income
- increases, exports will decrease.
 - increases, net exports will decrease.
 - increases, imports will decrease.
 - decreases, net exports will decrease.
 - decreases, exports will decrease.
- 16) A parallel downward shift in the net export (NX) function can be caused by
- an increase in domestic national income.
 - a decrease in foreign national income.
 - a decrease in domestic prices.
 - an increase in the Canadian-dollar price of foreign currency.
 - a decrease in foreign prices.

- 17) Consider the following news headline: "China signs deal to buy more Canadian wheat." Assuming that aggregate output is demand-determined, what effect will this have, all other things equal, on the AE function and on equilibrium national income?
- A) The AE function will shift down parallel to itself and equilibrium national income will fall.
 - B) The AE function will rotate upward (become steeper) and equilibrium national income will rise.
 - C) The AE function will rotate downward (become flatter) and national income will fall.
 - D) The AE function will shift up parallel to itself and equilibrium national income will rise.
 - E) There will be no change in the AE function or in equilibrium national income.
- 18) Which of the following would likely cause a downward shift in the *AE* curve and a movement upward along the *AD* curve?
- A) a decrease in the business confidence of firms
 - B) a reduction in government purchases
 - C) a decrease in the marginal propensity to consume
 - D) a decrease in the price level
 - E) an increase in the price level
- 19) The short-run aggregate supply curve (SRAS) tends to be relatively steep when GDP is above potential output because firms are operating above _____ and _____ are rising rapidly.
- A) equilibrium output; unit costs
 - B) profit-maximizing output; total costs
 - C) capacity; unit costs
 - D) equilibrium output; total costs
 - E) equilibrium output; average costs
- 20) If the economy's *AS* curve is upward sloping, a positive aggregate demand shock will result in
- A) an increase in prices but not output.
 - B) an increase in output but not prices.
 - C) an increase in both output and prices.
 - D) a decrease in both output and prices.
 - E) a decrease in output and an increase in prices.
- 21) If the economy is experiencing a recessionary output gap, the adjustment process operates as follows:
- A) wages do not adjust, but the *AD* curve shifts to the right.
 - B) wages fall, unit costs fall, and the *AD* curve shifts rightward.
 - C) wages rise, unit costs rise, and the *SRAS* curve shifts up.
 - D) wages rise, unit costs rise, and the *SRAS* curve shifts down.
 - E) wages fall, unit costs fall, and the *SRAS* curve shifts down.
- 22) In the basic AD/AS macro model, which of the following events would cause stagflation?
- A) a large decrease in wages
 - B) a large increase in business confidence
 - C) a large increase in the net tax rate
 - D) a large increase in the price of raw materials
 - E) a large increase in labour productivity

The diagram below shows an AD/AS model for a hypothetical economy which is initially in a short-run equilibrium at point A.

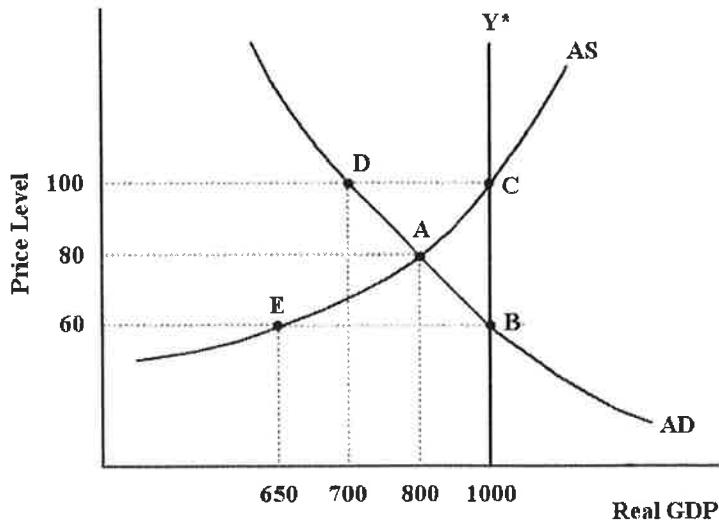


FIGURE 24-6

- 23) Refer to Figure 24-6. The government could close the existing output gap by
- increasing the net tax rate.
 - decreasing the net tax rate.
 - decreasing government purchases.
 - decreasing government transfer payments.
 - implementing a contractionary fiscal policy.

The diagram below shows alternate growth paths for two hypothetical economies, each starting with GDP of \$1 billion.

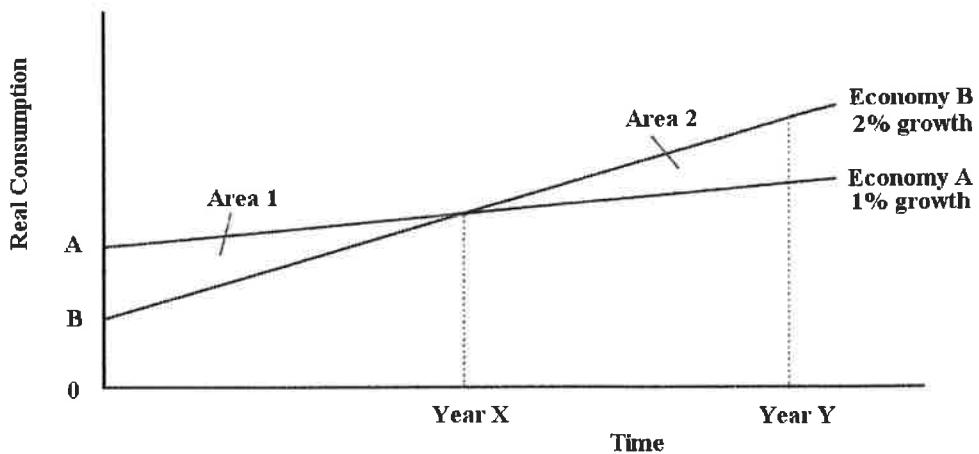


FIGURE 25-1

- 24) Refer to Figure 25-1. The area marked Area 1 represents
- the value of consumption from Year 0 to Year X in Economy A.
 - the value of the investment in capital goods undertaken by Economy B.
 - the value of the investment in capital goods undertaken by Economy A.
 - the sacrifice of current consumption by Economy B, as compared to Economy A.
 - the sacrifice of current consumption by Economy A, as compared to Economy B.

- 25) Consider the market for financial capital for a closed economy in the long run. Other things being equal, a country with a high national saving rate will tend to have
- A) a high growth rate because aggregate expenditure will be high out of any given income.
 - B) a high growth rate because sustained high investment is possible with high saving.
 - C) an AS curve moving continually to the left.
 - D) trouble achieving potential real national income in the short run.
 - E) either a high or low growth rate depending on the investment demand schedule.
- 26) One important assumption of the Neoclassical growth model is that, with a given state of technology,
- A) increases in the use of a single factor bring increasing returns.
 - B) increases in the use of a single factor result in constant returns.
 - C) increases in the use of single factor bring diminishing returns.
 - D) the return from successive units of a single factor increases over time.
 - E) increases in GDP are possible only if all factors are increased at an equal rate.
- 27) Which of the following is an example of the use of money as a medium of exchange?
- A) Dave keeps \$250 in his drawer for a "rainy day."
 - B) Mike gets a friend to give him a beer today in return for promising to give the friend two beer when Mike gets paid at the end of the month.
 - C) Judy lends her car to a friend who signs a promissory note that she will pay Judy \$10 a day for the use of the car after she returns the car to Judy.
 - D) Barry pays \$275 with his bank debit card for tickets for an NHL play-off game.
 - E) ABC Investments Inc. enters in its account books that it owes Nallai \$20 for his last month's investment income.
- 28) If the annual interest rate is 10%, \$5.00 received today has the same present value as
- A) \$4.00 received one year from now.
 - B) \$4.50 received one year from now.
 - C) \$5.00 received one year from now.
 - D) \$5.50 received one year from now.
 - E) \$6.00 received one year from now.
- 29) Speculative demand for money arises from the desire by individuals and firms to hold cash balances
- A) for speculative equity purchases.
 - B) in anticipation of changes in interest rates and bond prices.
 - C) to meet unforeseen business expenses.
 - D) in anticipation of investing in capital purchases for the firm.
 - E) to maintain adequate cash flow in case of inflation.
- 30) Consider the monetary transmission mechanism. A disturbance to monetary equilibrium which changes the interest rate will affect aggregate demand through
- A) a shift of the investment demand function and a movement along the aggregate expenditure curve.
 - B) a movement along the investment demand function and a shift of the aggregate expenditure curve.
 - C) a shift of both the investment demand function and the aggregate expenditure curve.
 - D) movements along the investment demand function and the aggregate expenditure curve.
 - E) a movement along the aggregate expenditure curve.

- 31) Most central banks, including the Bank of Canada, implement monetary policy by
A) controlling the money supply directly.
B) influencing a short-term interest rate directly.
C) influencing investment demand directly.
D) influencing the demand for money directly.
E) controlling the process of deposit creation in the commercial banking system.
- 32) In an effort to maintain inflation at its targeted level the Bank of Canada designs its policies, in the short run, to
A) eliminate all unemployment.
B) keep real GDP close to potential output.
C) minimize the growth of the money supply.
D) allow the aggregate supply curve to close any output gaps.
E) eliminate all negative shocks to the economy.
- 33) Suppose economists were able to measure frictional unemployment as 3%, cyclical unemployment as 2%, and structural unemployment as 4%. Then we would know that the NAIRU is _____ and the actual unemployment rate is _____.
A) 6%; 5% B) 5%; 9% C) 7%; 9% D) 7%; 7% E) 6%; 6%
- 34) Which of the following is consistent with constant inflation: expected future inflation of _____, output-gap inflation of _____, and supply-shock inflation _____.
A) 2%; 2%; 2% B) 2%; 0%; -2% C) 2%; 0%; 0% D) 1%; 1%; 1% E) 0%; 0%; -2%
- 35) If the Bank of Canada validates a positive *AD* shock,
A) it will have eliminated the possibility of a continued inflation.
B) there is the risk of continued inflation.
C) wages will fall to reduce the resulting unemployment.
D) output will fall more rapidly than if the shock had not been validated.
E) the *AD* curve will shift to the left and inflation will stop.
- 36) Non-market-clearing theories of the labour market feature _____ wages, and thus involuntary unemployment _____.
A) perfectly flexible; cannot exist
B) perfectly flexible; can exist
C) sticky; cannot exist
D) sticky; can exist
E) efficiency wages; cannot exist

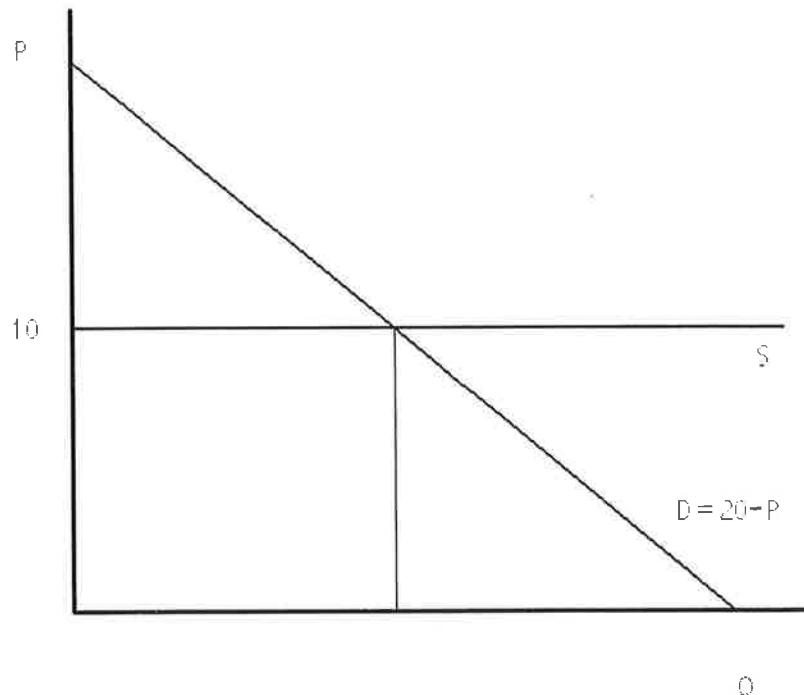
- 37) An increase in the rate of aggregate economic growth usually speeds up the rate of change in the structure of labour demand. As a result, we can expect that structural unemployment will _____, and will therefore cause the NAIRU to _____.
A) decrease; increase
B) decrease; decrease
C) remain constant; remain constant
D) increase; increase
E) increase; decrease
- 38) The federal government's "primary budget deficit"
A) includes domestic borrowing but excludes foreign borrowing.
B) excludes debt-service payments.
C) is the amount of government borrowing in a fiscal year.
D) is the amount of tax revenue minus the amount of interest paid on the public debt.
E) is the most important indicator of the level of government spending.
- 39) Suppose the government's actual budget deficit is equal to the structural (or cyclically adjusted) budget deficit. Then it must be the case that
A) the primary budget deficit is zero.
B) the overall government budget is balanced.
C) the debt-to-GDP ratio is stable.
D) real GDP is equal to potential GDP.
E) the government is not reporting all of its expenses.
- 40) In an open economy like Canada's, a fiscal expansion by the government tends to
A) reduce capital inflow, depreciate the currency, and increase net exports.
B) attract foreign capital and encourage increased investment.
C) crowd out net exports and encourage private investment.
D) attract foreign capital, appreciate the currency, and crowd out net exports.
E) attract foreign capital, depreciate the currency, and crowd out net exports.

Part B-110 [8 marks]

Answer all 8 questions; each question is worth 1 mark.

The following 8 questions (41-48) relate to the information given below. Try to do the questions in order since the answers for some questions depend on the answers to previous questions in the series.

The following diagram illustrates student A's monthly demand curve for cannabis. A can (now legally) buy as many grams as desired at the constant price of \$10.00, which we assume reflects the marginal private cost of cannabis production. As illustrated, A's demand is given by $Q = 20 - P$ or (inverted) $P = 20 - Q$.



- 41) The optimal level of cannabis consumption for student A is
 A) 0 grams B) 5 grams C) 10 grams D) 15 grams E) 20 grams
- 42) Suppose now that student A is living in the same house as student B who does not like student A's cannabis use. Every gram that student A buys imposes an unavoidable cost of \$5.00 on student B. The socially optimal level of cannabis consumption for the household is
 A) 0 grams B) 5 grams C) 10 grams D) 15 grams E) 20 grams

- 43) In this example, cannabis use is
- A) rivalrous and excludable
 - B) non-rivalrous and excludable
 - C) rivalrous and non-excludable
 - D) non-rivalrous and non-excludable
 - E) a pure private good
- 44) The deadweight loss associated with student A's behaviour is
- A) \$0.00
 - B) \$10.00
 - C) \$12.50
 - D) \$20.00
 - E) \$25.00
- 45) The government, if it were interested, could ensure the socially optimal consumption of cannabis use in this household by
- A) subsidizing A's purchases of cannabis by \$10.00
 - B) subsidizing A's purchases of cannabis by \$5.00
 - C) doing nothing – A's purchases are optimal already
 - D) taxing A's purchases of cannabis by \$5.00
 - E) taxing A's purchases of cannabis by \$10.00
- 46) The Direct Burden of this government policy would be
- A) \$0.00
 - B) \$10.00
 - C) \$12.50
 - D) \$20.00
 - E) \$25.00
- 47) Alternatively, the social optimum might be assured if:
- A) A paid B every time A bought a gram
 - B) B paid A every time A didn't buy a gram
 - C) B paid A every time A bought a gram
 - D) options A) or B) above
 - E) options A) or C) above
- 48) Suppose A and B also know students C and D. Student C enjoys cannabis use by others and actually gets a benefit of \$5.00 every time someone consumes a gram. Student D is completely unaffected by the use of cannabis by others. Other things being equal, for efficiency (assuming two-person housing options):
- A) A should live with B
 - B) A should live with D
 - C) C should live with D
 - D) C should live with B
 - E) A should live with C

Part C [8 marks]

Answer all 8 questions; each question is worth 1 mark.

The following 8 questions (49-56) relate to the information given below. Try to do the questions in order since the answers for some questions depend on the answers to previous questions in the series.

Consider the following model of a closed economy. Output prices, factor prices and interest rates are assumed constant. We have the following information, where Y_D is disposable income and Y is national income.

Consumption: $C = 150 + (0.8)Y_D$

Investment: $I = 150$

Government Spending $G = 500$

Taxes (net of transfers) $T = (0.25)Y$

The space below is provided for you to keep track of your answers as you work through the series of questions. [Hint: You may want to sketch an *AE* diagram to help with this process.]

49) The equation for aggregate expenditures is given by:

- A) $AE = 800 + (.80)Y$
- B) $AE = 800 + (.75)Y$
- C) $AE = 800 + (.60)Y$
- D) $AE = 700 + (.80)Y$
- E) $AE = 700 + (.60)Y$

- 50) The equilibrium level of national income is:
A) 1500 B) 1750 C) 2000 D) 3500 E) 4000
- 51) In equilibrium, the government:
A) has a balanced budget.
B) is running a deficit of 125.
C) is running a deficit of 200.
D) is running deficit of 325.
E) is running a surplus.
- 52) Suppose that, as a result of a financial crisis, **both** autonomous consumption and investment fall by 100.
The new equilibrium level of national income is:
A) 1500 B) 1750 C) 2000 D) 3500 E) 4000
- 53) In this model, the multiplier is equal to:
A) 5.00 B) 4.00 C) 2.50 D) 2.00 E) 1.00
- 54) In the new equilibrium, the government:
A) has a balanced budget.
B) is running a deficit of 125.
C) is running a deficit of 200.
D) is running deficit of 325.
E) is running a surplus.
- 55) Suppose that government wants to use fiscal policy to restore the original level of national income. A policy that would accomplish this goal is:
A) an increase in spending of 50.
B) an increase in spending of 100.
C) an increase in spending of 200.
D) an increase in spending of 500.
E) an increase in spending of 1000.
- 56) After the change in government fiscal policy, the government:
A) has a balanced budget.
B) is running a deficit of 125.
C) is running a deficit of 200.
D) is running deficit of 325.
E) is running a surplus.

Part D [8 marks]

Answer all 8 questions; each question is worth 1 mark.

The following 8 questions (57-64) relate to the information given below. Try to do the questions in order since the answers for some questions depend on the answers to previous questions in the series.

Suppose the balance sheet for the only commercial bank in a particular country is given below. Assume that the only money in the country is in the form of deposits at the commercial bank.

Assets		Liabilities	
Reserves	200	Deposits	2200
Loans to the Public	1600		
Government Bonds	300		
Other Assets	300	Capital	200
Total	2400	Total	2400

- 57) The reserve ratio for the bank is
 A) 1/6 B) 1/7 C) 1/9 D) 1/11 E) 1/12
- 58) The capital/loan ratio for the bank is
 A) 1/1 B) 2/3 C) 1/3 D) 1/4 E) 1/8
- 59) Suppose the central bank of the country wishes to increase the size of the money supply, and does so by increasing the reserves at the bank to 300 units through an open market operation. Immediately after this transaction the reserve ratio will be:
 A) 3/22 B) 1/6 C) 1/8 D) 1/11 E) 3/26

- 60) Assuming that the bank creates new loans in order to keep its reserve ratio at the original level, this will lead to the creation of new loans equal to _____ and an overall new money supply equal to _____:
A) 1100, 3300
B) 400, 2600
C) 400, 2700
D) 300, 2700
E) 1100, 3100

61) Suppose now that the bank is governed by *additional* regulations that require it to have a capital/loan ratio of at least 10%. As above, the central bank of the country wishes to increase the money supply and increases the reserves at the bank to 300 through an open market operation. Under the assumption that the bank will increase its loans by the most it is allowed, this will lead to the creation of new loans equal to _____ and an overall new money supply equal to _____:
A) 1100, 3300
B) 400, 2600
C) 400, 2700
D) 300, 2700
E) 1100, 3100

62) After the open market operation and the increase in loans, the reserve ratio will be:
A) 3/22 B) 1/6 C) 1/8 D) 1/11 E) 3/26

63) Under these same circumstances (a constraint to keep a capital/loan ratio of at least 10% and a desire to keep the reserve ratio equal to the original level), suppose that, instead of using an open market operation, the government of the country increases the reserves at the bank to 300 through a capital injection – i.e. it buys shares in the bank and pays for them by adding to the bank’s deposits at the central bank. This will lead to the creation of new loans equal to _____ and an overall new money supply equal to _____:
A) 1100, 3300
B) 1400, 3600
C) 400, 2800
D) 300, 2700
E) 1100, 3100

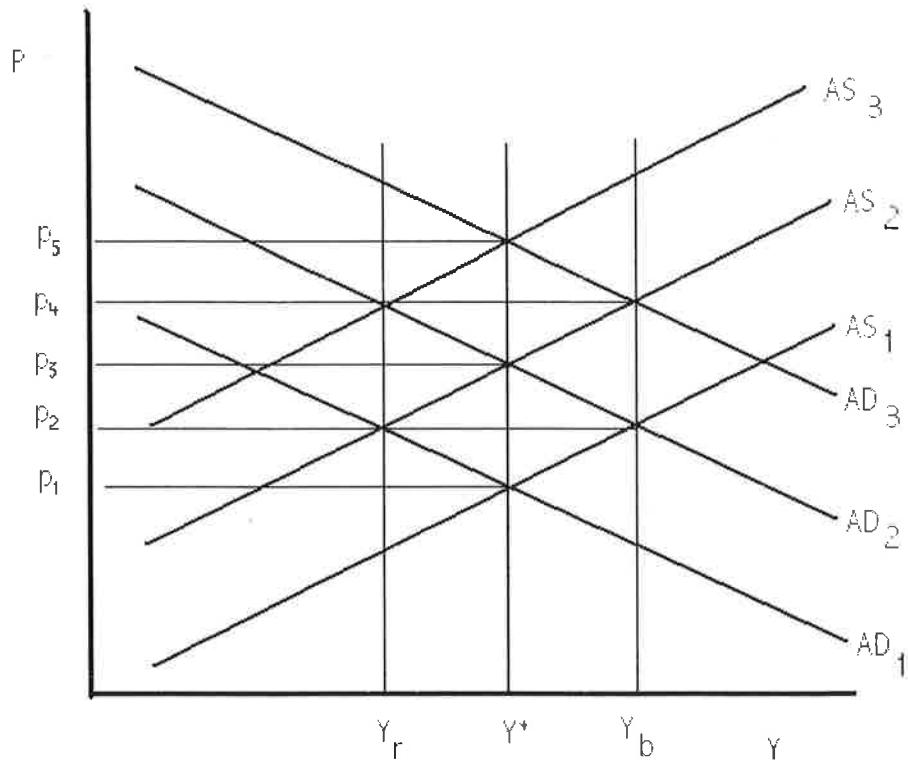
64) After this new transaction and the increase in loans, the reserve ratio will be:
A) 3/22 B) 1/6 C) 1/8 D) 1/11 E) 3/26

Part E [8 marks]

Answer all 8 questions; each question is worth 1 mark.

The following 8 questions (65-72) relate to the information given below. Try to do the questions in order since the answers for some questions depend on the answers to previous questions in the series.

The following is an aggregate supply – aggregate demand diagram for a country. Initially the curves are stable at AD_2 and AS_2 .



- 65) Initially, real GDP and the price level are given by:
 A) Y^*, P_3 B) Y_r, P_4 C) Y_b, P_2 D) Y^*, P_2 E) Y_b, P_4
- 66) Suppose there is an increase in investment due to growing business confidence. This will lead to a new short-run equilibrium given by:
 A) Y^*, P_3 B) Y_r, P_4 C) Y_b, P_2 D) Y^*, P_2 E) Y_b, P_4

- 67) Assuming that neither the government nor the central bank take any policy action, the result of the increase in investment will be:
- A) A boom followed by a return to Y^* , and continuing inflation.
 - B) A boom followed by a return to Y^* and then a recession with no effect on inflation.
 - C) A recession and a positive inflation rate, followed eventually by a deflation and a return to Y^* .
 - D) A boom and a positive inflation rate, followed by a return to Y^* and no further inflation.
 - E) A recession and deflation, followed eventually by inflation and a return to Y^* .
- 68) Suppose instead that the central bank does not want to wait for the natural adjustment of the economy to occur and decides to pursue a countercyclical monetary policy. It should:
- A) leave interest rates unchanged to pursue a contractionary monetary policy
 - B) increase interest rates to pursue a contractionary monetary policy
 - C) decrease interest rates to pursue a contractionary monetary policy
 - D) increase interest rates to pursue an expansionary monetary policy
 - E) decrease interest rates to pursue an expansionary monetary policy
- 69) If the lag until the full effects of monetary policy changes are fully reflected in the economy is short, the new equilibrium for the economy will be:
A) Y^*, P_3 B) Y_r, P_4 C) Y_b, P_2 D) Y^*, P_2 E) Y_b, P_4
- 70) If the lag until the full effects of monetary policy changes are fully reflected in the economy is long, and the natural adjustment of the economy coincides with the full effect of the monetary policy change, the new equilibrium for the economy will be:
A) Y^*, P_3 B) Y_r, P_4 C) Y_b, P_2 D) Y^*, P_2 E) Y_b, P_4
- 71) Suppose that after the change in investment the country becomes engaged in a trade dispute with its largest trade partner who threatens to enact a tariff policy that would reduce the country's exports. If the foreign country makes good on its threat the result would be:
A) neutral, that is leave both AD and AS unchanged
B) a positive AD shock
C) a negative AD shock
D) a positive AS shock
E) a negative AS shock
- 72) If the lag until the full effects of monetary policy changes contemplated in #68 are fully reflected in the economy is long, and the effects of the trade dispute from #71 coincides with the full effect of the monetary policy change, the new equilibrium for the economy will be:
A) Y_r, P_2 B) Y_r, P_4 C) Y_b, P_2 D) Y^*, P_2 E) Y_b, P_4

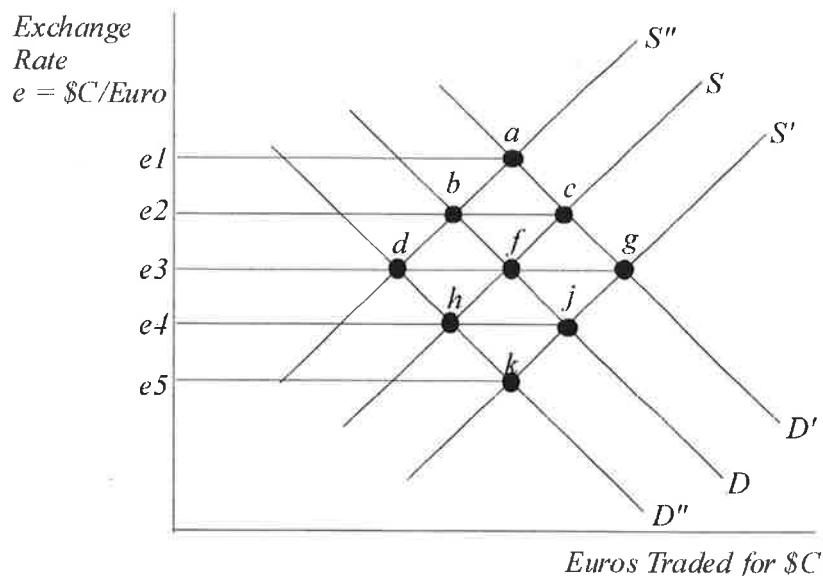
Part F [8 marks]

Answer all 8 questions; each question is worth 1 mark.

The following 8 questions (73-80) relate to the information given below. Try to do the questions in order since the answers for some questions depend on the answers to previous questions in the series.

The diagram below represents the market for Euros exchanged for Canadian dollars. The horizontal axis measures the quantity of Euros traded for Canadian dollars ($\$C$) and the vertical axis measures the exchange rate, the number of $\$C$ per Euro.

Assume that the market is in the equilibrium represented by point "f", and that the exchange rate between the Canadian dollar and the Euro is fully flexible.



73) The demand curve of Euros for Canadian dollars is downward sloping because, as e rises,

- A) the Canadian dollar appreciates so Canadians want to purchase fewer exports from Europe.
- B) the Canadian dollar depreciates so Canadians want to purchase fewer exports from Europe.
- C) the Canadian dollar appreciates so Canadians want to purchase more exports from Europe.
- D) the Canadian dollar depreciates so Canadians want to purchase more exports from Europe.
- E) the Canadian dollar depreciates so Europeans want to purchase fewer exports from Canada.

74) At the initial equilibrium point f ,

- A) the current account balance plus the capital account balance is positive.
- B) the current account balance plus the capital account balance is negative.
- C) the current account balance plus the capital account balance is zero.
- D) the balance on the official financing account at the Bank of Canada is positive.
- E) the balance on the official financing account at the Bank of Canada is negative.

75) Suppose consumer tastes in Europe change toward maple syrup (a major Canadian export to Europe).

The new exchange rate will be ____ and the new equilibrium will be at ____.

- A) e_2 ; point b B) e_1 ; point a C) e_3 ; point d D) e_5 ; point k E) e_4 ; point j

Return to the original equilibrium at point "f". For the balance of the series suppose that, as a result of Canadian monetary policy expansion, interest rates in Canada decrease relative to those in Europe.

76) As a result of the decrease in Canadian interest rates, the new exchange rate will be ____ and the new equilibrium will be at ____.

- A) e_2 ; point b B) e_1 ; point a C) e_3 ; point d D) e_5 ; point k E) e_4 ; point j

77) As a result of the change in Canadian interest rates,

- A) the Canadian dollar depreciates and Canadian net exports to Europe will increase.
B) the Canadian dollar depreciates and European net exports to Canada will increase.
C) the value of the Canadian dollar is unchanged so Canadian net exports to Europe will be unchanged.
D) the Canadian dollar appreciates and Canadian exports to Europe will decrease.
E) the Canadian dollar appreciates and European net exports to Canada will increase.

78) As a result of the change in Canadian interest rates, in Canada

- A) the short run aggregate supply curve shifts left.
B) the short run aggregate supply curve shifts right.
C) neither the short run aggregate supply curve nor the aggregate demand curve are affected.
D) the aggregate demand curve shifts left.
E) the aggregate demand curve shifts right.

79) If Canada was initially running a current account surplus, then the change in Canadian interest rates will

- A) cause a decrease the amount of the current account surplus.
B) have no effect on the amount of the current account surplus.
C) cause an increase the amount of the current account surplus.
D) result in a change the amount of the current account surplus but we cannot tell whether it would rise or fall.
E) cause the current account to fall into deficit.

80) As a result of the change in Canadian interest rates, Canada will

- A) not change its net borrowing from the rest of the world.
B) increase its net borrowing from the rest of the world.
C) decrease its net borrowing from the rest of the world.
D) increase its net lending to the rest of the world.
E) decrease its net lending to the rest of the world.

