NANYANG TECHNOLOGICAL UNIVERSITY

HE2002 MACROECONOMICS II

SEMESTER 2 AY 2023/2024

Practice Questions

Lecture 1

1) Which of the following is true for a "closed economy"?
A) government spending equals taxes
B) there are no imports or exports
C) exports equal imports
D) there is no saving
E) there is no government spending or taxes

2) Disposable income equals
A) income minus saving.
B) income minus both saving and taxes.
C) consumption minus taxes.
D) the sum of consumption and private saving.
E) none of these

3) The marginal propensity to consume represents
A) the level of consumption that occurs if disposable income is zero.
B) the ratio of total consumption to disposable income.
C) total income minus total taxes.
D) the change in output caused by a one-unit change in autonomous demand.
E) the change in consumption caused by a one-unit change in disposable income.

4) Let the consumption function be represented by the following equation: $C = c0 + c1YD$. For this equation, we assume that c1 is
A) negative.
B) larger than c0.
C) different at different levels of income.
D) equal to one.
E) none of these

5) Suppose the consumption equation is represented by the following: $C = 250 + .75YD$. The multiplier in this economy is
A) .25.
B) .75.
C) 1.

D) 4.
E) 5.

6) Equilibrium in the goods market requires that
A) production equals income.
B) production equals demand.
C) consumption equals saving.
D) consumption equals income.
E) government spending equals taxes minus transfers.

7) Which of the following would tend to make the multiplier smaller?
A) an increase in the marginal propensity to consume
B) an increase in the marginal propensity to save
C) a reduction in taxes
D) a reduction in government spending
E) none of these

8) Suppose there is an increase in autonomous consumption. Specifically, suppose c0 increases where C = c0 + c1YD. This increase in autonomous consumption will cause which of the following to increase?
A) equilibrium income
B) equilibrium disposable income
C) demand
D) all of these
E) none of these

9) If C = 2000 + .9YD, what increase in government spending must occur for equilibrium output to increase by 1000?
A) 100
B) 200
C) 250
D) 500
E) 1000

10) Autonomous spending in a closed economy equals which of the following?
A) c0 + I + G - c1T
B) C + I + G
C) Z
D) c0 + I + G + c1T

11) Based on our understanding of the model presented in Lecture 1, we know that an increase in c1 (where C = c0 + c1YD) will cause
A) the ZZ line to become steeper and a given change in autonomous consumption (c0) to have a smaller effect on output.

B) the ZZ line to become steeper and a given change in autonomous consumption (c0) to have a larger effect on output.
C) the ZZ line to become flatter and a given change in autonomous consumption (c0) to have a smaller effect on output.
D) the ZZ line to become flatter and a given change in autonomous consumption (c0) to have a larger effect on output.

12) An increase in the marginal propensity to save from .3 to .4 will cause
A) the ZZ line to become steeper and a given change in autonomous consumption (c0) to have a smaller effect on output.
B) the ZZ line to become steeper and a given change in autonomous consumption (c0) to have a larger effect on output.
C) the ZZ line to become flatter and a given change in autonomous consumption (c0)) to have a smaller effect on output.
D) the ZZ line to become flatter and a given change in autonomous consumption (c0) to have a larger effect on output.

13) When the economy is in equilibrium, we know with certainty that
A) public saving equals investment.
B) private saving equals investment.
C) G = T.
D) none of these

14) When a closed economy is in equilibrium, we know with certainty that
A) I = S + (T - G).
B) I = S.
C) I = S + (G - T).
D) G = T and S = I.

15) Based on our understanding of the model presented in Chapter 3, we know with certainty that an equal and simultaneous increase in G and T will cause
A) an increase in output.
B) no change in output.
C) a reduction in output.
D) an increase in investment.

16) Based on our understanding of the model presented in Chapter 3, a reduction in investment will cause
A) an increase in the multiplier.
B) a reduction in the multiplier.
C) a reduction in the marginal propensity to save.
D) a reduction in output.
E) a reduction in the multiplier and output.

17) Suppose the marginal propensity to consume equals .8 (i.e., c1 = .8). Given this information, which of the following events will cause the largest increase in output?
A) G increases by 200
B) T decreases by 200
C) I increases by 150
D) G increases by 200 and T increases by 200

18) Suppose the consumption equation is represented by the following: C = 250 + .75YD, then private savings is
A) -250+0.25YD.
B) -250+0.75YD.
C) -1000+0.25YD.
D) -1000+0.75YD.

19) If C = 2000 + .9YD, what decrease in taxes must occur for equilibrium output to increase by 1000?
A) 111
B) 100
C) 1000
D) 500

20) Which of the following about IS relation is *not* correct?
A) It is the the relation between interest rate and savings.
B) It is the equilibrium condition for the goods market.
C) It stands for "Investment equals saving."
D) It shows what firms want to invest must be equal to what people and the government want to save.

Lecture 1

(Please note that these solutions are provided as suggestions and may not be error-free. I encourage you to engage in discussions, compare your answers with peers, and feel free to ask questions if you find any typos or mistakes. Learning requires practice, and your attempts will contribute to a better understanding of the material.)

1) B
2) D
3) E
4) E
5) D
6) B
7) B
8) D
9) A
10) A
11) B
12) C
13) D
14) A
15) A
16) D
17) A
18) A
19) A
20) A

Lecture 2

1) Which of the following is a characteristic of bonds?
A) pay zero nominal interest
B) can be used for transactions
C) are sold for a price that varies inversely with the interest rate
D) all of these
E) none of these

2) Which of the following is a component of money?
A) bonds
B) saving
C) income
D) stocks
E) none of these

3) Which of the following is a component of money?
A) coins held by the nonbank public
B) bills held by banks
C) checkable deposits
D) all of these

4) Which of the following will cause an increase in the amount of money that one wishes to hold?
A) an increase in the interest rate increase
B) a reduction in the interest rate increase
C) a reduction in income
D) none of these

5) The money demand curve will shift to the right when which of the following occurs?
A) an increase in income
B) a reduction in the interest rate
C) an increase in the money supply
D) all of these
E) none of these

6) Which of the following affects demand for money?
A) prices
B) nominal income
C) interest rate
D) all of these
E) none of these

7) At the current interest rate, suppose the supply of money is less than the demand for

money. Given this information, we know that
A) the price of bonds will tend increase.
B) the price of bonds will tend to fall.
C) production equals demand.
D) the goods market is also in equilibrium.
E) the supply of bonds also equals the demand for bonds.

8) The interest rate will increase as a result of which of the following events?
A) an increase in income
B) an open market purchase of bonds by the central bank
C) a reduction in income
D) all of these
E) none of these

9) Which of the following is *not* an *asset* on a bank's balance sheet?
A) reserves
B) loans
C) checkable deposits
D) all of these
E) none of these

10) Which of the following is a *liability* for the *central* bank?
A) currency
B) bonds
C) savings accounts
D) loans
E) checkable deposits

11) Suppose a one-year discount bond offers to pay $1000 in one year and currently has a 15% interest rate.
Given this information, we know that the bond's price must be
A) $869.56.
B) $1150.
C) $850.
D) $950.
E) none of these

12) Which of the following generally occurs when a central bank pursues expansionary monetary policy?
A) the central bank purchases bonds and the interest rate increases.
B) the central bank purchases bonds and the interest rate decreases.
C) the central bank sells bonds and the interest rate increases.
D) the central bank sells bonds and the interest rate decreases.

13) Which of the following will occur when the central bank pursues expansionary monetary policy?
A) a leftward shift in the money demand curve and a leftward shift in the money supply curve
B) a rightward shift in the money demand curve and a leftward shift in the money supply curve.
C) a leftward shift in the money demand curve and a rightward shift in the money supply curve.
D) a rightward shift in the money demand curve and a rightward shift in the money supply curve.
E) none of these

14) Which of the following is an asset of a central bank?
A) currency
B) bonds
C) reserves
D) none of these

15) Which of the following is a component of money base?
A) bonds held by banks, loans, and bank reserves
B) currency in circulation plus bank reserves
C) currency in circulation plus checkable deposits
D) bonds held by banks plus checkable deposits
E) the sum of currency in circulation, bank reserves, and checkable deposits

16) For this question, assume that individuals do *not* hold currency (i.e., c = 0). If the ratio of reserves to deposits is .10, the money multiplier is
A) .1.
B) .9.
C) 4.
D) 5.
E) 10.

17) For this question, assume that individuals do *not* hold currency (i.e., c = 0). The money multiplier is equal to
A) 1/(1-c).
B) 1/[c + θ(1 - c)].
C) [c + θ(1 - c)].
D) 1/θ.
E) none of these

18) We would expect which of the following to occur when the central bank pursues expansionary monetary policy?
A) an increase in bond prices and an increase in the interest rate (i)

B) a reduction in bond prices and an increase in i
C) an increase in bond prices and a reduction in i
D) a reduction in bond prices and a reduction in i
E) none of these

19) Based on our understanding of the determinants of the interest rate and bond prices, we know that a reduction in income will cause
A) an increase in bond prices and an increase in the interest rate (i).
B) a reduction in bond prices and an increase in i.
C) an increase in bond prices and a reduction in i.
D) a reduction in bond prices and a reduction in i.
E) none of these

20) We would expect which of the following to occur when the central bank conducts an open market sale of bonds?
A) a reduction in the monetary base (H)
B) a reduction in the money multiplier
C) an increase in H
D) an increase in the money multiplier
E) an increase in H and the money multiplier

21) An increase in the reserve ratio, θ, will cause
A) an increase in the monetary base (H).
B) a reduction in H.
C) an increase in the money multiplier.
D) a reduction in the money multiplier.
E) none of these
Answer: D
Diff: 2

22) An increase in income will cause
A) a reduction in the supply of central bank money.
B) a reduction in the demand for currency.
C) an increase in the demand for reserves.
D) none of these

23) When a liquidity trap situation exists, we know that
A) an open market operation will have no effect on the supply of money.
B) an open market operation will have no effect on the monetary base.
C) fiscal policy will have no effect on the demand for goods.
D) expansionary monetary policy will be deflationary.
E) none of these

24) An open market purchase of bonds by the central bank will cause which of the

following when a liquidity trap situation exists?
A) The interest rate will decrease.
B) The interest rate will not change.
C) Output will increase.
D) The money supply, M, will not change.
E) none of these

25) When a liquidity trap situation exists, the most appropriate policy to increase output would be
A) a central bank sale of bonds.
B) an increase in government spending.
C) a central bank purchase of bonds.
D) none of these

Lecture 2

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1) C
2) E
3) D
4) B
5) A
6) D
7) B
8) A
9) C
10) A
11) A
12) B
13) E
14) B
15) B
16) E
17) D
18) C
19) C
20) A
21) D
22) C
23) E
24) B
25) B

Lecture 3

1) The IS curve represents
A) the single level of output where the goods market is in equilibrium.
B) the single level of output where financial markets are in equilibrium.
C) the combinations of output and the interest rate where the money market is in equilibrium.
D) the combinations of output and the interest rate where the goods market is in equilibrium.
E) none of these

2) The IS curve will shift to the right when which of the following occurs?
A) an increase in the money supply
B) an increase in government spending
C) a reduction in the interest rate
D) all of these
E) none of these

3) Which of the following occurs as the economy moves leftward along a given IS curve?
A) An increase in the interest rate causes investment spending to decrease.
B) An increase in the interest rate causes money demand to increase.
C) An increase in the interest rate causes a reduction in the money supply.
D) A reduction in government spending causes a reduction in demand for goods.
E) An increase in taxes causes a reduction in demand for goods.

4) Suppose policy makers decide to reduce taxes. This fiscal policy action will cause which of the following to occur?
A) The LM curve shifts and the economy moves along the IS curve.
B) The IS curve shifts and the economy moves along the LM curve.
C) Both the IS and LM curves shift.
D) Neither the IS nor the LM curve shifts.
E) Output will change causing a change in money demand and a shift of the LM curve.

5) Suppose investment spending is *not* very sensitive to the interest rate. Given this information, we know that
A) the IS curve should be relatively flat.
B) the IS curve should be relatively steep.
C) the LM curve should be relatively flat.
D) the LM curve should be relatively steep.
E) neither the IS nor the LM curve will be affected.

6) For each interest rate, the LM curve illustrates the level of output where
A) the goods market is in equilibrium.

B) inventory investment equals zero.
C) money supply equals money demand.
D) all of these
E) none of these

7) The LM curve shifts down when which of the following occurs?
A) an increase in taxes
B) an increase in output
C) an open market sale of bonds by the central bank
D) an increase in consumer confidence
E) none of these

8) Which of the following statements is consistent with a given (i.e., fixed) LM curve?
A) A reduction in the interest rate causes investment spending to increase.
B) A reduction in the interest rate causes money demand to decrease.
C) A reduction in the interest rate causes an increase in the money supply.
D) An increase in output causes an increase in demand for goods.
E) An increase in output causes an increase in money demand.

9) In late 2007 and early 2008, the U.S. Federal Reserve pursued expansionary monetary policy. Which of the following will occur as a result of this monetary policy action?
A) The LM curve shifts down.
B) The LM curve shifts up.
C) The IS curve shifts rightward as the interest rate falls.
D) The IS curve shifts leftward as the interest rate increases.
E) none of these

10) Which of the following is the definition for the real supply of money?
A) The stock of money measured in terms of goods, not dollars.
B) The stock of high powered money only.
C) The real value of currency in circulation only.
D) The actual quantity of money, rather than the officially reported quantity.
E) The ratio of the real GDP to the nominal money supply.

11) Suppose the economy is currently operating on both the LM curve and the IS curve. Which of the following is true for this economy?
A) Production equals demand.
B) The quantity supplied of bonds equals the quantity demanded of bonds.
C) The money supply equals money demand.
D) Financial markets are in equilibrium.
E) all of these

12) Suppose the economy is operating on the LM curve but not on the IS curve. Given

this information, we know that
A) the goods market is in equilibrium and the money market is not in equilibrium.
B) the money market and bond markets are in equilibrium and the goods market is not in equilibrium.
C) the money market and goods market are in equilibrium and the bond market is not in equilibrium.
D) the money, bond and goods markets are all in equilibrium.
E) neither the money, bond, nor goods markets are in equilibrium.

13) An increase in consumer confidence will tend to cause which of the following to occur?
A) a rightward shift in the IS curve
B) a leftward shift in the IS curve
C) an upward shift in the LM curve
D) a downward shift in the LM curve

14) In our standard IS-LM model, assume that investment does *not* depend on the interest rate. A reduction in the money supply will cause which of the following for this economy?
A) no change in the interest rate
B) no change in output
C) a reduction in investment
D) an increase in investment

15) In the model with commercial banks and the central bank, an increase in the reserve deposit ratio, θ, will most likely have which of the following effects?
A) a rightward shift in the IS curve
B) a leftward shift in the IS curve
C) an upward shift in the LM curve
D) a downward shift in the LM curve

16) A Fed purchase of securities will most likely have which of the following effects?
A) a rightward shift in the IS curve
B) a leftward shift in the IS curve
C) an upward shift in the LM curve
D) a downward shift in the LM curve

17) Given same real GDP Y, an increase in the aggregate price level, P, will most likely have which of the following effects?
A) a rightward shift in the IS curve
B) a leftward shift in the IS curve
C) an upward shift in the LM curve
D) a downward shift in the LM curve

18) The IS curve will *not* shift when which of the following occurs?
A) a reduction in government spending
B) a reduction in the interest rate
C) a reduction in consumer confidence
D) all of these
E) none of these

19) Which of the following best defines the IS curve?
A) the combinations of i and Y that maintain equilibrium in the goods market
B) illustrates the effects of changes in i on investment
C) illustrates the effects of changes in i on desired money holdings by individuals
D) the combinations of i and Y that maintain equilibrium in financial markets

20) Which of the following best defines the LM curve?
A) the combinations of i and Y that maintain equilibrium in the goods market
B) illustrates the effects of changes in i on investment
C) illustrates the effects of changes in i on desired money holdings by individuals
D) the combinations of i and Y that maintain equilibrium in financial markets

21) Based on our understanding of the IS-LM model that takes into account dynamics, we know that a reduction in the money supply will cause
A) an immediate drop in Y and immediate increase in i.
B) an immediate increase in i and no initial change in Y.
C) a gradual increase in i and gradual reduction in Y.
D) none of these

22) Based on our understanding of the IS-LM model that takes into account dynamics, we know that a reduction in government spending will cause
A) an immediate drop in Y and immediate increase in i.
B) an immediate reduction in i and no initial change in Y.
C) a gradual reduction in i and gradual reduction in Y.
D) a gradual reduction in i and an immediate reduction in Y.

23) Suppose there is a simultaneous fiscal expansion and monetary expansion. We know with certainty that
A) output will increase.
B) output will decrease.
C) the interest rate will increase.
D) the interest rate will decrease.
E) both output and the interest rate will increase.

24) Suppose there is a simultaneous fiscal expansion and monetary contraction. We know with certainty that
A) output will increase.

B) output will decrease.
C) the interest rate will increase.
D) the interest rate will decrease.
E) both output and the interest rate will increase.

25) Suppose there is a simultaneous central bank purchase of bonds and increase in taxes. We know with certainty that this combination of policies must cause
A) an increase in the interest rate (i).
B) a reduction in i.
C) an increase in output (Y).
D) a reduction in Y.

Lecture 3

(Please note that these solutions are provided as suggestions and may not be error-free. I encourage you to engage in discussions, compare your answers with peers, and feel free to ask questions if you find any typos or mistakes. Learning requires practice, and your attempts will contribute to a better understanding of the material.)

1) D
2) B
3) A
4) B
5) B
6) C
7) E
8) E
9) A
10) A
11) E
12) B
13) A
14) B
15) C
16) D
17) C
18) B
19) A
20) D
21) B
22) C
23) A
24) C
25) B

Lecture 4

1) Which of the following best defines the real interest rate (r)?
A) the amount of goods we must give up next year in order to consume more goods today
B) the amount of dollars we must give up next year in order to consume more goods today
C) the amount of dollars we must give up next year in order to have more dollars today
D) the amount of dollars we must give up today in order to have more dollars next year
E) the amount of dollars we must give up today in order to consume more goods today

2) The nominal interest rate is
A) the interest rate measured in terms of goods.
B) always less than the real interest rate.
C) equal to the real interest rate minus the rate of inflation.
D) the type of interest rate typically reported in the financial pages of newspapers.
E) equal to the expected rate of inflation.

3) If the nominal interest rate 8% and expected inflation 3%, the expected real interest rate in year t is approximately
A) 2%.
B) 3%.
C) 5%.
D) 8%.
E) 11%.

4) Suppose that the nominal interest rate increases while the expected inflation rate rises. Given this information, we know with certainty that the real interest rate
A) will not change.
B) will fall.
C) will fall, but only if the increase in the nominal rate is smaller than the increase in expected inflation.
D) will fall, but only if the increase in the nominal rate is greater than the increase in expected inflation.
E) none of these

5) If the expected inflation rate is negative, the expected real interest rate must be
A) negative.
B) less than the nominal interest rate.
C) equal to the nominal interest rate.
D) greater than the nominal interest rate.
E) none of these

6) Data on real and nominal interest rates of one-year U.S. T-Bills show that, over the

past twenty years,
A) the nominal rate has always been less than the real rate.
B) whenever the nominal rate rises, the real rate falls, and vice versa.
C) the nominal rate has varied, but the real rate has not.
D) the real rate has varied, but the nominal rate has not.
E) the real rate has always been less than the nominal rate.

7) When individuals make decisions about how much money and bonds to hold, which of the following variables affects those decisions?
A) the real interest rate only
B) the nominal interest rate only
C) the expected inflation rate only
D) either the real interest rate or the expected inflation rate
E) both the nominal and real interest rates

8) (Think about the extended IS-LM model) Suppose that the nominal interest rate and expected inflation both decrease by 2%. Given this information, we would expect which of the following to occur?
A) an increase in the real interest rate
B) a reduction in the real interest rate
C) a reduction in investment
D) an increase in money demand
E) an increase in the real interest rate and a reduction in investment

9) The risk that interest payments will not be made, or that the face value of a bond is not repaid when a bond matures is
A) interest rate risk.
B) inflation risk.
C) liquidity risk.
D) default risk.

10) Which of the following bonds are considered to be default-risk free?
A) municipal bonds
B) investment-grade bonds
C) U.S. Treasury bonds
D) junk bonds

11) The spread between the interest rates on bonds with default risk and default-free bonds is called the
A) risk premium.
B) junk margin.
C) bond margin.
D) default premium.

12) Which of the following long-term bonds has the highest interest rate?
A) corporate BBB bonds
B) U.S. Treasury bonds
C) corporate AAA bonds

13) Risk premiums on corporate bonds tend to _____ during business cycle expansions and _____ during recessions, everything else held constant.
A) increase; increase
B) increase; decrease
C) decrease; increase
D) decrease; decrease

14) Which of the following statements are *true*?
A) A bank's assets are its sources of funds.
B) A bank's liabilities are its uses of funds.
C) A bank's balance sheet shows that total assets equal total liabilities plus equity capital.
D) A bank's balance sheet indicates whether or not the bank is profitable.

15) The leverage ratio is the ratio of a bank's
A) assets divided by its liabilities.
B) income divided by its assets.
C) assets divided by capital.
D) capital divided by its total liabilities.

16) The capital ratio is the ratio of a bank's
A) assets divided by its liabilities.
B) income divided by its assets.
C) capital divided by its assets.
D) capital divided by its total liabilities.

17) Channeling funds from individuals with surplus funds to those desiring funds when the saver does not purchase the borrower's security is known as
A) barter.
B) redistribution.
C) financial intermediation.
D) taxation.

18) Securitization is a process of asset transformation that involves a number of different financial institutions working together. These financial institutions are known collectively as the
A) transformers.
B) amalgamation.
C) movers and shakers.
D) shadow banking system.

19) A bank is insolvent when
A) its liabilities exceed its assets.
B) its assets exceed its liabilities.
C) its capital exceeds its liabilities.
D) its assets increase in value.

20) The new term introduced in the extended IS-LM model is
A) risk premium.
B) nominal interest rate.
C) taxes.
D) G.

21) When x increases
A) IS curve shifts to the left.
B) IS curve shifts to the right.
C) LM curve shifts upward.
D) LM curve shifts downward.

22) When x increases leading decrease in output, a better policy tool is
A) decrease in policy rate.
B) increase in policy rate.
C) increase in government spending.
D) decrease in government spending.

23) Given the zero lower bound on the nominal rate, the lowest real interest rate the central bank can achieve is
A) $-\pi^e$
B) π^e
C) 0.
D) i.

24) Suppose bank A has assets of 100, liabilities of 80, and capital of 20. Its capital ratio is
A) 20%.
B) 25%.
C) 11%.
D) 10%.

25) Suppose bank A has assets of 100, liabilities of 80, and capital of 20. Its leverage ratio is
A) 4.

B) 5.
C) 10.
D) 9.

26) Firms with _____ ratings are considered the safest.
A) AAA
B) BBB
C) CCC
D) BB

Lecture 4

(Please note that these solutions are provided as suggestions and may not be error-free. I encourage you to engage in discussions, compare your answers with peers, and feel free to ask questions if you find any typos or mistakes. Learning requires practice, and your attempts will contribute to a better understanding of the material.)

1) A
2) D
3) C
4) C
5) D
6) E
7) B
8) D
9) D
10) C
11) A
12) A
13) C
14) C
15) C
16) C
17) C
18) D
19) A
20) A
21) A
22) A
23) A
24) A
25) B
26) A

Lecture 5

1) Which of the following is considered out of the labor force?
A) the unemployed
B) those temporarily laid off who will soon be recalled
C) those who worked full time, but in a family business
D) those individuals who have started searching for employment for the first time
E) none of these

The non-institutional civilian population is 250 million, of which 100 million are employed and 10 million are unemployed.
2) Based on the information above, the unemployment rate is
A) 4%.
B) 6.6%.
C) 9.1%.
D) 10%.
E) 11.1%.

3) Based on the information above, the labor force participation rate is
A) 36%.
B) 40%.
C) 44%.
D) 90.1%.
E) 66%.

4) Based on the data provided in the Lecture Slides, which of the following represents the largest component of the labor force?
A) discouraged workers
B) retired individuals
C) employed
D) unemployed

5) The labor force is defined as
A) the sum of the employed and unemployed.
B) the total number employed.
C) the total number of working age individuals in the population.
D) the sum of the number of employed, unemployed and discouraged individuals.

6) A reduction in the unemployment rate will tend to cause which of the following?
A) an increase in the separation rate
B) a reduction in the nominal wage
C) a reduction in the duration that one is unemployed
D) none of these

7) When the unemployment rate is low, we would expect that
A) the probability of losing a job is high.
B) the probability of losing a job is low.
C) the probability an unemployed individual will find another job is low.
D) the separation rate will increase.

8) Which of the following variables is most directly determined in the labor market?
A) stock prices
B) nominal wages
C) interest rates
D) all of these
E) none of these

9) The reservation wage is
A) the wage that an employer must pay workers to reduce turnover to a reasonable level.
B) the wage that ensures a laid-off individual will wait for re-hire, rather than find another job.
C) the lowest wage firms are allowed by law to pay workers.
D) the wage offer that will end a labor-strike.
E) none of these

10) Efficiency wage theory suggests that
A) workers will be paid less than their reservation wage.
B) productivity might drop if the wage rate is too low.
C) the government can only set tax rates so high before people will prefer not to work.
D) unskilled workers will have a lower turnover rate than skilled workers.
E) firms will be more resistant to wage increases as the labor market tightens.

11) In the wage-setting relation, the nominal wage tends to decrease when
A) the price level increases.
B) the unemployment rate decreases.
C) unemployment benefits decrease.
D) the minimum wage increases.
E) all of these

12) The price setting equation is represented by the following: $P = (1 + m)W$. When there is perfect competition, we know that m will equal
A) W.
B) P.
C) 1.
D) W/P.
E) none of these

13) The natural level of output is the level of output that occurs when
A) the goods market and financial markets are in equilibrium.
B) the economy is operating at the unemployment rate consistent with both the wage-setting and price-setting equations.
C) the markup (m) is zero.
D) the unemployment rate is zero.
E) there are no discouraged workers in the economy.

14) Suppose we wish to examine the determinants of the equilibrium real wage and equilibrium level of employment (N). In a graph with the real wage on the vertical axis, and the level of employment on the horizontal axis, the price-setting relation will now be
A) a vertical line.
B) a horizontal line.
C) an upward sloping line.
D) a downward sloping line.
E) kinked at the natural rate of unemployment.

15) Suppose we wish to examine the determinants of the equilibrium real wage and equilibrium level of employment (N). In a graph with the real wage on the vertical axis, and the level of employment on the horizontal axis, the wage-setting relation will now be
A) a vertical line.
B) a horizontal line.
C) an upward sloping line.
D) a downward sloping line.
E) a curve that first slopes upward, then downward.

16) With the real wage on the vertical axis and the unemployment rate on the horizontal axis, we know that
A) the WS curve is upward sloping.
B) the WS curve is downward sloping.
C) the PS curve is upward sloping.
D) the PS curve is downward sloping.

17) The natural level of employment (N) will increase when which of the following occurs?
A) an increase in the markup of prices over costs
B) a reduction in unemployment benefits
C) an increase in the actual unemployment rate
D) all of these
E) none of these

18) Suppose the aggregate production function is given by the following: Y = AN. Given this information, we know that labor productivity is represented by which of the following?
A) 1/A
B) A
C) 1/N
D) N/Y

19) Suppose the aggregate production function is given by the following: Y = N. Given this information, we know that labor productivity is represented by which of the following?
A) 1/N
B) N
C) N/Y
D) 1

20) An increase in the minimum wage will tend to cause which of the following?
A) an upward shift in the WS curve
B) a downward shift in the WS curve
C) an upward shift in the PS curve
D) a downward shift in the PS curve
E) none of these

21) Suppose that increased international trade makes product markets more competitive in the U.S. Given this information, we would expect to observe which of the following?
A) an upward shift in the WS curve
B) a downward shift in the WS curve
C) an upward shift in the PS curve
D) a downward shift in the PS curve
E) none of these

22) Based on our understanding of the labor market model presented in Lecture 5, we know that an increase in the minimum wage will cause
A) an increase in the equilibrium real wage.
B) a reduction in the equilibrium real wage.
C) a reduction in the natural rate of unemployment.
D) a reduction in the equilibrium real wage and natural rate of unemployment
E) no change in the equilibrium real wage.

23) Based on wage setting behavior, we know that an increase in the unemployment rate will cause
A) no change in the real wage.
B) a reduction in the real wage.
C) an increase in the real wage.
D) an upward shift of the WS curve.

Lecture 5

(Please note that these solutions are provided as suggestions and may not be error-free. I encourage you to engage in discussions, compare your answers with peers, and feel free to ask questions if you find any typos or mistakes. Learning requires practice, and your attempts will contribute to a better understanding of the material.)

1) E
2) C
3) C
4) C
5) A
6) C
7) B
8) B
9) E
10) B
11) C
12) E
13) B
14) B
15) C
16) B
17) B
18) B
19) D
20) A
21) C
22) E
23) B

Lecture 6

1) In the Phillips curve equation, which of the following will cause an increase in the current inflation rate?
A) an increase in the expected inflation rate
B) a reduction in the unemployment rate
C) an increase in the markup, m
D) all of these
E) none of these

2) Which of the following individuals *first* discovered the relationship between unemployment and inflation?
A) Solow
B) Samuelson
C) Friedman
D) Phillips

3) Since approximately 1970, the Phillips-type relationship for the United States has been between which of the following?
A) the rate of inflation and the change in the unemployment rate
B) the unemployment rate and the change in the rate of inflation
C) the change in the unemployment rate and the change in the rate of inflation
D) the inverse of the unemployment rate and the rate of inflation
E) the unemployment rate and the rate of inflation

4) Which of the following assumptions best characterized the assumption about how individuals formed expectations of inflation by the early 1970s?
A) Expected inflation for the current year was smaller than the previous year's inflation rate.
B) Expected inflation for the current year was approximately equal to the previous year's inflation rate.
C) Expected inflation for the current year was less than the previous year's inflation rate.
D) Expected inflation for the current year equal to the average inflation rate over the past five years.
E) Expected inflation for the current year equal to the average inflation rate over the past ten years.

5) When inflation has been persistent, as was the case in the United States during the 1970s, low unemployment rates will likely be associated with
A) low natural rates of unemployment.
B) high natural rates of unemployment.
C) low but stable rates of inflation.
D) high but stable rates of inflation.

E) increases in the inflation rate.

6) For this question, assume that individuals form expectations of inflation according to the following equation $\pi et = \theta \pi t\text{-}1$. From 1970 on, the value of θ for this equation
A) increased over time and approached 1.
B) decreased over time and approached zero.
C) remained constant at zero.
D) remained constant at negative one.
E) none of these

7) For this question, assume that the expected rate of inflation is a function of past year's inflation. Also assume that the unemployment rate has greater than the natural rate of unemployment for a number of years. Given this information, we know that
A) the rate of inflation will approximately be equal to zero.
B) the rate of inflation should neither increase nor decrease.
C) the rate of inflation should steadily increase over time.
D) the rate of inflation should steadily decrease.
E) the inflation rate will be approximately equal to the natural rate of unemployment.

8) For this question, assume that the Phillips curve equation is represented by the following: $\pi_t - \pi_t^e = (m + z) - \alpha u_t$. Which of the following will cause a reduction in the natural rate of unemployment?
A) an increase in m
B) an increase in z
C) an increase in α
D) an increase in actual inflation
E) an increase in expected inflation

9) For this question, assume that the Phillips curve equation is represented by the following: $\pi_t - \pi_t^e = (m + z) - \alpha u_t$. Which of the following will *not* cause an increase in the natural rate of unemployment?
A) a reduction in m
B) a reduction in z
C) an increase in α
D) an increase in the expected rate of inflation
E) all of these

10) In which of the following decades did the original Phillips curve break down for the U.S.?
A) 1940s
B) 1950s
C) 1960s

D) none of these

11) Assume that expected inflation is based on the following: $\pi_t^e = \theta\pi_{t-1}$. An increase in θ will cause
A) an increase in the natural rate of unemployment.
B) a reduction in the natural rate of unemployment.
C) no change in the natural rate of unemployment.
D) inflation in period t to be more responsive to changes in unemployment in period t.

12) Assume that expected inflation is based on the following: $\pi_t^e = \theta\pi_{t-1}$. If θ = 0, we know that
A) a reduction in the unemployment rate will have no effect on inflation.
B) low rates of unemployment will cause steadily increasing rates of inflation.
C) high rates of unemployment will cause steadily declining rates of inflation.
D) the Phillips curve illustrates the relationship between the level of inflation rate and the level of the unemployment rate.

13) Assume that expected inflation is based on the following: $\pi_t^e = \theta\pi_{t-1}$. If θ = 1, we know that
A) a reduction in the unemployment rate will have no effect on inflation.
B) low rates of unemployment will cause steadily increasing rates of inflation.
C) the actual unemployment rate will not deviate from the natural rate of unemployment.
D) the Phillips curve illustrates the relationship between the level of inflation rate and the level of the unemployment rate.

14) Suppose when there is an increase in the price of oil, firms tend to increase their markups and charge higher prices given same labor costs. An increase in the price of oil will likely cause which of the following?
A) increase the markup in the Phillips curve equation
B) increase the sum "m + z" in the Phillips curve equation
C) increase the natural rate of unemployment
D) all of these
E) none of these

15) Suppose the Phillips curve is represented by the following equation: $\pi_t - \pi_t^e = 0.2 - 2u_t$. Given this information, we know that the natural rate of unemployment in this economy is
A) 10%.
B) 20%.
C) 6.5%.
D) 5%.
E) none of these

16) Which of the following explains why the original Phillips curve relation

disappeared or, as some economists have remarked, "broke down" in the 1970s?
A) Individuals assumed the expected price level for the current year would be equal to the actual price level from the previous year.
B) Individuals assumed that expected inflation would be zero
C) Individuals changed the way they formed expectations of inflation.
D) Monetary policy became contractionary.
E) More labor contracts became indexed to changes in inflation.

17) Which of the following situations generally exists when deflation occurs?
A) Inflation and unemployment are both increasing.
B) Inflation and unemployment are both decreasing.
C) The price level is decreasing.
D) The rate of inflation is falling from, for example, 10% to 3%.
E) The natural rate of unemployment is zero.

18) In the Phillips curve equation, which of the following will cause a reduction in the current inflation rate?
A) a reduction in the expected inflation rate
B) an increase in the unemployment rate
C) a reduction in the markup, m
D) all of these
E) none of these

Lecture 6

(Please note that these solutions are provided as suggestions and may not be error-free. I encourage you to engage in discussions, compare your answers with peers, and feel free to ask questions if you find any typos or mistakes. Learning requires practice, and your attempts will contribute to a better understanding of the material.)

1) D
2) D
3) B
4) B
5) E
6) A
7) D
8) C
9) D
10) D
11) C
12) D
13) B
14) D
15) A
16) C
17) C
18) D