

Practice Problems (Topics 6,7)

Answers are shown in bold.

1. Real GDP is nominal GDP adjusted for:
 - A) double counting.
 - B) changes in prices.**
 - C) population.
 - D) imports
2. An example of a government transfer is a(n):
 - A) expenditure on an interstate highway.
 - B) bequest from a deceased relative.
 - C) Social Security payment.**
 - D) salary for a member of the armed forces.
3. Real GDP is measured in ____ prices while nominal GDP is measured in ____ prices.
 - A) foreign, domestic
 - B) base year, current year**
 - C) current year, base year
 - D) intermediate, final
4. Anticipated inflation affects:
 - A) borrowers only.
 - B) lenders only.
 - C) all aspects of the economy.**
 - D) only business firms involved in investment spending

Scenario: Real GDP (For questions 5 and 6)

Suppose that in year 1 an economy produces 100 golf balls that sell for \$3 each and 75 pizzas that sell for \$8 each. The next year the economy produces 110 golf balls that sell for \$3.25 each and 80 pizzas that sell for \$9 each.

5. Using year 1 as the base year, real GDP in year 2 is:
- A) \$900.
 - B) \$970.**
 - C) \$1,000.
 - D) \$1,077.50.
6. The value of nominal GDP in years 1 and 2 respectively is:
- A) \$900; \$1,077.50.**
 - B) \$900; \$990.
 - C) \$180,000; \$257,400.
 - D) \$1,000; \$1,005.
7. Which of the following do economists view as investment spending?
- A) stocks
 - B) bonds
 - C) spending on physical capital**
 - D) mutual fund investing
8. Enchante Inc., a designer clothing company, buys \$400 worth of silk from a silk trader and \$30 worth of accessories from AccessoriesRuS to produce each dress. If the value added by Enchante is equal to \$200, then according to the value-added approach, the price of the designer dress should be:
- A) \$630.**
 - B) \$230.
 - C) \$200.
 - D) \$830.
9. Suppose that aggregate consumption is \$1,000,000, aggregate investment is \$200,000, government spending is \$300,000, the value of exports is \$100,000, and the value of imports is \$200,000. What is the value of Gross Domestic Product (GDP)?
- A) \$1,800,000
 - B) \$1,500,000
 - C) \$1,400,000**
 - D) \$1,700,000

10. Kelly goes to the grocery store to make her monthly purchase of ginger ale. As she enters the soft drink section, she notices that the price of ginger ale has increased 15 percent, so she decides to buy some peppermint tea instead. To which problem in the construction of the CPI is this situation most relevant?
- A) **substitution bias**
 - B) introduction of new goods
 - C) unmeasured quality change
 - D) income effect
11. A worker received \$5 for a daily wage in 1930. What is the value of that wage today if the CPI was 17 in 1930 and is 230 today?
- A) 37 cents
 - B) \$4.63
 - C) **\$67.65**
 - D) \$37.86
12. If a timber yard sells \$1,000 of timber to a carpenter and the carpenter uses the timber to build a garage which he sells for \$5,000, the contribution to GDP is
- A) \$4000.
 - B) **\$5000.**
 - C) \$6000.
 - D) None of the above.
13. If nominal GDP in 2005 exceeds nominal GDP in 2004, real output **must** have risen.
- A) True
 - B) **False**
 - C) Not enough information.
 - D) Must have stayed the same.
14. Gross Domestic Product can be measured as the sum of
- A) final goods and services, intermediate goods, transfer payments, and rent.
 - B) **consumption, investment, government purchases, and net exports.**
 - C) consumption, transfer payments, wages, and profits.

D)Net National Product, Gross National Product, and Disposable personal income.

15. Suppose that aggregate consumption is \$1,000,000, aggregate investment is \$200,000, government spending is \$300,000, the value of exports is \$100,000, and the value of imports is \$200,000. What is the value of Gross Domestic Product (GDP)?

A)\$1,800,000

B)\$1,500,000

C)\$1,400,000

D)\$1,700,000

16. GDP would include which of the following?

A)the value of taking a day off from work

B)consulting services

C)intermediate sales

D)illegal drug sales

The following table contains information about an economy that produces only pens and books. The base year is 2003.

Year	Price of pens	Quantity of pens	Price of books	Quantity of books
2003	€3	100	€10	50
2004	3	120	12	70
2005	4	120	14	70

17. What is the value of real GDP for 2004?

A)€800

B)€1,060

C)€1,460

D)€1,200

18. How is your purchase of a \$40,000 BMW automobile that was produced entirely in Germany recorded in the US GDP accounts?

A)Consumption increases by \$40,000 and net exports decreases by \$40,000.

B)Net exports increases by \$40,000.

C)There is no impact because this transaction does not involve domestic production.

D)Investment increases by €40,000 and net exports increases by \$40,000.

19. In 1989, the CPI was 124.0. In 1990, it was 130.7. What was the rate of inflation over this period?
- A) **5.4 percent**
 - B) 30.7 percent
 - C) You can't tell without knowing the base year.
 - D) 8.1 percent
20. Which of the following would probably cause the CPI to rise more than the GDP deflator in the US?
- A) **An increase in the price of BMWs produced in Germany and sold in the US.**
 - B) An increase in the price of Peugeots produced in the US.
 - C) An increase in the price of helicopters purchased by the Royal Navy.
 - D) An increase in the price of domestically produced armored vehicles sold exclusively to India.