

PRACTICE TEST #2 – Please note that this test covers chapters 5 to 10. The following questions are from chapters 5 and 6 (prepare for similar questions on your first test).

MC – 1,3,4,6,9,11,12,15,18,23,24,29,30

SA – 1,2

ECONOMICS 1BB3
Introductory Macroeconomics
Sections C02, C03, C04

Term Test #2
March 13, 2010
9:00am

This examination paper includes 11 pages including the title page and 43 questions. You are responsible for ensuring that your copy of the paper is complete. Please bring any discrepancy to the attention of your invigilator.

Special Instructions:

Only the McMaster Standard (Casio - FX991) Calculator may be used. This test paper must be returned along with the scan sheet. Write your name and student number on the test paper and the scan sheet. If you are writing in the wrong room, you will lose 5 points off your test score. If you are wearing a baseball cap, please turn it so the peak is in the back. Please turn off all cell phones. There should be no electronic devices at your seat other than a calculator. All books and bags must be left at the front of the room. You will need your student ID card at your desk, along with your calculator, a pencil, and a pen. If you complete the short answer section in pencil your test will not be re-graded if there is a dispute. Use an HB pencil to fill in the scan sheet. If a TA has to grade your scan sheet by hand, you will lose 5 points off your test score. You cannot fill in the version number of your test paper on the scan sheet.

Part A: Multiple Choice Questions: There are 40 multiple choice questions. Please record your answers on the scan answer sheet provided.

Part B: Short Answer Questions: There are 3 short answer questions. Please record your answers on the test paper.

Part A – Multiple Choice	/40
Part B – Short Answer	/15
Total	/55

OMR EXAMINATION - STUDENT INSTRUCTIONS

NOTE: IT IS YOUR RESPONSIBILITY TO ENSURE THAT THE ANSWER SHEET IS PROPERLY COMPLETED: YOUR EXAMINATION RESULT DEPENDS UPON PROPER ATTENTION TO THESE INSTRUCTIONS.

The scanner, which reads the sheets, senses the shaded areas by their non-reflection of light. A heavy mark must be made, completely filling the circular bubble, with a HB pencil. Marks made with a pen or felt-tip marker will **NOT** be sensed. Erasures must be through or the scanner may still sense a mark. Do **NOT** use correction fluid on the sheets. Do **NOT** put any unnecessary marks or writing on the sheets.

1. Print your name, student number, course name, section number and the date in the space provided at the top of Side 1 (red side) of the form.
2. Mark your student number in the space provided on the sheet on Side 1 and fill in the corresponding bubbles underneath.
3. Mark only ONE choice from the alternatives (1,2,3,4,5, or A,B,C,D,E) provided for each question. If there is a True/False question, enter response of 1 (or A) as True, and 2 (or B) as False. The question number is to the left of the bubbles. Make sure that the number of the question on the scan sheet is the same as the question number on the test paper.
4. Pay particular attention to the Marking Directions on the form.
5. Begin answering questions using the first set of bubbles, marked "1".

Part A - Multiple Choice (40 points)

Identify the choice that best completes the statement or answers the question. Answer on the scan sheet provided.

1. In an economy consisting of only households and firms, GDP can be computed by
 - a. adding up the total expenditures of households.
 - b. adding up the total income paid by firms.
 - c. Either a or b are correct.
 - d. None of the above are correct.
2. Cyclical unemployment refers to
 - a. the relation between the probability of unemployment and a worker's changing level of experience.
 - b. year-to-year fluctuations of unemployment around its natural rate.
 - c. how often a worker is likely to be employed during her lifetime.
 - d. long-term trends in unemployment.
 - e. None of the above are correct.

Table 24-5

The table below pertains to an economy with only two goods -- books and calculators. The fixed basket consists of 5 book and 10 calculators.

Year	Price of Books	Price of Calculators
2005	\$24	\$8
2006	\$30	\$12
2007	\$32	\$15

3. **Refer to Table 24-5.** Using 2006 as the base year, the consumer price index is
 - a. 200 in 2005, 270 in 2006, and 310 in 2007
 - b. 100 in 2005, 135 in 2006, and 155 in 2007
 - c. 74.07 in 2005, 100 in 2006, and 114.81 in 2007
 - d. 78.22 in 2005, 100 in 2006, and 121.10 in 2007
 - e. None of the above is correct.
4. Suppose GDP consists of wheat and rice. In 2006, 20 bushels of wheat are sold at \$4 per bushel, and 10 bushels of rice are sold at \$2 per bushel. If the price of wheat was \$2 per bushel and the price of rice was \$1 per bushel in 2001, the base year, nominal 2006 GDP is
 - a. \$40, real 2006 GDP is \$100, and the GDP deflator is 50.
 - b. \$50, real 2006 GDP is \$100, and the GDP deflator is 200.
 - c. \$100, real 2006 GDP is \$50, and the GDP deflator is 200.
 - d. \$100, real 2006 GDP is \$50, and the GDP deflator is 50.
5. Human capital is the
 - a. knowledge and skills that workers acquire through education, training, and experience.
 - b. total number of hours worked in an economy.
 - c. stock of equipment and structures that is used to produce goods and services.
 - d. same thing as technological knowledge.

6. When the relative price of a good increases, consumers will respond by buying
 - a. less of it and more of its substitutes.
 - b. more of it and its substitutes.
 - c. more of it and less of its substitutes.
 - d. less of it and its substitutes.
7. Which of the following is correct?
 - a. Banks charge borrowers a slightly lower interest rate than they pay to depositors.
 - b. Stocks, bonds, and deposits are all similar in that each provides a medium of exchange
 - c. Banks lend mostly to large and familiar companies rather than smaller local firms.
 - d. None of the above are correct.
8. Unemployment compensation is
 - a. part of GDP because the recipients must have worked in the past to qualify.
 - b. not part of GDP because it is a transfer payment.
 - c. part of GDP because it represents income.
 - d. not part of GDP because the payments reduce business profits.
9. If Canadian GDP in the fourth quarter is \$10 trillion dollars, then
 - a. to find the amount actually produced in that quarter we would have to divide by four because GDP is reported at annual rates.
 - b. this number reflects the actual amount of final goods and services produced in the fourth quarter.
 - c. the amount actually produced in the fourth quarter is somewhat higher because GDP is seasonally adjusted and nonseasonally adjusted GDP for the fourth quarter is typically higher.
 - d. to find the amount actually produced in that quarter would require both dividing it by about four and then adding back in what had been removed for seasonal adjustment.
 - e. None of the above is correct.
10. Suppose a country has a consumption tax that is similar to a provincial sales tax. If its government eliminates the consumption tax and replaces it with an income tax that includes an income tax on interest from savings, what happens?
 - a. The interest rate increases and saving decreases.
 - b. There is no change in the interest rate or saving.
 - c. The interest rate decreases and saving increases.
 - d. None of the above are correct.
11. When the quality of a good improves the purchasing power of the dollar
 - a. increases, so the CPI understates the change in the cost of living if the quality change is not accounted for.
 - b. decreases, so the CPI understates the change in the cost of living if the quality change is not accounted for.
 - c. decreases, so the CPI overstates the change in the cost of living if the quality change is not accounted for.
 - d. increases, so the CPI overstates the change in the cost of living if the quality change is not accounted for.

12. The GDP deflator is the ratio of
 - a. real GDP to nominal GDP.
 - b. real GDP to nominal GDP multiplied by 100.
 - c. nominal GDP to real GDP.
 - d. nominal GDP to real GDP multiplied by 100.
13. Which list ranks assets from most to least liquid?
 - a. fine art, currency, stocks
 - b. fine art, stocks, currency
 - c. currency, stocks, fine art
 - d. currency, fine art, stocks
14. The slope of the demand for loanable funds curve represents the
 - a. negative relation between the real interest rate and saving.
 - b. positive relation between the real interest rate and investment.
 - c. positive relation between the real interest rate and saving.
 - d. negative relation between the real interest rate and investment.
15. If a country reported a nominal GDP of 85 billion in 2007 and 100 billion in 2006 and reported a GDP deflator of 100 in 2007 and of 105 in 2006, then from 2006 to 2007 real output
 - a. and prices both fell.
 - b. rose and prices fell.
 - c. and prices both rose.
 - d. fell and prices rose.
16. All else equal, which of the following would tend to cause GDP per person to rise?
 - a. rapid growth in the number of workers
 - b. high population growth
 - c. investment in human capital
 - d. All of the above are correct.
17. If the reserve ratio is 10 percent, banks do not hold excess reserves, and people do not hold currency, then when Bank of Canada purchases \$20 million of government bonds, bank reserves
 - a. increase by \$20 million and the money supply eventually decreases by \$200 million.
 - b. decrease by \$20 million and the money supply eventually decreases by \$200 million.
 - c. decrease by \$20 million and the money supply eventually increases by \$200 million.
 - d. increase by \$20 million and the money supply eventually increases by \$200 million.
18. Which of the problems in the construction of the CPI is the creation of the mobile phone most relevant to?
 - a. income bias
 - b. substitution bias
 - c. introduction of new goods
 - d. unmeasured quality change

19. Efficiency wages
 - a. increase worker turnover.
 - b. reduce the incentive to shirk.
 - c. reduce the natural rate of unemployment.
 - d. reduce labour-force participation rates.
 - e. None of the above are correct.

Use the balance sheet for the following questions.

Table 29-3

<u>Last Bank of Cedar Bend</u>			
Assets		Liabilities	
Reserves	\$25,000	Deposits	\$180,000
Loans	\$155,000		

20. **Refer to Table 29-3.** If the reserve requirement is 30 percent, this bank
 - a. has \$29,000 of excess reserves.
 - b. needs \$29,000 more of reserves to meet its reserve requirements.
 - c. just meets its reserve requirement.
 - d. needs \$10,000 more of reserves to meet its reserve requirements.
21. The labour-force participation rate is defined as
 - a. $(\text{Labor Force} \div \text{Adult Population}) \times 100$.
 - b. $(\text{Adult Population} \div \text{Labor Force}) \times 100$.
 - c. $(\text{Employed} \div \text{Labor Force}) \times 100$.
 - d. $(\text{Employed} \div \text{Adult Population}) \times 100$.
 - e. None of the above are correct.
22. In 2007, Freedonia had a population of 2,700 and real GDP of about 1,080,000. In 2006 it had a population of 2,500 and real GDP of about 1,000,000. What was the approximate growth rate of real GDP per person in Freedonia between 2006 and 2007?
 - a. 7.5 percent
 - b. 2.5 percent
 - c. 10 percent
 - d. 5 percent
 - e. 0 percent
23. When the consumer price index rises, the typical family
 - a. can spend fewer dollars to maintain the same standard of living.
 - b. finds that its standard of living is not affected.
 - c. has to spend more dollars to maintain the same standard of living.
 - d. can offset the effects of rising prices by saving more.

24. In the country of Hyrkania, the CPI in 2005 was 140 and the CPI in 2006 was 154. Jake, a resident of Hyrkania, borrowed money in 2005 and repaid the loan in 2006. If the nominal interest rate on the loan was 14 percent, then the real interest rate was
- impossible to determine without knowing the base year for the CPI.
 - 10 percent.
 - 14 percent.
 - 18 percent.
 - 4 percent.
25. Unemployment insurance
- creates frictional unemployment and unions create structural unemployment.
 - and unions both create frictional unemployment.
 - and unions both create structural unemployment.
 - creates structural unemployment and unions create frictional unemployment.
26. Lucy wants to start her own psychiatric practice, but her expenditures exceed her income. Lucy is a
- borrower who demands money from the financial system.
 - saver who supplies money to the financial system.
 - borrower who supplies money to the financial system.
 - saver who demands money from the financial system.
27. Which of the following might explain why Canada has so much currency per person?
- People use credit and debit cards more frequently.
 - Canadian citizens are holding a lot of foreign currency.
 - Currency may be a preferable store of wealth for criminals.
 - All of the above help explain the abundance of currency.
28. Who would be included in the labour force?
- Homer, an unpaid homemaker
 - Brett, who has become discouraged looking for a job and has quit looking for awhile
 - Derrick, who is waiting for his new job to start
 - None of the above would be included in the labour force.
29. In a simple circular-flow diagram, total income and total expenditures in an economy are
- never equal because some people's income is not for production.
 - equal only if there is no saving.
 - equal because every transaction has a buyer and a seller.
 - equal because firms are ultimately owned by households.
 - none of the above is true
30. In Canada, if the price of imported oil rises so that the price of gasoline and heating oil rise the
- GDP deflator rises much more than does the consumer price index.
 - consumer price index rises much more than does the GDP deflator.
 - consumer price index rises slightly more than does the GDP deflator.
 - GDP deflator and the consumer price index rise by about the same amount.

31. In a closed economy, what does $(T - G)$ represent?
- investment
 - national saving
 - private saving
 - public saving
 - None of the above are correct.
32. Paper money
- is used in a barter economy.
 - is valuable only because of the legal tender requirement.
 - has a high intrinsic value.
 - is valuable because it is generally accepted in trade.
 - All of the above are correct.
33. The relationship between the quantity of output created and the quantity of inputs needed to create it is called
- the capital accumulation function.
 - human capital.
 - the proprietary function.
 - technological knowledge.
 - the production function.
34. The Bank of Canada does all except which of the following?
- control the value of money
 - make loans to individuals
 - control the supply of money
 - regulate the banking system
 - It does all of the above.
35. Discouraged workers
- are not counted either as part of the adult population or as part of the labour force.
 - are counted as part of the adult population, and as unemployed.
 - are counted as part of the adult population, but not as part of the labour force.
 - None the above are correct.
36. If the tax revenue of the federal government exceeds spending, then the government
- will increase taxes.
 - runs a national debt.
 - runs a budget deficit.
 - runs a budget surplus.
37. When a country removes trade barriers and exports pork chops and imports stereos,
- it is essentially transforming pork chops into stereos.
 - its growth slows.
 - its productivity decreases.
 - its economic well-being decreases while that of the country that sells stereos increases.
 - All of the above are correct.

38. Which of the following is a cause of frictional unemployment?
- a. a worker leaving a job to find one with better benefits
 - b. the minimum wage
 - c. labour unions
 - d. All of the above are correct.
39. Suppose that the reserve ratio is 5 percent and that a bank has \$3,000 in deposits. Its required reserves are
- a. \$1,500.
 - b. \$150.
 - c. \$3,000.
 - d. \$50.
 - e. \$500.
40. If Microsoft sells a bond they are
- a. borrowing directly from the public.
 - b. lending directly to the public.
 - c. borrowing indirectly from the public.
 - d. lending indirectly to the public.

Part B - Short Answer (15 points)

Answer on the test paper.

1. Suppose the only two goods produced in Springbreakland are coconut drinks and sarongs. The prices and quantities sold are given in the following table.

	Coconut Drinks		Sarongs	
	Price	Quantity	Price	Quantity
2001	\$5	1000	\$20	100
2002	\$3	1600	\$10	200
2003	\$2	2000	\$10	300

- a) Using 2002 as the base year, calculate nominal GDP and real GDP for each year. **(3 points)**
- b) Calculate the GDP deflator in 2001 and 2002. What is the inflation rate from 2001 to 2002? **(4 points)**

2. Compute how much each of the following is worth in terms of today's dollars using 177 as the price index for today. **(4 points)**
- a) In 1926 the CPI was 17.7 and the price of a movie ticket was \$0.25
- b) In 1932 the CPI was 13.1 and a cook earned \$15.00 a week
3. Describe the two things that limit the precision of the Bank of Canada's control of the money supply and explain how each limits that control. **(4 points)**