



Midterm Examination II

Spring, 2015

Course number: ECON 102
Course title: Introductory Macroeconomics
Section(s): 001 and 002
Name of instructor: Zhen He
Date of exam: July 3rd, 2015
Exam time: 4:30 PM - 6:00 PM
Duration of exam: 1.5 hours
Number of exam pages: 12 pages (includes cover page)
Exam type: Closed book
Material allowed: Standard Calculator
Exams are printed double sided on white paper.

Student name: _____
(First name) (Last name)

Waterloo student ID #: _____

Course Section #: _____

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

1. At the beginning of the year, your wealth is \$10,000. During the year, you have an income of \$90,000 and you spend \$80,000 on consumption goods and services. You pay no taxes. Your wealth at the end of the year is
A) \$100,000. B) \$0. C) \$10,000. D) \$20,000. E) \$90,000.
2. Suppose that a bond promises to pay its holder \$100 a year forever. If the price of the bond increases from \$1,000 to \$1,250, then the interest rate on the bond _____.
A) does not change because the purchaser buys the bond knowing that interest rates will be adjusted
B) falls from 10 percent a year to 8 percent a year
C) falls from 10 percent a year to 6 percent a year
D) rises from 8 percent a year to 10 percent a year
E) rises because the bond becomes a better investment
3. Capital stock increases when
A) gross investment exceeds net investment.
B) net investment is zero.
C) net investment exceeds gross investment.
D) gross investment is negative.
E) net investment is positive.

Refer to the table below to answer the following questions.

Table 23.2.1

Item	Millions of dollars
Consumption expenditure	80
Government expenditure on goods and services	30
Net taxes	35
Investment	20
Imports	10
Exports	20

4. Refer to Table 23.2.1. Private saving is
A) -\$15 million. B) \$80 million. C) \$40 million. D) \$25 million. E) \$20 million.
5. Approximately, the real interest rate _____ the inflation rate _____ the nominal interest rate.
A) minus; equals
B) plus; equals
C) equals; plus
D) times; divided by 100 equals
E) equals; minus
6. A decrease in the real interest rate leads to a _____ the demand for loanable funds curve, and a decrease in expected profit leads to a _____ the demand for loanable funds curve.
A) movement down along; movement up along
B) rightward shift of; leftward shift of
C) movement down along; leftward shift of
D) rightward shift of; movement up along
E) movement down along; rightward shift of

7. All of the following are sources of loanable funds *except*
- A) private saving.
 - B) government budget surplus.
 - C) international borrowing.
 - D) business investment.
 - E) none of the above.
8. If households' disposable income decreases, then
- A) households' saving will decrease.
 - B) households' saving will increase.
 - C) the supply of loanable funds decreases.
 - D) a movement occurs down along the supply of loanable funds curve.
 - E) both A and C are correct.
9. Changes in all of the following *shift* the supply curve of loanable funds *except*
- A) expected future income.
 - B) disposable income.
 - C) default risk.
 - D) the real interest rate.
 - E) wealth.
10. If the real interest rate is below the equilibrium real interest rate,
- A) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate falls.
 - B) a surplus of loanable funds exists.
 - C) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate falls.
 - D) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate rises.
 - E) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate rises.
11. If the Ricardo-Barro effect occurs, _____ in private saving finances the government budget deficit and the real interest rate _____.
- A) a decrease; remains the same
 - B) an increase; rises
 - C) a decrease; increases
 - D) an increase; remains the same
 - E) an increase; falls
12. A very small country is a net foreign lender and its supply of loanable funds increases. As a result, the equilibrium quantity of loanable funds used in the country _____ and the country's foreign lending _____.
- A) increases; does not change
 - B) does not change; increases
 - C) does not change; does not change
 - D) does not change; decreases
 - E) increases; decreases

13. If China's government increases its budget surplus, there is _____ in the supply of loanable funds, private saving _____ and investment _____.
A) an increase; increases; increases
B) a decrease; decreases; increases
C) an increase; decreases; increases
D) an increase; decreases; is crowded out
E) a decrease; increases; increases
14. Loanable funds flow among countries because _____.
A) including differences in risk, the real interest rate is always higher in some countries than in others and this real interest rate differential will not change
B) rational investors want diversified portfolios
C) funds flow into the country with the highest real interest rate and out of the country in which the real interest rate is lowest
D) it creates more stability for domestic businesses to have foreign investors
E) funds flow into the country with the highest nominal interest rate and out of the country in which the nominal interest rate is lowest
15. Which one of the following is *not* a function of money?
A) store of value
B) unit of account
C) measure of liquidity
D) medium of exchange
E) means of payment
16. Which of the following is *not* considered money in Canada today?
A) deposits at banks
B) coins
C) debit cards
D) deposits at credit unions
E) bank of Canada notes
17. During a period of severe inflation, which function of money is most seriously affected?
A) means of payment
B) medium of exchange
C) unit of account
D) store of value
E) none of the above
18. Pooling risk
A) occurs when one person lends to an entire group or pool of borrowers.
B) refers to the lower cost of obtaining funds from a depository institution.
C) refers to a default contract made by a bank to other banks.
D) is now illegal under the Nuisance Act of 2007.
E) refers to spreading the risk of loan default among all the depositors within the depository institution.

19. The Monetary Base consists of the sum of
- A) Bank of Canada notes held within the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks and the public.
 - B) Bank of Canada notes held outside the Bank of Canada, the desired reserves of chartered banks, and coins held by banks.
 - C) Bank of Canada notes held outside the Bank of Canada, bank deposits at the Bank of Canada, and notes and coins held by banks.
 - D) Bank of Canada notes held within the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks.
 - E) Bank of Canada notes held outside the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks and the public.
20. The money creation process begins when
- A) the quantity of money increases.
 - B) banks lend reserves.
 - C) bank deposits increase.
 - D) desired reserves increase because of an increase in deposits.
 - E) banks have excess reserves.
21. Suppose that a country has \$50 billion in bank reserves, \$100 billion in currency held by the public, and \$500 billion in bank deposits. The currency drain ratio is
- A) 18%. B) 30%. C) 20%. D) 10%. E) 50%.
22. The quantity of money that the banking system can create is limited by
- A) the quantity of bank notes released by the Bank of Canada.
 - B) the credit ratings of the consumers who are applying for loans.
 - C) bank managers' decisions.
 - D) the monetary base, desired reserves, and desired currency holdings.
 - E) the number of consumers who apply for loans.
23. The banks on Sunny Island have deposits of \$4 million, reserves of \$600,000, and loans of \$2.4 million. The desired reserve ratio is 10 percent. The banks have _____ of desired reserves and _____ of excess reserves.
- A) \$200,000; \$400,000
 - B) \$200,000; \$600,000
 - C) \$400,000; \$600,000
 - D) \$600,000; \$200,000
 - E) \$400,000; \$200,000
24. If the interest rate is below the equilibrium, how is equilibrium achieved in the money market?
- A) People sell bonds to get rid of their excess money, lowering the price of bonds and raising the interest rate.
 - B) People sell bonds to try and raise more money, lowering the price of bonds and raising the interest rate.
 - C) People buy goods to get rid of their excess money, lowering the price of goods and raising the interest rate.
 - D) People buy bonds to get rid of their excess money, raising the price of bonds and raising the interest rate.
 - E) People sell goods to get rid of their excess money, lowering the price of goods and raising the interest rate.

Use the figure below to answer the following questions.

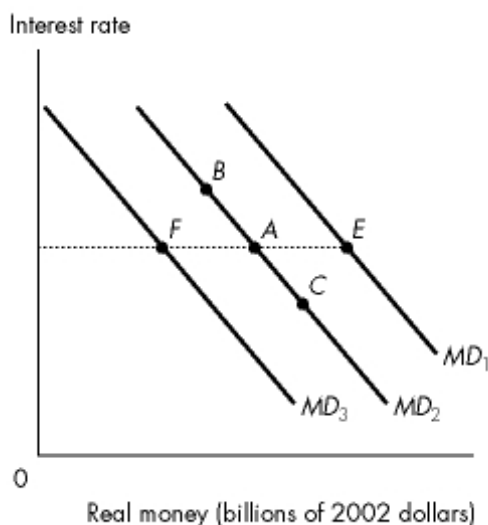


Figure 24.4.2

25. Refer to Figure 24.4.2. Which one of the following best describes the response to a decrease in real GDP?
 - A) A movement from A to B
 - B) A movement from A to E
 - C) A movement from E to A
 - D) A movement from A to C
 - E) A movement from B to C
26. When the nominal interest rate rises, the opportunity cost of holding money _____.
 - A) falls and people hold more money
 - B) rises and people hold more money
 - C) does not change
 - D) falls and people hold less money
 - E) rises and people hold less money
27. Real GDP is \$2,000 billion, the price level is 120, and the velocity of circulation is 5. Nominal GDP is
 - A) \$166.67 billion.
 - B) \$2,400 billion.
 - C) \$2,000 billion.
 - D) \$600 billion.
 - E) \$24 billion.
28. Which of the following will increase the size of the money multiplier?
 - A) a decrease in the desired reserve ratio
 - B) an increase in the currency drain ratio
 - C) a decrease in the currency drain ratio
 - D) an increase in the desired reserve ratio
 - E) either A or C above
29. Suppose that the banking system has excess reserves of \$10 million, the desired reserve ratio is 10 percent and the currency drain ratio is 40 percent. By how much will the quantity of money increase?

A) \$50 million	B) \$22 million	C) \$40 million	D) \$12.5 million	E) \$28 million
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30. The lower the exchange rate, the
- A) smaller is the quantity of Canadian dollars demanded in the foreign exchange market.
 - B) larger is the quantity of Canadian dollars demanded in the foreign exchange market.
 - C) smaller is the quantity of Canadian dollars supplied in the foreign exchange market.
 - D) larger is the quantity of Canadian dollars supplied in the foreign exchange market.
 - E) B and C.
31. The Canadian exchange rate appreciates if
- A) the Canadian interest rate falls.
 - B) prices increase in the United States and other countries but remain constant in Canada.
 - C) the U.S. interest rate rises.
 - D) all of the above.
 - E) none of the above.
32. If the price of a burger is \$2.90 Canadian in Toronto and \$3 U.S. in New York, and if purchasing power parity holds, then the exchange rate is
- A) 97 cents U.S. per Canadian dollar.
 - B) 103 cents U.S. per Canadian dollar.
 - C) \$3 U.S. per Canadian dollar.
 - D) \$1 U.S. per Canadian dollar.
 - E) none of the above.
33. Suppose interest rates are 3 percent in Japan and 6 percent in Canada. The current value of the exchange rate is 110 Japanese yen per dollar, and it is generally expected that in one year the exchange rate will be 106.7 yen per dollar. Under these circumstances,
- A) an international investor could make money by borrowing in Canada and lending in Japan, assuming no transaction costs.
 - B) an international investor could make money by borrowing in Japan and lending in Canada, assuming no transaction costs.
 - C) interest rate parity is violated.
 - D) interest rate parity is not violated.
 - E) A and C are true.
34. Choose the correct statements.
- 1. The exchange rate is the value of the Canadian dollar expressed in units of foreign currency per Canadian dollar.
 - 2. The real exchange rate is the relative price of Canadian-produced goods and services to foreign-produced goods and services.
 - 3. The exchange rate is a measure of the quantity of the real GDP of other countries that a unit of Canadian real GDP buys.
 - 4. The exchange rate is the relative price of Canadian-produced goods and services to foreign-produced goods and services.
- A) Statements 3 and 4 are correct.
 - B) Statements 2 and 3 are correct.
 - C) Statements 1 and 3 are correct.
 - D) Statements 2 and 4 are correct.
 - E) Statements 1 and 2 are correct.

35. If a country's central bank does not intervene in the foreign exchange market, the country has
- A) a responsible exchange rate policy.
 - B) a fixed exchange rate policy.
 - C) a crawling peg exchange rate policy.
 - D) no exchange rate policy.
 - E) a flexible exchange rate policy.

Refer to the figure below to answer the following questions.

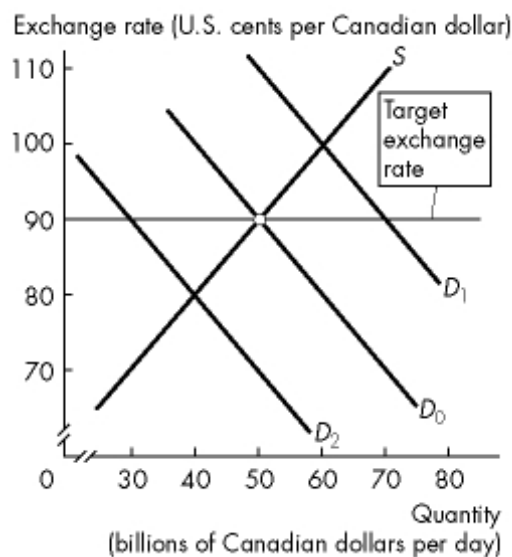


Figure 25.3.1

36. In Figure 25.3.1, suppose the demand for dollars *temporarily* decreases so that the demand curve shifts to D_2 . To maintain the target exchange rate, the Bank of Canada
- A) must violate both interest rate parity *and* purchasing power parity.
 - B) must lower the target exchange rate.
 - C) buys dollars.
 - D) must raise the target exchange rate.
 - E) sells dollars.
37. Which one of the following is a balance of payments account?
- A) official lending account
 - B) public account
 - C) borrowing account
 - D) current account
 - E) net interest account
38. The change in Canadian official reserves is recorded in the
- A) current account.
 - B) international investment account.
 - C) capital and financial account.
 - D) consumption expenditure account.
 - E) official settlements account.

39. Complete the following sentence. Potential GDP
- A) does not vary with the price level.
 - B) increases as the price level rises.
 - C) is the level of real GDP when unemployment is zero.
 - D) increases as the quantity of money in the economy increases.
 - E) never changes.
40. Which one, if any, of the following events shift the short-run aggregate supply curve but not the long-run aggregate supply curve?
- A) A change in the quantity of capital.
 - B) An advance in technology.
 - C) A change in factor prices.
 - D) An increase in the full-employment quantity of labour.
 - E) None of the above.
41. An increase in oil prices to a country that is a net importer of oil shifts
- A) the short-run aggregate supply curve leftward, but leaves the long-run aggregate supply curve unchanged.
 - B) both the short-run aggregate supply and long-run aggregate supply curves leftward.
 - C) the long-run aggregate supply curve rightward, but leaves the short-run aggregate supply curve unchanged.
 - D) both the short-run aggregate supply and long-run aggregate supply curves rightward.
 - E) the short-run aggregate supply curve leftward, but shifts the long-run aggregate supply curve rightward.
42. An increase in the money wage rate shifts
- A) both *SAS* and *LAS* leftward.
 - B) *LAS* rightward, but leaves *SAS* unchanged.
 - C) *SAS* leftward, but leaves *LAS* unchanged.
 - D) both *SAS* and *LAS* rightward.
 - E) *SAS* rightward, but leaves *LAS* unchanged.

Use the figure below to answer the following questions.

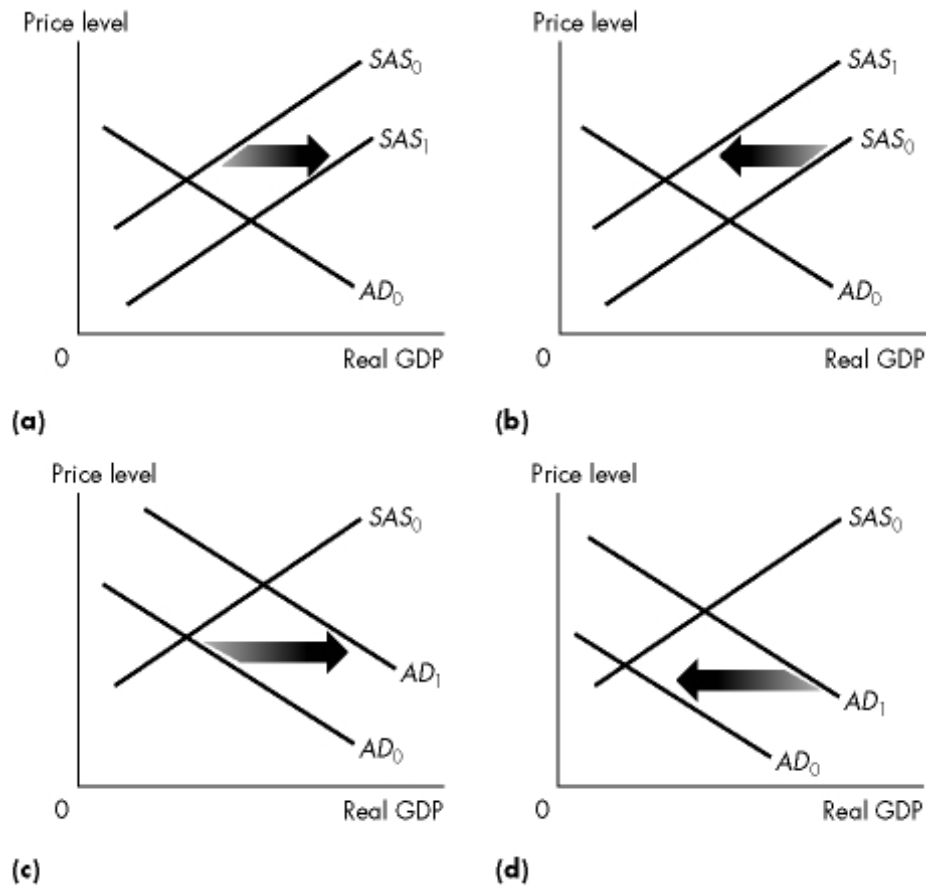


Figure 26.2.1

43. Refer to Figure 26.2.1. Which graph illustrates what happens when expected future income increases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) None of the above.

44. Refer to Figure 26.2.1. Which graph illustrates what happens when the quantity of money increases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Use the figure below to answer the following questions from the economy of Mythlo.



Figure 26.3.2

45. Refer to Figure 26.3.2. Short-run macroeconomic equilibrium real GDP in Mythlo is _____ billion.
 A) \$475 B) \$600 C) \$550 D) \$500 E) \$650
46. Refer to Figure 26.3.2. As the economy of Mythlo automatically adjusts to long-run equilibrium, the
 A) *AD* curve shifts rightward.
 B) *AD* curve shifts leftward.
 C) *SAS* curve shifts leftward.
 D) *LAS* curve shifts rightward.
 E) *SAS* curve shifts rightward.
47. Refer to Figure 26.3.2. Consider statements (1) and (2) and select the correct answer.
 (1) The actual unemployment rate exceeds the natural unemployment rate in the short run.
 (2) *SAS* automatically shifts rightward as the economy adjusts to long-run equilibrium.
 A) (1) is true; (2) is false.
 B) (1) and (2) are false.
 C) (2) is true; (1) is false.
 D) (1) is false; (2) is true if the *LAS* curve shifts rightward at the same time.
 E) (1) and (2) are true.

Use the figure below to answer the following questions.

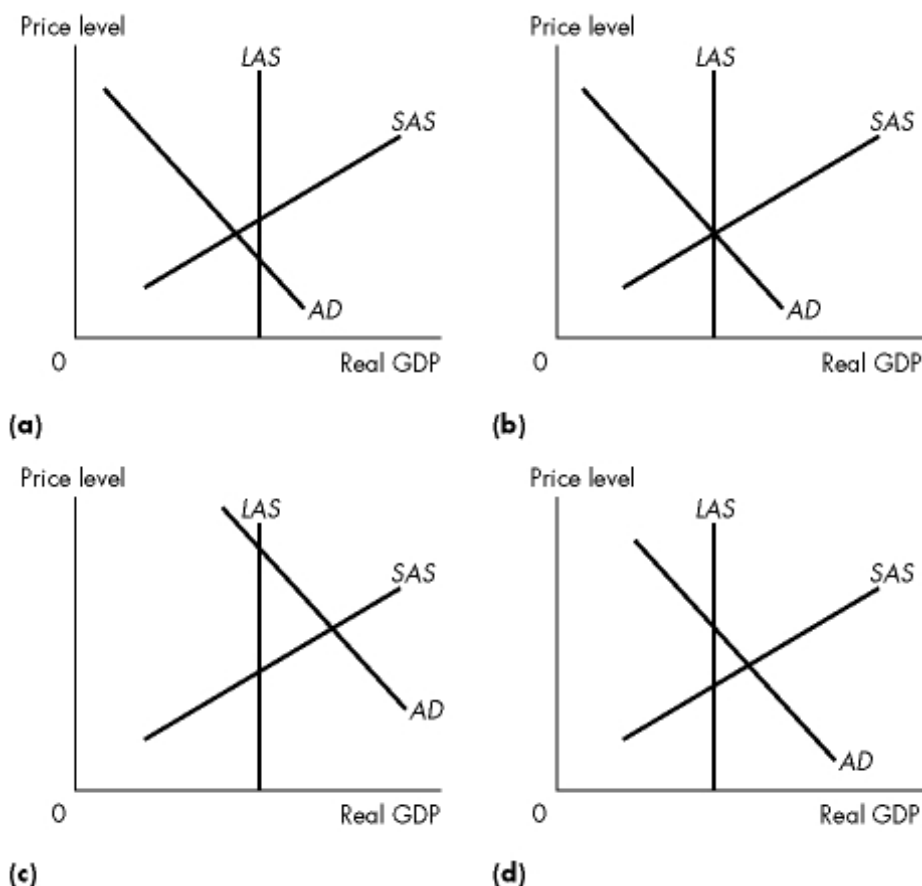


Figure 26.3.3

48. Refer to Figure 26.3.3. In which of the graphs would we predict that eventually the price level will fall and real GDP will decrease, all else remaining the same?
- A) (a)
 - B) (b)
 - C) (c)
 - D) (d)
 - E) none of the graphs
49. Refer to Figure 26.3.3. Which one of the graphs illustrates a full-employment equilibrium?
- A) (a) only
 - B) (b) only
 - C) (c) only
 - D) (d) only
 - E) (c) and (d)
50. Keynesian macroeconomists recommend
- A) policies that minimize the disincentive effects of taxes on employment, investment, and technological change.
 - B) an increase in the quantity of money to offset decreases in aggregate demand and a decrease in the quantity of money to offset increases in aggregate demand.
 - C) policies that actively offset changes in long-run aggregate supply that result in negative economic growth.
 - D) policies that actively offset changes in aggregate demand that bring recession.
 - E) none of the above.

Answer Key

Testname: ECON102 MIDTERM 2

1. D
2. B
3. E
4. D
5. B
6. C
7. D
8. E
9. D
10. D
11. D
12. B
13. C
14. C
15. C
16. C
17. D
18. E
19. E
20. E
21. C
22. D
23. E
24. B
25. C
26. E
27. B
28. E
29. E
30. E
31. B
32. B
33. D
34. E
35. E
36. C
37. D
38. E
39. A
40. C
41. A
42. C
43. C
44. C
45. B
46. C
47. B
48. E
49. B
50. D