

Econ102 Midterm Exam 2

(You have 90 minutes to finish 50 multiple choices questions.)

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

1. Capital is
 - A) financial wealth.
 - B) the tools, instruments, machines, buildings, and other items that have been produced in the past and that are used today to produce goods and services.
 - C) gross investment.
 - D) the sum of investment and government expenditure on goods.
 - E) net investment.

2. In January 2011, Tim's Gyms, Inc. owned machines valued at \$1 million. During the year, the market value of the machines fell by 10 percent. During 2011, Tim spent \$200,000 on new machines. During 2011, Tim's net investment was
 - A) \$100,000.
 - B) \$1.1 million.
 - C) \$300,000.
 - D) \$200,000.
 - E) \$1 million.

3. Choose the statement that is *incorrect*.
 - A) Insolvency and illiquidity were at the core of a global financial meltdown in 2007-2008.
 - B) A financial institution's net worth is the market value of what it has lent minus the market value of what it has borrowed.
 - C) A financial institution can be solvent but illiquid.
 - D) A firm is illiquid if it has made long-term loans with borrowed funds and is faced with a sudden demand to repay more of what it has borrowed than its available cash.
 - E) All of the above are true.

4. As the _____ interest rate rises _____.
 - A) real; a movement occurs down along the demand for loanable funds curve
 - B) real; a movement occurs up along the demand for loanable funds curve
 - C) real; the demand for loanable funds curve shifts rightward
 - D) nominal; the demand for loanable funds curve shifts leftward
 - E) nominal; the demand for loanable funds curve shifts rightward

5. Changes in all of the following *shift* the supply curve of loanable funds *except*
 - A) wealth.
 - B) expected future income.
 - C) default risk.
 - D) disposable income.
 - E) the real interest rate.

Refer to the figure below to answer the following questions.

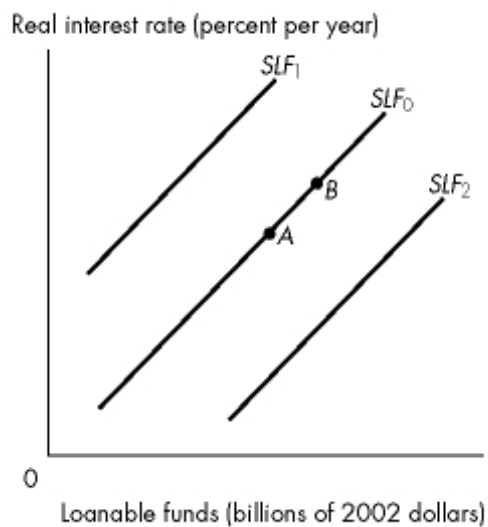


Figure 23.2.4

6. Refer to Figure 23.2.4. In Figure 23.2.4, the economy is at point A on the supply of loanable funds curve SLF_0 . What happens if disposable income decreases?
- A) The supply of loanable funds curve shifts rightward to a curve such as SLF_2 .
 - B) There is a movement to a point such as B on the supply of loanable funds curve SLF_0 .
 - C) The supply of loanable funds curve shifts leftward to a curve such as SLF_1 .
 - D) Nothing; the economy would remain at point A.
 - E) None of the above.

Refer to the figure below to answer the following questions.

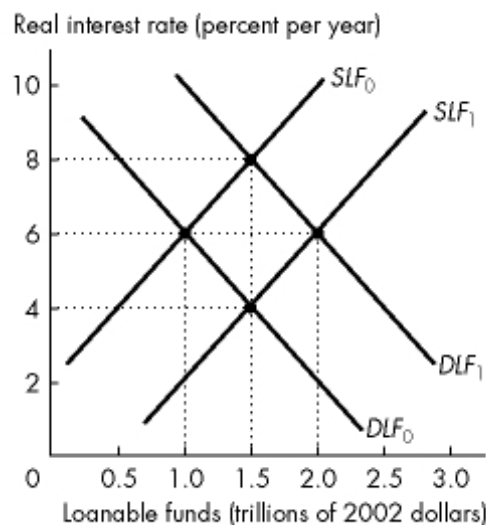


Figure 23.2.5

7. Refer to Figure 23.2.5. In Figure 23.2.5, the supply of loanable funds curve is SLF_0 and the demand for loanable funds curve is DLF_0 . An expansion that increases disposable income and expected profit
- shifts the demand for loanable funds curve rightward to curve DLF_1 and does not shift the supply of loanable funds curve.
 - shifts the supply of loanable funds curve rightward to curve SLF_1 , and shifts the demand for loanable funds curve rightward to curve DLF_1 .
 - shifts the supply of loanable funds curve rightward to curve SLF_1 and does not shift the demand for loanable funds curve.
 - has no effect on either the demand for loanable funds curve or the supply of loanable funds curve.
 - none of the above.
8. Crowding out leads to all of the following *except*
- a decrease in private saving.
 - a decrease in investment.
 - a smaller quantity of capital in the future.
 - a higher real interest rate.
 - crowding out leads to all of the above.
9. A government budget surplus occurs, which _____ loanable funds. The real interest rate _____, household saving _____, and investment _____.
- decreases the demand for; falls; decreases; increases
 - increases the supply of; falls; decreases; increases
 - increases the demand for; rises; increases; decreases
 - decreases the supply of; decreases; decreases; increases
 - increases the supply of; falls; increases; decreases

10. In an individual economy that is integrated into the global market, the demand for loanable funds is determined by the _____ demand and the supply of loanable funds is determined by the _____ supply.
- A) world's; country's
 - B) country's; country's
 - C) world's; World Bank's
 - D) country's; world's
 - E) world's; world's
11. An increase in the government budget deficit _____. If the country is an international borrower, the government budget deficit _____. If the country is an international lender, the government budget deficit _____.
- A) decreases the country's demand for loanable funds; decreases foreign lending; increases foreign borrowing
 - B) decreases the country's supply of loanable funds; increases foreign borrowing; decreases foreign lending
 - C) increases the country's demand for loanable funds; decreases foreign borrowing; increases foreign lending
 - D) increases the country's supply of loanable funds; decreases foreign lending; increases foreign borrowing
 - E) increases the country's demand for loanable funds; increases foreign borrowing; decreases foreign lending
12. The higher and more unpredictable the changes in a monetary unit, the
- A) more likely it will be used as a standard of deferred payment.
 - B) less likely contracts will be written to counterbalance the uncertainty of its value in the future.
 - C) more confidence people will have in holding it for the future.
 - D) more likely it will be used as a store of value.
 - E) less likely it will be used as a store of value.
13. The official definitions of money can include all of the following *except*
- A) deposits at trust and mortgage loan companies.
 - B) cheques.
 - C) currency outside banks.
 - D) non-chequable deposits.
 - E) personal chequable deposits.
14. If Wolfgang transfers \$1,000 out of his non-chequable deposit account and places it in his chequable deposit account,
- A) M1 and M2 fall.
 - B) M1 falls and M2 remains the same.
 - C) M1 falls and M2 rises.
 - D) M1 rises and M2 remains the same.
 - E) M1 falls and M3 rises.
15. The reserves of a bank include
- A) the cash in its vault plus any deposits held on account at the Bank of Canada.
 - B) the cash in its vault plus the value of its chequable deposits.
 - C) the cash in its vault plus any gold held for the bank at the Bank of Canada.
 - D) all of its common stock holdings, the cash in its vault, and all deposits held on account with the Bank of Canada.
 - E) the cash in its vault plus any deposits held on account with the Bank of Canada plus the value of any government bonds that it holds.

16. Which of the following is an economic function of a chartered bank?

- A) Pooling risk.
- B) Conducting monetary policy.
- C) Issuing bank notes.
- D) Supervising financial markets.
- E) None of the above.

17. Whenever actual reserves exceed desired reserves, the bank

- A) will go out of business.
- B) can make new loans.
- C) will raise the interest rate on its loans.
- D) will borrow funds from another bank.
- E) needs to call in loans.

18. 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) 50%.
- D) 10%.
- E) 20%.

Use the information below to answer the following questions.

Fact 24.3.1

The Bank of Speedy Creek has chosen the following initial balance sheet:

Assets		Liabilities	
Reserves	\$40	Deposits	\$500
Loans	<u>\$460</u>		
	\$500		

19. Refer to Fact 24.3.1. Based on the Bank of Speedy Creek's initial balance sheet, what is its desired reserve ratio?

- A) 40 percent
- B) 4 percent
- C) 25 percent
- D) 12.5 percent
- E) 8 percent

20. Real money is equal to

- A) nominal income divided by the price level.
- B) nominal income divided by the velocity of circulation.
- C) nominal money divided by the price level.
- D) nominal money divided by nominal income.
- E) the price level divided by nominal money.

Use the figure below to answer the following questions.

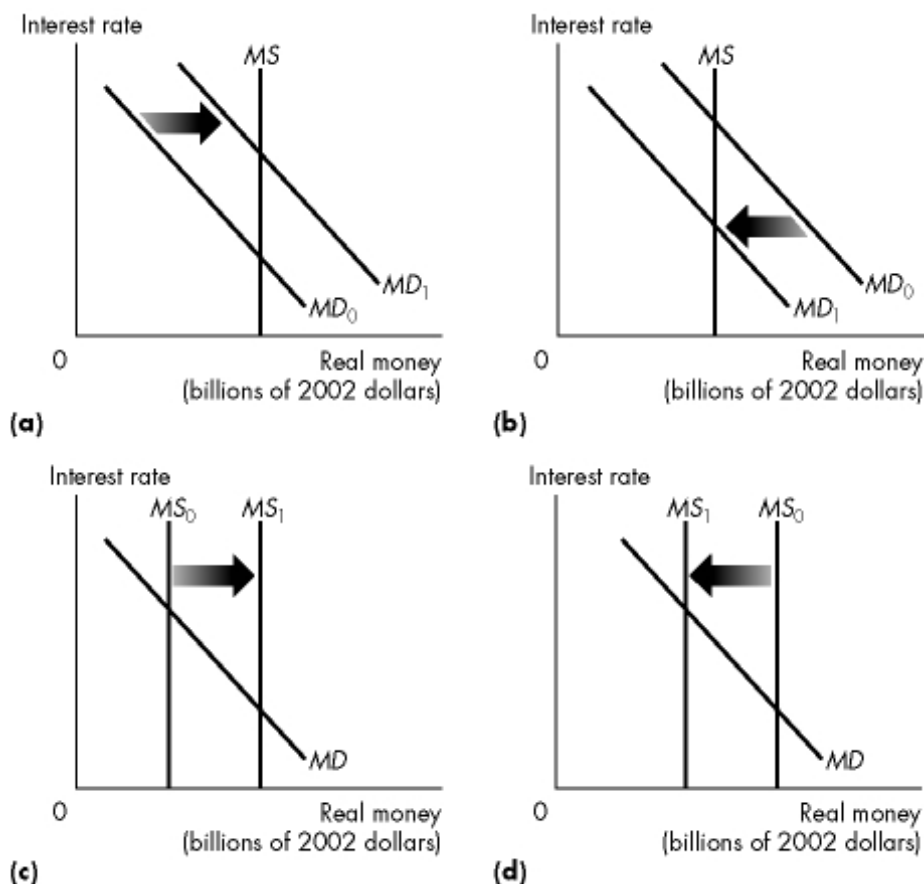


Figure 24.4.1

21. Refer to Figure 24.4.1. Everything else remaining the same, which graph best shows an increase in real GDP?
 A) (a) B) (b) C) (c) D) (d) E) (a) and (c)
22. The opportunity cost of holding currency is
 A) consumption given up.
 B) the real interest rate.
 C) the price level.
 D) the nominal interest rate.
 E) the inflation rate.
23. Money market equilibrium occurs
 A) only under a fixed exchange rate.
 B) when the quantity of real money supplied equals the quantity of real money demanded.
 C) when interest rates are constant.
 D) when bond prices are constant.
 E) when the level of real GDP is constant.

24. If the interest rate is above the equilibrium rate, how is equilibrium achieved in the money market?
- A) People buy bonds to get rid of their excess money, raising the price of bonds and lowering the interest rate.
 - B) People sell bonds to get rid of their excess money, raising the price of bonds and lowering the interest rate.
 - C) People sell goods to get rid of their excess money, lowering the price of goods and lowering the interest rate.
 - D) People buy goods to get rid of their excess money, lowering the price of goods and lowering the interest rate.
 - E) People sell bonds to get rid of their excess money, lowering the price of bonds and lowering the interest rate.
25. GDP is \$2,000 billion, the price level is 100, and the velocity of circulation is 5. The quantity of money is
- A) \$400 billion.
 - B) \$10,000 billion.
 - C) \$500 billion.
 - D) \$2,000 billion.
 - E) \$20 billion.
26. Suppose that people decide to hold more money as cash. Which statement best illustrates the impact of this action on the money multiplier? The money multiplier
- A) increases because of a decrease in deposits.
 - B) decreases because of the decrease in the currency drain ratio.
 - C) decreases because of the increase in the currency drain ratio.
 - D) increases because of the decrease in the currency drain ratio.
 - E) increases because of the increase in the currency drain ratio.
27. Currency depreciation is a reduction in the
- A) amount of domestic currency that must be exchanged for a unit of foreign exchange.
 - B) precious metal content in coins, such as the replacement of silver with copper in quarters.
 - C) goods and services a currency can purchase within its own country, usually the result of a period of inflation.
 - D) amount of domestic goods foreign currency can purchase.
 - E) amount of foreign currency that can be obtained in trade for each unit of domestic currency.
28. Suppose that the following situation exists in the foreign exchange market: 1 Canadian dollar buys \$1.01 U.S., and 1 Canadian dollar buys 6.63 South African rand. How many U.S. dollars will one rand buy?
- A) \$0.17 B) \$6.63 C) \$1.01 D) \$0.15 E) \$6.56
29. Which of the following factors influence the demand for Canadian dollars?
- A) Interest rates in Canada and other countries, and the expected future exchange rate.
 - B) The world demand for Canadian exports.
 - C) The world demand for Canadian exports and Canadian demand for imports.
 - D) Both A and B.
 - E) Both B and C.

30. Consider the market for Canadian dollars. If the exchange rate rises from 2 Mexican pesos per dollar to 4 Mexican pesos per dollar, _____.
 A) a movement down along the demand curve for Canadian dollars occurs
 B) the demand for Canadian dollars decreases
 C) a movement up along the demand curve for Canadian dollars occurs
 D) the demand for Canadian dollars increases
 E) none of the above
31. Which one of the following would result in the dollar depreciating against the Japanese yen?
 A) a rise in the Canadian interest rate
 B) an increase in the Canadian interest rate differential
 C) a fall in the Japanese interest rate
 D) a fall in the Canadian interest rate
 E) an increase in the expected future Canadian exchange rate
32. Suppose that people expect that the Canadian exchange rate will decrease in the near future. How will this situation affect the Canadian exchange rate?
 A) The supply of Canadian dollars decreases, the demand for Canadian dollars increases and the exchange rate rises.
 B) Neither the supply of Canadian dollars nor the demand for Canadian dollars changes.
 C) The supply of Canadian dollars increases, the demand for Canadian dollars decreases and the exchange rate falls.
 D) The supply of Canadian dollars decreases, the demand for Canadian dollars decreases and the exchange rate falls.
 E) The supply of Canadian dollars increases, the demand for Canadian dollars decreases and the exchange rate rises.
33. Suppose that Canada's demand for imports decreases. All other things equal,
 A) the demand for Canadian dollars decreases and the supply of Canadian dollars increases.
 B) both the supply of and demand for Canadian dollars decreases.
 C) the demand for Canadian dollars increases.
 D) the supply of Canadian dollars decreases and demand for Canadian dollars increases.
 E) the supply of Canadian dollars decreases.
34. Given the Canadian price level P , the foreign country price level P^* , and the nominal exchange rate E in foreign currency per Canadian dollar, the real exchange rate RER equals _____.
 A) $(P/P^*) / E$ B) $P \times (E/P^*)$ C) $E \times (P^*/P)$ D) $P \times E \times P^*$ E) $E \times (P/P^*)$
35. Suppose the Bank of Canada follows a fixed exchange rate of \$1 U.S. per Canadian dollar. If the demand for Canadian dollars temporarily increases, to maintain the target exchange rate, the Bank can
 A) violate purchasing power parity.
 B) sell Canadian dollars.
 C) enforce interest rate parity.
 D) buy Canadian dollars.
 E) violate interest rate parity.

36. If the current account is in deficit and the capital and financial account is also in deficit, then the official settlements account balance is
- A) positive.
 - B) probably close to zero, but could be either negative or positive.
 - C) equal to the sum of the current account and the capital account.
 - D) negative.
 - E) zero.
37. Suppose that a country's government expenditures are \$400 billion, net taxes are \$300 billion, saving is \$300 billion, and investment is \$250 billion. Net exports are a
- A) surplus of \$150 billion.
 - B) deficit of \$150 billion.
 - C) deficit of \$50 billion.
 - D) surplus of \$50 billion.
 - E) deficit of \$250 billion.
38. A creditor nation is a country
- A) whose official settlements account is rising in value.
 - B) that has contributed money for the advancement of health care in less developed countries.
 - C) that has active monetary policy to ensure adequate loans for housing of the poor.
 - D) that does not borrow money from foreign nations.
 - E) that during its entire history has invested more in the rest of the world than other countries have invested in it.

Use the figure below to answer the following questions.

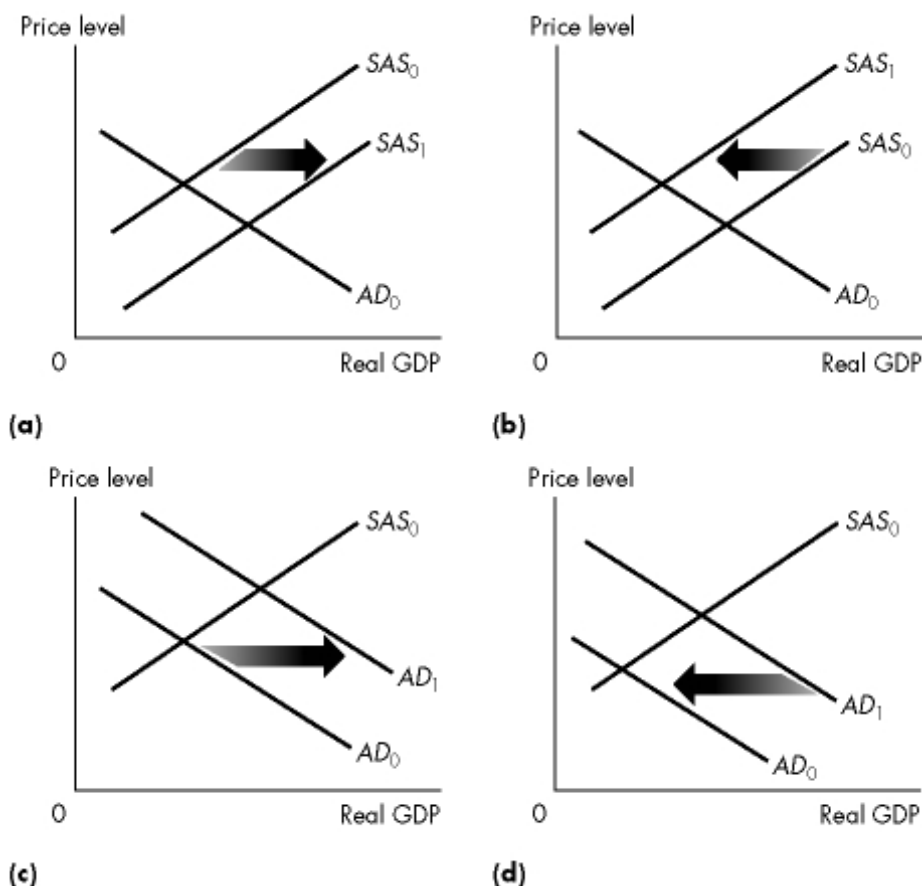


Figure 26.1.1

39. Refer to Figure 26.1.1. Which graph illustrates what happens when factor prices decrease?
- A) (a) B) (b) C) (c) D) (d) E) (a) and (b)
40. Which one of the following newspaper quotations describes a movement along an *LAS* curve?
- A) "Recent higher wage settlements are expected to cause higher inflation this year."
 B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
 C) "The recent tornadoes destroyed many factories in Calgary and Edmonton."
 D) "The decrease in consumer spending may lead to a recession."
 E) "Growth has been unusually high the last few years due to more women entering the labour force."
41. Complete the following sentence. Potential GDP
- A) is the level of real GDP when unemployment is zero.
 B) increases as the price level rises.
 C) increases as the quantity of money in the economy increases.
 D) never changes.
 E) does not vary with the price level.

42. The short-run aggregate supply curve indicates
- A) the relationship between the purchasing power of wages and the quantity of labour supplied by households.
 - B) the relationship between the price level and real GDP demanded by consumers, investors, governments, and net exporters.
 - C) the relationship between the quantity of real GDP supplied and the price level when the money wage rate, the prices of other resources, and potential GDP remain constant.
 - D) the various quantities of real GDP producers supply at different income levels.
 - E) the relationship between the price level and the natural unemployment rate.
43. Disposable income is aggregate income
- A) minus fixed expenses such as rent and utilities.
 - B) minus taxes and benefits.
 - C) minus taxes.
 - D) plus transfer payments.
 - E) minus taxes plus transfer payments.
44. Which one of the following factors will *not* shift the aggregate demand curve?
- A) an increase in the quantity of money
 - B) an increase in the interest rate
 - C) an increase in expected future profits
 - D) an increase in the price level
 - E) an increase in the expected inflation rate
45. Everything else remaining the same, an increase in foreign income
- A) decreases Canada's aggregate demand.
 - B) increases Canada's aggregate supply.
 - C) decreases Canada's aggregate supply.
 - D) increases Canada's aggregate demand.
 - E) creates a movement downward along Canada's aggregate demand curve.

Use the figure below to answer the following questions.

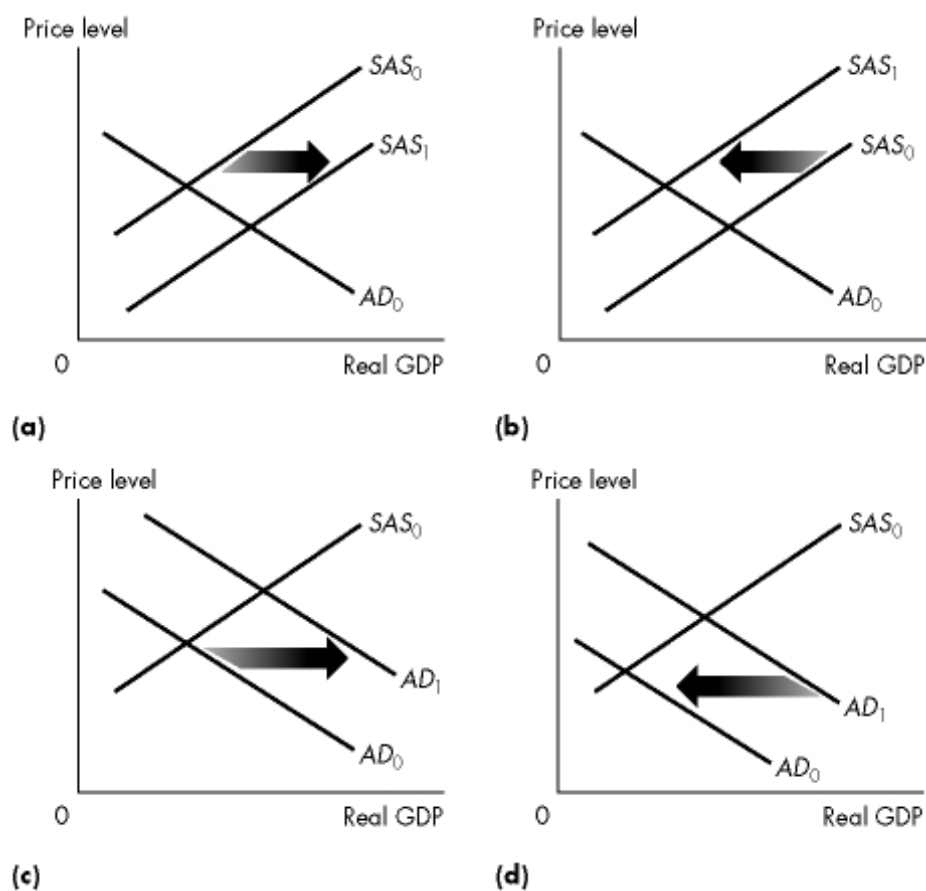


Figure 26.2.1

46. Refer to Figure 26.2.1. Which graph illustrates what happens when the quantity of money decreases?
- A) (a)
 - B) (b)
 - C) (c)
 - D) (d)
 - E) None of the above

Use the figure below to answer the following questions.

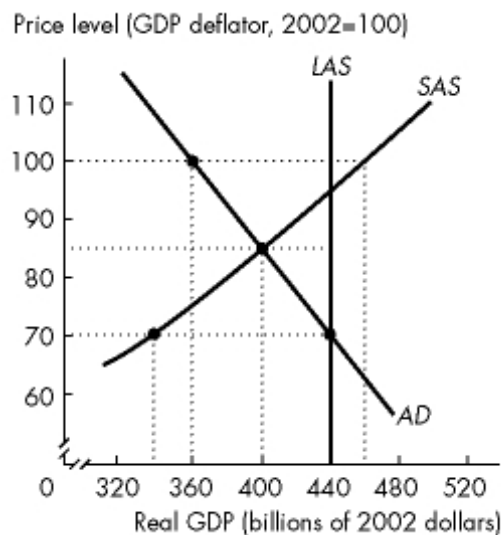


Figure 26.3.1

47. Refer to Figure 26.3.1. As Econoworld automatically adjusts to long-run equilibrium, the
- A) AD curve shifts rightward.
 - B) LAS curve shifts leftward.
 - C) SAS curve shifts rightward.
 - D) SAS curve shifts leftward.
 - E) AD curve shifts leftward.

Use the figure below to answer the following questions.



Figure 26.3.2

48. Refer to Figure 26.3.2. If the economy of Mythlo automatically adjusts to long-run equilibrium, then
- real GDP is \$600 billion.
 - the actual unemployment rate exceeds the natural unemployment rate.
 - the SAS curve shifts rightward.
 - potential GDP decreases.
 - the price level rises to 90.
49. Refer to Figure 26.3.2. Consider statements (1) and (2) and select the correct answer.
- The economy of Mythlo is experiencing an above full-employment equilibrium.
 - SAS will automatically shift rightward as the economy adjusts to long-run equilibrium.
- (1) is true; (2) is true only if the LAS curve shifts rightward at the same time.
 - (1) and (2) are true.
 - (1) is true; (2) is false.
 - (2) is true; (1) is false.
 - (1) and (2) are false.
50. The defining feature of the classical view of macroeconomics is that the economy is
- the most significant influence on aggregate demand is expectations.
 - rarely at full employment.
 - self-regulating and always at full employment.
 - constantly bombarded by shocks that arise from the uneven pace of technological change.
 - driven by expectations called "animal spirits."

Answer Key

Testname: ECON102 SAMPLE MIDTERM 2

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