

Name: \_\_\_\_\_ Days/Times Class Meets: \_\_\_\_\_ Today's  
Date: \_\_\_\_\_

**Macroeconomics, Fall 2007, Exam 2, several versions, Week 11, 2007**

**Read these Instructions carefully! You must follow them exactly!**

**I) On your Scantron card you must print three things:**

- 1) Print your full name clearly;
- 2) Print the day and time of your section (for example TTh 7 AM);
- 3) Print the number I have written in ink on the upper right corner of your copy of this test. (This number tells me which version of the test you have. Without it your test cannot be graded properly and you get no credit for your answers.)

**II) Answer on your Scantron card, using a #2 pencil.**

Warning: SOME QUESTIONS MUST BE ANSWERED SEVERAL TIMES! Such questions will begin with a phrase such as this:

**(Repeat answer on Scantron lines 37, 38 and 39)**

---Remember to do it!

**III) You must turn in this printed exam along with your Scantron card, otherwise your score on this exam is "F".**

**Questions:**

- \_\_\_\_\_ 1. If you borrow \$1000 for 30 days from a bank, and the bank tells you the interest rate is 5%,
- a. when you pay back the loan you will owe \$1,000 plus \$50 interest.
  - b. this interest rate is roughly equivalent to 60% per year.
  - c. this interest rate is equal to 5% per year, so you will owe much less than \$50 when you repay the loan.
  - d. two of the other answers are correct.
  - e. none of the other answers is correct.
- \_\_\_\_\_ 2. When explaining expansions and recessions, the classical model is
- a. reliable
  - b. seriously flawed
  - c. the favorite explanatory tool of economists
  - d. overly focused on the labor market
  - e. sometimes accurate and sometimes not
- \_\_\_\_\_ 3. **(Repeat your answer on Scantron lines 29 and 30.)** Evaluate each of the following statements about the historical record of inflation in the U.S. and then choose the best answer from a through e. below:
- 1) From 1950 to 2003 the two worst years of price inflation occurred in the early and late 1970's and in each of those two years prices rose by more than 10%.
  - 2) From 1950 to 2003, most years had inflation rates of at least 5%.
  - 3) From 1922-2003 there have been 7 years in which prices actually fell, and several of those years have occurred since 1960.
- a. Statements 1) through 3) are all true.
  - b. Only statement 1 is true.
  - c. Only statement 2 is true.
  - d. Only statement 3 is true.
  - e. None of statements 1) through 3) are true.

- \_\_\_\_\_ 4. **(Repeat your answer on Scantron lines 31 and 32.)** Based on the circular flow model as presented in recent lectures, and starting from an “unemployment equilibrium”, decide whether each of the following statements is True or False, then choose the best answer from among a. through e. below.
- 1) If the government cuts taxes, this will stimulate the economy to grow.
  - 2) If the government increases government spending, this will stimulate the economy to grow.
  - 3) If the government increases the money supply, this will stimulate the economy to grow.
- a. All three of the statements 1), 2) and 3) are true.
  - b. Statements 1) and 2) are true but 3) is false.
  - c. Statements 1) and 2) are false but 3) is true.
  - d. All three of the statements 1), 2) and 3) are false
  - e. Statements 2) and 3) are true, but tax cuts cannot stimulate the economy so 1) is false.
- \_\_\_\_\_ 5. **(Repeat your answer on Scantron line 33.)** Choose the best answer:
- a. Nominal GDP was more than 12,000 Billion in 2005.
  - b. Nominal GDP was less than 1,000 Billion in 2004.
  - c. Nominal GDP was a bit less than 12,000 Billion in 2005.
  - d. Nominal GDP was between 12 and 13 Billion in 2005.
  - e. In 2000 dollars, real GDP was more than 12,000 Billion in 2000.
- \_\_\_\_\_ 6. **(Repeat your answer on Scantron line 34.)** Compute the value added in the year 2006 of the following firm, Acme Screw and Bolt Company. Data: No prices changed during the year; the firm sold \$20 million of screws and bolts; the inventory of unsold screws and bolts declined by \$1 million during the year; the firm bought \$8 million of inputs (including copper, iron and many other inputs); the firm’s inventories of inputs increased by \$3 million during the year.
- a. Value added was \$14 million
  - b. Value added was \$8 million
  - c. Value added was \$16 million
  - d. Value added was \$10 million
  - e. Value added was 19 million
- \_\_\_\_\_ 7. Choose the best answer. Based on what your professor has said in lecture, if the economy is in a full employment equilibrium and the money supply increases by a small amount, like 3%,
- a. prices will rise about 3% within a year.
  - b. economic activity will increase by 3% within a year.
  - c. prices will rise by 3% within two years.
  - d. prices may take a very long time to rise, and will not rise more than about 3%
  - e. the smaller the inflation rate, the more immediate the response, so prices will rise quickly.
- \_\_\_\_\_ 8. **(Repeat your answer on Scantron lines 35 and 36.)** Which statement best describes economic fluctuations?
- a. Expansions and contractions typically have about the same lengths.
  - b. Expansions typically last 7 years, while recessions typically last 3 years.
  - c. Expansions tend to be shorter than contractions.
  - d. The percent change in output is larger during recessions than during expansions.
  - e. Expansions and contractions vary in duration and magnitude, with expansions tending to last longer than contractions.

- \_\_\_\_\_ 9. The reason a shock to one sector can spread to the whole economy is that
- a decrease in production in one sector leads to an overall decrease in spending
  - firms will need to help bail out other firms that are having troubles
  - an increase in production in one sector will lead to an overall decrease in spending
  - most shocks are not sector-specific but economy-wide
  - workers laid off in the one sector will purchase more goods in another sector
- \_\_\_\_\_ 10. **(Repeat your answer on Scantron lines 37 and 38.)** Which of the following statements about measuring prices are true?
- 1) If my "base year basket" costs \$30,000 to purchase this year, and three years from now it costs \$33,000 to purchase the same base year basket, then the price index based on this basket will tell you that prices have risen by 10%.
  - 2) If the cost of my base year basket has risen by 10%, then the cost of your base year basket has also risen by 10%.
  - 3) A new base year basket must be calculated every few years, otherwise inflation starts looking lower than it really is.
  - 4) If a good rises in price and also in quality, calculated inflation will be lower than actual inflation.
    - All the above statements are correct.
    - Only statements 1 and 2 are correct.
    - None of these statements are correct.
    - Only statement 1 is correct.
    - Only statements 1 and 3 are correct.
- \_\_\_\_\_ 11. If the economy is in full employment equilibrium, and the money supply is increased 12%, then we expect:
- the economy to grow.
  - prices to rise by more than 12%
  - prices to rise 12%
  - prices to rise by less than 12%
  - nothing will happen

- \_\_\_\_\_ 12. **(Repeat your answer on Scantron lines 39 and 40.)** Which of the following statements about measuring prices are true?
- 1) If my "base year basket" costs \$1,000 to purchase this year, and one year from now it costs \$1,200 to purchase the same base year basket, then the price index based on this basket will tell you that prices have risen by 10%.
  - 2) If dingbats are one of the goods in the base year basket, and 30% of the base year budget was spent on dingbats, and in some future year all prices are unchanged except the price of dingbats has increased by 20%, then the price index will have risen by 6%.
  - 3) Suppose people are now purchasing more computers and fewer typewriters than in the base year, however we are still using the base year basket to calculate inflation. Suppose also that typewriter prices have been rising and computer prices have been falling. Then the computed price index will show less inflation than actually exists.
- a. All the above statements are correct.
  - b. Only statement 1 is correct.
  - c. Only statement 2 is correct.
  - d. Only statement 3 is correct.
  - e. Only statements 2 and 3 are correct.
- \_\_\_\_\_ 13. **(Repeat your answer on Scantron lines 41 and 42.)** Based on the simple circular flow model as presented in recent lectures, if the economy is in an **unemployment equilibrium** (wages and prices are "downward sticky") and the government cuts taxes but the money supply is not permitted to change, evaluate each of the following statements:
- 1) Inflation definitely will occur because the tax cut leaves more income in the hands of the public, permitting them to increase spending.
  - 2) The economy will definitely be stimulated by the tax cut and begin to recover from the recession.
  - 3) Interest rates will decline and the economy will begin to recover.
  - 4) Interest rates will rise and the economy will begin to recover.
  - 5) Interest rates will rise but the economy will not be stimulated by the tax cut.
- Choose the best answer:
- a. Statement 2 is correct.
  - b. Statement 3 is correct.
  - c. Statements 2 and 4 are correct.
  - d. Statement 4 is correct.
  - e. Statement 5 is correct.
- \_\_\_\_\_ 14. **(Repeat your answer on Scantron line 43.)** If the price of oil rises 9% while the cost of living (the price index) falls 7% then real oil prices have
- a. fallen about 2%.
  - b. fallen considerably more than 2%.
  - c. risen by about 9%.
  - d. risen by about 2%.
  - e. risen by about 16%.

Recall:

$$FR = IR * (FN/IN)*(II/FI)$$

- \_\_\_\_\_ 15. **(Repeat your answer on Scantron line 44.)** Suppose the nominal price of oil in 1984 was \$30 per barrel when the consumer price index was 100. What is the real price of oil today, assuming it was \$30 per barrel in 1984? (You can assume that today's price of oil is \$100 per barrel and today's price index is 200.)
- \$50 per barrel.
  - \$40 per barrel.
  - \$35 per barrel.
  - \$30 per barrel.
  - \$25 per barrel.
- \_\_\_\_\_ 16. **(Repeat your answer on Scantron line 45.)** Suppose the nominal price of oil in 1984 was \$30 per barrel when the consumer price index was 100 and today's price of oil is \$100 per barrel while the price index is 200. What has been the **percentage change in the real price of oil?**
- up 77.75%
  - up 42.33%
  - up 66.67%
  - down 15.33%
  - almost unchanged (changed less than 5%).
- \_\_\_\_\_ 17. **(Repeat your answer on Scantron line 46.)** Based on the text, which of the following answers contains the most dates of recessions which happened to be triggered by oil price increases.
- 1970 1974 1980 1990
  - 1974 1980 1990
  - 1970 1974 1980 1981-82 1990
  - 1953 1970 1974 1980 1990
  - 1970 1974 1980 1981-82 1990 2001
- \_\_\_\_\_ 18. **(Repeat your answer on Scantron line 47.)** Evaluate the following statements, then choose the best answer.
- 1) The 1981-82 recession was triggered by a change in Federal Reserve policy leading to a decline in spending on new homes, auto and net investment.
  - 2) The 2001 recession was triggered by large increases in oil prices leading to reduced spending on energy using products.
  - 3) The 1953 recession was triggered by the end of the Korean war leading to a decline in defense spending.
- All three statements are correct.
  - None of the three statements are correct.
  - Only statements 1 and 3 are correct.
  - Only statements 1 and 2 are correct.
  - Only statements 2 and 3 are correct.

- \_\_\_\_\_ 19. A Texas oil company extracts petroleum and sells it to a refinery for \$1,000. After processing, the refinery sells the gasoline to a wholesaler for \$1,500, who then sells it to a gas station for \$1,700. The gas station sells it to customers for \$2,500. No firm increases its inventories. In these transactions, how much has been added to GDP?
- \$1,000
  - \$1,500
  - \$1,700
  - \$2,500
  - \$6,700
- \_\_\_\_\_ 20. This year, Tom sold his 1998 minivan to Honest John's Used Car Emporium for \$5,000. Honest John then sold the van to Bob for \$7,000. How much would be recorded in GDP this year from these transactions?
- \$0
  - \$2,000
  - \$5,000
  - \$7,000
  - \$12,000
- \_\_\_\_\_ 21. Which of the following would not be included in the consumption component of GDP?
- movie ticket sales
  - purchase of a new home
  - medical bills
  - clothing purchases
  - home electricity bills
- \_\_\_\_\_ 22. *Transfer payments* are
- payments for goods or services that individuals provide
  - funds given to people or organizations when no good or service is received in exchange
  - included in the government purchases category of GDP
  - examples of government investment
  - used to pay state employees
- \_\_\_\_\_ 23. If nominal GDP increased, which of the following could also have occurred?
- Both prices and real GDP decreased.
  - Prices remained the same and real GDP decreased.
  - Prices decreased and real GDP remained the same.
  - Prices increased and real GDP decreased.
  - Both prices and real GDP remained the same.
- \_\_\_\_\_ 24. **(Repeat your answer on Scantron line 48.)** When is the U.S. economy at full employment?
- when there is no cyclical unemployment
  - when there is no structural unemployment
  - when there is no full employment
  - when there is no seasonal unemployment
  - when there is no frictional unemployment

- \_\_\_\_\_ 25. The unemployment rate for blacks is approximately twice the rate for
- Hispanics
  - white teenagers
  - women
  - black teenagers
  - whites
- \_\_\_\_\_ 26. With which of the following responses would the Census Bureau declare the person unemployed?
- "I am currently working full-time but my employer is going to lay me off tomorrow."
  - "I am currently working part-time but I would like to work full-time."
  - "I was working at two different jobs, I lost my primary job a few weeks ago, and I am searching for a new job."
  - "I would love a job but I am not looking for one because I have no chance of finding one."
  - "I just turned 16 and I am looking for a job."
- \_\_\_\_\_ 27. If some of unemployed individuals became discouraged workers, which of the following would result?
- The labor force would decrease and the unemployment rate would decrease.
  - The labor force would decrease and the unemployment rate would remain the same.
  - The labor force would increase and the unemployment rate would decrease.
  - The labor force would decrease and the unemployment rate would increase.
  - The labor force would increase and the unemployment rate would remain the same.
- \_\_\_\_\_ 28. **(Repeat your answer on Scantron lines 49 and 50.)** Evaluate the following statements about the historical record since 1960 of Real GDP growth rates:
- In the majority of years, Real GDP grew more than 3%
  - There are several years when Real GDP grew by 7% or more.
  - Real GDP has declined in at least 15 of those 47 years, always during the recessions.
- Only statement 1 is true.
  - Only statement 2 is true.
  - Only statements 2 and 3 are true.
  - Only statements 1 and 3 are true.
  - Only statements 1 and 2 are true.

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Answer Section**

**MULTIPLE CHOICE**

1. ANS: C
2. ANS: B
3. ANS: B
4. ANS: C
5. ANS: A
6. ANS: A
7. ANS: D
8. ANS: E
9. ANS: A
10. ANS: D
11. ANS: C
12. ANS: C
13. ANS: E

Reference: The Money Supply Equation, with Time Dep

14. ANS: E
15. ANS: A
16. ANS: C
17. ANS: B
18. ANS: C
19. ANS: D
20. ANS: B
21. ANS: B
22. ANS: B
23. ANS: D
24. ANS: A
25. ANS: E
26. ANS: E
27. ANS: A
28. ANS: A