

Name: _____ Days/Times Class Meets: _____ Today's
Date: _____

Macroeconomics, Fall 2007 Exam 3, TTh classes, various versions

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:

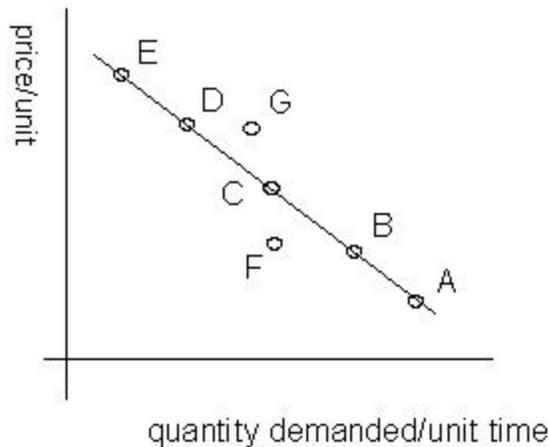
(Repeat answer on Scantron lines 37, 38 and 39)

---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. The opportunity cost of any activity can be measured by the
- a. value of the best alternative to that activity
 - b. price (or monetary costs) of the activity
 - c. level of technology
 - d. time needed to select among various alternatives
 - e. fringe benefits associated with the activity
- _____ 2. The money we pay for a good or service
- a. generally exceeds its opportunity cost
 - b. generally equals its opportunity cost
 - c. has no part in determining its opportunity cost
 - d. generally equals two-thirds of its opportunity cost
 - e. generally is only part of its opportunity cost



- _____ 3. **(Repeat your answer on Scantron lines 28 and 29.)** Refer to the graph above. Evaluate statements 1 through 4 and then select the answer from A) through E):
- 1) Moving from point E to point F is accompanied by an increase in demand.
 - 2) Moving from point E to point F is accompanied by a decrease in demand.
 - 3) Moving from point E to point C is accompanied by no change in demand.
 - 4) Moving from point E to point C is accompanied by an increase in demand.
- a. Only statements 1 and 4 are true.
 - b. Only statement 1 is true.
 - c. Only statement 4 is true.
 - d. Only statements 2 and 3 are true.
 - e. None of these statements are true because all of these moves actually are changes in quantity demanded, not changes in demand..
- _____ 4. **(Repeat this answer on Scantron lines 30 and 31.)** If the Fed sells bonds in an open market operation, which of the following is most likely to occur?
- a. GDP will decrease, at least temporarily
 - b. the money supply increases
 - c. the interest rate falls
 - d. the aggregate demand curve shifts to the right
 - e. the open market operation is said to be expansionary

$$Y = \left(\frac{1}{1 - c(1 - t) + w} \right) (a + I_g + G - cT_f + X)$$

- _____ 5. **(Repeat this answer on Scantron line 32.)** Which of the following statements are true about "the multiplier" and "autonomous spending"?
- If the Keynesian model is correct, if the multiplier gets larger GDP will get smaller.
 - If the Keynesian model is correct, if the multiplier gets larger autonomous spending will get smaller.
 - Government spending is part of autonomous spending in the basic Keynesian model, but exports are not.
 - no other answer is true.
 - all other answers are true (except "no other answer is true").
- _____ 6. **(Repeat your answer on Scantron lines 33 and 34.)** (You may refer to the equation above.) Choose the **most complete answer**. Assume the Keynesian model gives correct answers. Suppose a recession abroad reduces exports by \$100 billion per year, also gross investment spending in the U.S. declines by \$100 billion per year, and also an increase in unemployment insurance payments increases autonomous consumption spending ("a" in the equation) by \$50 billion, then
- Both c and d are true.
 - Both c and e are true.
 - The economy will experience a recession.
 - The economy will experience no recession provided government spending is increased by \$150 billion.
 - The economy will experience no recession provided government spending is increased by \$200 billion.
- _____ 7. **(Repeat your answer on Scantron line 35.)** (You may refer to the equation above.) In the Keynesian multiplier model, if the marginal propensity to consume falls, the economy will
- expand
 - contract
 - not change
 - may either expand or contract
- _____ 8. **(Repeat this answer on Scantron lines 36 and 37.)** Using the AD/AS model, if there is an increase in the price of oil and the Fed wishes to maintain price stability, the Fed should
- do nothing because the economy must go into a recession to create a deflationary gap to reduce other costs of production
 - do nothing because the price level seldom changes when the price of oil increases
 - sell bonds in the open market
 - encourage firms to not adjust the wages they pay
 - buy bonds in the open market

- _____ 9. **(Repeat this answer on Scantron lines 38 and 39.)** If people used to expect prices to rise at 2% per year, but expected inflation now has risen to 5% per year,
- nominal interest rates will increase by exactly 3 percentage points, but real interest rates will not be affected very much in the long run.
 - interest rates will decline, since purchasing power now is eroding much faster than before.
 - wealth obviously will be redistributed in haphazard ways, since expected inflation always equals actual inflation--lenders will gain and borrowers will lose.
 - nominal interest rates will be affected far less than real interest rates, which will increase.
 - more than one of these answers is correct.
- _____ 10. **(Repeat this answer on line 40.)** Your instructor probably believes the following:
- As a general rule, the government not borrow money to pay for current consumption expenditures, and instead should pay for them with taxes.
 - As a general rule the government should not borrow money to fight a war, and instead should pay for them with taxes.
- 1 and 2 are both true.
 - 1 and 2 are both false
 - Only statement 1 is true.
 - Only statement 2 is true.

Equation for the Money Supply

$$M_s = (C_T + T_f + L_f) \frac{\left(1 + \frac{1}{r_{cd}}\right)}{\left(1 - \frac{x_d}{r_{cd}} + \frac{x_t}{r_{ct}}\right)}$$

- _____ 11. **(Repeat this answer on Scantron line 41.)** Suppose that two major U.S. banks unexpectedly fail. Many citizens lose access to their checking accounts for several weeks. Also assume the Fed stupidly does nothing--does not buy or sell Government securities, does not lend at the discount window, does not change reserve requirements. Evaluate each of the following statements and select the best answer. (Refer to the money supply equation given just above if this helps you.)
- x_d and x_t in the equation will increase because many bankers will fear a banking panic.
 - the public's desired ratios of currency to demand deposits, and currency to time deposits, will increase.
 - the money supply will increase because people will want to hold more cash than before, as a safety factor.
- all three statements are correct.
 - all three statements are false.
 - only statements 1 and 2 are correct.
 - only statements 2 and 3 are correct.
 - only statement 2 is correct.

- _____ 12. **(Repeat your answer on Scantron line 42.)** In the money supply equation just above, assume that $C_T = 50$; $T_f = 130$, $L_f = 20$; $r_d = .4$ and $r_t = .1$, $s_d = .3$ and $s_t = .6$; $r_{cd} = 1$ and $r_{ct} = 1$. Then
- the "money multiplier" is 1.34
 - the "money multiplier" is 1.00
 - the "money multiplier" is some other number than given in a) or b) above
 - if C_T increases to 75, the money supply will grow by more than 25
 - both c) and d) are correct
- _____ 13. **(Repeat your answer on Scantron line 43.)** In the money supply equation just above, if the "money multiplier" is .60, then if the Fed sells \$5 billion of Treasury bonds and at the same time puts \$5 billion of new currency into circulation, then the money supply will:
- increase by \$3 billion.
 - increase by \$5 billion.
 - increase by \$6 billion
 - increase by \$10 billion.
 - neither increase nor decrease.
- _____ 14. If, in the Aggregate Demand/Aggregate Supply model (as presented in the text and lecture) the two curves intersect to the right of Full Employment Output,
- 1) There is a "deflationary gap".
 - 2) Prices and wages will begin to rise, shifting the AS curve upward.
- Only statement 1 is correct.
 - Only statement 2 is correct.
 - Both statements 1 and 2 are correct.
 - Neither statement 1 nor 2 is correct.
- _____ 15. The increase in world oil prices in 1990 initially
- caused the AS curve to shift upward as wage rates quickly adjusted
 - increased the level of GDP associated with high price levels
 - shifted the aggregate expenditure line upward
 - caused the AS curve to shift upward due to higher costs per unit of output
 - caused the AD curve to shift leftward due to an increasing interest rate
- _____ 16. Stagflation is the combination of
- falling output and a falling price level
 - falling output and rising unemployment
 - falling output and a rising price level
 - falling output and falling unemployment
 - rising unemployment and a falling price level
- _____ 17. A labor union anticipates a 7 percent inflation rate in each of the next three years. It wants to obtain a 3 percent increase in real wages in each of those three years. To obtain this goal, the requisite nominal wage hike it should negotiate is
- 7 percent each year
 - 3 percent each year
 - 10 percent each year
 - 10 percent the first year and 3 percent each year thereafter
 - 21 percent the first year and 3 percent each year thereafter

- _____ 18. **(Repeat your answer on Scantron line 44.)** Suppose the nominal interest rate charged is 5 percent and the expected inflation rate is 2 percent. Which of the following is the expected real interest rate?
- 2 percent
 - 5 percent
 - 7 percent
 - 3 percent
 - 3 percent
- _____ 19. **(Repeat your answer on Scantron lines 45 and 46.)** In general, a higher-than-anticipated inflation rate
- helps everyone
 - hurts everyone
 - helps creditors and harms debtors
 - helps debtors and harms creditors
 - helps sellers
- _____ 20. Which of the following real-world phenomena does the classical model ignore?
- frictional unemployment
 - inflation
 - real output growth
 - cyclical unemployment
 - structural unemployment
- _____ 21. In the short-run macro model, what type of unemployment is caused by insufficient spending?
- cyclical
 - structural
 - frictional
 - seasonal
 - all types of unemployment are caused by insufficient spending
- _____ 22. The largest group of depository institutions (measured in terms of assets) is
- commercial banks
 - credit unions
 - savings and loan associations
 - mutual savings banks
 - ATM machines
- _____ 23. **(Repeat your answer on Scantron line 47.)** The Federal Reserve System was created in
- 1800
 - 1894
 - 1913
 - 1930
 - 1936
- _____ 24. How many districts does the Federal Reserve System have?
- 50
 - 1
 - 12
 - 48
 - 4

- _____ 25. **(Repeat your answer on Scantron line 48.)** Given the balance sheet below and assuming a required reserve ratio of 20 percent, how much (in dollar terms) is this bank actually holding in reserves?

<u>Assets</u>		<u>Liabilities and Net Worth</u>	
Property	\$ 5 million	Demand deposits	\$ 80 million
Government bonds	\$ 10 million		
Vault cash	\$ 15 million		
Deposited in Federal Reserve accounts	\$ 20 million	Net worth	\$ 20 million
Loans	<u>\$ 50 million</u>		
TOTAL ASSETS	\$100 million	TOTAL LIABILITIES PLUS NET WORTH	_____ \$100 million

- a. \$3.5 million
 b. \$8 million
 c. \$15 million
 d. \$20 million
 e. \$35 million
- _____ 26. How long are the terms of members of the Board of Governors in the Federal Reserve System?
 a. 2 years
 b. 4 years
 c. 6 years
 d. 14 years
 e. the remainder of the governor's life
- _____ 27. **(Repeat your answer on Scantron lines 49 and 50.)** The group within the Federal Reserve System that determines the general course for the nation's money supply is the
 a. Federal Monetary Oversight Committee
 b. Federal Advisory Council
 c. Board of Governors
 d. Department of Commerce
 e. Federal Open Market Committee

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Answer Section**

MULTIPLE CHOICE

1. ANS: A
2. ANS: E
3. ANS: D
4. ANS: A
5. ANS: D
6. ANS: A
7. ANS: B
8. ANS: A
9. ANS: A
10. ANS: C
11. ANS: C
12. ANS: B
13. ANS: E
14. ANS: B
15. ANS: D
16. ANS: C
17. ANS: C
18. ANS: E
19. ANS: D
20. ANS: D
21. ANS: A
22. ANS: A
23. ANS: C
24. ANS: C
25. ANS: E
26. ANS: D
27. ANS: E