INSTRUCTIONS

In each question there is only one correct answer. Select the answer you believe to be most correct. Each correct answer is worth 2 points.

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1. Aggregate demand is affected by
   a. shocks to the economy such as changes in the value of the stock market.
   b. government policy such as changes in taxes and government expenditures.
   c. Both of the above are correct.
   d. None of the above are correct.

2. When the Fed buys government bonds, the money supply curve
   a. shifts right.
   b. shifts left.
   c. does not change.
   d. becomes flatter.

3. When the interest rate increases, the opportunity cost of holding money
   a. increases, so the quantity of money demanded increases.
   b. increases, so the quantity of money demanded decreases.
   c. decreases, so the quantity of money demanded increases.
   d. decreases, so the quantity of money demanded decreases.

4. The quantity of money demanded is
   a. inversely related to the interest rate.
   b. independent of the interest rate.
   c. positively related to the interest rate.
   d. positively related to interest rates when interest rates are high and inversely related when interest rates are low.

5. In the short run, a decrease in the money supply causes interest rates to
   a. increase, and aggregate demand to shift right.
   b. increase, and aggregate demand to shift left.
   c. decrease, and aggregate demand to shift right.
   d. decrease, and aggregate demand to shift left.

6. A monetary injection by the Fed
   a. increases interest rates and increases aggregate demand.
   b. increases interest rates and decreases aggregate demand.
   c. decreases interest rates and decreases aggregate demand.
   d. decreases interest rates and increases aggregate demand.

7. If the stock market booms,
   a. aggregate demand increases, which the Fed could offset by increasing the money supply.
   b. aggregate demand increases, which the Fed could offset by decreasing the money supply.
   c. aggregate demand decreases, which the Fed could offset by increasing the money supply.
   d. aggregate demand decreases, which the Fed could offset by decreasing the money supply.
8. A decrease in government spending initially and primarily shifts
   a. aggregate demand right.
   b. aggregate demand left.
   c. aggregate supply right.
   d. neither aggregate demand nor aggregate supply.

For the following four questions, use the diagram below.

9. Which of the following would cause the aggregate demand curve to shift from AD₁ to AD₂?
   a. an increase in government purchases
   b. a decrease in stock prices
   c. consumers and firms become more optimistic about the future
   d. None of the above is correct.

10. If the economy is at point b, the correct policy to restore full employment would be
    a. an increase in the money supply.
    b. a decrease in government purchases.
    c. an increase in taxes.
    d. All of the above are correct.

11. Which of the following is true?
    a. A wave of optimism could move the economy from a to b.
    b. If aggregate demand moves from AD₁ to AD₂, the economy will stay at b in both the short and long run.
    c. It is possible that either fiscal or monetary policy might have caused the shift from AD₁ to AD₂.
    d. All of the above are correct.

12. Which of the following is not true?
    a. Unemployment rises as the economy moves from a to b.
    b. Either fiscal or monetary policy could be used to move the economy from b to a.
    c. As the economy moves from b to long-run equilibrium, the price level will fall further.
    d. At point b there is an excess demand for goods and services.
13. Which part of real GDP fluctuates most over the course of the business cycle?
   a. consumption
   b. government expenditures
   c. investment
   d. net exports

14. The classical dichotomy refers to the separation of
   a. real and nominal variables.
   b. changes in money and changes in government expenditures.
   c. endogenous and exogenous variables.
   d. business cycle and other variables.

15. According to classical economic theory, changes in the money supply
   a. affect nominal variables and real variables.
   b. affect nominal variables, but not real variables.
   c. affect exogenous variables, but not endogenous variables.
   d. affect real variables, but not nominal variables.

16. Most economists believe that classical economic theory is a good description of the world
   a. in the short run and in the long run.
   b. in the short run, but not in the long run.
   c. in the long run, but not in the short run.
   d. in neither the short nor long run.

17. The long-run aggregate supply curve shifts right if
   a. the capital stock increases.
   b. there is a hurricane.
   c. the government outlaws some production methods.
   d. None of the above are correct.

18. The long-run aggregate supply curve
   a. is vertical.
   b. is an application of the classical dichotomy.
   c. indicates monetary neutrality in the long run.
   d. All of the above are correct.
Consider the graph below for the following seven questions.

19. An increase in the money supply would move the economy from C to
   a. B in the short run and the long run.
   b. D in the short run and the long run.
   c. B in the short run and A in the long run.
   d. D in the short run and C in the long run.

20. An increase the money supply would move the economy from C to
   a. A in the long run.
   b. B in the long run.
   c. return to C in the long run.
   d. D in the long run.

21. If the economy is at A and there is a fall in aggregate demand, in the short run the economy
   a. stays at A.
   b. moves to B.
   c. moves to C.
   d. moves to D.
22. If the economy starts at A and there is a fall in aggregate demand, the economy moves
   a. back to A in the long run.
   b. to B in the long run.
   c. to C in the long run.
   d. to D in the long run.

23. If the economy starts at A and moves to D, the economy moves
   a. to A in the long run.
   b. to B in the long run.
   c. to C in the long run.
   d. back to D in the long run.

24. The economy would be moving to long-run equilibrium if it started at
   a. A and moved to B.
   b. C and moved to B.
   c. D and moved to C.
   d. None of the above are correct.

25. An adverse shift in aggregate supply would move the economy from
   a. A to B.
   b. B to C.
   c. C to D.
   d. D to A.

26. Gaussland has net exports of $400 million and buys $300 million of goods from overseas.
   Gaussland has
   a. $700 million of imports, and $700 million of exports.
   b. $400 million of imports, and $700 million of exports.
   c. $300 million of imports, and $400 million of exports.
   d. None of the above are correct.

27. A German company sells cameras to a retailer in the United States. These sales
   a. increase U.S. and German net exports.
   b. increase U.S. net exports and decrease German net exports.
   c. have no affect on U.S. net exports and increase German net exports.
   d. decrease U.S. net exports and increase German net exports.

28. If exports are less than imports, the trade balance
   a. is in deficit.
   b. is balanced.
   c. is in surplus.
   d. cannot be determined from this information alone.
29. An open economy's GDP is given by
   a. \( Y = C + I + G + S \).
   b. \( Y = C + I + G + NX \).
   c. \( Y = C + I + G \).
   d. \( Y = C + I + G + T \).

30. Which of the following equations is correct?
   a. \( S = I + C \)
   b. \( S = I - NX \)
   c. \( S = I + NFI \)
   d. Both b and c are correct.

31. A country has $100 million of Net Exports and $170 million of saving. Net Foreign Investment is
   a. $70 million and Domestic Investment is $70 million.
   b. $70 million and Domestic Investment is $270 million.
   c. $100 million and Domestic Investment is $70 million.
   d. None of the above are correct.

32. If the exchange rate is 45 rupee per dollar and it changes to 35 rupee per dollar, then a pair of sandals that costs 450 rupee in India would now cost
   a. more dollars.
   b. fewer dollars.
   c. the same number of dollars.
   d. None of the above is necessarily correct.

33. If the exchange rate changes from 120 yen per dollar to 100 yen per dollar, then the dollar has
   a. appreciated and so buys more Japanese goods.
   b. appreciated and so buys fewer Japanese goods.
   c. depreciated and so buys more Japanese goods.
   d. depreciated and so buys fewer Japanese goods.

34. Suppose that a bushel of wheat costs $3 in the United States and costs 20 pesos in Mexico. If the nominal exchange rate is 10 pesos per dollar, the real exchange rate is
   a. 3/2 bushels of Mexican wheat per bushel of American wheat.
   b. 2/3 bushels of Mexican wheat per bushel of American wheat.
   c. $2 per bushel of Mexican wheat.
   d. $1.50 per bushel of Mexican wheat.
35. If the nominal exchange rate $e$ is foreign currency per dollar, the domestic price is $P$, and the foreign price is $P^*$, the real exchange rate is defined as
   a. $e(P^*/P)$.
   b. $e(P/P^*)$.
   c. $e + P/P^*$.
   d. $e - P/P^*$.

36. To be counted as unemployed, a person must
   a. be in the labor force.
   b. be age 16 or older.
   c. not be working.
   d. All of the above are correct.

37. The labor-force participation rate
   a. equals 1 minus the unemployment rate.
   b. measures the percentage of the total adult population that is in the labor force.
   c. measures the percentage of the total adult population that is employed.
   d. measures the percentage of the labor force that is employed.

38. The BLS recently reported that there were 45.06 million people over age 16 who had at least a bachelor’s degree. Of this number 36.21 million were in the labor force and 35.54 were employed. What was the labor-force participation rate and the unemployment rate for this group?
   a. about 98 percent and 1.49 percent
   b. about 80 percent and 1.85 percent
   c. about 79 percent and 1.89 percent
   d. None of the above is correct.

39. Which of the following equations represents national saving in a closed economy?
   a. $Y - I - G - NX$
   b. $Y - I - C$
   c. $Y - C - G$
   d. $G + C - Y$

40. In a closed economy, what does $(T - G)$ represent?
   a. private saving
   b. public saving
   c. national saving
   d. investment
41. Suppose that in a closed economy GDP is equal to 8,000, Taxes are equal to 2,000, Consumption equals 5,000, and Government expenditures equal 1,000. What are private saving and public saving?
   a. 2000 and -2000  
   b. 2000 and 1000  
   c. 1000 and -1000  
   d. 1000 and 2000

42. The relationship between the quantity of output created and the quantity of inputs needed to create it is called
   a. the capital accumulation function.  
   b. the production function.  
   c. technological knowledge.  
   d. human capital.

43. Which of the following would increase productivity?
   a. an increase in the physical capital stock per worker  
   b. an increase in human capital per worker  
   c. an increase in natural resources per worker  
   d. All of the above are correct.

44. One way that government can encourage growth and, in the long run, raise the economy's standard of living is by encouraging
   a. population growth.  
   b. saving and investment.  
   c. consumption.  
   d. spending.

45. If there are diminishing returns to capital,
   a. increases in the capital stock eventually decrease output.  
   b. increases in the capital stock increase output by ever smaller amounts.  
   c. capital produces fewer goods as it ages.  
   d. new ideas are not as useful as old ideas.
46. The logic behind the catch-up effect is that
   a. workers in countries with low income will work harder than workers in countries with high
      incomes.
   b. the capital stock in rich countries deteriorates more rapidly than the capital stock in poor
      countries.
   c. new capital adds more to production in a country that doesn’t have much capital than in a
      country that already has much capital.
   d. None of the above are correct.

47. The price index in 2001 is 120, and in 2002 the price index is 126. What is the inflation rate?
   a. 5 percent
   b. 6 percent
   c. 26 percent
   d. The inflation rate is impossible to determine without knowing the base year.

48. Which change in the price index shows the greatest rate of deflation?
   a. 150 to 120
   b. 120 to 100
   c. 100 to 90
   d. 100 to 150

49. Because the CPI is based on a fixed basket of goods, substitution bias causes the index to
   a. overstate the increase in the cost of living from one year to the next.
   b. ignore any increase in the cost of living from one year to the next.
   c. understate the increase in the cost of living from one year to the next.
   d. sometimes understate, and sometimes overstate the increase in the cost of living from one year
      to the next.

50. Unmeasured quality change is a problem in the CPI because
   a. if the quality of a good deteriorates, the purchasing power of a dollar decreases even if the
      price of the good remains the same.
   b. the Bureau of Labor statistics does not attempt to account for quality changes that affect the
      standard of living.
   c. if the quality of a good improves, the purchasing power of a dollar increases even if the price
      of the good remains the same.
   d. a and c