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Economics 202

Midterm #2: Practice Midterm

Questions 1-3 relate to the market for Goods and Services.
1. If there are large increases in consumer expenditure within the Aggregate Demand-Aggregate Supply model (AD/AS model), then we observe which of the following:
a. there will be an increase in national output and increase in the price level
b. there will be a decrease in national output and decrease in the price level
c. there will be a decrease in national output and increase in the price level
d. there will be an increase in national output and decrease in the price level
e. there will be an increase in national output, but no change in the price level

2. Assume that at lower levels of GDP, the AS curve is flat but that as GDP increases, the AS curve becomes increasingly steep and ultimately vertical.
Which of the following best explains why this would occur:
a. at low levels of output, the price level is more flexible
b. any constraints on output decrease as GDP increases
c. prices rise more quickly as we approach full employment
d. productivity increases at higher levels of GDP

3. Which of the following is a true statement about the goods and services market:
a. an increase in the price level leads to a shift in the Aggregate Expenditure model (AE model):
b. an increase in the price level leads to a shift in the AD/AS model
c. the AD/AS model is a fixed price level model
d. the AE model is a flexible price level model

Questions 4-5 relate to the market for labor.
4. Which of the following is a true statement about labor markets:
a. when wages are constant, decreases in the demand for labor do not lead to a surplus of labor
b. decreases in the demand for labor lead will always lead to increases in both voluntary and involuntary unemployment
c. decreases in Aggregate Demand cause decreases in the supply of labor
d. when the labor market operates at an equilibrium, the market only experiences voluntary unemployment
e. increases in the wage causes a decrease in the demand for labor

5. When consumers demand fewer goods and services, how is the labor market affected?
a. decrease in labor supply
b. decrease in labor demand
c. no change in labor demand unless wages are flexible
d. no change in labor supply unless wages are flexible
e. decrease in both labor supply and labor demand

Questions 6 relate to the US market for Loanble Funds.

6. Assume that the US is currently experiencing capital inflow. In this situation, how does an increase in the demand for loanable funds affect this market?
a. there is a decrease in the quantity of domestic savings
b. there is no change in the quantity of domestic savings
c. there is a decrease in interest rates
d. there is a decrease in capital inflow
e. there is an increase in capital inflow

Questions 7-9 relate to the US market for Foreign Exchange with Japanese currency (the yen).

7. How does an increase in US exports to Japan affect the market for Foreign Exchange?
a. increase in the demand for Foreign Exchange
b. increase in the supply of Foreign Exchange
c. decrease in the demand for Foreign Exchange
d. decrease in the supply of Foreign Exchange
e. increase in both the demand for and supply of Foreign Exchange

8. How does an increase in capital outflow within the US affect the market for US Foreign Exchange with Japan?
a. increase in the price and quantity of Foreign Exchange
b. decrease in the price and quantity of Foreign Exchange
c. increase in the price of Foreign Exchange and decrease in the quantity of Foreign Exchange
d. decrease in the price of Foreign Exchange and increase in the quantity of Foreign Exchange

9. If we assume that the price of foreign exchange in this situation is equal to dollars divided by yen (i.e. $P_{FE} = \frac{\$}{Yen}$), then how is this market affected by an increase in the demand for Foreign Exchange?
a. the dollar appreciates relative to the yen
b. the yen appreciates relative to the dollar
c. the yen depreciates relative to the dollar
d. US goods are more expensive for Japanese citizens
e. both a and c are correct

10. In which situation are inventories most likely to rise unexpectedly:
a. when aggregate expenditure is greater than national output
b. when aggregate expenditure is less than national output
c. when aggregate expenditure is equal to national output
d. both a and b are correct

11. Autonomous consumption is defined as:
a. consumption that changes with changes in Gross Domestic Product (GDP)
b. consumption that changes with changes in interest rates
c. consumption that doesn't change with changes in disposable income
d. consumption that changes as inventories rise or fall
e. none of the above

12. Assume the following is true about consumption at different levels of disposable income:

Row	C	DI
1	7400	8000
2	7800	8500
3		10000

C = Consumption
DI = Disposable Income

In this situation, the quantity of consumption in Row 3 is:
a. 8000
b. 9000
c. 10000
d. 7500
e. none of the above

13. Which of the following is the best description of Potential GDP:
a. the output achieved when only voluntary unemployment exists
b. the output achieved when the economy is producing at full employment
c. the output achieved when all involuntarily unemployed workers get jobs
d. all of the above

14. Which of the following is a true statement about the marginal propensity to consume (MPC) within the AE model:
a. an increase in the MPC leads to an increase in the price level
b. an increase in the MPC leads to an increase in the government expenditure multiplier
c. an increase in the MPC leads to a decrease in Consumption Expenditure
d. an increase in the MPC leads to a decrease in the economy's real GDP
e. an increase in the MPC leads to AE increasing to an amount greater than real GDP

15. What problem(s) typically exist(s) with the implementation of expansionary fiscal policy?
a. the inside lag can be very long
b. rapid increases in deflation
c. expansionary policy is more difficult to implement than contractionary policy
d. expansionary fiscal policy tends to cause interest rates to decrease too much
e. all of the above

16. When we work with the AE model from class, we know that balanced budget spending leads to which of the following changes in equilibrium real GDP:
a. equilibrium real GDP will increase
b. equilibrium real GDP will not change
c. equilibrium real GDP will decrease
d. equilibrium real GDP can increase or decrease, depending on whether prices rise or fall

Questions #17-21 correspond with the Aggregate Expenditure model from class and relate to the equations below, which tell us about expenditure in Country X.

$C = 0.8DI + 4000$	C = consumption expenditures, DI = Disposable Income
$I = 4000$	I = investment expenditure
$G = 8000$	G = government expenditures
$T = 5000$	T = tax revenues
$X = 1000$	X = expenditure on exports
$M = 1000$	M = expenditure on imports
$DI = Y - T$	Y = real GDP

17. If Potential GDP is 50,000 (Yp = 50,000), there is a(n) _____________ gap of __________.
a. recessionary; 20,000
b. inflationary; 20,000
c. inflationary; 10,000
d. recessionary; 10,000
e. none of the above

18. Which of the following statements about this economy is true:
a. the value of the government expenditure multiplier is 4
b. the value of the tax multiplier is -4
c. the government's budget is in surplus
d. the government’s budget is balanced
e. there is a trade deficit

19. If the government increased taxes (T) by 1000, then:
a. equilibrium GDP would decrease by 5000
b. equilibrium GDP would decrease by 3000
c. equilibrium GDP would decrease by 4000
d. equilibrium GDP would increase by 3000
e. none of the above

20. If the government increased government expenditure (G) by 1000, then:
a. equilibrium GDP would increase by 5000
b. equilibrium GDP would increase by 3000
c. equilibrium GDP would increase by 4000
d. equilibrium GDP would decrease by 3000
e. none of the above

21. If there is an output gap of 10,000, such that Yp – Y* = 10,000, then the government could close this output gap by doing which of the following:
a. decrease G by 2000
b. increase G by 1000
c. increase G by 2000
d. increase G by 5000

22. Assume that the government chooses to increase government expenditure and that they will pay for that spending increase with (government) borrowing. When this occurs, we expect to observe which of the following outcomes:
a. an increase in interest rates
b. an increase in real GDP
c. an increase in the budget deficit
d. all of the above

23. Which of the following is the best description of a situation we called crowding out:
a. this is a situation where government borrowing lowers disposable income, which decreases private sector consumption
b. this is a situation where government borrowing decreases interest rates, which decreases private sector loans
c. this is a situation where government borrowing increases the price level, which decreases purchasing power
d. this is a situation where government borrowing decreases interest rates, which increases private sector investment
e. this is a situation where government borrowing increases interest rates, which decreases private sector investment

24. Increasing government expenditure during recessionary gaps and lowering government expenditure during inflationary gaps so that the budget is balanced on average over time has what effect on the business cycle?
a. causes the business cycle to become less extreme during these gaps
b. causes the business cycle to become more extreme during these gaps
c. causes the business cycle to become more extreme during recessionary gaps only
d. causes the business cycle to become more extreme during inflationary gaps only

25. Increasing government expenditure during recessionary gaps and lowering government expenditure during inflationary gaps so that the budget is balanced on average over time is an example of which budget balancing philosophy?
a. the balancing annually approach
b. the Functional Finance approach
c. the balancing over the business cycle approach
d. all of the above
e. both b and c are correct