

Econ 1A. Final Review Questions. Spring 2014

I. Multiple choices (120)

Circle the letter of the one answer that you think is correct or closest to correct.

1. Economics is the study of how people choose
 - a. abundance over scarcity.
 - b. to use limited resources.
 - c. to use their infinite resources.
 - d. scarcity over abundance.

2. Economic models
 - a. do not address questions about the economy.
 - b. are better if they include most of the detail of the real economy.
 - c. rely on simplification.
 - d. make no assumptions that have not been proved.

3. Output combinations inside a PPF
 - a. are unattainable.
 - b. are attainable only with the full utilization of all resources.
 - c. are associated with unemployment.
 - d. result in more rapid growth.

4. Trade + Specialization + CA leads to
 - a. an increase in absolute advantage.
 - b. a decline in the standard of living of a country.
 - c. a decrease in the total available goods and services.
 - d. an increase in the total available goods and services.

5. If opportunity cost is constant, PPF would be
 - a. bowed outward.
 - b. bowed inward.
 - c. a straight line.
 - d. positively sloped.

6. Which of the following will not affect DD for fishing poles?
 - a. pollution of local streams and rivers.
 - b. an increase in the price of fishing licenses.
 - c. an increase in the population.
 - d. an increase in the price of a fishing pole.

7. Equilibrium in a market indicates:
 - a. scarcity is eliminated.
 - b. quantity demanded equals quantity supplied.
 - c. price equals quantity.
 - d. everyone is content.

8. The standard of living is measured by the level of
 - a. RGDP.
 - b. GDP.
 - c. RGDP per person.
 - d. GDP per person.

9. GDP using the expenditure approach equals
- a. $C+S+G+(X-M)$ b. $C+S+G-(X-M)$. c. $C+I+G+(X-M)$. d. $C+I+G-(X-M)$.
10. When the economy is at full employment the
- a. $NUR = 0$. b. $NUR = UR$. c. $NUR = 10\%$. d. $UR = 0$.
11. Assume that U.S. population is 220, the labor force is 150. The labor employed is 130, what is the unemployment rate
- a. 9.0%. b. 13.3%. c. 11.4%. d. 15.4%.
12. If the CPI in 1990 was 100 and the CPI in 1991 was 115, the rate of inflation was
- a. 1.5%. b. 15%. C. 100%. D. 115%.
13. The real interest rate (r) is equal to the
- a. $i - \pi$ b. $i + \pi$. c. $i \times \pi$. d. $i \div \pi$.
14. If the population growth rate is 0.9% and GDP growth rate is 4.4% during a year, the growth rate of RGDP per person is
- a. 3.5 %. b. 5.3%. c. 4.4 %. d. none of the above.
15. Which of the following is not a source of growth in labor productivity?
- a. S and I in physical capital. b. expansion of human capital.
c. the wage rate. d. discovery of new technology.
16. The best example of money is
- a. check. b. ATM card. c. credit card. d. none of the above.
17. In order to conduct monetary policy, Fed. adjusts
- a. nominal interest rate. b. quantity of money. c. tax rates. d. unemployment rate.
18. A loan is a bank's
- a. asset. b. reserve. c. liability d. net worth.

19. "Crowding out" refers to a situation where
- G, financing through borrowing, reduces C.
 - G, financing through borrowing, encourages high level of I.
 - G, financing through borrowing, stimulates S by domestic residents.
 - G, financing through borrowing, reduces I.
20. Suppose required reserve ratio = 20%. If Capital Bank has deposits of \$200 and total assets of \$1000, the amount of required reserve is
- \$200.
 - \$1,200.
 - \$40.
 - \$160.
21. Control of the nation's money supply is handled by
- Congress.
 - the Federal Reserve System.
 - The President.
 - Commercial banks.
22. Which of the following statement is true? Holding everything else constant,
- an economy can eliminate an inflationary gap ($Y > Y_p$) by $G \uparrow$.
 - when $Y_p > Y$, the economy faces a recessionary gap.
 - expansionary fiscal policy refers to $Tax \uparrow$.
 - when AS intersects AD to the right of LAS, the economy faces a recessionary gap.
23. Which of the following does not shift AD?
- a decrease M.
 - an increase in I.
 - an increase in taxes.
 - an increase in P.
24. A recessionary gap means the short-run macroeconomic equilibrium Y
- is less than Y_p .
 - equals Y_p .
 - is more than Y_p .
 - all of the above.
25. As the price level falls, the quantity of real wealth (A/P) _____ and the aggregate quantity of RGDP demanded _____.
- increases; increases.
 - increases; decreases.
 - decreases; increases.
 - decreases; decreases.
26. If the Fed carries out the open market operation and sells US government securities, MB
- fall and M increases.
 - rises and M increases.
 - fall and M decreases.
 - rise and M decreases.

27. National saving equals

- a. $S + (T - G)$. b. $S + (T - G) + (M - X)$. c. $(T - G) + (M - X)$ d. all of the above.

28. If Rob deposits \$300 in currency into his savings account at Bank of America,

- a. M1 decreases. b. M1 does not change.
c. M2 increases. d. M2 decreases.

29. Holding everything else constant, an economy can eliminate an inflationary gap ($Y > Y_p$), i.e., it can decrease inflation by

- a. $G \uparrow$ and $Tax \downarrow$. b. $AD \downarrow$ and $M \downarrow$. c. $M \uparrow$. d. $AD \uparrow$ and $M \uparrow$.

30. The Fed purchases \$1 million of U.S. Treasury Bill from Bank of America. The desired reserve ration (R) = 0.1, currency-deposit ration (C) = 0.5, and banks loans all excess reserves. The money multiplier is

- a. 0.1. b. 0.6. c. 10. d. 2.5.

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1: b. 2: c. 3: c. 4: d. 5: c. 6: d. 7: b. 8: c. 9: c. 10: b. 11: b. 12: b. 13: a. 14: a. 15: c. 16: d. 17: b. 18: a. 19: d. 20: c. 21: b. 22: b. 23: d. 24: a. 25: a. 26: c. 27: a. 28: a. 29: b. 30: d.

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II. The economic model of market is a very powerful tool for explaining many economic problems.

1. Explain carefully under what assumptions we can use DD and SS curves to describe the market. [10]
2. Use DD and SS curves to evaluate the following two statements: (**Please state the cause and the effect explicitly**)
 - a. The price of milk has been rising due to unusually hot summer weather which discourages milk production. (9/16/96, San Jose Mercury News). [10]
 - b. Higher chicken prices on the way as producers plan to cut supply by killing off mother hens. (3/23/96, San Jose Mercury News). [10]

III. Potential GDP (Y_p) model shows the relationship between employment (L) and Y_p .

1. Explain carefully under what assumptions we can use $Y = F(L;K,N,E)$ and LD and LS curves to describe the Y_p model. [10]
2. Suppose the following events occur. Use Potential GDP (Y_p) model to show the effects of each event on w (real wage), L_f (full employment quantity of labor) and Y_p (potential RGDP) **graphically**. Please state the **cause** and the **effect** explicitly.
 - (a) In US, more teenagers go to college this year. [10]
 - (b) Dell introduces a new supercomputer that everyone can afford. [10]

IV. The loanable funds market provides the channels through which saving (S) flow to finance the investment (I) in new capital (ΔK) that make the economy grow.

- a. Under what assumptions we can use DLF and SLF curves to describe the loanable funds market? [10]
- b. Please utilize the loanable funds market, i.e., PDLF, DLF & SLF, to examine the impact of government budget deficit, i.e., $T - G < 0$ on real interest rate (r) and quantity of private loanable fund demanded, i.e., private investment (I) **graphically**. Also state **Cause** and **Effect** explicitly. [15]
- c. What is crowding out effect? Show the amount of crowding out in your graph in b. [5]

V. The AS-AD model is the workhorse model of macroeconomics because it explains how the behavior of producers, consumers and the government influences the economy's short-run fluctuations around the trend of long-run growth.

- a. Under what assumptions we can use this model to describe an economy? [10]
- b. Explain carefully what is the full employment (long-run) macroeconomic equilibrium? Plot AD, AS, LAS and show the equilibrium P and Y graphically. [5]
- c. Professor Martin Feldstein (former economic adviser to President Regan) pointed out that "Falling home prices have ...reduced homeowner wealth (A) by about \$3 trillion; the stock market decline has cut wealth by additional \$8 trillion. This reduced household wealth is causing consumers to cut spending." If the economy is in long-run macroeconomic equilibrium, show the impact of home prices falling and stock market decline on AD, P , Y and UR. Is the economy facing an inflationary or a recessionary gap? Please explain your answer **verbally** and **graphically**. [15]