Exam

Name___________________________________

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

Use the information provided below to answer the following questions.

The non-institutional civilian population is 250 million, of which 100 million are employed and 10 million are unemployed.

1) Based on the information above, the unemployment rate is 1) ________

A) 6.6%. B) 11.1% C) 10%. D) 4%. E) 9.1%.

2) As the unemployment rate falls, 2) ________

A) the proportion of the unemployed finding a job increases.
B) the separation rate increases.
C) the young and unskilled experience larger-than-average decreases in unemployment.
D) both A and C.
E) all of the above

3) If efficiency wage theory is valid, we would expect a relatively low premium over the reservation wage when 3) ________

A) workers can be easily monitored.
B) the job requires very little training.
C) the unemployment rate is low.
D) workers have few other options for employment in the area.
E) all of the above

4) In the wage-setting relation, the nominal wage tends to decrease when 4) ________

A) unemployment benefits decrease.
B) the unemployment rate decreases.
C) the minimum wage increases.
D) the price level increases.
E) all of the above

5) An increase in the minimum wage will tend to cause which of the following? 5) ________

A) an upward shift in the WS curve
B) a downward shift in the WS curve
C) an upward shift in the PS curve
D) a downward shift in the PS curve
E) none of the above

6) For this question, assume that Y = N. Based on our understanding of the labor market model presented in Chapter 6, we know that a reduction in the markup will cause 6) ________

A) no change in the natural level of output.
B) an increase in the natural level of output.
C) a reduction in the natural level of output.
D) a reduction in the natural level of employment.

7) In the aggregate supply relation, the current price level depends upon 7) ________
A) monetary policy.
B) fiscal policy.
C) expected price level.
D) consumer confidence.
E) all of the above

8) The neutrality of money is consistent with which of the following statements? 8) ________
A) changes in the money supply will not affect the price level in the medium run
B) changes in the money supply will not affect employment in the medium.
C) changes in the money supply will not affect the price level in the short run
D) changes in the money supply will not affect employment in the short run.

9) Assume the economy is initially operating at the natural level of output. Now suppose that individuals decide to reduce their desire to save. We know with certainty that which of the following will occur in the short run as a result of decreased desire to save? 9) ________
A) higher output and lower investment
B) greater investment
C) no change in the economy at all
D) an increase in the nominal wage
E) less investment

10) The short-run aggregate supply curve (AS) presented in the textbook has its particular shape because of which of the following explanations? 10) ________
A) an increase in the aggregate price level causes an increase in nominal money demand and an increase in the interest rate.
B) a reduction in output causes a reduction in employment, an increase in unemployment, a reduction in the nominal wage and a reduction in the price level.
C) a reduction in the aggregate price level will cause a reduction in the interest rate and an increase in output.
D) a drop in the nominal wage causes an increase in the amount of output that firms are willing to produce.

11) A reduction in the price of oil will tend to cause which of the following? 11) ________
A) no change in the interest rate in the medium run
B) an increase in the aggregate price level as output increases
C) an increase in investment in the medium run
D) no change in the real wage in the medium run

12) For this question, assume that the economy is initially operating at the natural level of output. An increase in consumer confidence will cause 12) ________
A) ambiguous effects on the real wage in the medium run.
B) a reduction in the real wage in the medium run.
C) an increase in the real wage in the medium run.
D) no change in the real wage in the medium run.

13) Suppose bank A has assets of 100, liabilities of 60, and capital of 40. Its leverage ratio is 13) ________
A) 0.4. B) 0.6. C) 2.5. D) 1.5.

14) Ted spread is 14) _______
A) the difference between the riskless rate and return on stocks.
B) the difference between the riskless rate and the rate at which banks are willing to lend to each other.
C) the difference between the riskless rate and the yield on corporate bonds.
D) none of the above

15) American Recovery and Reinvestment Act 2009 calls for 15) _______
A) both tax increases and government spending reductions.
B) both tax increases and government spending increases.
C) both tax reductions and government spending reductions.
D) both tax reductions and government spending increases.

16) An open market purchase of bonds by the central bank will cause which of the following when a liquidity trap situation exists? 16) _______
A) the money supply, M, will not change.
B) the interest rate will not change.
C) the interest rate will decrease.
D) output will increase.
E) none of the above

17) One of the possible solutions for the Japanese slump is to 17) _______
A) maintain a constant aggregate price level.
B) implement macroeconomic policies to create inflation.
C) maintain the real interest rate at its original level.
D) none of the above

18) When inflation has NOT been very persistent, as was the case in the United States before the mid-1960s, we can expect that 18) _______
A) the current inflation rate will not depend heavily on past years' inflation rates.
B) lower unemployment rates will be associated with higher inflation rates.
C) the expected price level for a given year will equal the previous year's actual price level.
D) all of the above
E) none of the above

19) For this question, assume that the expected rate of inflation is a function of past year's inflation. Also assume that the unemployment rate has greater than the natural rate of unemployment for a number of years. Given this information, we know that 19) _______
A) the rate of inflation should neither increase nor decrease.
B) the inflation rate will be approximately equal to the natural rate of unemployment.
C) the rate of inflation should steadily decrease.
D) the rate of inflation will approximately be equal to zero.
E) the rate of inflation should steadily increase over time.

20) Suppose the Phillips curve is represented by the following equation: $\pi_t - \pi_{t-1} = 20 - 2u_t$. Given this information, we know that the natural rate of unemployment in this economy is 20) _______
A) 10%.
B) 5%.
C) 6.5%.
D) 20%.
E) none of the above

21) Which of the following explains why the original Phillips curve relation disappeared or, as some economists have remarked, "broke down" in the 1970s? 21) ______

A) individuals assumed the expected price level for the current year would be equal to the actual price level from the previous year.
B) more labor contracts became indexed to changes in inflation.
C) individuals assumed that expected inflation would be zero
D) monetary policy became contractionary.
E) individuals changed the way they formed expectations of inflation.

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

22) Based on your understanding of the aggregate supply and aggregate demand model and the IS-LM model, graphically illustrate and explain what effect a tax increase will have on the economy. In your graphs, clearly illustrate the short-run and medium-run equilibria.

1) E
2) D
3) A
4) A
5) A
6) B
7) C
8) C
9) D
10) B
11) C
12) D
13) C
14) B
15) D
16) B
17) B
18) D
19) C
20) A
21) E
22) A tax increase will cause a reduction in consumption and a leftward shift in both the IS and AD curves. As demand falls, firms will reduce employment to cut production. This will cause an increase in u and a reduction in W. As W falls, firms' costs fall and they cut prices. Once expectations adjust to the higher price level, the adjustment will be similar to that described in the textbook. The economy will return to the natural level of output at a lower price. The interest rate will be lower causing all of the decreased consumption to be offset by the increase in investment.