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American University of Beirut
Economics Department



Exam II, Spring 2004
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Time: 50 minutes

Student Name: _____

ID number: _____

Please count the number of pages.
You should have 9 pages.

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Good Luck!

If the economy is currently producing more than its full employment level of output, which of the following would be most likely to direct the economy back to its potential output?

- a. An increase in prices of factors of production
- b. A decrease in prices of factors of production
- c. An expansionary fiscal policy
- d. Optimistic expectations of future profits

The government granted a patent to Aspirin's inventors for a number of years. As a result:

- a. Aspirin enjoyed a monopoly
- b. Aspirin and Panadol became a duopoly
- c. An oligopoly between Aspirin and a number of other producers was created
- d. Aspirin and thousands of producers of similar products formed a perfectly competitive industry

Use the figure below to answer the following 5 questions:

What rate of output maximizes total profit?

- a. $Q = 4.5$
- b. $Q = 5$
- c. $Q = 4$
- d. $Q = 5.5$

What is MR at this rate of output?

- a. $MR = 7$
- b. $MR = 8$
- c. $MR = 10$
- d. $MR = 9$

What is the price at this rate of output?

- a. $P = 7$

- b. $P = 8$
- c. $P = 10$
- d. $P = 9$

If output is increased beyond that point, what is the relationship of MC to MR?

- a. $MC = MR$
- b. $MC > MR$
- c. $MC < MR$
- d. Cannot be determined

How will this affect total profit?

- a. Total profits will increase
- b. Total profits will remain the same
- c. Total profits will decrease
- d. Cannot be determined

Which of the following would most likely cause both inflation and unemployment to decrease?

- a. an increase in government spending
- b. a decrease in government spending
- c. a tax increase
- d. a technological innovation

From year 1 to year 2, the price of all goods exactly doubles, but the quantities produced of all goods remain constant. It can be concluded that from year 1 to year 2,

- a. both nominal GDP and real GDP doubled.
- b. both nominal GDP and real GDP remained constant.
- c. nominal GDP doubled, but real GDP remained constant.
- d. real GDP doubled, but nominal GDP remained constant.

From year 1 to year 2 the price level index and nominal GDP both increase, but nominal GDP increased by a larger percent than the price level increased. It can be concluded that from year 1 to year 2 real GDP

- a. increased by a larger percent than nominal GDP increased.
- b. increased by a smaller percent than nominal GDP increased.
- c. increased by a larger percent than the price level index increased.
- d. increased by a smaller percent than the price level index increased.

If some of the unemployed became discouraged and stopped looking for work, which of the following would result?

- a. the labor force would decrease and the unemployment rate would decrease
- b. the labor force would decrease and the unemployment rate would

- remain the same
- c. the labor force would increase and the unemployment rate would decrease
 - d. the labor force would decrease and the unemployment rate would increase

The labor force is made up of:

- a. the number of people employed minus the number of people unemployed
- b. the whole population
- c. just the number of people employed
- d. the number of people employed plus the number of people unemployed

During 1998, a business produced \$20 million worth of goods but sold only \$19 million. Is the \$1 million increase in inventories (produced but not sold goods) part of the gross domestic product in 1998?

- a. No, because inventories are intermediate goods
- b. No, because if these inventories were later sold in 1999, they would be counted twice.
- c. Only if the inventories are sold; otherwise they will never be counted
- d. Yes, because these inventories are part of the output of the economy in 1998.

If a large number of students graduate from college, which category of unemployment would increase?

- a. structural unemployment
- b. frictional unemployment
- c. cyclical unemployment
- d. they would have no effect on unemployment

Which one of the following would not shift the aggregate demand curve?

- a. a change in the price level
- b. optimistic expectations about firms' future performance
- c. a decline in the interest rate at each possible price level
- d. an increase in tax rates

Jade is writing an article about government expenditures and their effect on economic activity; which conclusion does he not reach?

- a. Government construction of highways have no effect on the level of production
- b. Government spending on national defense definitely positively affects economic activity, which would positively affect the level of GDP
- c. Government spending on public schools has no effect on the level of GDP
- d. Both a and c

A contractionary fiscal policy should cause:

- a. higher prices, higher output and lower unemployment
- b. higher prices, lower output and higher unemployment
- c. lower prices, lower output and higher unemployment
- d. lower prices, higher output and lower unemployment

Assume that Lebanon's CPI (consumer price index) this year is 180 versus last year's 200. What is the inflation rate?

- a. Around 10% of inflation
- b. Around 1% of inflation
- c. Around 10% of deflation
- d. Around 1 percent deflation
- e. We cannot calculate it from the above information

Suppose that Nader already knows that the inflation rate in 2004 will be 10% and he aims at a 2% increase in his REAL purchasing power . In that case, he would want to index his next one-year wage to:

- a. At least, the 10%, the inflation rate
- b. At least 2%, after all increasing his one-year wage by 2% will increase his real purchasing power by 2%
- c. At least 12%
- d. None of the above, his boss will make the decision of his raise based on his performance

Suppose the economy of Wonderland produces 3 CDs at \$15 a CD, 6 gallons of ice cream at \$3 a gallon and 10 cases of Red Bull pops at \$5 a case. The gross domestic product of Wonderland is:

- a. \$19
- b. \$23
- c. \$83
- d. \$113

If real GDP for last year was \$200 billion and real GDP this year is \$250, then the growth rate of real GDP is

- a. \$50
- b. 20%
- c. 25%
- d. 2%

A business cycle is:

- a. Seasonal variations in the sales of a private business
- b. When output 1st climbs to a peak, then decreases. After hitting a trough, the economy recovers, with real GDP increasing again
- c. Not an economic concept, only business students know how to answer this question

A recession occurs when:

- a. Output declines for 2 or more consecutive quarters
- b. Output increases for 2 or more consecutive quarters
- c. The mood of the people in an economy is depressed, it is only a psychological concept
- d. A government monopoly shuts down for 2 or more consecutive quarters

If nominal GDP stayed the same while real GDP doubled. We can conclude that:

- a. both prices and quantities have doubled
- b. prices have doubled while quantities have stayed the same
- c. prices have stayed the same while quantities have doubled
- d. quantities have doubled while prices have halved

If the price of computers doubles in an economy, while prices of other goods remain unchanged:

- a. It means that the economy is experiencing an inflation of 100%
- b. It means that the economy is experiencing a in the relative prices of computers
- c. It means that the economy is experiencing a high level of unemployment
- d. It means that the economy is experiencing an inflation of 50%

Assume that the average worker produces \$10,000 of GDP. Also assume that there are 2 million labor-force participants and the unemployment rate is 5.2 percent. How much is GDP?

- a. \$104 thousand
- b. \$18.960 million
- c. \$ 20 billion
- d. Cannot be calculated from the information above

Using the same information in the question above, please calculate the increase in GDP if the unemployment rate rises from 5.2% to 4.5%.

- a. GDP will stay the same
- b. GDP will increase by \$140 million
- c. GDP will increase by \$19 million
- d. GDP will increase by \$18 million

Assume the economy to be at full employment and that investment spending declines dramatically. Under these conditions:

- a. There will be an increase in AD which will cause a higher price level and higher GDP
- b. There will be a decrease in AD which will cause a lower price level and lower GDP

- c. There will be an increase in AS which will cause lower price level and higher GDP
- d. There will be a decrease in AS which will cause a higher price level and lower GDP

Due to the recession that has hit the Lebanese economy, Lara was laid off from her job as a manager at Starbucks. Lara is considered:

- a. Frictionally unemployment
- b. Structurally unemployment
- c. Cyclically unemployment
- d. Not yet in the labor force

Assume that, between 1999 and 2000, the nominal GDP of an economy increased to \$ 5 trillion and that the appropriate price index increased from 100 to 125. Which of the following expresses GDP in 2000 in terms of 1999 prices (real GDP)?

- a. \$ 3 trillion
- b. \$3.2 trillion
- c. \$4 trillion
- d. \$5 trillion

An example of an expansionary fiscal policy is:

- a. A tax cut
- b. An increase in the money supply
- c. A tax increase
- d. A cut in government spending

The consumer price index this year is 150 versus last year's 125. We have experienced X inflation. How much does X stand for?

- a. 10% inflation
- b. 15% inflation
- c. 20 inflation
- d. 25% inflation

Jordan's government decides to decrease the prices of electricity, telecom, and land (which are all considered to be factors of production for Jordanian industry) in the suburbs of Amman. This move will have the following impact:

- a. prices will fall and output will remain fixed
- b. output will increase even though prices will climb
- c. output will fall because of lower prices
- d. output will climb and prices will fall

Car workers have been unfortunate in that technological innovations such as the introduction of robots have led to a decreased demand for their skills. We consider them as:

- a. frictionally unemployed
- b. structurally unemployed
- c. cyclically unemployed
- d. cannot be determined from the given information

If the nominal interest rate on a loan was set to be 10% because the expected inflation was 5% at the time the loan was set. One year later, at the time of repay, the inflation rate turned out to be 8%. Given this information, we can deduce that:

- a. lenders were better off; the interest rate received is above the inflation rate.
- b. Borrowers were better off; high unexpected inflation benefits anyone who has to pay
- c. They are both neutral
- d. Cannot be determined from the above information

If the nominal interest rate was 8%, but the inflation rate was 3%, then the real interest rate is:

- a. 3%
- b. 5%
- c. 8%
- d. cannot be determined from the given information

Determinants behind consumption include:

- a. Expectations of future income
- b. Income minus taxes or disposable income
- c. Wealth
- d. All of the above

The relationship between MPC and MPS is:

- a. A direct relationship based on the relationship between C and S
- b. $MPS = 1 - MPC$
- c. Both a and b
- d. Neither a nor b

If the monopoly sets the price at 15\$. The $ATC = \$10$ and $AVC = 8\$$. What should the monopolist do?

- a. The monopolist should shut down

- b. The monopolist is making a profit of \$5 per unit and should continue operating
- c. The monopolist is making a profit of \$7 per unit and should continue operating
- d. The monopolist is making a profit of \$10 per unit and should continue operating

The population size is 20 million and the number of people unemployed is 5 million. Then the unemployment rate is:

- a. 5%
- b. 25%
- c. 75%
- d. cannot be determined from the given information