

**MIDTERM I – Practice Test**

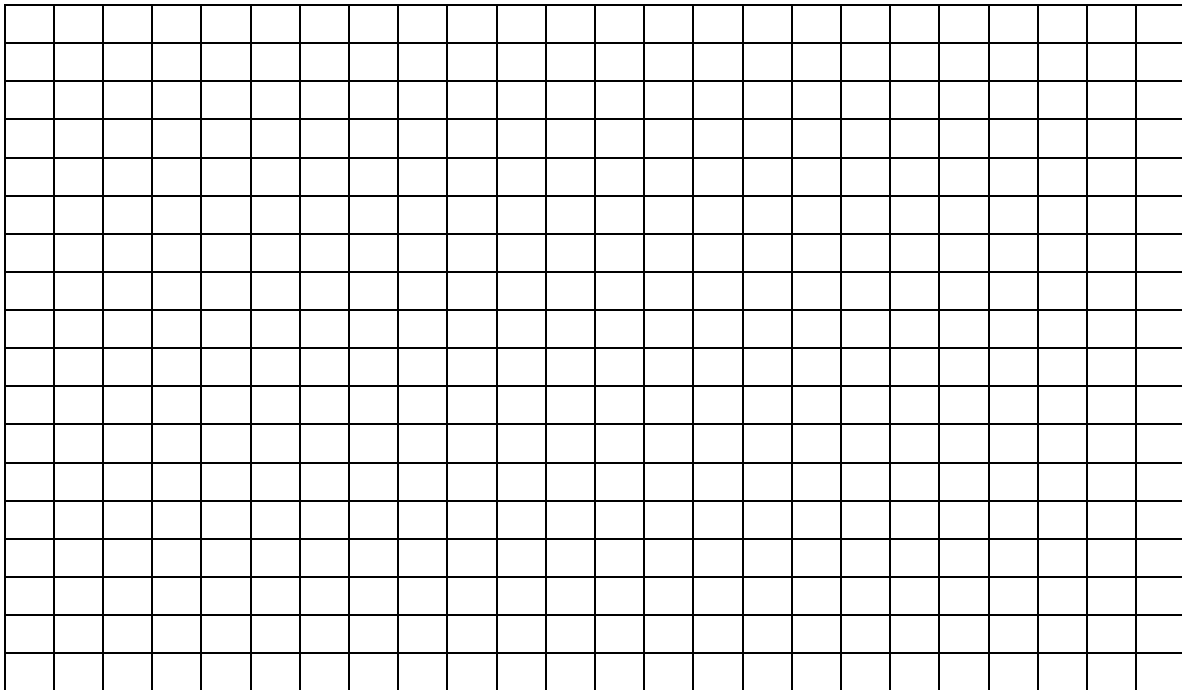
**Question 1: True-False. Please explain your choice.**

- |  |   |   |
|--|---|---|
| a) A change in the price of carrots will cause a movement along the demand curve for substitute vegetables and a shift in the demand for carrots.              | T | F |
| b) An increase in the number of Americans taking vacations in Mexico would be expected to increase the value of the peso.                                      | T | F |
| c) The four phases of the business cycle are, <u>in order</u> , peak, expansion, trough, and recession.  | T | F |
| d) There is no difference in Macroeconomics between short-run stabilization policy and long-run growth policy  | T | F |
| e) Nominal GDP can never be equal to real GDP.   | T | F |
| f) An increase in the number of firms causes the supply curve to shift rightward, resulting in a decrease in price and a movement down along the demand curve. | T | F |
| g) An effective price ceiling causes excess demand, resulting in the need to ration.   | T | F |

**Question 2:**

As a result of the phenomenal performance of the U.S. stock market in the late 1990s European investors invested heavily in U.S. stocks. At the same time U.S. investors predominantly invested at home, rather than abroad.

Using supply/demand analysis, show graphically why the value of the euro relative to the dollar declined after it was first introduced in 1999. Explain your graphs.



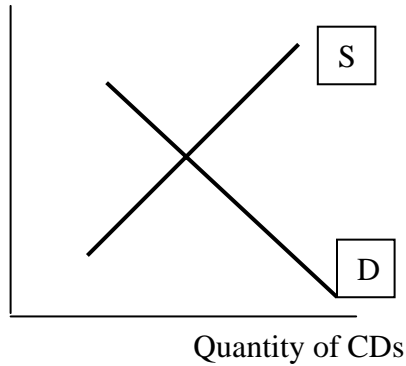
**Question 3:**

Why might per capita GDP comparisons between countries be misleading? What do economists do to avoid some of the problems?

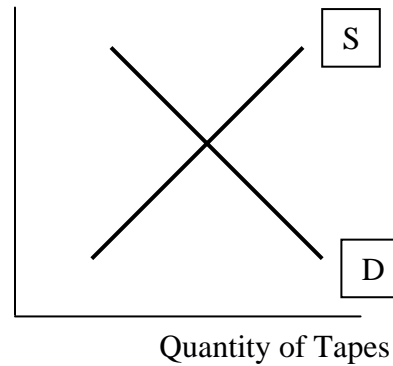
**Question 4:**

The two accompanying diagrams show supply and demand curves for two substitute commodities: Tapes and CDs (Compact Discs).

Price of CDs



Price of Tapes



- a) On the right hand diagram, show what happens when the rising raw material prices make it costlier to produce tapes. Explain!
- b) On the left hand diagram, show what happens to the market for CDs. Explain!

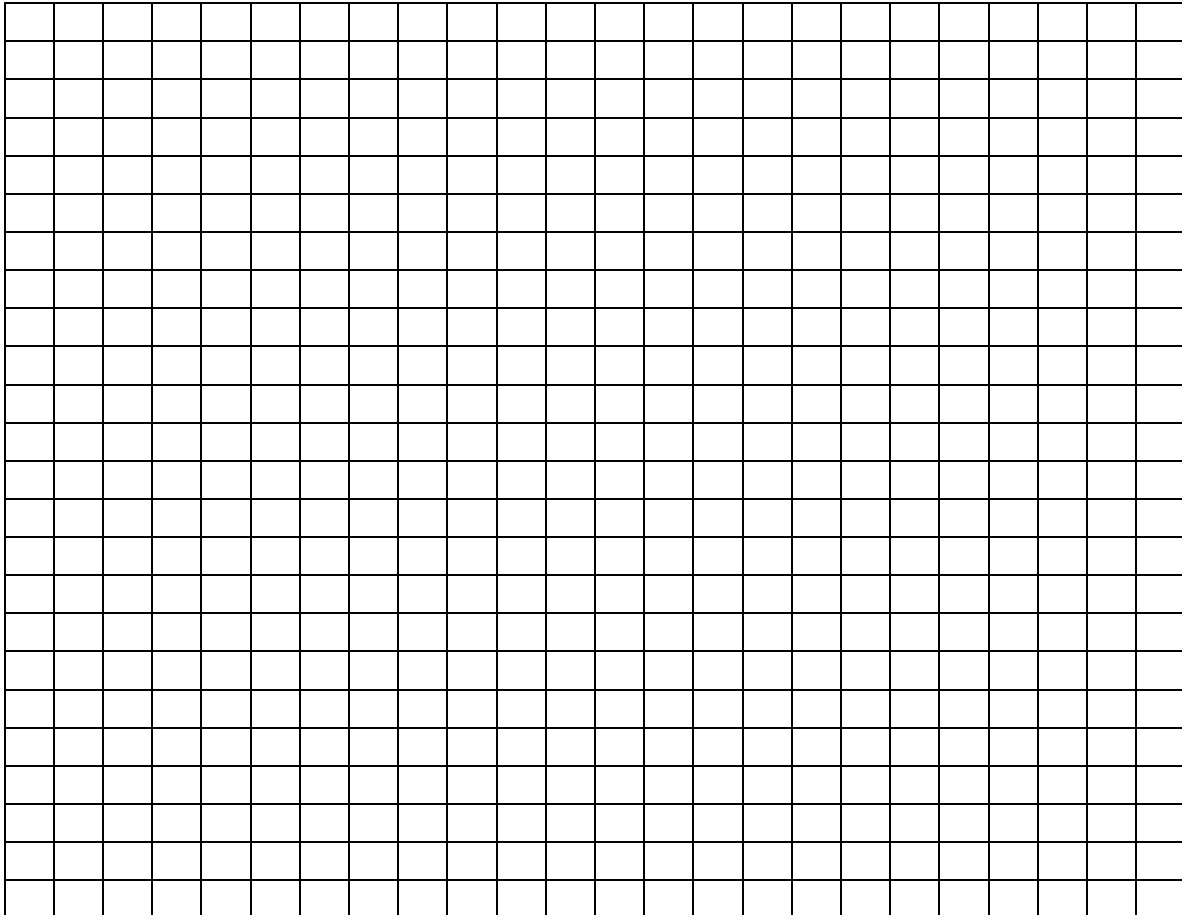
**Question 5:** How is the unemployment rate calculated? Describe the three principal types of unemployment.

**Question 6:**

Suppose the United States and Japan have the following production possibilities tables:

Japan		United States	
Rice	Wheat	Rice	Wheat
1000	0	500	0
800	100	400	200
600	200	300	400
400	300	200	600
200	400	100	800
0	500	0	1000

- a) Draw each countries production possibilities curve.
- b) Define the concept of 'comparative advantage'.
- c) In what good does the United States have a comparative advantage? Japan?



**Question 7:**

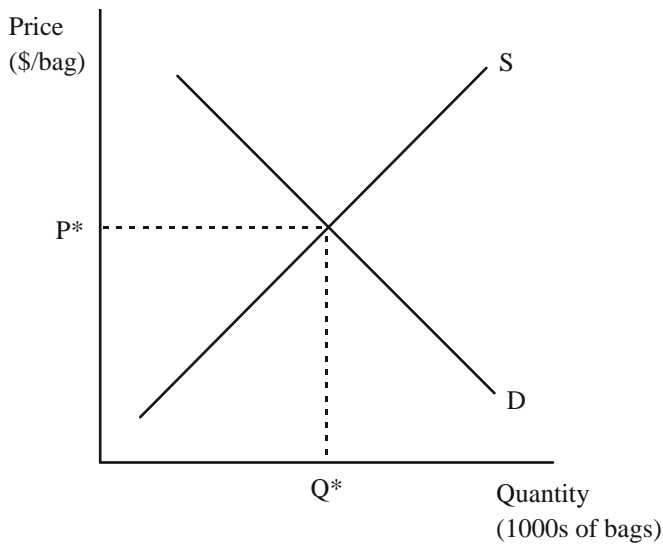
Below is the production possibilities table for the country of Lavaland.

% resources devoted to production of tanks	Number of tanks	% resources devoted to production of pizza	Number of pizzas	Row
0	0	100	15	A
20	4	80	14	B
40	7	60	12	C
60	9	40	9	D
80	11	20	5	E
100	12	0	0	F

- (a) Use the information in the Table to draw the production possibilities curve (PPC) for Lavaland. Put tanks on the horizontal axis.
- (b) What is the cost to Lavaland of moving from point A to point B on its PPC? Of moving from point E to point F?
- (c) What general economic principle is being illustrated by your answers to part (b) above? Explain.

**Question 8:**

Consider the following supply and demand diagram for Tootsie Rolls. Note that the market is currently in equilibrium, with a price of  $P^*$  and a quantity exchanged of  $Q^*$ .



For each of the scenarios below, draw a picture that illustrates the impact on price and quantity exchanged. Explain each of your pictures by describing what is happening to the **demand** side of the market.

- (a) The American Association of Chocolate Lovers designates the Tootsie Roll as its official candy.
- (b) The Tootsie Roll Company computerizes their Tootsie Roll manufacturing plant, lowering unit costs of production.