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

1) Economic theory developed to answer which question?
   A) Why does man have the will to power?
   B) Can we create a government strong enough to tie its own hands?
   C) How are countless individuals led to do “the right thing” without ever caring about doing good?
   D) Is greed good?

2) Suppose a study finds most pot-smokers drank milk as young children. If we reach the conclusion that because most pot smokers "started" on milk, milk drinking "leads" to pot-smoking (at least among certain susceptible groups of milk users), we are most likely
   A) engaging in correct analysis.
   B) confusing statistical correlation with causation.
   C) following the axioms of selfish interests.
   D) assuming people really do not know what is in their own interests.

3) Henry David Thoreau faced a choice: Stay in the village of Concord or move out to Walden Pond. He decided to move to Walden. What was his "opportunity cost"?
   A) There was no opportunity cost if he didn’t pay rent for his cabin on Walden Pond.
   B) The satisfaction he would have enjoyed were he to stay in Concord.
   C) The sweat and toil of building his own cabin and living off the land at Walden Pond.
   D) There was no opportunity cost, because he made a free and voluntary decision to live the way he preferred to live.

4) Suppose Ann can produce 8 units of a material good (M) or 4 units of a spiritual good (S) in a day, while Ben can produce only 3 Ms or 3 Ss in a day. Which statement below is true?
   A) Ben has a comparative advantage in spiritual goods.
   B) Ann has a comparative advantage in spiritual goods.
   C) Ben has a comparative advantage in material goods.
   D) Ann has a comparative advantage in both spiritual and material goods.
Figure 2-7 shows the production possibilities frontiers for Pakistan and Indonesia. Each country produces two goods, cotton and cashews.

5) Refer to Figure 2-7. What is the opportunity cost of producing 1 bolt of cotton in Pakistan?  
A) 3/8 pounds of cashews  
B) 5/8 pounds of cashews  
C) 1 3/5 pounds of cashews  
D) 150 pounds of cashews

6) Refer to Figure 2-7. What is the opportunity cost of producing 1 pound of cashews in Indonesia?  
A) 3/8 bolts of cotton  
B) 5/8 bolts of cotton  
C) 2 2/3 bolts of cotton  
D) 320 bolts of cotton

7) Refer to Figure 2-7. Which country has a comparative advantage in the production of cotton?  
A) Indonesia  
B) They have equal productive abilities.  
C) Pakistan  
D) neither country

8) What is the difference between an "increase in demand" and an "increase in quantity demanded"?  
A) There is no difference between the two terms; they both refer to a shift of the demand curve.  
B) An "increase in demand" is represented by a rightward shift of the demand curve while an "increase in quantity demanded" is represented by a movement along a given demand curve.  
C) There is no difference between the two terms; they both refer to a movement downward along a given demand curve.  
D) An "increase in demand" is represented by a movement along a given demand curve, while an "increase in quantity demanded" is represented by a rightward shift of the demand curve.
Table 3-1

<table>
<thead>
<tr>
<th>Loose leaf Tea Price per lb. (dollars)</th>
<th>Sunil’s Quantity Demanded (lbs)</th>
<th>Mia’s Quantity Demanded (lbs)</th>
<th>Rest of Market Quantity Demanded (lbs)</th>
<th>Market Quantity demanded (lbs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$8</td>
<td>4</td>
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<td>6</td>
<td>7</td>
<td>2</td>
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<td>5</td>
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<tr>
<td>4</td>
<td>12</td>
<td>5</td>
<td>64</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>15</td>
<td>8</td>
<td>90</td>
<td></td>
</tr>
</tbody>
</table>

9) Refer to Table 3-1. The table above shows the demand schedules for loose-leaf tea of two individuals (Sunil and Mia) and the rest of the market. At a price of $5, the quantity demanded in the market would be
   A) 51 lbs.        B) 63 lbs.        C) 76 lbs        D) 146 lbs.

10) If a decrease in income leads to an increase in the demand for macaroni, then macaroni is
   A) an inferior good.        B) a neutral good.        C) a necessity.        D) a normal good.

11) The Internet has created a new category in the book selling market, namely, the "barely used" book. How does the availability of barely used books affect the market for new books?
   A) the demand curve for new books shifts to the right.
   B) the demand curve for new books shifts to the left.
   C) the supply curve for new books shifts to the right.
   D) the supply curve for new books shifts to the left.

12) Which of the following would cause a decrease in the supply of milk?
   A) an increase in the price of cookies (assuming that milk and cookies are complements)
   B) a decrease in the price of milk
   C) an increase the price of a product that producers sell instead of milk
   D) an increase in the number of firms that produce milk

13) Farmers can plant either corn or soybeans in their fields. Which of the following would cause the supply of soybeans to increase?
   A) an increase in the price of soybeans
   B) a decrease in the price of corn
   C) an increase in the demand for corn
   D) an increase in the price of soybean seeds
14) Refer to Figure 3-3. At a price of $5,
   A) there would be a surplus of 4 units.  B) there would be a scarcity of 4 units.
   C) there would be a shortage of 6 units.  D) there would be a shortage of 4 units.

15) Refer to Figure 3-3. At a price of $15, the quantity sold
   A) is 2 units.  B) is 4 units.
   C) is 6 units.  D) cannot be determined.

16) Refer to Figure 3-3. In a free market such as that depicted above, a shortage is eliminated by
   A) a price increase, increasing the supply and decreasing the demand.
   B) a price decrease, decreasing the supply and increasing the demand.
   C) a price decrease, decreasing the quantity supplied and increasing the quantity demanded.
   D) a price increase, increasing the quantity supplied and decreasing the quantity demanded.

17) Fill in the blank: Other things constant, the growing availability of college degrees being offered
    through online programs will tend to ______ the price elasticity of demand for more traditional
    college degree programs.
    A) leave unchanged  B) decrease
    C) increase  D) alter for the better

18) Olive oil producers want to sell more olive oil at a higher price. Which of the following events
    would have this effect?
    A) an increase in the price of olive oil presses
    B) a decrease in the cost of transporting olive oil to markets
    C) an increase in the price of land used to plant olives
    D) research finds that consumption of olive oil reduces the risk of heart disease
19) Refer to Table 4-1. The table above lists the highest prices three consumers, Tom, Dick and Harriet, are willing to pay for a short-sleeved polo shirt. If the price of one of the shirts is $28 dollars
   A) Tom will buy two shirts, Dick will buy one shirt and Harriet will buy no shirts.
   B) Tom will receive $12 of consumer surplus from buying one shirt.
   C) Tom and Dick receive a total of $70 of consumer surplus from buying one shirt each. Harriet will buy no shirts.
   D) Harriet will receive $25 of consumer surplus since she will buy no shirts.

20) Refer to Table 4-1. The table above lists the highest prices three consumers, Tom, Dick and Harriet, are willing to pay for a short-sleeved polo shirt. If the price of the shirts falls from $28 to $20
   A) consumer surplus increases from $14 to $35.
   B) Tom will buy two shirts; Dick and Harriet will each buy one shirt.
   C) consumer surplus will increase from $70 to $95.
   D) Harriet will receive more consumer surplus than Tom or Dick.

21) Refer to Table 4-2. The table above lists the marginal cost of polo shirts by Marko’s, a firm that specializes in producing men’s clothing. If the market price of Marko’s polo shirts is $18
   A) Marko’s will produce four shirts.
   B) producer surplus from the first shirt is $18.
   C) producer surplus will equal $22.
   D) there will be a surplus; as a result, the price will fall to $7.

22) Refer to Table 4-2. The table above lists the marginal cost of polo shirts by Marko’s, a firm that specializes in producing men’s clothing. If the price of polo shirts increases from $15 to $20
   A) consumers will buy no polo shirts.
   B) the marginal cost of producing the third polo shirt will increase to $20.
   C) producer surplus will rise from $13 to $28.
   D) there will be a surplus of polo shirts.
23) Consumer surplus in a market for a product would be equal to the area under the demand curve if  
A) producer surplus was equal to zero.  
B) marginal cost was equal to the market price.  
C) the product was produced in a perfectly competitive market.  
D) the market price was zero.

24) Which of the following statements is true?  
A) Consumer surplus measures the total benefit from participating in a market.  
B) When a market is in equilibrium consumer surplus equals producer surplus.  
C) Consumer surplus measures the net benefit from participating in a market.  
D) Producer surplus measures the total benefit received by producers from participating in a market.

Figure 4–6 shows the market for apartments in Bay City. Recently, the government imposed a rent ceiling at R0.

25) Refer to Figure 4–6. With rent control, the quantity supplied is Q1. Suppose apartment owners ignore the law and rent this quantity for the highest rent they can get. What is the highest rent they can get?  
A) R*  
B) R1  
C) R0  
D) more than R1

26) Refer to Figure 4–6. What is the area that represents consumer surplus after the imposition of the ceiling?  
A) A + B + D  
B) A + B + C  
C) A + B + D + F  
D) A + B + D + F + G

27) Refer to Figure 4–6. What is the area that represents the producer surplus after the imposition of the ceiling?  
A) F + G  
B) F  
C) D + F + G  
D) A + B + D + F + G

28) Refer to Figure 4–6. What is the area that represents the portion of producer surplus transferred to consumers as a result of the rent ceiling?  
A) D + E  
B) D + F  
C) D  
D) F
29) Refer to Figure 4-6. What area represents the deadweight loss after the imposition of the ceiling?
A) $G + H$  
B) $J + H$  
C) $C + E + J + H$  
D) $C + E$

30) The actual division of the burden of a tax between buyers and sellers in a market is called
A) tax incidence.  
B) tax liability.  
C) tax bearer.  
D) tax parity.

31) What is the voting paradox?
A) the observation that less than 60 percent of those eligible to vote actually vote  
B) the observation that majority voting may not always result in consistent choices  
C) the idea that wealthy corporations are able to sway politicians to act in ways contrary to the desires of the majority  
D) people are aware that their votes will not change the political outcome since these outcomes are predetermined by a group of influential politicians

32) The voting paradox suggests that the "voting market", as represented by elections,
A) lead to a superior outcome in representing consumer preferences compared to the private market for goods and services.  
B) may often lead to an inefficient outcome in representing consumer preferences compared to the private market for goods and services.  
C) is no different from the private market for goods and services in terms of representing consumer preferences.  
D) may not lead to an efficient outcome but certainly leads to a more equitable outcome in terms of distributing goods and services.

33) Why is a typical person likely to gather more information when buying a new car than when voting for a member of Congress?
A) because a person’s preferences are more likely to be met with little effort in the political sphere but this is not the case when buying a car in the private marketplace  
B) because it is less costly to acquire information about consumer items than it is about political candidates  
C) because buying a new car affects a person more immediately and personally compared to voting for a member of Congress; in the latter, a person’s vote is only one of many voters and therefore, not likely to have a large impact on the outcome  
D) because the effects of buying a car are long term while a member of Congress has a relatively short tenure

34) One important difference between the political process and the market process is that
A) the political process results in collective actions in which not everyone is required to participate, while in the market process individuals are obliged to participate.  
B) the political process results in collective actions in which everyone is obliged to participate, while in the market process individuals are free to participate or not.  
C) the political process results in collective actions that maximize economic surplus, while the market process may lead to efficiency losses.  
D) the political process results in collective actions in which everyone is made better off, while the market process results in actions that favor some groups only.

35) A marginal tax rate is
A) the fraction of income that must be paid in taxes.  
B) the fraction of each additional dollar of income that must be paid in taxes.  
C) the incremental income one must earn to offset each additional dollar of tax.  
D) the ratio of a change in income to a change in taxes paid.
36) If you pay $2,000 in taxes on an income of $20,000, and a tax of $3,500 on an income of $30,000, then over this range of income the tax is
   A) regressive.
   B) proportional.
   C) progressive.
   D) There is insufficient information to answer the question.

37) A patent or copyright is a barrier to entry based on
   A) ownership of a key necessary raw material.
   B) large economies of scale as output increases.
   C) government action to protect a producer.
   D) widespread network externalities.

38) What is a network externality?
   A) It refers to having a network of suppliers and buyers for a good or service.
   B) It refers to lobbying to form a public enterprise.
   C) It refers to a situation in which a product’s usefulness increases with the number of people using it.
   D) It refers to a product that requires connection to a network for it to be useful.

39) The De Beers Company, one of the longest-lived monopolies, is facing increasing competition. One source of competition comes from people who might resell their previously owned diamonds. Why is De Beers worried that people might resell their previously owned diamonds?
   A) because De Beers will not be able to guarantee the quality of previously owned diamonds and fears that its reputation might be harmed.
   B) because the availability of previously owned diamonds would increase the market demand for diamonds and dilute De Beers’ monopoly.
   C) because previously owned diamonds would be a close substitute to newly mined diamonds and therefore reduce De Beers’ market power.
   D) because the availability of previously owned diamonds would make the market demand curve for diamonds more inelastic and force De Beers to lower its price.

40) Most markets are not monopolies in the real world because
   A) supply curves slope upward.
   B) price is usually set equal to marginal cost by firms.
   C) firms usually face downward-sloping demand curves.
   D) there are reasonable substitutes for most goods.

41) Most movie theatres charge different prices to different groups of customers for movie admission but not on movie popcorn. Which of the following is a reason for this?
   A) because the markup on movie popcorn is very high and movie theatres do not want to forego this source of revenue.
   B) because the demand for popcorn is very high relative to the demand for movie admissions.
   C) because it is easier to limit resale in movie admissions but not in popcorn.
   D) because the cost of operating a concession stand in a movie theatre is very high compared to the cost of showing a movie.
42) From an economic perspective, price discrimination is desirable because

A) the increase in profits is more than offset by the loss in consumer surplus, resulting in a net increase in economic surplus.
B) it enables firms to increase profits with no loss in economic surplus, and in turn, this could provide firms with incentives to engage in beneficial product innovation.
C) the increase in profits results in higher corporate tax revenues received by the government which could be used to subsidize consumption for low-income individuals.
D) it redistributes wealth from wealthy consumers to highly innovative firms.

43) Colleges and universities use donor resources to subsidize students and thus charge a price for education that is below their costs. They do this because:

A) They are impelled to pay students a “wage” for the their contribution to the process of educating one another.
B) They want to create an excess demand for places so that they can select those students who will be most productive in helping to educate other students.
C) They are nonprofit firms and thus don’t need to behave rationally.
D) Both (a) and (b).

44) The market for used college textbooks has:

A) Decreased the price of new textbooks because the used books generate competition with the new books.
B) Increased the price of new textbooks by lowering the print run over which publishers can spread their production costs.
C) Allowed publishers to price discriminate.
D) Had no effect on the price of new textbooks.

45) A local laundry advertises that the clothes it washes smell "sunshine fresh" because it line dries everything outside. Then a steel factory moves in next door and emits black smoke which stains the clothes drying at the laundry. According to the Coase theorem, granting the

A) steel factory the right to pollute would be efficient, but granting the laundry the right to clean air would be equitable.
B) laundry the right to clean air would be efficient, but granting the steel factory the right to pollute would be equitable.
C) steel factory the right to pollute has the same effect on equity as granting the laundry the right to clean air.
D) steel factory the right to pollute has the same effect on efficiency as granting the laundry the right to clean air.

46) A dentist shares an office building with a radio station. The electrical current from the dentist's drill causes static in the radio broadcast, causing the radio station to lose $10,000 in profits. The radio station could put up a shield at a cost of $30,000; the dentist could buy a new drill that causes less interference for $6,000. Either would restore the radio station's lost profits. What is the economically efficient outcome?

A) The radio station puts up a shield, which it pays for.
B) The radio station puts up a shield, which the dentist pays for.
C) Neither the radio station nor the dentist purchase additional equipment.
D) The dentist gets a new drill; it does not matter who pays for it.
47) In the United States, the bulk of health care spending is paid by health insurance companies. Such a system is also called a third-party payer system where consumers of health care pay a nominal fee and the rest are paid by the health insurance provider. Why might such a system lead to an inefficient outcome?
   A) Health insurance companies have an incentive to control cost and therefore tend to deny consumers many cutting edge medical treatments.
   B) Consumers have an incentive to over-consume health care services because they pay prices well below the cost of providing these services.
   C) Physicians concerned that insurance companies may not approve payments tend not to order expensive tests for their patients.
   D) Consumers fearing that excessive use of health care services may lead to a rise in insurance premiums tend to under-consume health care services.

48) The basic cause of deadweight losses from the existence of common resources and externalities is
   A) a lack of clearly defined and enforceable property rights.
   B) the self interested rationality of human beings.
   C) the use of a market system to deal with scarcity.
   D) the absence of government intervention.

49) Compared to the command and control approach to pollution control, the tradable emissions allowance system is
   A) more efficient, because firms with low costs of pollution control would pollute the least and sell their extra permits to other firms with higher costs of pollution control.
   B) more efficient, because there are implementation and monitoring costs with the tradable emissions allowance system.
   C) less efficient, because the tradable emissions allowance system gives firms the right to pollute a certain amount.
   D) less efficient, because it does not raise funds for the government whereas under the command and control approach, firms are penalized for non-compliance.

50) An internet search is:
   A) A private good because it is provided by a private for-profit firm like Google or Microsoft.
   B) A public good because it is non-rivalrous and non-excludable.
   C) A common resource because it is non-excludable but subject to congestion.
   D) A quasi-public good because Google has a natural monopoly on internet searching.

51) Buying insurance is similar to
   A) selling risk.
   B) irrationally avoiding life’s risks.
   C) being a free rider.
   D) buying risk.

52) Insurance works by
   A) eliminating risks.
   B) decreasing risks.
   C) pooling risks.
   D) changing the individual’s marginal utility of wealth.
The International Maritime Bureau said the waters off Somalia are the world’s most dangerous, accounting for nearly a third reported pirate attacks worldwide between January and September 2008. Suppose all boats are insured to $100,000 and pay a premium of $10,000 each. Suppose 10 out of 100 boats are attacked by pirates and these 10 file claims with their insurance. If the insurance company’s only costs are the claims it must pay, has the insurance company earned an economic profit?

A) Yes, they earned an economic profit of $90,000
B) No, they broke even
C) No, they sustained an economic loss of $90,000
D) Yes, they earned an economic profit of $1,000,000

The real interest rate is the opportunity cost of making an investment

A) only if the firm does not need to borrow any of the funds for the investment.
B) only if the firm needs to borrow all of the funds for the investment.
C) only if the firm needs to borrow at least some but not necessarily all of the funds for the investment.
D) no matter if the firm must borrow all, some of, or none of the funds for the investment.
E) The question errs because the opportunity cost of making an investment is the price of the capital good purchased.

Which of the following approximately equals the real interest rate?

A) the nominal interest rate minus the inflation rate
B) the nominal interest rate plus the inflation rate
C) the nominal interest rate minus the growth rate of GDP
D) the rate paid when the best customers of banks borrow money
56) In the above figure, the economy is at point a on the initial demand for loanable funds curve $DLF_0$. What happens if the real interest rate rises?
   A) There is a movement to a point such as b on the demand for loanable funds curve $DLF_0$.
   B) The demand for loanable funds curve shifts rightward to a curve such as $DLF_2$.
   C) The demand for loanable funds curve shifts leftward to a curve such as $DLF_1$.
   D) none of the above

57) In the market for loanable funds, the supply comes from
   A) saving, the government budget surplus and international borrowing
   B) only saving and the government budget surplus
   C) only saving
   D) only the government budget surplus and international borrowing

58) An increase in the real interest rate increases the quantity of saving because the higher real interest rate
   A) increases the opportunity cost of current consumption.
   B) increases the cost of buying capital.
   C) decreases the benefit of saving.
   D) reduces taxes because interest payments are tax deductible.

59) As a result of the recession in 2008, the default risk increased. How did this change affect the loanable funds market?
   A) There was a movement up along the supply of loanable funds curve.
   B) There was a leftward shift in the supply of loanable funds curve.
   C) There was a movement down along the demand for loanable funds curve.
   D) There was a rightward shift in the supply of loanable funds curve.
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60) If we import more than we export from the rest of the world we
   A) must borrow an equal amount from the rest of the world.
   B) can lend an equal amount to the rest of the world.
   C) are running a trade surplus.
   D) are helping to finance investment in the rest of the world.

61) The United States regularly runs a trade _______ and therefore _______.
   A) surplus; loanable funds flow out of the United States
   B) deficit; loanable funds flow out of the United States
   C) surplus; loanable funds are sent to the United States
   D) deficit; loanable funds are sent to the United States

62) The real interest rate is _______ in the United States compared to Zimbabwe because _______.
   A) lower; there is a lower risk premium in the United States.
   B) higher; more firms want to borrow financial capital in the United States.
   C) lower; the United States is a net borrower.
   D) higher; Zimbabwe is a net borrower.

63) In calculating gross domestic product, the Bureau of Economic Analysis uses the sum of the market value of final goods and services produced. This means that the BEA
   A) simply counts the total number of goods produced in the market place and then adds them up.
   B) values goods at their market prices, multiplies them by the quantity produced, and then adds them up.
   C) simply counts the total number of goods and services produced in the marketplace and then adds them up.
   D) values goods and services at their market prices, multiplies them by the quantity produced, and then adds them up.

64) Suppose, in 2006, you purchased a house built in 2000. Which of the following would be included in gross domestic product for 2006?
   A) the value of the house in 2006
   B) the value of the house in 2000
   C) the value of the house in 2006 minus depreciation
   D) the value of the services of the real estate agent

65) Suppose Bob works for Mary as a proofreader. Mary and Bob fall deeply in love, marry and have eight children. Bob stops working for Mary in order to care for the children. What will be the effect on GDP?
   A) GDP will decrease.
   B) GDP will increase.
   C) GDP will not change.
   D) GDP may increase or may decrease depending on inflation.

66) Which of the following is likely to increase measured GDP?
   A) A greater number of women decide to stay at home and provide day care for their children under age 5.
   B) Marijuana becomes legal to grow and sell.
   C) Tax rates increase and more people attempt to underreport their income for tax purposes.
   D) The do-it-yourself craze becomes increasingly popular and more people decide to improve their own homes.
67) Which of the following is not a true statement about the impact of World War II on the U.S. economy?

A) U.S. GDP increased dramatically from 1941 to 1945.
B) The war time years were a period of prosperity for U.S. consumers.
C) More than 40% of the labor force was in the military or producing war goods.
D) Increased production of tanks, ships, planes, and munitions accounted for most of the increase in GDP.

68) If nominal GDP is $5 trillion and real GDP is $4 trillion, the GDP deflator is

A) 12.5.  B) 80.  C) 125.  D) 800.

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<tr>
<td>Salt</td>
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<td>$1.00</td>
</tr>
<tr>
<td>Bread</td>
<td>20</td>
<td>$2.00</td>
<td>$2.10</td>
</tr>
</tbody>
</table>

69) The data in the table above shows the consumption by families in a small (poor) economy. The families consume only salt and bread. The reference base period is 2005. The cost of the CPI market basket in 2005 is

A) $1.50.  B) $2.50.  C) $40.50.  D) $12.00  E) 100.

70) The data in the table above shows the consumption by families in a small (poor) economy. The families consume only salt and bread. The reference base period is 2005. The cost of the CPI market basket in 2006 is

A) $3.10.  B) $43.00.  C) $40.50.  D) $4.10.  E) unable to be calculated because information is needed about the quantities purchased in 2006.

71) The data in the table above shows the consumption by families in a small (poor) economy. The families consume only salt and bread. The reference base period is 2005. The CPI in 2005 is

A) 100.  B) 94.2.  C) 106.2.  D) 124.  E) 140.5.

72) The data in the table above shows the consumption by families in a small (poor) economy. The families consume only salt and bread. The reference base period is 2005. The CPI in 2006 is

A) 100.  B) 94.2.  C) 106.2.  D) 124.  E) 144.

73) The data in the table above shows the consumption by families in a small (poor) economy. The families consume only salt and bread. The reference base period is 2005. The inflation rate between 2005 and 2006 is

A) 52.5 percent.  B) 106.2 percent.  C) 6.2 percent.  D) 5.25 percent.  E) 6.9 percent.
The CPI overstates inflation because the average consumer buys
A) the same basket of goods every week.
B) more of those goods whose relative price has risen.
C) less of those goods whose relative price has risen.
D) lower quality goods if they have a choice.
E) a generally random assortment of goods and services each week because what is purchased depends on what the consumer needs.

An example of the outlet substitution bias in the calculation of the CPI is a price increase in
A) butter relative to margarine.
B) an MP3 player relative to a Walkman.
C) a 2006 Honda Civic LX relative to a 2001 Honda Civic LX.
D) textbooks bought through the campus bookstore relative to textbooks bought through Amazon.com.
E) a Caribbean cruise for a couple that had previously taken cruises in Alaska.

Why did prisoners use cigarettes as money in the P.O.W. camp example?
A) It was decreed by the German camp authorities.
B) It was decreed by American Generals.
C) The prisoners accidentally burned their paper currency.
D) The prisoners found they could easily trade cigarettes for most other items they valued.
E) For health reasons the Red Cross insisted prisoners trade, rather than smoke, their cigarettes.

If cigarettes are used as money, could they generate a price deflation?
A) No, because prices could never be measured in cigarettes.
B) Yes, if smoking causes some of the cigarettes to be withdrawn from circulation.
C) Yes, but only if the total number of cigarettes in circulation is unchanged.
D) No, because there is not a single historical example of cigarettes being used as money, let alone creating price deflation.

Financial panics characterized by depositor "runs" and consequent bank failures have not occurred in the United States since the 1930s primarily because
A) commercial banks now hold larger reserves.
B) the Federal Deposit Insurance Corporation has reduced the fears of depositors.
C) we have abandoned the gold standard.
D) we have had no major recessions since the 1930s.

If you withdraw currency from your bank savings account, you are
A) increasing M1, decreasing M2.
B) increasing both M1 and M2.
C) decreasing both M1 and M2.
D) not affecting M1 or M2.
E) increasing M1 but not affecting M2.

The "discount rate" is the rate used by the Fed when
A) the Fed extends a short-term loan directly to a commercial bank.
B) the Fed extends a short-term loan to one of the regional Federal Reserve banks.
C) the Fed calculates the present value of particular long-term investment projects.
D) the Fed makes cash available for the federal government.
81) The term for the Fed's day-to-day technique for controlling the stock of money is
A) discounting operations.
B) interest-rate operations.
C) liquidity operations.
D) open market operations.
E) treasury operations.

82) If a savings and loan "pools risk," which of the following must it do?
A) take funds in from a large number of lenders
B) have a large spread between the interest rate it charges borrowers and the interest rate it pays lenders
C) lend money to a large number of firms
D) Both answers A and C are correct.

83) When the Fed wants to undertake open market operations, it
A) can require all commercial banks to buy from or sell to it.
B) can require all member banks to buy from or sell to it.
C) buys or sells government securities.
D) buys government securities from or sells Government securities to the federal government.

84) Bill deposits in his bank $5,000 in cash that he has been hiding under his mattress. If all banks make as many loans as possible and the required reserve ratio is 10 percent, then the total increase in the quantity of money created by the banking system is
A) $5,000.  B) $20,000.  C) $45,000.  D) $10,000.  E) $4,000.

<table>
<thead>
<tr>
<th>TBK Bank Balance Sheet</th>
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<tbody>
<tr>
<td>Assets</td>
</tr>
<tr>
<td>Reserves $120</td>
</tr>
<tr>
<td>Loans 580</td>
</tr>
<tr>
<td>Total assets $700</td>
</tr>
<tr>
<td>Liabilities</td>
</tr>
<tr>
<td>Deposits $600</td>
</tr>
<tr>
<td>Net worth 100</td>
</tr>
<tr>
<td>Total liabilities $700</td>
</tr>
</tbody>
</table>

85) The above table presents the balance sheet of the TBK commercial bank. What is this bank's actual reserve ratio?
A) $120  B) $700  C) 20 percent  D) 17.14 percent

86) If an increase in the monetary base of $8 billion increases the quantity of money by $64 billion, then the money multiplier is equal to _______.
A) $64 billion  B) 8  C) $8 billion  D) 1/8

87) If real GDP is $10 trillion, the price level is 120, and the quantity of money is $4 trillion, what is the velocity of circulation?
A) 3  B) 2.5  C) 30  D) 25

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loans</td>
<td>$83</td>
<td>$78</td>
</tr>
<tr>
<td>Reserves</td>
<td>$4</td>
<td>$5</td>
</tr>
<tr>
<td>M1 Deposits</td>
<td>$114</td>
<td>$95</td>
</tr>
</tbody>
</table>

The data show that Sun Trust
A) increased its reserve ratio to 5.3 percent over the 12 months.
B) increased its reserve ratio to 6.4 percent over the 12 months.
C) has fewer excess reserves in 2008.
D) faced a higher currency drain ratio in 2008.

89) According to Milton Friedman, the US Federal Reserve allowed an ordinary recession to turn into the Great Depression because:
A) it failed to act as a lender of last resort.
B) it engaged in expansionary monetary policy.
C) its hands were tied by adherence to the gold standard.
D) it held inflexibly to the theories of John Maynard Keynes.

90) In 2008, the Treasury and Federal Reserve took action to save large financial firms such as Bear Stearns and AIG from failing. Which of the following is one reason why these measures were taken?
A) The Emergency Economic Stabilization Act required the Fed and the Treasury to provide financial assistance to firms that participated in regular open market actions with the Fed.
B) The bankruptcy of a large financial firm would force the firm to sell its holdings of securities, which could cause other firms that hold these securities to also fail.
C) The Fed and the Treasury wanted to allow Freddie Mac and Fannie Mae more time to buy the firms before they went bankrupt.
D) The failure of these firms would have forced the Fed to increase interest rates, which could have led to a severe recession.

91) The Federal Reserve cut the federal funds rate seven times between September 2007 and March 2008. What event led the Fed to make these reductions in the federal funds rate?
A) It was in response to reductions in the discount rate, which was also lowered seven times over the same time period.
B) The chairman of the Federal Reserve System persuaded members of the Federal Open Market Committee to lower interest rates in order to reduce the price of oil in international markets.
C) During this period there was a substantial reduction in the demand for housing.
D) Several large investment banks failed during this time period.

92) The economy suffered a mild recession in 2001. Despite the recession, home sales and durable goods sales remained high. Which of the following is a plausible explanation?
A) The Fed’s pursuit of contractionary policy stimulated these markets.
B) The Fed caused a reduction in the federal funds rate to its lowest level in 40 years.
C) Rising inflation encouraged many to invest in the real estate market.
D) Home building and consumer durable purchases are always high during a recession.
93) Inflation transfers wealth from:
   A) the relatively poor to the relatively wealthy.
   B) the relatively wealthy to the relatively poor.
   C) savers to borrowers.
   D) borrowers to savers.

94) Inflation functions as a tax because:
   A) the Treasury keeps all the new money created.
   B) the government takes a percentage of each new dollar created, a practice called seigniorage.
   C) the US is on the gold standard.
   D) the IRS bills taxpayers only in real dollars.
   E) inflation reduces the cost of government deficit spending at the expense of the purchasing power of private money holdings.

95) Significant economic growth did not begin in the world until
   A) 1000 A.D.   B) 1750 A.D.   C) 1820 A.D.   D) the 20th century A.D.

96) Growth in real GDP per capita for the world economy was greatest during
   A) the seventeenth century.   B) the eighteenth century.   C) the nineteenth century.   D) the twentieth century.

97) China's economy has grown tremendously from 1979 to the present. The reason the article gives for this growth is
   A) the introduction of the centrally planned economy in 1978.
   B) the introduction of market-oriented reforms in 1978.
   C) the introduction of the social networking site, MySpace.
   D) the total lack of governmental intervention in the economy.

98) Between 1996 and 2006, which of the leading industrial countries of the world had the highest average annual growth rate of productivity?
   A) the United States   B) the United Kingdom   C) Japan   D) Italy

99) Sustained economic growth generally occurs when a nation
   A) abandons the market system in favor of central economic planning.
   B) abandons the rule of law in favor of a series of licenses, regulations, and tariffs to control and protect the domestic economy.
   C) subsidizes loss-generating enterprises and thereby preserves jobs and incomes.
   D) creates conditions where people are free to specialize and exchange.

100) Economic growth is supported by
    A) the rule of law.
    B) competent and honest government officials.
    C) an educated populace.
    D) openness to international trade and investment.
    E) all of the above.