

Fun Set 4.1

Name: _____

1. A country's government runs a budget deficit when which of the following occurs in a given year?
- (A) The amount of new loans to developing nations exceeds the amount of loans paid off by developing nations.
 - (B) Government spending exceeds tax revenues.
 - (C) The debt owed to foreigners exceeds the debt owed to the country's citizens.
 - (D) The amount borrowed exceeds the interest payment on the national debt.
 - (E) Interest payments on the national debt exceed spending on goods and services.
42. A barter economy is different from a money economy in that a barter economy
- (A) encourages specialization and division of labor
 - (B) involves higher costs for each transaction
 - (C) eliminates the need for a double coincidence of wants
 - (D) has only a few assets that serve as a medium of exchange
 - (E) promotes market exchanges
3. The transaction demand for money is very closely associated with money's use as a
- (A) store of value
 - (B) standard unit of account
 - (C) measure of value
 - (D) medium of exchange
 - (E) standard of deferred payment
49. Which of the following is NOT a function of fiat money?
- (A) A standard of deferred payment
 - (B) A unit of account
 - (C) A source of intrinsic value
 - (D) A store of value
 - (E) A medium of exchange
56. In the narrowest definition of money, M1, savings accounts are excluded because they are
- (A) not a medium of exchange
 - (B) not insured by federal deposit insurance
 - (C) available from financial institutions other than banks
 - (D) a store of purchasing power
 - (E) interest-paying accounts
12. The amount of money that the public wants to hold in the form of cash will
- (A) be unaffected by any change in interest rates or the price level
 - (B) increase if interest rates increase
 - (C) decrease if interest rates increase
 - (D) increase if the price level decreases
 - (E) decrease if the price level remains constant
3. With a constant money supply, if the demand for money decreases, the equilibrium interest rate and quantity of money will change in which of the following ways?
- | <u>Interest Rate</u> | <u>Quantity of Money</u> |
|----------------------|--------------------------|
| (A) Increase | Decrease |
| (B) Increase | Not change |
| (C) Decrease | Decrease |
| (D) Decrease | Increase |
| (E) Decrease | Not change |

2007B Practice FRQ

1. Assume that Australia and New Zealand are trading partners. Australia's economy is currently in recession.
 - (a) Now assume that Australia begins to recover from its recession. Using a correctly labeled graph of aggregate demand and aggregate supply for New Zealand, show the impact of Australia's rising income on each of the following in the short run.
 - (i) Aggregate demand in New Zealand. Explain.
 - (ii) Output in New Zealand
 - (b) Using a correctly labeled graph of the money market for New Zealand, show the effect of the output change in part (a)(ii) on the following.
 - (i) Demand for money. Explain.
 - (ii) The nominal interest rate

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2. Assume that an economy is in long-run equilibrium. Assume that consumers wish to hold less money because they use credit cards more frequently to purchase goods and services than cash.
 - (a) Draw a correctly labeled graph of the money market and show the effect of the reduced holdings of money on the equilibrium nominal interest rate in the short run.
 - (b) Based on the change in the interest rate in part (a), what will happen to each of the following in the short run?
 - (i) Prices of previously issued bonds
 - (ii) The price level and real income. Explain.
 - (c) With a constant money supply, based on your answer to part b(ii), will the velocity of money increase, decrease, or remain the same, or is the change indeterminate?
 - (d) If the central bank wishes to reverse the change in the interest rate identified in part (a), what open market operation would it use?

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MACROECONOMICS

Section II

Planning Time—10 minutes

Writing Time—50 minutes

Directions: You have 50 minutes to answer all three of the following questions. It is suggested that you spend approximately half your time on the first question and divide the remaining time equally between the next two questions. In answering the questions, you should emphasize the line of reasoning that generated your results; it is not enough to list the results of your analysis. Include correctly labeled diagrams, if useful or required, in explaining your answers. A correctly labeled diagram must have all axes and curves clearly labeled and must show directional changes. Use a pen with black or dark blue ink.

1. Assume that declining stock market prices in the United States cause many United States financial investors to sell their stocks and increase their money holdings.
 - (a) Draw a correctly labeled graph of the money market and show the impact of the financial investors' actions on each of the following.
 - (i) Demand for money
 - (ii) Nominal interest rate