

- D 9. Which of the following alternatives is necessarily correct if a country is running a trade deficit?
- (A) Foreigners will sell the country's currency because they do not want assets in another country.
 - (B) The country's central bank will raise interest rates to strengthen the currency and reduce the chances of a speculative attack.
 - (C) The economic factors that created the trade deficits will reduce future welfare of the country's citizens.
 - (D) The country absorbs more output, in various activities, than it produces.
- D 10. Which of the following alternatives best describes the supply-side prediction about the effect of saving on the economy?
- (A) Workers that save a greater share of their income will supply more labor resources.
 - (B) Higher saving requires the central bank to lower interest rates which stimulates spending.
 - (C) Higher saving means lower consumption, reduced sales by business, and therefore lower employment.
 - (D) Higher saving lowers the cost of capital and encourages business investment.
- A 11. Abstraction is a key feature of good economic theory because:
- (A) Abstraction allows focus on important features of reality by ignoring less relevant details.
 - (B) Abstraction assures that economic models describe economic reality as well as possible.
 - (C) Abstraction allows normative conclusions to be drawn from realistic positive theory.
 - (D) Abstraction helps distinguish causation from misleading correlations.
- B 12. Which of the following statements best represents demand-side (Keynesian) macroeconomics?
- (A) A trade deficit can raise standards of living if it arises from the import of productive capital.
 - (B) Greater business investment encourages growth by raising sales for firms that produce capital goods.
 - (C) Higher business investment adds to the productive capital of the economy.
 - (D) Investment in education raises the economy's human capital and therefore enhances labor resources.
- A 13. Suppose that a laptop computer costs \$1,200 in the U.S. and €1,000 in Germany (€ is the symbol for the euro currency). Also suppose that the exchange rate is \$1.40 per euro. What can you conclude about the values of the dollar and the euro from this information alone?
- (A) The euro is overvalued relative to purchasing power parity.
 - (B) Germans should raise interest rates to restore purchasing power parity.
 - (C) The euro and dollar are in purchasing power parity.
 - (D) The euro is undervalued relative to purchasing power parity.
- D 14. Which statement below correctly reflects the link between interest rates and investment if a firm uses its own funds (cash flow) to finance their capital spending?
- (A) Higher interest rates do not discourage investment for this firm, because it has no need for a loan when it finances its spending from cash flow.
 - (B) Higher interest rates reduce any investment tax credit the firm receives, so it discourages investment regardless of whether its spending is paid for by cash flow or a bank loan.
 - (C) The firm's opportunity cost of cash flow is likely about the same as the cost of a loan, so higher interest rates discourage investment.
 - (D) Although the cost to the firm of cash flow is likely less than the cost of a loan, a higher interest rate still raises the opportunity cost of cash flow and discourages investment.

- C 15. Which of the following alternatives best describes a main reason why the U.S. government has encouraged the Chinese government to allow the Chinese currency to appreciate?
- (A) The U.S. wants to reduce the cost of imported Chinese goods bought by American consumers.
 - (B) The U.S. wants give Chinese citizens a greater incentive to hold dollar assets.
 - (C) The U.S. wants to raise its aggregate demand.
 - (D) The U.S. wants to raise the demand for Chinese labor so that Chinese wages increase.
- A 16. Which of the following statements best describes the expansion or “boom” phase of “Minsky Cycle?”
- (A) More aggressive lending leads to higher spending that stimulates income growth, validates financial practices, and encourages even more extensive lending.
 - (B) Low interest rates raise consumption, investment, and international trade which all contribute to higher demand, stronger sales, and more employment.
 - (C) Good economic results encourage government spending stimulates the demand side of the economy.
 - (D) Improved access to credit stimulates business investment that leads to more capital resources and higher potential output.
- C 17. In late 2010, Congress and the President agreed to cut taxes American workers pay for Social Security (retirement benefits) during calendar year 2011. Which of the of the following alternatives best describes a demand-side reason that these tax cuts are likely to have a relatively small effect on output and employment?
- (A) These tax cuts go to people with a relatively low marginal propensity to consume.
 - (B) Most workers save very little, so this tax cut will do little to provide future resources for the economy.
 - (C) Because the tax cuts expire at the end of December 2011, they will not do much to boost consumption.
 - (D) These tax cuts are too small to encourage more people to search for jobs.