Multiple Choice (30%)
Identify the letter of the choice that best completes the statement or answers the question.

1. When a market is in equilibrium,
   a. quantity demanded will equal quantity supplied.
   b. a shortage will be present.
   c. a surplus will be present.
   d. sellers will continue to expand production to increase revenues.

2. Demand for which of the following goods is the most likely to be (nearly) perfectly elastic?
   a. emergency surgery
   b. Ford automobiles
   c. Farmer Ben's wheat
   d. diamonds

3. Indifference curves tend to be bowed inward because of diminishing
   a. marginal rates of substitution.
   b. demand for the good as prices rise.
   c. income.
   d. supply of the good being consumed.

4. If the legal reserve requirement decreases, the
   a. money multiplier increases.
   b. money multiplier decreases.
   c. amount of excess reserves the bank has decreases.
   d. money multiplier is unaffected.

5. The discovery of new gold in South America will _________ the price of gold and _________ the quantity
   of gold traded.
   a. raise; raise
   b. lower; raise
   c. raise; lower
   d. lower; lower

6. As a result of heavy spring rains in the Midwestern states, the corn crop declined sharply. If corn growers
   experienced an increase in sales revenue, the demand for corn must be
   a. Price elastic.
   b. Price inelastic.
   c. Unitary elastic.
   d. Perfectly inelastic.

7. An equilibrium when there is perfect competition
   a. is undesirable.
   b. is economically efficient.
   c. leads to high consumer surplus at the expense of producer surplus.
   d. can be economically efficient only if the government steps in with price floors to protect
   sellers.

8. According to the Laffer Curve, when taxes are increased from 0 percent to a rate consistent with the
   maximum point on the curve, tax revenue will
   a. decrease.
   b. increase.
   c. be the same as the tax rate.
   d. remain constant.

9. Fred Jones won a lottery prize of $1 million. He put the money in the bank to save it for his daughter's college
   education. For him, money was functioning primarily as
   a. unit of account.
   b. store of value.
   c. means of payment.
   d. type of short-term loan.

10. Which of the following would not be an appropriate response to a trade deficit for the United States?
    a. increase tariffs
    b. appreciate the dollar
    c. subsidize exports
    d. impose import quotas

11. When the interest rate falls,
    a. the opportunity cost of holding money rises.
    b. people shift out of holding interest-yielding assets and into holding more liquid forms of
      money.
    c. the quantity of money people will hold decreases.
    d. investment spending decreases.
12. Which of the following can banks count as reserves?
   a. coins in the bank vaults
   b. paper currency in bank vaults
   c. deposits at the Federal Reserve banks
   d. All of the above are correct.

13. In the long run, the aggregate demand curve is
   a. horizontal.
   b. upward sloping.
   c. downward sloping.
   d. vertical.

14. Which of the following will cause the aggregate supply curve to shift to the right?
   a. increases in wages and salaries paid to employees
   b. increases in the prices of oil and natural gas
   c. increases in taxes for business
   d. new work rules that increase the productivity of labor

15. Which of the following is not true for the crowding-out effect?
   a. Federal budget deficits increase interest rates, which reduces investment spending.
   b. Crowding out reduces the ability of fiscal policy to combat a recession.
   c. If the government spends more on education, ceteris paribus, households may be forced to spend less on new homes.
   d. Crowding out occurs especially when the economy is in a deep recession and people are not spending all the available money.

PROBLEMS AND APPLICATIONS

1. One day Barry the Barber, Inc., collects $400 for haircuts. Over this day, his equipment depreciates in value by $50. Of the remaining $350, Barry sends $30 to the government in sales taxes, takes home $220 in wages, and retains $100 in his business to add new equipment in the future. From the $220 that Barry takes home, he pays $70 in income taxes. Based on this information, compute Barry’s contribution to the following measures of income.
   a. gross domestic product
   b. net national product
   c. national income
   d. personal income (20%)

2. Suppose that changes in bank regulations expand the availability of credit cards, so that people need to hold less cash.
   a. How does this event affect the demand for money?
   b. If the Fed does not respond to this event, what will happen to the price level? (20%)

3. The United States represents a small part of the world orange market.
   a. Draw a diagram depicting the equilibrium in the U.S. orange market without international trade. Identify the equilibrium price, equilibrium quantity, consumer surplus, and producer surplus.
   b. Suppose that the world orange price is below the U.S. price before trade, and that the U.S. orange market is now opened to trade. Identify the new equilibrium price, quantity consumed, quantity produced domestically, and quantity imported. Also show the change in the surplus of domestic consumers and producers. Has domestic total surplus increased or decreased? (20%)

4. Why are budget deficits and trade deficits sometimes called the twin deficits? (10%)