

**Chapter 2: Macroeconomics: getting started**

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1. GDP is
- a measure of economic growth.
  - a measure of the economy's potential.
  - another term for standard of living.
  - a measure of the total value of all goods and services produced in a country during a specific period of time.
  - the total value of all goods and services produced during a specific period of time adjusted for the general increase in prices.

ANS: D                    PTS: 1                    DIF: basic  
TOP: Real gross domestic product over time

2. Real GDP is
- a measure of economic growth.
  - a measure of the economy's potential to produce.
  - another term for standard of living.
  - a measure of the total value of all goods and services produced in a country during a specific period of time.
  - the total value of all goods and services produced during a specific period of time adjusted for the general increase in prices.

ANS: E                    PTS: 1                    DIF: basic  
TOP: Real gross domestic product over time

3. The long-term upward trend in real GDP is called
- the business cycle.
  - inflation.
  - prosperity.
  - economic growth.
  - economic fluctuations.

ANS: D                    PTS: 1                    DIF: basic  
TOP: Real gross domestic product over time

4. *Real*, in the term *real GDP*, is used to indicate that
- it measures trend production.
  - this measure of output is official as opposed to a forecast measure.
  - this measure of output is adjusted for the changes in the price level over time.
  - this measure of output is adjusted for the government's economic involvement.
  - it measures only real goods, not services.

ANS: C                    PTS: 1                    DIF: basic  
TOP: Real gross domestic product over time

5. *True or False*. Economic growth and economic fluctuations can occur simultaneously.

ANS: T                    PTS: 1                    DIF: basic  
TOP: Real gross domestic product over time

6. *True or False*. GDP is the total value of all goods and services newly produced in the economy during a specified period of time, adjusted for inflation.

ANS: F                    PTS: 1                    DIF: moderate  
TOP: Real gross domestic product over time

7. Potential GDP is
- a measure of short-term movements in GDP.
  - another name for GDP.
  - the trend line in real GDP.
  - another name for real GDP.
  - another name for aggregate demand.

ANS: C                    PTS: 1                    DIF: basic

TOP: Real gross domestic product over time

8. Which of the following statements is *true*?
- Real GDP fluctuates around potential GDP.
  - Potential GDP fluctuates around real GDP.
  - Real GDP is something like an average of GDP.
  - The growth rate of potential GDP is well known and generally agreed upon.
  - Real GDP cannot be any greater than potential GDP.

ANS: A                    PTS: 1                    DIF: moderate

TOP: Real gross domestic product over time

9. Economic growth theory
- explains the difference between long-run growth and the growth trend.
  - explains the long-term upward rise in real GDP.
  - explains the difference between real and nominal GDP.
  - determines the maximum amount that GDP can be at any time.
  - tries to explain the short-term fluctuations in real GDP.

ANS: B                    PTS: 1                    DIF: basic

TOP: Real gross domestic product over time

10. Economic growth describes increases in
- the labour force.
  - real GDP.
  - inflation.
  - interest rates.
  - None of the listed options is correct.

ANS: B                    PTS: 1                    DIF: basic

TOP: Real gross domestic product over time

11. Real GDP is the
- normal, or average, level of production for an economy.
  - maximum attainable level of production for an economy.
  - total of all goods and services produced in an economy during a specified period of time.
  - total of all goods and services produced in an economy during a specified period of time divided by the population.
  - None of the listed options is correct.

ANS: C                    PTS: 1                    DIF: basic

TOP: Real gross domestic product over time

12. The growth in real GDP per capita
- a. is slower than the growth in real GDP for countries with a growing population.
  - b. is faster than the growth in real GDP for countries with a growing population.
  - c. is about the same as the growth in real GDP for countries with a growing population.
  - d. has greatly decreased living standards over the past two centuries.
  - e. None of the listed options is correct.

ANS: A PTS: 1 DIF: moderate

TOP: Real gross domestic product over time

13. Economic growth describes increases in

- a. the labour force.
- b. real GDP.
- c. inflation.
- d. interest rates.
- e. None of the listed options is correct.

ANS: B PTS: 1 DIF: basic

TOP: Real gross domestic product over time

14. A fall in real GDP that lasts six months or more is called a(n)

- a. expansion.
- b. peak.
- c. economic growth slowdown.
- d. recession.
- e. None of the listed options is correct.

ANS: D PTS: 1 DIF: basic

TOP: Real gross domestic product over time

15. The highest point in the business cycle before the start of a recession is called a(n)

- a. trough.
- b. peak.
- c. recovery.
- d. expansion.
- e. None of the listed options is correct.

ANS: B PTS: 1 DIF: basic

TOP: Real gross domestic product over time

16. Real GDP is the

- a. normal, or average, level of production for an economy.
- b. maximum attainable level of production for an economy.
- c. total of all goods and services produced in an economy during a specified period of time.
- d. total of all goods and services produced in an economy during a specified period of time divided by the population.
- e. None of the listed options is correct.

ANS: C PTS: 1 DIF: basic

TOP: Real gross domestic product over time

17. The goal of economic growth theory is to explain
- short-run movements around the long-run growth path.
  - the short-term upward rise of real GDP over time.
  - the long-term upward rise of real GDP over time.
  - the long-term downward fall of real GDP over time.
  - None of the listed options is correct.

ANS: C PTS: 1 DIF: basic

TOP: Real gross domestic product over time

18. Theories of economic fluctuations emphasise

- the inflation rate.
- the interest rate.
- aggregate supply.
- aggregate demand.
- None of the listed options is correct.

ANS: D PTS: 1 DIF: basic

TOP: Real gross domestic product over time

19. Economic fluctuations theory

- postulates that business cycles are due to changes in potential GDP.
- postulates that business cycles are due to changes in inflation.
- describes business cycles as fluctuations of real GDP around potential GDP.
- describes business cycles as fluctuations of potential GDP around real GDP.
- None of the listed options is correct.

ANS: C PTS: 1 DIF: basic

TOP: Real gross domestic product over time

20. A boom occurs when real GDP is

- rising.
- rising above the trend growth rate.
- rising at an increasing rate.
- rising at a constant rate.
- above trend.

ANS: E PTS: 1 DIF: moderate

TOP: Real gross domestic product over time

21. A slump occurs when real GDP is

- below normal.
- below its earlier peak.
- falling.
- constant.
- growing at a lower rate.

ANS: A PTS: 1 DIF: moderate

TOP: Real gross domestic product over time

22. Which of the following is the best measure of how individuals benefit from economic growth?

- The rate of increase in GDP per capita
- The rate of increase in GDP
- The rate of increase in real GDP per capita
- The rate of inflation
- The rate of increase in real GDP

ANS: C PTS: 1 DIF: moderate

TOP: Australia's economic growth record in context

**Exhibit 2.1**

	A		B	
	2010	2011	2010	2011
<b>Real GDP</b>	\$144 billion	\$157 billion	\$396 billion	\$430 billion
<b>Population</b>	59.4 million	60.2 million	44.4 million	44.8 million

23. The data in Exhibit 2.1 shows the values of real GDP and population for two countries, A and B, for the years 2010 and 2011. Which of these two countries experienced a faster increase in the standard of living between 2010 and 2011?

ANS:

For country A, real GDP per capita grew by 7.6 per cent (from \$2424 to \$2609 per person). For country B, real GDP per capita grew by 7.6 per cent over the same period (from \$8919 to \$9598). Therefore, both of these countries experienced the same rate of growth in the standard of living.

PTS: 1                      DIF: moderate                      TOP: Measuring the economy

24. Because of the increase in population over the past 40 years,
- the rate of increase in real GDP per capita has been greater than the rate of increase in real GDP.
  - real GDP has grown at a slower rate than GDP.
  - the rate of increase in real GDP per capita has been less than the rate of increase in real GDP.
  - there has been no growth in real GDP.
  - the rate of increase in real GDP has been greater than the rate of increase in GDP.

ANS: C                      PTS: 1                      DIF: moderate

TOP: Australia's economic growth record in context

25. Economic fluctuations theory
26. postulates that business cycles are due to changes in potential GDP.
  - postulates that business cycles are due to changes in inflation.
  27. describes business cycles as fluctuations of real GDP around potential GDP.
  - describes business cycles as fluctuations of potential GDP around real GDP.
  - None of the listed options is correct.

ANS: C                      PTS: 1                      DIF: moderate

TOP: Real gross domestic product over time

26. A fall in the price level is called

27. growth slowdown.
- deflation.
28. disinflation.
- inflation
- None of the listed options is correct.

ANS: B                      PTS: 1                      DIF: moderate

TOP: Real gross domestic product over time

27. Over the past 40 years, the average rate of increase in Australia's real GDP *per capita* has been about

- a. 5 per cent.
- b. 0 per cent.
- c. 13 per cent.
- d. -3 per cent.
- e. 2 per cent.

ANS: E                    PTS: 1                    DIF: moderate

TOP: Australia's economic growth record in context

28. Suppose a country's real GDP increased 5 per cent between 2010 and 2011, while its population increased 2 per cent. Between 2010 and 2011, real GDP *per capita* of this country

- a. increased by 7 per cent.
- b. increased by 3 per cent.
- c. decreased by 7 per cent.
- d. decreased by 2 per cent.
- e. remained the same.

ANS: A                    PTS: 1                    DIF: moderate

TOP: Australia's economic growth record in context

29. If real GDP and population are both growing at a positive rate,

- a. real GDP must be growing slower than real GDP per capita.
- b. real GDP must be growing faster than real GDP per capita.
- c. real GDP per capita must be increasing.
- d. real GDP per capita must be decreasing.
- e. None of the listed options is correct.

ANS: B                    PTS: 1                    DIF: challenging

TOP: Australia's economic growth record in context

30. If real GDP is growing at a slower rate than the growth rate of population,

- a. real GDP must be growing more slowly than real GDP per capita.
- b. real GDP must be growing faster than real GDP per capita.
- c. real GDP per capita must be negative.
- d. real GDP per capita must be increasing.
- e. None of the listed options is correct.

ANS: B                    PTS: 1                    DIF: challenging

TOP: Australia's economic growth record in context

31. Which of the following statements is *true*?

- a. If real GDP grows faster than population, the real GDP per capita will decrease.
- b. If real GDP grows slower than population, the real GDP per capita will increase.
- c. If real GDP and population grow at the same rate, the real GDP per capita will remain constant.
- d. None of these
- e. All of these

ANS: C                    PTS: 1                    DIF: moderate

TOP: Australia's economic growth record in context

32. The recession phase
- involves any growth slowdown of at least two quarters in duration.
  - has almost the same duration and depth in all business cycles.
  - varies in duration and depth with each business cycle.
  - has almost the same depth in all business cycles.
  - has almost the same duration in all business cycles.

ANS: C            PTS: 1            DIF: moderate  
TOP: Economic fluctuations: temporary setbacks and recoveries

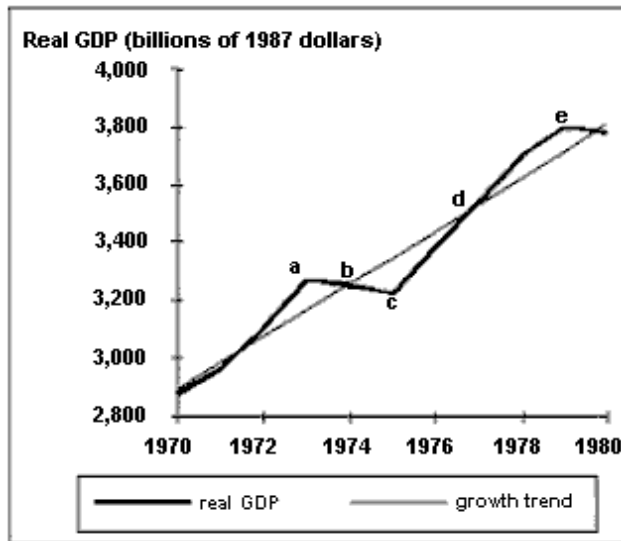
33. A growth recession occurs when real GDP is
- below its trend level.
  - below its earlier peak level.
  - falling.
  - growing at a constant rate.
  - growing at a lower rate.

ANS: E            PTS: 1            DIF: moderate  
TOP: Economic fluctuations: temporary setbacks and recoveries

34. A narrow (technical) definition of a recession is
- a fall in real GDP lasting at least one month.
  - a fall in real GDP lasting at least six months.
  - whenever real GDP falls below the long-term trend.
  - whenever real GDP falls below the long-term trend for at least one month.
  - a fall in real GDP lasting at least one year.

ANS: B            PTS: 1            DIF: moderate  
TOP: Economic fluctuations: temporary setbacks and recoveries

**Exhibit 2.2**



35. In Exhibit 2.2, the best example of a recession phase is
- from point a to point d.
  - from point a to point c.
  - from point a to point b.
  - from point b to point d.
  - from point b to point c.

ANS: B            PTS: 1            DIF: challenging  
TOP: Economic fluctuations: temporary setbacks and recoveries

36. In Exhibit 2.2, the best example of an expansion phase is

- a. from point *c* to point *e*.
- b. from point *a* to point *e*.
- c. from point *a* to point *d*.
- d. from point *b* to point *d*.
- e. from point *d* to point *e*.

ANS: A                      PTS: 1                      DIF: challenging

TOP: Economic fluctuations: temporary setbacks and recoveries

37. In Exhibit 2.2, the best example of a slump is

- a. from point *a* to point *e*.
- b. from point *a* to point *c*.
- c. from point *a* to point *b*.
- d. from point *b* to point *d*.
- e. from point *c* to point *d*.

ANS: D                      PTS: 1                      DIF: challenging

TOP: Economic fluctuations: temporary setbacks and recoveries

38. *True or False.* To say that a recession is over is the same as saying the economy has returned to normal.

ANS: F                      PTS: 1                      DIF: moderate

TOP: Economic fluctuations: temporary setbacks and recoveries

39. *True or False.* After a recession, the economy often takes years to return to its pre-recession state.

ANS: T                      PTS: 1                      DIF: basic

TOP: Economic fluctuations: temporary setbacks and recoveries

40. What is meant by a recession? As a rule of thumb, when is the economy considered to be in a recession?

ANS:

A recession occurs when real GDP falls. As a rule of thumb, this fall needs to last at least six months.

PTS: 1                      DIF: basic                      TOP: Economic fluctuations: temporary setbacks and recoveries



**Exhibit 2.3**

	<b>Real GDP</b>	<b>Growth Trend</b>
<b>Date</b>	<b>(billions of dollars)</b>	<b>(billions of dollars)</b>
Mar 2010	286	282
Jun 2010	284	284
Sep 2010	288	286
Dec 2010	289	288
Mar 2011	287	290
Jun 2011	286	292
Sep 2011	286	294
Dec 2011	287	296
Mar 2012	294	298
Jun 2012	294	300
Sep 2012	196	302
Dec 2012	298	304
Mar 2013	304	306
Jun 2013	309	308
Sep 2013	313	310
Dec 2013	318	312

41. The data in Exhibit 2.3 shows, for a certain country, real GDP and its growth trend from March 2010 through December 2013. Identify when the peak occurred, when the recession occurred, and when the economy reached its trough.

ANS:

Recall the rule of thumb that a fall in real GDP must last at least six months (two quarters) before it is considered a recession. The peak occurred in December 2010. The recession lasted from December 2010 through September 2011. The trough occurred in September 2011.

PTS: 1                      DIF: moderate              TOP: Economic fluctuations: temporary setbacks and recoveries

42. A recession that is very severe in depth and duration is called a

- panic.
- financial crisis.
- depression.
- deflation.

ANS: C                      PTS: 1                      DIF: basic

TOP: Recessions v depressions

43. What is the difference between a recession and a depression? Have there been any depressions over the last 50 years? Justify your answer.

ANS:

There is no formal definition for a depression. It is considered to be a very long and deep recession. Over the past 50 years there have not been any depressions. Declines in real GDP in recessions since the 1950s are not as deep as some of the recessions that occurred prior to the Second World War.

PTS: 1                    DIF: moderate            TOP: Recessions v depressions

44. The term *depression* best describes

- a. most of the recessions occurring after the Second World War except for the 1990–91 recession.
- b. most of the recessions occurring after the Second World War including the 1990–91 recession.
- c. most of the recessions that have occurred since the end of the Second World War.
- d. the 1990–91 recession.
- e. the recessions that occurred in the 1930s.

ANS: E                    PTS: 1                    DIF: moderate

TOP: Recessions v depressions

45. Which of the following is *not* considered to be scarce and limiting the ability to supply for an economy as a whole?

- a. Money
- b. Workers
- c. Land
- d. Machinery
- e. Factories

ANS: A                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

46. Another name for potential GDP is

- a. GDP.
- b. real GDP per capita.
- c. nominal GDP.
- d. real GDP.
- e. aggregate supply.

ANS: E                    PTS: 1                    DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

47. Which of the following is *not* a determinant of aggregate supply?

- a. The supply of labour
- b. Computers
- c. Aggregate demand
- d. The amount of factories in the economy
- e. Available know-how

ANS: C                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

48. Macroeconomic choices are made whenever
- money is limited.
  - there are too many alternatives.
  - aggregate supply is limited relative to human wants.
  - the society has abundant resources.
  - different people in an economy want different things.

ANS: C            PTS: 1            DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

49. *True or False.* Choices are necessary only for individuals but not for the economy as a whole.

ANS: F            PTS: 1            DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

50. Which of the following does a production possibilities schedule best illustrate?

- The concept of achieving an impossible goal
- The concept of unlimited possibilities
- The concept of opportunity cost
- The elimination of scarcity
- The concept that more is better than less

ANS: C            PTS: 1            DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

51. *True or False.* The production possibilities curve shows how an economy increases its output with more resources.

ANS: F            PTS: 1            DIF: moderate

TOP: Why the PPC shifts

52. Long-term economic growth can be shown by
- a shift of the production possibilities curve outward.
  - a point inside the production possibilities curve.
  - movement along the production possibilities curve.
  - a shift of the production possibilities curve inward.
  - changing the shape of the production possibilities curve.

ANS: A            PTS: 1            DIF: moderate

TOP: Why the PPC shifts

53. If a new labour-saving technology is discovered,
- the production possibilities curve remains unchanged.
  - the production possibilities curve shifts inward.
  - there is movement along the production possibilities curve.
  - society does not face a new set of trade-offs.
  - points that were previously unattainable to society may now be attainable.

ANS: E            PTS: 1            DIF: moderate

TOP: Why the PPC shifts

54. Which of the following does a production possibilities schedule best illustrate?

- The concept of achieving an impossible goal
- The concept of unlimited possibilities
- The concept of minimising opportunity cost
- The elimination of scarcity
- The concept of producing at efficient capacity

ANS: E            PTS: 1            DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

55. When an economy is operating on its production possibilities curve, more production of one good means less production of another because

- a. wants are unlimited.
- b. resources are limited.
- c. some resources are not employed.
- d. wants are limited.
- e. resources are not perfectly adaptable to alternative uses.

ANS: B                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

56. Which of the following is held constant when constructing a production possibilities curve for the economy?

- a. The opportunity cost
- b. The price level
- c. The amount of resources
- d. The combination of goods produced
- e. The amount of goods produced

ANS: C                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

57. A production possibilities curve shows

- a. what happens to the amount of available resources if it is not possible to produce a good.
- b. what can be produced with unlimited resources.
- c. what happens as available resources in an economy are moved from producing one type of good to another type, or vice versa.
- d. the choice between producing some goods versus other goods with unlimited resources.
- e. the different kinds of products that a firm can produce.

ANS: C                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

58. For an economy to attain what is currently impossible is

- a. a problem involving choice and scarcity, the choice being between current consumption and investment.
- b. a problem economists cannot solve.
- c. a problem of supply and demand.
- d. not an economic problem because one cannot choose something that does not exist.
- e. not an economic problem because future production is not a viable alternative to current production.

ANS: A                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

59. Suppose that an economy produces only two goods: computers and movies. If the economy at all times efficiently utilises all its resources, and it decides to use more of its available resources to produce computers,
- the production of movies will drop.
  - the production of both movies and computers will drop.
  - the production of movies will rise.
  - the production of movies will not change but the production of computers will increase.
  - there will be no change in the production of either computers or movies.

ANS: A                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

60. Josie has two classes: English and maths. She finds out that the grades for both classes have improved without spending more time studying. Using the production possibilities curve, Josie's situation can be represented by

- moving from a point on the production possibilities curve to a point inside the curve.
- a movement along the curve from the axis for English to the axis for maths.
- a movement along the curve from the axis for maths to the axis for English.
- an inward shift of the curve.
- an outward shift of the curve.

ANS: E                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

61. Given a production possibilities curve for defence goods and non-defence goods, if a nation is producing at a point inside the production possibilities curve, then

- too many resources are being used for non-defence goods.
- only new technology will increase the production of defence or non-defence goods.
- too many resources are being used for defence goods.
- society is maximising output from the limited number of resources.
- it is possible to increase defence goods production without sacrificing non-defence goods production.

ANS: E                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

62. *True or False.* The production possibilities curve is immovable, meaning that it is fixed regardless of the availability of resources.

ANS: F                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

63. *True or False.* Economic growth in the future can be encouraged by trade-offs made today.

ANS: T                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

64. Is it possible for an economy to make trade-offs in the present in order to attain what is currently unattainable? Explain.

ANS:

Yes, it is possible for an economy to make trade-offs today in order to attain what is currently unattainable. If an economy wants to grow, it might want to increase output of machinery and/or education at the expense of current consumption in order to have more resources in the future.

PTS: 1 DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

65. What explains the occurrence of increasing opportunity costs?

ANS:

Increasing opportunity costs occur because resources are better suited for one type of production compared to another. (Students of microeconomics may refer here to the law of diminishing returns as a reason.)

PTS: 1 DIF: moderate

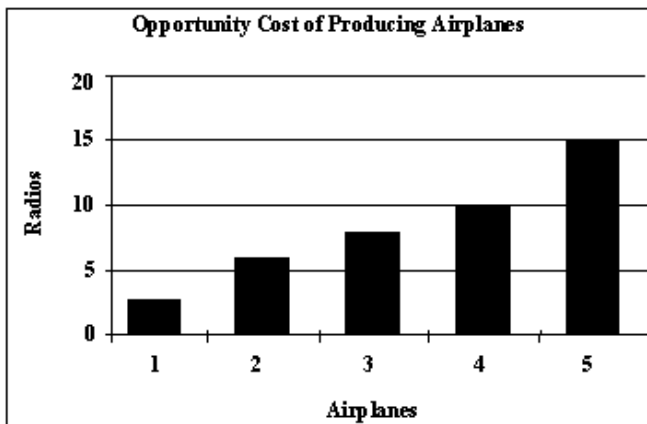
TOP: Increasing opportunity costs

66. Suppose an economy can produce either radios or airplanes. The production possibilities for this economy are shown in the table below. Show that this production possibilities schedule depicts increasing opportunity costs.

Combination	Radios	Airplanes
A	0	5
B	15	4
C	25	3
D	33	2
E	39	1
F	42	0

ANS:

A chart such as the one below shows that for each additional airplane produced, the amount of radios that needs to be given up increases as airplane production increases.



PTS: 1

DIF: moderate

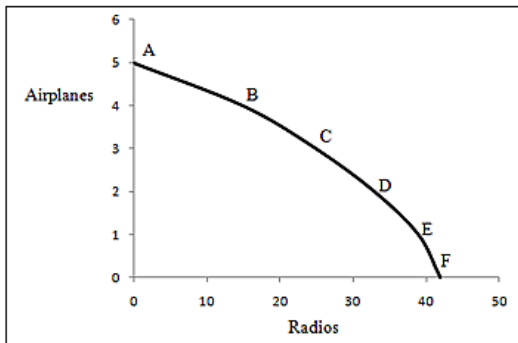
TOP: Increasing opportunity costs

67. Using the information in the table below, draw a production possibilities curve.

Production Possibilities for Radios and Airplanes		
Combination	Radios	Airplanes
A	0	5
B	15	4
C	25	3
D	33	2
E	39	1
F	42	0

- With this graph, depict the point that would show the combination of 30 radios and 1 airplane.
- With this graph, depict the point that would show the combination of 25 radios and 5 airplanes.
- With this graph, depict the point that would show the combination of 25 radios and 3 airplanes.

ANS:



A production possibilities curve that is bowed out should be drawn. The answer to part (a) should show a point inside the curve. The answer to part (b) should show a point outside the curve. The answer to part (c) should show a point along the curve.

PTS: 1                      DIF: moderate                      TOP: Increasing opportunity costs

68. If an economy produces only movies and computers, then the opportunity cost of producing more movies is

- the value of forgone computer production.
- the value of more computer production.
- the value of movie production minus the value of computer production.
- the total value of movie and computer production.
- zero because computers and movies are unrelated goods.

ANS: A                      PTS: 1                      DIF: basic

TOP: Increasing opportunity costs

69. If an economy produces only movies and computers, then producing more and more computers will most likely require
- giving up a decreasing amount of the production of movies.
  - giving up an increasing amount of the production of movies.
  - gaining an increasing amount of the production of movies.
  - gaining a decreasing amount of the production of movies.
  - no change in movie production.

ANS: B                      PTS: 1                      DIF: moderate  
 TOP: Increasing opportunity costs

**Exhibit 2.4**

Production Possibilities for Computers and TV Sets		
Combination	Computers	TV Sets
A	0	6
B	15	5
C	25	4
D	33	3
E	39	2
F	42	1
G	43	0

70. Refer to Exhibit 2.4. The opportunity cost of producing the first television set is
- 15 units of computers.
  - 5 units of computers.
  - 43 units of computers.
  - 42 units of computers.
  - 1 unit of computers.

ANS: E                      PTS: 1                      DIF: moderate  
 TOP: Increasing opportunity costs

71. Refer to Exhibit 2.4. The opportunity cost of producing the sixth television set is
- 15 units of computers.
  - 5 units of computers.
  - 43 units of computers.
  - 42 units of computers.
  - 1 unit of computers.

ANS: A                      PTS: 1                      DIF: moderate  
 TOP: Increasing opportunity costs

72. *True or False.* The typical production possibilities schedule shows that the opportunity cost for producing more of one good requires giving up an increasing amount of production of another good.

ANS: T                      PTS: 1                      DIF: moderate  
 TOP: Increasing opportunity costs



**Exhibit 2.5**

<b>Production Possibilities for Computers and TV Sets</b>		
Combination	Computers	TV Sets
A	0	6
B	15	5
C	25	4
D	33	3
E	39	2
F	42	1
G	43	0

73. Refer to Exhibit 2.5. The production possibilities curve representing the given schedule would be a

- a. negatively sloped curve that bows outward.
- b. negatively sloped straight line.
- c. positively sloped curve that bows outward.
- d. positively sloped curve that bows inward.
- e. positively sloped straight line.

ANS: A                      PTS: 1                      DIF: moderate

TOP: Increasing opportunity costs

74. A point lying inside the production possibilities curve

- a. indicates that resources are not being fully or efficiently used.
- b. illustrates resources being used to their fullest potential.
- c. requires more resources than are presently available.
- d. represents an increase in resources.
- e. is not an attainable combination.

ANS: A                      PTS: 1                      DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

75. The theory of economic fluctuations emphasises fluctuations in

- a. the growth rate of potential GDP.
- b. aggregate supply.
- c. aggregate demand.
- d. technology.
- e. potential GDP.

ANS: C                      PTS: 1                      DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

76. *True or False.* Real GDP can be greater than potential GDP.

ANS: T                      PTS: 1                      DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

77. *True or False.* The theory of economic fluctuations emphasises fluctuations in the supply of goods and services as the reason for the ups and downs in the economy.

ANS: F                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

78. If resources are being used efficiently,
- a. a society can increase the production of something only by decreasing the production of something else.
  - b. society need no longer worry about trade-offs.
  - c. production of one good can rise only by increasing the production of some other good.
  - d. resources are used to the fullest extent that is physically possible.
  - e. scarcity is zero.

ANS: A                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

79. Suppose a financial crisis prevents many companies from getting loans so that their production levels fall as they are unable to purchase the same amount of inputs as before. We can conclude that the economy is

- a. moving efficiently along the initial production possibility curve.
- b. operating outside the production possibility curve.
- c. operating inside the initial production possibility curve.
- d. more efficient.
- e. experiencing economic growth.

ANS: C                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

80. Inefficient underuse of a nation's resources would

- a. be depicted as a point inside or below a production possibilities curve.
- b. be depicted as a point on a production possibilities curve.
- c. shift a production possibilities curve outward.
- d. cause the economy's production possibilities curve to bow inward.
- e. be depicted as a point outside or above a production possibilities curve.

ANS: A                      PTS: 1                      DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

81. Inefficient overuse of a nation's resources would

- a. be depicted as a point inside or below a production possibilities curve.
- b. be depicted as a point on a production possibilities curve.
- c. shift a production possibilities curve outward.
- d. cause the economy's production possibilities curve to bow inward.
- e. be depicted as a point outside or above a production possibilities curve.

ANS: E                      PTS: 1                      DIF: basic

TOP: Production possibilities: a simple model of aggregate supply

82. Given a production possibilities curve for defence goods and non-defence goods, a production point outside the curve

- a. cannot be attained with the current level of resources and technology.
- b. may be attained by shifting resources to defence goods.
- c. may be attained by acquiring new technology.
- d. may be attained if new resources are discovered.
- e. may be attained by acquiring both new technology and greater resources.

ANS: B                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

**Exhibit 2.6**

<b>Production Possibilities for Computers and TV Sets</b>		
<b>Combination</b>	<b>Computers</b>	<b>TV Sets</b>
A	0	6
B	15	5
C	25	4
D	33	3
E	39	2
F	42	1
G	43	0

83. Refer to the production possibilities schedule in Exhibit 2.6. A combination of 20 units of computers and 2 television sets

- a. requires an infusion of technological know-how.
- b. illustrates underemployment of resources.
- c. is possible only with full and efficient use of all resources.
- d. is unattainable because it requires resources that are not available.
- e. cannot be produced with the current supply of resources.

ANS: B                    PTS: 1                    DIF: challenging

TOP: Production possibilities: a simple model of aggregate supply

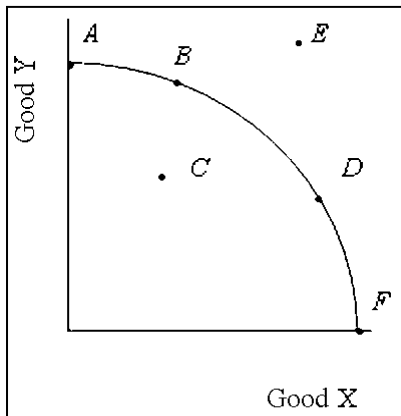
84. Refer to the production possibilities schedule in Exhibit 2.6. A combination of 40 units of computers and 4 television sets

- a. cannot be produced with the current supply of resources.
- b. is possible only with full and efficient use of all resources.
- c. has never been and never will be produced.
- d. illustrates underemployment of resources.
- e. will not satisfy the consumers' demands.

ANS: A                    PTS: 1                    DIF: challenging

TOP: Production possibilities: a simple model of aggregate supply

**Exhibit 2.7**



85. Refer to Exhibit 2.7. A movement from point *B* to point *D* indicates

- a. a gain in Good X and a loss in Good Y.
- b. a gain in Good Y and a loss in Good X.
- c. a gain in both Good X and Good Y.
- d. a loss in both Good X and Good Y.
- e. no change in the production of Good X or Good Y.

ANS: A                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

86. Refer to Exhibit 2.7. The production possibilities curve indicates that

- a. it is possible to produce more of one good without sacrificing some of the other good only if production occurs at a point inside the production possibilities curve.
- b. Good X is an input in the production of Good Y.
- c. producing an additional unit of Good X requires producing an additional unit of Good Y.
- d. more resources exist than the economy can efficiently use.
- e. the economy is experiencing decreasing opportunity costs.

ANS: A                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

87. Refer to Exhibit 2.7. Assume the economy is operating at point *C*. This indicates that

- a. the only way the economy could move toward a point such as *D* is by discovering new resources.
- b. the economy is efficiently using all its resources.
- c. there is no excess resource capacity in the economy.
- d. it is possible for the economy to produce more of Good X and Good Y with the given resources.
- e. it is possible for the economy to produce more of Good X only if it produces less of Good Y.

ANS: D                      PTS: 1                      DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

88. Refer to Exhibit 2.7. Point *C*

- a. occurs when resources are not efficiently allocated.
- b. may be attained with a sufficient improvement in technology.
- c. can be obtained with existing resources.
- d. is impossible to attain, even in the future.
- e. shows the most efficient use of valuable resources.

ANS: A

PTS: 1

DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

89. Refer to Exhibit 2.7. Point *E*

- a. occurs when resources are not efficiently allocated.
- b. may be attained with a sufficient improvement in technology.
- c. can be obtained with existing resources.
- d. is impossible to attain, even in the future.
- e. shows the most efficient use of valuable resources.

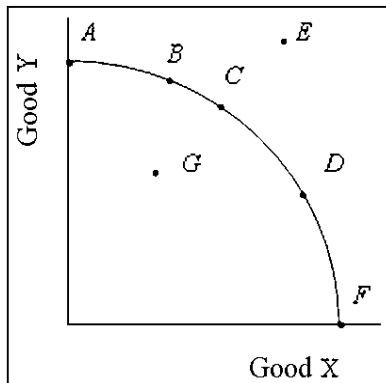
ANS: B

PTS: 1

DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

### Exhibit 2.8



90. Refer to Exhibit 2.8. The optimal point for the economy is

- a. *E*.
- b. *B*.
- c. *C*.
- d. *D*.
- e. impossible to determine from the given information.

ANS: A

PTS: 1

DIF: challenging

TOP: Production possibilities: a simple model of aggregate supply

91. Refer to Exhibit 2.8. Point *C* is more efficient than point \_\_\_\_.

- a. *A*
- b. *B*
- c. *D*
- d. *G*
- e. Ranking efficiency of two points is impossible using the given information.

ANS: D

PTS: 1

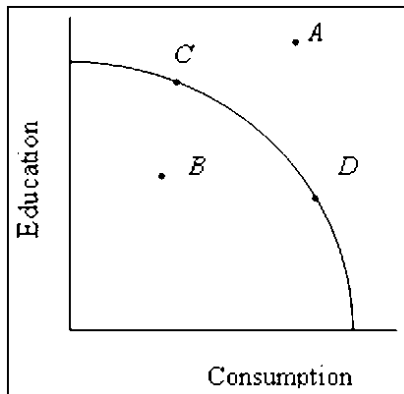
DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

92. If society begins by producing 3 units of X and 4 units of Y and then alters production so that it is now producing 4 units of X and 4 units of Y, and we know that the quantity and quality of resources were unchanged and that technology did not change, then
- society has moved along the production possibilities curve.
  - the combination of 3 units of X and 4 units of Y is best represented by a point inside the production possibilities curve.
  - the combination of 3 units of X and 4 units of Y is best represented by a point outside the production possibilities curve.
  - resources were being fully utilised at 3 units of X and 4 units of Y.
  - resources were being efficiently utilised at 3 units of X and 4 units of Y.
- ANS: B                    PTS: 1                    DIF: moderate  
 TOP: Production possibilities: a simple model of aggregate supply

93. A point outside the production possibilities curve may
- represent inefficient use of resources.
  - be due to overemployment.
  - require more resources than are currently available.
  - be attainable in the future.
  - All of the listed options are correct.
- ANS: E                    PTS: 1                    DIF: basic  
 TOP: Production possibilities: a simple model of aggregate supply

**Exhibit 2.9**



94. Refer to Exhibit 2.9. The attainment of point A in the future
- is more likely to occur if the economy chooses more investment in education.
  - can occur, but why it can is not yet understood.
  - is impossible.
  - is more likely to occur if the economy initially moves to point B to conserve resources.
  - is more likely to occur if the economy chooses more consumption.
- ANS: A                    PTS: 1                    DIF: moderate  
 TOP: Production possibilities: a simple model of aggregate supply

95. Refer to Exhibit 2.9. Which of the following is more likely to lead to the economy's attainment of point *A*?

- a. A decrease in investment in education
- b. Increased consumption
- c. An increase in the working-age population
- d. A depletion of resources
- e. None of these because point *A* is impossible to attain

ANS: C                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

96. Refer to Exhibit 2.9. If the economy depicted is at point *B*, then

- a. more consumption can be produced, but at the expense of education.
- b. any further increase in education will involve a decrease in consumption.
- c. any further increase in consumption will involve a decrease in education.
- d. any further increase in either consumption or education will benefit everyone.
- e. any further increase in either consumption or education will hurt everyone.

ANS: D                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

97. Refer to Exhibit 2.9. The trade-off that will enable the economy to reach point *A* from anywhere along the curve

- a. will be either a win-win or lose-lose situation.
- b. occurs when everyone can win.
- c. cannot occur.
- d. occurs when some people win only if others lose.
- e. occurs when everyone loses.

ANS: B                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

98. *True or False.* Moving from a point on the production possibilities curve to another point on the same curve implies a gain in production efficiency.

ANS: F                    PTS: 1                    DIF: moderate

TOP: Production possibilities: a simple model of aggregate supply

99. Which of the following statements is *true*?

- a. Real GDP fluctuates around potential GDP.
- b. Potential GDP fluctuates around real GDP.
- c. Real GDP is something like an average of GDP.
- d. Statistical analysis leads to reliable estimates of potential GDP that are generally agreed upon.
- e. Real GDP cannot be any greater than potential GDP.

ANS: A                    PTS: 1                    DIF: moderate

TOP: Real gross domestic product over time

100. The purpose of using a ratio scale (or a log scale) on an axis of a graph is

- a. to show the absolute variation in a variable.
- b. to make equal percentage changes in a variable have the same vertical distance.
- c. to make equal percentage changes in a variable have the same horizontal distance.
- d. to make equal absolute changes in a variable have the same vertical distance.
- e. to show how a variable is divided among its factors.

ANS: B                    PTS: 1                    DIF: moderate

TOP: Real gross domestic product over time

101. Why would it be a good idea to plot time-series data on a ratio scale (or log scale) instead of a regular scale in absolute units? What is the difference between the two types of graphs?

ANS:

On a ratio-scale graph, the vertical scale shrinks as the economic variable being plotted gets bigger. Equal *percentage* changes in the variable will have the same vertical distance instead of equal absolute differences having the same vertical distance. With a ratio-scale graph, a *variable that grows at a constant rate will be shown as a straight line*. On a regular graph, the same variable would look as if it were increasing at an exponential rate, which is misleading. If the line steepens, the variable is growing faster. Macroeconomists are often interested in growth rates, especially of prices (the rate inflation) and output.

PTS: 1 DIF: moderate

TOP: Real gross domestic product over time

102. Is it a good idea for the government to encourage workers to retire early and give them incentives to do so? How would this policy affect the economy's potential GDP?

ANS:

If the government encourages workers to retire early, potential GDP will fall. Unless there is some known market imperfection, any interference by the government is likely to reduce national welfare.

PTS: 1 DIF: moderate TOP: Explaining the long-term trend and short-term fluctuations

103. *True or False.* The movement from a point inside a production possibilities curve to a point outside the curve is likely to result in no change in an economy's total production.

ANS: F PTS: 1 DIF: moderate

TOP: Explaining the long-term trend and short-term fluctuations

104. The book that marked the beginning of the Keynesian revolution was entitled

- a. *The Wealth of Nations.*
- b. *A Monetary History of the United States.*
- c. *Money, Credit, and Finance.*
- d. *The General Theory of Employment, Interest and Money.*
- e. *Money, Interest and Prices.*

ANS: D PTS: 1 DIF: basic

TOP: Explaining the long-term trend and short-term fluctuations

105. According to Keynes, the prolonged slump of the 1930s was due to a decline in

- a. potential GDP.
- b. willingness to supply.
- c. private sector spending.
- d. interest rates.
- e. the size of the capital stock.

ANS: C PTS: 1 DIF: challenging

TOP: Explaining the long-term trend and short-term fluctuations



106. Which of the following statements about mainstream macroeconomics is true, according to the textbook?

- a. Classical theory validly explains long-term macroeconomic behaviour.
- b. Keynesian theory validly explains short-term macroeconomic fluctuations.
- c. It is a blend of classical and Keynesian economics.
- d. The invisible hand does not keep the economy on the production possibilities curve during the short term.
- e. All of the listed options are correct.

ANS: E PTS: 1 DIF: moderate

TOP: Explaining the long-term trend and short-term fluctuations

107. Which of the following statements is true, according to the textbook?

- a. Classical theory validly explains short-term macroeconomic behaviour.
- b. Keynesian theory validly explains long-term macroeconomic fluctuations.
- c. New Keynesian economics rejects classical economics as a long-term theory.
- d. A feature of Keynesian economics is that it is possible to be off the production possibilities curve.
- e. All of the listed options are correct.

ANS: D PTS: 1 DIF: moderate

TOP: Explaining the long-term trend and short-term fluctuations

108. The New Keynesian theory of fluctuations emphasises sudden changes in

- a. aggregate demand.
- b. technology.
- c. aggregate supply.
- d. potential GDP.
- e. weather and natural conditions (e.g., earthquakes).

ANS: A PTS: 1 DIF: basic

TOP: Explaining the long-term trend and short-term fluctuations

109. The production possibilities curve

- a. slopes downwards and is bowed out from the origin.
- b. slopes upwards and is bowed out from the origin.
- c. slopes downwards and is bowed in towards the origin.
- d. slopes upwards and is bowed in towards the origin.
- e. None of the listed options is correct.

ANS: A PTS: 1 DIF: basic

TOP: Explaining the long-term trend and short-term fluctuations

110. Points inside the production possibilities curve are

- a. efficient.
- b. inefficient, because resources are underused.
- c. inefficient, because resources are overworked.
- d. impossible.
- e. None of the listed options is correct.

ANS: B PTS: 1 DIF: basic

TOP: Explaining the long-term trend and short-term fluctuations

111. Points outside the production possibilities curve are

- a. efficient.
- b. inefficient, because resources are underused.
- c. inefficient, because resources are overworked.
- d. impossible.
- e. None of the listed options is correct.

ANS: D    PTS: 1    DIF: basic

TOP: Explaining the long-term trend and short-term fluctuations