Unit 12 AP Economics Practice Problems

Multiple Choice
Identify the choice that best completes the statement or answers the question.

1. Private savings is equal to:
    A. income less taxes, plus transfers, less consumption.
    B. taxes less government spending on goods and services.
    C. the total amount of savings accounts plus stocks plus bonds owned by households.
    D. income plus investment.
    E. income less consumption

2. If private savings increase:
    A. the demand for loanable funds will increase, interest rates will increase, and the amount of borrowing will increase.
    B. the demand for loanable funds will decrease, interest rates will decrease, and the amount of borrowing will decrease.
    C. the supply of loanable funds will increase, interest rates will decrease, and the amount of borrowing will increase.
    D. the supply of loanable funds will decrease, interest rates will increase, and the amount of borrowing will decrease.
    E. the supply of loanable funds will increase, interest rates will decrease, and the amount of borrowing will decrease.

3. National savings is equal to:
    A. private savings + consumption spending.
    B. trade balance + budget balance.
    C. private savings + budget balance.
    D. government spending + taxes.
    E. private savings + investment spending

4. The savings-investment spending identity says that savings and investment spending are:
    A. always equal because private savings match government savings.
    B. equal as long as there is no trade surplus or deficit.
    C. always equal for the economy as a whole.
    D. equal as long as there is not government budget deficit or surplus.
    E. always equal when there is a balanced government budget and net exports equal zero.

5. The government saves when it:
    A. has a balanced budget.
    B. has a budget deficit.
    C. has a budget surplus.
    D. borrows by selling bonds.
    E. spends more than it collects in tax revenue.

6. In a closed economy, investment spending, I, must equal:
    A. $GDP - C + G$.
    B. $GDP - C$.
    C. $GDP - C - G - X$.
    D. $GDP - [C*G]$.
    E. $GDP - C - G$.

7. Economists view investment spending as which of the following?
    A. stocks
    B. bonds

C. Spending on physical capital.
D. mutual fund investing
E. Spending on human capital.

Scenario 22-3: Economy of Centralia
Centralia has no trade and no government. GDP = $25 trillion. Consumption Spending = $18 trillion.

8. Use **Scenario 22-3.** Consider the information on the economy of Centralia. What is the level of private saving in Centralia?
   A. $43 trillion
   B. $18 trillion
   C. Cannot be determined from the information provided.
   D. -$7 trillion
   E. $7 trillion

9. Use **Scenario 22-3.** Consider the information on the economy of Centralia. What is the level of investment spending in Centralia?
   A. $18 trillion
   B. $7 trillion
   C. $25 trillion
   D. –$7 trillion
   E. $43 trillion

10. Use **Scenario 22-3.** Consider the information on the economy of Centralia. Suppose that there is a new government in Centralia, and it has decided to impose taxes on its citizens in order to spend on infrastructure. Taxes = $2 trillion. Government Spending = Taxes. What is the level of private saving in Centralia now?
    A. $11 trillion
    B. $7 trillion
    C. $5 trillion
    D. $18 trillion
    E. $9 trillion

11. Use **Scenario 22-3.** Consider the information on the economy of Centralia. Suppose that there is a new government in Centralia, and it has decided to impose taxes on its citizens in order to spend on infrastructure. Taxes = $3 trillion. Government Spending = Taxes. What is the level of investment spending in Centralia now?
    A. $7 trillion
    B. $4 trillion
    C. $18 trillion
    D. –$4 trillion
    E. $10 trillion

12. Crowding out negatively affects the economy by:
    A. decreasing government borrowing.
    B. decreasing consumption.
    C. increasing private borrowing.
    D. reducing investment spending on physical capital.
    E. decreasing government deficits.

Figure 29-8: Market for Loanable Funds II

Interest rate — Supply — r* = 8 — E — Demand — 0 — Q* = $300 — Quantity of loans
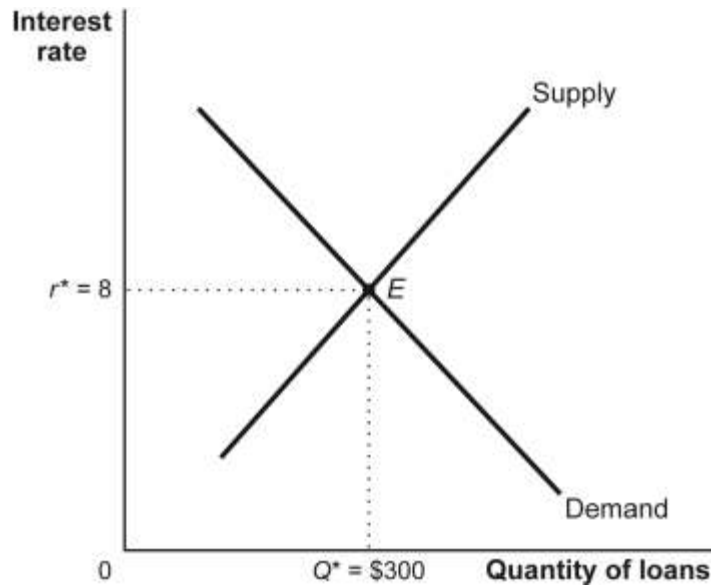
13. Use the "**Market for Loanable Funds II" Figure 29-8.** An increase in government borrowing will shift the demand for loanable funds to the:
   A. left and increase the interest rate.
   B. left and decrease the interest rate.
   C. right and increase the interest rate.
   D. right and decrease the interest rate.
   E. right and have no impact on the interest rate.

14. Use the "**Market for Loanable Funds II" Figure 29-8.** A decrease in government borrowing will shift the demand for loanable funds to the:
   A. left and increase the interest rate.
   B. right and decrease the interest rate.
   C. right and increase the interest rate.
   D. left and decrease the interest rate.
   E. left and have no impact on the interest rate.

Figure 29-9: Market for Loanable Funds II

Interest rate / Supply / Demand

$r^* = 8$ — E

0 — $Q^* = \$300$ — Quantity of loans
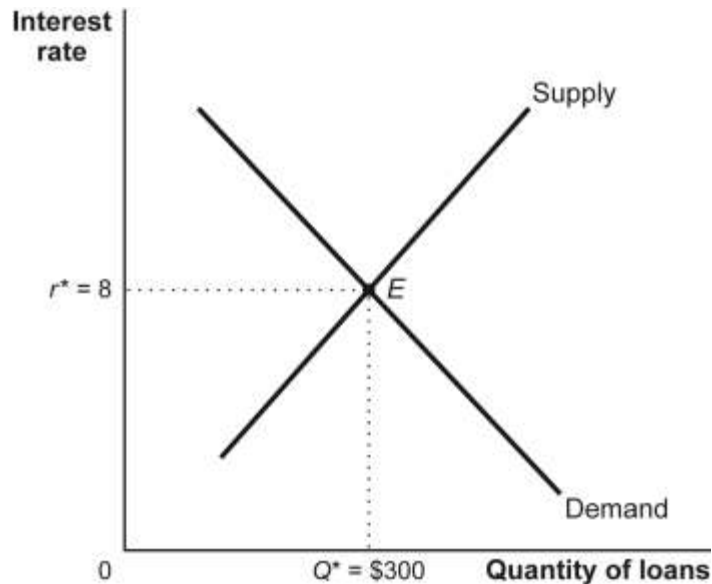
15. Use the "**Market for Loanable Funds II" Figure 29-9**. An increase in deficits by the the government will shift the demand of loanable funds to the:
   A. left and increase the interest rate.
   B. right and decrease the interest rate.
   C. right and increase the interest rate.
   D. left and decrease the interest rate.
   E. left and have no impact on the interest rate.

16. In a simple closed economy, all investment spending must come from:
   A. saving.
   B. money creation.
   C. debt issuance.
   D. foreign borrowing.
   E. government spending.

17. Finacial investment refers to all except:
   A. buying stocks.
   B. buying newly issued shares of stock.
   C. adding to physical capital.
   D. adding to one's retirement account.
   E. adding to one's education and skills.

18. The government has a budget deficit if:
   A. its total revenues are equal to its total expenditures.
   B. its total revenues are less than its total expenditures.
   C. its total revenues are greater than its total expenditures.
   D. the money supply is less than total expenditures.
   E. the money supply is greater than the money demand.

19. Public debt is:
   A. Taxes – Government purchases – Government transfers.
   B. government debt held by foreigners.
   C. government debt held by individuals and institutions outside the government.
   D. the government deficit divided by GDP.
   E. government debt held by other branches of the government.

20. If the natural rate of unemployment is 5%, and the actual rate of unemployment is 4%:

A. disinflation is likely to occur.
B. there will be no effect on prices.
C. inflation will increase.
D. the short-run Phillips curve will shift down.
E. deflation is likely to occur.

Figure 34-1: Expected Inflation and the Short-Run Phillips Curve
$SRPC_0$ is the Phillips curve with an expected inflation rate of 0%; $SRPC_2$ is the Phillips curve with an expected inflation rate of 2%.
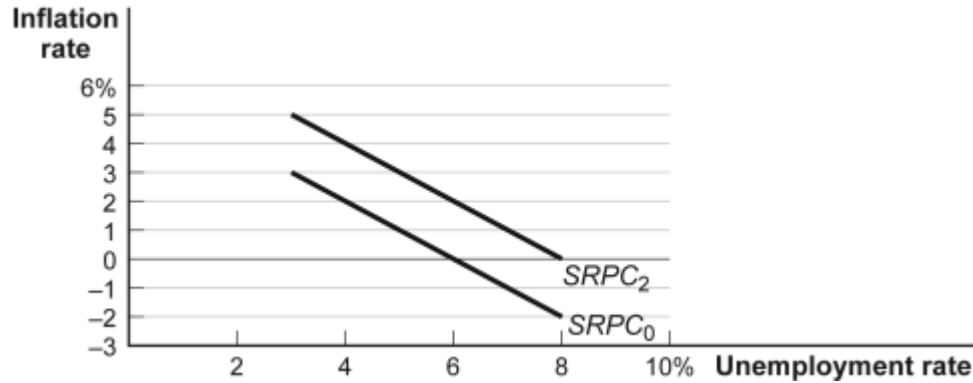
21. Use the "**Expected Inflation and the Short-Run Phillips Curve" Figure 34-1**. Suppose that this economy currently has an unemployment rate of 6%, inflation of 0%, and no expectation of future inflation. If the central bank increases the money supply such that aggregate demand shifts to the right and unemployment falls to 4%, then inflation would:
A. decrease to –2%.
B. not change.
C. increase to 2%.
D. increase to 4%.
E. increase to 8%.

22. Along a Phillips curve:
A. consumption depends on prices.
B. the inflation rate varies inversely with the unemployment rate.
C. the inflation rate varies directly with the unemployment rate.
D. prices and tax rates are directly related.
E. the interest rate varies inversely with investment spending.

23. Suppose you are told that the short-run Phillips curve has shifted upward. Which of the following must have happened?
A. The AD curve has shifted to the right.
B. The AD curve has shifted to the left.
C. The $SRAS$ curve has shifted to the right.
D. The $SRAS$ curve has shifted to the left.
E. The $LRAS$ curve has shifted to the right.

24. If workers expect a lower rate of inflation, the short-run Phillips curve will:
A. remain constant, but there will be a movement down the curve.
B. be unaffected.
C. shift up.
D. shift down.
E. remain constant, but there will be a movement up the curve.

25. Which of the following accurately portrays the shape of the long-run Phillips curve?
    A. horizontal
    B. vertical
    C. upward sloping
    D. downward sloping
    E. backward bending

26. As a consequence of the existence of a non-accelerating-inflation rate of unemployment, or NAIRU:
    A. cyclical unemployment can never be zero.
    B. there is no short-run tradeoff between unemployment and inflation.
    C. money is neutral.
    D. in the long run, unemployment can be equal to zero.
    E. there is no long-run tradeoff between unemployment and inflation.

Figure 34-3: Short-Run Phillips Curve
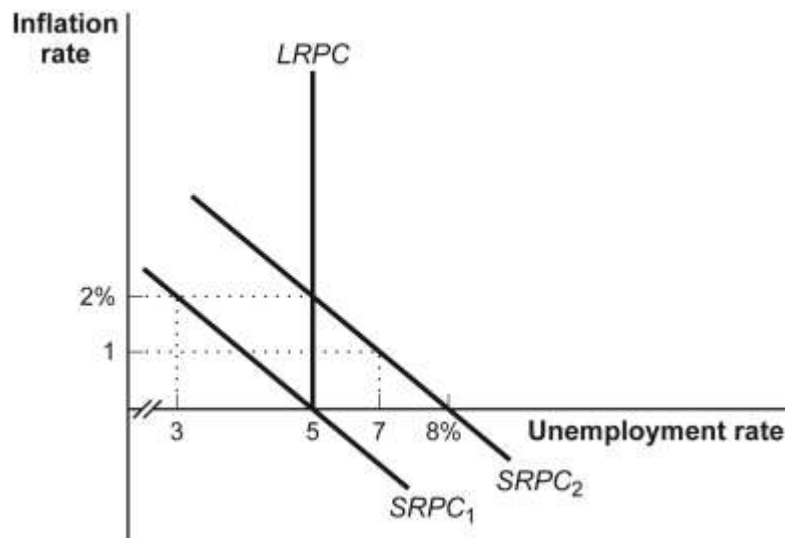
27. Use the "**Short-Run Phillips Curve**" **Figure 34-3.** The natural rate of unemployment is:
    A. 3%.
    B. 5%.
    C. 7%.
    D. 8%.
    E. 1%.

28. Disinflation means a decrease in:
    A. prices.
    B. the rate of inflation.
    C. aggregate supply.
    D. the money supply.
    E. unemployment.

29. Real per capita GDP is:
    A. real GDP divided by the population.
    B. real GDP divided by the amount of capital available in the economy.
    C. not a good useful measure of human welfare.
    D. rarely used as a tool to compare countries' possible resources.
    E. measures the value of the nation's financial markets.

30. Productivity declines when:
    A. the number of hours worked exceeds the number of workers.
    B. population growth exceeds real GDP growth.
    C. the ratio of adult civilians employed outside the home rises.
    D. real GDP growth exceeds population growth.
    E. the literacy rate grows and more workers complete college.

31. The term "Human capital" describes:
    A. improvement made possible by better machines and equipments available.
    B. improvement in the technology available to the work force.
    C. improvement in the worker made possible by education, training and knowledge.
    D. improvement in the robotics technology that can substitute for a human worker.
    E. improvement made possible by better information technology systems.

32. Investment in human capital shifts the aggregate production function:
    A. downward.
    B. leftward.
    C. inward.
    D. rightward.
    E. upward.

33. If the Fed conducts an open-market purchase:
    A. bank reserves decrease and the money supply decreases.
    B. bank reserves increase and the money supply increases.
    C. bank reserves decrease and the money supply increases.
    D. bank reserves increase and the money supply decreases.
    E. bank reserves increase and the money supply does not change.

Short Answer

1. Draw a correctly labled graph of the short run and long run Phillips Curve. Label the following:
        i. expected rate of infaltion and
        ii. natural rate of unemployment.
   B. Suppose the economy sees excessive GPD expansion, higher than natural rates of employment and unexpected increases in the price level.
        i. Label the current economy on your graph from A.
        ii Show, on your graph from A, how this economy reaches long-run equilibrium assuming no policy action. Explain.

Unit 12 AP Economics Practice Problems
Answer Section

MULTIPLE CHOICE

   1. ANS: A   BNK: Module 22
   2. ANS: C   BNK: Module 22
   3. ANS: C   BNK: Module 22
   4. ANS: C   BNK: Module 22
   5. ANS: C   BNK: Module 22
   6. ANS: E   BNK: Module 22
   7. ANS: C   BNK: Module 22
   8. ANS: E   BNK: Module 22
   9. ANS: B   BNK: Module 22
  10. ANS: C   BNK: Module 22
  11. ANS: B   BNK: Module 22
  12. ANS: D   BNK: Module 29
  13. ANS: C   BNK: Module 29
  14. ANS: D   BNK: Module 29
  15. ANS: C
  16. ANS: A   BNK: Module 22
  17. ANS: C
  18. ANS: B   BNK: Module 30
  19. ANS: C   BNK: Module 30
  20. ANS: C   BNK: Module 34
  21. ANS: C   BNK: Module 34
  22. ANS: B   BNK: Module 34
  23. ANS: D   BNK: Module 34
  24. ANS: D   BNK: Module 34
  25. ANS: B   BNK: Module 34
  26. ANS: E   BNK: Module 34
  27. ANS: B   BNK: Module 34
  28. ANS: B   BNK: Module 34
  29. ANS: A   BNK: Module 37
  30. ANS: B   BNK: Module 37
  31. ANS: C   BNK: Module 37
  32. ANS: E   BNK: Module 38
  33. ANS: B   BNK: Module 27

SHORT ANSWER

   1. ANS:
      X