Intermediate Macroeconomics (ECON 311)
Exam 1 Review

Key Terms

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True/False  Determine if the question is true or false (answer key at end of document)

1. When a firm sells a product out of inventory, investment expenditures increase at the same time consumption expenditures decrease.

2. The price level is an example of a nominal variable.

3. Modigliani’s life-cycle hypothesis puts great emphasis on saving for medical contingencies.

4. If time preferences were to rise economy-wide among capitalists, these capitalists, at the margin, would be willing to supply more capital (savings) to the investment market.

5. Overall, consumption responds positively to income and negatively to interest rates.

Multiple Choice  Select the best answer from among the available choices

6. All of the following are measures of GDP except the total:
   a) expenditures of all businesses in the economy.
   b) income from all production in the economy.
   c) expenditures on all final goods produced.
   d) value of all final production.

7. GDP is the market value of all _______ goods and services produced within an economy in a given period of time.
   a) used  b) intermediate  c) consumer  d) final

8. The marginal product of labor is:
   a) output divided by labor input.
   b) additional output produced when one additional unit of labor is added.
   c) additional output produced when one additional unit of labor and one additional unit of capital are added.
   d) value of additional output when one dollar’s worth of additional labor is added.
9. The *nominal* interest rate is the:
   a) rate of interest that investors pay to borrow money.
   b) same as the real interest rate.
   c) rate of inflation minus the real rate of interest.
   d) real rate of interest minus the rate of inflation.

10. The government raises lump-sum taxes on income by $100 billion, and the neoclassical economy adjusts so that output does not change. If the marginal propensity to consume is 0.6, private saving:
   a) rises by $40 billion.
   b) rises by $60 billion.
   c) falls by $60 billion.
   d) falls by $40 billion.

11. The average propensity to consume is the:
   a) ratio of consumption to income.
   b) amount consumed out of an additional dollar of income.
   c) amount available for consumption after precautionary saving.
   d) ratio of consumption to wealth.

12. In Irving Fisher’s two-period consumption model, if \( Y_1 = 20,000 \), \( Y_2 = 15,000 \), and the interest rate \( r \) is 0.50 (50 percent), then the maximum possible consumption in period one is:
   a) 20,000.  b) 25,000.  c) 30,000.  d) 35,000.

13. In Irving Fisher’s two-period model, if the consumer is initially saving in period one and the real interest rate rises, then first-period consumption will:
   a) certainly fall.  b) certainly rise.  c) remain constant.  d) either rise or fall.

14. Business fixed investment includes:
   a) rental housing that landlords buy to rent out.
   b) goods businesses put aside in fixed storage facilities, including materials and supplies.
   c) the fixed cost of borrowing that businesses pay for new equipment.
   d) equipment and structures that businesses buy to use in production.

15. The real interest rate should be inversely related to investment in:
   a) plant and equipment, home building, and inventories.
   b) plant and equipment and home building, but not inventories.
   c) plant and equipment and inventories, but not home building.
   d) inventories and home building, but not plant and equipment.

16. Inventory investment, at least in theory, should:
   a) rise when the real interest rate rises, other things being equal.
   b) not depend on the real interest rate, other things being equal.
   c) fall when the real interest rate rises, other things being equal.
   d) depend only on the change in real GDP.

17. The most volatile component of real GDP is:
   a) consumption spending.  c) investment spending.
   b) government spending.  d) net exports.

18. In Irving Fisher’s two-period model, if the consumer is initially borrowing in period one and the real interest rate rises, first-period consumption (assuming it is a normal good) will:
   a) certainly rise.  b) certainly fall.  c) remain constant.  d) either rise or fall.
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You should also be able to:

✓ Draw and use (i.e., be able to make predictions from) the 2-period Intertemporal choice model
✓ Draw and use the basic investment market model