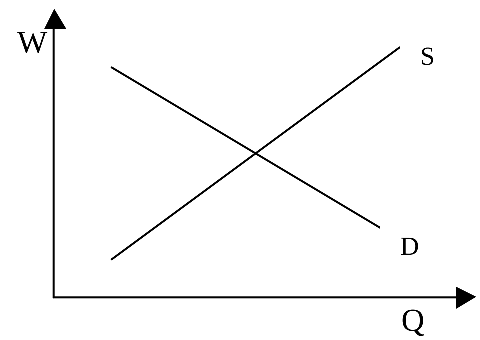
1B-0B Fall 1999 Section 9 Name: ______________________________

Student ID#: ______________________________

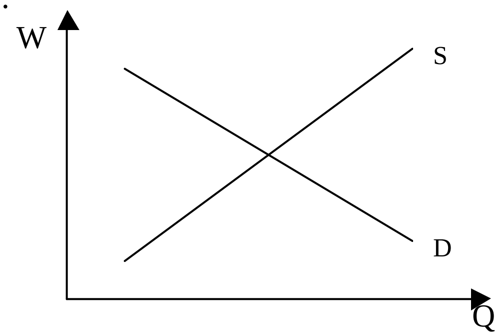
Quiz #2

Long Questions (Each Part worth 5 points) (Use the back if necessary)

1) We are examining the labor market for both High and Low Skilled workers. Suppose the government taxes high skilled workers in order to pay a subsidy to low skilled workers.
   a) In the Supply and Demand Graph below and in words, explain what occurs in the High Skilled labor market.



   b) Would this policy cause society to experience a dead weight loss? If so, explain why, and show the dead weight loss in the below separate graph.



   c) Would society be better off or worse off because of the subsidy paid to low skilled workers. Explain in words.

2) The required reserve ratio equals 1/4.
   a) Find the money multiplier.

   b) On a trip to the San Fransisco Fed, I am the 1 millionth visitor. For this they give me, $1 million in newly printed currency. I take all of this to the bank. What is the maximum amount of loans this bank can make, just from my deposit.

   c) What is the maximum amount that the Feds $1 million gift can change the money supply, after it has entered the banking system.

Multiple Choice Questions: (3 points Each)

1) Which of the following is not a good reason for a government to run a deficit?
   a) Government Investment Projects.
   b) Stabilizing the economy during a boom.
   c) Retraining workers after their industry collapsed.
   d) None of the above.

2) A Government has a true pay-as-you-go social security system with no surplus or deficit. They pay benefits of $10,000 a year to the elderly population. There twice as many young people as elderly people in the country. The average income of a young person is $20,000. What must the social security tax be:
   a) 1/5
   b) 1/4
   c) 1/3
   d) 1/2

3) Private investment is a 10% share of GDP when the government has a balanced budget. However, each 1% share of GDP increase in the government deficit crowds out 1% share of GDP worth of private investment. Government investment is 3%. According the “Golden Rule,” what is the highest deficit the government can run and still be a “good” deficit. (Only whole Numbers)
   a) 13% share of GDP
   b) 10% share of GDP
   c) 7% Share of GDP
   d) 6% Share of GDP
   e) 0% Share of GDP

4) Suppose the required reserve ratio is .2 and banks hold no excess reserves. The Fed sells $100 worth of bonds on the open market, what happens to the total money supply.
   a) Increases by $100.
   b) Decreases by $100
   c) Increases by $20
   d) Increases by $500
   e) Decreases by $500

5) Tom transfers $100 from his Checking account into his savings account. Which of the following occurred:
   a) M1 increased, M2 increased
   b) M1 decreased, M2 decreased
   c) M1 decreased, M2 increased
   d) M1 decreased, M2 remains the same
   e) M1 remains the same, M2 increased

6) Which of the following statements is true?
   a) If the Fed sells bonds on the open market, the interest rate will fall and the money supply will increase.
   b) If the Fed sells bonds on the open market, the interest rate will increase and the money supply will fall.
   c) If the Fed sells bonds on the open market, both the interest rate and the money supply will increase.
   d) If the Fed sells bonds on the open market, both the interest rate at the money supply will fall.

7) During the late 1980s and early 1990s, one key area of macroeconomic research was the study of "Twin Deficits." The twin deficits are:
   a) Federal Government deficit and State Government deficit
   b) Government deficit and Trade deficit
   c) US Government Deficit and UK Government deficit
   d) Consumer deficits and Government deficit.

8) The Brazilian social security crisis has been caused by all of the following EXCPET:
   a) corruption
   b) legal loopholes
   c) “political myopia”
   d) foreign intervention

9) If the non-bank public decides to hold more money as currency, by holding less as checking account deposits, this would most likely cause.
   a) a decrease in the money supply
   b) an increase in the money supply
   c) a drop in interest rates
   d) a rise in aggregate demand
   e) a rise in bank reserves

10) If the Fed increases its holdings of government bonds at the same time the federal deficit is increasing,
   a) The Fed and Congress are, as usual, coordinating their activities.
   b) The Fed is trying to push up interest rates
   c) The deficit is being monetized
   d) Crowding out is more likely to occur
   e) Inflation will be reduce