

PRC - 3

BUSINESS AND ECONOMIC INSIGHTS



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VOLUME - II

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NATURE AND SCOPE OF ECONOMICS

1. Islamic economic system:
 - a) allows short selling
 - b) no ban on state ownership
 - c) applies to consumers but not to firms.
 - d) refers only to state not on general public.
2. Which of the following statements is not correct?
 - a) Economics is a behavioural science.
 - b) Economics is the study of how people make choices.
 - c) If poverty were eliminated, there would be no reason to study economics.
 - d) Economic analysis can be used to explain how both individuals and societies make decisions.
3. The concept of opportunity cost
 - a) is relevant only to economics.
 - b) can be applied to the analysis of any decision-making process.
 - c) applies to consumers but not to firms.
 - d) refers only to actual payments and incomes.
4. Which of the following is not an opportunity cost of attending college?
 - a) the alternative admission in any other college sacrificed
 - b) the income you could have earned if you didn't attend college
 - c) the alternative uses of the time you spend studying
 - d) the cost of the food that you consume while you are attending college
5. Economics is best defined as the study of
 - a) financial decision making.
 - b) how consumers make purchasing decisions.
 - c) choices made by people faced with scarcity.
 - d) inflation, unemployment, and economic growth.
6. Studying how the management of XY computer company decides how many computers to produce and the price to charge for its computers would be considered
 - a) descriptive economics.
 - b) empirical economics.
 - c) microeconomics.
 - d) macroeconomics

7. Which of the following is a microeconomics question?
 - a) Is it sensible for a government to subsidize tobacco production?
 - b) Why do some countries grow faster than others?
 - c) Should Congress and the president take action to reduce global warming?
 - d) Should the government attempt to influence the interest rate to lower inflation?
8. We can use macroeconomic analysis to
 - a) learn how to balance a checkbook.
 - b) study the choices made by households.
 - c) understand marginal changes in the macroeconomy.
 - d) understand why economies grow.
9. The government should extend the duration of unemployment benefits to those workers who lost their jobs due to outsourcing. This statement is best described as
 - a) an example of marginalism.
 - b) an example of the fallacy of composition.
 - c) a normative statement.
 - d) a positive statement.
10. Which of the following would an economist classify as capital?
 - a) A Rs.50 thousands bill payable
 - b) A corporate bond
 - c) A post office employee
 - d) A guitar used by a musician
11. In a market economy, the allocation of resources between different productive activities is determined mainly by the:
 - a) Decisions of the government
 - b) Wealth of entrepreneurs
 - c) Pattern of consumer expenditure
 - d) Supply of factors of production
12. In a market economy the price system provides all of the following except which one?
 - a) An estimation of the value placed on goods by consumers
 - b) A distribution of income according to needs
 - c) Incentives to producers
 - d) A means of allocating resources between different uses
13. The 'central economic problem' means:
 - a) The output of goods and services is limited by scarce resources
 - b) Market prices do not always equal costs of production
 - c) All businesses must make a profit
 - d) Consumers cannot maximize their utility because of limited information

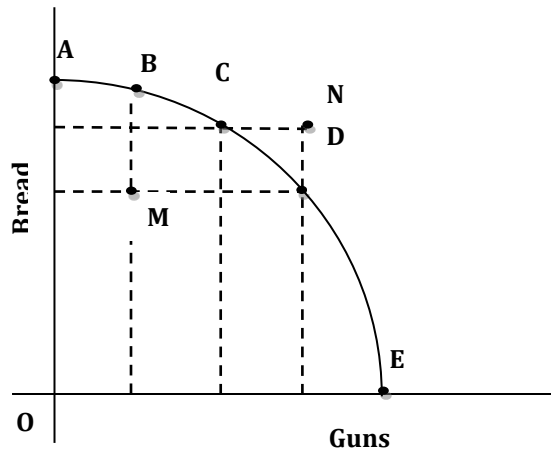
14. Which one of the following statements is not true?
 - a) The basic economic problem is the same in planned and free market economies.
 - b) The basic economic problem is one of choice between alternatives.
 - c) Factors of production are limited in supply.
 - d) Choice is necessary because of limited consumer wants.
15. Which one of the following is not a characteristic of a mixed economy?
 - a) Weights and measures legislation
 - b) Employment protection legislation
 - c) Oligopolies in some industries
 - d) Absence of a stock market
16. In a planned economy, the pattern of production is determined by:
 - a) Central allocation
 - b) Consumer preference
 - c) The price mechanism
 - d) The private sector
17. In a free market economy, the price mechanism:
 - a) Aids government control
 - b) Allocates resources
 - c) Reduces unfair competition
 - d) Measures national wealth
18. Which one of the following would not shift a country's production possibility frontier outwards?
 - a) An increase in exports
 - b) Technical progress reducing production costs
 - c) An increase in the working population
 - d) An improvement in the literacy rate
19. Which one of the following is not a social cost?
 - a) Alcohol-related violence
 - b) Compensation paid by a company to a customer
 - c) Crimes caused by unemployment
 - d) Stress caused by overwork
20. Which of the following is not a feature of a mixed economy?
 - a) Welfare payments to the long-term sick
 - b) Public ownership of all means of production
 - c) Government control of interest rates
 - d) Private ownership of land

21. Economic value (exchange value) depends upon_____:
- a) The size of the money supply
 - b) Specialization
 - c) Scarcity
 - d) None of the above
22. In Islam Ijara is a leasing agreement.
- a) True
 - b) False
23. Which of the following is likely to shift the production possibility frontier outwards (away from the origin)?
- a) An increase in the participation rate
 - b) An increase in specialization
 - c) An increase in productivity
 - d) All of the above
24. In a mixed or market economy, which of the following would tend to contribute to continuing growth?
- a) Expectation of future growth
 - b) A rise in the general level of prices
 - c) A fall in the level of unemployment
 - d) None of the above
25. Farming is regarded as the primary sector of an economy?
- a) True
 - b) False
26. Which of the following is not a factor reward?
- a) An in-work welfare payment
 - b) The discount on a bill of exchange
 - c) The increased value of a share option
 - d) A repayment by the government of tax overpaid
27. Production possibility curve is upward sloping left to right.
- a) True
 - b) False
28. Which of the following is not a public good?
- a) Public Park
 - b) Defence system
 - c) A public library
 - d) Community Dastarkhwan
29. Short selling and non-asset backed derivatives are not permitted in Islam.
- a) True
 - b) False

30. Where a financial expert offers specialist investment in which the customer and bank share profits is called Ijara.
 - a) True
 - b) False
31. The secondary sector of the economy consists of industries that provide services.
 - a) True
 - b) False
32. When a transaction has an effect that extends beyond the parties to the transaction, that effect is called externality.
 - a) True
 - b) False
33. _____ is a limitation of microeconomics?
 - a) Excessive Generalization
 - b) Heterogeneity is ignored
 - c) Overall analysis can be misleading
 - d) it provides a restricted picture of economy
34. _____ is the payment for the use of factors of production that are fixed in supply.
 - a) Wages
 - b) Labour
 - c) Rent
 - d) Profit
35. Consumption of “Economic bad” can lead to negative externalities.
 - a) True
 - b) False
36. _____ and _____ are the benefit(s) of division of labour in a production process?
 - a) Saving time
 - b) Reduce inflation
 - c) Increase productivity
 - d) All of these
37. The substance of the transaction is that the bank buys an item then sells it to the customer on a deferred basis is called Mudaraba.
 - a) True
 - b) False
38. _____ is an advantage of the market economic system?
 - a) It aims for equality of income
 - b) It ensures the provision of defense and law and order
 - c) It gives an incentive to produce
 - d) It reduces pollution and congestion

39. Due to _____ The production possibility frontier is concave to the origin:
- a) In order to produce one good, resources must be diverted from the other
 - b) Some resources are better at producing one good and some resources are good at producing other good
 - c) There is always some level of unemployment
 - d) All resources contribute towards production equally
40. Economics studies individuals and organizations in society engaged in the _____ the:
- a) Production of goods and services
 - b) Distribution of goods and services
 - c) Consumption of goods and services
 - d) All of the above
41. Economic principles, theories or models
- a) Seek to explain and predict economic events in the hope of developing policies to correct economic problems
 - b) Identify all of the numerous detailed causes of an economic event
 - c) Develop rules of individual behavior in order to generalize and predict society's economic behavior
 - d) All of the above
42. _____ does not refer to macroeconomics?
- a) The study of aggregate economic activity
 - b) The study of the economic behavior of individual decision-making units such as consumers resource owners, and business firms
 - c) The study of the causes of and policies to remedy unemployment
 - d) The study of the causes of inflation
43. The economic problem of for whom to produce refers to the decision of _____
- a) How to allocate economic resources
 - b) How many of the wants of various members of society are to be satisfied
 - c) Who will be the potential buyers
 - d) How much saving should go on in the economy
44. The production-possibility curve shifts outward when _____:
- a) There is an increase in the opportunity cost of a good,
 - b) Increased drug use decreases the skills of the labor force,
 - c) There is a technological advance,
 - d) Resources are cut off.
45. Passive factor of production is:
- a) entrepreneur
 - b) labour
 - c) land
 - d) gold

46. In given diagram movement from point A to E is called:



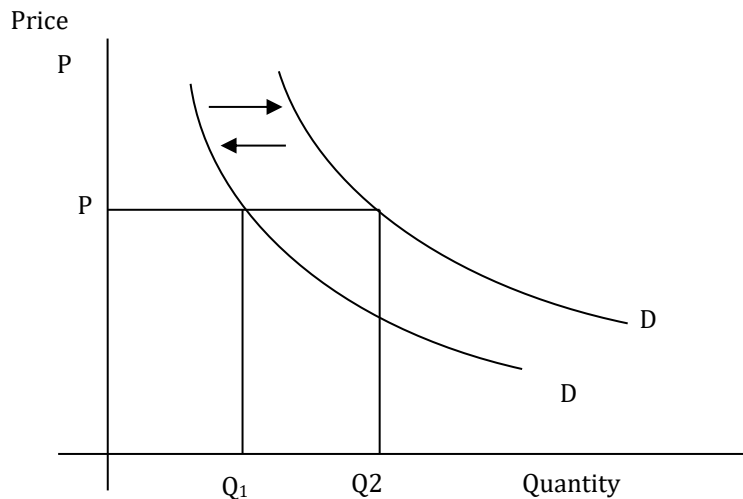
- a) Trade-off
 - b) Sale
 - c) Purchase
 - d) loss
47. Goods are being produced with intentions to sell them who have ability to buy them.
- a) How to produce?
 - b) How much to produce?
 - c) For whom to produce?
 - d) What to produce?

ANSWERS TO SELF TEST QUESTIONS

1	(b)	11	(c)	21	(c)	31	(b)	41	(a)
2	(c)	12	(b)	22	(a)	32	(a)	42	(b)
3	(b)	13	(a)	23	(d)	33	(d)	43	(c)
4	(d)	14	(d)	24	(a)	34	(c)	44	(c)
5	(c)	15	(d)	25	(a)	35	(a)	45	(c)
6	(c)	16	(a)	26	(a)	36	(a & c)	46	(a)
7	(a)	17	(b)	27	(b)	37	(b)	47	(c)
8	(d)	18	(a)	28	(d)	38	(c)		
9	(c)	19	(b)	29	(a)	39	(b)		
10	(d)	20	(b)	30	(b)	40	(d)		

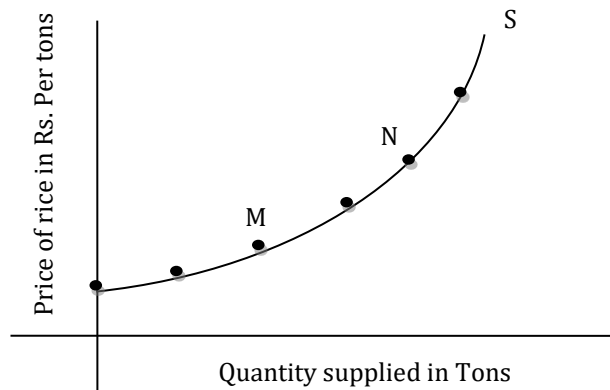
DEMAND, SUPPLY AND MARKET EQUILIBRIUM

1. When the price of a good is held below the equilibrium price, the result will be
 - a) Excess supply
 - b) A shortage of the good
 - c) A surplus of the good
 - d) $Q_d = Q_s$
2. The following demand curve for a product will shift to the left when there is.



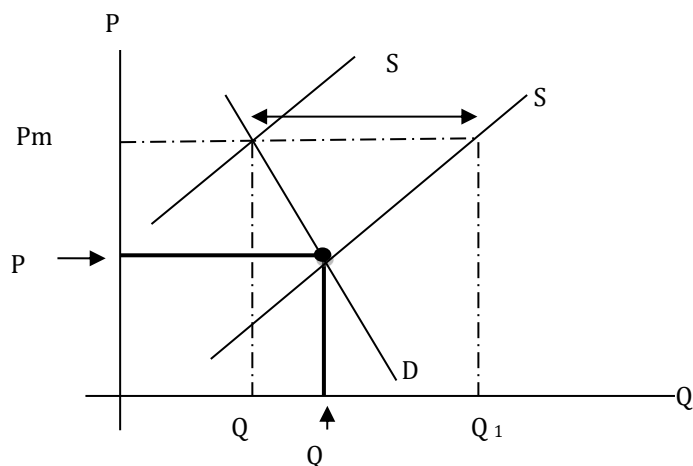
- a) A rise in household income
 - b) An increase in the product's desirability from the point of view of fashion
 - c) A fall in the price of a substitute
 - d) A fall in the price of a complement
3. Which of the following is likely to lead to a fall in the price of good Q?
 - a) A rise in the price of good P, a substitute for good Q
 - b) A fall in the level of household incomes generally
 - c) A fall in the price of good T, a complement to good Q
 - d) A belief that the price of good Q is likely to double in the next 3 months
4. Which of the following goods is not complementary to the service of movie framing?
 - a) Rented accommodation
 - b) Wooden tables
 - c) Camera
 - d) Photographic film

5. Giving following diagram movement from M to N is due to:



- a) A reduction in subsidies
 - b) A reduction in direct taxation on incomes
 - c) A reduction in price of the product
 - d) An increase in the price of a product
6. Which one of the following would normally cause a rightward shift in the demand curve for a product?
- a) A fall in the price of a substitute product
 - b) A reduction in direct taxation on incomes
 - c) A reduction in price of the product
 - d) An increase in the price of a complementary produce
7. If the price of coffee falls, which one of the following outcomes would be expected to occur?
- a) A fall in the quantity of coffee demanded
 - b) A rise in the price of tea
 - c) A fall in the demand for drinking cups
 - d) A fall in the demand for tea
8. Consider the price and demand for flower vases. The price of cut flowers goes up sharply. Which of the following would you expect to happen?
- a) The demand curve for flower vases will shift to the left and their price will rise
 - b) The demand curve for flower vases will shift to the right and their price will rise
 - c) There will be a movement along the demand curve for flower vases and their price will go down
 - d) The demand curve for flower vases will shift to the left and their price will go down
9. Which of the following changes will cause the demand curve for chocolate to shift to the right?
- a) A fall in the price of chocolate
 - b) A health campaign which claims that chocolate makes you fat
 - c) A rise in the price of chocolate substitutes
 - d) A fall in consumers' income

10. The government set the price floor at P_m , which shows:



- Surplus of good Q
 - An expected rise in the tax on future consumption
 - An expected rise in the price of the good
 - Shortage of goods in market
11. Which of the following goods have demand curves that do not slope downwards from left to right?
- Giffen good
 - Display good on outlet
 - A good for which demand is perfectly inelastic
 - All of the above
12. A rightward shift of the market supply curve for a manufactured good cannot be the result of:
- A fall in the cost of factors of production
 - A rise in the price of substitutes in supply
 - A rise in production efficiency
 - All of the above
13. Which of the following is not a likely consequence of a government setting a maximum price that is lower than the equilibrium price?
- Waiting lists
 - A black market
 - An excess of supply over demand
 - Rationing
14. Which of the following would cause a reduction in the demand for motor cars?
- A fall in the price of petrol
 - A substantial reduction in train fares
 - A rise in the cost of motor cycle road tax licenses
 - None of these

15. Advertising campaign by firms in the industry and an increase in wages to workers in industry, the price and quantity consumed of a particular product change:
- a) A movement along the demand curve and a shift in the supply curve
 - b) A shift in the demand curve and a shift in the supply curve
 - c) A movement along the demand curve and a movement along the supply curve
 - d) A shift in the demand curve and a movement along the supply curve
16. An increase in demand for a good is likely to cause decrease in demand for another good that is a substitute.
- a) True
 - b) False
17. A rise in household income is likely to result in a leftward shift in demand for inferior goods.
- a) True
 - b) False
18. The defining characteristic of a Giffen good is that when price increases, demand falls.
- a) True
 - b) False
19. A legal minimum price is set which is above the equilibrium. What will be the magnitude of the eventual excess supply?
- a) Cannot tell
 - b) Greater effect
 - c) Less effect
 - d) None of these
20. The demand by firms for goods is derived demand since it depends on the demand of household goods those firms produce in turn.
- a) True
 - b) False
21. Complements are goods that tend to be bought and used instead of one another.
- a) True
 - b) False
22. Equilibrium in the market for good A obtains
- a) When there is no surplus or shortage prevailing in the market
 - b) Where the demand and supply curves for A intersect
 - c) When all of what is produced of A is consumed
 - d) All of the above

23. _____ is called preconditions of the law.
- Government regulation
 - Ceteris paribus
 - Price the product
 - A and B
24. Rise in price of the resources will _____
- Contraction in supply
 - Extension in supply
 - Rise in supply
 - Fall in supply
25. _____ price is determined by state authorities.
- Reserve price
 - Psychological price
 - Support price
 - Discriminated
26. The supply curve would shift to the left when:
- Price of good goes down
 - Taxes of government go down
 - Prices of complements go down
 - Prices of substitute goods go down
27. The reason behind downward sloping demand curve is
- Less price attracts new buyers in market
 - Elasticity of demand
 - Inelastic demand
 - Law of diminishing marginal utility
28. In given table point D shows _____

Price	QD	QS	Situation
1	50	10	A
2	40	20	B
3	30	30	C
4	20	40	D
5	10	50	E

- Market clearance
- Surplus
- Shortage
- Loss

29. Earthquake in Abbottabad destroyed significant portion of agricultural land used to produce fruits. What would be the short-run effect on supply side for the fruits?
- A movement down the existing supply curve
 - A movement up the existing supply curve
 - A shift to the right of the supply curve
 - A shift to the left of the supply curve
30. _____ supply curve shows perishable goods
- Parallel to X-axis
 - Parallel to Y-axis
 - 45°
 - 120°
31. Which one of the following would normally cause a rightward shift in the demand curve for a product?
- A reduction in the price of a substitute product
 - A reduction in direct taxation on incomes
 - A decrease in price of the product
 - A rise in the price of a complementary product
32. If the price of cooking oil of company A falls, which one of the following outcomes would be expected to occur?
- A fall in the quantity of A's oil demanded
 - A rise in the price of B's oil
 - A fall in the demand for plastic bags
 - A fall in the demand for B's oil
33. The supply curve for sofas has moved to the right. Which of the following could have caused this shift?
- A decrease in the price of sofas
 - A decrease in the price of futons (a substitute)
 - A decrease in the cost of horsehair (a raw material used in making sofas)
 - An increase in the wage rate in the sofa industry
34. When a price floor is imposed above the market equilibrium level
- A shortage will outcome
 - A surplus will outcome
 - Scarcity will outcome
 - over production
35. Which statement most correctly describes merit goods in an economy?
- They are over produced
 - They are non-exclusive
 - They are under-provided in the free market economy
 - They are indivisible

36. Select the factor/s which force government to intervene into market for price determination:
- To protect the strong agents of an economy
 - To avoid artificial shortage of the goods
 - To increase government revenue
 - None of the above
37. A rise in price of substitutive good, will lead to rise in demand of commodity under discussion.
- True
 - False
38. The minimum price a firm is willing to receive for its goods is called_____
- Reservation price
 - Support price
 - minimum price
 - none of these
39. Price is the _____of any tangible or intangible product
- accepted value
 - monetary value
 - real value
 - regulated value
40. In case of cob-web model, price is diverging from equilibrium as supply curve is more elastic than the demand curve. ($E_s > E_d$)
- True
 - False
41. A change in demand occurs when_____ changes.
- Wage rate
 - Price of the product
 - Utilities
 - Income of the buyer
42. _____ is also known as equilibrium price.
- Reserve price
 - Regulated price
 - Support price
 - Clearing price
43. E-business enables customers to buy what, when and where they want to buy, which shifts the demand curve.
- True
 - False
44. The process of buying and selling of goods and services or exchange of information regarding business activities through digitalized systems including internet is called E-business.
- True
 - False

ANSWERS TO SELF TEST QUESTIONS

1	(b)	11	(a)	21	(b)	31	(b)	41	(d)
2	(c)	12	(b)	22	(d)	32	(d)	42	(d)
3	(b)	13	(c)	23	(b)	33	(c)	43	(a)
4	(b)	14	(b)	24	(d)	34	(b)	44	(a)
5	(d)	15	(b)	25	(c)	35	(c)		
6	(b)	16	(a)	26	(c)	36	(b)		
7	(d)	17	(a)	27	(d)	37	(a)		
8	(d)	18	(b)	28	(b)	38	(a)		
9	(c)	19	(a)	29	(d)	39	(b)		
10	(a)	20	(a)	30	(b)	40	(a)		

ELASTICITY OF DEMAND AND SUPPLY

1. Which of the following statements is true?
 - a) If the price elasticity of demand is more than 1, a fall in price will result in a fall in total expenditure on the product.
 - b) The income elasticity of demand will only be zero in the case of inferior goods.
 - c) The cross-elasticity of demand for complementary goods will always be positive.
 - d) None of these
2. The demand for a product will tend to be inelastic when:
 - a) It has very few close substitutes
 - b) It is very quickly consumed
 - c) It tends to be purchased by people on subsistence incomes
 - d) It has a wide range of different uses
3. The demand for a product will tend to be elastic when:
 - a) The product has a number of different uses.
 - b) The product is bought mainly by people on subsistence incomes.
 - c) The product has very close substitutes
 - d) The product is non-durable consumer good that is quickly consumed.
4. If the price elasticity of demand for petrol were zero, what would be the effect of an increase in taxation on petrol?
 - a) The producer would pay all the tax.
 - b) The quantity of petrol consumed would be unchanged.
 - c) Total petrol sales would fall (in quantity) by the same proportion as the increase in price caused by the tax.
 - d) In order to maintain sales volume, petrol stations would have to adopt a pricing policy whereby they absorbed some of the tax.
5. If the demand for a good is price inelastic, which one of the following statements is correct?
 - a) If the price of the good rises, the total revenue earned by the producer increases.
 - b) If the price of the good rises, the total revenue earned by the producer falls.
 - c) If the price of the good falls, the total revenue earned by the producer increases.
 - d) If the price of the good falls, the total revenue earned by the producer is unaffected.
6. Which of the following statements is incorrect?
 - a) When price elasticity of demand is 1 along the entire demand curve, total consumer expenditure on the product will be the same at all price levels.
 - b) If the quantity demanded of a product falls by 18% when its price is raised by 12%, demand is relatively price elastic.
 - c) When demand is price elastic, consumers' expenditure on a product will go up when its price is reduced.
 - d) Products which are staple goods or necessities of life have a low negative income elasticity of demand.

7. The main factor affecting price elasticity of demand is:
- Availability of substitutes
 - Availability of complements
 - Percentage change in household income
 - Existence of stocks of the good
8. When demand for a good is price elastic, a price increase will result in:
- A fall in demand but total revenue will rise
 - A fall in demand and total revenue will fall
 - A fall in demand and total revenue will remain the same
 - None of the above
9. If total revenue falls when price is reduced, then_____:
- The good in question is an inferior good
 - Cross-elasticity of demand is positive
 - Demand is switching to substitutes
 - Demand is price-inelastic
10. Supply of a good is likely to be elastic if:
- The good is imperishable
 - Barriers to entry to the industry are low
 - Unemployment is low
 - All of these
11. If the price elasticity of demand is more than 1, a fall in price will result in a fall in total expenditure on the product.
- True
 - False
12. The income elasticity of demand will only be zero in the case of inferior goods.
- True
 - False
13. The cross-elasticity of demand for complementary goods will always be positive.
- True
 - False
14. When the price rises from Rs. 40 to Rs. 50, what is the elasticity of demand?

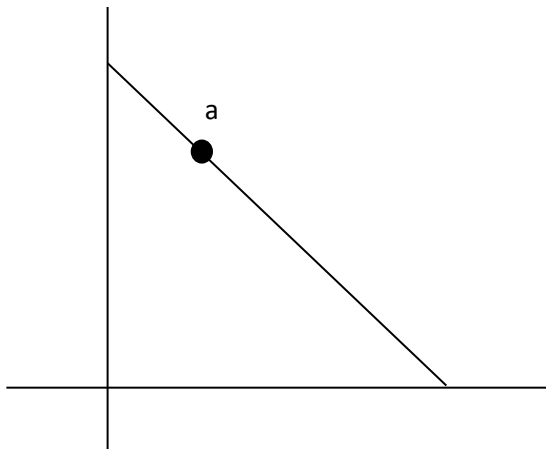
Price of good	Demand per week	Supply per week
Rs.	Units	Units
40	200	100
50	150	160
60	100	200

- a) 0
 - b) unitary elastic¹
 - c) Greater than 1
 - d) Between zero and 1
15. The graph of a supply schedule which has a price elasticity of supply equal to 1 will be:
- a) a rectangular hyperbola
 - b) any straight line drawn through the origin
 - c) straight line drawn through the origin at 90 degrees
 - d) a vertical line
16. Which of the following statements is incorrect?
- a) If cross elasticity of demand is equal to zero, the two products are neither complements nor substitutes.
 - b) Cross elasticity of demand is measured by the percentage change in the price of good X divided by the percentage change in the quantity of good Y demanded.
 - c) A high positive cross elasticity of demand means that the two products are very close substitutes.
 - d) All are incorrect
17. If total receipts of a company remain unchanged after it has put up its prices, which of the following would describe the price elasticity of demand?
- a) it is absolutely inelastic
 - b) It is elastic
 - c) It has unitary elasticity
 - d) It is inelastic
18. Which of the following statements about elasticity of supply is correct?
- a) Elasticity of supply is normally negative rather than positive
 - b) Elasticity of supply is normally greater the shorter the time period involved
 - c) Elasticity of supply depends on the alternative uses to which suppliers can put their resources.
 - d) All of above are correct
19. Good X and Good Y are two rival brands of flavoured yoghurt drinks, which have a cross elasticity of demand of +2. The price of Good X rises from Rs. 20 to Rs. 30 per carton. What will be the percentage increase in demand for similar-sized cartons of Good Y?
- a) 20%
 - b) 25%
 - c) 75%
 - d) 100%
20. Which of the following factors influence the elasticity of supply of a good?
- a) The time period over which changes in supply are measured.
 - b) The marginal cost of producing the good
 - c) The range of alternative production opportunities available to suppliers.
 - d) All of the above

21. If the price elasticity of demand for petrol were 0, what would be the effects of an increase in taxation on petrol?
- a) The consumer would pay all the tax
 - b) The quantity of petrol consumed would be changed
 - c) Total petrol sales would fall (in quantity) by the same proportion as the increase in price caused by the tax.
 - d) In order to maintain sales volume, petrol stations would have to adopt a pricing policy whereby they absorbed some of the tax.
22. When price elasticity of demand is 1 along the entire demand curve, total consumer expenditure on the product will be the same at all price levels
- a) True
 - b) False
23. If the quantity demanded of a product fall by 18% when its price is raised by 12%, demand is relatively price elastic
- a) True
 - b) False
24. When demand is price elastic, consumer's expenditure on a product will go up when its price is reduced
- a) True
 - b) False
25. Products which are staple goods or necessities of life have a low negative income elasticity of demand.
- a) True
 - b) False
26. A manufacturer of power drills was charging Rs. 26 for a drill, and demand was 1,800 drills per week. He then raised the price to Rs.30, and demand went down by 300 drills per week. What is the arc elasticity of demand between the prices of Rs. 26 and Rs. 30?
- a) -0.79
 - b) -1.08
 - c) -1.25
 - d) -1.27
27. Annual demand for good A is 10 million units at Rs. 2.50 each and 8 million at Rs. 33.50 each. Its elasticity of demand is:
- a) Elastic
 - b) Inelastic
 - c) Unitary
 - d) Perfect Elastic
28. When demand is price elastic, consumer's expenditure on a product will go up when its price is reduced
- a) True
 - b) False

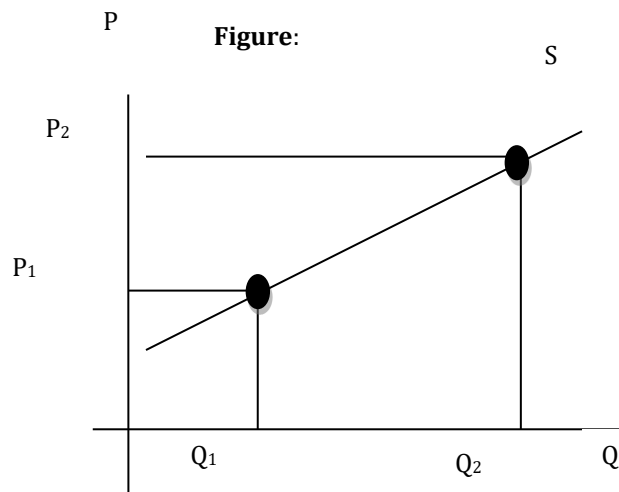
29. A supply curve with unit elasticity along all of its length is a straight line through the origin.
 - a) True
 - b) False
30. If the income elasticity of demand is greater than 1, the commodity is
 - a) A necessity
 - b) A luxury
 - c) An inferior good
 - d) An independent good
31. If the amounts of two commodities purchased both increase or decrease when the price of one commodity changes, the cross elasticity of demand between them is
 - a) Negative
 - b) Positive
 - c) Zero
 - d) One
32. Elasticity of supply for a positively sloped straight-line supply curve that intersects the price axis is
 - a) Equal to zero
 - b) Equal to one
 - c) Greater than one
 - d) Less than one
33. Which of the following elasticity measures a movement along a curve rather than a shift in the curve?
 - a) The cross elasticity of demand
 - b) The income elasticity of demand
 - c) The price elasticity of demand
 - d) None of the above
34. In case of superior good, the income elasticity of demand is
 - a) Positive
 - b) Unitary
 - c) Negative
 - d) Zero
35. In case of the two commodities are substitutes, cross elasticity of demand will be
 - a) Positive
 - b) Negative
 - c) Unitary
 - d) Zero
36. Sales of Good T are currently 10,000 per year, and income elasticity of demand for Good T is + 1.5. If household incomes rise by 4%, what will be the new annual sales of Good T _____?
 - a) 10,600
 - b) 10,400
 - c) 9,600
 - d) 9,400

37. Sales of Good Y have increased from 20,000 to 23,000 following a rise in the price of Good Z from Rs. 5 to Rs. 6. What is the cross elasticity of demand for Good Y?
- a) - 0.75
 - b) + 0.5
 - c) + 0.75
 - d) +1.5
38. Sales of Good E have increased from 250,000 to 255,000 following a reduction in the price of good F from Rs. 10 to Rs. 9.50. Which one of the following statements most accurately describes the relationship between Goods E & F are _____?
- a) Goods E & F are close complements
 - b) Goods E & F are close substitutes
 - c) Neutral Goods
 - d) Unrelated Goods
39. An increase in quantity demanded caused no change in the equilibrium price. Thus, demand curve must be:
- a) Perfectly inelastic
 - b) Unitary elastic
 - c) Elastic
 - d) Perfectly elastic
40. Using following diagram at point a demand for product is:



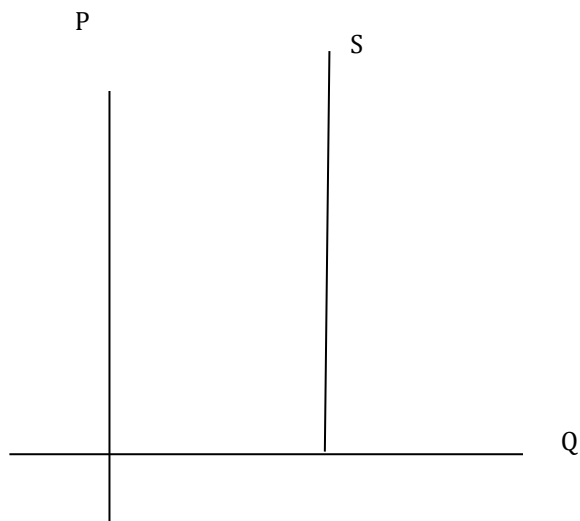
- a) Relatively elastic
 - b) Relatively less elastic
 - c) Gradient will be greater than one
 - d) Gradient will be smaller than one
- i. a and c are correct
 - ii. b and c are correct

41. In following diagram supply curve shows:



- a) Relatively elastic
- b) Relatively inelastic
- c) Perfectly elastic
- d) Perfectly inelastic

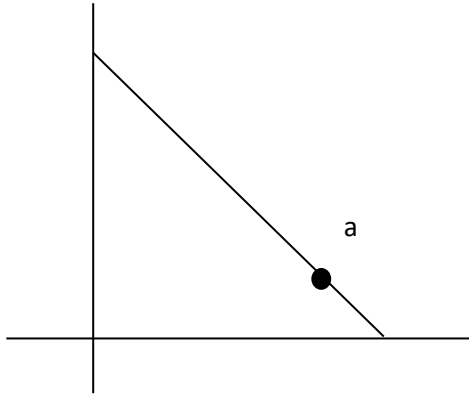
42. Given diagram shows:



- a) Inelastic supply curve
- b) Perfectly inelastic supply curve
- c) Perfectly elastic supply curve
- d) Elastic supply

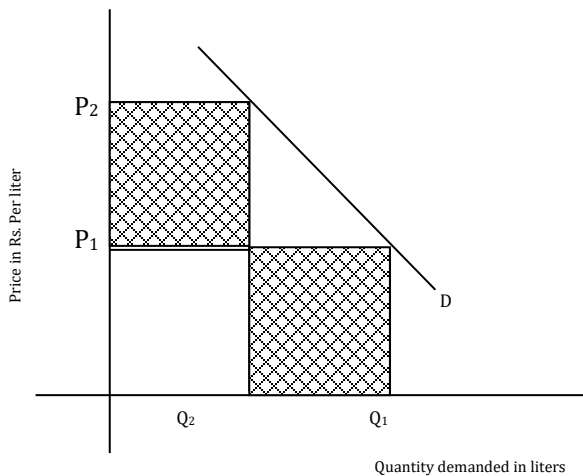
43. In *short period* of time, although the plant capacity is fixed, with little alterations in techniques of production or with more efficient use of resources, supply can be adjusted up to a little extent, and supply is therefore:
- Relatively elastic
 - relatively *inelastic*.
 - Perfectly elastic
 - Unitary elastic.
44. A business currently sells 20,000 units of its product per month, at a price of Rs. 10 per unit. The product has a price elasticity of -0.8 . If price rise by 5% then _____
- New price will be Rs 15
 - New sales will be 19200 units
 - New sales will be 22000 units
 - Total revenue from the product will increase by 40,000
45. When quantity demanded increases 5% due to decrease in prices by 10%. The price elasticity of demand for laptop is _____ and total revenue from laptop sales will _____.
- Elastic; decrease
 - Elastic; increase
 - Inelastic; increase
 - Unit elastic; not change
46. Price elasticity of demand is calculated as the change in price divided by the change in quantity demanded.
- True
 - False
47. A shopkeeper sells 24 pens at a price of Rs.20 per day. At a price of Rs.18 he sells 33 pens a day. Since total revenue is _____ by the price decrease, demand must be _____.
- Increased; elastic
 - Increased; inelastic
 - Increased; unit elastic
 - Decreased; elastic
48. A demand curve with constant slope over all quantity values can have a continuously changing price elasticity of demand.
- True
 - False
49. Alif College wanted to increase revenues. They decided to raise fees paid by students with Bachelor's degrees to Rs.50 per unit because they believed this would result in greater revenues. But in reality, total revenues fell. Therefore, the demand for Alif College courses by people with Bachelor's degrees must have actually been_____:
- Relatively inelastic
 - Unit elastic
 - Relatively elastic
 - Perfectly elastic

50. In given demand curve at point a, any increase in price of the product will _____ the total expenditures.



- a) Increase
- b) Decrease
- c) Remain unchanged
- d) Insufficient information

51. Following diagram showing result of change in price and quantity demanded for a product which shows _____.



- a) Relatively elastic demand
- b) Relatively less elastic demand
- c) Unitary elastic demand
- d) Perfectly inelastic demand

ANSWERS TO SELF TEST QUESTIONS

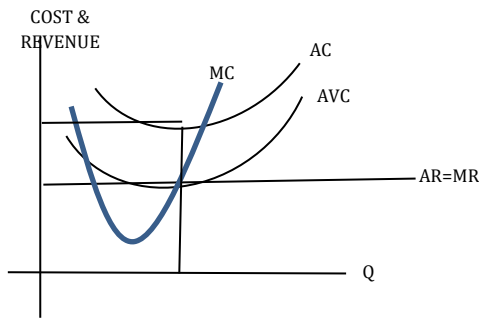
1	(a)	11	(b)	21	(a)	31	(a)	41	(a)	51	(c)
2	(a)	12	(b)	22	(a)	32	(c)	42	(b)		
3	(c)	13	(b)	23	(a)	33	(c)	43	(b)		
4	(b)	14	(c)	24	(a)	34	(a)	44	(b)		
5	(a)	15	(b)	25	(b)	35	(a)	45	(c)		
6	(d)	16	(b)	26	(d)	36	(a)	46	(b)		
7	(a)	17	(c)	27	(b)	37	(c)	47	(a)		
8	(b)	18	(c)	28	(a)	38	(a)	48	(a)		
9	(d)	19	(d)	29	(a)	39	(d)	49	(c)		
10	(d)	20	(d)	30	(b)	40	(i)	50	(a)		

FIRM THEORY

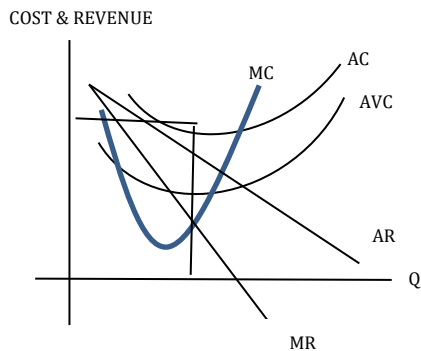
1. Suppose that you purchased a ticket to a ICAP festival for Rs.100 from an online ticket broker. Once you arrived at the festival, you discovered that parking costs you an additional Rs.10. In this situation, the additional Rs.10 you pay for parking is an example of
 - a) An economic loss.
 - b) Opportunity cost.
 - c) Marginal cost.
 - d) An inefficient cost.
2. You have decided that you want to attend a costume party as Iron Man. You estimate that it will cost Rs 40 to assemble your costume. After spending Rs 40 on the costume, you realize that the additional pieces you need will cost you Rs 25 more. The marginal cost of completing the costume is
 - a) Rs 15.
 - b) Rs 25.
 - c) Rs 40.
 - d) Rs 65.
3. If you can buy 9 DVDs for Rs 126 or you could buy 10 DVDs for Rs 130, then the marginal cost of the tenth DVD is
 - a) Rs 4.
 - b) Rs 13.
 - c) Rs 14.
 - d) Rs 130
4. If you can download 10 ring tones for your cell phone for Rs 10 or you could download 11 ring tones for your cell phone for Rs 10.50, then the marginal cost of the eleventh ring tone is
 - a) Rs 0.50
 - b) Rs 10.00
 - c) Rs 10.50
 - d) Rs 20.50
5. Which of the following best describes the law of diminishing returns? As more labour is added to a fixed amount of capital:
 - a) Total output will decline
 - b) Increase in total output will become smaller for each additional unit of labour employed
 - c) Marginal product will rise
 - d) Production costs will rise because higher wages will have to be paid to attract more labour
6. Which one of the following is not a source of economies of scale?
 - a) The introduction of specialist capital equipment
 - b) Bulk buying
 - c) The employment of specialist managers
 - d) None of these.

7. All of the following are characteristics of a market displaying perfect competition except which one?
- The product is homogeneous but differentiated by advertising.
 - There are no information gathering costs.
 - Producers act rationally.
 - There is a large number of sellers in the market.

8. Following diagram depicts:



- Super profit of a firm under monopoly
 - Normal profit of a firm under perfect competition
 - Shut down condition of firm under perfect competition
 - Wait and watch condition for a firm under perfect competition
9. Following diagram depicts:



- Firms normal profit under monopoly
 - Firm normal loss under monopoly
 - Firm super profit under monopoly
 - None of the above
10. Oligopoly markets typically do not display price competition because:
- Barriers to entry exist
 - Products are clearly differentiated
 - Producers' decisions are interdependent
 - There is always a price leader

11. An individual firm in long term equilibrium in a perfect competitive market will produce at a level where:
 - a) A Marginal cost exceeds average cost
 - b) Marginal cost is less than average cost
 - c) Marginal cost and average cost are equal
 - d) Marginal revenue is greater than average revenue
12. Which of the following arguments could not be used to support the existence of monopolies?
 - a) Monopolies can achieve maximum economies of scale.
 - b) Monopolists can practice price discrimination.
 - c) Monopolies can finance more new projects out of profits.
 - d) Monopolies invest in long term projects.
13. A monopolist's average revenue curve always slopes downwards because:
 - a) Economies of scale exist in distribution
 - b) There are allocative inefficiencies
 - c) Market demand increases as price falls
 - d) Marginal revenue can be negative
14. The long-run average cost curve for a business will eventually rise because of:
 - a) The law of diminishing returns
 - b) Increasing competition in the industry
 - c) Limits to the size of the market for the good
 - d) Diseconomies of scale
15. In a perfectly competitive market, all producers charge the same price because:
 - a) They are all profit maximisers
 - b) They have the same costs
 - c) The product is homogeneous
 - d) All firms are small
16. In conditions of perfect competition, the demand curve for the product of a firm:
 - a) Is identical to the firm's marginal revenue curve
 - b) Intersects the firm's marginal revenue curve at the point where $MC = MR$
 - c) Intersects the firm's average cost
 - d) Is perfectly inelastic
17. According to the traditional theory of the firm, the equilibrium position for all firms will be where:
 - a) Profits are maximised
 - b) Output is maximised
 - c) Revenue is maximised
 - d) Costs are minimized

18. The law of diminishing returns can apply to a business only when:
- All factors of production can be varied.
 - At least one factor of production is fixed.
 - All factors of production are fixed.
 - Capital used in production is fixed.
19. Adil & Co employs 30 men in his factory which manufactures sweets. He pays them Rs.5 per hour and they all work maximum hours. To employ one more worker he would have to raise the wage rate to Rs. 5.50 per worker hour. If all other costs remain constant, the marginal cost per hour of labour is now:
- Rs. 20.50
 - Rs. 15.00
 - Rs. 5.50
 - Rs. 0.50
20. In economics, what is the normal profit per unit of a product?
- The difference between its average revenue and average cost
 - The difference between its marginal revenue and marginal cost
 - An element in the cost of producing the product
 - None of these
21. Which of the following statements best describes long run equilibrium in a market where there is monopolistic competition?
- Marginal revenue equals average cost.
 - There is excess capacity in the industry since firms could reduce average costs by expanding output.
 - Firms will earn supernormal profits because price exceeds marginal cost.
 - Price equals marginal cost, but does not equal average cost.
22. Where $MR = 0$, there the firm's total revenue is maximum and demand is unitary elastic.
- True
 - False
23. Which one of the following statements about price discrimination is Incorrect?
- Dumping is not a form of price discrimination.
 - For price discrimination to be possible, the seller must be able to control the supply of the product
 - Price discrimination is only profitable where the elasticity of demand is different in at least two of the markets.
 - An example of price discrimination is the sale of first class and second class tickets on an aero plane journey
24. Slope of total cost = slope of total revenue is enough condition for profit maximization for a firm.
- True
 - False

25. The conditions necessary for a successful policy of price discrimination by a company include which of the following?
 - a) There are at least four separate markets
 - b) Marginal costs are different in each market
 - c) The price elasticities of demand are different in each market
 - d) The price elasticities of demand are the same in each market
26. Shut down conditions of a firm under perfect competition in short run are:
 - a) $P=ATC$
 - b) $P < AVC$
 - c) $AR = AVC$
 - d) $AR < AVC$
 - i. Only a is correct
 - ii. Options a and c are correct
 - iii. Options b and d are correct
 - iv. Only d is correct
27. Explicit cost = Total cost – opportunity cost.
 - a) True
 - b) False
28. Suppose that all inputs are increased by 50%, and as a result, total output increases by 30%. This would be an illustration of which of the following?
 - a) The law of variable proportions
 - b) Decreasing returns to scale
 - c) A declining long run average cost curve
 - d) None of these
29. In 3rd stage of law of variable proportions MP is positive
 - a) True
 - b) False
30. Which one of the following would be a variable cost to a firm?
 - a) Mortgage payments on the factory
 - b) The cost of raw materials
 - c) Depreciation of machines
 - d) Interest on debentures
31. Which one of the following would not act as a barrier to the entry of new firms into an industry?
 - a) Perfect consumer knowledge
 - b) Economies of scale
 - c) High fixed costs of production
 - d) Brand loyalty

32. The purpose of a cartel is to _____:
- a) Rationalise production
 - b) Reduce consumer uncertainty
 - c) Standardise product quality
 - d) Ensure that a dominant group of producers charge the same price
33. The law of diminishing marginal returns states that:
- a) As more factors of production are employed, output will rise initially and then fall
 - b) As more factors of production are employed, output will rise, but at a diminishing rate
 - c) As more variable factors of production are added to a fixed factor, output will rise at a faster rate initially and then fall
 - d) As more variable factors of production are added to a fixed factor, output will rise at a decreasing rate after a certain point.
34. Which of the following statements is correct?
- a) MC will equal ATC when ATC is at its minimum amount, but will not equal AVC when AVC is at its minimum.
 - b) MC will equal AVC when AVC is at its minimum amount, but will not equal ATC when ATC is at its minimum.
 - c) MC will equal ATC when ATC is at its minimum amount and AVC when AVC is at its minimum, which is at the same output level.
 - d) MC will equal ATC when ATC is at its minimum amount and AVC when AVC is at its minimum, but this will occur at different output levels.
35. Which of the following statement is correct?
- a) When average cost is constant, the marginal cost must be falling
 - b) When average cost is rising, the marginal cost is lower than the average cost
 - c) When average cost is rising, the marginal cost is higher than the average cost
36. As its output increases, a firm's short-run marginal cost will eventually increase because of:
- a) Diseconomies of scale
 - b) A lower product price
 - c) The firm's need to break even
 - d) Diminishing returns
37. Marginal Revenue is greater than zero if:
- a) The elasticity of demand is greater than one
 - b) The elasticity of demand is less than one
 - c) The elasticity of demand is one
 - d) None of the above

38. Following data has been provided to the Chief Executive Officer of a monopoly firm:

Marginal revenue Rs. 10 Marginal cost Rs. 11

Average revenue Rs. 16 Average cost Rs. 12

To maximize profit the firm should:

- a) Reduce price and increase output
- b) Reduce price and reduce output
- c) Increase price and increase output
- d) Increase price and reduce output

39. In perfect competition $AR = MR$ because:

- a) Each additional units of output producing higher revenue
- b) Each additional unit of output is generating same revenue
- c) Firms are price makers
- d) None of these

40. By substituting TR equation into AR equation, we observe AR is equal to:

- a) Quantity
- b) Price
- c) MC
- d) AC

41. AVC become U-shape, when output increases beyond a normal capacity level due to:

- a) Down pressure of AFC is out weighted
- b) Law of diminishing returns
- c) Average total cost is also U-shape
- d) All of these

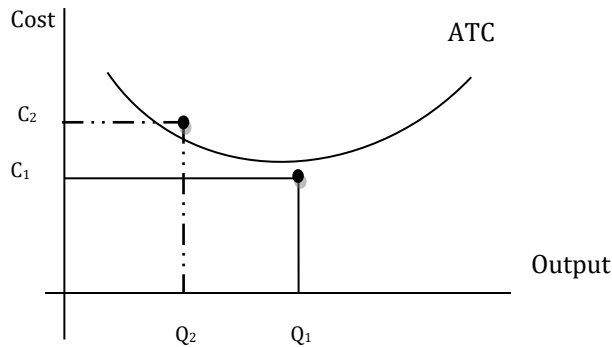
42. Due to changing productivity proportion of Factors of production total cost curve will be:

- a) 45 degrees straight curve
- b) L-shape curve
- c) Inverted S-shape
- d) U-shape

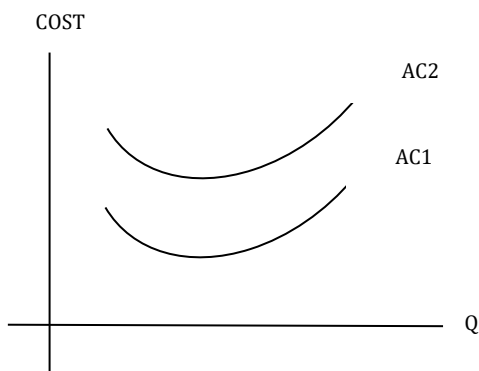
43. Which of the following _____ is NOT a characteristic of oligopoly?

- a) Mutual dependence
- b) Growth through merger
- c) Large number of firms
- d) Non-price competition

44. Given diagram depicts the concept of X-inefficiency of a state-owned enterprise.



- a) True
 - b) False
45. Total revenue for a firm with a downward sloping demand curve, will be maximised when
- a) Marginal cost = marginal revenue
 - b) Marginal cost = average revenue
 - c) Average cost = average revenue
 - d) Marginal revenue is zero
46. Collusion in oligopolistic markets will lead to
- a) Firms setting price where industry marginal revenue is equal to marginal costs and supernormal profits being earned
 - b) Firms setting price where industry marginal revenue is equal to marginal costs, and normal profits being earned
 - c) Firms setting price equal to average total cost, and supernormal profits being earned
 - d) Firms setting price equal to average total cost, and normal profits being earned
47. Diagram shows:



- a) Productive efficiency
- b) X-inefficiency
- c) Productive inefficiency
- d) Allocative efficiency

ANSWERS TO SELF TEST QUESTIONS

1	(c)	11	(c)	21	(b)	31	(a)	41	(d)
2	(b)	12	(b)	22	(a)	32	(d)	42	(c)
3	(a)	13	(c)	23	(a)	33	(d)	43	(c)
4	(a)	14	(d)	24	(b)	34	(d)	44	(b)
5	(b)	15	(c)	25	(c)	35	(c)	45	(d)
6	(d)	16	(a)	26	(iii)	36	(d)	46	(a)
7	(a)	17	(a)	27	(a)	37	(a)	47	(b)
8	(d)	18	(b)	28	(b)	38	(d)		
9	(b)	19	(a)	29	(b)	39	(b)		
10	(c)	20	(c)	30	(b)	40	(b)		

NATIONAL INCOME AND ITS DETERMINATION

1. Which of the following is not a leakage from the circular flow of income?
 - a) corporation tax
 - b) expenditure on foreign goods
 - c) personal saving
 - d) retirement pensions
2. During a year, a country's national income in money terms increased by 6%, prices increased by 4% and total population increased by 2%.

What is the approximate change in real per capita income?

- a) decrease of 2%
 - b) no change
 - c) an increase of 2%
 - d) an increase of 4%
3. Which of the following will directly result in an increase in China's Gross National Product?
 - a) increased wages earned in a Malaysian-owned factory in China
 - b) increased imports of goods and services
 - c) increased outflows of net property income
 - d) increased taxes on domestic expenditure
4. A country's GDP declines but the welfare of its population rises. What could explain this?
 - a) a fall in leisure time
 - b) a fall in the size of the subsistence sector
 - c) a rise in positive externalities
 - d) a rise in the size of the population
5. The information in the table is taken from a country's national income accounts.

	Rs million
National income	500
Consumer spending	200
Investment spending	75
Government spending	150
Taxation	140
Exports	125

What is the value of imports?

- a) Rs125 million
- b) Rs75 million
- c) Rs50 million
- d) Rs25 million

6. A government uses real personal disposable income as a measure of the standard of living.

What does this measure not take into account?

- a) the distribution of income
- b) the level of national income
- c) the size of the population
- d) the average price level

7. What is likely to increase GDP per worker in a developing economy?

- a) a decrease in the numbers engaged in subsistence agriculture
- b) a decrease in the numbers engaged in manufacturing
- c) an increase in the employment rate
- d) an increase in the population of working age

8. What is most likely to lead in the long run to an increase in world real GDP per head?

- a) faster population growth
- b) trade liberalization
- c) a lower propensity to save
- d) faster growth of the money supply

9. What is likely to be the effect of an oil price increase on the global economy?

- a) a strengthening of demand inflation
- b) a weakening of cost inflation
- c) a decrease in the rate of growth
- d) a decrease in unemployment

10. The information in the table is taken from a country's national income accounts.

	Rs million
National income	600
Consumer spending	400
Investment spending	80
Government spending on goods and services	100
Taxation	90
Imports	120

What is the value of exports?

- a) Rs100 million
- b) Rs120 million
- c) Rs140 million
- d) Rs230 million

11. What is not a leakage from the circular flow of income?

- a) expenditure on foreign goods
- b) indirect taxes
- c) undistributed profits
- d) unemployment benefits

12. Which is likely to cause a decrease in aggregate supply?

- a) a decrease in consumption expenditure
- b) an increase in labor productivity
- c) a decrease in rates of unemployment benefit
- d) an increase in wage costs per unit of output

13. Over a given period, money income in an economy increased by 8%. Over the same period, prices rose on average by 6%.

What can be deduced from this?

- a) Real income decreased by 2%.
- b) The income velocity of circulation decreased by 2%.
- c) The money supply increased by 14%.
- d) The volume of output increased by 2%.

14. If there is reduction in government spending, there will not necessarily be a fall in National income if there is an increase in

- 1. exports
 - 2. taxation
 - 3. Investment
- a) 1 and 2
 - b) 1 and 3
 - c) 2 and 3
 - d) All of 1, 2 and 3

15. Which one of the following items is most likely to increase the circular flow of income?

- a) Increased taxation
- b) Increased spending on imports
- c) Lower government spending
- d) Reductions in personal savings

16. Which of the following may cause an increase in National Income?
- A fall in investment
 - A rise in exports
 - An increase in saving
 - A fall in consumer spending
17. Which of the following would not give the value of the Pakistan's Gross National Product?
- Gross National Expenditure minus exports
 - Gross Domestic Product plus net property income from abroad
 - Total factor incomes earned by Pakistani residents
 - Net National Income plus depreciation
18. Net National Product at factor cost
- +Capital consumption
 - +Indirect taxes on expenditure
 - Subsidies
- Equals**
- Gross National Product at market prices
 - Gross National Product at factor cost
 - Gross Domestic Product at market prices
 - Gross Domestic Product at factor cost
19. Calculate the following with given data set:
- Gross National Product at factor cost
 - Gross National Product at market prices
 - National Income at factor cost

	Rs Million
Consumers' expenditure	2,500
General government final consumption	800
Gross domestic fixed capital formation	750
Value of physical increase in stocks	0
Exports of goods and services	1,200
Imports of goods and services	1,000
Taxes on expenditure	650
Subsidies	100
Net property income from abroad	40
Capital consumption	450

- a) Gross National Product at factor cost in this economy is
 - i. Rs 3,700 million
 - ii. Rs 3,740 million
 - iii. Rs 4,290 million
 - iv. Rs 4,840 million
 - b) Gross National Product at market prices in this economy is
 - i. Rs 4,050 million
 - ii. Rs 4,090 million
 - iii. Rs 4,250 million
 - iv. Rs 4,290 million
 - c) National Income at factor cost in this economy is
 - i. Rs 3,290 million
 - ii. Rs 3,740 million
 - iii. Rs 3,800 million
 - iv. Rs 3,840 million
20. Which of the following items is not included in the calculation of Gross National Product at factor cost?
- a) the cost of building new government offices
 - b) value added tax on business services
 - c) dividends received from shares in a company abroad
 - d) Imputed rent of owner-occupied houses
21. An individual earns Rs 30,000 in a year. Of this Rs 8,000 is tax free. The rate of income tax is 25 Ps in Re1. The individual's personal disposable income for the year is:
- a) Rs 22,000
 - b) Rs 22,500
 - c) Rs 24,500
 - d) Rs 30,000
22. Which of the following cannot be termed as 'transfer payment' for the purpose of National Income accounting?
- a) Interest paid to holders of government stock
 - b) Salaries paid to Members of Parliament
 - c) Payments of state pensions
 - d) Social security payments
23. Which of the following Investments creates an injection into the circular flow of income?
- a) An Increase by a firm in its stocks of finished goods, prior to a marketing campaign
 - b) The purchase by a pension fund of shares in a newly-privatized company
 - c) The purchase of a second-hand piece of farming machinery with their savings by a farming co-operative group
 - d) The takeover of one company by another company

24. In order to measure whether there has been a change in the standard of living of people in a country over a period of years, it would be necessary to obtain relevant statistics for
- National Income, population, retail price Index
 - National product, balance of payments, retail price index
 - National Income, investment, working population
 - Industrial output, working population, balance of payments
25. If there is a reduction in government spending, there will not necessarily be a fall in National Income if there is an increase in:
- Savings
 - Taxation
 - Investment
 - Imports
26. Which of the following cannot be termed a 'transfer payment' for the purpose of National Income accounting?
- Amount given on health cards
 - Salaries paid to private sector employees
 - Payments of state pensions
 - Social security payments
27. Which of the following investments do not create an injection into the circular flow of income?
- The takeover of one company by another company
 - The purchase by a pension fund of shares in a newly privatized company
 - The purchase of a second-hand piece of farming machinery with their savings by a farming co-operative group
 - All of above
28. Which one of the following items is not included in the calculation of Gross National Product at factor cost?
- The cost of building new government offices
 - Tax on consumption
 - Dividends received from shares in a company abroad
 - Imputed rent of owner-occupied houses
29. Insert the missing term in the equation below.
- $GNP - GDP = \underline{\hspace{2cm}}$
30. Withdrawals from the circular flow consist of savings, taxations and imports.
- True
 - False
31. Which of the following would not be counted in 2023's GDP?
- The value of a 2018 boat you purchase from a boat dealer in 2023
 - The 2023 salary of a used motorcycle salesperson
 - The commissions earned by a real estate agent in selling condominiums built prior to 2023
 - The value of a refrigerator manufactured in 2023 but not sold in 2023

32. If no foreign companies produce in a country, but many of the country's companies produce abroad, then
- The country's GNP will tend to exceed its GDP.
 - The country's GDP will tend to exceed its GNP.
 - The country's GNP and GDP will tend to be equal.
 - The country's GDP will tend to be equal to its domestic income.
33. _____ method of computing national income helps us to avoid double counting of any value.
- Value added
 - Product approach
 - Income approach
 - Expenditure approach
34. The value of what KFC produces in Pakistan is included in the U.S _____ and in Pakistan _____.
- GDP; GDP
 - GNP; GNP
 - GNP; GDP
 - GDP; GNP
35. Double counting can be avoided by using the value-added approach when calculating GDP.
- True
 - False
36. _____ is an integral part of aggregate expenditure.
- Spending by government
 - Spending by households
 - Spending by firms
 - All of the above
37. _____ is the hurdle while calculating national income in Pakistan.
- Illegal activities
 - Barter Transactions
 - Undocumented economy
 - All of the above
38. _____ the main reason behind calculating national income of a country.
- Economic planning
 - Measuring living standards
 - Comparing economic growth of various countries
 - All of above
39. Following is Macroeconomic objective
- Economic growth
 - Control inflation & unemployment
 - Equilibrium in balance of payments
 - All of above

40. National income at factor cost is defined as
- GNP at market price
 - GDP at market price
 - NNP at factor cost
 - Personal disposable income
41. The circular flow of income for a two-sector model shows
- The flow of income between the household and business sectors
 - The amount of money held by the household and business sectors
 - Whether the household sector is satisfied with the output of the business sector
 - Whether the business sector is satisfied with the spending of the household sector
42. If GNP rose from Rs100 million to Rs150 million and price rose by 50% over this period
- Real GNP fell by 100%
 - Real GNP fell by 50%
 - Real GNP stayed the same
 - Real GNP rose by 50%
43. A country has a GDP at factor cost of Rs.150 m. Government expenditure was Rs.25 m, subsidies were Rs.10 m and taxes were Rs.17 m. What is its GDP at market prices?
- Rs.143 m
 - Rs.157 m
 - Rs.168 m
 - Rs.182 m
44. Which of the following is NOT an item of public consumption?
- Expenditure on health
 - Expenditure on education
 - Expenditure on general administration
 - Expenditure as transfer payments
45. Depreciation is also called capital consumption.
- True
 - False
46. $\text{Real GDP} = \text{Nominal GDP} / \text{Current GDP} \times 100$
- True
 - False
47. Which of the following represents a withdrawal from the circular flow of national income?
- A rise in consumption
 - A deficit on the balance of trade
 - A surplus on the balance of trade
 - A rise in public investment

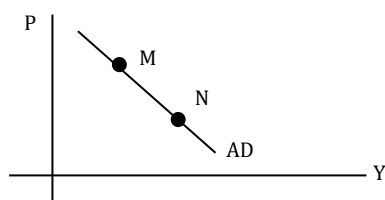
48. If depreciation equals zero and retained earnings equal Rs.25 billion, then

- a) GNP is less than net national product by Rs.25 billion.
- b) GNP equals net national product.
- c) Net national product is less than GNP by Rs.25 billion.
- d) GNP is greater than GDP by Rs.25 billion.

49. Real GDP = _____ x 100

- a) Nominal GDP/ Current GDP
- b) Real GDP/ Nominal GDP
- c) Nominal GDP/ GDP deflator
- d) Real GDP/ Inflation

50. Basic reason behind movement from M to N is:



- a) a reduction in the real value of money balances
- b) a reduction in interest rates
- c) domestic deflation
- d) the expectation of further price falls

51. One of the reasons why a country's aggregate demand curve slopes downwards is that a fall in the average price level

- a) leads to an increase in interest rates
- b) reduces the real value of money balances
- c) makes the country's goods cheaper relative to foreign goods
- d) leads to the expectation of further price falls

52. Workers in poor countries are often less productive than workers using the same technology in rich countries. What would be most likely to remedy this situation?

- a) an increase in the saving ratio in poor countries
- b) increased investment in education in poor countries
- c) increased freedom of migration from poor countries to rich countries
- d) the removal of trade barriers imposed by rich countries on imports from poor countries

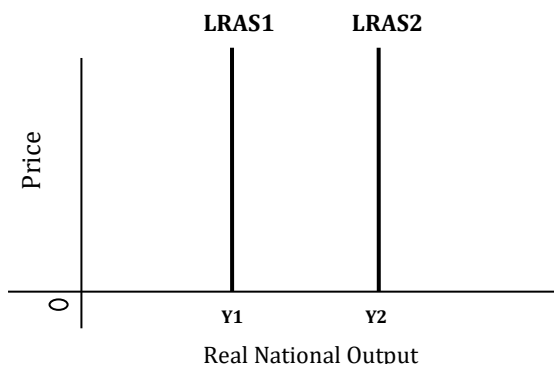
53. In an economy, the marginal propensity to consume of the unemployed is higher than the taxpayers.

The government increases both expenditure on unemployment benefits and taxation by Rs 10 million.

What will be the impact on aggregate demand?

- a) It will be unchanged.
- b) It will increase by less than Rs 10 million.
- c) It will increase by Rs 10 million
- d) It will decrease by Rs 10 million

54. According to monetarist theory, what will be the short-run effect of an unexpected increase money supply?
- an appreciation of the foreign exchange rate
 - an increase in employment
 - an increase in real wages
 - an increase in the rate of interest
55. What is likely to cause a decrease in aggregate supply?
- a decrease in consumption expenditure
 - an increase in labor productivity
 - a decrease in rates of unemployment benefit
 - an increase in wage costs per unit output
56. What is held constant when drawing an AD curve?
- the exchange rate
 - the money supply
 - the rate of interest
 - the general price level
57. which one is NOT a reason for shifting of LRAS1 TO LRAS2:



- Improvement in labour skills.
 - Improvement in technology.
 - Exploring new natural resources
 - Increase in wage rate
58. In a closed economy with no government, consumption is three-quarters of income at all levels of income.
The present equilibrium level of income is Rs 220 million.
The full employment level of income is Rs 240 million.
By how much would investment have to increase to reach full employment?
- Rs 5 million
 - Rs 15 million
 - Rs 20 million
 - Rs 30 million

59. Which of the following is an appropriate government policy for closing a deflationary gap?

- a) an increase in the rate of interest
- b) an open market sale of bonds
- c) an increase in government spending
- d) an increase in income tax

60. An aggregate demand curve slopes downwards from left to right.

One reason for this is that a reduction in the average price level will lead to

- a) an increase in the real value of money balances
- b) an increase in interest rates
- c) a decline in the country's international competitiveness
- d) the expectation of further price falls

61. Which government policy will increase aggregate demand?

- a) raising indirect taxation
- b) reducing the budget surplus
- c) removing import quotas
- d) removing subsidies

62. What would explain why an economy's short-run aggregate supply curve is upward sloping?

- a) an increasing price level
- b) Increase in money wages
- c) diseconomies of scale
- d) economies of scale

63. The national income is initially in equilibrium.

If there were a decrease in exports, which change of equivalent value would restore national income to its initial equilibrium level?

- a) an increase in investment
- b) an increase in saving
- c) a reduction in government expenditure on goods and services
- d) an increase in taxation

64. In a closed economy with no government $C = 30 + 0.8 Y$ and $I = 50$, where C is consumption, Y is income and I is investment.

What is the equilibrium level of income?

- a) 64
- b) 80
- c) 250
- d) 400

65. Over a given period, the nominal value of a country's national income increased by 10% and the average price level increased by 20%.

What can be deduced from this information?

- a) The country's money supply increased by 10%.
 - b) There was an increase in the income velocity of circulation.
 - c) There was a reduction in the demand for money.
 - d) There was a reduction in the volume of output.
66. During a year, a country's national income in money terms increased by 8%, prices increased by 4% and total population increased by 2%.

What was the approximate change in real income per head?

- a) a decrease of 2%
 - b) nil
 - c) an increase of 2%
 - d) an increase of 4%
67. In closed economy, the full employment level of income is Rs 200 million.

$$C = \frac{3}{4} Y$$

$$I = \text{Rs } (50 - 5r) \text{ million}$$

Where C = Consumption

Y = Income

I = Investment

r = Rate of interest

If planned government expenditure is Rs 30 million, what rate of interest would be required for there to be full employment?

- a) 2% per annum
 - b) 4% per annum
 - c) 6% per annum
 - d) 8% per annum
68. In a closed economy with no government sector, $C = 30 + 0.7 Y$, where C is consumption and Y is income.

The equilibrium level of income is 300. What is the level of investment?

- a) 60
- b) 100
- c) 210
- d) 270

69. When national income equals Rs 40000 million and government spending equals Rs 15000 million, an economy is in equilibrium below full employment. Out of every increase of Rs 100 in national income, Rs 15 is taken in taxes, Rs 30 is spent on imports and Rs 5 is saved.

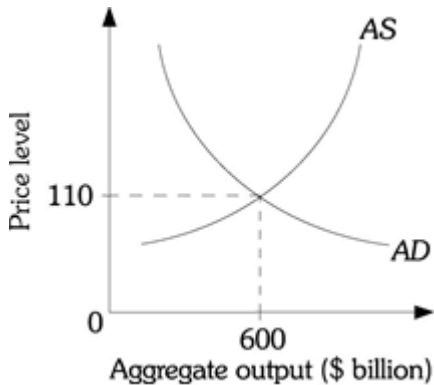
To raise national income to the full employment level of Rs 50000 million, to which level will the government need to raise its own spending?

- a) Rs 15500 million
 - b) Rs 20000 million
 - c) Rs 25000 million
 - d) Rs 35000 million
70. What will cause the long run aggregate supply curve to shift from outwards?
- a) an increase in consumer spending
 - b) an increase in inflation
 - c) an increase in productivity
 - d) an increase in net exports
71. What helps to explain why the aggregate demand curve is downward sloping?
- a) When exports increase there will be an increase in national income.
 - b) When government expenditure increases there will be an increase in national output
 - c) When investment increases there will be an increase in consumption.
 - d) When the price level increases there will be a decrease in demand.
72. What is likely to cause the aggregate supply curve to shift to the left?
- a) improvements in technology
 - b) schemes to increase the geographical mobility of labor
 - c) an increase in investment due to a reduction in interest rates
 - d) an increase in the marginal rate of income tax
73. Which one of the following would cause a fall in the level of aggregate demand in an economy?
- a) A decrease in the level of imports
 - b) A fall in the propensity to save
 - c) A decrease in government expenditure
 - d) A decrease in the level of income tax
74. The marginal propensity to consume measures
- a) The relationship between changes in consumption and changes in consumer utility
 - b) The proportion of household incomes spent on consumer goods
 - c) The proportion of total national Income spent on consumer goods
 - d) The relationship between changes in consumption and changes in income
75. An inflationary gap in the economy could be closed by an increase in the:
- a) Accelerator and multiplier
 - b) Government's budget surplus
 - c) Average propensity to consume
 - d) Country's export surplus

76. A redistribution of income from rich to poor households is likely to lead to an increase in aggregate demand.
- True
 - False
77. Which one of the following is most likely to lead to a rise in aggregate demand?
- Decrease in government expenditure
 - Decrease in income tax rate
 - Increase in autonomous savings
 - Increase in rate of interest
78. When equilibrium GNP is too small, we have
- A deflationary gap
 - A depression
 - An inflationary gap
 - None of the above
79. There is an inflationary gap when
- Equilibrium GNP is equal to full employment GNP
 - Equilibrium GNP is smaller than full employment GNP
 - Equilibrium GNP is larger than full employment GNP
 - None of the above
80. What determines the slope of the aggregate supply curve is
- How fast the prices of factors of production respond to changes in the price level.
 - How much more the economy can produce without any change in the price level.
 - How fast the output level changes after a technological advance.
 - None of the above
81. When the aggregate supply curve is vertical, which of the following is not true?
- The economy is at full capacity.
 - The economy is producing the maximum sustainable level of output.
 - Any increase in the price level will not cause an increase in aggregate output.
 - The economy is expanding quickly
82. If the economy is operating on the relatively vertical segment of the aggregate supply curve, an increase in aggregate demand causes a _____ change in the price level and a _____ change in output.
- Small; small/no
 - Big; big
 - Big; small/no
 - Small/no; big
83. An increase in aggregate demand when the economy is operating at full capacity is likely to result in
- An increase in both output and the overall price level.
 - An increase in output but no increase in the overall price level.
 - An increase in the overall price level but no increase in output.
 - No increase in either output or the overall price level.

84. Coal is used as a source of energy in many manufacturing processes. Assume a long strike by coal miners reduced the supply of coal and increased the price of coal. This would cause:
- The short-run aggregate supply curve to shift to the right.
 - The short-run aggregate supply curve to become flatter.
 - The short-run aggregate supply curve to shift to the left.
 - The short-run aggregate supply curve to become nearly vertical at all levels of output
85. All of the following shift the short-run aggregate supply curve except _____
- A change in the price level of finished goods.
 - A change in the price of oil.
 - A change in the price of raw material.
 - A change in wages as a result of a labor strike.
86. An oil price increase would _____
- Increase aggregate demand.
 - Decrease short-run aggregate supply.
 - Decrease aggregate demand.
 - Increase short-run aggregate supply.
87. The aggregate supply curve shows the relationship between the aggregate quantity of output supplied by _____ and _____.
- All the firms in an economy; the overall price level
 - The government; aggregate demand
 - Domestically owned firms in the economy; the interest rate
 - The world; the money supply
88. An increase in the quantity and productivity of the factors of production, or advancement in technological capabilities in the economy would cause an increase in the productive potential which shifts LRAS to the left.
- True
 - False
89. Negative gap or deflationary gaps are same:
- True
 - False
90. An eminent economist David Ricardo released his well-known book entitled "General Theory of Employment, Interest and Money"
- True
 - False
91. If exports become more attractive to foreign firms then AD curve will shift leftward.
- True
 - False

92. The aggregate demand curve shows a _____ relationship between _____ and aggregate output _____.
- positive; the interest rate; demanded
 - negative; the price level; supplied
 - positive; the price level; demanded
 - negative; the price level; demanded
93. The aggregate demand curve shows that at higher price levels the total quantity of output demanded is greater.
- True
 - False
94. As the interest rate decreases, the planned aggregate expenditure curve shifts downward.
- True
 - False
95. Suppose the equilibrium output is initially \$600 billion. A decrease in taxes, there will be an _____ in equilibrium output and _____ the price level.



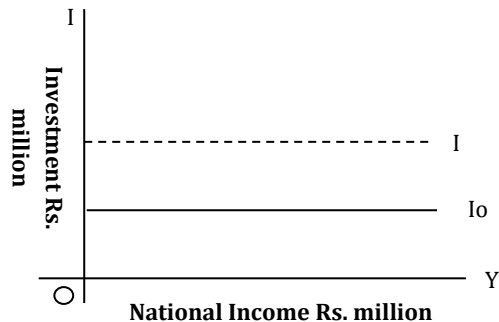
- Decrease; leaves unchanged
 - Leaves unchanged; increase
 - Increase; increase
 - Increase; decrease
96. Higher prices with higher unemployment is called
- Inflation
 - Deflation
 - Recession
 - Stagflation

ANSWERS TO SELF TEST QUESTIONS

1	(d)	21	(c)	41	(a)	61	(b)	81	(d)
2	(b)	22	(b)	42	(c)	62	(a)	82	(c)
3	(a)	23	(a)	43	(b)	63	(a)	83	(c)
4	(c)	24	(a)	44	(d)	64	(d)	84	(c)
5	(c)	25	(c)	45	(a)	65	(d)	85	(a)
6	(a)	26	(b)	46	(b)	66	(c)	86	(b)
7	(a)	27	(d)	47	(b)	67	(c)	87	(a)
8	(b)	28	(b)	48	(b)	68	(a)	88	(b)
9	(c)	29	Net property income from abroad	49	(c)	69	(b)	89	(a)
10	(c)	30	(a)	50	(c)	70	(c)	90	(b)
11	(d)	31	(a)	51	(c)	71	(d)	91	(b)
12	(d)	32	(a)	52	(b)	72	(d)	92	(d)
13	(d)	33	(a)	53	(b)	73	(c)	93	(b)
14	(b)	34	(c)	54	(b)	74	(d)	94	(b)
15	(d)	35	(a)	55	(d)	75	(b)	95	(c)
16	(b)	36	(d)	56	(b)	76	(a)	96	d
17	(a)	37	(d)	57	(d)	77	(b)		
18	(a)	38	(d)	58	(a)	78	(a)		
19	a(ii), b(iv), c(i)	39	(d)	59	(c)	79	(c)		
20	(b)	40	(c)	60	(a)	80	(a)		

CONSUMPTION, SAVING AND INVESTMENT

1. Shift of I_0 to I can be due to:



- substantial reduction in public development programs
 - substantial increase in public development programs
 - reduction in non-development spending
 - none of the above
2. In a closed economy, the full employment level of income is Rs.90 million, $C = \frac{2}{3}Y$ and $I = \text{Rs. } (40 - 3r)$ million, where C = consumption, Y = income, I = investment and r = the rate of interest.
- If planned government expenditure is Rs.20 million, what rate of interest would be required for there to be full employment?
- 10% per annum
 - 12% per annum
 - 14% per annum
 - 16% per annum
3. Which of the following is most likely to lead to an increase in a developing country's long-run rate of growth of income per head?
- a higher birth rate
 - a higher saving ratio
 - the reduction of import controls
 - an increase in government spending on defence
4. 'Expenditure done by households or firms on capital goods is called_____.'
- Consumption
 - Saving
 - Postponed consumption
 - Investment

5. What might explain why the consumption function shifts over time?
- a) Autonomous consumption is greater than zero.
 - b) Income is only one of several variables that affect consumption.
 - c) The average propensity to consume falls as income increases.
 - d) The marginal propensity to consume falls as income increases.
6. A closed economy is initially in equilibrium with a national income of Rs.100 million, and a capital stock of Rs.25 million. Aggregate demand increases by Rs.10 million.

According to the accelerator principle, by how much will investment increase?

- a) 10
 - b) 5
 - c) 2.5
 - d) 2
7. What will cause interest rates to rise?
- a) an unexpected increase in the prices of bonds
 - b) an increase in the nominal money supply
 - c) an increase in the volume of output
 - d) a reduction in the price level
8. Other things being equal, what is likely to result from an increase in interest rates in a country?
- a) a capital outflow from the country
 - b) a depreciation of the country's currency
 - c) a decrease in consumption
 - d) an increase in investment
9. In the relationship between consumption expenditure and income, which statement is correct?
- a) The average propensity to consume is constant
 - b) The average propensity to consume is rising.
 - c) The marginal propensity to consume is equal to the average propensity to consume
 - d) The marginal propensity to consume is less than the average propensity to consume
10. What is most likely to increase as a result of a rise in interest rates in a country?
- a) the level of house prices
 - b) the inflow of short-term foreign capital
 - c) the level of private investment
 - d) the return on capital investment
11. The marginal propensity to consume measures
- a) the relationship between changes in consumption and changes in consumer utility
 - b) the proportion of household incomes spent on consumer goods
 - c) the proportion of total National Income spent on consumer goods
 - d) the relationship between change in consumption and change in income

12. In a country with a very low income per head of the population
 - a) APC will be low and MPS will be low
 - b) APC will be low and MPS will be high
 - c) APC will be high and MPS will be low
 - d) APC will be high and MPS will be high
13. In a country with a closed economy and no government sector, the equilibrium National Income was Rs.1,000 million, with consumption of Rs.700 million. The marginal propensity to consume is 0.8. The equilibrium National Income has now risen to Rs.1,100 million and this includes
 - a) Consumption of Rs.770 million and Investment of Rs.300 million
 - b) Consumption of Rs.770 million and investment of Rs.330 million
 - c) Consumption of Rs.780 million and investment of Rs.320 million
 - d) Consumption of Rs.880 million and investment of Rs.220 million
14. An inflationary gap in the economy could be closed by an increase in the
 - a) Accelerator and multiplier
 - b) Government's budget surplus
 - c) Average propensity to consume
 - d) Country's export surplus
15. Which of the following responses is correct?
 A fall in the rate of interest may directly result in
 Response
 1. A switch to more capital-intensive methods of production
 2. A decline in the marginal efficiency of capital
 3. higher levels of investment
 - a) Responses 1 and 2 are correct
 - b) Responses 1 and 3 are correct
 - c) Responses 2 and 3 are correct
 - d) Responses 1, 2 and 3 are correct
16. Which one of the following is least likely to influence the rate of interest a business is charged on a loan?
 - a) Existing levels of debt of the business
 - b) The rate of corporate tax paid by the business
 - c) The business's past trading record
 - d) The availability of assets to secure borrowings
17. An increase in the savings ratio will always lead to an increase in investment.
 - a) True
 - b) False
18. The consumption function specifies that consumption spending is
 - a) negatively related to the level of disposable income,
 - b) positively related to the level of disposable income,
 - c) negatively related to the rate of interest,
 - d) positively related to the rate of interest.

19. Suppose consumption is Rs.10.0 million when disposable income is Rs.10.5 million, and consumption is Rs.10.5 million when disposable income is Rs.11.5 million, the marginal propensity to consume is
- 0.50
 - 0.75
 - 0.80
 - 0.90
20. The average propensity to consume is the ratio of
- a change in consumption to a change in disposable income
 - a change in consumption to total disposable income at a specific income level
 - total consumption to total disposable income at a specific income level
 - total consumption to a change in disposable income
21. A marginal propensity to consume of 0.80 indicates that
- ΔC to ΔY_d is 0.80
 - C/Y_d is 0.80
 - ΔY_d to ΔC is 0.80
 - Y_d/C is 0.80
22. The saving function is
- the level of planned saving for every change in disposable income
 - the level of planned saving at different levels of disposable income
 - the ratio of total saving to total disposable income
 - the ratio of a change in planned saving to a change in disposable income
23. When the MPC is 0.80 and the APC is 0.95, the MPS is
- 0.20 and the APS is 0.05,
 - 0.05 and the APS is 0.20,
 - 0.20 and the APS is 0.20,
 - 0.05 and the APS is 0.05.
24. Gross investment in the national income accounts includes
- Public Savings
 - Private Savings
 - changes in business inventories plus depreciation cost
 - all of the above
25. Which of the following statements is true?
- Gross investment is solely determined by the rate of interest
 - Gross investment is negatively related to the rate of interest, ceteris paribus
 - Gross investment is positively related to the rate of interest, ceteris paribus
 - Investment on capital goods by private sector is called public expenditures

26. Which of the following statements is true?
 - a) Imports lower aggregate spending on domestically produced goods and services
 - b) Exports lower aggregate spending on domestically produced goods and services
 - c) An increase in net exports lowers aggregate spending on domestically produced goods and services
27. Spending on purchasing new intelligence system for defense is non-development expenditure. Which of the following statements is false?
 - a) A country's exports increase when the economic activity of its major trading partners increases, ceteris paribus
 - b) A country's exports increase when its currency depreciates, ceteris paribus
 - c) A country's exports increase when it imports less, ceteris paribus
 - d) A country's exports increase when the price level of its major trading partners decreases, ceteris paribus
28. An increase in consumer confidence, ceteris paribus, shifts the consumption function upward.
 - a) True
 - b) False
29. Disposable income is the only variable that determines consumption.
 - a) True
 - b) False
30. A change in disposable income causes an equal change in consumption.
 - a) True
 - b) False
31. The distance from the consumption line to the 45° line is the level of saving at each level of disposable income.
 - a) True
 - b) False
32. The APC is constant along a linear consumption line.
 - a) True
 - b) False
33. Investment spending is positively related to the rate of interest, ceteris paribus.
 - a) True
 - b) False
34. Investment spending is the most unstable component of aggregate spending.
 - a) True
 - b) False
35. The investment demand curve shifts outward when households become more willing to purchase residential units.
 - a) True
 - b) False

36. Consumption and investment spending in the national income accounts is solely for domestically produced goods and services.
- c) True
d) False
37. Imports by a country are unrelated to its level of GDP.
- a) True
b) False
38. Find the value of Consumption and Saving, when $C_o = \text{Rs.}160$, $Y = \text{Rs.}500$ and marginal propensity to consume is 0.2.
- a) Answer: Consumption=_____ and Savings= _____
39. Find the values of marginal propensity to consume and marginal propensity to save from the following data:

Income in Rs.	Savings in Rs.
650	400
1000	680

Answer: MPC=_____ and MPS=_____

40. Which of the following factors might cause an upward shift in the country's consumption function?
- a) A fall in share prices
b) Expected increase in inflation
c) Households deciding to be economical
d) Fall in disposable personal income
41. Increase in the distribution of disposable income
- a) Cause upward shifts in the consumption function
b) Cause downward shifts in the consumption function
c) Have no effect upon the consumption function if income recipients have the same APC
d) Cause the consumption function to shift if the income recipients have the same APC
42. Keynes fundamental psychological law states that
- a) The change in income is greater than the change in consumption
b) The change in consumption is greater than the change in income
c) People stop consuming when they become affluent
d) People stop saving when they become affluent
43. If $C = 50 + 0.80Y$ then;
- a) The MPC is 0.50
b) The MPC is 0.20
c) The MPS is 0.80
d) The MPS is 0.20

44. Consumption increasing along with increase in income. But rate of change in consumption is lesser than change in income which leads to an increase in saving.
- True
 - False
45. People increase their consumption as their income increases, but not by as much as their income increases.
- True
 - False
46. If $C_o = \text{Rs.}160$, $Y = \text{Rs.}500$ and marginal propensity to consume is 0.2 then consumption will be_____
- Rs. 360
 - Rs. 260
 - Rs. 160
 - Rs. 140
47. _____is the minimum level of consumption that one must dispose-off regardless of his income.
- Induced consumption
 - Autonomous consumption
 - Average consumption
 - Marginal consumption
48. Consumption on y intercept is_____
- Induced consumption
 - Autonomous consumption
 - Autonomous saving
49. Keynes law of consumption is that people increase their consumption as their_____, but not by as much as their income increases.
- Demand increases
 - Emotions changes
 - Behavior changes
 - income increases

ANSWERS TO SELF TEST QUESTIONS

1	(b)	11	(d)	21	(a)	31	(a)	41	(a)
2	(a)	12	(c)	22	(b)	32	(b)	42	(a)
3	(b)	13	(c)	23	(a)	33	(b)	43	(d)
4	(d)	14	(b)	24	(c)	34	(a)	44	(a)
5	(b)	15	(b)	25	(b)	35	(a)	45	(a)
6	(c)	16	(b)	26	(a)	36	(b)	46	(a)
7	(c)	17	(b)	27	(c)	37	(b)	47	(b)
8	(c)	18	(b)	28	(a)	38	260 and 240	48	(b)
9	(d)	19	(a)	29	(b)	39	0.2 and 0.8	49	(d)
10	(b)	20	(c)	30	(b)	40	(b)		

MULTIPLIER AND ACCELERATOR

1. In a closed economy with no government the full employment level of output is Rs.25 million, the actual level of output is Rs.20 million, and the marginal propensity to consume is $\frac{4}{5}$. What is the size of the investment needed to achieve full employment level?
 - a) Rs.1 million
 - b) Rs.4 million
 - c) Rs.5 million
 - d) Rs.16 million
2. The marginal propensity to consume in a country is 0.9 and the average propensity is 0.8. What is the value of the multiplier?
 - a) 1.1
 - b) 1.25
 - c) 5
 - d) 10
3. According to the accelerator theory
 - a) net investment is positive if output is rising at an increasing rate
 - b) net investment may rise even if output rises at a declining rate
 - c) increases in investment occur when interest rates are falling
 - d) increases in investment will cause a more than proportionate increase in national income
4. Out of any addition to national income, 20% is spent on imports, 25% is paid in taxes, 5% is saved and the rest is spent on domestically produced goods.
What is the value of the multiplier?
 - a) 20
 - b) 5
 - c) 2
 - d) 0.5
5. In a closed economy with no government sector the multiplier shows the impact of a change in
 - a) Consumption on investment
 - b) Investment on national income
 - c) national income on consumption
 - d) national income on investment

6. In an economy with unemployed resources the government increases its expenditure. This would be least likely to increase national income by the full multiplier effect if the
- level of autonomous private investment is increased
 - marginal propensity to save is reduced
 - government allows money supply to expand
 - level of interest rates rises
7. According to the accelerator theory, what determines this year's net investment?
- last year's consumption
 - last year's output
 - the change in last year's output
 - the change in last year's investment
8. What is the value of the multiplier in an economy with no government where the marginal propensity to save is $\frac{1}{6}$, and the marginal propensity to import is $\frac{1}{3}$?
- $\frac{1}{2}$
 - $1\frac{1}{2}$
 - 2
 - 3
9. Which of the following is most likely to be found in a developing economy?
- a low capital-labor ratio
 - a high capital-labor ratio
 - a high capital-output ratio
 - a low labor-output ratio
10. The effect of the multiplier on national income will be small
- when there is high unemployment in the economy
 - when the marginal propensity to save is low
 - because of a deflationary gap
 - because of leakages from the circular flow in addition to savings
11. The multiple effect of government investment is likely to be greater when
- there is excess production capacity in the private sector of industry
 - there is a high marginal propensity to consume
 - the increased spending is financed by higher taxation
 - there is a high level of stocks in firms
12. In a closed economy with no government sector, the consumption function is thought to be $C = 30,000 \text{ million} + 0.4Y$
Investment is Rs.30,000 million per year.
Which of the following statements is correct?
- Equilibrium income is 80,000 million & Value of the multiplier = 1.67
 - Equilibrium income is 80,000 million & Value of the multiplier = 2.50
 - Equilibrium income is 100,000 million & Value of the multiplier = 1.67
 - Equilibrium income is 100,000 million & Value of the multiplier = 2.50

13. Investment in a closed economy (with no government sector) is expected to increase by Rs.6,000 million in the next year. Given a marginal propensity to save of 0.4, what will be the expected growth in national Income!
 - a) Rs.10,000 million
 - b) Rs.15,000 million
 - c) Rs.16,000 million
 - d) Rs.21,000 million

14. In an open economy, the marginal propensity to consume domestically produced goods is 0.25 at all levels of income. If exports increase by Rs.100 million, and there are no other changes, National income will increase by
 - a) Rs.25 million
 - b) Rs.100 million
 - c) Rs.125 million
 - d) Rs.133 million

15. A nation's income rises by Rs.2,500 million and its inhabitants spend Rs.2,000 million on consumer goods. The value of the multiplier is
 - a) 0.80
 - b) 1.25
 - c) 4
 - d) 5

16. An economy with no government sector has a consumption function which is thought to be (in Rs. billion) $C = 100 + 0.8Y$. However, of additional goods consumed, three quarters are imports.
 There is an increase in investment spending of Rs.20 billion.
 By how much will national income increase?
 - a) Rs.25 billion
 - b) Rs.45 billion
 - c) Rs.100 billion
 - d) Rs.120 billion

17. An increase in saving will always act to the benefit of a country.
 - a) True
 - b) False

18. The paradox of thrift suggests that an attempt to increase the amount saved out of a given level of national income will result in a fall in national income.
 - a) True
 - b) False

19. It is generally accepted by economists that the multiplier is a useful analytical device, but it does have certain limitations. Which of the following is not such a limitation?
 - a) The multiplier-induced changes between one national Income equilibrium and another take a long time to happen
 - b) The consumption function is often unstable
 - c) The multiplier only affects real Income when there is an inflationary gap
 - d) The multiplier only affects real income when there is unemployment caused by deficient demand

20. Complete the following statement.

The accelerator principle states:

- a) how an Initial increase in a component of national income leads to much greater eventual rise in national income
- b) that a small change in investment will lead to a much greater change in the output of consumer goods
- c) that a small change in the output of consumer goods will lead to a much greater change in the production of capital goods
- d) that changes in investment level are the cause of trade cycles

21. The following formula shows the amount of new investment that an economy will undertake.

New Investment = $(v \times \text{Increase in national income})$

Where, v is the desired capital-output ratio.

Two changes occur

Change 1: Some capital-saving technology progress occurs

Change 2: The possibility of substituting labor for capital is reduced.

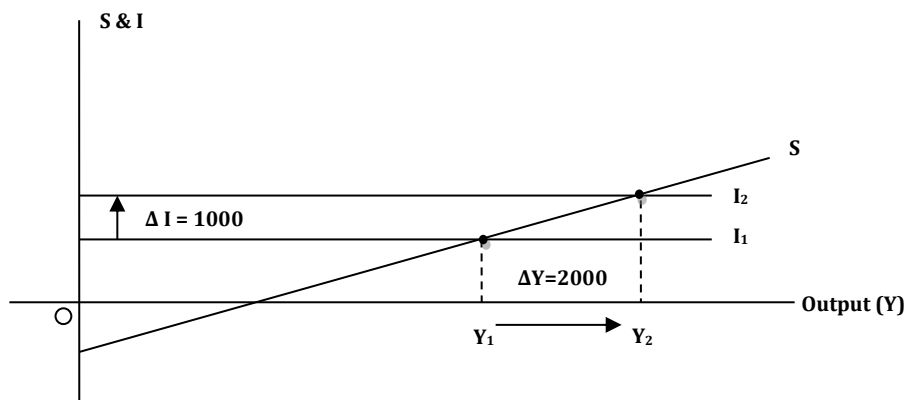
What will happen?

- a) Change 1 will increase v & Change 2 will reduce v
- b) Change 1 will reduce v & Change 2 will reduce v
- c) Change 1 will increase v & Change 2 will increase v
- d) Change 1 will reduce v & Change 2 will increase v

22. Which of the following is the correct sequence in a business cycle?

- a) Boom Recession Depression Recovery
- b) Recession Recovery Boom Depression
- c) Boom Recovery Recession Depression
- d) Recovery Recession Depression Boom

23. In reference to the given diagram, the value of multiplier will be:



- a) 2
- b) 3
- c) 4
- d) 5

24. Keynes suggested that investment grows faster than consumption because of:
 - a) The multiplier
 - b) The J-curve effect
 - c) A low marginal propensity to consume
 - d) The accelerator
25. The trade cycle is:
 - a) The accounting reference period
 - b) A sequence of varying rates of growth
 - c) The period over which all factors of production may be varied
 - d) The process by which a small injection into the circular flow produces a larger rise in national income
26. To which one of the following statements would supply side economists subscribe?
 - a) Price regulation enhances the signal function of market prices.
 - b) Government subsidies encourage inefficiency.
 - c) An unregulated labour market cannot ensure full employment.
 - d) An unregulated labour market encourages over-manning
27. The effect of the multiplier on national income will be small:
 - a) When there is high unemployment in the economy
 - b) When the marginal propensity to save is low
 - c) Because of a deflationary gap
 - d) Because of leakages from the circular flow in addition to savings
28. Which of the following is the correct sequence in a business cycle?
 - a) Boom Recession Trough Expansion
 - b) Recession Recovery Boom Depression
 - c) Boom Recovery Recession Depression
 - d) Recovery Recession Depression Boom
29. The recession phase of the trade cycle will normally be accompanied by all of the following except which one?
 - a) A rise in the rate of inflation
 - b) A fall in the level of national output
 - c) An improvement in the trade balance
 - d) A rise in the level of unemployment
30. The multiplier principle explains how investment in capital goods responds disproportionately to changes in consumer demand.
 - a) True
 - b) False
31. In Country A, the marginal propensity to consume is 0.8. The Country A's government injects Rs.4 billion into the economy. Increase in national income will be: _____ billion

32. The accelerator principle explains how capital investment changes in direct proportion to changes in consumption.
- a) True
 - b) False
33. Suppose consumer saving is specified as $S = -50 + 0.50Y$, investment spending is Rs.75 b, gross exports total Rs.50 b, and gross imports equal Rs.35 b. Find the equilibrium level of output algebraically by equating leakages and injections.
- a) Rs. 180 b
 - b) Rs. 290 b
 - c) Rs. 390 b
 - d) Rs 280 b
34. A recessionary gap exists when
- a) Aggregate supply exceeds aggregate demand,
 - b) The aggregate spending line intersects the 45° line at an output level to the right of the full- employment level of output.
 - c) The aggregate spending line intersects the 45° line at an output level to the left of the full- employment level of output.
 - d) The aggregate spending line intersects the aggregate supply curve at a lower price level.
35. There is a multiplier effect from changes in investment spending because
- a) aggregate supply is related to the level of output,
 - b) consumer spending is positively related to the level of output,
 - c) consumer spending is negatively related to the level of output,
 - d) exports are positively related to the level of output.
36. The multiplier measures the rate of change in
- a) output resulting from a change in spending,
 - b) consumption resulting from a change in output,
 - c) output resulting from a change in consumption,
 - d) investment resulting from a change in output.
37. When the marginal propensity to consume is 0.4, the value of the multiplier is
- a) 2
 - b) 3
 - c) 4
 - d) 1.7
38. When aggregate supply is horizontal and the marginal propensity to consume is 0.50, a \$10 increase in investment spending will result in
- a) a \$10 increase in the equilibrium level of output
 - b) a \$20 increase in the equilibrium level of output
 - c) a \$50 increase in the equilibrium level of output
 - d) no change in the equilibrium level of output

39. When aggregate supply is positively sloped and the marginal propensity to consume is 0.80, a \$10 increase in investment spending will result in
 - a) a \$10 increase in the equilibrium level of output
 - b) a \$50 increase in the equilibrium level of output
 - c) an increase in the equilibrium level of output less than \$50
 - d) an increase in the equilibrium level of output greater than \$50
40. The multiplier is 5 when the marginal propensity to save is 0.20.
 - a) True
 - b) False
41. A Rs 5 billion increase in investment spending results in a Rs 50 billion increase in the equilibrium level of output when the MPC is 0.90 and aggregate supply is horizontal.
 - a) True
 - b) False
42. A Rs 10 billion increase in investment spending results in less than a Rs 40 billion increase in the equilibrium level of output when the MPC is 0.75 and aggregate supply is positively sloped.
 - a) True
 - b) False
43. An equilibrium level of output exists when output is Rs 550 billion, investment spending is Rs 70 billion, net exports equal Rs 30 billion, and the consumption function is $C = 10 \text{ billion} + 0.80Y$.
 - a) True
 - b) False
44. Fill in the gaps. A redistribution of income from rich to poor households is likely to lead to _____ in aggregate demand because the poorer households have a higher _____.
 - a) An increase; marginal propensity to save
 - b) A decrease; marginal propensity to save
 - c) An increase; marginal propensity to consume
 - d) A decrease; marginal propensity to consume
45. The effect of the multiplier on national income will be small:
 - a) When there is high unemployment in the economy
 - b) When the marginal propensity to save is low
 - c) Because of a deflationary gap
 - d) Because of leakages from the circular flow in addition to savings
46. In country X, an open economy, for every additional Rs.1 of income, 20% is taken as taxes, 10% is saved and 50% is spent on domestically produced goods. What is the value of the multiplier in country X?
 - a) 0.8
 - b) 1.25
 - c) 2
 - d) 3.33

47. Under which of the following circumstances, the value of the multiplier would be higher?
- a) When both marginal propensity to consume and marginal propensity to import are low
 - b) When marginal propensity to consume is low and marginal propensity to import is high
 - c) When marginal propensity to consume is high and marginal propensity to import is low
 - d) When both marginal propensity to consume and marginal propensity to import are high
48. According to Samuelson cyclical fluctuation in business cycle is due to
- a) Change in multiplier
 - b) Change in accelerator
 - c) Interaction of both multiplier and accelerator
 - d) No link with multiplier and accelerator

ANSWERS TO SELF TEST QUESTIONS

1	(a)	11	(b)	21	(d)	31	(20)	41	(a)
2	(d)	12	(c)	22	(a)	32	(b)	42	(a)
3	(a)	13	(b)	23	(a)	33	(d)	43	(a)
4	(c)	14	(d)	24	(d)	34	(c)	44	(c)
5	(b)	15	(d)	25	(b)	35	(b)	45	(d)
6	(d)	16	(a)	26	(b)	36	(a)	46	(c)
7	(c)	17	(b)	27	(d)	37	(d)	47	(c)
8	(c)	18	(a)	28	(a)	38	(d)	48	(c)
9	(a)	19	(c)	29	(a)	39	(b)		
10	(d)	20	(c)	30	(b)	40	(a)		

1. Without any change in government policy, what will be the effect of an economic recession on tax revenue and on government expenditure?

	Tax Revenue	Government expenditure
A	Decrease	Decrease
B	Decrease	Increase
C	Increase	Increase
D	Increase	Decrease

2. What is the major cause of high rates of inflation in many developing economies?
- Balance of payments deficits
 - Budget deficit
 - Low levels of unemployment
 - overvalued exchange rates
3. A regressive tax is defined as one which requires
- all taxpayers to pay the same absolute amount of their income in taxation
 - high income earners to pay less in taxes than low-income earners
 - high income earners to pay more in taxes than low-income earners
 - high income earners to pay a lower proportion of their income in taxes than low-income earners
4. The table shows the marginal tax rates paid by a country's taxpayers at different levels of income.

Income (Rs.)	Tax rate
First 4000	Zero
4001-20000	20%
Above 20000	40%

Which of the following correctly describes this tax?

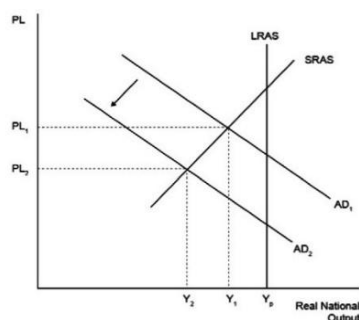
- It is regressive over the entire range of income.
- It is proportional over the income range 4001 - 20000.
- It is proportional over the range of income above 20000.
- It is progressive over the range of income above 4000.

5. Which of the following elements of a tax and benefits system is regressive?
- the taxation of capital gains
 - the payment of child benefits to families
 - specific taxes on beverages and tobacco
 - rent subsidies to tenants of publicly owned housing
6. Which of the following would be a fiscal measure by a government which would have the effect of restricting the growth in the money supply?
- An increase in short term (money market) interest rates
 - An increase in the rate of GST
 - An increase in the Public Sector Borrowing Requirement
 - The imposition of a prices and incomes policy
7. Which of the following consequences should be the result of an increase in the rates of personal taxation accompanied by a reduction in government expenditure?
- Consequence
- An Improvement in the balance of trade
 - A reduction in the rate of inflation
 - A reduction in unemployment
- Consequences 1 and 2 only
 - Consequences 1 and 3 only
 - Consequences 2 and 3 only
 - Consequence 2 only
8. Mr. Rohail earns Rs.8,000 per year and pays Rs.1,000 in income tax. Mr. Shaffan earns Rs.16,000 per year and pays Rs.2,500 in income tax. Harold earns Rs.24,000 per year and pays Rs.5,500 in income tax. The income tax system is:
- Regressive
 - Flat rate
 - Proportional
 - Progressive
9. The government of a certain country decides to introduce an election tax, which will involve a flat levy of Rs.500 on every adult member of the population. This new tax could be described as:
- Regressive
 - Proportional
 - Progressive
 - Ad valorem
10. If a reduction in the taxes on energy drinks resulted in a less even distribution of wealth in society, with a greater proportion of wealth in the hands of the rich sections of society, we could conclude that, on average.
- People with low incomes spend more on energy drinks than people with high incomes
 - People with low incomes spend less on energy drinks than people with high incomes
 - People with low incomes spend a bigger proportion of their income on energy drinks than people with high incomes
 - People with low incomes spend a lower proportion of their income on energy drinks than people with high incomes

11. The opportunity cost of leisure can be defined as the quantity of goods and services which individuals forgo by not working. This being so, the opportunity cost of leisure would rise as a consequence of:
 - a) An increase in (wealth) tax on capital transfers
 - b) A reduction in the rate of income tax
 - c) An increase in the rate of indirect taxes
 - d) Introducing a poll tax
12. Which one of the following is an aspect of fiscal policy measures by the government?
 - a) To raise short-term interest rates in the money markets
 - b) To support the exchange rates for the country's currency
 - c) To control growth in the money supply
 - d) To alter rates of taxation
13. If a government wishes to increase consumer spending, it could increase the rate of:
 - a) Income tax
 - b) Corporation tax
 - c) Import duties
 - d) Social security payments
14. An equal rise in government purchases and taxes raises output.
 - a) True
 - b) False
15. Government macroeconomic policy must take account of automatic stabilizers. These are of two types. One type is tax revenues that fall as national income rises.
 - a) True
 - b) False
16. GST is a regressive tax.
 - a) True
 - b) False
17. An increase in the income tax rate shifts the consumption line downward and makes the consumption line more steeply sloped.
 - a) True
 - b) False
18. Fiscal policy refers to any change in government tax revenue and/or in government spending.
 - a) True
 - b) False
19. Net tax revenues fall when a decrease in economic activity results in automatic increases in tax payments.
 - a) True
 - b) False

20. An increase in taxes, ceteris paribus, shifts the leakage line (S+T+M) rightward, which results in an increase in the equilibrium level of output.
- True
 - False
21. A managed change in government spending and/or tax revenue is a discretionary fiscal policy.
- True
 - False
22. The governments of many countries raise revenue from a tax on a wide range of essential goods and services. What is the nature of this tax?
- It is direct and proportional
 - It is direct and regressive
 - It is indirect and proportional
 - It is indirect and regressive
23. What is meant by a regressive indirect tax?
- A tax on income that falls more heavily on the poor
 - A tax on income that falls more heavily on the rich
 - A tax on spending that falls more heavily on the poor
 - A tax on spending that falls more heavily on the rich
24. What is the main reason why indirect tax is thought to be unfair?
- Not everyone pays an indirect tax
 - The consumer is unaware of the rate of tax
 - The retailer is forced to collect the tax for the government
 - The tax burden is greater for people of low incomes
25. Which of the following policies help in increasing economic growth?
- Increase in imports
 - Increase in government spending
 - Reduction in subsidies
 - Increase in unemployment
26. Which of the following measures is NOT likely to boost a country's rate of economic growth?
- Tax cuts
 - Tax rebates
 - Reduction in subsidies
 - Increase in government spending
27. Sales tax on petrol is an example of
- Direct tax
 - Fixed tax
 - Progressive tax
 - Regressive tax

28. Which one of the following is NOT a feature of a good tax system?
- It should be equitable
 - It should be economical
 - The rate should be same for everybody
 - It should be certain
29. Which of the followings are examples of direct tax?
- Sales tax
 - Service tax
 - Wealth tax
 - Value added tax
30. Government of Pakistan decides to introduce a new tax, which will involve a charge of Rs.5000 on every member of ICAP. This new tax could be described as:
- Regressive
 - Proportional
 - Progressive
 - Ad valorem
31. Which is the best example of expansionary fiscal policy?
- Taxes are increased
 - Taxes are decreased and government spending are increased
 - Government spending are decreased and taxes increased
 - Government spending are increased
32. In case contractionary fiscal policy in an economy:
- Taxes are increased
 - Tax rebates are increased
 - Government spending are increased
 - All of the above
33. Following diagram shows:

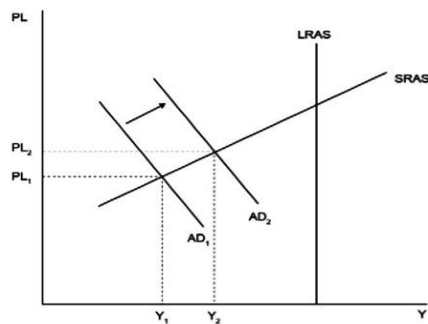


- Contractionary fiscal policy
- Expansionary fiscal policy
- Inflationary fiscal policy
- Anti deflationary fiscal policy

34. Which one of these is an expression of fiscal deficit?
- a) $T > G$
 - b) $G < T$
 - c) $T < G$
 - d) $T = G$
35. A flat fee of PTV of Rs. 35 included in electricity bill is an example of
- a) Regressive tax
 - b) Progressive tax
 - c) Proportional tax
 - d) Corporate tax
36. Crowding out is a result of:
- a) Extraordinary government expenditure and lower investment
 - b) Low government expenditure with high private investment
 - c) High taxes
 - d) None of these
37. Which of the following measures is likely to boost a country's rate of economic growth?
- a) Tax cuts
 - b) Reduction in tax rebates
 - c) Reduce import duties
 - d) Decrease in government spending
38. Which of the following is an objective of fiscal policy?
- a) Zero inflation
 - b) Balance of payment surplus
 - c) Low exchange rates
 - d) Stable economic growth
39. Murad pays a tax of Rs. 100 on his income of Rs. 1000 while Sohail pays a tax of Rs. 200 on his income of Rs. 800. Identify the tax system prevailing in the country.
- a) Progressive
 - b) Regressive
 - c) Proportional
 - d) Equitable
40. _____ does not satisfy canon of equality.
- a) Proportional
 - b) Progressive
 - c) Regressive
 - d) None of these

41. "The tax which each individual is bound to pay ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid ought all to be clear and plain to the contributor and to every other person." is called cannon of _____.
 - a) Certainty
 - b) Economy
 - c) Convenience
 - d) Equality
42. Income tax in a particular slab where rate remains unchanged are the examples of _____ taxes
 - a) Proportional
 - b) Progressive
 - c) Regressive
 - d) None of these
43. Mohsin pays income tax of Rs. 2,500 on his earnings of Rs. 20,000. Danish pays Rs. 4,000 income tax on his earnings of Rs. 32,000. Kinza pays Rs. 5,000 income tax on her earnings of Rs. 40,000. The income tax system is:
 - a) Regressive
 - b) Proportional
 - c) Progressive
 - d) Equitable
44. Which of the following is an instrument of expansionary policy?
 - a) Increase taxes
 - b) Reduce subsidies
 - c) Allow tax rebates
 - d) None of these
45. Which of the subsequent is not included in public expenditure?
 - a) Capital spending by public companies
 - b) Expenditure by government departments
 - c) Investment by nationalized industries
 - d) Spending by local governments
46. A budget deficit causes _____ government debt.
 - a) Increase in
 - b) Decrease in
 - c) Has no effect on
 - d) Eliminates
47. Which one of these are functions of taxation:
 - a) Fiscal
 - b) Allocation
 - c) Regulatory
 - d) All of the above

48. Internal and external borrowing is possible in private finance only
- True
 - False
49. Income received by state authorities other than its tax is known as tax revenues.
- True
 - False
50. Non-development expenditure incurred on defence, social services, to maintain law and order situation, general administration, debt servicing and subsidies.
- True
 - False
51. following diagram predict:

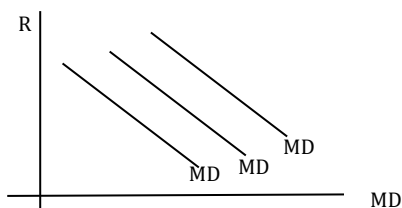


- Contractionary fiscal policy
 - Expansionary fiscal policy
 - Anti-inflationary fiscal policy
 - None of the above
52. Direct taxes reduce the disposable income and cause a leftward shift in aggregate demand that is why it helps in controlling demand pull inflation.
- True
 - False
53. Zakat rate is like proportional tax rate.
- True
 - False
54. According to Rostow, which one in hierarchy of stages in growth:
- Pre-take of stage
 - Drive to maturity
 - Age of mass consumption
 - Take of stage
- I, II, III, IV
 - IV, II, III, I
 - I, IV, II, III
 - II, I, III, IV

ANSWERS TO SELF TEST QUESTIONS

1	(b)	11	(c)	21	(a)	31	(b)	41	(a)	51	(b)
2	(b)	12	(d)	22	(d)	32	(a)	42	(a)	52	(a)
3	(d)	13	(d)	23	(c)	33	(a)	43	(b)	53	(a)
4	(d)	14	(a)	24	(d)	34	(c)	44	(c)	54	(c)
5	(c)	15	(b)	25	(b)	35	(a)	45	(a)		
6	(b)	16	(a)	26	(c)	36	(a)	46	(a)		
7	(a)	17	(b)	27	(d)	37	(a)	47	(d)		
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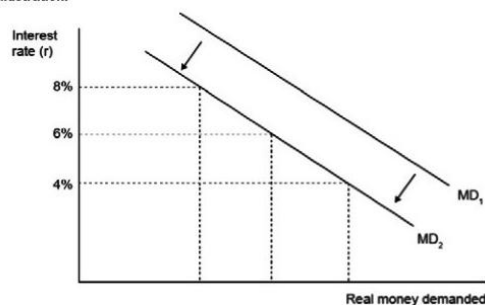
1. What is most likely to cause the public to hold less cash in relation to the level of money income?
 - a) a fall in interest rates
 - b) a fall in the level of output
 - c) a greater availability of cash substitutes
 - d) a rise in the general price level
2. What would cause an expansionary fiscal policy to be relatively ineffective?
 - a) a low marginal propensity to import
 - b) a fixed exchange rate
 - c) a fixed money supply
 - d) large-scale unemployment of resources
3. According to Keynesian theory, what would cause individuals to want to hold more idle money balances?
 - a) an increase in bond prices
 - b) an increase in the rate of interest
 - c) an increase in the rate of inflation
 - d) an increase in the level of cutout
4. In a closed economy, if the income velocity of circulation of money remains constant, what will be the result of an increase in the money supply?
 - a) a proportionate increase in the level of money income
 - b) a proportionate increase in the level of output
 - c) a proportionate increase in the rate of growth of money income
 - d) a proportionate increase in the rate of growth of output
5. What would cause an increase in the transactions demand for money?
 - a) an increase in the rate of interest
 - b) an increase in nominal national income
 - c) a fall in the price of bonds
 - d) an increase in unemployment
6. Demand for money moving from MD1 to MD3 is:



- a) Rise in demand
 - b) Fall in demand
 - c) Extension in demand
 - d) Contraction in demand
7. All of the following would tend to result in a reduction of the rate of growth in the broad money supply EXCEPT
- a) an increase in the rate of interest offered on National Savings
 - b) a reduction in the Public Sector Borrowing Requirement (PSBR)
 - c) the sale of long-term bonds by the government to the banking sector
 - d) the sale of treasury bills to the discount houses
8. The velocity of circulation can be defined as
- a) the money stock in a given time period divided by the level of prices
 - b) the average time in which households spend their money income
 - c) the total value of transactions in a given time period divided by the average price level
 - d) the number of times in a given time period that a unit of money is used to purchase final output
9. For the Quantity Theory of Money equation $MV = PT$ to explain short-run price behaviour, it is necessary that
- a) P varies inversely with M
 - b) interest rates remain unchanged
 - c) changes in V in the short run are predictable
 - d) T remains unchanged
10. Which one of the following four functions of money was central to Keynes's analysis of the demand for money?
- a) a means of exchange
 - b) a unit of account
 - c) a standard of deferred payment
 - d) a store of value
11. According to Keynes, which one of the following is very sensitive to changes in interest rates?
- a) The supply of money
 - b) The speculative demand for money
 - c) The precautionary demand for money
 - d) The transactions demand for money
12. Other things remaining the same, according to Keynes, an increase in the money supply will tend to reduce
- a) interest rates
 - b) liquidity preference
 - c) the volume of bank overdrafts
 - d) prices and incomes
13. Which of the following actions by the government would be most likely to increase aggregate monetary demand?
- a) Reductions in subsidies on food, offset by a reduction in taxation
 - b) A rise in the State Bank of Pakistan's short term interest rate (for open market operations)
 - c) Increased value added tax on a wide range of goods
 - d) Insisting that public corporations should break even

14. Using given diagram, select the correct option:

Illustration:



- a) Due to financial innovation
 - b) Due to high liquidity in financial markets
 - c) Due to fall in GDP
 - d) All of above
15. Which one of the following is not a function of a central bank?
- a) The conduct of fiscal policy
 - b) Management of the national debt
 - c) Holder of the foreign exchange reserves
 - d) Lender of the last resort
16. Which of the following would lead to a rise in the demand for money?
- a) A fall in disposable income
 - b) A rise in interest rates
 - c) An expected increase in inflation
 - d) A decrease in the money supply
17. In the theory of the demand for money, the transactions demand for money is determined by:
- a) The level of consumers' incomes
 - b) Expected changes in interest rates
 - c) Expected changes in bond prices
 - d) The level of notes and coins in circulation
18. The velocity of circulation can be defined as:
- a) The money stock in a given period divided by the level of prices
 - b) The average time in which households spend their money income
 - c) The total value of transactions in a given time period divided by the average price level
 - d) The number of times in a given time period that a unit of money is used to purchase final output
19. According to Keynes, which one of the following is very sensitive to changes in interest rates?
- a) The money supply
 - b) The speculative demand for money
 - c) The precautionary demand for money
 - d) The transactions demand for money

20. For the Quantity Theory of Money equation $MV = PT$ to explain short-run price behaviour, it is necessary that:
- P varies inversely with M
 - Interest rates remain unchanged
 - Changes in V in the short run are predictable.
 - T remains unchanged
21. Other things remaining the same, according to Keynes, an increase in the money supply will tend to reduce:
- Interest rates
 - Liquidity preference
 - The volume of bank overdrafts
 - Prices and incomes
22. Using the new quantity theory of money identity $MV = PT$, if the velocity of circulation and level of national output remain constant but the money supply grows by 5%, the rate of inflation will:
- Increase by 10%
 - Decrease by 10%
 - Increase by 5%
 - Constant
23. If interest rate rises, the market price of fixed interest investments such as bonds will fall.
- True
 - False
24. Keynes suggested that people choose to keep money on hand in case they have a sudden need for it; this is called the:
- Speculative
 - Traditional
 - Transactional
 - Precautionary
25. Which of the following is not a function of money?
- A store of value
 - A unit of account
 - A certificate of deposit
 - A medium of exchange
26. According to Keynes's Liquidity Preference Theory
- Transaction motive
 - Speculative motive
 - Precautionary motive
 - All of the above
27. Money is not what it is but what it does. This statement is
- False
 - True

28. Money which has no intrinsic value & government decrees it as a legal tender is
- Commodity money
 - Fiat money
 - Barter
 - Plastic money
29. According to Keynes, Liquidity Preference is actually
- Supply of money
 - Aggregate demand
 - Equilibrium of demand & supply of money
 - Demand for money
30. Liquidity trap is a situation in which
- Prevailing interest rates are low and savings are also low
 - Prevailing interest rates are low and savings are high
 - Both interest rates and savings are high
 - None of the above
31. Which of the following are true:
- If interest rates are low but expected to rise, liquidity preference will be high
 - If interest rates are high but expected to fall, liquidity preference will be high
 - The demand for money is high when interest rates are low
 - The demand for money is high when interest rates are high
- (i) only
 - (ii) only
 - (i) and (iii)
 - (ii) and (iv)
32. If a country has 10 million spending transactions per year, at an average price of Rs 50, and the annual velocity of circulation is 4, what is its money supply?
- Rs.100 million
 - Rs.125 million
 - Rs.150 million
 - Rs.200 million
33. In Pakistan paper currency issued by the SBP
- is backed by gold but is not convertible into gold,
 - has no intrinsic value but is backed by gold,
 - has no intrinsic value,
 - has no value in exchange.
34. Which of the following factors causes the barter system to be inefficient?
- Its cost of transaction is too low.
 - The cost associated with information search is too low.
 - It requires a double coincidence of wants.
 - It requires high liquidity

35. The development of money as a medium of exchange has facilitated the expansion of trade because
- holding money increases people's wealth.
 - holding money increases people's income.
 - money eliminates the "double coincidence of wants" problem.
 - no other mediums of exchange are available.
36. A currency that is not backed by gold, silver, or any other precious commodity equal to the face value of the money is known as
- credit money.
 - weak money.
 - token money.
 - commodity money
37. According to the monetarists there is a trade-off between inflation and unemployment in the long run.
- True
 - False
38. Due to financial innovations, people prefer to hold it in cash form.
- True
 - False
39. Speculative demand for money is also inversely related to the interest rate but relatively inelastic.
- True
 - False
40. Larger budget deficit is used as tool to overcome from liquidity trap.
- True
 - False
41. When rate of interest falls, the bond price rises.
- True
 - False
42. Unemployment rate cannot be zero because of _____
- Frictional unemployment
 - Structural unemployment
 - Voluntary unemployment
 - All of above
43. Quantity theory of money presented by eminent economist "Irving Fisher".
- True
 - False
44. Value of money is inversely proportional to money supply.
- True
 - False

45. CPI in 2021=120, CPI in 2022=140 then inflation rate is
- a) 20%
 - b) 14%
 - c) 17%
 - d) Cannot be determined

ANSWERS TO SELF TEST QUESTIONS

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INFLATION AND UNEMPLOYMENT

1. What could be expected to increase the pressure of demand-pull inflation in an open economy?
 - a) An appreciation of the foreign exchange rate
 - b) an increase in indirect taxes
 - c) an increase in interest rates
 - d) the imposition of import controls
2. What is likely to be the effect of a fall in oil prices on the global economy?
 - a) a decrease in the rate of economic growth
 - b) a decrease in unemployment
 - c) a strengthening of cost-push inflation
 - d) a weakening of demand-pull inflation
3. The natural rate of unemployment in an economy is 5%.
What will happen if a government persists in trying to achieve a target rate of unemployment of 3% by expansionary monetary policy?
 - a) an accelerating rate of inflation
 - b) a diminishing rate of inflation
 - c) a high but constant rate of inflation
 - d) a negative rate of inflation
4. Which combination of policy measures is most likely to reduce unemployment?
 - a) lowering both the exchange rate and domestic interest rates
 - b) lowering the exchange rate and increasing direct taxation
 - c) raising both the exchange rate and domestic interest rates
 - d) raising both the exchange rate and direct taxation
5. Which type of unemployment is associated with a deficiency in aggregate demand?
 - a) Cyclical
 - b) Frictional
 - c) Structural
 - d) Voluntary
6. In short-run Phillips curve, what is assumed to remain constant when drawing this curve?
 - a) the average price level
 - b) the money supply
 - c) the exchange rate
 - d) the natural rate of unemployment

7. In an economy the long-run rate of growth of potential output is 2.5%.
What must happen in the short run if actual output grows at 5%?
- an increase in employment
 - an increase in the rate of inflation
 - a deterioration in the balance of trade
 - an increase in labor productivity
8. All else remaining unchanged, which measure would be most likely to increase the natural rate of unemployment?
- an increase in expenditure on education and training
 - an increase in the rate of unemployment benefits
 - a reduction in the government's budget deficit
 - a reduction in the general level of interest rates
9. Between 2000 and 2002 national output in the Pakistan increased by 2%.
Over the same period the unemployment rate increased from 4% to 6%.
What would explain this?
- There was a decrease in labor productivity
 - There was a decrease in the size of the labor force
 - There was a fall in the rate of inflation
 - Potential growth in national output was above actual growth
10. Which type of unemployment arose from the worldwide decline in the demand for electronic goods beginning in the summer of 2001?
- Seasonal
 - Voluntary
 - Frictional
 - Structural
11. Which of the following policies is specifically designed to reduce the level of structural unemployment?
- a reduction in interest rates
 - a reduction in the level of direct taxation
 - the provision of retraining schemes
 - an increase in the level of state benefit paid to the unemployed
12. Which of the following factors might cause cost-push inflation?
- Factor
- Higher wage levies in domestic industries
 - Higher consumer spending
 - Higher Import prices
- Factor 1 only
 - Factors 1 and 2 only
 - Factors 1 and 3 only
 - Factors 2 and 3 only

13. A government may seek to reduce the rate of demand-pull inflation by any of the following means EXCEPT
- reducing interest rate
 - increasing indirect tax
 - applying more stringent controls over bank lending
 - reducing public expenditure
14. The Keynesian view of inflation is associated with which of the following concepts?
- Rational expectations of inflation
 - Supply side economics
 - The natural rate of unemployment
 - The inflationary gap
15. If a retail price index changed from 250 to 260 over a period of twelve months, this would indicate that
- the standard of living has fallen
 - wages will need to rise by 4% if Incomes are to keep pace with price rises
 - the pattern of consumer expenditure has probably changed during the year
 - the value of money has fallen

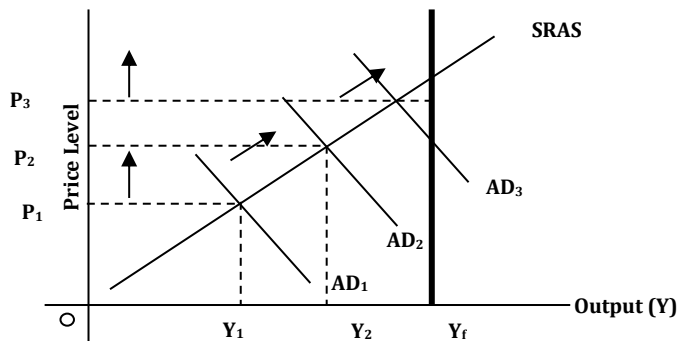
16. Weightings in the Retail Price Index for country T for the year 1992 were as follows:

Food	317
Health	63
Transport and Vehicles	82
Utilities and fuel (water, gas etc)	75
Clothing	116
Housing	109

From this, we can conclude that

- people placed more value on transport than on housing
 - people ate more by volume than they spent on health
 - spending on food has risen faster than spending on any other category
 - people spent a greater proportion of their income on clothing than they spent on any other head
17. Frictional unemployment arises because of
- long term changes in the pattern of demand
 - due to low expected wages
 - transitioning from one job to another
 - certain industries regularly shedding labor at certain times of the year
18. Structural unemployment is best defined as unemployment caused by
- defects in the industrial and commercial structure
 - a long-term decline in a particular industry
 - a mismatch between available jobs and the unemployed
 - a switch from labor-intensive to capital-Intensive production methods

19. Given diagram depicts:



- a) Demand pull inflation
 - b) Cost push inflation
 - c) Hyper inflation
 - d) None of the above
20. According to the views represented by a Phillips curve, which of the following is correct?
- a) Higher inflation causes unemployment
 - b) Higher unemployment causes inflation
 - c) Unemployment and inflation are not related
 - d) Full employment and low inflation cannot be achieved together
21. Which of the following measures would be most consistent with the views of Friedman and other monetarist economists, for reducing the rate of inflation or unemployment?
- a) The government should impose an incomes policy to keep inflation down
 - b) The government can achieve lower unemployment, but only by accepting high levels of inflation
 - c) The government should control the money supply so as to keep output in the economy at a full employment level
 - d) Lower unemployment can be achieved without higher inflation if the government reduces welfare benefits for the unemployed
22. Which of the following measures has NOT been recommended by Friedman and like-minded monetarist economists as a means of reducing the natural rate of unemployment to a lower level?
- a) Measures to stimulate consumer demand for more goods
 - b) Schemes to retrain workers in new job skills
 - c) Measures to cut trade union power
 - d) Restructuring the income tax system
23. All of the following measures might be used by a government to help to control cost-push inflation EXCEPT
- a) a revaluation/appreciation of the currency
 - b) higher direct taxation
 - c) measures to control 'wage drift'
 - d) linking public sector pay increases to productivity improvements

24. Which of the following measures might be used by a government to help to control demand-pull inflation?
 - a) Increasing money supply
 - b) Paying subsidies to farmers for agricultural produce
 - c) Increasing the size of the budget deficit
 - d) Rising interest rates
25. A government might seek to reduce demand-pull inflation by any of the following means EXCEPT
 - a) reducing the rates of GST
 - b) reducing bank lending
 - c) reducing interest rate
 - d) reducing public sector investment
26. Which one of the following measures would be expected to reduce the level of unemployment?
 - a) An increase in GST rate
 - b) On job and off job trainings
 - c) By increasing imports of raw material
 - d) A reduction in investment in the nationalized Industries
27. During a period of war with a neighboring country, government imposes a system of rationing on all consumer goods. This is most likely to result in
 - a) Deflation
 - b) Stagflation
 - c) Hyperinflation
 - d) Suppressed inflation
28. Structural unemployment is best defined as that caused by:
 - a) The long-term decline of particular industries
 - b) The trade cycle
 - c) Insufficient level of aggregate demand
 - d) Seasonal variations in demand for particular goods and services
29. Which of the following actions by the government would be most likely to increase aggregate monetary demand?
 - a) lower wage levels in domestic industries
 - b) Higher consumer spending
 - c) Higher import prices
 - d) None of these
30. If a county's consumer price index changed from 125 to 200 over a period of twelve months, this would - indicate that:
 - a) The standard of living has fallen
 - b) Wages will need to rise by 10% if incomes are to keep pace with price rises
 - c) The pattern of consumer expenditure has probably changed during the year
 - d) The value of money has fallen

31. Phillips curve shows _____ relationship between unemployment and inflation:
- a) Positive
 - b) Inverse
 - c) Moderate
 - d) Unstable
32. Phillips curve demonstrates an inverse relationship between:
- a) Employment and inflation
 - b) Unemployment and interest rate
 - c) Wages and unemployment
 - d) Unemployment and inflation
33. All of the following measure might be used by a government to help to control cost-push inflation except
- a) A revaluation/appreciation of the currency
 - b) Reduce direct taxes
 - c) Measures to control 'wage drift'
 - d) Linking public sector pay increases to productivity improvements
34. Which one of the following measures would be expected to reduce the level of unemployment?
- a) An increase in value added tax
 - b) A higher budget surplus
 - c) Reducing unemployment allowance
 - d) None of these
35. Unemployment caused by long-term changes in the conditions under which an industry operates is called:
- a) Structural
 - b) Seasonal
 - c) Frictional
 - d) Cyclical
36. Inflation caused by a persistent excess of aggregate demand over aggregate supply is called demand push inflation.
- a) True
 - b) False
37. Expectational inflation arises when governments raise interest rates and firms and households anticipate that prices will rise.
- a) True
 - b) False
38. Higher inflation reduces output because the demand for goods falls as prices rise.
- a) True
 - b) False
39. Unemployment always puts pressure on wages to fall.
- a) True
 - b) False

40. The Phillips curve suggests that it may be possible to increase total tax revenue by reducing tax rates.
- True
 - False
41. While inflation has its disadvantages, it also has the advantage of redistributing wealth from rich to poor.
- True
 - False
42. Stagflation is marked with slow economic growth combined with high unemployment leading to economic stagnation with higher inflation and reduced gross domestic product
- True
 - False
43. $\text{Real interest} = \text{Nominal Interest} - \text{Inflation}$
- True
 - False
44. Real wage unemployment also known as classical unemployment.
- True
 - False
45. Frictional unemployment is called short run unemployment.
- True
 - False
46. Which group is most likely to benefit from inflation?
- Debtors
 - Retirement pensioners
 - Salaried officials
 - Unemployed persons
47. Complete the sentence below. _____ unemployment is best tackled by supply side measures. Demand management can only affect _____ unemployment.
- Structural; frictional
 - Frictional; cyclical
 - Structural; cyclical
 - Cyclical; structural
48. _____ would not lead to cost push inflation?
- Rising import prices
 - Increase in wages
 - Increases in indirect taxation
 - High consumer expenditure such that aggregate demand exceeds aggregate supply

49. Vertical Phillips curve shows
- a) No trade off between unemployment and inflation
 - b) Trade off between unemployment and inflation
 - c) Fixed relation between unemployment and inflation
 - d) Infinite relation between unemployment and inflation

ANSWERS TO SELF TEST QUESTIONS

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MONETARY POLICY

1. An economy has underemployed resources. Which method of financing an increase in government expenditure is likely to have the greatest expansionary effect?
 - a) Borrowing from the central bank
 - b) borrowing from the non-bank private sector
 - c) increased direct taxation
 - d) increased indirect taxation
2. With initial deposit of Rs. 1000 million and reserve requirement by central bank is 10%, the total amount of credit creation will be:
 - a) 1000
 - b) 10000
 - c) 100000
 - d) 1000000
3. In the long run, productive potential in an economy grows at an average rate of 3% per year. In particular year actual growth is zero because of a fall in domestic consumption.
What is likely to occur?
 - a) an increase in the rate of inflation
 - b) an increase in the trade deficit
 - c) an increase in unemployment
 - d) a reduction in the government budget deficit
4. A closed economy has a banking system consisting of a single bank. The bank operates with a cash ratio of 10%. Customers deposit Rs.10,000 in cash.
Assuming no subsequent change in notes and coins in circulation what is the maximum amount of loans that the bank can create?
 - a) Rs.1,000
 - b) Rs.9,000
 - c) Rs.90,000
 - d) Rs.100,000
5. Which method of financing a government deficit will leave the money supply unchanged?
 - a) the sale of government securities to the central bank
 - b) the sale of government securities to the commercial banks
 - c) the sale of government securities to domestic residents
 - d) the sale of government securities to overseas residents

6. A financial intermediary is best defined as
 - a) an institution which matches lenders' supply of funds with borrowers' demand for funds
 - b) an institution which operates on the Stock Exchange, matching buyers and sellers of stocks and shares
 - c) an institution which allows firms to obtain equipment from suppliers by providing leasing or hire purchase finance
 - d) None of these
7. Which of the following items will not be found in the assets of a retail bank?
 - a) overdrafts
 - b) bank bills
 - c) customers' deposits
 - d) loans to the money markets
8. A banking system in a small country consists of just five banks. Each bank has decided to maintain a minimum cash ratio of 10%. Each bank now receives additional cash deposits of Rs.1 million. There will now be a further increase in total bank deposits up to a maximum of
 - a) Rs.500,000
 - b) Rs.5 million
 - c) Rs.45 million
 - d) Rs.50 million
9. If all the commercial banks in a national economy operated on cash reserve ratio of 20%. How much cash would have to be deposited with the banks for the money supply to increase by Rs.300 million?
 - a) Rs.60 million
 - b) Rs.75 million
 - c) Rs.225 million
 - d) Rs.240 million
10. If the real rate of interest is 3% pa and the expected rate of inflation is 6% pa, the nominal interest rate will be approximately
 - a) 0.5%
 - b) 2%
 - c) 3%
 - d) 9%
11. Other things being equal, all of the following would lead to a rise in share prices except which one?
 - a) A rise in interest rates
 - b) A reduction in corporation tax
 - c) A rise in company profits
 - d) A decline in the number of new share issues
12. Which one of the following is most likely to result from an increase in the size of the public sector net cash requirement?
 - a) A decrease in the rate of inflation
 - b) A reduction in the level of taxation
 - c) A rise in the price of shares
 - d) A rise in rates of interest

13. The credit multiplier is the process by which:
 - a) An injection of government spending increases national income
 - b) The relationship between the value of a bank's deposits and its cash holdings is governed
 - c) Cash leaks out of the banking system into less formal accumulations
 - d) Government controls the creation of credit
14. Which of the following is a central bank least likely to be responsible for?
 - a) Fixing the general level of interest rates
 - b) Regulating the banking industry
 - c) Determining the public sector borrowing requirement
 - d) Maintaining national reserves of foreign currency
15. Which one of the following is not fundamental to retail banking operations?
 - a) Profitability
 - b) Liquidity
 - c) Security
 - d) Elasticity
16. Which of the following is functions of a central bank?
 - a) Issuing notes and coins
 - b) To reduce tax rate.
 - c) Conducting fiscal policy on behalf of the government
 - d) Holding foreign exchange reserves
17. A financial intermediary is best defined as:
 - a) An institution that matches lenders' supply of funds with borrowers' demand for funds
 - b) An institution that operates on the Stock Exchange, matching buyers and sellers of stocks and shares
 - c) An institution that allows firms to obtain equipment from suppliers by providing leasing or hire purchase finance
 - d) An institution that mints currency
18. Commercial banks are able to create money via the credit multiplier mechanism because they are required to hold adequate deposits with the central bank.
 - a) True
 - b) False
19. When the State Bank of Pakistan is expanding the money supply, ceteris paribus,
 - a) bank lending should increase and interest-sensitive spending should decrease,
 - b) bank lending should decrease and interest-sensitive spending should decrease,
 - c) bank lending should decrease and interest-sensitive spending should increase,
 - d) bank lending should increase and interest-sensitive spending should increase.
20. A financial intermediary is a financial institution through which savers can indirectly provide funds to borrowers
 - a) True
 - b) False

21. Which is/are the function of commercial bank?
- a) Receiving deposits
 - b) To control interest rate
 - c) Note issue
 - d) Provide loan to govt.
22. _____ exists between a customer and a seller, usually in the commercial sector. A purchaser can order a good, receive the good, and then pay for it after a certain period of time.
- a) Advances
 - b) Trade credit
 - c) Bank credit
 - d) None of these
23. Credit creation might increase money supply in the country which may cause inflation.
- a) True
 - b) False
24. Rs.200 million can be created, if the reserve ratio (r) is 5% and initial deposit is Rs. 10 million.
- a) True
 - b) False
25. How much money, banks can create if the reserve ratio (r) is 5% and initial deposit is Rs. 10 million with 3% leakages in an economy.
- Answer: Rs. _____ million
26. Central bank can issue currency notes by keeping a certain percentage of reserves in form of gold, silver or foreign currencies is called fixed fiduciary system.
- a) True
 - b) False
27. If 33% reserve requirement is being followed by the State Bank of Pakistan needs to issue currency notes of worth Rs. 200 million. Hence, it needs to keep a reserve of Rs. _____million:
- a) 66
 - b) 76
 - c) 90
 - d) 81
28. If a government were to pursue an expansionary monetary policy it would
- a) Raise interest rates and sell securities
 - b) Lower interest rates and sell securities
 - c) Raise interest rates and buy securities
 - d) Lower interest rates and buy securities

29. Which of the following is an example of contractionary monetary policy?
- a) A decrease in spending on infrastructure
 - b) An increase in direct taxes
 - c) An increase in interest rates
 - d) A decrease in reserve to be maintained with central bank
30. Which one of the following would lead to an increase in money supply?
- a) An increase in the rate of interest
 - b) Decrease in demand for borrowing from the people
 - c) Sale of government securities by the central bank
 - d) Purchase of government securities by the central bank
31. Monetary assets (M2) in Pakistan refer to
- a) $M2 = C + T$
 - b) $M2 = C + D + T$
 - c) $M2 = C + D$
 - d) $M2 = C + D + T + \text{Shares}$
32. Which one of the following is not a function of a central bank?
- a) The conduct of fiscal policy
 - b) Management of the national debt
 - c) Holder of the foreign exchange reserves
 - d) Lender of the last resort
33. The credit multiplier is the process by which:
- a) An injection of government spending increases national income
 - b) The relationship between the value of a bank's deposits and credit creation
 - c) Cash leaks out of the banking system into less formal accumulations
 - d) Government controls the creation of credit
34. As all commercial banks have accounts with the central bank, when undertaking transactions, they can do so within the central bank, reducing the necessity of issuing and transferring cash is called_____.
- a) Credit rationing
 - b) Clearing agent
 - c) Lender of the last resort
 - d) Banker to the banks
35. A bank has decided to maintain a minimum cash ratio of 5%. The bank now receives additional cash deposits of Rs.10 million. There will now be a further increase in total bank deposits up to a maximum of:
- a) Rs.0.1 million
 - b) Rs.5 million
 - c) Rs.200 million
 - d) Rs.50 million

36. Trade credit exists between a customer and a seller, usually in the commercial sector. A purchaser can order a good, receive the good, and then pay for it after a certain period of time.
- a) True
 - b) False
37. If all the commercial banks in a national economy operated on a cash reserve ratio of 20%, how much cash would have to be deposited with the banks for the money supply to increase by Rs.100 million?
- a) Rs.125 million
 - b) Rs.75 million
 - c) Rs.225 million
 - d) Rs.240 million
38. In Pakistan reserve requirement varies from _____.
- a) 30% - 40%
 - b) 40%-50%
 - c) 50%-60%
 - d) 10%-20%
39. Bank Rate is also called discount rate.
- a) True
 - b) False
40. When a central bank purchases government securities, this will tend to:
- a) Reduce the demand for money
 - b) Reduce the money supply
 - c) Increase the money supply
 - d) Increase the demand for money
41. If interest rates go up, the required rate of return on equities will go _____ and equity prices will _____
- a) Up, rise
 - b) Up, fall
 - c) Down, rise
 - d) Down, fall
42. If the nominal rate of interest is 5% per annum and the annual rate of inflation is 10%, real rate of interest (to the nearest whole number) will be _____?
- a) 2%
 - b) -5%
 - c) 5%
 - d) 7%
43. The government of country A is looking to reduce the supply of money in the economy. Which one of the following would be the best to do it so?
- a) Reducing government expenditure
 - b) Reducing interest rates
 - c) Selling government bonds
 - d) Encouraging banks to lend more

44. The central bank of country Y has adopted a policy of inflation targeting to help control inflation levels in the country. Currently, inflation appears to be above the target level. Which of the following would you most expect to happen as a result of this?
- The bank will raise interest rates
 - The bank will increase the money supply
 - The budget deficit will increase
 - The bank will buy government bonds
45. The central bank in Country K is trying to reduce the growth of money supply and has decided to control bank lending. The central bank has recently imposed a restriction on the amount commercial banks can lend to property companies. This restriction is best described as being an example of
- Quantitative controls
 - A special directive (a direct control)
 - Open market operations
 - Managing reserve requirements
46. If reserve ratio increases from 10% to 20% then credit in the economy will be_____
- increase by 50%
 - decrease by 50%
 - increase by 10%
 - decrease by 5%
47. In regulating supply of money by the State Bank of Pakistan, open market operations include
- Buying & selling bills, bonds & securities in economy
 - Increase or decrease rate of discount
 - Increase or decrease of offer rate by the banks
 - Increase or decrease in reserve requirement for banks

ANSWERS TO SELF TEST QUESTIONS

1	(a)	11	(a)	21	(a)	31	(b)	41	(b)
2	(b)	12	(d)	22	(b)	32	(a)	42	(b)
3	(c)	13	(b)	23	(a)	33	(b)	43	(c)
4	(d)	14	(c)	24	(a)	34	(b)	44	(a)
5	(c)	15	(d)	25	(125)	35	(c)	45	(b)
6	(a)	16	(a)	26	(b)	36	(a)	46	(b)
7	(c)	17	(a)	27	(a)	37	(a)	47	(a)
8	(c)	18	(b)	28	(d)	38	(a)		
9	(b)	19	(d)	29	(c)	39	(a)		
10	(d)	20	(a)	30	(d)	40	(c)		