

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 100 points (to be scaled up to 160 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 10-point question should take 5 minutes. I cannot give extra time because of the class which follows yours.

1) (8 points) Answer ONE of the following three parts.

A) Give an example of cyclical unemployment. Explain why that person would fit that definition of unemployment.

B) Suppose there are only two goods, Mountain Dew and pizza. In 2005, there were 1000 and 500 of each sold respectively at \$0.50/can and \$1.00 per slice. If in 2006, there were 2000 and 400 of each sold respectively at \$0.40/can and \$1.30 per slice, then what would the nominal GDP and real GDP be in 2006 if 2005 is the base year. Show the formula.

C) If the inflation rate is 10% and the nominal interest rate is 32%, then what is the real interest rate? Write the equation used and show all work.

2) (10 points) Answer EITHER Part A OR Part B.

A) Use the table to the right to calculate the marginal tax rate, total tax rate, and the average tax rate for a person who is earning \$100,000 a year. Show all work and if there is no work to show, then explain how you got it.

B) What is meant by tax incidence? Without using a graph, explain why the incidence of a sales tax is not completely the consumer.

Income	Rate
\$0 - \$40,000	10%
\$40,000 - 90,000	20%
\$90,000 - 150,000	30%
\$150,000 and up	40%

3) (10 points) Answer EITHER Part A OR Part B.

A) What is meant by the tax base? Why is it important to know how a policy will affect it?

B) If inflation is 10%, does that mean most people are 10% poorer? Explain your logic.

4) (14 points) Answer EITHER Part A OR Part B.

A) The unemployment numbers may be misleading. Give at least TWO reasons why this is true.

B) The real GDP per capita numbers may be misleading. Give at least TWO reasons why this is true.

5) (16 points) State the problem which is developing with Social Security. For EITHER the proposal in Part A OR the proposal in Part B, explain how that proposal will reduce the problem with social security. Would you use that method? Explain your logic.

A) Increase the social security tax.

B) Have the social security fund buy stocks.

6) (18 points) Answer EITHER Part A OR Part B.

A) If the current CPI is 200 and next year it is 204, and if people had expected 3% inflation, then who will gain and who will lose? Explain your logic stating at least two groups of people who gain and two groups of people who lose.

B) High unemployment has many problems besides reduced production and income. Explain THREE of them.

7) (24 points) Answer EITHER Part A OR Part B.

A) If I gave you GDP = \$1400, depreciation = \$300, net factor payments = \$20, indirect business taxes = \$120, business taxes = \$200, government transfers = \$150, and personal taxes = \$250, then how would you calculate PI? Write the equation or equations you would use. Briefly explain why you added or subtracted each item. You may not use all information.

B) What would GDP be if the following were the only events in the economy? For each item, briefly explain why you added, subtracted, or ignored it. You think the prices of houses in Bethany will rise soon, so you buy a \$123,000 house including \$8,000 in commissions. The government pays \$10,000 in unemployment benefits. A friend of yours buys a \$15,000 new car from Japan. You buy a \$40 shirt made of Egyptian cotton.