

Ministry of Higher Education & Scientific Research
Salahaddin University-Erbil
College of Administration and Economics
Department: Economics
Stage: Third Year
Economic Theories in English
First and second term question bank for the academic year 2021 – 2022

Q1/ What two things does gross domestic product measure? How can it measure two things at once?

A/ GDP measures two things at once: the total income of everyone in the economy and the total expenditure on the economy's output of goods and services. Both of these things are basically the same. For an economy as a whole, income must equal expenditure.

Q2/ How can an economy's income be the same as its expenditure?

A/ Every transaction has two parts to it: a buyer and a seller. If someone spends a dollar, that dollar is an income for someone else.

Example of similar income and expenditure

Example: Karen pays Bill \$100 to mow her lawn. Bill is selling his service, and Karen is buying it. Karen spends \$100, while Bill earned it. The transaction contributes equally to the economy's income and to its expenditure. Whether measured as total income or total expenditure, GDP rises by \$100.

Q/ Which contributes more to GDP - the production of a pound of hamburger or the production of a pound of caviar? Why?

A/ A pound of caviar contributes more to GDP because it costs more than a pound of hamburger. The contribution to GDP is measured by market value and the price of a pound of caviar is much higher than the price of a pound of hamburger.

Q/ What items are not included in the measurement of GDP?

A/ Illegal transactions, such as the black market, sales of stocks and bonds, things produced at home but not sold (cooking, plumbing etc), sale of used goods, value of leisure, social well-being, and pollution and other negative externalities.

Q/ List the four components of expenditure. Which is the largest?

A/ The four components of expenditure are: (1) consumption; (2) investment; (3) government purchases; and (4) net exports. The largest component is consumption, which accounts for more than two-thirds of total expenditure.

Q/ Is buying a house an investment or consumption?

The purchase of a new house is considered an investment. Hopefully, the money you spend on the house will in turn generate you more money when you sell, rent out, or use the house for your financial gain.

Q/ Define real GDP and nominal GDP. Which is a better measure of economic well being? Why?

A/ Nominal GDP is the production of goods and services valued at current prices. Real GDP is the production of goods and services valued at constant prices. Real GDP is a better measure of economic well being because it is corrected for inflation.

Q/ What is our goal in computing GDP?

GDP is used to gauge how well the overall economy is performing. Because GDP measures the economy's production of goods and services, it reflects the economy's ability to satisfy people's needs and desires.

Q/ Why should policy makers care about GDP?

A/ Although GDP is not a perfect measure of well-being, policymakers should care about it because a larger GDP means that a nation can afford better healthcare, better educational systems, and more of the material necessities of life.

Q/ Why is GDP a good measure of economic well being for most-but not all- purposes? GDP includes many things, but it also leaves out a lot of things as well.

Example. 100 people with an annual income of \$50,000 has a GDP of \$5 million. A society in which 10 people earn \$500,000 and 90 suffer still have a GDP of \$5 million, but they are not equivalent.

Q/ What is gross domestic product (GDP) and what is the equation to find it? What are the four components of GDP?

A/ GDP is the market value of all final goods and services produced within a country in a given period of time. GDP consists of consumption (C), investment (I), government purchases (G), and net exports (NX). The equation is as follows:

$$Y = C + I + G + NX$$

Q/ What is the difference between an intermediate good and a final good?

A/ An intermediate good is a good used as an input towards the final product. A final good is a good or service consumed by the end user. An intermediate good is used to make a final good. Example: paper is an intermediate good, and the greeting card is the final good.

Q/ What is the GDP deflator? How can we find it?

The GDP deflator is a measure of the price level calculated as the ratio of nominal GDP to real GDP times 100.

Q/ What is consumption? What are some goods include in consumption?

A/ Consumption is spending by households on goods and services, with the exception of purchases of new housing. Goods that are included in consumption are durable goods, such as automobiles, and appliances, and nondurable goods, such as food and clothing. Some intangible services, including haircuts and medical care are included.

Q/ What is an investment? How is it different than a financial investment?

An investment is spending on capital equipment, inventories, and structures, including household purchases of new housing. Because GDP measures expenditure on goods and services, here the word investment means purchases of investment goods, including capital equipment, inventories, and structures.

Q/ What are government purchases? Are social security payments from the government included?

Government purchases are spending on goods and services by local, state, and federal governments. Social Security, and spending similar to this, is called a transfer payment, because it is not made in exchange for a currently produced good or services. They do not reflect the economy's production. Transfer payments are not counted as part of government purchases.

Q/ What are Net Exports? Give an example that would increase net exports.

A/ Net exports are spending on domestically produced goods by foreigners (exports) minus spending on foreign goods by domestic residents (imports). A domestic firm's sale to a buyer in another country, such as the Boeing sale to British Airways, increases net exports.

Q/ What is Microeconomics?

A/ Microeconomics is the study of how households and firms make decisions and how they interact in markets.

Q/ What is Macroeconomics? What is the goal of macroeconomics?

A/ Macroeconomics is the study of economy wide phenomena, including inflation, unemployment, and economic growth. The goal of macroeconomics is to explain the economic changes that affect many households, firms, and markets simultaneously.

Q/ How are Microeconomics and Macroeconomics closely linked?

Because the economy as a whole is just a collection of many households and many firms interacting in many markets, microeconomics and macroeconomics are closely linked. Demand is just as important to macro as it is to micro.

Q1. Answer the following multiple choice questions (00 points each)

- 1- The measure of the cost of a standard basket of goods and services in any period relative to the cost of the same basket of goods and services in the base year is called the:
- A.cost-of-living indicator.
 - B.consumption production index.
 - C.consumer production index.
 - D.consumer price index.**

D

- 2- The consumer price index for the current year measures the cost of a standard basket in the _____ year relative to the cost of the same basket in the _____ year.
- A.current; base**
 - B.current; current
 - C.base; index
 - D.base; current

a

- 3- The CPI is a measure of the:
- A.real wage.
 - B.price of a specific good or service.
 - C.rate of inflation.
 - D.average level of prices relative to prices in the base year.**

d

- 4- Suppose that the total expenditures for a typical household in 2000 equaled \$2,500 per month, while the cost of purchasing exactly the same items in 2005 was \$3,000. If 2000 is the base year, the CPI for 2000 equals:
- A.0.83
 - B.1.00**
 - C.1.20
 - D.1.25

b

- 5- A CPI that equals 1.34 in 2005 (when 2000 is the base year) means that:
- A.prices in 2005 are 34 percent higher than in 2004.
 - B.the CPI equals \$1.34 in 2005.
 - C.the inflation rate in 2005 is 134 percent.
 - D.the average level of prices is 34 percent higher in 2005 than in the base year.**

d

- 6- In 1929, the CPI equaled 0.171 and in 1930, the CPI equaled 0.167. These data provide evidence of a period of:
- A.inflation.
 - B.deflation.**

- C.trade deficit.
- D.expansion.

b

- 7- The core rate of inflation excludes food and energy prices because:
- A.these prices don't change very frequently.
 - B.these prices are most frequently responsible for short-run fluctuations in the inflation rate.
 - C.consumers do not directly face these prices.
 - D.these prices do not matter to policymakers.

b

- 8- A quantity measured in terms of current dollar value is called a(n) _____ quantity.
- A.nominal
 - B.real
 - C.deflated
 - D.indexed

a

- 9- The price of a gallon of gasoline at the pump increased by 10 percent at the same time that the inflation rate was 15 percent. The nominal price of gasoline _____, and the real price of gasoline _____.
- A.increased; also increased
 - B.increased; decreased
 - C.increased; did not change
 - D.decreased; increased

a

- 10- In New Zealand, population increased from 1 million to 1.1 million, the number of employed workers increased from 500,000 to 600,000, but average labor productivity decreased from \$20,000 per worker per year to \$19,000 per worker per year. Total output in New Zealand _____ and the average standard of living _____. C increased; remained constant
- A.decreased; decreased
 - B.decreased; increased
 - C.increased; increased
 - D.increased; decreased

c

- 11- The wage paid to workers measured in terms of real purchasing power is called the:
- A.nominal wage.
 - B.cost of living.
 - C.minimum wage.
 - D.real wage.

d

- 12- The real wage is the wage:
- A.measured in current dollars.
 - B.required to maintain a minimum standard of living.
 - C.employers are required to pay workers.
 - D.measured in terms of purchasing power

d

13- If workers received a 5 percent wage increase and the rate of inflation was 10 percent, then their real wage:
A.increased.
B.decreased.
C.remained constant.
D.equaled the nominal wage.

b

14- If workers received a 5 percent wage increase and the rate of inflation was 3 percent, then their real wage:
A.increased.
B.decreased.
C.remained constant.
D.equaled the nominal wage.

a

15- A report indicated that the average real wage in manufacturing declined by 2% between 1990 and 2000. If the CPI equaled 1.30 in 1990, 1.69 in 2000, and the average nominal wage in manufacturing was \$35 in 2000, what was the average nominal wage in manufacturing in 1990?
A.\$21.13
B.\$26.40
C.\$26.92
D.\$27.47

d

16- A factory worker earned \$10 an hour in 1980. The CPI was 0.82 in 1980. The same factory worker was earning \$15 an hour in 1990 when the CPI was 1.31. From 1980 to 1990, the factory worker's hourly real wage:
A.increased from \$7.63 to \$18.29.
B.decreased from \$12.20 to \$11.45.
C.remained constant.
D.increased from \$10 to \$15.

b

17- The practice of increasing a nominal quantity each period by an amount equal to the percentage increase in a specified price index is called:
A.a substitution bias.
B.the Fisher effect.
C.deflating.
D.indexing.

d

18- Indexing is the process of:
A.dividing a real quantity by a price index.
B.dividing a nominal quantity by a price index.
C.increasing a nominal quantity by an amount equal to the percentage change in a price index.
D.increasing a real quantity by an amount equal to the percentage change in a price index.

c

19- To ensure that your salary maintains its real purchasing power from year to year, your nominal salary must be:

- A.deflated.
- B.indexed.**
- C.aggregated.
- D.hyperinflated.

b

20- If you wish to maintain a constant purchasing power when you retire, you should choose retirement income options that are:

- A.deflated.
- B.nominal.
- C.indexed.**
- D.inflated.

c

21- _____ is an increase in the price level, while _____ is an increase in the price of one good in comparison to other goods and services.

- A.Inflation; hyperinflation
- B.A relative price increase; inflation
- C.Hyperinflation; inflation
- D.Inflation; a relative price increase**

d

22- Inflation makes it difficult to distinguish relative price changes from changes in the general level of prices. Consequently, inflation _____ the efficiency of the market system.

- A.increases
- B.decreases**
- C.does not change
- D.may either increase or decrease

b

23- Inflation _____ the signals sent by price changes to demanders and suppliers of goods and services.

- A.amplifies**
- B.obscures
- C.enhances
- D.has no impact on

b

24- The phenomenon known as _____ occurs when inflation causes people to pay an increasing percentage of their income in taxes even when their real incomes have not changed.

- A.hyperinflation
- B.bracket creep**
- C.the Fisher effect
- D.substitution bias

b

25- To prevent people paying a higher percentage of their income in taxes even when their real incomes have not changed, Congress:

- A. implemented a flat tax.
- B. reduced the capital gains tax.
- C. indexed the income tax brackets to the CPI.
- D. deflated the income tax brackets to the CPI.

c

26- The shoe leather costs of inflation include all of the following EXCEPT:

- A. the lost purchasing power of cash.
- B. the extra costs incurred to avoid holding cash.
- C. the cost of more frequent trips to the bank.
- D. the installation of a new cash management system.

a

27- The extra costs incurred to avoid holding cash when there is inflation are called the:

- A. average costs of inflation.
- B. consumer price index costs.
- C. external costs.
- D. shoe leather costs

d

28- Making more frequent, but smaller cash withdrawals from banks _____ the inflation losses from holding cash and _____ the shoe leather costs of inflation.

- A. increases; increases
- B. increases; reduces
- C. reduces; has no impact on
- D. reduces; increases

d

29- As the rate of inflation increases, the increased cost to a consumer of more frequent trips to the bank to make cash withdrawals represents an increase in the:

- A. shoe leather costs of inflation.
- B. erosion of the purchasing power of cash.
- C. tax distortion generated by inflation.
- D. "noise" in the price system.

a

30- If workers and employers agree to a three-year wage contract under the expectation of 3% inflation, and inflation turns out to be 5%, then:

- A. workers gain and employers gain.
- B. workers gain and employers lose.
- C. workers lose and employers gain.
- D. workers lose and employers lose.

c

Questions

1- What does per capita GDP tell us about the economy?

Per capita GDP is a measure of the total output of a country that takes gross domestic product (GDP) and divides it by the number of people in the country.

The per capita GDP is useful and measures the differences in the living standards when comparing one country to another.

2- Why are some countries rich and others poor? How did these differences come about? Give an example for each country

United States is an example for the rich country, and Bangladesh and Uganda, Central African Republic (SAR) are an example for the poor countries. The most basic reason that the United States is why rich?

Rich countries have productive workers, better factors of production. Rich countries - they have a lot of physical capital and a lot of human capital, and that capital is organized using the best technological knowledge.

So U.S has high 1- Real GDP per capita, 2- the standard of living and 3- has a greater life expectancy compared to the poor country . In contrast, Bangladesh and Uganda, both of which have a low Real GDP per capita today, and the standard of living and has a shorter life expectancy.

3- Why some countries in the world today has a greater life expectancy than even the richest countries had in 1800?

That's because poor countries have benefited from spillovers from growth in the rich countries. Things like the eradication of diseases like small pox, the creation of antibiotics.

4- What are the key similarities between GDP deflator and CPI?

Both are used to (1) determine price inflation/deflation and (2) reflect the current economic state of a particular nation.

5- What are the key differences between CPI and the GDP deflator?

GDP deflator is not based on a fixed basket of goods and services; the "basket" for the GDP deflator is allowed to change from year to year with people's consumption and investment patterns.

6- What are the limitations of using CPI?

There are some limitations of using CPI such as;

- 1- **Substitution Bias:** When the price of a certain product increases, consumers may start to buy less of it in favor of some cheaper substitute. as the prices of goods and services change from one year to the next, they do not all change by the same amount.
- 2- **New products:** New products constantly enter the market, but they don't become part of the basket of goods used to calculate the CPI until they become common consumer goods. As a result, CPI may fail to account for the price changes of new products when estimating inflation.
- 3- **Quality Changes.**
- 4- **CPI tends to consider insignificant goods,** even the outdated ones that are not really purchased by the consumers anymore.
- 5- **Investment goods are not considered in the CPI:** the prices of other items used in production are not considered as well as the prices of investment goods. Only consumer items are taken into account, the machines and the industrial equipment that are used to make them are not considered.
- 6- Using the table below calculate the CPI for Country C in year 2010 using year 2010 as the base year. And assume the fixed basket is 1 corn and chicken.

Table (3)

Years	Price of corn	Price of chicken
2010	\$ 0.50	\$ 1.00
2011	\$ 1.00	\$ 2.00
2012	\$ 1.50	\$ 3.00

Solution:

$$\text{CPI} = (\$0.50 + \$1) / (\$0.50 + \$1)$$

$$\text{CPI} = 100$$

From previous example, use table 3, to compute the CPI for Country C in year 2011 using year 2010 as the base year.

Solution:

$$\text{CPI} = (\$1 + \$2) / (\$0.50 + \$1) = 200$$

7- What is the percent increase in the price level in Country C from year 2010 to year 2011?

Solution:

$$\text{Percent increase in CPI} = (\text{CPI}_2 - \text{CPI}_1)$$

$$\text{CPI}_1 = [(\$0.50 + \$1) / (\$0.50 + \$1)] \times 100 = 100$$

$$\text{CPI}_2 = [(\$1 + \$2) / (\$0.50 + \$1)] \times 100 = 200$$

$$\text{Percent increase in CPI} = (200 - 100) = 100\%$$

8- What does institution mean? give an example for country that applying good institution and the other who has bad institution?

9- **What would be the incentives to work hard, to invest?**

When effort is not divorced from payment there's very high incentive to work productively. In fact, "You can't be lazy when you work for your family and yourself. So, incentives are important.

10- Why do some countries have good incentives?

Because they have good institutions. So which institutions create incentives that spur prosperity.

Q/ Define the following terms?

- 1- **Purchasing power parity conversions** is the most accurate way we know to compare living standards across different countries.
- 2- **GDP deflator** is a measure of the level of prices of all new final goods and services, domestically produced, in an economy. It is a price index that measures price inflation or deflation.
- 3- **Deflation** is a reduction of the general level of prices in an economy. In other words, deflation is a contraction in the supply of circulated money within an economy, and therefore the opposite of inflation.

- 4- **GDP deflator** can be calculated by dividing Nominal GDP by Real GDP and then multiplying by 100. If expressed mathematically, GDP Deflator = (Nominal GDP/Real GDP) x 100.
- 5- **The consumer price index or CPI** is based on the overall cost of a fixed basket of goods and services purchased by a typical consumer, relative to price of the same basket in some base year.
- 6- **The CPI** is the second approach is a more direct measure than per capita GDP. It measures the cost of living based on the relative cost of a fixed basket of goods and services consumed by household.
- 7- **Institutions include** laws and regulations, including property rights, reliable courts, and political stability. They also mean cultural institutions, including norms around honesty, trust, and cooperation.
- 8- **Rich countries have more factors of production due to** incentive matter.
- 9- **Property rights allow you** to protect your investment
- 10- **Competitive and open markets let** market signals do their work, and they let the farmer innovate and grow her business.
- 11- **Human capital** is tools in the mind or the stuff in people's heads that makes them productive. Human capital - it's not something we're born with. It's produced by an investment in education and training and experience.
- 12-

Translate the following to the Kurdish or Arabic

	bread						
2000	1	80	2	100	280	280	100
2001	2	90	3	200	780	490	159.1837
2002	3	100	4	250	1300	600	216.6667
2003	4	100	5	300	1900	700	271.4286

Q1: Define the following terms:

1- Government purchases,
 Government purchases includes all of the following: social security payments, government employee wages, and tanks purchased by the government.

2-Tradeoffs, 3-Net exports

Q1/ Fill in these brakets?

1-Because every country in the world is faced with scarce (limited) resources, every country must answer three questions: 1- **What goods and services should be produced?** 2- **How should these goods and services be produced?**3- **Who consumes these goods and services ? "For whom?"**

1-There are three goals of macroeconomics. 1-Economic growth, which is the increase in real GDP over time 2- full employment 3- price level stability.

1-A business cycle occurs due to the fluctuations that an economy experiences over time resulting from changes in economic growth.

1- **In general, a business cycle describes changes in the demand-side of the economy as measured by GDP,** where: $GDP = C + I + G + NX$

2-Institutions mean laws and regulations, including property rights, reliable courts, and political stability. They also mean cultural institutions, including norms around honesty, trust, and cooperation.

2- **GDP is the market value of all finished goods and services. A finished good or service is one that will not be sold again as part of some other good.**

2- **GDP is the market value of all finished goods and services. A finished good or service is one that will not be sold again as part of some other good.**

3-Intermediate goods and services will not be counted because they are not finished goods, they will be sold again as part of the other goods.

3-When a bakery buys flour, eggs, and butter, we don't count these sales in GDP because these goods aren't finished.

4- Real GDP per capita is positively correlated with all of the following 1- life expectancy. 2- happiness. 3- education.

4-Real GDP per capita, or per person can be counted by dividing Real GDP by a country's population.

5- Government purchases includes all of the following: social security payments, government employee wages, and tanks purchased by the government. *

5-Purchasing power parity conversions is the most accurate way we know to compare living standards across different countries.

5-GDP can increase through two ways 1- first prices increases2- second .when we produce more valuable goods and services.

5-Honest government is another key institution that allows our farmer to invest. 6-GDP Deflator is a measure of the level of prices of all new final goods and services, domestically produced, in an economy. It is a price index that measures price inflation or deflation.

6- The consumer price index or CPI is based on the overall cost of a fixed basket of goods and services purchased by a typical consumer, relative to price of the same basket in some base year.

7-Deflation is reduction of the general level of prices in an economy. In the other words, deflation is a contraction in the supply of circulated money within an economy, and therefore the opposite of inflation

7-The key differences between CPI and the GDP deflator are GDP deflator is not based on a fixed basket of goods and services; the "basket" for the GDP deflator is allowed to change from year to year with people's consumption and investment patterns.

7- The key similarities between GDP deflator and CPI are (1) determine price inflation/deflation and (2) reflect the current economic state of a particular nation.

7- Financial intermediary is an institution that helps bridge the gap between savers and borrowers.

Q1: Read the following sentences and tick the correct answer (15 Marks)

- 1- Macroeconomics is focused on the movement and trends in the economy as a whole.
- 2- Microeconomics the focus is placed on factors that affect the decisions made by firms and individuals.
- 3- In economics, the term trade-off is often expressed as an opportunity cost, which is the most preferred possible alternative. (✓)
- 4- Making decisions requires trading off one item against another. (✓)
- 5- Although the tractor is used to make other goods, it won't be sold again as part of another good, so the tractor is still a finished good.
- 6- There are also goods that are used to make other goods, but are still considered finished goods. These are called capital goods.
- 7- If a country's nominal GDP increases, it does not mean the country is producing more goods and services.
- 8- GDP can be increased through two ways when first prices increase, second when we do produce more valuable goods and services.
- 9- Real GDP per capita is usually used to compare the standard of living of two different countries.
- 10- Real GDP per capita is usually used to compare the standard of living of one country at different points in time.

11-Government purchases are just the money spent directly by government on goods and services.(✓)

12-In South Korea, the prevailing incentive was for commercial cooperation. If entrepreneurs succeeded, they were **allowed** to earn profit and keep that profit.

13-Rich countries - they have a lot of physical capital and a lot of human capital, and that **capital is organized using the best technological knowledge.**

Q3: What are the differences between Real & Nominal GDP?

- **Q/ What are the limitations of using CPI?**

There are some limitations of using CPI such as;

11- **Substitution Bias:** When the price of a certain product increases, consumers may start to buy less of it in favor of some cheaper substitute. as the prices of goods and services change from one year to the next, they do not all change by the same amount.

12- **New products:** New products constantly enter the market, but they don't become part of the basket of goods used to calculate the CPI until they become common consumer goods. As a result, CPI may fail to account for the price changes of new products when estimating inflation.

13- **Quality Changes.**

14- **CPI tends to consider insignificant goods,** even the outdated ones that are not really purchased by the consumers anymore.

15- **Investment goods are not considered in the CPI:** the prices of other items used in production are not considered as well as the prices of investment goods. Only consumer items are taken into account, the machines and the industrial equipment that are used to make them are not considered.

16- Institutions means **laws and regulations, including property rights, reliable courts, and political stability.** They also mean cultural institutions, including norms around honesty, trust, and cooperation.

Q/ Discuss the life cycle theory of saving by using graph?

Q/ What Do Financial intermediaries (Bank) Do?

Banks attract savings from many different depositors by paying interest on deposits. And the banks make loans for which they charge interest. Banks earn a profit by charging a higher interest rate on the money that they lend, than they pay on the deposits that they receive. They earn this money by being a valuable middleman.

Not only do the banks link savers with borrowers, they evaluate the quality of the borrowers, so that the loans are productive. Imagine that Howard Schultz came looking for a loan of a million dollars to buy a coffee company called Starbucks and transform it into something new.

Bank coordinates the lending of everyone's deposits, and a bank has specialized people and systems to evaluate loan applications. The bank scans the landscape, looking for the most qualified businesses and individuals to receive loans. By pooling the savings of many different individuals, the bank can make large loans, and also spread the risk across a whole portfolio of loans.

1- Why economists find it useful to split GDP into different categories?

A/ Economists find it useful because the forces that determine consumption, investment, and government purchases, they're very different. And if GDP falls, we may be interested in knowing, was that caused by a fall in consumption, investment or government purchase.

1- Why some countries in the world today has a greater life expectancy than even the richest countries had in 1800?

That's because poor countries have benefited from spillovers from growth in the rich countries. Things like the eradication of diseases like small pox, the creation of antibiotics.

2- Why do GDP and GDI differ? and what does that imply?

In national economic accounting, GDP and GDI are conceptually equal, In practice, GDP and GDI differ because they are used different sources of information and they're calculated in very different ways they usually give slightly different results.

Q/ What are the key similarities and differences between GDP deflator and CPI?

Both are used to (1) determine price inflation/deflation and (2) reflect the current economic state of a particular nation.

However, the key differences between CPI and the GDP deflator, GDP deflator is not based on a fixed basket of goods and services; the "basket" for the GDP deflator is allowed to change from year to year with people's consumption and investment patterns.

3- **What are the differences between Real & Nominal GDP ?**

Real GDP

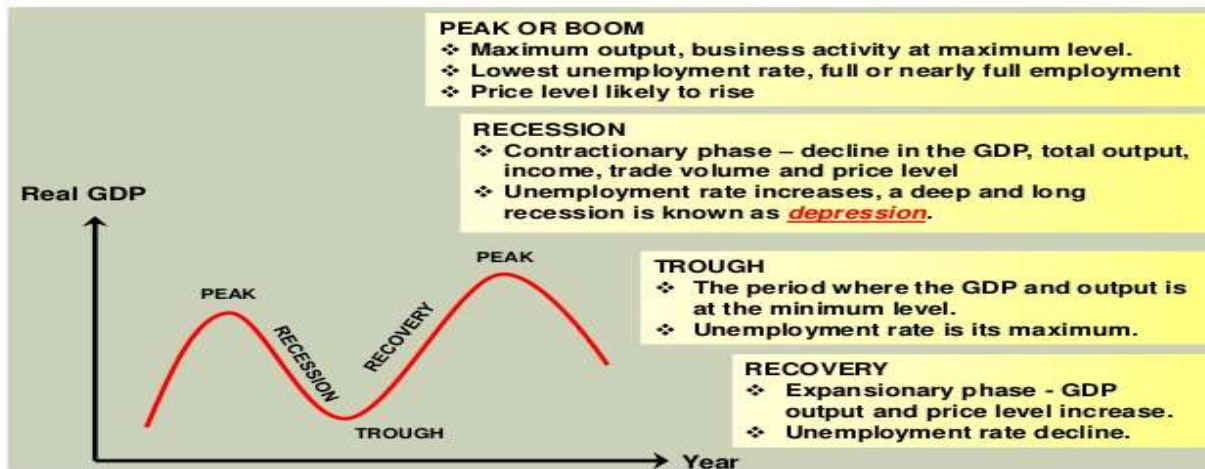
- It is the market value of the all finished goods and services produced within country in a year;
- It takes into account change in the prices (constant prices)
- It controls for inflation
- It uses the same set of the prices over the time

Nominal GDP

- It is the market value of the all finished goods and services produced within country in a year.
- It doesn't take into account change in the prices (current prices)
- It doesn't control for inflation
- It uses different set of the prices over the time

Q/ list and explain the four phases of the business cycle?

PHASES OF BUSINESS CYCLE



Why GDP per capita is far from perfect ?

Is Real Per Capita a perfect measure of the standard of the living?

No, because it misses income distribution, but it is the **best single measure of the average standard of living in a country. Real GDP per capita is correlated with many of the other things like life expectancy, the level of the education, happiness.**

Q4: Translate the following paragraph into Kurdish or Arabic language?

How can the number of people living in abject poverty be so different, when Real GDP per capita is about the same? The reason is that income in Nigeria is much more unequally distributed than in Pakistan or Honduras.

Q2: Why do we use real GDP instead of nominal when comparing economic growth?

Q2: Why do we use real GDP instead of nominal when comparing economic growth?

Q4: Translate the following paragraph into Kurdish or Arabic language?

Overall, Real GDP and Real GDP per capita have proven to be useful measures for comparing the standard of living of two different countries, or for comparing the same country at different points in time.

Q4: Translate the following paragraph into Kurdish or Arabic language?

Overall, Real GDP and Real GDP per capita have proven to be useful measures for comparing the standard of living of two different countries, or for comparing the same country at different points in time.

Q1/ Fill in the following blanks with appropriate words: (12 Marks)

- 1- A business cycle occurs due to -----
-----.
- 2- Because every country in the world is faced with scarce (limited) resources, every country must answer three questions: 1----- 2- -----
---3-----.
- 3- Institutions mean -----
-----.
- 4- Real GDP per capita is positively correlated with all of the following 1----- 2-
---- 3-----.
- 5- The consumer price index or CPI is-----
-----.
- 6- Financial intermediary is -----
-----.

Q2/ Read the following sentences and tick the correct answer (14 Marks)

- 11- Macroeconomics the focus is placed on factors that affect the decisions made by firms and individuals.
- 12- In economics, the term trade-off is often expressed as an opportunity cost, which is the most preferred possible alternative.
- 13- Although the tractor is used to make other goods, it will be sold again as part of another good, so the tractor is not a finished good.
- 14- If a country's nominal GDP increases, it does mean the country is producing more goods and services.
- 15- Real GDP per capita is usually used to compare the standard of living in one country at different points in time.
- 16- Government purchases are just the money spent indirectly by government on goods and services.
- 17- In South Korea, the prevailing incentive was for commercial cooperation. If entrepreneurs succeeded, they were not allowed to earn profit and keep that profit.

1- What are the differences between Real & Nominal GDP ? (10 Marks)

2- List and explain the four phases of the business cycle? (10 Marks)

3- Why do GDP and GDI differ? and what does that imply? (10 Marks)

Q4: Translate the following paragraph into Kurdish or Arabic language?

(14 Marks)

Banks attract savings from many different depositors by paying interest on deposits. And the banks make loans for which they charge interest. Banks earn a profit by charging a higher

interest rate on the money that they lend, than they pay on the deposits that they receive. They earn this money by being a valuable middleman.

Q1/ What are the key similarities and differences between GDP deflator and CPI?

Q2/ Discuss the life cycle theory of saving by using graph?

Q3/ What Do Financial intermediaries (Bank) Do?

Q4: Translate the following paragraph into Kurdish or Arabic language?

Deflation is reduction of the general level of prices in an economy. In the other words, deflation is a contraction in the supply of circulated money within an economy, and therefore the opposite of inflation.

Q1/ Fill in the following blanks with appropriate words: (12 Marks)

- 2- There are three goals of macroeconomics. 1-Economic growth, which is the increase in real GDP over time 2- full employment 3- price level stability.
- 3- **In general, a business cycle describes changes in the demand-side of the economy as measured by GDP**, where: $GDP = C + I + G + NX$
- 4- GDP is the market value of all finished goods and services. A finished good or service is one that will not be sold again as part of some other good.
- 5- The key differences between CPI and the GDP deflator are **GDP deflator is not based on a fixed basket of goods and services; the "basket" for the GDP deflator is allowed to change from year to year with people's consumption and investment patterns.**
- 6- When a bakery buys flour, eggs, and butter, we don't count these sales in GDP because **these goods aren't finished.**
- 7- Purchasing power parity conversions is **the most accurate way we know to compare living standards across different countries.**

Q2: Read the following sentences and tick the correct answer (12 Marks)

- 1- **Microeconomics** is focused on the movement and trends in the economy as a whole. (X)
- 2- **Making decisions requires trading off one item against another.** (✓)
- 3- There are also goods that **are used** to make other goods, but are still considered finished goods. These are called capital goods. (✓)
- 4- GDP can be **decreased** through two ways when first prices increase, second when we do produce more valuable goods and services. (X)
- 5- **Real GDP per capita is usually used to compare the standard of living of two different countries.** (✓)
- 6- Real GDP per capita, or per person can be counted by **dividing Nominal GDP** by a country's population. (X)

1- Why GDP per capita is far from perfect ?

Is Real Per Capita a perfect measure of the standard of the living?

No, because it misses income distribution, but it is the **best single measure of the average standard of living in a country. Real GDP per capita is correlated with many of the other things like life expectancy, the level of the education, happiness.**

2- What are the limitations of using CPI?

There are some limitations of using CPI such as;

- 17- **Substitution Bias:** When the price of a certain product increases, consumers may start to buy less of it in favor of some cheaper substitute. as the prices of goods and services change from one year to the next, they do not all change by the same amount.
- 18- **New products:** New products constantly enter the market, but they don't become part of the basket of goods used to calculate the CPI until they become common consumer goods. As a result, CPI may fail to account for the price changes of new products when estimating inflation.
- 19- **Quality Changes.**
- 20- **CPI tends to consider insignificant goods,** even the outdated ones that are not really purchased by the consumers anymore.
- 21- **Investment goods are not considered in the CPI:** the prices of other items used in production are not considered as well as the prices of investment goods. Only consumer items are taken into account, the machines and the industrial equipment that are used to make them are not considered.

3- Why some countries in the world today has a greater life expectancy than even the richest countries had in 1800?

That's because poor countries have benefited from spillovers from growth in the rich countries. Things like the eradication of diseases like small pox, the creation of antibiotics.

Q4: Translate the following paragraph into Kurdish or Arabic language? (16 Marks)

Bank coordinates the lending of everyone's deposits, and a bank has specialized people and systems to evaluate loan applications. The bank scans the landscape, looking for the most qualified businesses and individuals to receive loans. By pooling the savings of many different individuals, the bank can make large loans, and also spread the risk across a whole portfolio of loans.

البنك ينسق الإقراض للودائع الجميع ويوجد لدى البنك أشخاص متخصصون ونظم لتقييم طلبات القروض . البنك بفحص الأرضية وتبحث عن الشركات والأفراد الأكثر تأهيلا للحصول على لقروض من خلال تجميع مدخرات العديد من الأفراد المختلفين، كما تنتشر المخاطر عبر محفظة كاملة من القروض يمكن للبنك تقديم قروض كبيرة،

Q1/ Fill in the following blanks with appropriate words:

22- Institutions means **laws and regulations, including property rights, reliable courts, and political stability.** They also mean cultural institutions, including norms around honesty, trust, and cooperation.

- 23- In general, a business cycle describes changes in the demand-side of the economy as measured by GDP, where: $GDP = C + I + G + NX$.
- 24- Human capital: refers to knowledge, experience and skills of an employee. It's produced by an investment in education and training and experience.
- 25- Technological knowledge is knowledge about how the world works, such as an understanding of genetics, soil composition, chemistry.
- 26- 1- Human capital 2- physical capital and 3- technological knowledge ; they should be worked together and organized in a way that produces valuable goods and services.
- 27- in a capitalist society, the entrepreneurs (organizer) who bring 1- ideas, 2- people (human capital) and 3- capital (physical capital) together in order to produce valuable products.
- 28- Some countries have good incentives because they have good institutions.
- 29- Property rights allow you to protect your investment.
- 30- The Solow Model draws a distinction between two types of growth: catching up growth and cutting edge growth.
- 31- The marginal product of capital describes how much additional output is produced with each additional unit of capital.

32-

33- The key differences between CPI and the GDP deflator are GDP deflator is not based on a fixed basket of goods and services; the "basket" for the GDP deflator is allowed to change from year to year with people's consumption and investment patterns.

34- When a bakery buys flour, eggs, and butter, we don't count these sales in GDP because these goods aren't finished.

35- Purchasing power parity conversions is the most accurate way we know to compare living standards across different countries.

Japan's and Germany's economic growth after World War II are both examples of

- a. Catching-up growth.
- b. Cutting-edge growth.

The Solow model is a simple model to explain

- a. Economic growth.
- b. Country differences.
- c. Income inequality.

Select the order of symbols below that mimics the following order: human capital, physical capital, ideas.

- a. eL, eK, A
- b. L, A, K
- c. eK, L, A
- d. L, K, eA
- e. eL, K, A

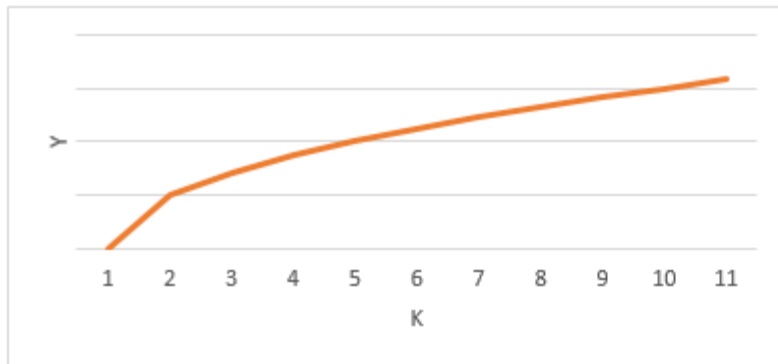
In the equation $Y=f(k)$, Y equals *Correct

- a. Output
- b. Knowledge
- c. Factors of production

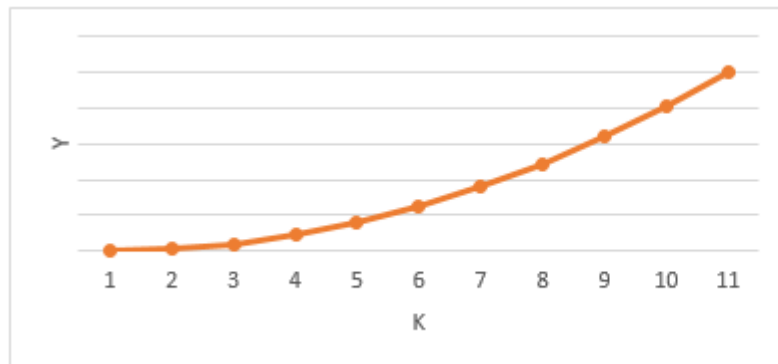
- d. Inputs
- e. A constant
- f. A function

Which of the following graphs best represents the relationship between Y and K in the Solow model? *Correct

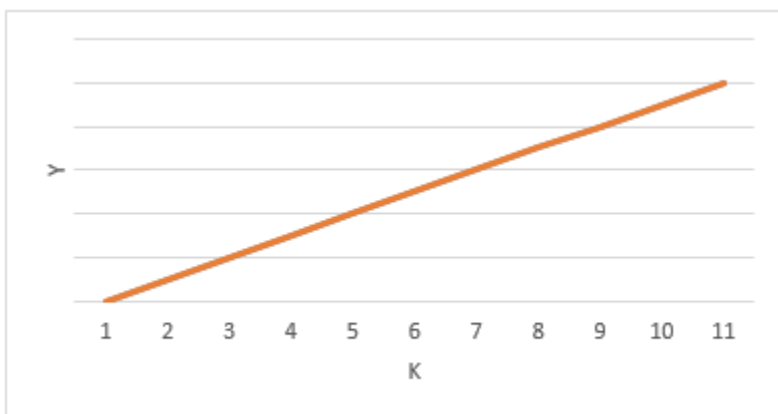
- a.



- b.



- c.



- d. a & b only
- e. Can not be determined from the given information.

For the next two questions, consider the following: Country A has $K=10,000$ and produces GDP according to the following equation: $GDP=5\sqrt{K}$. If the country devotes 25% of its GDP to making investment goods, how much is the country investing? *Incorrect

- a. 12.5
- b. 25
- c. 125
- d. 1,250
- e. Can not be determined with the given information.

If 1% of all machines become worthless every year (they depreciate, in other words) in Country A, GDP is *Incorrect

- a. Increasing.
- b. Decreasing.
- c. In steady state.
- d. Can not be determined with the given information.

Suppose instead that 2% of all machines become worthless every year. In Country A, the capital stock (K) will be *Correct

- a. increasing.
- b. decreasing.
- c. in steady state.
- d. Can not be determined with the given information.

According to the Solow model, when a country is in steady state, *Correct

- a. Depreciation > investment.
- b. Depreciation < investment.
- c. Depreciation = investment.
- d. Depreciation < output.
- e. Depreciation > output.
- f. Depreciation = output.

5- the money for capital accumulation come from

- a. From savings.
- b. From investment.
- c. from saving and investment.
- d. none of these answers.

Q2: Read the following sentences and tick the correct answer (12 Marks)

- 7- Rich countries have more incentives and factors of production. (✓)
- 8-
- 9- Collective property meant that the incentive to invest and to work hard was low. (✓)
- 10- When effort is separated from payment there's very little incentive to work productively. (✓)
- 11- Honest government (transparency and accountability) is another key institution that discourages our farmer to invest. (X)
- 12- Political stability is needed to give investors' confidence to invest. (✓)
- 13- Competitive and open markets let market signals do their work, and they let the farmer innovate and grow her business. (✓)
- 14- It is possible for very poor countries to grow very quickly and to reach their true potential goals, once better incentives and institutions are put into right place. (✓)
- 15- In the past several decades, China has been growing at astonishing rates of growth, 2% per year, doubling only once every 35 years. (X)
- 16- Advanced economies like the United States, Canada, or France, they're growing around 7 to 10% per year. Its income are doubling every 7to 10 years. (x)
- 17- The growth of catching up countries can be much faster than growing on the cutting edge countries. (✓)
- 18- A key part of the solow model is a production function, a simplified description of how resources, inputs, are used to produce output. (✓)
- 19-
- 20-

- 21- GDP can be **decreased** through two ways when first prices increase, second when we do produce more valuable goods and services. (X)
- 22- Real GDP per capita is usually used to compare the standard of living **of two different countries**. (✓)
- 23- Real GDP per capita, or per person can be counted by **dividing Nominal GDP by a country's population**. (X)

4- Why GDP per capita is far from perfect ?

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Q/ what does diminishing rate mean?

A/ when any factor of production, as labor, is increased while other factors, as capital and land, are held constant in amount, the output per unit of the variable factor will eventually **diminish (decrease)**.

Q/ What does the Iron Logic of Diminishing Returns mean?

A/ we can use a simple production function, the square root function.

Output equals the square root of the capital inputs , $GDP = \sqrt{K}$. So if we input 1 unit of capital, output is 1. If we input 4 units of capital, output is 2. If we input 9 units of capital, output is...3. The marginal product of capital describes how much additional output is produced with each additional unit of capital.

the marginal product of the first unit of capital is really high. But as the capital stock grows, the marginal product of capital is less and less and less.

Q/ Why the growth was fast in Germany and Japan after World War II?

Because after the war II those countries didn't have a lot of capital. So that meant that the first units of capital had very high marginal product. Capital's very productive when you don't have a lot of it. While in the case of developed countries, because of the iron logic of diminishing returns, the same additions to the capital stock may get you less and less output.

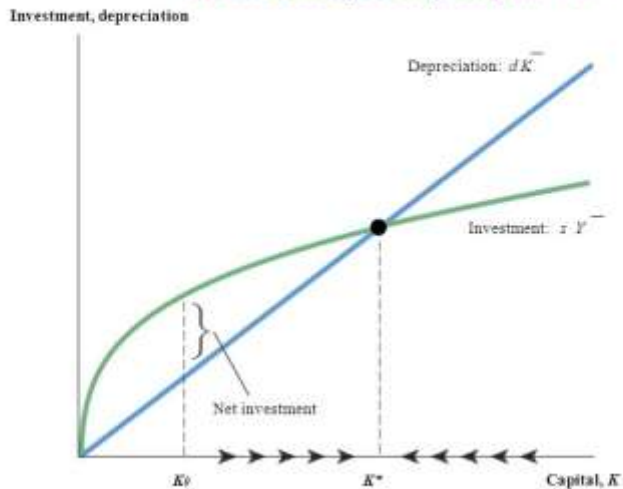
Q/ what is the steady state in the solow growth model ? and use a diagram to explaining it.

If we have the amount of capital on the horizontal axis and the amount of depreciation on the vertical axis. We can then model the relationship like this. Depreciation increases at a constant rate as the capital stock increases. The more capital you have, the more capital depreciation you have.

Notice that our first units of capital, they're very productive and so they create a lot of output and thus also a lot of investment. But as we add more and more units of capital, we get less output and also less investment. That's the iron logic of diminishing returns once again.

The Solow Diagram:

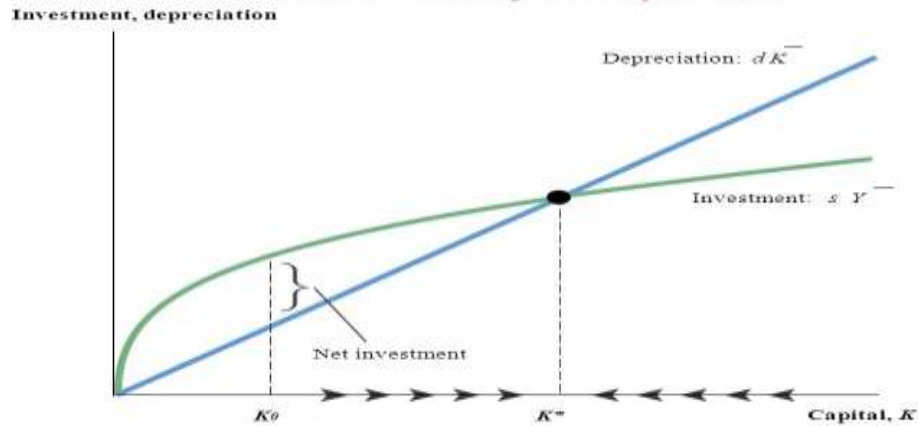
When investment is greater than depreciation, the capital stock increases
The capital stock rises until investment equals depreciation:
At this *steady state* point, $dK = 0$



Now let's put investment and depreciation on the same graph. Depreciation is growing at the same rate as the capital stock grows. Each new unit of capital creates an equal amount of depreciation. Now notice that when investment is greater than depreciation, that means the capital stock must be growing. We're adding more units of capital than are depreciating.

At the Steady-State an investment is equal to depreciation. That means that all of investment is being used just to repair and replace the existing capital stock. No new capital is being created.

The Solow Diagram:
When investment is greater than depreciation, the capital stock increases
The capital stock rises until investment equals depreciation:
At this *steady state* point, $dK = 0$



5- What are the limitations of using CPI?

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