Questions of Final

1. Provide explanation of 4 out of 10 principles of Economics and give some examples about them.
2. Mercedes-Benz Comapany produces cars and sells them in the market. If the price of a certain car model is 10000$, it will sell 200 cars and if the price is 15000$, it will sell 300 cars. What kind of relation exists between these two variables? Draw this correlation in coordinate system (graph line) and show the direction of graph line. Calculate the slope of the grapline.
3. There are 5 pairs of two variables which show the direction of the correlation as follows:

|  |  |
| --- | --- |
| X(price) | Y(quantity) |
| 30  25  20  15  10 | 5  9  13  17  21 |

Assume the budget is 30 dollars and X and Y stands for bread price and quantity of bread respectively. Draw the graph line based on above pairs. Assume that positive shock was happened which increases the budget (1 case) and the person lost his job which was resulted with half loss of previous budget (2 case). How will these shocks affect graph. What will happen on graph if there is change in price?.

1. What are advantages of market economy form centrally planned economy. Does it always achieve efficiency in the economy? Why and why not?
2. Draw production possibility frontier for bread and chewing gum. Using the concept of opportunity cost explain why it most likely has a bowed-out shape. Show the efficient, inefficient and economically infeasible points in the graph and explain them.
3. Economy consists of 4 workers: Azer, Fuad, Leyla and Aynur. Each works 6 hours a day and can produce two goods: butter and copybook. In an hour, Azer can either make 2 butter or make 1 copybook; Fuad can either make 1 butter or 1 copybook; Leyla can make either 3 butter or 2 coppybooks; Aynur can make either 2 butter or 2 copybooks.

1 case - Assume all spend their time making butter.

2 case- Assume all spend their time making copybook.

3 case- All four spends half their time on each activity.

4 case- Azer spends half his time on making butter and others only make copybook.

Draw a production possibility frontier based on above information and show each above case as a single point in frontier. If exist show efficient, inefficient, extreme or infeasible points.

1. What is a normative and positive statement? What are the differences between them? Provide example for each statement.
2. What is tradeoff between equality and efficiency? Explain your answer and provide example about this tradeoff.
3. Draw production possibility frontier for tomato and car production. If there is drought in year, how will it affect the frontier? Explain also the effect of high taxes on car production. If the price of tomato increased dramatically, how the frontier will change?
4. The ABC Enterprises has invested 11 million in new project which has not finished yet. Expected value of this new project is 10 million after completion. It will cost extra 9 million to complete it. Should the Enterprises go ahead and do so? Why and why not?
5. Suppose that T account for the first national bank is as follows:

|  |  |
| --- | --- |
| Assets | Liabilities |
| Reserves 50  Loans 150 | Deposits 200 |

1. If Central government requires banks to hold Reserve Ratio 5%, how much in excess reserves does first national bank now hold?
2. If the first National bank reduce its reserve to only required amount, by how much would the economy`s money supply increase.
3. Explain Functions of Money by providing examples. Moreover, mention the differences between fiat and commodity money.
4. There are total money of 3000$ in the economy. Reserve Ratio is 5% and the number of banks is infinity. What are Money Multiplier and Total Money Supply in the economy?
5. What is Money Multiplier and why do we use it?
6. If we assume there are 5 banks in the economy, what will be the total Money Supply in the economy? Total amount of money in the economy is 900$, Deposits=400 $, Reserve Ratio is 15%. There are no excess reserves that banks hold. People keep 500 $ in their pocket (at home).
7. What tools does the Central Bank use to control money supply in the market. Explain each of them and provide examples.
8. Write quantity equation. For what purpose do we use it? and explain each variable in the equation. What is velocity and how can we derive it?
9. M=100; T=100; P=50; Real GDP=200. Find transaction velocity of money and income velocity of money.
10. 1 case-The Central Bank lowers the reserve requirement to 5%, but banks choose to hold another 5% of deposits as excess reserves. Why might banks do so? What is overall change in the money multiplier and the money supply? 2 Case- If Central Bank sells 1 million of government bonds, what is the effect on the economy´s reserves and money supply?
11. Use the quantity equation for this problem. Suppose the money supply is €200, real output is 1,000 units, and the price per unit of output is €1.

a. What is the value of velocity?

b. If velocity is fixed at the value you solved for in part (a), what does the quantity theory of money suggest will happen if the money supply is increased to €400?

c. Suppose that when the money supply is doubled from €200 to €400, real output grows a small amount (say 2 per cent). Now what will happen to prices? Do prices more than double, less than double, or exactly double? Why?

21. The following questions are related to the Fisher effect.

a. To demonstrate your understanding of the Fisher effect, complete the following table.

|  |  |  |
| --- | --- | --- |
| Real Interest Rate | Nominal interest rate | Inflation rate |
| 3% | 10% | ? |
| ? | 6% | 2% |
| 5% | ? | 3% |

b. Suppose people expect inflation to be 3 per cent and suppose the desired real interest rate is 4 per cent. What is the nominal rate?

c. Suppose inflation turns out to be 6 per cent. What is the actual real interest rate on loans that were signed based on the expectations in part (b)?

d. Was wealth redistributed to the lender from the borrower or to the borrower from the lender when inflation was expected to be 3 per cent, but in fact, turned out to be 6 per cent?

1. Explain the difference between nominal and real variables and give two examples of each. According to the principle of monetary neutrality, which variables are affected by changes in the quantity of money?
2. Explain seigniorage problem? Moreover, mention costs and benefits of inflation.
3. Suppose that the reserve requirement for demand deposits is 10% and that banks do not hold any excess reserves.
4. If the Central government sells 1 thousand of government bonds, what is effect on the economy´s reserves and money supply?
5. Central Banks lowers the reserve requirement to 5 %, but banks choose to hold another 5 percent of deposits as excess reserves. Why might banks to so? What is overall change in the money multiplier and the money supply?
6. What is called the deviation from classical dichotomy and the Fischer effect? How might you decide whether this deviation is important in practice?
7. What is Net Capital Outflow? Why does NCO always equal to Net Export Level (explain it with one example)? Explain some important variables that influences net capital outflow.
8. Consider 3 different possibilities for economy: a country with a trade deficit, a country with balanced trade and country with a trade surplus. Explain possible outcomes for these three economic conditions. (What is level of export, import, national Income, Investment, saving, Net Capital outflow)
9. Assume that Germany sells Machine X for 100 Euros, while Azerbaijan sells the same machine for 125 Manats. Nominal exchange rate 1 euro is 1.2 manat. Assume there are no transportation or transaction costs. Find real exchange rate and interpret it. Explain the arbitrage strategy if it exists. Explain how may the presence of transportation costs affect the arbitrage?
10. A bottle of wine costs 20 Lari in Georgia and 15 manat in Azerbaijan. What would be lari-manat exchange rate if purchasing parity holds? IF Monetary expansion in Georgia doubled all price in the economy, while the all prices in Azerbaijan economy increased 15 %, what would be lari-manat exchange rate? Or assume the all prices in Georgia decreased 35 % and all prices increased in Azerbaijan by 28%. In this situation how will lari-manat exchange rate change?
11. Would each of the following groups be happy or unhappy if Azerbaijan Manat appreciated? Explain your answer for each group.
12. Dutch Pension Fonds holding Azerbaijan Government Bonds

b) Azerbaijan manufacturing Industries

c) European tourists planning a trip to Baku

d) Azerbaijan firm trying to purchase property in Europe

32. Explain Basic Logic and limitations of Purchasing Power Parity.

33. Explain demand and supply side of Market for Loanable Funds and Market for Foreign-Currency Exchange. Draw diagram for both markets. By using these market draw a diagram that shows Equilibrium in the Open Economy.

34. Explain the effect of Excess government revenue on the Equilibrium of Open Economy by help of diagrams. How were the key variables in both markets affected with this abnormal excess revenue? What will happen to interest rate, NCO, real exchange rate and NX? Explain your answer

35. Assume Azerbaijan Government ceases (stops) all import quotas and tariffs in country and follow open trade policy. Explain the effect of this on the Equilibrium of Open Economy by help of diagrams. How were the key variables in both markets affected? What will happen to interest rate, NCO, real exchange rate and NX? Explain your answer

36. Assume Azerbaijan Government imposes strict tariffs and import quotas. Explain the effect of this on the Equilibrium of Open Economy by help of diagrams. How were the key variables in both markets affected? What will happen to interest rate, NCO, real exchange rate and NX? Explain your answer

37. Suppose the Azerbaijan Government is considering an investment tax credit, which subsidize domestic Investment.

a) How does this policy affect national saving, domestic investment, net capital outflow, the trade balance?

b) Representatives of several large exporters oppose the policy. Why might that be the case?

38. If people in Azerbaijan decides to spend smaller fraction of their income. What would be effect on saving, investment, interest rates, the real exchange rate, and the trade balance? Explain effects on diagrams.

39. What is capital flight? What is the possible reason for it? Discuss the effect of capital flight on interest rate and exchange rate.

40.What is nominal and real exchange rate? What is appreciation and depreciation? Explain separately their impact on Net Export level

41. Which contributes more to GDP-the production of an economy car or the production of Luxury car? Why? And also mention the components of GDP.

42. What is Economic Fluctuation? And Explain three key facts about Economic fluctuations.

43. Explain two causes of Economic Fluctuations by applying Aggregate Demand and Supply Model (use diagram).

44. Discuss the 3 theories that explain upward sloping of short-run aggregate supply curve.

45. For each of the following events, explain the short-run and long-run effects on output and the price level, assuming government takes no action,

- The consumer wealth decreased sharply

- Government increases spending

- Natural disaster happened

46. Explain graphically the effect of a Shift in Aggregate Demand (both left and right).

47. Explain graphically the effect of a Shift in Aggregate Supply (both left and right).

48. Why Aggregate Supply Curve is Vertical in Long-run? Explain the variables that may shift Supply Curve.

49. Discuss some factors that may shift Aggregate-Demand Curve Shift. (Hint: think about components of GDP)

50. List and explain the three reasons the aggregate demand curve is downward sloping.

51. Explain the effect of the following events on short and long run equilibrium:

- Azerbaijan experiences a wave of immigration

- Invention of more productive technology

- Increase in Money Supply.

52. The country X has collected the following information:

Population – 240000; Employed people – 180000; Unemployed – 20000

Calculate Labor Force, Unemployment Rate and Labor-Force Participation Rate. And also explain theoretically the differences between Unemployment Rate and Labor-Force Participation rate.

53. Are the following workers more likely to experience short-term or long-term unemployment? Why? Explain

a) A construction worker laid-off because of bad weather

b) A manufacturing worker who loses her job at a plant in an isolated area.

c) A stagecoach industry worker laid off because of competition from railroads

d) An expert with little formal education loses his job when company installs new production process.

54. Suppose Azerbaijan government passes a law requiring employers to provide employees some benefit that raises the cost of an employee by $4 per hour.

a) How will this law affect labor demand?

b) If employees place a value on this benefit exactly equal to its cost, what will happen to the supply of labor?

c) Suppose that wage in this market was $3 above the minimum wage before this law. How does this law affect the wage and the level of unemployment? Who is better off or worse-off?

55. By using the diagram of labor market, discuss the effect of an increase in the minimum wage on the wage paid to workers, the labor supply, the number of workers demanded and the amount of unemployment.

56. Assume that the economy has two sectors – one manufacturing and the other one is service. Suppose initially that the workers of both sectors are not unionized.

A) If manufacturing workers formed a union, what impact on the wages and employment in manufacturing sector would you predict?

B) How would these changes in manufacturing labor market affect the supply of labor in the market for service workers? What would happen to the equilibrium wage and employment in this labor market?

57. The Azerbaijan Statistics Committee announced that in November 2015, all employed adults are

4.530.000, unemployed is 503000 and 3.510.000 (500. 000 of them are children) was not in the labor

force. Using this information

Calculate: the adult population, the labor force, the labor-force participation rate, the unemployment rate.

58. Explain the 3 reasons for structural Unemployment. Discuss separately each of them.

59. What are reasons for the efficiency wages? And discuss consequences of this Efficiency wages on the labor market by the help of diagram.

60. You visited the government unemployment office for every month for a year to survey unemployed. Each week you find that there are 16 unemployed workers. The 11 of them are the same individuals for the whole year, while the rest changes every month. Based on this experience, would you say that unemployment is typically short-term or long-term?

61. What types of unemployment do we observe in the labor market? Explain each of them. And also discuss briefly the natural rate of unemployment.

62. Suppose the natural rate of unemployment is 9 %. On one graph, draw two Phillips curves that can be used to describe the four situations. Label the point that shows the position of the economy in each case:

a) Actual inflation is 7% and expected inflation is 3%.

b) Actual inflation is 4% and expected inflation is 7%.

c) Actual inflation is 4% and expected inflation is 4%.

d) Actual inflation is 7% and expected inflation is 7%.

63. Illustrate the effects of the following events on both the short-run and the long-run Phillips curves. Give the economic reasoning for each following events.

A) Increase in the natural rate of unemployment

B) A decrease in the price of production factors

64. Illustrate the effects of the following events on both the short-run and the long-run Phillips curves. Give the economic reasoning for each following events.

A) Decrease in expected Inflation

B) Increase in the price of imported oil

65. Assume that Y=500L, which is aggregate production function. Y is real GDP of Azerbaijan and L is the number of employed labor. Labor force is 150 people and Output is 60000 AZN. Price is given as 100 AZN.

a) What is the natural rate of unemployment?

b) Assume that in the next year fiscal expansion increased aggregate demand curve and it shifted to the right. And price id 102 AZN and quantity of output produced is 70000AZN. Find the natural rate of unemployment and inflation rate.

66. What is the equation of a typical short-run Phillips curve? What does it imply about the relation between the inflation rate and the unemployment rate in the short-run? What is the effect of an increase and decrease in expected inflation? Explain by help of diagrams.

67. Suppose that expected inflation is 2% and the labor force is 900.000 and employed people is 800000. And the natural rate of unemployment is 5%. a is 0.09. Find the actual inflation. But what will happen in the long-run?

68. Suppose the price of oil falls sharply. Show the impact of such a change in both aggregate demand/ aggregate supply diagram and in the Phillips curve diagram. What happens to inflation and unemployment in the short-run?

69. Explain the long-run Phillip curve. According to what theory can we explain this vertical curve?

70. Explain the equation of the short-run Phillips curve, which was proposed by Friedman and Phelps. Discuss each variable in the equation. What will happen to this equation in the long-run?

71. How does Fiscal Policy influence Aggregate Demand? Mention some tools that are used by government (use diagram analysis).

72. What is Multiplier effect on Aggregate Demand curve? Explain difference between Multiplier Effect and Crowding-out Effect?

73. Assume that Azerbaijan government increases government purchase by 10 million Manat. There is no crowding-out effect and marginal propensity to consume is 4/20.

a) What is initial effect of increase in government purchase on Aggregate demand curve?

b) What additional effects follow this initial effect? What is the total effect of the tax cut on Aggregate Demand?

74. Assume that Azerbaijan government increases government purchase by 15 million Manat. There is no crowding-out effect and marginal propensity to consume is 25/30. The crowding out effect is 1.5 million manat.

a) What is initial effect of increase in government purchase on Aggregate demand curve?

b) What additional effects follow this initial effect? What is the total effect of the tax cut on Aggregate Demand?

75. Discuss that how does increase or decrease in Money demand or Money supply affect Aggregate demand curve?

The Central Bank expands the money supply by 5%.

a) Use the theory of liquidity preference in order to illustrate graphically the effect of this policy on the interest rate.

b) Use the model of aggregate demand and aggregate supply to illustrate the impact of this change in the interest rate on output and the price level in the short-run.