Georgia Assessments for the Certification of Educators®

GACE® Study Companion

Economics Assessment

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About the Assessment

Assessment Name	Economics
Grade Level	6–12
Test Code	Test I: 038 Test II: 039 Combined Test I and Test II: 538
Testing Time	Test I: 2 hours Test II: 2 hours Combined Test I and Test II: 4 hours
Test Duration	Test I: 2.5 hours Test II: 2.5 hours Combined Test I and Test II: 5 hours
Test Format	Computer delivered
Number of Selected-response Questions	Test I: 80 Test II: 80 Combined Test I and Test II: 160
Question Format	The test consists of a variety of short-answer questions such as selected-response questions, where you select one answer choice or multiple answer choices (depending on what the question asks for), questions where you enter your answer in a text box, and other types of questions. You can review the possible question types in the ***Guide to Taking a GACE Computer-delivered Test***.
Number of Constructed-response Questions	Test I: 0 Test II: 0 Combined Test I and Test II: 0

The GACE Economics assessment is designed to measure the professional knowledge of prospective teachers of secondary school Economics in the state of Georgia.

This assessment includes two tests. You may take either test individually or the full assessment in a single session. The testing time is the amount of time you will have to answer the questions on the test. Test duration includes time for tutorials and directional screens that may be included in the test.

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

The questions in this assessment assess both basic knowledge across content areas and the ability to apply principles.

The total number of scored questions is typically lower than the total number of questions on the test. Most tests that contain selected-response questions include embedded pretest questions, which are not used in calculating your score. Including pretest questions in the assessment allows ETS to analyze actual test-taker performance on proposed new questions and determine whether to include them in future versions of the test.

Content Specifications

Each test in this assessment is organized into content **subareas**. Each subarea is further defined by a set of **objectives** and their **knowledge statements**.

- The objectives broadly define what an entry-level educator in this field in Georgia public schools should know and be able to do.
- The knowledge statements describe in greater detail the knowledge and skills eligible for testing.
- Some tests also include content material at the evidence level. This content serves as descriptors of what each knowledge statement encompasses.

See a breakdown of the subareas and objectives for the tests in this assessment on the following pages.

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Test I Subareas

Subarea	Approx. Percentage of Test
I. Fundamental Economic Concepts	20%
II. Microeconomics	80%

Test I Objectives

Subarea I: Fundamental Economic Concepts

Objective 1: Demonstrates an understanding of the fundamental concepts of economics

The beginning Economics teacher:

A. Understands the concepts of scarcity, choice, and opportunity cost

B. Identifies and describes the factors of production (e.g., land, labor, physical capital, human capital, entrepreneurship) and gives an example of each

C. Understands how changes in marginal costs and marginal benefits affect decision making

D. Understands how the production possibility curve is used to illustrate trade-offs, economic efficiency, economic inefficiency, and economic growth

E. Understands how specialization increases productivity and results in greater output of goods and services

F. Understands that both buyers and sellers gain from specialization and voluntary exchange

G. Compares command, market, and mixed economic systems with regard to ownership and allocation of resources

H. Understands how each type of system answers the three economic questions of what, how, and for whom goods and services are produced

I. Understands how each system addresses broad social and economic goals such as growth, equity, and stability

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Subarea II: Microeconomics

Objective 1: Demonstrates an understanding of supply and demand and elasticity

The beginning Economics teacher:

A. Understands how the simple circular-flow model is used to describe how households and businesses interact through the product and factor markets

B. Understands the law of supply and the law of demand and how they are illustrated, using supply and demand curves

C. Understands how the supply-and-demand graph is used to determine equilibrium price and quantity in a competitive market

D. Understands how prices guide the allocation of resources and the production and distribution of goods

E. Understands how competitive markets eliminate surpluses and shortages

F. Identifies the determinants of market supply and demand, and understands how changes in the determinants of supply and demand affect the market equilibrium

G. Understands the distinction between a shift of the supply or demand curves versus a movement along the supply or demand curves

H. Understands the concepts of consumer and producer surpluses and how they are used to measure the benefits and costs of price changes

I. Understands how the concepts of total utility and marginal utility are used to explain consumer choices

J. Defines the price elasticity of supply and the price elasticity of demand, and understands how to calculate them

K. Understands the different classifications of elasticity such as elastic and inelastic supply and demand curves

L. Understands the relationship between total revenue and elasticity of demand

M. Identifies and explains the factors affecting the price elasticity of supply and demand

N. Understands the concept of income elasticity of demand and how it is used to distinguish between normal and inferior goods

O. Understands the concept of cross-price elasticity of demand and how it is used to identify whether two goods are substitutes or complements

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Objective 2: Demonstrates an understanding of the impacts of government intervention in markets

The beginning Economics teacher:

A. Understands how the graph of supply and demand is used to analyze the impact of price floors or price ceilings
B. Understands how the graph of supply and demand is used to analyze the effects of taxes and subsidies on the equilibrium market price and quantity
C. Understands how the existence of public goods, externalities, and income distribution causes market failure
D. Understands how the government attempts to remedy market failure to improve the allocation of resources
E. Understands why government protects property rights
F. Gives examples of government regulation and deregulation and their effects on consumers and producers
G. Understands the meaning of progressive, regressive, and proportional taxes and their effects on household income

Objective 3: Demonstrates an understanding of the concepts of production, cost, and market structures

The beginning Economics teacher:

A. Identifies and compares the three forms of business organization
B. Understands the role of profit as an incentive for entrepreneurs
C. Understands the relationship among revenues, costs, and profits
D. Understands the difference between explicit and implicit costs
E. Understands the relationships between inputs and outputs (production function, total product, and marginal product)
F. Understands the distinction between the short run and the long run
G. Understands the law of diminishing marginal returns
H. Understands the relationships among the various cost measures; e.g. total cost, total variable cost, total fixed cost, average total cost, average variable cost, average fixed cost, and marginal cost
I. Understands long-run costs and the concept of economies of scale
J. Understands the concept of derived demand for a factor of production, such as labor
K. Understands how equilibrium wages and employment are determined in a competitive labor market

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

L. Understands how changes in labor demand and labor supply affect equilibrium wages and employment

M. Understands and illustrates on a graph how firms choose the profit-maximizing price and output using the marginal cost and marginal revenue analysis

N. Identifies the characteristics of perfect competition, and understands and illustrates on a graph how individual firms determine output to maximize profit

O. Identifies the characteristics and sources of monopolies, and understands and illustrates on a graph how a monopoly determines output and price to maximize profit

P. Compares a monopoly to a perfectly competitive market with respect to price, output, and allocative efficiency

Q. Identifies the characteristics of monopolistic competition and compares them to other market structures

R. Identifies the characteristics of an oligopoly and compares them to other market structures

S. Understands the role of profits in motivating entry into or exit from a market in the long run

Test II Subareas

Subarea	Approx. Percentage of Test
I. Macroeconomics	64%
II. International Economics	20%
III. Personal Finance	16%

Test II Objectives

Subarea I: Macroeconomics

Objective 1: Demonstrates an understanding of the measures of economic performance

The beginning Economics teacher:

A. Understands how the expanded circular flow model is used to describe the economic transactions that occur among the major sectors of the economy — households, businesses, government, and the rest of the world — as they interact through the product markets, factor markets, and financial markets

B. Understands the macroeconomic goals for an economy, including economic growth, full employment, and price stability

C. Understands how gross domestic product (GDP) is defined and the different approaches used to measure GDP

D. Understands the shortcomings of GDP as a measure of output and standard of living

E. Understands the components of GDP, including consumption, investment, government purchases, and net exports

F. Understands the distinction between nominal and real GDP

G. Defines inflation and understands how it is measured using the consumer price index (CPI)

H. Understands the distinction between nominal and real values for variables such as wages and interest rates

I. Understands how inflation may benefit or hurt various groups of people

J. Defines unemployment and understands how it is measured

K. Understands the distinction among various types of unemployment; e.g., structural, cyclical, and frictional

L. Understands the concept of the natural rate of unemployment

M. Defines the business cycle and explains the phases of the cycle

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

N. Defines the aggregate demand curve and its components, and understands the factors that shift the aggregate demand curve

O. Understands the distinction between short-run and long-run aggregate supply and explains their determinants

P. Understands how the aggregate supply and aggregate demand model is used to determine equilibrium price level and output in the short run and in the long run

Q. Understands how employment is related to real GDP

R. Understands how inflationary and recessionary gaps are defined in the context of the aggregate supply and aggregate demand model

Objective 2: Demonstrates an understanding of fiscal policy, monetary policy, and economic growth

The beginning Economics teacher:

A. Identifies the major sources of revenue for the federal government and the major categories of government spending

B. Understands the concept of marginal propensity to consume and how it is used to calculate the spending multiplier and the tax multiplier

C. Defines fiscal policy and understands how changes in government spending and taxes are used to promote price stability, full employment, and economic growth

D. Understands the distinction between expansionary and contractionary fiscal policies and the mechanism by which each can affect price level, output, and employment

E. Understands the distinction between discretionary fiscal policy and automatic stabilization

F. Understands the distinction between the national debt and government deficits

G. Understands the structure and composition of the financial system

H. Understands the structure and the functions of the Federal Reserve System

I. Understands the definition and the functions of money

J. Understands the different measures of the money supply

K. Understands how banks create money and the concept of money multiplier

L. Understands how equilibrium is determined in the money market

M. Defines monetary policy and understands how the Federal Reserve Bank uses the tools of monetary policy to promote price stability, full employment, and economic growth

N. Understands the distinction between expansionary and contractionary monetary policies and the mechanism by which each can affect price level, output, and employment

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

O. Understands the meaning of productivity

P. Understands the concept of economic growth and explains the determinants of economic growth

Q. Understands the relationship among savings, investment, and economic growth

R. Understands government policies designed to promote economic growth

Subarea II: International Economics

Objective 1: Demonstrates an understanding of the fundamental concepts of international trade and capital flows

The beginning Economics teacher:

A. Understands the distinction between absolute advantage and comparative advantage

B. Understands how opportunity costs are used to determine comparative advantage given production possibility curves for different countries

C. Understands how comparative advantage is used to determine specialization and the direction of trade among countries

D. Understands how specialization and trade lead to gains and interdependence

E. Understands the difference between trade deficits and trade surpluses

F. Understands how a country uses trade barriers to restrict free trade; e.g., tariffs, quotas, embargoes, and standards

G. Understands the costs and benefits of trade barriers

H. Understands the arguments for and against free trade

I. Understands why trading blocs exist, and give examples of them; e.g., the EU, NAFTA, and ASEAN

J. Understands the roles of international organizations; e.g., World Bank, IMF, and WTO

K. Understands how a country's balance of payments is used to record its international transactions in trade and finance

L. Understands the relationship between the current account balance and financial account balance in a country's balance of payments

M. Defines the exchange rate of a currency and understands how it is determined under a fixed exchange-rate system and a flexible exchange-rate system

N. Understands how to calculate an exchange rate from a set of data and determine whether the currency has appreciated or depreciated

O. Understands the effect of currency appreciation or depreciation on a country's exports, imports, and trade balance

P. Understands the causes of financial capital inflows and outflows

Q. Understands who gains and who loses from currency appreciation or depreciation

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Subarea III: Personal Finance

Objective 1: Demonstrates an understanding of the fundamentals of household spending, saving, and investment behavior

The beginning Economics teacher:

A. Understands the impact of investment in education, training, and skill development on an individual's earnings

B. Understands how people respond to incentives with respect to saving, investing, and spending decisions

C. Understands how changes in fiscal and monetary policies affect an individual's income and spending and saving choices

D. Understands how an increase in sales tax affects different income groups

E. Understands the roles of different types of financial institutions in saving and financial investment

F. Understands the role of a bank as a financial intermediary between savers and investors.

G. Understands the relationship between risk and return

H. Understands the difference between savings and financial investment instruments, including stocks, bonds, and mutual funds

I. Understands how insurance and other risk-management strategies protect against financial losses

J. Understands the factors that affect credit worthiness

K. Understands the difference between simple and compound interest rates

L. Understands the concept of the time value of money; e.g., present value and future value

M. Compares the advantages and disadvantages of variable and fixed interest-rate loans

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Practice Questions

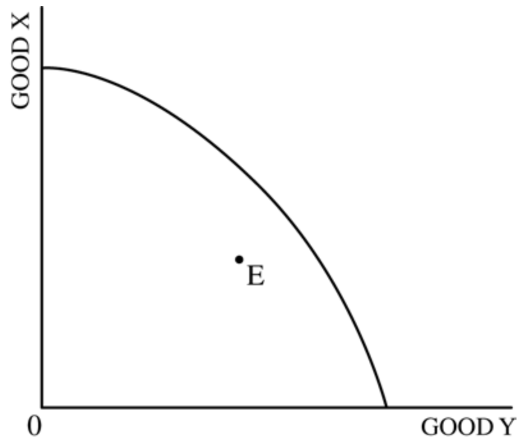
The practice questions in this study companion are designed to familiarize you with the types of questions you may see on the assessment. While they illustrate some of the formats and types of questions you will see on the test, your performance on these sample questions should not be viewed as a predictor of your performance on the actual test. Fundamentally, the most important component in ensuring your success is familiarity with the content that is covered on the assessment.

To respond to a practice question, choose one of the answer options listed. Be sure to read the directions carefully to ensure that you know what is required for each question. You may find it helpful to time yourself to simulate actual testing conditions. A correct answer and a rationale for each sample test question are in the section following the practice questions.

Keep in mind that the test you take at an actual administration will have different questions, although the proportion of questions in each subarea will be approximately the same. You should not expect the percentage of questions you answer correctly in these practice questions to be exactly the same as when you take the test at an actual administration, since numerous factors affect a person's performance in any given testing situation.

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Directions: Each of the questions or incomplete statements below is followed by four suggested answers or completions. Select the one that is best in each case.



1. The diagram above shows the production possibilities curve for an economy. Which of the following is true if the economy is currently producing at point E?

   A. It is producing the maximum possible output given the scarcity of resources
   B. It is devoting more of its resources to producing Good Y
   C. It is not using its resources fully and efficiently
   D. It can increase the production of Good X only if it decreases the production of Good Y

Answer and Rationale

2. In a command economy, resource allocation is managed primarily by

   A. large corporations.
   B. labor unions.
   C. competitive markets.
   D. central planning.

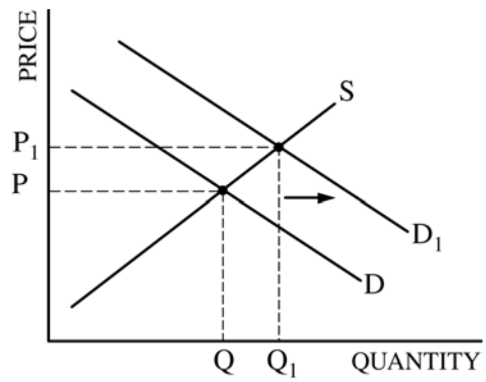
Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

3. When the opportunity cost ratios for two individuals performing a particular task differ, a basis for specialization and mutually beneficial trade exists. The specialization will be based on which of the following?

A. Comparative advantage
B. Absolute advantage
C. Price elasticity
D. Equilibrium

Answer and Rationale



4. What will happen to the equilibrium price and quantity if the demand curve shifts from D to D_1 in the market described by the graph above?

	Equilibrium Price	Equilibrium Quantity
A.	Increase	Decrease
B.	Increase	Increase
C.	Not change	Increase
D.	Increase	Not change

Answer and Rationale

Note: After clicking on a link, right click and select “Previous View” to go back to original text.

5. If marginal utility increases as more of a good is consumed, what happens to total utility?

   A. Total utility decreases at an increasing rate
   B. Total utility decreases at a decreasing rate
   C. Total utility increases at an increasing rate
   D. Total utility increases at a decreasing rate

Answer and Rationale

6. An increase in the price of smartphones will result in

   A. an increase in total revenue for producers if the demand for smartphones is elastic.
   B. an increase in total revenue for producers if the demand for smartphones is inelastic.
   C. a decrease in the demand for smartphones.
   D. an increase in the supply of smartphones.

Answer and Rationale

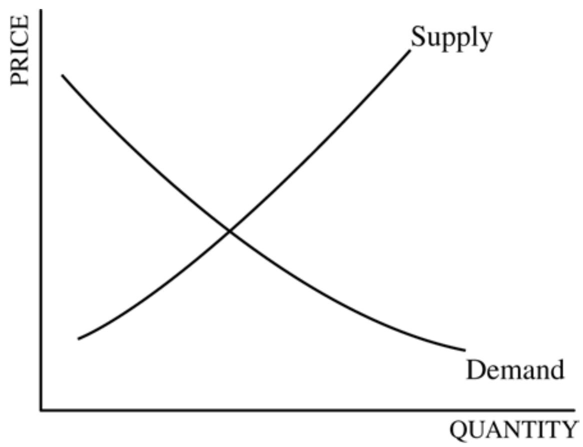
Note: After clicking on a link, right click and select "Previous View" to go back to original text.

7. In the circular flow model of a market economy, which of the following describes the roles of firms and households in the product markets and in the factor markets?

	Product Markets	**Factor Markets**
A.	Firms sell goods to households	Firms sell resources to households
B.	Firms sell goods to households	Firms buy resources from households
C.	Firms buy goods from households	Firms buy resources from households
D.	Firms buy goods from households	Firms sell resources to households

Answer and Rationale

Use the diagram below, which shows the supply and demand curves for leather garments, to answer the next two questions.



8. Assume that a leather garment is a normal good. An increase in the price of leather and a simultaneous increase in consumers' incomes will most likely have which of the following effects on the equilibrium price and quantity of leather garments?

	Price	**Quantity**
A.	Increase	Increase
B.	Increase	Indeterminate
C.	Indeterminate	Decrease
D.	Decrease	Decrease

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

9. If the government places a price ceiling on leather garments that is below the equilibrium price, which of the following will occur in the market for leather garments?

   A. There will be a shortage
   B. There will be a surplus
   C. The demand curve for leather garments will shift leftward
   D. The supply curve for leather garments will shift rightward

Answer and Rationale

10. The primary purpose of antitrust laws is to

   A. help businesses that are in financial trouble.
   B. encourage business investment.
   C. prevent business behavior that hampers competition.
   D. establish trust between government and businesses.

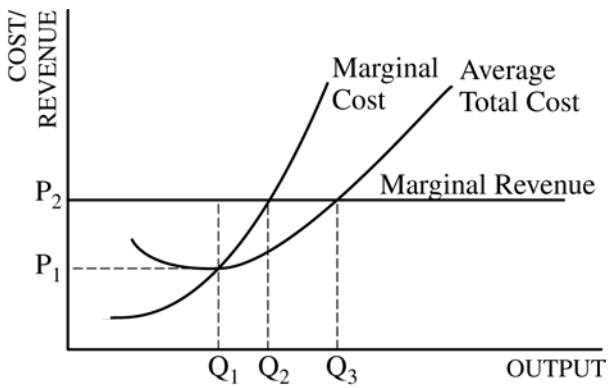
Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

11. When the production of a good generates negative externalities, the private market will

A. overproduce the good relative to the socially optimal level of output.
B. underproduce the good relative to the socially optimal level of output.
C. compensate the third parties harmed by the negative externality.
D. charge lower than the market equilibrium price to compensate for the externality.

Answer and Rationale



12. The profit-maximizing price and quantity of output for the firm whose cost and revenue curves are shown above will be which of the following?

	Price	Quantity
A.	P_1	Q_2
B.	P_2	Q_1
C.	P_2	Q_2
D.	P_2	Q_3

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

13. Which of the following is NOT true about a monopoly?

A. It is the only firm selling a particular product
B. It has a downward-sloping demand curve
C. Its primary goal is to maximize profit
D. It charges a price below average variable cost to maximize profit

Answer and Rationale

14. The demand for labor is called derived demand because it is

A. dependent on the demand for the final product that the labor is used to produce.
B. inversely related to the wage rate.
C. dependent on the availability of capital goods.
D. directly related to the marginal utility of working.

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

15. Which of the following is the best example of a fixed cost for a bakery?

A. Monthly rental payments on the building it occupies
B. The cost of flour and sugar
C. Wage payments to its workers
D. Fuel costs for operating its delivery trucks

Answer and Rationale

16. If a firm's long-run average total cost decreases as output increases, the firm is

A. operating efficiently.
B. perfectly competitive.
C. experiencing economies of scale.
D. making positive economic profits.

Answer and Rationale

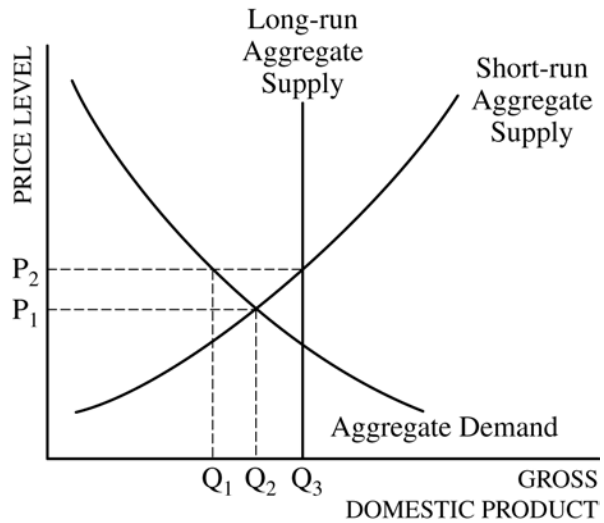
Note: After clicking on a link, right click and select "Previous View" to go back to original text.

17. Spending by households to purchase goods and services is called

A. investment.
B. exports.
C. consumption.
D. public-sector spending.

Answer and Rationale

Consider the following graph illustrating the aggregate supply and demand for a national economy.



18. In the short-run equilibrium, the economy described by the graph has

A. a recessionary gap.
B. an inflationary gap.
C. a labor shortage.
D. experienced diminishing returns.

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

19. Which of the following types of inflation would result if the price level rose because of an increase in the price of raw materials?

   A. Deflation
   B. Hyperinflation
   C. Demand-pull inflation
   D. Cost-push inflation

Answer and Rationale

20. Real gross domestic product (GDP) is defined as the ratio of nominal GDP to the

   A. money supply.
   B. unemployment rate.
   C. government’s budget deficit.
   D. GDP deflator.

Answer and Rationale

Note: After clicking on a link, right click and select “Previous View” to go back to original text.

21. For an economy that is in a recession, the actual unemployment rate is

  A. equal to the natural rate of unemployment.
  B. less than the natural rate of unemployment.
  C. greater than the natural rate of unemployment.
  D. less than the growth rate of the economy.

Answer and Rationale

22. During a recession, an appropriate fiscal policy would be

  A. an increase in taxes.
  B. an increase in government spending.
  C. a decrease in the reserve requirement.
  D. a decrease in the discount rate.

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

23. The Federal Reserve's primary policy tools include all of the following EXCEPT

   A. open-market operations.
   B. borrowing from foreign governments.
   C. changing the discount rate.
   D. setting reserve requirements.

Answer and Rationale

24. The marginal propensity to consume is the ratio of

   A. total consumption to total disposable income.
   B. the change in consumption to the change in disposable income.
   C. the change in equilibrium income to the change in investment spending.
   D. equilibrium income to total consumption.

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Use the information below to answer the next two questions.

Assume that the required reserve ratio is 20 percent and that a bank is currently fully loaned up. The bank receives a cash deposit of $500 from a new customer.

25. The bank is legally required to

    A. keep 20 percent of the $500 as reserves.
    B. keep 80 percent of the $500 as reserves.
    C. lend 20 percent of the $500 and keep the rest as reserves.
    D. send 80 percent of the $500 to the regional Federal Reserve Bank.

Answer and Rationale

26. The maximum increase in the money supply that can be generated from the deposit in the banking system is

    A. $400
    B. $500
    C. $2,000
    D. $2,500

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

27. If consumers in the United States increase their demand for imports over domestically produced goods, the international value of the United States dollar and United States exports will most likely change in which of the following ways?

	International Value of the Dollar	Exports
A.	Appreciate	Increase
B.	Appreciate	Decrease
C.	Depreciate	Increase
D.	Depreciate	Decrease

Answer and Rationale

28. The infant industry argument for trade barriers is advanced for

A. instituting permanent trade barriers for certain industries.
B. ensuring the safety of imported baby food.
C. protecting domestic producers of baby products from foreign competition.
D. protecting newly established domestic industries from foreign competition.

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

29. Assume that Country X can produce either 100 computers or 20 cars, whereas Country Y can produce either 30 computers or 10 cars using the same amount of resources. Which of the following statements is true?

   A. Country X has a comparative advantage in producing both computers and cars.
   B. Country Y has a comparative advantage in producing both computers and cars.
   C. Country X has a comparative advantage in producing cars, and Country Y has a comparative advantage in producing computers.
   D. Country X has a comparative advantage in producing computers, and Country Y has a comparative advantage in producing cars.

Answer and Rationale

30. How would an increase in personal income taxes affect disposable income and savings?

   A. It would decrease both disposable income and savings
   B. It would decrease disposable income and increase savings
   C. It would increase disposable income and decrease savings
   D. It would increase both disposable income and savings

Answer and Rationale

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

31. The difference between fixed-interest-rate loans and variable-interest-rate loans is that

    A. payments on fixed-interest-rate loans fluctuate with changes in market conditions, whereas payments on variable-interest-rate loans remain the same throughout the life of the loan.
    B. payments on fixed-interest-rate loans remain the same throughout the life of the loan, whereas payments on variable-interest-rate loans fluctuate with changes in market conditions.
    C. fixed-interest-rate loans are available only when financial markets are in favorable conditions, whereas variable-interest-rate loans are available all the time.
    D. variable-interest-rate loans are available only when financial markets are in favorable conditions, whereas fixed-interest-rate loans are available all the time.

Answer and Rationale

32. Which of the following statements is true regarding the relationship between risk and return on investments?

    A. The expected return is generally greater when the risk is lower.
    B. The expected return is generally lower when the risk is higher.
    C. The expected return is generally greater when the risk is higher.
    D. There is no relationship between risk and expected return.

Answer and Rationale

Answer Key and Rationales

Question Number	Correct Answer	Rationale
1	C	**Option C is correct.** If the economy is producing at point E, it is by definition not fully employing all its resources and can move toward the curve without changing current techniques of production. Back to Question
2	D	**Option D is correct.** In a command economy, the government determines the allocation of resources and the distribution of outputs through central planning. Back to Question
3	A	**Option A is correct.** Each individual would have a comparative advantage in performing a specific task if each individual can specialize in the task in which he/she has the lower opportunity cost. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
4	B	**Option B is correct.** A rightward shift of the demand curve leads to an increase in both the equilibrium price and quantity. Back to Question
5	C	**Option C is correct.** Marginal utility is the increase in total utility associated with the consumption of one extra unit of a good. If the marginal utility increases, total utility must be increasing at an increasing rate. Back to Question
6	B	**Option B is correct.** When demand is inelastic, total revenue increases as price increases because the percentage increase in price exceeds the percentage decrease in quantity demanded. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
7	B	**Option B is correct.** Firms produce goods and sell them to consumers (households). In a market economy, it is assumed that all resources — land, labor, and capital — are owned by households and that businesses purchase these resources from households through the factor markets. Back to Question
8	B	**Option B is correct.** An increase in the price of leather decreases the supply of leather garments, and an increase in incomes will increase the demand for leather garments (normal good). These simultaneous shifts in the curves will result in an increase in price, but the effect on quantity is indeterminate and will depend on the extent of the shift of each curve. Back to Question
9	A	**Option A is correct.** The result of an effective price ceiling below the equilibrium price will be an excess of quantity demanded over quantity supplied, which will result in a shortage. Back to Question

Note: After clicking on a link, right click and select “Previous View” to go back to original text.

Question Number	Correct Answer	Rationale
10	C	**Option C is correct.** Antitrust laws are designed to prevent business practices that restrain competition. Back to Question
11	A	**Option A is correct**. Negative externalities impose costs on third parties, and these costs are not reflected in the private market equilibrium price. As a result, goods generating negative externalities are overproduced relative to the socially optimal level of production. Back to Question
12	C	**Option C is correct.** The diagram shows demand and cost curves for a firm in perfect competition. Such a firm maximizes profit when it produces the quantity at which marginal revenue equals marginal cost; since it is a price-taker, the price will always be equal to marginal revenue, which is P_2 corresponding to Q_2. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
13	D	**Option D is correct.** If the price charged by the monopoly falls below its average variable cost, the monopoly will shut down. Back to Question
14	A	**Option A is correct.** The demand for labor depends on the demand for the final product that the labor produces. The higher the demand for the product, the higher the demand for labor. Back to Question
15	A	**Option A is correct.** The bakery's rental payments are not tied to its production level; it must continue to make its monthly rental payments regardless of the level of output. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
16	C	**Option C is correct.** A firm is said to have economies of scale if its long-run average total cost decreases as its output increases. As the firm's size of operation increases, unit costs decline because of specialization of resources. Back to Question
17	C	**Option C is correct.** Consumption is defined as spending by households to purchase goods and services. Back to Question
18	A	**Option A is correct.** On the graph, the short-run equilibrium is at P_1 and Q_2. A recessionary gap occurs when short-run equilibrium gross domestic product (Q_2) is less than the full-employment gross domestic product (Q_3). Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
19	D	**Option D is correct.** Cost-push inflation comes about because the increased costs of production are passed on to the consumer. The prices of raw materials are a cost and, as they rise, the increased prices are pushed on to the consumer. Back to Question
20	D	**Option D is correct.** Real GDP is calculated by dividing the nominal GDP by the price index, which is the GDP price deflator. Back to Question
21	C	**Option C is correct.** The natural rate of unemployment is the unemployment rate that prevails when the economy produces the full-employment output. During a recession, the actual level of real output falls below the full-employment output level, and unemployment rises. Therefore, the actual unemployment rate exceeds the natural rate of unemployment. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
22	B	**Option B is correct.** Moving the economy out of a recession requires implementing either an expansionary fiscal policy or a monetary policy. In this case, an expansionary fiscal policy involves either lowering taxes or increasing government purchases. Back to Question
23	B	**Option B is correct.** Borrowing from foreign governments is not a policy instrument that the Federal Reserve uses. The three other choices are the primary tools that the Federal Reserve utilizes to conduct monetary policy. Back to Question
24	B	**Option B is correct.** The marginal propensity to consume is the ratio of the change in consumption to the change in disposable income. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
25	A	**Option A is correct.** The required reserve ratio refers to the fraction of deposits a bank is legally required to keep as reserves to meet its liabilities. Back to Question
26	C	**Option C is correct.** Assuming there are no cash leakages and the bank does not keep more than the minimum required in reserves, the maximum increase in the money supply that can be obtained from the $500 deposit is $2,000 — that is, the money multiplier, (1/.2=5) times the amount of excess reserves. From the $500 deposit, the bank will have excess reserves equal to $400, which is $500 minus 0.2 ($500). Thus, the maximum increase in the money supply will be equal to $2,000, which is 5 times $400. Back to Question
27	C	**Option C is correct.** Favoring imports over domestically produced goods results in an increase in the amount of imports to the United States. This increase in imports increases the supply of United States dollars on the foreign exchange markets, resulting in a depreciation of the dollar. The depreciating dollar will make goods produced in the United States relatively less expensive in the world market, causing United States exports to increase. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
28	D	**Option D is correct.** The infant industry argument is intended to provide temporary protection to newly established domestic industries until they are able to mature and compete with foreign competitors. Back to Question
29	D	**Option D is correct.** Country X has a comparative advantage in producing computers because it has a lower opportunity cost than Country Y. Country Y has a comparative advantage in producing cars because it has a lower opportunity cost than Country X. Back to Question
30	A	**Option A is correct.** Increasing the tax rate decreases disposable income, which leaves consumers with less money to spend and save. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Question Number	Correct Answer	Rationale
31	B	**Option B is correct.** A fixed interest rate is a one-time rate charged on a loan, and a variable interest rate changes according to the changes in the market. Back to Question
32	C	**Option C is correct.** The return on investment depends on the level of risk individuals are willing to take. When an individual takes a higher risk when investing money, he/she expects a higher return. Back to Question

Note: After clicking on a link, right click and select "Previous View" to go back to original text.

Preparation Resources

The resources listed below may help you prepare for the GACE assessment in this field. These preparation resources have been identified by content experts in the field to provide up-to-date information that relates to the field in general. You may wish to use current issues or editions of these materials to obtain information on specific topics for study and review.

Guide to Taking a GACE Computer-delivered Assessment

This guide explains how to navigate through a GACE assessment and how to answer different types of test questions. This free download is available in the Test Preparation Resources section of the GACE website at ***www.gace.ets.org/prepare***.

Reducing Test Anxiety

This guide provides practical help for people who suffer from test anxiety. Designed specifically for GACE test takers, but useful to anyone who has to take tests, this guide reviews the major causes of test anxiety and offers practical advice for how to counter each one. Download this guide for free from the Test Preparation Resources section of the GACE website at ***www.gace.ets.org/prepare***.

Study Tips: Preparing for a GACE Assessment

This document contains useful information on preparing for selected-response and constructed-response tests. The instruction, tips, and suggestions can help you become a better-prepared test taker. See the Test Preparation Resources section of the GACE website at ***www.gace.ets.org/prepare*** for this free download.

Journals

Journal of Economic Theory — ***www.journals.elsevier.com/journal-of-economic-theory***

Journal of Business & Economic Statistics — ***www.tandfonline.com/toc/ubes20/current***

Journal of Monetary Economics — ***www.journals.elsevier.com/journal-of-monetary-economics***

Other Resources

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Miller, R, Benjamin, D., and North, D. (2011), *The Economics of Public Issues*, Seventeenth Edition, Prentice Hall.

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Wild, J., and Wild, K. (2011*). International Business*, Sixth Edition, Prentice Hall.

Woerheide, W. (2011). Fundamentals of Investments for Financial Planning, Sixth Edition, the American College Press.

Wright, R., and Quadrini, V. (2009). *Money and Banking*, Flat World Knowledge.

Online Resources

U.S Department of Commerce Bureau of Economic Analysis — ***www.bea.gov***

Georgia Department of Education — ***www.gadoe.org/Pages/Home.aspx***

Federal Reserve Bank of Atlanta — ***www.frbatlanta.org***

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