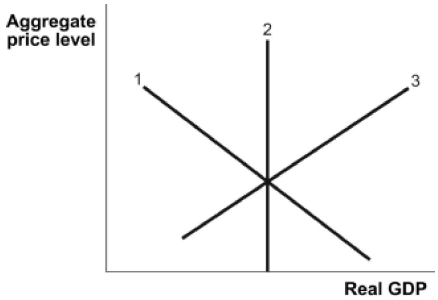
Unit 3 make up exam

Multiple Choice
Identify the choice that best completes the statement or answers the question.

1. A movement along the aggregate demand curve is caused by a:
   A. a change in the aggregate price level.
   B. an increase in consumer spending.
   C. a fall in commodity prices.
   D. a reduction in government spending.
   E. a decline in net exports.
2. Producing a short-run level of aggregate output that exceeds the economy's potential output results in:
   A. a downward adjustment in nominal wages.
   B. an upward adjustment in profits per unit of output.
   C. a downward adjustment in production costs.
   D. an upward adjustment in nominal wages.
   E. a downward adjustment in the price level.

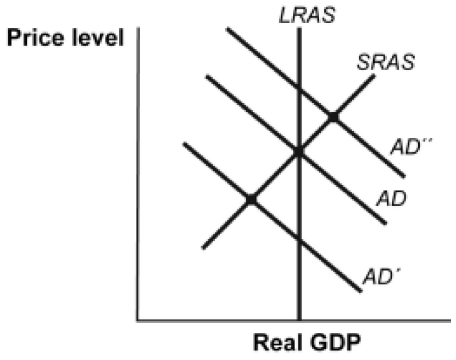
Figure 19-2: Macroeconomics Equilibrium



3. Use the "**Macroeconomics Equilibrium**" **Figure 19-2**. In the accompanying figure, curve 1 refers to _____, curve 2 refers to _____, and curve 3 refers to _____.
   A. long-run aggregate supply; short-run aggregate supply; aggregate demand
   B. aggregate demand; short-run aggregate supply; long-run aggregate supply
   C. short-run aggregate supply; long-run aggregate supply; aggregate demand
   D. aggregate demand; long-run aggregate supply; short-run aggregate supply
   E. short-run aggregate supply; aggregate demand; long-run aggregate supply
4. Which of the following will cause short-run aggregate supply to increase?
   A. A law that requires employers to provide health insurance for all employees.
   B. An increase in the aggregate price level.
   C. A large decrease in the price of oil.
   D. An increase in the minimum wage.
   E. A decrease in government transfer payments.
5. Actual investment spending equals:
   A. unplanned investment divided by the planned investment.
   B. planned investment minus unplanned investment.
   C. unplanned investment, even if there is a positive amount of planned investment.
   D. unplanned investment minus planned investment.
   E. planned investment plus unplanned investment.

6. Aggregate demand will shift to the right, if:
   A. the aggregate price level increases.
   B. the government purchases increase.
   C. there is an increase in taxes.
   D. there is a decrease in money supply.
   E. there is an increase in interest rates.
7. The marginal propensity to save:
   A. is the change in consumer saving divided by the change in consumption.
   B. is the change in saving divided by the change in disposable income.
   C. equals *MPC* + 1.
   D. rises when the *MPC* rises.
   E. is the ratio of total savings in the economy divided by real GDP.

Figure 20-8: Fiscal Policy Options



8. Use the "**Fiscal Policy Options" Figure 20-8.** If the aggregate demand curve is *AD*':
   A. a contractionary fiscal policy may be warranted.
   B. an expansionary fiscal policy may be warranted.
   C. the economy is in long-run equilibrium.
   D. the economy is experiencing an inflationary gap.
   E. the unemployment rate is lower than the natural rate of unemployment.
9. Use the "**Fiscal Policy Options" Figure 20-8.** If the aggregate demand curve is *AD*", of the choices below, the most appropriate discretionary fiscal policy would be to:
   A. increase government spending and decrease income tax rates.
   B. increase government spending and maintain income tax rates.
   C. decrease government spending and decrease income tax rates.
   D. decrease government spending and maintain income tax rates.
   E. increase government spending and increase transfer payments.
10. A negative supply shock often results in:
   A. a leftward shift of the *AD* curve.
   B. a decrease in the aggregate price level and a decrease in aggregate output.
   C. no change in the price level.
   D. a drop in the unemployment level.
   E. an increase in the aggregate price level and a decrease in aggregate output.

Disposable Income (in Billions)	Consumer Spending (in Billions)
$0	$100
200	220
400	340
600	460
800	580
1,000	700

Table 16-2: Disposable Income and Consumption

11. Use **Table 16-2.** Use the information in the table, the *MPC* is equal to:
    A. .80.
    B. 2.
    C. 1.20.
    D. .60.
    E. .75.
12. Suppose the economy is currently operating at an output level of $4,000 billion. Assume furthermore that potential output is $5,000 billion and the marginal propensity to consume is 0.75. Which of the following would be required to close this recessionary gap?
    A. A $25 billion increase in government spending.
    B. A $25 billion increase in taxes.
    C. A $250 billion increase in government spending.
    D. A $1,000 billion increase in government spending.
    E. A $500 billion increase in transfer payments.
13. The multiplier is equal to:
    A. 1/[1–*MPC*].
    B. *MPS*/*MPC*.
    C. 1/[*MPC*].
    D. 1/[1+*MPC*].
    E. 1/[1–*MPS*].
14. Which of the following would shift the aggregate demand curve to the left?
    A. An increase in the interest rate.
    B. An increase in the aggregate price level.
    C. An increase in consumer wealth.
    D. Stronger consumer optimism about future income.
    E. Lower income taxes.

Disposable Personal Income	Consumption
$100	$140
200	220
300	300
400	380
500	460

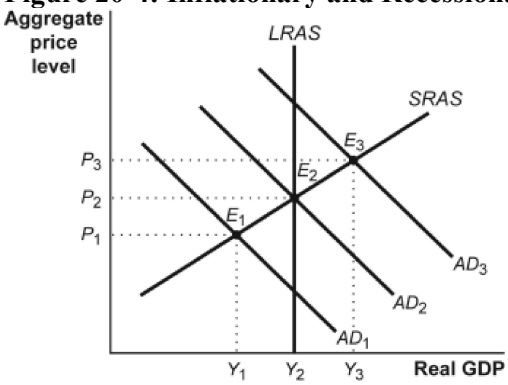
Table 16- 1: Income and Consumption

15. Use **Table 16- 1.** When disposable personal income is $400, the level of personal saving is:
    A. –$40.
    B. –$20.
    C. $0.
    D. $20.
    E. $40.

16. Suppose that the economy is in a recessionary gap. The policy makers in the government can:
    A. increase taxes and increase aggregate spending via the multiplier to remove the recessionary gap
    B. increase the money supply, lower the interest rate, increase investment and consumption spending and thus increase aggregate demand.
    C. cut government expenditure, decrease investment and consumption spending and thus increase aggregate supply.
    D. increase nominal wages, shift the short run aggregate supply to the left and thus remove the recessionary gap.
    E. decrease taxes and decrease aggregate spending via the multiplier to remove the recessionary gap
17. Changes in short-run aggregate supply can be caused by changes in:
    A. wages.
    B. wealth.
    C. government spending.
    D. consumption spending.
    E. investment spending.
18. The aggregate demand curve:
    A. slopes downward for the same reasons that an ordinary demand curve does.
    B. slopes downward in part because when the price level falls the real wealth of the public falls, and this induces people to change their consumption.
    C. slopes downward in part because as the price level falls the ability of households and firms to borrow cheaply increases.
    D. slopes upward, unlike an ordinary demand curve.
    E. is vertical, unlike an ordinary demand cure.
19. Suppose the marginal propensity to consume is equal to 0.90 and investment spending increases by $50 billion. Assuming no taxes and no trade, by how much will real GDP change?
    A. $450 billion increase.
    B. $90 billion increase.
    C. $500 billion increase.
    D. $500 billion decrease.
    E. $900 billion increase.
20. Assume that marginal propensity to consume is 0.8, and potential output is $800 billion. The tax multiplier is:
    A. 0.8.
    B. 1.25.
    C. 5.
    D. 4.
    E. 8.
21. Assume that marginal propensity to consume is 0.8, and potential output is $800 billion. If current real GDP is $700 billion, which of the following policies would bring the economy to potential output?
    A. Decrease taxes by $100 billion.
    B. Increase taxes by $100 billion.
    C. Decrease taxes by $25 billion.
    D. Decrease government transfers by $25 billion.
    E. Decrease taxes by $20 billion.
22. Government payments to households for which no good or service is provided in return are called:
    A. transfer payments.
    B. government purchases.
    C. consumption expenditures.
    D. investment expenditures.
    E. tax revenues.

23. Suppose the equilibrium aggregate price level is rising and the equilibrium level of real GDP is falling. Which of the following most likely caused these changes?
    A. An increase in short-run aggregate supply.
    B. An increase in aggregate demand.
    C. A decrease in short-run aggregate supply.
    D. A decrease in aggregate demand.
    E. An increase in short-run aggregate supply and an increase in aggregate demand.
24. The long-run aggregate supply curve is vertical because in the long run:
    A. technological progress outpaces raises in nominal wages.
    B. all factors of production increase.
    C. the price of labor is flexible, while the price of physical capital is fixed.
    D. all prices are flexible.
    E. the level of potential GDP is flexible.
25. An unplanned fall in inventories leads to:
    A. prices falling.
    B. production falling.
    C. production increasing.
    D. interest rates increasing.
    E. a weaker economy.
26. The aggregate demand curve is negatively sloped in part because of the impact of:
    A. the wealth effect on consumer spending.
    B. a changing exchange rate on potential output.
    C. the stickiness of nominal wages and salaries.
    D. the flexibility of nominal wages and salaries.
    E. the substitution effect on government spending.
27. When the aggregate price level falls, the purchasing power of assets rises which leads to:
    A. an increase in the quantity of aggregate output demanded.
    B. a decrease in the quantity of aggregate output demanded.
    C. a shift in the *AD* curve to the right.
    D. a shift in the *AD* curve to the left.
    E. a shift in the *SRAS* curve to the right.

Figure 20-4: Inflationary and Recessionary Gaps



28. Use the "**Inflationary and Recessionary Gaps" Figure 20-4**. The movement from AD_3 to AD_1 would be caused by:
    A. increased government purchases.
    B. increased government transfers.
    C. increasing the money supply.
    D. decreased taxes.
    E. increased taxes.

29. Suppose the economy is currently experiencing a recessionary gap. Which of the following fiscal policy options is most likely to increase real GDP by the largest amount?
    A. a decrease in taxes
    B. an increase in government purchases
    C. an increase in transfer payments
    D. an increase in government purchases, paid for by an increase in taxes.
    E. an increase in taxes.
30. Starting from its potential output, an economy's government decides to increase spending. In the long run, an economy will find:
    A. that it is producing at an output level which is greater than its potential output.
    B. it is producing at its potential output, but at a higher aggregate price level.
    C. it is producing at an output level which is below its potential output.
    D. it is producing at its potential output level, but at a lower aggregate price level.
    E. it is producing at its potential output, with no change in the aggregate price level.

Problem

1. Assume the economy of Lakewoodland is currently operating below the full-employment level of real gross domestic product with a balanced budget.
    (a) Draw a correctly labeled graph of short-run aggregate supply, long-run aggregate supply, and aggregate demand. Show each of the following.
        (i.) Current output and price level, labeled Y_1 and PL_1, respectively
        (ii.) Full-employment output, labeled as Y_f
    (b) The Lakewoodland government increases spending on goods and services by $100 billion, which is financed by borrowing. How will the increase in government spending affect each of the following?
        (i.) Cyclical unemployment
        (ii.) The natural rate of unemployment
    (c) If the marginal propensity to consume is equal to 0.75, calculate the <u>maximum</u> possible change in real gross domestic product that could result from the $100 billion increase in government spending.
    (d) In the absence of any additional changes in policies, in the long run will the short-run aggregate supply curve shift to the left, shift to the right, or remain unchanged as a result of the expansionary fiscal policy? Explain.
    (e) Now assume that in order to fund the $100 billion dollars of government spending the Lakewoodland government increases taxes by $100 billion (rather than borrowing the money) With this equal increase in government spending and taxes, will the real gross domestic product increase, decrease, or remain the same? Explain.

2. How does each of the following changes affect the real gross domestic product and price level of an open economy in the short run? Explain each.
    (a) An increase in the price of crude oil, an important natural resource
    (b) A technological change that increases the productivity of labor
    (c) An increase in spending by consumers
    (d) An increase in net exports