

FISCAL POLICY PRACTICE TEST

(All figures in billions of dollars)

Output (Income)	Net Taxes	Consumption Spending	Planned Investment	Government Purchases
Y	T	C	I	G
500	100	400	150	150
1,000	100	800	150	150
1,500	100	1,200	150	150
2,000	100	1,600	150	150
2,500	100	2,000	150	150

Figure 10.2

- Refer to Figure 10.2.** At an output level of \$2,500, there is an unplanned inventory

 - decrease of \$300 billion.
 - decrease of \$200 billion.
 - change of \$0.
 - increase of \$200 billion.
- Refer to Figure 10.2.** The equilibrium level of output is _____ billion.

 - \$1000
 - \$1,500
 - \$2,000
 - \$2,500
- The leader of Atlantis hires you as an economic consultant. He is concerned that the output level in Atlantis is too low and that this will cause prices to fall. He feels that it is necessary to increase output by \$100 billion. He tells you that the MPC in Atlantis is .9. Which of the following would be the best advice to give to the Atlantin President?

 - Reduce government spending in Atlantis by \$100 billion.
 - Increase taxes in Atlantis by \$10 billion.
 - Reduce government spending in Atlantis by \$10 billion.
 - Increase government spending in Atlantis by \$10 billion.
- If taxes are \$200 billion, the equilibrium level of output is \$6,000 billion. If taxes increase to \$300 billion, everything else the same, the equilibrium level of output falls to \$5,500 billion. The value of the tax multiplier

 - is -5.5.
 - is -5.
 - is 5.
 - cannot be determined from this information because the MPC is not given.
- Assume that the MPC is .75. By increasing government spending by \$400, equilibrium output _____; and by increasing taxes by \$400, equilibrium output _____.

 - increases by \$1,600; decreases by \$1,600.
 - increases by \$1,600; decreases by \$1,200.
 - increases by \$1,200; decreases by \$1,600.
 - increases by \$400; decreases by \$400.

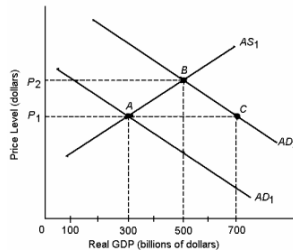
Answers: 1.d 2.b 3.d 4.b 5.b

Practice Test on AS-AD

1. When we consider an upward-sloping aggregate supply curve and a downward-sloping aggregate demand curve, a decrease in aggregate expenditures is reflected as
 - A) a leftward shift in the AS curve, which increases the equilibrium price level and decreases equilibrium real GDP.
 - B) a rightward shift in the AD curve, which increases both the equilibrium price level and equilibrium real GDP.
 - C) a leftward shift in the AD curve, which increases the equilibrium price level and decreases equilibrium real GDP.
 - D) a rightward shift in the AS curve, which increases both the equilibrium price level and equilibrium real GDP.
 - E) a leftward shift in the AD curve, which decreases both the equilibrium price level and equilibrium real GDP.

2. We would expect higher interest rates on business loans to result in
 - A) a decrease in aggregate expenditures.
 - B) an increase in aggregate supply.
 - C) an increase in aggregate demand.
 - D) a decrease in government spending.
 - E) an increase in investment spending.

Use the following to answer question 3:



3. Consider the economy above. The shift in aggregate demand from AD_1 to AD_2 could have been caused by
 - A) an increase in saving.
 - B) lower resource prices.
 - C) an increase in autonomous net exports.
 - D) a decrease in the price level.
 - E) government budget cuts.

4. A simultaneous increase in inflation and decrease in economic growth is associated with
 - A) an increase in aggregate demand and aggregate supply.
 - B) a decrease in aggregate demand with no change in aggregate supply.
 - C) a decrease in aggregate supply with no change in aggregate demand.
 - D) a decrease in aggregate supply and aggregate demand.
 - E) an increase in aggregate supply with no change in aggregate demand.

5. A simultaneous increase in both unemployment and inflation would most likely be the result of
 - A) an increase in the long-run aggregate supply curve and an increase in the aggregate demand curve.
 - B) an increase in short-run aggregate supply.
 - C) an increase in long-run aggregate supply.
 - D) a decrease in the short-run aggregate supply curve.
 - E) a decrease in the aggregate demand curve.

6. Cost-push inflation
 - A) is the result of increased consumer spending.
 - B) is a by-product of business cycles that arise on the supply side.
 - C) is associated with an economic expansion.
 - D) is identical to demand-pull inflation.
 - E) is a by-product of business cycles that arise on the demand side.

Practice Test on Money/Monetary Policy

1. Assume that banks become more conservative in their lending policies, and start holding some excess reserves. Compared to a situation in which banks are not holding excess reserves, the size of the money multiplier will be
 - (a) smaller.
 - (b) larger.
 - (c) the same.
 - (d) zero.
2. Refer to Figure 12.1. The money demand curve will shift from M_1^d to M_2^d if
 - (a) the interest rate increases.
 - (b) the interest rate decreases.
 - (c) aggregate output increases.
 - (d) b and c.

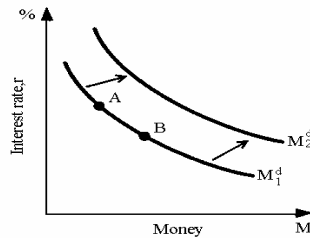


Figure 12.1

3. For a given interest rate, a higher level of output means
 - (a) a decrease in the number of transactions and thus a lower demand for money.
 - (b) a decrease in the number of transactions and thus a higher demand for money.
 - (c) an increase in the number of transactions and thus a lower demand for money.
 - (d) an increase in the number of transactions and thus a higher demand for money.
4. Refer to Figure 12.3. At an interest rate of 8%, firms and households
 - (a) will attempt to reduce their holdings of money by buying bonds.
 - (b) will attempt to increase their holdings of money by selling bonds.
 - (c) are satisfied with the amount of money they are holding.
 - (d) will attempt to increase both their holdings of money and their holdings of bonds.

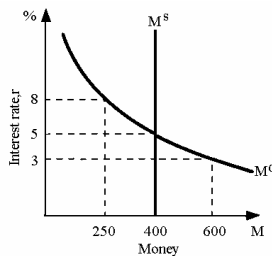


Figure 12.3

5. Which of the following pairs of events will definitely lead to an increase in the equilibrium interest rate?
 - (a) a decrease in the level of aggregate output and a decrease in the required reserve ratio
 - (b) an increase in the price level and an increase in the discount rate
 - (c) an increase in the level of aggregate output and the purchase of government securities by the Federal Reserve
 - (d) a decrease in the price level and the sale of government securities by the Federal Reserve
6. An example of a tight monetary policy is
 - (a) an increase in the reserve requirement.
 - (b) the Fed buying government securities in the open market.
 - (c) a decrease in the prime lending rate.
 - (d) a decrease in the discount rate.