

### Practice questions 3

1. An increase in net exports that results from a change in the price level in the United States:
  - a. Will shift the aggregate demand curve to the right.
  - b. Will shift the aggregate demand curve to the left.
  - c. Will not cause the aggregate demand curve to shift.
  - d. Will have an indeterminate effect on aggregate demand.
  
2. Which of the following factors cause the long-run aggregate supply curve to shift to the right each year?
  - a. An increase in the number of workers in the economy.
  - b. The accumulation of more machinery and equipment.
  - c. Technological change.
  - d. All of the above.
  
3. If firms and workers could predict the future price level exactly, the short-run aggregate supply curve would be:
  - a. Downward sloping.
  - b. Upward sloping.
  - c. Horizontal.
  - d. The same as the long-run aggregate supply curve.
  
4. What is the impact of an increase in the price level on the short-run aggregate supply curve?
  - a. A shift of the curve to the right.
  - b. A shift of the curve to the left.
  - c. A movement of the economy up and to the right along a stationary curve.
  - d. A combination of a movement along the curve and a shift of the curve
  
5. If oil prices rise unexpectedly,
  - a. There will be a movement upward along a stationary aggregate supply curve.
  - b. There will be a movement downward along a stationary aggregate supply curve.
  - c. The short-run aggregate supply curve will shift up and to the left.
  - d. The short-run aggregate supply curve will shift to the right.
  
6. How does the dynamic model of aggregate supply and aggregate demand explain inflation?
  - a. By showing that productivity increases result in a slower pace of hiring workers and a slow recovery that increases inflation, but only slightly.
  - b. By showing that productivity increases do not always translate into higher wages but are absorbed instead by higher profits.
  - c. By showing that if total spending in the economy grows faster than total production, prices will rise.
  - d. None of the above.

7. A double coincidence of wants refers to:
- the instance in which a good that is used as money also has value independent of its use as money.
  - the fact that for a barter trade to take place between two people, each person must want what the other one has.
  - the idea that a barter economy is more efficient than a monetary economy.
  - the fact that two parties are involved in transactions where money is the medium of exchange.
8. Money serves as a unit of account when:
- sellers are willing to accept it in exchange for goods or services.
  - it can be easily stored and used for transactions in the future.
  - prices of goods and services are stated in the monetary unit.
  - All of the above.
9. If Irving Fisher was correct about his prediction of velocity, then the quantity equation can be written to solve for inflation as follows:
- Inflation rate = Growth rate of the money supply + Growth rate of real output.
  - Inflation rate = Growth rate of the money supply – Growth rate of real output.
  - Inflation rate = Growth rate of the money supply – Growth rate of velocity.
  - Inflation rate = Growth rate of the money supply + Growth rate of velocity.
10. In the definition of the money supply, where do credit cards belong?
- M1.
  - M2.
  - M3.
  - None of the above.
11. If the reserve requirement is 10% and there is no currency leakage in the loan-deposit cycle, how much is the total increase in checking account deposits caused by an initial deposit of \$1,000?
- \$100
  - \$1,000
  - \$10,000
  - \$100,000
12. To increase the money supply, the FOMC directs the trading desk, located at the Federal Reserve Bank of New York to:
- buy U.S. Treasury securities from the public.
  - sell U.S. Treasury securities to the public.
  - print U.S. Treasury securities and put them out in circulation.
  - buy U.S. dollars in the foreign exchange market.

13. When is the opportunity cost of holding money higher?

- a. When interest rates are high.
- b. When interest rates are low.
- c. When people hold less cash and more financial assets.
- d. When the money supply increases.

14. If real GDP increases,

- a. The money demand curve shifts to the right.
- b. The money demand curve shifts to the left.
- c. There is a movement downward along a stationary money demand curve.
- d. There is a movement upward and to the left along a stationary money demand curve.

15. If the price level increases,

- a. The money demand curve shifts to the right.
- b. The money demand curve shifts to the left.
- c. There is a movement downward along a stationary money demand curve.
- d. There is a movement upward and to the left along a stationary money demand curve.

16. Suppose you buy a U.S. Treasury bill today for \$950 that matures in one year, at which time the Treasury will pay you \$1,000. How much interest will you earn on your investment of \$950?

- a. 4.75%.
- b. 5.26%.
- c. 19%.
- d. 5%.

17. Suppose that the FOMC meets and learns that real GDP will fall short of full-employment real GDP by \$200 billion. If the FOMC tries to correct this situation, it will enact this type of policy:

- a. Expansionary policy to decrease short-run aggregate supply.
- b. Expansionary policy to increase aggregate demand.
- c. Expansionary policy to increase short-run aggregate supply.
- d. Contractionary policy to decrease long-run aggregate supply.

18. By using the Taylor rule, the predicted federal funds rate target is \_\_\_\_\_ than the actual target used by the Fed during the period of the late 1970s and early 1980s when Paul Volcker was Federal Reserve Chairman. The same rule predicts a \_\_\_\_\_ fed funds target than the actual target used by the Fed when Arthur Burns was chairman from 1970 to 1978.

- a. higher; higher
- b. lower; lower
- c. higher; lower
- d. lower; higher

19. The wealth effect refers to the fact that:
- When the price level falls, the real value of household wealth rises, and so will consumption.
  - When income rises, consumption rises.
  - When the price level falls, the nominal value of assets rises, while the real value of assets remains the same.
  - All of the above.
20. The effect of productivity growth on employment is as follows:
- Productivity affects employment, but only in the short run.
  - Productivity affects employment permanently.
  - The relationship between productivity and employment is nonexistent.
  - The relationship between productivity and employment is indeterminate.
21. Why does the short-run aggregate supply curve slope upward?
- Because profits rise when the prices of the goods and services firms sell rise more rapidly than the prices they pay for inputs.
  - Because an increase in market price results in an increase in quantity supplied, as stated by the law of supply.
  - Because, as the number of workers, machinery, equipment, and technological changes increase, quantity supplied increases.
  - All of the above.
22. Which of the following are reasons why firms and workers fail to adjust their predictions of the future price level?
- Contracts make some wages and prices “sticky.”
  - Businesses are often slow to adjust wages.
  - Menu costs make some prices “sticky.”
  - All of the above.
23. The long economic expansion that began in March 1991 and ended in March 2001 gave way to a recession. The recession was caused by a decline in aggregate demand. Which factors contributed to this decline?
- The end of the stock market “bubble” and excessive investment in information technology.
  - The terrorist attacks of September 11, 2001.
  - The corporate accounting scandals.
  - All of the above.
24. As productivity and real GDP rose during 2002 and 2003, economists noticed that if firms can produce more output with the same number of workers:
- They will be inclined to hire more workers rapidly.
  - They might be less likely to hire additional workers.
  - Labor productivity will be the main determinant of output in the long run.
  - They will make their production processes more labor intensive and less capital intensive.

25. The Federal Reserve System is:
- the central bank of the United States.
  - the institution that regulates all state banks.
  - an institution that regulates all securities and exchange in financial markets.
  - an institution also known as the Treasury of the United States.
26. There are \_\_\_\_\_ members of the Board of Governors, who are appointed by the President of the United States to \_\_\_\_\_, non-renewable terms. One of the Board members is appointed Chairman for a \_\_\_\_\_, renewable term.
- nine; 7-year; eight-year
  - twelve; 4-year; four-year
  - seven; 14-year; four-year
  - fourteen; 4-year; four-year
27. The actions the Federal Reserve takes to manage the money supply and interest rates to pursue economic objectives is called:
- Fiscal policy.
  - Open market operations.
  - Monetary policy.
  - Financial management.
28. The Fed uses three monetary policy tools. Which of the following is not one of those tools?
- Open market operations.
  - Discount policy.
  - Reserve requirements.
  - Federal funds rate setting.
29. Which of the following people vote on monetary policy at the Federal Open Market Committee (FOMC) meetings?
- The seven members of the Federal Reserve's Board of Governors.
  - The president of the Federal Reserve Bank of New York.
  - Four presidents from Federal Reserve banks other than the president of the Federal Reserve Bank of New York (rotating basis).
  - All of the above.
30. The Fed conducts monetary policy primarily through:
- open market operations.
  - discount policy.
  - reserve requirements.
  - None of the above.

31. When the central bank commits to conducting policy in a manner that achieves a publicly announced inflation target, it is using:
- Inflation targeting.
  - The Taylor rule.
  - Contractionary monetary policy.
  - Monetary policy independence.
32. Which of the following can be affected by monetary policy?
- The level of real GDP in the long run.
  - Inflation in the long run.
  - Both the level of real GDP and inflation in the long run.
  - Neither the level of real GDP nor inflation in the long run.
33. The Fed's performance in the 1980s, 1990s, and early 2000s received high marks from economists. Which of the following contributed to the Fed's good performance during those years?
- Inflation targeting.
  - A strategy of keeping inflation low and stable in the long run, but without inflation targeting.
  - The ability of the Fed to conduct monetary policy in close coordination with Congress and the president.
  - The pursuit of effective fiscal policy.
34. The main reason to keep the Fed – or any country's central bank – independent of the rest of the government is to avoid:
- Inflation.
  - Unemployment.
  - High interest rates.
  - All of the above.
35. The more bonds the central bank buys, the \_\_\_\_\_ the money supply grows, and the \_\_\_\_\_ the inflation rate will be.
- slower; lower
  - slower; higher
  - faster; lower
  - faster; higher
36. The Federal Reserve System is:
- An institution that mirrors the values of a democracy such as ours in the United States.
  - An institution that closely resembles others in government, where officials are accountable for their actions to the electorate.
  - An institution where the chairman has only one vote in seven on the Board of Governors but plays an outsized role in policy setting.
  - All of the above.

37. The goal of expansionary fiscal policy is:
- To increase short-run aggregate supply.
  - To increase long-run aggregate supply.
  - To increase aggregate demand.
  - All of the above.
38. An attempt to reduce inflation requires \_\_\_\_\_ fiscal policy, which causes real GDP to \_\_\_\_\_ and the price level to \_\_\_\_\_.
- expansionary; rise; rise
  - expansionary; rise; fall
  - contractionary; rise; fall
  - contractionary; fall; fall
39. Which of the following statements is incorrect?
- Just as increasing or decreasing the money supply does not have any direct effect on government spending or taxes, increasing or decreasing government spending or taxes will not have any direct effect on the money supply.
  - Fiscal policy and monetary policy may have the same goals, but they have different effects on the economy.
  - The only difference between fiscal policy and monetary policy in fighting recessions and stimulating spending is where the money comes from.
  - None of the above. All of the above statements are correct.
40. By how much will equilibrium real GDP increase as a result of a \$100 billion increase in government purchases?
- By more than \$100 billion.
  - By less than \$100 billion.
  - By exactly \$100 billion.
  - None of the above. Equilibrium real GDP will not change as a result of an increase in government purchases.
41. The multiplier effect consists of:
- A series of autonomous expenditures that result from an initial increase in government expenditures.
  - A series of autonomous expenditure increases that result from an initial increase in induced expenditures.
  - A series of induced increases in consumption spending that result from an initial increase in autonomous expenditures.
  - A change in government spending resulting from a change in equilibrium income.
42. How would you decompose the total effect of an increase in government purchases on the aggregate demand curve? (Note: the magnitudes of the shifts don't have to be the same.)
- The aggregate demand curve shifts once to the right and then back to the left.
  - The aggregate demand curve shifts as a result of two distinct effects, twice to the right.
  - The aggregate demand curve shifts as a result of two distinct effects, twice to the left.
  - The aggregate demand curve does not shift, but there are two movements, one downward and one upward, along the curve.

43. According to the crowding out effect, if the federal government increases spending, the demand for money and the equilibrium interest rate will \_\_\_\_\_, which will cause some consumption, investment, and net exports to \_\_\_\_\_.
- increase; increase
  - increase; decrease
  - decrease; decrease
  - decrease; increase
44. Higher interest rates in the United States will attract foreign investors. This will cause \_\_\_\_\_ in the exchange rate between the dollar and other currencies, and \_\_\_\_\_ in net exports.
- an increase; an increase
  - an increase; a decrease
  - a decrease; an increase
  - a decrease; a decrease
45. What is the long run effect of a permanent increase in government spending?
- A decline in investment, consumption, and net exports that is smaller than the increase in government purchases, therefore, aggregate demand increases.
  - A decline in investment, consumption, and net exports that is larger than the increase in government purchases, therefore, aggregate demand decreases.
  - A decline in investment, consumption, and net exports that exactly offsets the increase in government purchases, therefore, aggregate demand remains unchanged.
  - No change in investment, consumption, or net exports, therefore, no change in aggregate demand.
46. Budget deficits automatically \_\_\_\_\_ during recessions and \_\_\_\_\_ during expansions.
- increase; increase
  - increase; fall
  - fall; increase
  - fall; fall
47. To obtain a more accurate measure of the effects on the economy of the government's spending and tax policies, economists prefer to look at:
- The actual budget deficit or surplus.
  - The cyclically adjusted budget deficit or surplus.
  - The mounting size of the debt.
  - The justifications for increased spending, regardless of revenues.
48. Every time the federal government runs a budget deficit, the Treasury must:
- Buy securities from the Fed in order to increase its reserves.
  - Print money in order to finance the excess expenditures.
  - Borrow funds from savers by selling Treasury securities.
  - Supply funds in the federal funds market.

49. Currency \_\_\_\_\_ occurs when the market value of a country's currency rises relative to the value of another country's currency, while currency \_\_\_\_\_ occurs when the market value of a country's currency declines relative to value of another country's currency.
- appreciation; depreciation
  - depreciation; appreciation
  - valuation; devaluation
  - devaluation; valuation
50. If the exchange rate changes from  $¥100 = \$1$  to  $¥120 = \$1$ , the dollar has \_\_\_\_\_ and the yen has \_\_\_\_\_.
- appreciated; depreciated
  - depreciated; appreciated
  - valuated; devaluated
  - devaluated; valuated
51. Which two factors do economists combine to establish the real exchange rate between two countries?
- The balance of payments and whether or not the currency of either country faces a shortage or surplus in the foreign exchange market.
  - The money supply in each country and the fixed exchange rate between the two countries.
  - The relative price levels and the nominal exchange rate between the two countries' currencies.
  - Net exports and whether there is currency appreciation or depreciation between the two countries.
52. If the exchange rate between the U.S. dollar and the yen is  $\$1 = ¥100$ , the price level in the United States is 110 and the price level in Japan is 100, what is the real exchange rate?
- 90.90.
  - 110.
  - 121.
  - 1.1.
53. When imports are greater than exports, as is usually the case for the United States, which of the following must be true?
- There will be a net capital inflow as people in the United States sell assets and borrow to pay for the surplus of imports over exports.
  - The United States must be a net borrower from abroad.
  - U.S. net foreign investment must be negative.
  - All of the above.

54. Which of the following is the saving-investment equation?
- a.  $\text{Private Saving} = \text{National Income} - \text{Consumption} - \text{Taxes}$
  - b.  $\text{National Saving} = \text{Domestic Investment} + \text{Net Foreign Investment}$
  - c.  $\text{Public Saving} = \text{Taxes} - \text{Government Spending}$
  - d.  $\text{Domestic Investment} = \text{Private Saving} + \text{Public Saving}$
55. In the strict sense of the concept of net foreign investment, a country such as the United States that has negative net foreign investment must be:
- a. Investing less than it is saving domestically.
  - b. Saving less than it is investing domestically.
  - c. Experiencing positive net exports.
  - d. A net lender, not a borrower.
56. Budget deficits reduce:
- a. Domestic investment but not net foreign investment.
  - b. Net foreign investment but not domestic investment.
  - c. Both domestic investment and net foreign investment.
  - d. Neither domestic investment nor net foreign investment.
57. A country experiences twin deficits when a government budget deficit causes:
- a. a trade deficit.
  - b. a service exports deficit.
  - c. a current account deficit.
  - d. a financial account deficit.
58. What impact does the additional policy channel available in an open economy have?
- a. It increases the ability of an expansionary monetary policy to affect aggregate demand.
  - b. It decreases the ability of an expansionary monetary policy to affect aggregate demand.
  - c. It does not have any impact on the ability of an expansionary monetary policy to affect aggregate demand.
  - d. It has an indeterminate effect, sometimes increasing and sometimes decreasing the ability of an expansionary monetary policy to affect aggregate demand.
59. In an open economy, an expansionary fiscal policy may be \_\_\_\_\_ effective because the crowding out effect could be \_\_\_\_\_.
- a. more; larger
  - b. more; smaller
  - c. less; larger
  - d. less; smaller

60. Which of the following determines how many of units of a foreign currency you can purchase with one dollar?

- a. The real exchange rate.
- b. The nominal exchange rate.
- c. The Federal Reserve.
- d. The purchasing power parity of one dollar.

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
c	d	d	c	c	c	b	c	b	d	c	a	a	a	a	b	b	d	a	a

21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38	39	40
a	d	d	b	a	c	c	d	d	a	a	b	b	a	d	c	c	d	c	a

41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60
c	b	b	b	c	b	b	c	a	a	c	b	d	b	b	c	c	a	c	b