NANYANG TECHNOLOGICAL UNIVERSITY

HE2002 MACROECONOMICS II

SEMESTER 2 AY 2023/2024
QUIZ 1 Version 01

Student's Name …… Matriculation Number ……..
(Family Name) (Given Name)

Tutor's Name …… Tutorial Group ……..

INSTRUCTIONS TO STUDENTS

- This Quiz paper consists of **SIX (6) pages** including the cover page.
- Quiz duration is **60 minutes**.
- This paper consists of **25** multiple-choice questions.
- Each correct answer is worth **1 mark**.
- Give only **ONE answer per question**.
- Choosing more than one answer will invalidate all answers to the question.
- Please write required information and fill the circles on the **bubble sheet** for Quiz 1.
- Don't forget to **fill the circles for paper version** and **matriculation number** on the bubble sheet.
- The quiz paper must be submitted and answers on the paper will not be marked.
- Paper with missing pages will not be marked and will be deemed as zero.

1) Which of the following is an exogenous variable in the basic IS-LM model we learned in class?

A) disposable income (Y_D)
B) saving (S)
C) taxes (T)
D) consumption (C)
E) none of these

2) Think about the model of the goods market in Lecture 1, $C = c_0 + c_1 Y_D$ and $I = \bar{I}$. Suppose the marginal propensity to consume equals 0.6 (i.e., $c_1 = 0.6$). Given this information, an equal and simultaneous decrease in government spending G and taxes T by 100 will cause

A) output Y decreases by 150
B) output Y decreases by 100
C) output Y increases by 100
D) output Y decreases by 250
E) no change in output Y

3) Which of the following would tend to make the multiplier smaller?

A) an increase in the marginal propensity to save
B) an increase in the marginal propensity to consume
C) a reduction in taxes
D) a reduction in government spending
E) none of these

4) Which of the following about IS relation is ***not*** correct?

A) It is the relation between interest rate and savings.
B) It is the equilibrium condition for the goods market.
C) It stands for "Investment equals saving."
D) It shows the investment must be equal to what people and the government want to save.

5) The money demand curve will shift to the left when which of the following occurs?

A) a decrease in the money supply
B) a reduction in income
C) an increase in the interest rate
D) all of these
E) none of these

6) We would expect which of the following to occur when the central bank pursues contractionary monetary policy?

A) an increase in bond prices and an increase in the interest rate (i)
B) a reduction in bond prices and an increase in i
C) an increase in bond prices and a reduction in i
D) a reduction in bond prices and a reduction in i
E) none of these

7) Which of the following statements is ***false***?

A) A bank issues liabilities to acquire funds.
B) Bank capital is recorded as an asset on the bank balance sheet.
C) The bank's assets provide the bank with income.
D) A bank's assets are its uses of funds.

8) Which of the following is a ***liability*** for the *central* bank?
A) checkable deposits
B) bonds
C) savings accounts
D) loans
E) currency

9) Consider a monetary system that includes simple commercial banks. The public holds no currency. The ratio of reserves to deposits is 0.2. The demand for money is given by $M^d = \$Y(0.6 - 2i)$. The supply of central bank money H is \$400 billion, and nominal income is \$ 4 trillion. What is the equilibrium interest rate by setting the demand for central bank money equal to the supply of central bank money?

A) 15%
B) 25%
C) 5%
D) 2.5%
E) 10%

10) Suppose there is a simultaneous fiscal contraction and monetary expansion. The economy is not in the liquidity trap. We know ***with certainty*** that

A) output will increase
B) output will decrease
C) the interest rate will increase
D) the interest rate will decrease
E) both output and the interest rate will decrease

11) During the financial crisis in the United States, consumer confidence fell significantly. Which of the following will occur as a result of this reduction in consumer confidence?

A) The IS curve will shift rightward.
B) The LM curve will shift down.
C) The IS curve will shift leftward.
D) The LM curve will shift up.
E) The IS curve will shift rightward, and the LM curve will shift up.

12) The IS curve will shift to the right when which of the following occurs?

A) an increase in the money supply
B) an increase in government spending
C) a reduction in the interest rate
D) all of these
E) none of these

13) In late 2007 and early 2008, the U.S. Federal Reserve engaged in open market purchase of government bonds. Which of the following will occur as a result of this monetary policy action?

A) The LM curve shifts up.
B) The LM curve shifts down.
C) The IS curve shifts rightward as the interest rate falls.
D) The IS curve shifts leftward as the interest rate increases.
E) none of these

14) From 1982 to 2004, the nominal interest rate has declined considerably, but the real rate has declined much less than the nominal rate. This is because

A) the nominal interest rate is set by the central bank
B) the real interest rate is close to zero
C) expected inflation has declined
D) expected inflation has increased
E) the real interest rate is set by the central bank

15) Suppose a bank has chosen its preferred leverage ratio and suppose that the value of its assets declines, which of the following is ***wrong***?

A) To maintain the leverage ratio, it can ask investors to provide more funds.
B) Its leverage ratio decreases.
C) To maintain the leverage ratio, it can call back loans.
D) The bank is more at risk than it was before.
E) none of these

16) When the risk premium *x* decreases

A) IS curve shifts to the left.
B) IS curve shifts to the right.
C) LM curve shifts upward.
D) LM curve shifts downward.

17) Suppose that in the initial equilibrium, the real interest rate $r = 2\%$, risk premium $x = 2\%$ and $\pi^e = 1\%$. The financial shocks hit the economy, and the risk premium x increases by 4% to 6%. Problems in the financial system lead to a recession. Which of the following macroeconomic policy is ***impossible*** to return output to its previous level and avoid recession?

A) an increase in G
B) a financial policy that improves the solvency of the financial system
C) a decrease in T
D) a decrease in the policy rate
E) none of these

18) (Think about the extended IS-LM model with financial markets) In an economy with the rate at which firms can borrow is much higher than the federal funds rate, equivalently that the risk premium, *x* is high, and the nominal interest rate is at the zero lower bound, which of the following statement is ***correct***?

A) The policy that improve the solvency of the financial system and make banks become more willing to lend implemented by the government is called quantitative easing and it is a kind of macroeconomic policy.
B) Suppose quantitative easing increases the expected inflation, LM curve shifts down.
C) Fed has no policy options to stimulate the economy when the federal funds rate is zero.
D) The risk premium *x* increases when quantitative easing successfully facilitates the flow of credit in the financial markets.
E) none of these

19) When the unemployment rate is low, we would expect that

A) the probability of losing a job is low.
B) the probability of losing a job is high.
C) the probability an unemployed individual will find another job is low.
D) the separation rate will increase.

20) An increase in unemployment benefits will tend to cause which of the following?

A) an upward shift in the WS curve
B) an upward shift in the PS curve
C) a downward shift in the WS curve
D) a downward shift in the PS curve
E) none of these

21) Suppose the natural level of output is the level of output when the unemployment rate is at its natural level. The natural level of output occurs when

A) the goods market and financial markets are in equilibrium.
B) the unemployment rate is zero.
C) the markup (m) is zero.
D) the economy is operating at the unemployment rate consistent with both the wage-setting and price-setting equations.
E) there are no discouraged workers in the economy.

22) Suppose we wish to examine the determinants of the equilibrium real wage and equilibrium level of employment (N) with fixed total labor force (L) in the economy. In a graph with the real wage on the vertical axis, and the level of employment (N) on the horizontal axis instead of unemployment rate, the wage-setting relation will now be

A) a vertical line.
B) an upward sloping line.
C) a horizontal line.
D) a downward sloping line.
E) a curve that first slopes upward, then downward.

23) In the Phillips curve equation, which of the following will cause a reduction in the current inflation rate?

A) a reduction in the markup, m
B) a reduction in the expected inflation rate
C) an increase in the unemployment rate
D) all of these
E) none of these

24) The original Phillips curve shows that when the unemployment rate is lower than the natural rate,

A) policy rate is higher than expected.
B) policy rate is lower than expected.
C) inflation is higher than expected.
D) inflation is lower than expected.

25) Which of the following assumptions best characterized the assumption about how individuals formed expectations of inflation by the early 1970s?

A) Expected inflation for the current year was unchanged over time.
B) Expected inflation for the current year was approximately equal to the previous year's inflation rate.
C) Expected inflation for the current year was less than the previous year's inflation rate.
D) Expected inflation for the current year equal to the average inflation rate over the past five years.
E) Expected inflation for the current year equal to the average inflation rate over the past ten years.