Name: ___________________________ Date: _____________

1. Which of the following is a tool that the Federal Reserve can use to influence AD?
   A) open market operations
   B) lending to banks and other financial institutions
   C) changes in reserve requirements and the interest rate paid on reserves
   D) All of the answers are correct.

2. If businesses react to a pessimistic outlook and decrease spending, the Fed can counteract this by:
   A) decreasing money supply to spur the economy out of the recession.
   B) increasing money supply, which will lower real interest rates and encourage borrowing.
   C) increasing government expenditures to spur the economy out of the recession.
   D) decreasing corporate taxes to encourage firms to increase their spending.

3. When a negative shock to aggregate demand occurs, the inflation rate will:
   A) increase.
   B) remain the same.
   C) decrease.
   D) be automatically adjusted by the Fed.

4. How can the Fed offset a positive shock to aggregate demand?
   A) Increase the growth rate of the money supply.
   B) Decrease the growth rate of the money supply.
   C) Increase the growth rate of government spending.
   D) Decrease the growth rate of government spending.

5. In the dynamic *AD–AS* model, an increase in money growth will cause the growth rate of real GDP to increase in:
   A) the short run only.
   B) the long run only.
   C) both the short run and the long run.
   D) neither the short run nor the long run.

6. What philosophy of economic adjustment is against tying the hands of the central bank?
   A) rules
   B) discretion
   C) prudence
   D) inclination

7. Economists who believe that the Federal Reserve is likely to make lots of mistakes in the implementation of monetary policy believe:
   A) in monetary policy discretion.
   B) in monetary policy run by the federal government.
   C) in monetary policy commitment.
   D) that the Federal Reserve should be abolished.

8. An economy where the Central Bank overstimulates aggregate demand will suffer from:
   A) inflation.
   B) unemployment.
   C) increases in money supply.
   D) deflation.

9. When people believe that a central bank will stick with its policy, monetary policy is likely to have:
   A) high credibility.
   B) low credibility.
   C) a high bandwagon effect.
   D) a low bandwagon effect.

10. Monetary policy works best to counteract:
    A) negative aggregate demand shocks.
    B) negative supply shocks.
    C) positive supply shocks.
    D) Solow growth shocks.

Answer Key

1. D
2. B
3. C
4. B
5. A
6. B
7. C
8. A
9. A
10. A