Aggregate Demand and Aggregate Supply

Problem 1. When we say that economic fluctuations are irregular and unpredictable, we mean that

(a) the relationship between output and unemployment is erratic and difficult to characterize.
(b) when one macroeconomic variable that measures income or spending is falling, other macroeconomic variables that measure income or spending are likely to be rising.
(c) recessions do not occur at regular intervals.
(d) All of the above are correct.

Problem 2. According to classical macroeconomic theory, changes in the money supply affect

(a) real GDP and the price level.
(b) real GDP but not the price level.
(c) the price level, but not real GDP.
(d) neither the price level nor real GDP.

Problem 3. In the context of aggregate demand and aggregate supply, the wealth effect refers to the idea that, when the price level decreases, the real wealth of households

(a) increases and as a result consumption spending increases. This effect contributes to the downward slope of the aggregate-demand curve.
(b) decreases and as a result consumption spending increases. This effect contributes to the upward slope of the aggregate-supply curve.
(c) increases and as a result households increase their money holdings; in turn, interest rates increase and investment spending decreases. This effect contributes to the downward slope of the aggregate-demand curve.
(d) decreases and as a result households increase their money holdings; in turn, interest rates increase and investment spending decreases. This effect contributes to the upward slope of the aggregate-supply curve.

Problem 4. Which of the following lists includes only changes that shift aggregate demand to the right?

(a) repeal of an investment tax credit, an increase in the money supply
(b) repeal of an investment tax credit, a decrease in the money supply
(c) passing of an investment tax credit, an increase in the money supply
(d) passing of an investment tax credit, a decrease in the money supply

Problem 5. The position of the long-run aggregate supply curve

(a) is determined by resource usage and technology.
(b) is at the point where the unemployment rate is zero.
(c) shifts to the right when the money supply increases.
(d) is at the point where the economy would cease to grow.

Problem 6. Which of the following can explain the upward slope of the short-run aggregate supply curve?

(a) nominal wages are slow to adjust to changing economic conditions
(b) as the price level falls, the exchange rate falls
(c) an increase in the money supply lowers the interest rate
(d) an increase in the interest rate increases investment spending

Problem 7. Which of the following shifts short-run, but not long-run aggregate supply right?

(a) a decrease in the actual price level
(b) a decrease in the expected price level
(c) a decrease in the capital stock
(d) an increase in the money supply

Problem 8. Changes in the price of oil

(a) can only lead to recessions.
(b) have not contributed much to output fluctuations in the United States.
(c) change the economy principally by changing aggregate demand.
(d) created both inflation and recession in the United States in the 1970s.

Monetary and Fiscal Policy in the AD/AS Model

Problem 9. Fiscal policy is determined by

(a) the president and Congress and involves changing government spending and taxation.
(b) the president and Congress and involves changing the money supply.
(c) the Federal Reserve and involves changing government spending and taxation.
(d) the Federal Reserve and involves changing the money supply.

Problem 10. According to the liquidity preference theory, an increase in the overall price level of 10 percent

(a) increases the equilibrium interest rate, which in turn decreases the quantity of goods and services demanded.
(b) decreases the equilibrium interest rate, which in turn increases the quantity of goods and services demanded.
(c) increases the quantity of money supplied by 10 percent, leaving the interest rate and the quantity of goods and services demanded unchanged.
(d) decreases the quantity of money demanded by 10 percent, leaving the interest rate and the quantity of goods and services demanded unchanged.

Problem 11. In the short run, an increase in the money supply causes interest rates to

(a) increase, and aggregate demand to shift right.
(b) increase, and aggregate demand to shift left.
(c) decrease, and aggregate demand to shift right.
(d) decrease, and aggregate demand to shift left.

Problem 12. A situation in which the Feds target interest rate has fallen as far as it can fall is sometimes described as a

(a) liquidity preference.
(b) liquidity trap.
(c) open-market trap.
(d) interest-rate contraction.

Problem 13. If the MPC is 0.8 and there are no crowding-out or accelerator effects, then an initial increase in aggregate demand of $120 billion will eventually shift the aggregate demand curve to the right by

(a) $216 billion.
(b) $150 billion.
(c) $600 billion.
(d) $480 billion.

Problem 14. 14. In a certain economy, when income is $500, consumer spending is $375. The value of the multiplier for this economy is 5. It follows that, when income is $510, consumer spending is

(a) $381.67.
(b) $378.
(c) $383.
(d) $383.33.

Problem 15. Suppose households attempt to increase their money holdings. To stabilize output by countering this increase in money demand, the Federal Reserve would

(a) increase government spending.
(b) increase the money supply.
(c) decrease government spending.
(d) decrease the money supply.

Problem 16. A tax cut targeted at ____________ people may have a bigger effect because

(a) poorer; poorer people tend to spend a higher share of their income.
(b) poorer; poorer people tend to spend a lower share of their income.
(c) wealthier; wealthier people tend to spend a higher share of their income.
(d) wealthier; wealthier people tend to spend a lower share of their income.