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. Most economists use the aggregate demand and aggregate supply model primarily to analyze

(a) short-run fluctuations in the economy.

(b) the effects of macroeconomic policy on the prices of individual goods.

(c) the long-run effects of international trade policies.

(d) productivity and economic growth.

Problem 3. Let Y denote real GDP. Investment is a

(a) small part of Y, accounting for a small share of the fluctuation in Y.

(b) small part of Y, yet it accounts for a large share of the fluctuation in Y.

(c) large part of Y, so it accounts for a large share of the fluctuation in Y.

(d) large part of Y, yet it accounts for a small share of the fluctuation in Y.

Problem 4. The saying "Money is a veil" means that

(a) while nominal variables are the first thing we may observe about an economy, whats important are the real variables and the forces that determine them.

(b) money is the principal medium of exchange in most economies.

(c) the primary determinant of short-run economic fluctuations is not real variables, but rather changes in the money supply.

(d) in the long run money is of no importance to the determination of either real or nominal variables

Problem 5. In order to understand how the economy works in the short run, we need to

(a) study the classical model.

(b) study a model in which real and nominal variables interact.

(c) understand that money is a veil.

(d) understand that money is neutral in the short run

Problem 6. Which of the following effects helps to explain the downward slope of the aggregate-demand curve?

(a) the exchange-rate effect

(b) the wealth effect

(c) the interest-rate effect

(d) All of the above are correct

Problem 7. Suppose a stock market boom makes people feel wealthier. The increase in wealth would cause people to desire

(a) increased consumption, which shifts the aggregate-demand curve right.

(b) increased consumption, which shifts the aggregate-demand curve left.

(c) decreased consumption, which shifts the aggregate-demand curve right.

(d) decreased consumption, which shifts the aggregate-demand curve left

Problem 8. The long-run aggregate supply curve shifts right if

(a) immigration from abroad increases.

(b) the capital stock increases.

(c) technology advances.

(d) All of the above are correct

Problem 9. According to the sticky-wage theory of the short-run aggregate supply curve, if workers and firms expected prices to rise by 4 percent, but instead they rise by 2 percent, then

(a) employment and production rise.

(b) employment rises and production falls.

(c) employment falls and production rises.

(d) employment and production fall.

Problem 10. Wages tend to be sticky

(a) because of contracts, social norms, and notions of fairness.

(b) because of contracts, but not social norms or notions of fairness.

(c) because of social norms and notions of fairness, but not contracts.

(d) None of the above are correct

Problem 11. The misperceptions theory of the short-run aggregate supply curve says that if the price level is higher than people expected, then some firms believe that the relative price of what they produce has

(a) decreased, so they increase production.

(b) decreased, so they decrease production.

(c) increased, so they increase production.

(d) increased, so they decrease production.

Shifting SRAS

- Shifts in the long-run aggregate-supply curve normally arise from changes in labor, capital, natural resources, or technological knowledge. These same variables shift the short-run aggregate-supply curve.
- An increase in the expected price level reduces the quantity of goods and services supplied and shifts the short-run aggregate-supply curve to the left. (And vice versa.)
- So if OPEC decides to restrict the supply of oil—this is likely to be a *temporary* increase in the price of oil. The SRAS will shift to the left, but LRAS will not shift.

Four Steps for Analyzing Macro Fluctuations

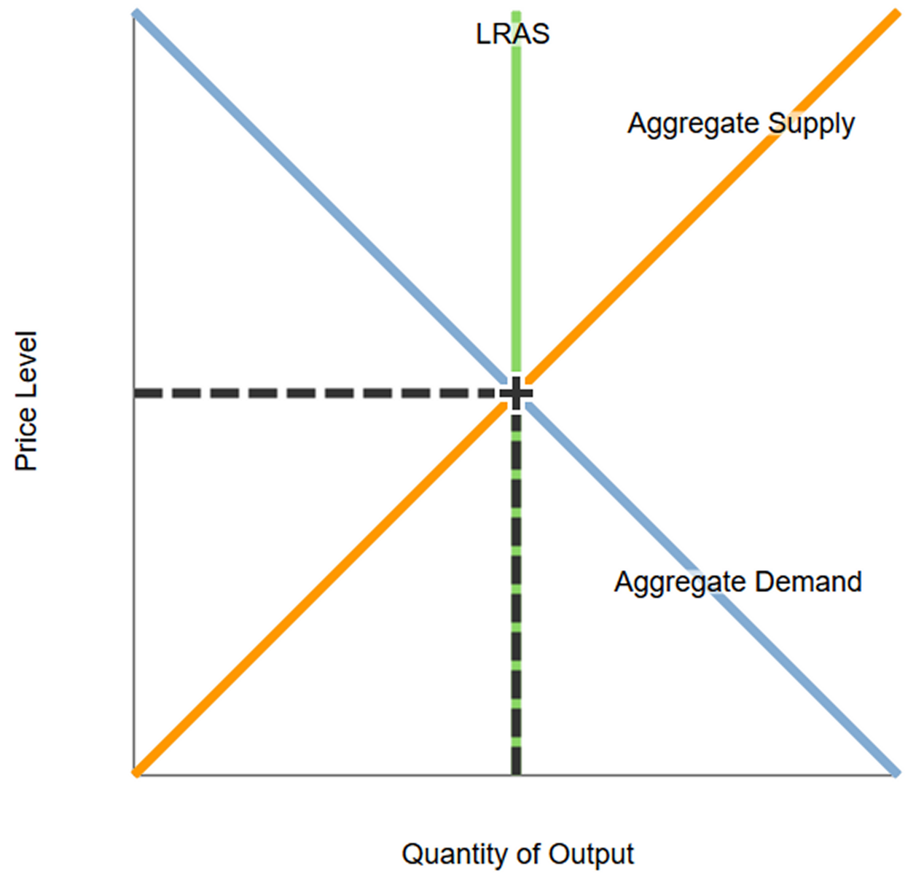
1. Decide whether the event shifts the aggregate-demand curve or the aggregate-supply curve (or perhaps both).

2. Decide the direction in which the curve shifts.

3. Use the diagram of aggregate demand and aggregate supply to determine the impact on output and the price level in the short run.

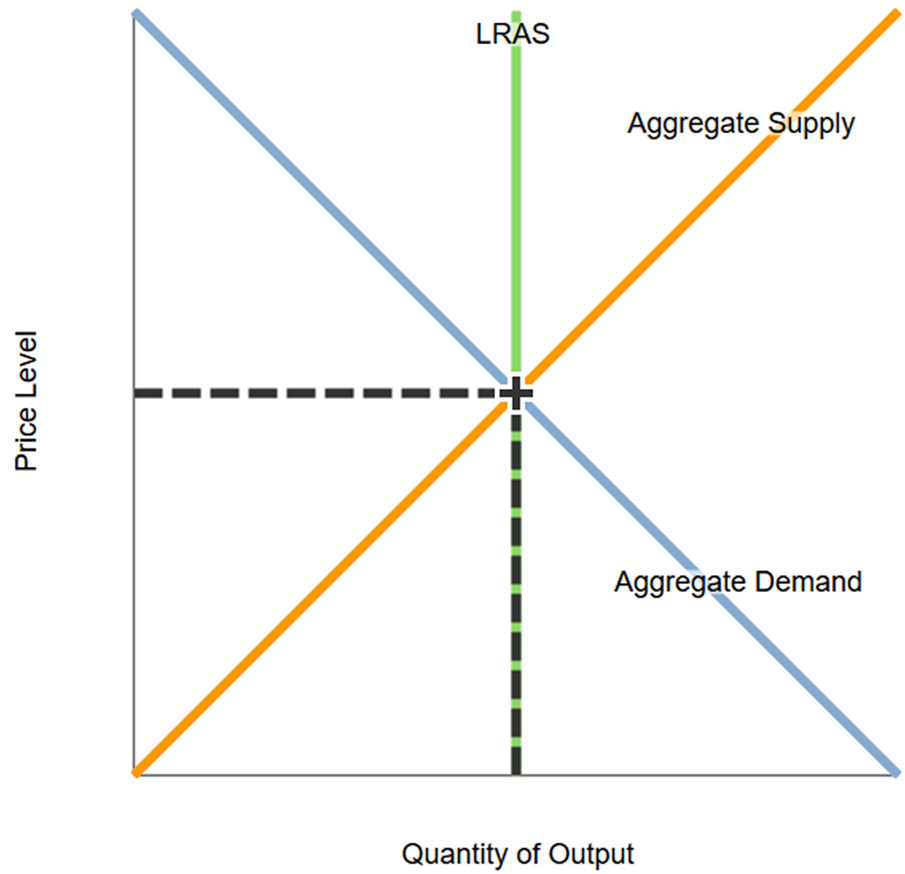
4. Use the diagram of aggregate demand and aggregate supply to analyze how the economy moves from its new short-run equilibrium to its long-run equilibrium

Problem 12. Suppose the economy is in a long-run equilibrium, as shown in the following graph.



Now suppose that a stock market crash causes aggregate demand to fall. Graph the effects in the short run. What happens to the unemployment rate?

Problem 13. Suppose the economy is in a long-run equilibrium, as shown in the following graph.



Florida orange groves suffer a prolonged period of below-freezing temperatures, from which they will eventually recover. What happens?

Problem 14. Stagflation exists when prices

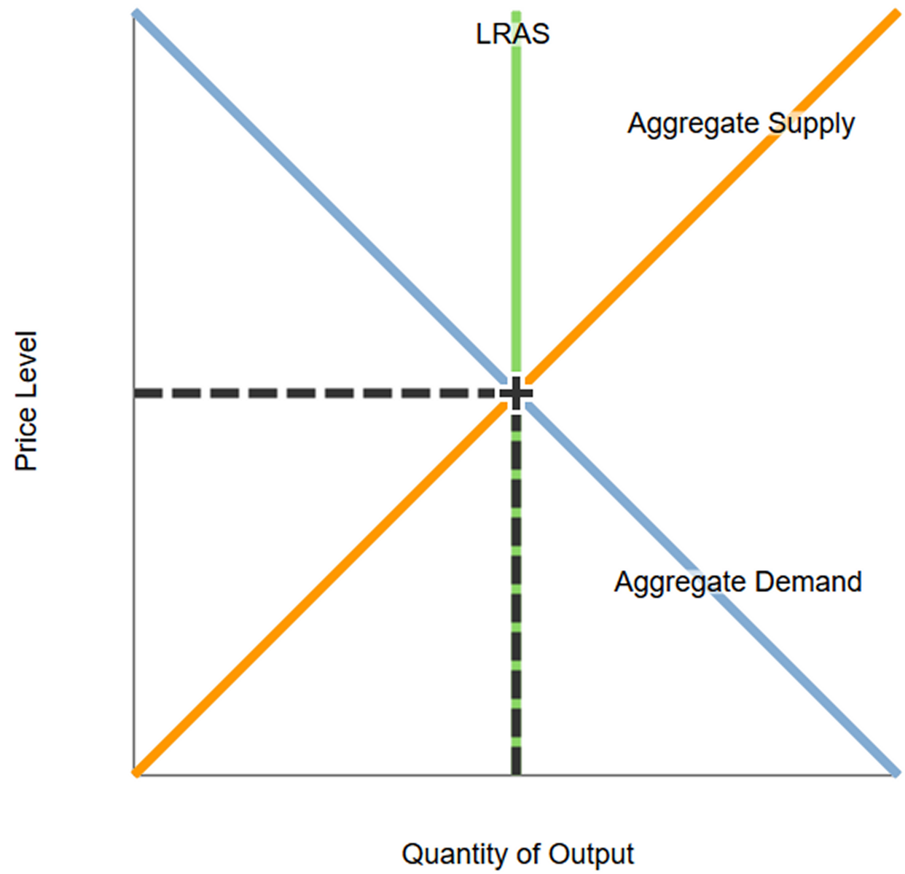
(a) and output rise.

(b) rise and output falls.

(c) fall and output rises.

(d) and output fall

Problem 15. Suppose the economy is in a long-run equilibrium, as shown in the following graph.



Increased job opportunities overseas cause many people to leave the country permanently. What happens?