

National Income and Price Determination Unit Test
AP Macroeconomics
Chastain

Multiple Choice: Write the letter of the BEST answer choice.

1. Changes in which of the following leads to a shift of the aggregate consumption function?
 - I. Expected future disposable income
 - II. Aggregate wealth
 - III. Current disposable income
 - a. I only
 - b. II only
 - c. III only
 - d. II and III only
 - e. I, II, and III

2. If the primary goal is to reduce inflation, which of the following fiscal policy actions would be appropriate during a period of a rapidly increasing consumer price index?
 - I. Reduce government expenditures for defense and space research.
 - II. Increase transfer payments to those most severely affected by the rising price index.
 - III. Increase personal income tax rates.
 - a. I only
 - b. II only
 - c. III only
 - d. I and III only
 - e. II and III only

3. Which of the following fiscal policy actions would be most effective in combating a recession?

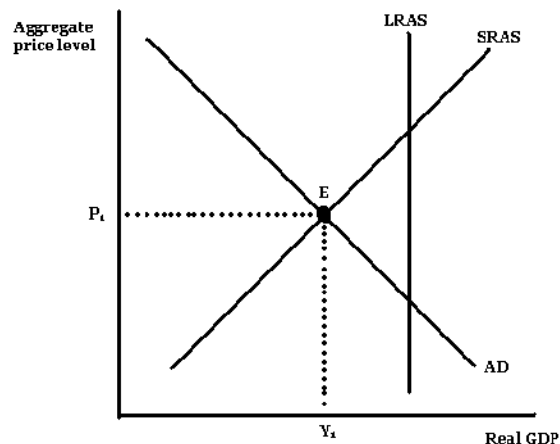
<u>Taxes</u>	<u>Government Spending</u>
a. \$25 billion decrease	\$25 billion decrease
b. \$25 billion decrease	\$25 billion increase
c. \$25 billion decrease	No Change
d. \$25 billion increase	\$25 billion decrease
e. \$25 billion increase	\$25 billion increase

4. The level of planned investment spending is negatively related to the
 - a. rate of return on investment.
 - b. level of consumer spending.
 - c. level of actual investment spending
 - d. interest rate.
 - e. all of the above

5. Which of the following explains the slope of the aggregate demand curve?
- I. The wealth effect of a change in the aggregate price level
 - II. The interest rate effect of a change in the aggregate price level
 - III. The product-substitution effect of a change in the aggregate price level
- a. I only
 - b. II only
 - c. III only
 - d. I and II only
 - e. I, II, and III
6. Which of the following will shift the aggregate demand curve to the right?
- a. A decrease in wealth
 - b. Contractionary fiscal policy
 - c. Pessimistic consumer expectations
 - d. An increase in the quantity of money
 - e. A decrease in the existing stock of capital
7. Decreases in the stock market decrease aggregate demand by decreasing which of the following?
- a. Interest rates
 - b. Tax revenues
 - c. The price level
 - d. Consumer wealth
 - e. The stock of existing physical capital
8. Which of the following government policies will shift the aggregate demand curve to the right?
- a. An increase in taxes
 - b. A decrease in interest rates
 - c. An increase in government transfers
 - d. A decrease in the quantity of money
 - e. An increase in government purchases of goods and services
9. Which of the following will shift the short-run aggregate supply curve? A change in
- a. productivity.
 - b. nominal wages.
 - c. commodity prices.
 - d. profit per unit at any given price level.
 - e. all of the above.
10. Because changes in the aggregate price level have no effect on aggregate output in the long run, the long-run aggregate supply curve is
- a. Fixed
 - b. Vertical
 - c. Horizontal
 - d. Positively sloped
 - e. Negatively sloped

11. The horizontal intercept of the long-run aggregate supply curve at macroeconomic equilibrium is
- Negative
 - At the origin
 - At current output
 - At potential output
 - At current and potential output
12. A decrease in which of the following will cause the short-run aggregate supply curve to shift to the left?
- Inputs
 - Productivity
 - Commodity prices
 - The cost of health care insurance premiums paid by employers
 - The use of cost-of-living allowances in labor contracts
13. Which of the following causes a negative supply shock?
- An increase in minimum wage
 - An increase in the interest rates on loans
 - An increase in oil prices
- I only
 - II only
 - III only
 - I and III only
 - I, II, and III
14. Which of the following causes a positive demand shock?
- An increase in taxes
 - An increase in wealth
 - Pessimistic consumer expectations
 - A decrease in government spending
 - An increase in the existing stock of capital

Refer to the graph for questions 15 and 16:

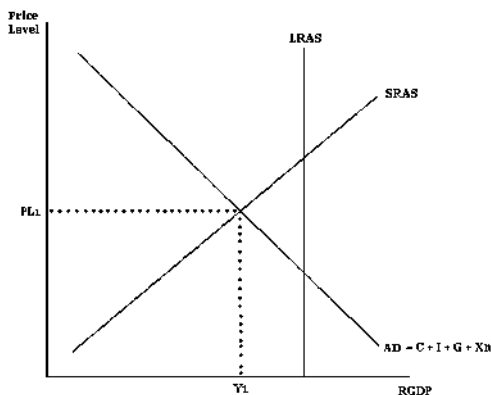


15. Which of the following statements is true if this economy is operating P_1 and Y_1 ?
- I. The level of aggregate output equals potential output.
 - II. It is in short-run macroeconomic equilibrium.
 - III. It is in long-run macroeconomic equilibrium.
- a. I only
 - b. II only
 - c. III only
 - d. II and III
 - e. I and II
16. The economy depicted in the graph is experiencing a(n)
- a. Contractionary gap
 - b. Recessionary gap
 - c. Inflationary gap
 - d. Demand gap
 - e. Supply gap
17. Which of the following contributes to the lag in implementing fiscal policy?
- I. It takes time for Congress and the President to pass spending and tax changes.
 - II. Current economic data take time to collect and analyze.
 - III. It takes time to realize an output gap exists.
- a. I only
 - b. II only
 - c. III only
 - d. I and III only
 - e. I, II, and III

18. Which of the following is an example of expansionary fiscal policy?
- Increasing taxes
 - Decreasing interest rates
 - Increasing the money supply
 - Increasing government spending
 - Decreasing government transfers
19. Which of the following is a fiscal policy that is appropriate to combat inflation?
- Decreasing taxes
 - Increasing interest rates
 - Expansionary fiscal policy
 - Decreasing government spending
 - Increasing government transfers
20. An income tax rebate is an example of
- An expansionary fiscal policy
 - A contractionary fiscal policy
 - An expansionary monetary policy
 - A contractionary monetary policy
 - None of the above
21. The Federal Reserve is responsible for controlling which of the following
- Money supply
 - Interest rates
 - Taxes and government spending
- I only
 - II only
 - III only
 - I and II
 - I, II, and III
22. The marginal propensity to consume
- Has a negative relationship to the multiplier
 - Is equal to 1
 - Represents the proportion of consumers' disposable income that is spent
- I only
 - II only
 - III only
 - I and III only
 - I, II, and III
23. Which of the following is NOT an automatic stabilizer?
- Medicaid
 - Food stamps
 - Income taxes
 - Monetary policy
 - Unemployment insurance

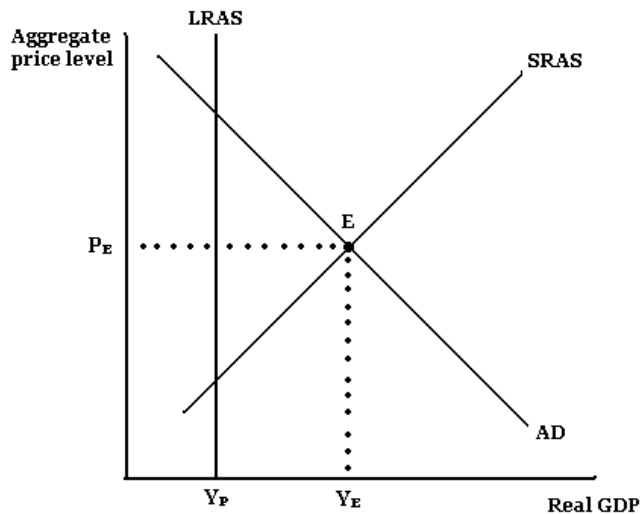
Short Answer: Answer the question by either explaining the question or by drawing an appropriate graph. Make sure you LABEL EVERYTHING!

24. For each event, explain whether the initial effect is a change in planned investment spending or a change in unplanned inventory investment, and indicate the direction of the change (positive or negative).
- A sharp decrease in the cost of business borrowing.
 - An expected decrease in consumer spending.
 - A sharp decline in the economy's growth rate of real GDP.
 - An unanticipated increase in sales.
25. Draw a correctly labeled graph showing aggregate demand.
- On your graph, illustrate a decrease in aggregate demand.
 - List the four factors that shift aggregate demand.
 - Describe a change in each determinant of aggregate demand that would lead to the shift you illustrated in part (a).
26. If Bill receives a paycheck for \$2500 this month and he spends \$600 of his disposable income, what will be the multiplier effect and tax multiplier effect of the money spent? $MPC = .6$
(Show all of your work to receive credit)
27. Draw a correctly labeled graph illustrating a long-run macroeconomic equilibrium graph.
- On your graph, illustrate an increase in short-run aggregate supply.
 - List three possible causes that could have caused the shift in short-run aggregate supply from part (a).
28. Refer to the graph below to answer the following questions:



- Is the economy in short-run macroeconomic equilibrium? Explain.
- Is the economy in long-run macroeconomic equilibrium? Explain.
- What type of gap exists in this economy?
- What type of fiscal policy should be utilized to correct the economic situation?

29. Refer to the graph below to answer the following questions:



- a. What type of gap exists in this economy?
- b. What type of fiscal policy should be utilized to correct the economic situation?

Free Response Question: Answer every part of the question. Make sure graphs are at least 4 lines big on your paper so that you can properly label each piece of the graphs.

30. Assume that the country of Luella is currently in long run equilibrium.

- a. Assume that Luella produces only military goods and civilian goods. Draw a correctly labeled production possibilities curve for Luella. Show a point that could represent the current output combination and label it A.
- b. On your graph from part (a), show a point that could represent additional resources being added into the economy of Luella and label it B.
- c. Using a correctly labeled graph of aggregate supply and aggregate demand, show each of the following:
 - i. Long-run aggregate supply.
 - ii. The current output level, labeled Y_E , and the current price level, labeled PL_E .
- d. Assume consumer confidence falls due to unforeseen financial issues from the federal government. Show on your graph from part (c) the short-run impact of the change in consumer confidence and label the new equilibrium price level PL_1 and the new output level Y_1 .
- e. Using your shift from part (d), identify the fiscal policy the government should use to correct the situation of having falling consumer confidence. Explain why this fiscal policy should be implemented.