TOBB-ETU, Economics Department

Macroeconomics I (IKT 233)

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Practice Questions with Answers (for Final)

9. CHAPTER: Aggregate Demand I

1-) In the long run, the level of output is determined by the: (c)
a-) interaction of supply and demand
b-) money supply and the levels of government spending and taxation.
c-) amounts of capital, labor and the available technology
d-) preferences of the public

2-) The aggregate demand curve tells us possible: (c)
a-) combinations of M and Y for a given value of P.
b-) combinations of M and P for a given value of Y.
c-) combinations of P and Y for a given value of M.
d-) results if the CB reduces the money supply

3-) An economy is in a recessionary gap. According to the classical economists, which of the following should occurr? (d)
a-) wages should fall which would cause more workers to be hired
b-) prices should fall which would increase consumer spending
c-) interest rates should fall which would increase consumer and investment spending
d-) all of the above should have occurred

4-) If the short-run AS curve is horizontal and the long-run AS curve is vertical, then a change in the government spending will change ... in the short run and change ... in the long run. (b)
a-) only prices; only output.
b-) only output; only prices.
c-) both prices and output; only prices.
d-) both prices and output; both prices and output.

5-) Crowding out occurs when an increase in government spending ... the interest rate and investment ... (b)

a-) increases; increases

b-) increases; decreases

c-) decreases; increases

d-) decreases; decreases

6-) In the short run, a favorable supply shock causes (c)

a-) both prices and output to rise

b-) prices to rise and output to fall

c-) prices to fall and output to rise.

d-) both prices and output to fall.

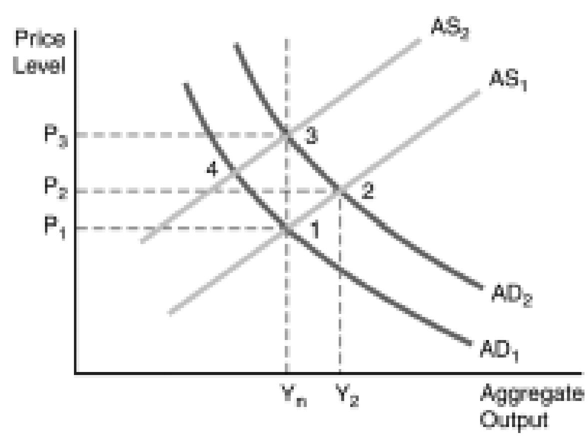
7-) In the below Figure, the initial effect of an increase in the money supply is illustrated as a movement from (a)

a-) point 1 to point 2.

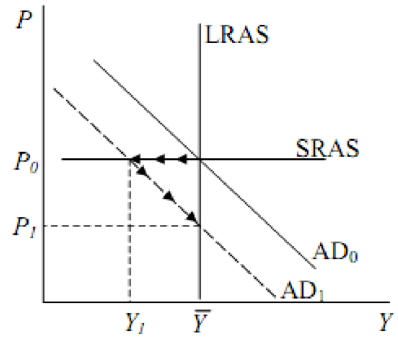
b-) point 2 to point 3.

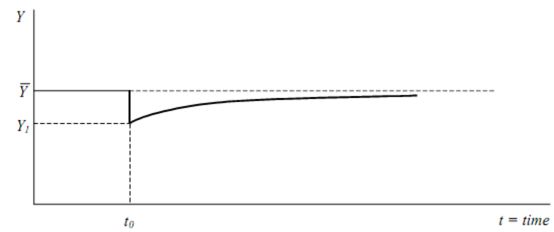
c-) point 1 to point 3.

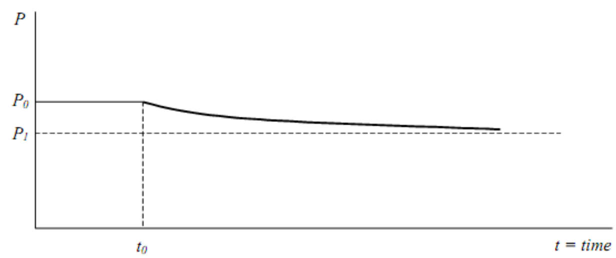
d-) point 2 to point 1.



8-) A permanent leftward shift of the Aggregate Demand Curve, occurring at time t_0, as shown in the figure. Show the path followed by Y and P on the separately in two graphs.







10 & 11. CHAPTERS Aggregate Demand II: The IS-LM Model to Explain Fluctuations

1-) An increase in \$1 in government purchases will: (b)

a-) Shift the LM curve upwards

b-) Shift the IS curve to the right by \$1/(1-MPC).

c-) Not shift the LM curve.

d-) All of the above

2-) An increase in investment spending due to optimism of companies about investment profitability causes the aggregate demand function to shift ..., the equilibrium level of aggregate output to rise, and the IS curve to shift to the.... (b)

a-) up; left

b-) up; right

c-) down; left

d-) down; right

3-) Which of the following statements is FALSE? (e)

a-) The IS curve represents equilibrium in the goods market.

b-) The equilibrium condition in the goods market is:

$$Y = C(Y - \bar{T}) + I(r) + \bar{G}$$

c-) The LM curve represents money market equilibrium.

d-) The equilibrium condition in the money market is:

$$\bar{M}/\bar{P} = L(r, Y)$$

e-) There are multiple combinations of Y and r that satisfy equilibrium in both goods and money markets

4-) An interpretation of why the IS curve slopes downward and to the right is that as income rises, national saving rises, and this increase drives the interest rate: (b)

a-) down, thereby decreasing investment.

b-) down, thereby increasing investment.

c-) up, thereby decreasing investment.

d-) up, thereby increasing investment.

5-) When the LM curve is drawn, the quantity that is held fixed is: (b)

a-) the nominal money supply.

b-) the real money supply.

c-) government spending.

d-) the tax rate.

6-) If there is an exogenous decrease in the investment, then (b)

a-) the LM curve would shift to the left.

b-) the IS curve would shift to the left.

c-) the IS curve would shift to the right.

d-) the AD curve would shift to the right.

7-) If the short -run IS-LM equilibrium occurs at a level of income below the natural rate of output, then in the long run the price level will ..., shifting the ... curve to the right and returning output to the natural rate. (d)

a-) increase; IS

b-) decrease; IS

c-) increase; LM

d-) decrease; LM

8-) A decrease in taxes will shift the: (b)

a-) IS curve to the left and decrease both the interest rate and the level of income.

b-) IS curve to the right and increase both the interest rate and the level of income.

c-) IS curve to the right and increase the level of income but decrease the interest rate.

d-) LM curve downward (to the right) and increase the level of income but decrease the interest rate

9-) What is the most direct effect when CB targets a higher nominal interest rate? (b)

a-) The money supply increases.

b-) The money supply decreases.

c-) The inflation rate increases.

d-) The inflation rate decreases.

10-) According to the IS-LM model, if government raises taxes but the CB wants to hold the interest rate constant, then the CB must ... the money supply. (b)

a-) increase

b-) decrease

c-) first increase and then decrease

d-) first decrease and then increase

11-) If people suddenly wish to hold more money at each interest rate: (d)

a-) The money demand curve will shift to the right.

b-) The LM curve will shift upward (to the left).

c-) Real income will fall.

d-) All of the above.

12-) All of the following events are consistent with the spending hypothesis as contributing to the Great Depression except: (d)

a-) the decline in investment spending on housing because of a decline in immigration in the 1930s.

b-) the decline in consumption spending caused by the stock market crash of 1929.

c-) fiscal policy to reduce the budget deficit by raising taxes in 1932.

d-) the 25-percent reduction in the money supply between 1929 and 1933.

13-) According to the Classical Economic Theory, when the Great Depression started, the government should have: (a)

a-) done nothing

b-) had a large increase in government spending

c-) gone off the Gold Standard

d-) enacted high tariffs

14-) If there is an adverse supply shock such as a sharp increase in oil prices, then in the short run (c)

a-) the AS curve would shift downward

b-) the price would increase, and income would not change.

c-) the price would increase, and income would decrease.

d-) the AD curve would shift downward

e-) the IS curve would shift to the left.

15-) Government spending may affect investment, and interest rates. Suppose government spending is now \$500 billion. If the government permanently raises spending to \$600 billion to finance national health insurance, which of the following is true for: Real GDP, Private Investment, Interest Rates (b)

a-) fall rise fall

b-) rise fall rise

c-) fall fall rise

d-) no change no change no change

e-) rise rise no change

16-) Consider an economy that is characterized by the following equations:

$C = 300 + 0.75(Y - T) - 300r$

$T = 100 + 0.2Y$

$I = 200 - 200r$

$L = 0.5Y - 500i$

$Y = 2500$, $G = 600$, $M = 133.200$ $\pi^e = 0.05$, $P = 120$

where r is the real interest rate, I is the nominal interest rate, M is the money supply, π^e is expected inflation, and P is the price level. Find the equation for the IS curve using the equilibrium condition that $Y = C^d + I^d + G$. (Answer: $Y = \{300 + 0.75[Y - (100 + 0.2Y)] - 300r\} + [200 - 200r] + 600$

$r = 2.05 - 0.0008Y$ which is the IS curve)