

Chapter 11

Classical and Keynesian Macro Analyses

11.1 The Classical Model

1) Whom among the following was a classical economist?

- A) Adam Smith
- B) A. C. Pigou
- C) David Ricardo
- D) all of the above

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB:

Question Status: Previous Edition

2) All of the following were classical economists EXCEPT

- A) Adam Smith
- B) A. C. Pigou
- C) David Ricardo
- D) John Maynard Keynes.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB:

Question Status: New

3) Which of the following is NOT an assumption of the classical model?

- A) Wages and prices are fixed.
- B) People are motivated by the own self-interest.
- C) Pure competition exists.
- D) Buyers react to changes in relative prices.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

4) The idea that supply creates its own demand is known as

- A) the law of supply.
- B) the law of demand.
- C) Keynes' law.
- D) Say's law.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 5) In the classical model, an increase in aggregate demand will cause
- A) an increase in actual output, or Gross Domestic Product (GDP).
 - B) a decrease in actual output, or Gross Domestic Product (GDP).
 - C) an increase in price level.
 - D) a decrease in price level.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 6) Classical economists assumed that
- A) prices were sticky.
 - B) individuals suffered from money illusion.
 - C) wages were inflexible.
 - D) none of the above.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 7) The first systematic attempt to explain the determinants of the price level and national levels of income, employment, consumption and real Gross Domestic Product (GDP) was made by _____ economists.
- A) Keynesian
 - B) supply-side
 - C) monetarist
 - D) classical

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Classical economists wrote from the 1770s to the _____.
- A) 1850s
 - B) 1890s
 - C) 1930s
 - D) 1960s

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 9) "Supply creates its own demand" is known as
- A) Smith's law.
 - B) Say's law.
 - C) the circular flow.
 - D) the Ricardian dilemma.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

10) Say's law says that

- A) consumption is greater than supply.
- B) desired expenditures always equal actual expenditures.
- C) people produce the goods they consume.
- D) people consume the goods they produce.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

11) Say's law argues that

- I. overproduction is typical in a market economy.
 - II. supply creates its own demand.
- A) I only B) II only C) Both I and II D) Neither I nor II

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

12) Say's law states that

- A) supply creates its own demand.
- B) supply and demand are never equal.
- C) demand may be greater than supply.
- D) supply will usually be greater than demand.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

13) The classical model uses the assumption that

- A) all wages and prices are flexible.
- B) monopoly is widespread in the economy.
- C) interest rates are not flexible.
- D) economic markets are fragile and have no tendency to move towards an equilibrium.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 14) According to the classical model, the income generated by production is
- A) enough to meet the needs of everyone in society.
 - B) enough to purchase all the goods and services produced.
 - C) fully spent on savings.
 - D) always insufficient to purchase all the goods and services produced.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 15) The implication of Say's law is that
- A) Gross Domestic Product is the same whether we use the expenditure approach or the income approach.
 - B) a barter economy is the most efficient economy.
 - C) increased consumption today leads to increased production tomorrow.
 - D) overproduction in a market economy is not possible.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 16) All the following are assumptions of the classical model EXCEPT
- A) pure competition exists.
 - B) buyers and sellers react to nominal money prices rather than to relative prices.
 - C) people are motivated by self-interest.
 - D) wages and prices are flexible.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 17) Say's law explains
- A) how long-term real Gross Domestic Product (GDP) stability is achieved in the classical model.
 - B) how long-run real Gross Domestic Product (GDP) stability is achieved in the Keynesian model.
 - C) how the economy can go into recession.
 - D) why economies experience business cycles.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

18) If a consumer buys less gasoline because gas prices increased by 10 percent, even though all other prices have also increased by 10 percent, then

- A) the consumer is paying too close attention to changes in relative prices.
- B) wages and prices are too flexible.
- C) the consumer has been fooled by money illusion.
- D) inflation is not a problem in the economy.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

19) Which of the following is an example of money illusion?

- A) An individual is willing to work more hours when the nominal wage rises by 5 percent and the overall price level rises by 4 percent.
- B) An individual is willing to work more hours when the nominal wage rises by 5% and the overall price level rises by 7 percent.
- C) An individual will neither increase nor decrease the number of hours she is willing to work when the nominal wage rises by 5 percent and the overall price level rises by 5 percent.
- D) none of the above.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

20) According to the circular flow of income and output, saving causes

- A) total output to fall.
- B) consumption expenditures and total output to fall.
- C) consumption expenditures to fall short of total output.
- D) investment spending to fall.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

21) One key assumption of the classical model is

- A) government spending plays a major role.
- B) money illusion cannot fool workers.
- C) wages are sticky.
- D) prices are sticky.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 22) Classical economists tend to
- A) see unemployment as a persistent economic problem.
 - B) believe in Keynesian economics.
 - C) reject the equality of savings and investment.
 - D) support Say's law.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 23) In the classical model, an increase in the unemployment rate
- A) will persist when the reduction in output is caused by a reduction in aggregate demand.
 - B) will result in an increase in the price level if the reduction in output is caused by a change in aggregate demand.
 - C) will likely be temporary.
 - D) is a signal of demand-pull inflation.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 24) According to classical economists,
- A) Say's law is not valid.
 - B) unemployment will not be a serious problem in a market economy.
 - C) wage levels are always "sticky."
 - D) demand stimulus is needed to produce full employment.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 25) In the classical model, aggregate demand and aggregate supply will
- A) not exist.
 - B) intersect at less than full employment.
 - C) intersect at the point of full employment.
 - D) not intersect.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 26) An individual who is suffering from money illusion is more concerned with
- | | |
|--|---|
| A) relative prices than with nominal prices. | B) relative prices than with real prices. |
| C) nominal prices than with relative prices. | D) real prices than with nominal prices. |

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 27) An individual who suffers from money illusion will
- | |
|--|
| A) feel that a doubling of prices and income improves his economic position. |
| B) concentrate on relative prices. |
| C) never be fooled by the impact of price changes on the purchasing power of income. |
| D) try to use counterfeit money. |

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 28) Suppose Paris thinks a 5 percent increase in her hourly wage as an incentive to work more hours while the price level also increases by 5 percent. Paris is said to be suffering from
- | | |
|--------------------|--------------------------------|
| A) money illusion. | B) rationality. |
| C) irrationality. | D) the effects of competition. |

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: New

- 29) The classical model assumes that
- | |
|--|
| A) imperfect competition predominates in most markets. |
| B) people have money illusion. |
| C) wages and prices are flexible. |
| D) wages are flexible but prices are not. |

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 30) All of the following are assumptions of the classical model EXCEPT
- | | |
|----------------------|--------------------------------------|
| A) inflexible wages. | B) absence of money illusion. |
| C) pure competition. | D) self-interest of economic actors. |

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

31) One tenet of classical economics is that

- A) the role of the government should be limited, since the market will always be self-correcting.
- B) the government should intervene whenever necessary to avoid any unemployment.
- C) wages and prices are "sticky downward."
- D) the government should set a minimum wage slightly above the natural market equilibrium rate.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

32) Which of the following statements is correct?

- I. If other factors are held constant, the level of employment in the economy determines real Gross Domestic Product (GDP).
 - II. According to classical economists, only voluntary unemployment exists in the long run.
- A) I only B) II only C) Both I and II D) Neither I nor II

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

33) Which of the following statements about the classical model of the economy is FALSE?

- A) Savings and investment will always be equal.
- B) Wages and prices are flexible.
- C) The economy will always move toward, or be at, full employment.
- D) Individuals pursue the public interest, not their own self-interest.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

34) If you feel you are better off because you receive a 20 percent raise even when the price level also increases by 20 percent, then you are a victim of the

- A) real income effect.
- B) money income effect.
- C) money illusion.
- D) real purchasing power effect.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

35) Which of the following is NOT an assumption of the classical model?

- A) Wages and prices are flexible.
- B) People are motivated by self-interest.
- C) Money illusion exists.
- D) Pure competition exists.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

36) A classical model of the economy predicts

- A) full employment in the long run.
- B) a 15 to 20 percent unemployment level whenever the economy is in equilibrium.
- C) the same unemployment rates as the Keynesian model.
- D) cyclical changes in the unemployment rate.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

37) A key assumption in the classical model is

- A) sticky wages.
- B) pure competition exists.
- C) sticky prices.
- D) the government plays a major role in economic problems.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

38) According to the classical model, more saving leads to more investment because

- A) the people who save are the same people who invest.
- B) the interest rate adjusts to keep investment equal to saving.
- C) saving and investment are two sides of the same activity.
- D) the interest rate is set by the federal government.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 39) At higher rates of interest,
A) households save less and businesses invest more.
B) households save less and businesses invest less.
C) households save more and businesses invest less.
D) households save more and businesses invest more.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 40) The equilibrating force in the credit market in the classical model is
A) the interest rate. B) the price level.
C) full employment. D) fiscal policy.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Classical economists argued that
A) there would always be an excess of saving over investment.
B) workers had money illusion.
C) excess savings would create unemployment.
D) a flexible interest rate would make saving equal to investment.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 42) According to classical economists, a decrease in the rate of interest will
A) increase unemployment. B) increase consumer saving.
C) increase business investment. D) increase business failures.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 43) Individuals will increase their saving as
A) the interest rate falls. B) business investment falls.
C) the rate of unemployment increases. D) the interest rate increases.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 44) In the classical model, desired saving
- A) exceeds investment.
 - B) is inversely related to real income.
 - C) is equal to desired investment.
 - D) is less than desired investment.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 45) The classical economists argued that planned saving and planned investment will always be equal because of changes in
- A) the level of real disposable income.
 - B) the interest rate.
 - C) the price level.
 - D) wages.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 46) According to classical theory, desired saving always equals investment due to changes in
- A) prices.
 - B) wages.
 - C) the interest rate.
 - D) taxes.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 47) In economics, investment is defined as
- A) the spending by businesses on capital goods and inventories.
 - B) the spending by households on human capital and durable goods.
 - C) disposable income minus consumption.
 - D) disposable income plus consumption.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 48) With respect to unemployment, the classical model states that
- A) unemployment of any kind cannot exist.
 - B) only voluntary unemployment exists.
 - C) unemployment fluctuates with the interest rate.
 - D) involuntary unemployment will always exceed voluntary unemployment.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 49) According to classical theory, full employment in the labor market occurs
- A) whenever aggregate demand is less than aggregate supply.
 - B) at a wage rate at which quantity demanded equals quantity supplied.
 - C) only when the economy has just experienced a demand shock.
 - D) only when actual expenditures are greater than desired expenditures.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 50) In the classical model, what occurs if a wage of \$20/hour results in unemployed workers?
- A) The workers will go on strike to demand that more jobs be created.
 - B) Producers will quickly create more jobs and hire the unemployed workers, so unemployment is short-lived.
 - C) The wage rate will drop, more workers will be hired, and the unemployment rate falls.
 - D) The government will step in and order firms to hire more workers.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 51) According to classical theory, total employment and real Gross Domestic Product (GDP) are
- A) unrelated.
 - B) positively related.
 - C) inversely related.
 - D) negatively related.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 52) In the classical model, the aggregate supply curve is
- A) upward sloping.
 - B) downward sloping.
 - C) horizontal.
 - D) vertical.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 53) In the classical model, real Gross Domestic Product (GDP) per year is
- A) due to supply conditions plus the extent of government intervention in the economy.
 - B) determined by supply and demand conditions together.
 - C) supply determined.
 - D) demand determined.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 54) Suppose an economy originally in long-run equilibrium experiences a decrease in aggregate demand. According to the classical model,
- A) real Gross Domestic Product (GDP) will not change but the price level will fall.
 - B) real Gross Domestic Product (GDP) will fall, and then the price level will fall also.
 - C) the price level will not change but real Gross Domestic Product (GDP) will fall.
 - D) real Gross Domestic Product (GDP) will fall, wages will fall, but the prices of goods and services will stay the same.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 55) In the classical model, a shift to the right in aggregate demand would result in
- A) a permanent increase in unemployment.
 - B) a permanent increase in real incomes.
 - C) an increase in the price level.
 - D) a permanent shift past full employment.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 56) According to the classical theory, an inward shift in aggregate demand would reduce
- A) real Gross Domestic Product (GDP) and the price level.
 - B) the price level but have no effect on real Gross Domestic Product (GDP).
 - C) real income but have no impact on the price Gross Domestic Product (GDP).
 - D) the price level but increase real Gross Domestic Product (GDP).

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 57) According to classical theory, a shift in aggregate demand will affect
- A) the price level only.
 - B) real Gross Domestic Product (GDP) only.
 - C) the level of employment only.
 - D) both real Gross Domestic Product (GDP) and the level of employment.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 58) According to the classical model, an increase in aggregate demand would
- A) lead the economy to recession.
 - B) lead the economy to a deflationary cycle.
 - C) cause an adjustment to a higher price level.
 - D) raise real Gross Domestic Product (GDP) but leave the price level unchanged.

Answer: C

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 59) In the classical model, the aggregate supply curve is
- A) upward sloping in the short run but vertical in the long run.
 - B) always vertical.
 - C) the same as the aggregate supply curve in the Keynesian model.
 - D) flat at low levels of output and then eventually slopes upward as output increases.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 60) According to the classical theory, the aggregate supply curve is
- A) downward sloping.
 - B) horizontal.
 - C) upward sloping.
 - D) vertical.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 61) According to classical theory, any changes in aggregate demand will
- A) lead to changes in the price level.
 - B) lead to changes in real Gross Domestic Product (GDP), but not in the price level.
 - C) lead to changes in both real Gross Domestic Product (GDP) and the price level.
 - D) have no affect on prices or real Gross Domestic Product (GDP).

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 62) According to Say's law,
- A) desired expenditures are always less than actual expenditures.
 - B) desired expenditures are always more than actual expenditures.
 - C) desired expenditures are always equal to actual expenditures.
 - D) desired expenditures cannot be compared with actual expenditures.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 63) Say's law implies that
- A) the willingness to purchase other goods is unrelated to the production of goods and services.
 - B) producing goods and services generates the means and the willingness to purchase other goods and services.
 - C) prices and wages are sticky downwards.
 - D) wages and prices are inflexible.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 64) In a classical model,
- A) equilibrium real GDP is supply determined.
 - B) equilibrium real GDP is demand determined.
 - C) equilibrium real GDP is determined by both aggregate supply and aggregate demand.
 - D) equilibrium real GDP is neither determined by aggregate supply nor by aggregate demand.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 65) The condition of fully flexible wages and prices was assumed by
- A) the classical economists.
 - B) the Keynesian economists.
 - C) modern economists.
 - D) no economists.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 66) The approach to understanding the determination of real GDP and the price level that emphasizes flexible wages and prices and competitive markets is
- A) the classical model.
 - B) the Keynesian model.
 - C) Adam Smith's Law.
 - D) the aggregate demand model.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 67) The classical economists assumed that
- A) monopoly was widespread in the economy.
 - B) government intervention in the economic system was necessary and helpful.
 - C) wages and prices were inflexible, especially downward.
 - D) wages and prices were flexible.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 68) According to the classical economists, an economy producing \$15 trillion in goods and services
- A) may be producing too much since the needs of people may not be this great.
 - B) simultaneously generates the income necessary to purchase \$15 trillion in goods and services.
 - C) is supplying \$15 trillion in goods and services, but could be demanding more or less than \$15 trillion in goods and services for a very long period of time.
 - D) could experience a permanent glut if no one has estimated the demand for goods and services in the economy.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 69) According to the classical economists, actual real GDP
- A) always equals actual aggregate income.
 - B) sometimes equals actual aggregate income.
 - C) never equals actual aggregate income.
 - D) is not related to aggregate income.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

70) "Supply creates its own demand" is known as

- A) Keynes' Rule.
- B) the circular flow.
- C) Smith's law.
- D) Say's law.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

71) The concept that producing goods and services generates the means and the willingness to purchase other goods and services is

- A) the Keynesian approach.
- B) money illusion.
- C) Say's Law.
- D) cost-push inflation.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

72) Say's law states that

- A) desired expenditures will equal actual expenditures.
- B) people produce only the goods they want.
- C) demand is always less than supply.
- D) overproduction is never possible because of limited resources.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

73) Which of the following statements is NOT true about Say's law?

- A) Desired expenditures will equal actual expenditures.
- B) Surpluses will be eliminated by falling prices and shortages will be eliminated by increasing prices.
- C) People produce more goods than they want for their own use only if they seek to trade them for other goods.
- D) Markets would be regularly hit by severe shortages and surpluses.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

74) Say's law implies that

- A) surpluses never occur.
- B) surpluses or shortages are possible, but only for a short time.
- C) there will always be unemployment.
- D) shortages never occur.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

75) Which of the following is NOT true according to Say's law?

- A) Supply creates its own demand.
- B) No overproduction is possible in a market economy in the long run.
- C) Desired expenditures will always be higher than actual expenditures.
- D) Producing goods and services generates the means and the willingness to purchase other goods and services.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

76) An assumption of the classical model is that

- A) money illusion is widespread.
- B) people make decisions based on nominal prices rather than real prices.
- C) prices are flexible while wages are inflexible.
- D) people are motivated by self-interest.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

77) Which of the following is NOT an assumption of the classical model?

- A) Wages and prices are flexible.
- B) Investment will lead to money illusion.
- C) People are motivated by self-interest.
- D) Pure competition exists.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

78) Which of the following is NOT an assumption of the classical model?

- A) Buyers and sellers react to changes in relative prices.
- B) Households want to maximize economic well being.
- C) No single buyer or seller of a commodity can affect its price.
- D) Wages and prices will move freely in the upward direction but not the downward direction.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

79) Given the assumptions of the classical model,

- A) the economy will often experience recessions and expansions.
- B) expansion will be the normal condition, but recessions will often be severe and require government intervention.
- C) the macroeconomy is erratic, and problems will often be increased over time.
- D) the market is a self-correcting mechanism.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

80) A consumer who buys more coffee when the price of coffee falls 5 percent, while all other prices fell 5 percent too, is

- A) suffering from money illusion.
- B) worrying too much about a coming recession.
- C) behaving in accordance with classical economic theory.
- D) paying too much attention to changes in relative prices.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

81) Joe's increase in wages has been identical to the increase in the price level. Joe thinks that he is better off and has increased his expenditures. Joe's behavior is consistent with

- A) Say's Law.
- B) the classical model.
- C) a vertical aggregate supply curve.
- D) money illusion.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

82) Money illusion is

- A) a basic condition that all classical economists assume people have.
- B) when people think they are better off when their income increases even though prices have increased by the same amount.
- C) when people are motivated by self-interest.
- D) could not exist if the economy did not have competitive markets.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

83) Saving represents

- A) a source of funds for business investment.
- B) a normal part of the circular flow of income and output.
- C) an injection to the circular flow of income and output.
- D) a counter-example to Say's Law that the classical economists never considered.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

84) Leakages in the circular flow model are

- A) caused by people not acting rational.
- B) possible when unemployment exists.
- C) reflected in the vertical long-run aggregate supply curve.
- D) caused by people saving instead of spending.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

85) In an economy with no government and no international trade, consumption expenditures will be less than the total value of goods and services when

- A) investment is zero.
- B) saving is zero.
- C) people save some of their income.
- D) people barter rather than use money in making exchanges.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 86) Saving is not a problem in the classical model because
- A) the classical economists assume that saving was beneficial to people for retirement.
 - B) saving would be spent by consumers eventually.
 - C) interest rates are flexible, and savings were channeled into investment.
 - D) savers and investors are the same people.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 87) Which of the following statements is true?
- A) There is a direct relationship between investment and the interest rate.
 - B) There is an inverse relationship between investment and the interest rate.
 - C) There is no relationship between investment and the interest rate.
 - D) Investment is always less than savings.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 88) At higher rates of interest,
- A) households save less because it is more expensive to save.
 - B) households save more because they get a greater return on their savings.
 - C) businesses demand more investment because future profitability is likely to be greater.
 - D) businesses demand more investment because there are more funds available to invest.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 89) Regarding unemployment, the classical model implies that
- A) unemployment always exists.
 - B) unemployment cannot exist.
 - C) voluntary unemployment is zero, but involuntary unemployment often is fairly high.
 - D) only voluntary unemployment exists.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 90) In the classical model,
- A) unemployment will never exist since workers will be willing to accept lower wages and will then be able to find work.
 - B) unemployment will never exist because employers will be willing to pay the wage rate demanded by the workers.
 - C) wages will go up but never go down.
 - D) full employment will never be reached.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 91) Higher unemployment tends to be associated with
- A) the classical model.
 - B) higher real GDP.
 - C) higher nominal GDP.
 - D) lower real GDP.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 92) In the classical model, high unemployment due to a change in aggregate demand
- A) can persist for an indefinite period of time.
 - B) will return to its normal level quickly as wages adjust.
 - C) will persist if due to a supply shock but not if due to a demand shock.
 - D) never exists because unemployment can never deviate from its normal level.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 93) The aggregate supply curve in the classical model is
- A) horizontal.
 - B) vertical.
 - C) upward sloping.
 - D) downward sloping.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 94) Which of the following statements is true about the long-run and short-run aggregate supply curve in the classical model?
- A) The long-run aggregate supply curve is vertical, and the short-run curve is horizontal.
 - B) The long-run aggregate supply curve is not defined, and the short run curve is vertical.
 - C) The long-run and short-run curves start out horizontal and eventually become vertical.
 - D) The long-run curve is vertical, and there is no short-run curve since all adjustments occur quickly.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 95) The classical model makes little distinction between the long run and short run because
- A) the model has not been fully developed yet.
 - B) the classical economists knew that we are always operating in the short run.
 - C) current changes influence the long run, so it is not possible to plan for the future.
 - D) wages and prices adjust so fast that the economy is quickly moving towards the long run.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 96) In the classical model, the aggregate supply curve
- A) is horizontal.
 - B) is positively sloped.
 - C) is consistent with the natural rate of unemployment.
 - D) is not related to the employment rate.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 97) In the classical model, an increase in aggregate demand will lead to an increase in wage rates while a decrease in aggregate demand will
- A) leave wages unchanged since workers will not take a cut in pay.
 - B) decrease wages.
 - C) increase wages since business will be desperate for labor.
 - D) change the price of capital.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

98) Which of the following is NOT an assumption of the classical model?

- A) Pure competition.
- B) Wages and prices are flexible.
- C) People are motivated by self-interest.
- D) Wage rigidity.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

99) In the classical model, a change in aggregate demand

- A) causes a change in long-run real GDP but not in the price level.
- B) causes a change in the price level but not in the long-run real GDP.
- C) causes changes in both the long-run real GDP and in the price level.
- D) has no effect on either real GDP or the price level.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

100) An economy in long-run equilibrium experiences an increase in aggregate demand. According to the classical model,

- A) the price level will rise first, then real GDP will increase.
- B) the price level and real GDP will increase at the same time.
- C) the price level will increase, but real GDP will not change.
- D) the price level will increase, but real GDP will decrease.

Answer: C

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

101) In the classical model,

- A) the level of real GDP per year does not depend on the level of aggregate demand.
- B) the level of GDP is demand determined.
- C) changes in aggregate supply affect the price level, not real GDP.
- D) the level of GDP determines prices independent of demand.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

102) In the classical model,

- A) a decrease in aggregate demand will lead to a decrease in the price level and a decrease in real GDP.
- B) changes in aggregate supply leave real GDP unchanged.
- C) a decrease in aggregate demand will lead to an increase in the price level and a decrease in real GDP.
- D) changes in aggregate demand affect only the price level, not real GDP.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

103) Which of the following is NOT a key assumption of the classical model?

- A) There is a single monopoly seller in many markets for goods and services.
- B) People cannot be fooled by money illusion.
- C) People are motivated by self-interest.
- D) Wages and prices are flexible.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

104) Say's law implies that

- A) wages and prices are not flexible.
- B) people supply goods and services to the market because they want to consume other goods and services.
- C) government regulation is needed to prevent shortages from becoming a problem.
- D) government regulation is needed to prevent surpluses from becoming a problem.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

105) In the classical model, the interest rate will adjust to equate

- A) consumption spending with real GDP.
- B) saving with investment.
- C) the economic growth rate with the growth rate of import spending.
- D) export spending with import spending.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 106) Why is there NO persistent unemployment in the classical model?
- A) The wage level adjusts to eliminate unemployment.
 - B) The interest rate adjusts to eliminate unemployment.
 - C) The rate of economic growth is always high enough to allow those who want to work at current wages to find jobs.
 - D) Unionization creates job security for workers.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 107) Which of the following is NOT an assumption of the classical system?
- A) Pure competition exists.
 - B) People are motivated by self interest.
 - C) Wages and prices are inflexible.
 - D) There is no money illusion.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 108) In the classical model, changes in interest rates will always ensure that
- A) consumption equals production.
 - B) saving equals investment.
 - C) consumption equals investment.
 - D) consumption equals income.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 109) The concept of Say's law can be summed up by the phrase,
- A) "supply creates its own demand."
 - B) "demand creates its own supply."
 - C) "supply and demand are equivalent concepts."
 - D) "supply and demand are irrelevant concepts."

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB:

Question Status: Previous Edition

- 110) Full employment in the classical model is maintained by
- A) flexible interest rates.
 - B) flexible wage rates.
 - C) flexible prices.
 - D) flexible income.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

111) In the classical model, the aggregate supply curve is

- A) a horizontal line.
- B) an upward sloping line.
- C) a vertical line.
- D) a combination of horizontal, upward sloping, and vertical lines.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

112) In the classical model, a rightward shift in the aggregate demand curve will, in the long run,

- A) increase real GDP and the price level.
- B) increase real GDP and will not change the price level.
- C) decrease real GDP and will not change the price level.
- D) not change real GDP and will increase the price level.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

113) Why is wage and price flexibility an important assumption of the classical model?

- A) Flexible wages and prices guarantee that there will be no scarcity.
- B) Flexible wages and prices allow business firms to fool their workers through the money illusion.
- C) Flexible wages and prices allow business firms to fool their customers through the money illusion.
- D) Flexible wages and prices allow markets to reach equilibrium.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

114) Which one of the following statements is NOT true?

- A) The classical model assumes that people suffer from money illusion.
- B) The classical model assumes that people are motivated by self-interest.
- C) The classical model assumes that pure competition exists.
- D) The classical model assumes that no single seller of a commodity can affect its price.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

115) What is true when the credit market is in equilibrium?

- A) Desired saving equals desired investment.
- B) Desired employment equals the number of jobs available.
- C) Desired consumption spending equals the total of saving plus investment.
- D) The legal minimum wage equals the actual wage.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

116) What is true of the aggregate supply curve in the classical model?

- A) The aggregate supply curve is downward sloping.
- B) The aggregate supply curve is horizontal.
- C) The aggregate supply curve is vertical.
- D) The aggregate supply curve is not determined by the level of employment.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

117) Long-run aggregate supply curve in the classical model

- A) is the level of real GDP corresponding to 100 percent labor force participation.
- B) is the level of real GDP corresponding to the natural rate of unemployment.
- C) is a downward sloping line.
- D) is determined by the capital stock of the economy, not the labor force.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

118) In the classical model, what is the result of an increase in aggregate demand?

- A) Real GDP increases, and the price level remains constant.
- B) Real GDP decreases, and the price level remains constant.
- C) The price level increases, and real GDP remains constant.
- D) The price level decreases, and real GDP remains constant.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

119) Which one of the following is true?

- A) The intersection of aggregate demand and aggregate supply identifies an equilibrium interest rate and an equilibrium wage level.
- B) The intersection of aggregate demand and aggregate supply identifies an equilibrium interest rate and an equilibrium level of exports.
- C) The intersection of aggregate demand and aggregate supply identifies an equilibrium level of employment and an equilibrium level of investment.
- D) The intersection of aggregate demand and aggregate supply identifies an equilibrium price level and an equilibrium level of real GDP.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

120) In the classical model, how do shifts in aggregate demand affect real GDP?

- A) Real GDP will remain unchanged.
- B) Increases in aggregate demand increase real GDP.
- C) Increases in aggregate demand decrease real GDP.
- D) Decreases in aggregate demand increase real GDP.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

121) Which of the following is NOT an assumption of the classical model?

- A) Government intervention is necessary for economic stability.
- B) No one buyer or seller of a good or service can affect the price of the good or service.
- C) People are motivated by self-interest.
- D) People are not fooled by the money illusion.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

122) According to the classical model, desired saving is

- A) a function of real GDP.
- B) equal to desired investment.
- C) identical to the demand for saving at each level of real GDP.
- D) affected by the money illusion at low income levels.

Answer: B

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

123) According to the classical model, investment

- A) is a function of real GDP.
- B) is a function of the nominal GDP.
- C) is inversely related to the interest rate.
- D) is influenced by the money illusion at low income levels.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

124) The classical model indicates that at the equilibrium interest rate, saving is

- A) equal to investment.
- B) greater than investment.
- C) unnecessary for investment.
- D) less than investment.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

125) If your income and the price level both rise by 5 percent, and you think you now have more real income, you are suffering from

- A) diminishing marginal expectations.
- B) leakages.
- C) injections.
- D) money illusion.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

126) Long-run unemployment in the classical model is considered to be impossible because

- A) the government will intervene to aid the unemployed.
- B) job placement and training programs are rampant in the United States.
- C) flexible prices and wages keep workers fully employed.
- D) the labor supply is horizontal.

Answer: C

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

127) The idea that "supply creates its own demand" is attributed to which of the following economists?

- A) Adam Smith
- B) David Ricardo
- C) J. B. Say
- D) A. C. Pigou

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 128) Which of the following is NOT an assumption of the classical model?
- A) Pure competition exists.
 - B) Wages and prices are flexible.
 - C) Government spending is necessary to achieve economic stability.
 - D) People are motivated by self-interest.

Answer: C

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 129) According to Say's law,
- A) supply creates its own demand.
 - B) demand creates supply.
 - C) changes in supply create supply-side inflation.
 - D) changes in demand create demand-side inflation.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 130) According to the classical model,
- A) long-term unemployment is unavoidable.
 - B) unemployment is a temporary phenomenon.
 - C) unemployment only exists during periods of war.
 - D) the natural rate of unemployment is zero.

Answer: B

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 131) According to the classical model, prices and wages
- A) are flexible.
 - B) must be set by government.
 - C) move downward easily, but are "sticky" upward.
 - D) move upward easily, but are "sticky" downward.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB:

Question Status: Revised

- 132) According to classical economists, the credit market reaches an equilibrium when
- A) planned investment equals government expenditures.
 - B) desired investment equals planned investment.
 - C) desired investment equals planned changes in aggregate supply.
 - D) desired investment equals desired saving.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 133) According to classical economists, when aggregate demand decreases,
- A) unemployment is reduced, the price level increases, and equilibrium real GDP is reached.
 - B) unemployment is reduced, the price level decreases, and equilibrium real GDP is reached.
 - C) unemployment temporarily increases, the price level increases, and equilibrium real GDP is reached.
 - D) unemployment temporarily increases, the price level decreases, and equilibrium real GDP is reached.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 134) A congressman states, "If a government attempts to increase employment through increased government spending, all we will end up with is a higher price level." This congressman assumes that the
- A) aggregate demand curve is a horizontal line.
 - B) aggregate demand curve is a vertical line.
 - C) aggregate supply curve is a horizontal line.
 - D) aggregate supply curve is a vertical line.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 135) Q: How many economists does it take to screw in a light bulb?
- A: None. If the light bulb really needed changing, market forces would have already caused it to happen.
- This joke represents the view of
- A) classical economists.
 - B) Keynesian economists.
 - C) economists who conclude that money illusion is widespread.
 - D) economists who conclude that wages and prices are inflexible.

Answer: A

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 136) Classical economists suggest that unemployment is a short-lived phenomenon because
- A) wages adjust quickly to equilibrate quantity of labor demanded with quantity of labor supplied.
 - B) wages remain unchanged when the quantity of labor demanded exceeds the quantity of labor supplied.
 - C) wages remain unchanged when the quantity of labor supplied exceeds the quantity of labor demanded.
 - D) wages tend to rise slowly when the quantity of labor demanded equals the quantity of labor supplied.

Answer: A

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 137) Which statement best characterizes the classical economists' view of saving and investment?
- A) Saving equals investment
 - B) Saving exceeds investment
 - C) Saving is less than investment
 - D) Saving and investment are not related to one another

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

- 138) In the classical view, if desired saving exceeds desired investment,
- A) government spending must fall.
 - B) government spending must rise.
 - C) the interest rate would decline.
 - D) the interest rate would increase.

Answer: C

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 139) In the classical view, flexible wage rates would assure
- A) low inflation.
 - B) high rates of unemployment.
 - C) high secular inflation rates.
 - D) full employment.

Answer: D

Diff: 1

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

140) In the classical model, what happens to the level of real GDP if aggregate demand increases?

- A) Real GDP increases.
- B) Real GDP decreases.
- C) Real GDP would increase at first, then decrease.
- D) Real GDP would remain the same, at equilibrium.

Answer: D

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

141) "Supply creates its own demand" implies that

- A) the very act of supplying a particular level of goods and services necessarily equals the level of goods and services demanded.
- B) the very act of demanding a particular level of goods and services necessarily equals the level of goods and services supplied.
- C) the government will buy up any surplus of goods and services in a country to avoid economic problems.
- D) the very act of supplying a particular level of goods and services will not necessarily equal the level of goods and services demanded.

Answer: A

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

142) What is Say's Law and what does it mean?

Answer: Say's Law is: Supply creates its own demand. It means that a general glut or overproduction is not possible. The very process of producing specific goods is proof that other goods are desired. The income received from selling one's goods is used to purchase other goods. While some goods may have a surplus, others will have a shortage, and these would be corrected by price changes. There will not be an excess quantity supplied of all goods.

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

143) Saving is a leakage from the circular flow. Why didn't the classical economists think saving might cause consumption expenditures to fall short of total output?

Answer: The classical economists believed that each dollar saved would be invested by firms so that the leakage of saving would be exactly matched by an injection of investment spending. The interest rate would adjust to ensure that saving equaled investment.

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 144) "In the classical model, the equilibrium level of real Gross Domestic Product (GDP) is completely supply-determined." Do you agree or disagree? Why?

Answer: Agree. The long-run aggregate supply curve is vertical, so the equilibrium level of real Gross Domestic Product (GDP) is determined by the location of the aggregate supply curve. Shifts in aggregate demand affect only the price level.

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 145) Why did the classical economists think that large-scale unemployment was not possible in a market economy?

Answer: The classical economists accepted Say's Law, which indicated that desired expenditures will equal actual expenditures. The act of producing indicates one wants to buy other goods. A surplus or shortage in one market would soon be corrected because prices and wages were assumed to be flexible, and they assumed people could not be fooled by money illusion. They also assumed pure competition and that people were motivated by self-interest. Combining all these ideas, they concluded that full employment would be the norm.

Diff: 3

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Previous Edition

- 146) "The level of employment in an economy determines its real GDP, other things held constant." Do you agree or disagree? Why? What assumptions are necessary for your conclusion based on the classical model?

Answer: Agree. Production requires workers so the more workers that are employed the greater total production. This assumes that workers who are employed actually work and are productive.

Diff: 2

Topic: 11.1 The Classical Model

AACSB: Analytic skills

Question Status: Revised

11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

- 1) According to the Keynesian model, the short-run aggregate supply (SRAS) curve is horizontal when

- A) real Gross Domestic Product (GDP) is at full capacity but prices are not flexible.
- B) there are no unemployed resources and wages do not change when prices change.
- C) prices react to an aggregate demand shock but real Gross Domestic Product (GDP) does not.
- D) there are unemployed resources and prices do not fall when aggregate demand falls.

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 2) The Keynesian model is basically
- A) a long-run theory.
 - B) a short-run theory.
 - C) a combination of long- and short-run theories.
 - D) a theory about the economy in both the long run and the short run.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 3) According to Keynes, involuntary unemployment is possible because of
- A) the existence of capital markets.
 - B) long-term labor contracts and the existence of labor unions.
 - C) government interference in the market economy.
 - D) inflation.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 4) A decrease in aggregate demand will cause
- A) prices to fall according to classical economists, and unemployment to increase according to Keynes.
 - B) prices to fall and unemployment to increase according to both classical economists and Keynes.
 - C) aggregate supply to fall according to classical economists, and prices to fall according to Keynes.
 - D) aggregate supply to fall according to Keynes, and unemployment to increase according to classical economists.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 5) Involuntary unemployment
- A) occurs when the wage rate is below the equilibrium wage rate.
 - B) exists when there is an excess quantity of labor supplied.
 - C) will increase as the wage rate falls.
 - D) exists when there is a shortage of labor.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 6) If a shift in aggregate demand only affects real Gross Domestic Product (GDP), then the short-run aggregate supply (SRAS) curve must be

A) vertical. B) upward sloping.
C) horizontal. D) downward sloping.

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 7) The Keynesian short-run aggregate supply (SRAS) curve is

A) upward sloping. B) vertical.
C) horizontal. D) downward sloping.

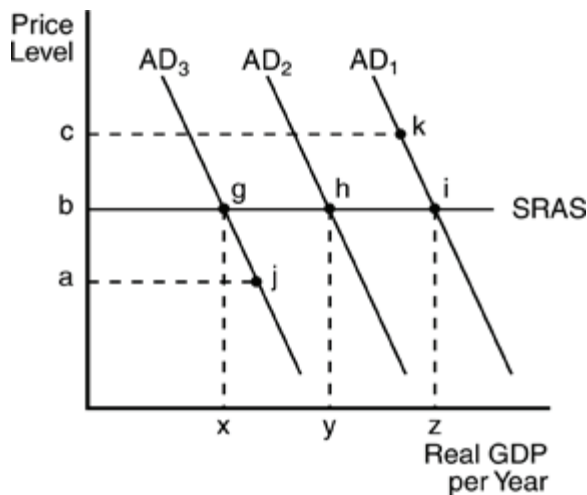
Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition



- 8) The above figure presents the view of the economy according to

A) Keynesian economics. B) classical economics.
C) microanalysis. D) Ricardian economics.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Refer to the above figure. Suppose the current aggregate demand is represented by AD₂. If aggregate demand falls to line AD₃, then
- A) the new equilibrium will be at j.
 - B) the new equilibrium will be at k.
 - C) the new equilibrium real Gross Domestic Product (GDP) will be x.
 - D) a new price level will be established at a.

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 10) Keynes argued that
- I. Capitalism did not always lead to full employment.
 - II. Nominal prices were more important than relative prices.
- A) I only
 - B) II only
 - C) Both I and II
 - D) Neither I nor II

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 11) The original Keynesian economic theory states that
- A) the short-run aggregate supply (SRAS) curve is always vertical.
 - B) many prices would not decline even when aggregate demand decreases.
 - C) wages tend to fall more quickly than the overall price level.
 - D) the economy naturally self-regulates so as to reach full employment quickly.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 12) Keynes argued that an economy could be in equilibrium when the economy was
- A) operating at maximum potential capacity.
 - B) operating with some unutilized productive capacity.
 - C) trying to operate at some output level beyond its potential capacity.
 - D) operating either at full productive capacity or at less than full capacity.

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 13) Keynes and his followers believed that
- A) capitalism was one economic system that guaranteed full employment.
 - B) wages and prices in the short run were flexible.
 - C) the economy could not operate at any level of real Gross Domestic Product (GDP) less than full capacity.
 - D) there was no guarantee that a capitalist economy would reach a full employment equilibrium.

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 14) A key component of the Keynesian model is that
- A) prices are sticky.
 - B) prices are flexible.
 - C) wages are flexible.
 - D) people are not fooled by money illusion.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 15) According to Keynes, once a system attains an economy-wide equilibrium,
- A) there may or may not be excess productive capacity.
 - B) planned consumption will be zero.
 - C) planned investment will be zero.
 - D) the economy will be at full productive capacity.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 16) The Keynesian portion of the short-run aggregate supply (SRAS) curve
- A) is horizontal.
 - B) is vertical.
 - C) slopes upward.
 - D) slopes downward.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

17) The simple Keynesian model assumes that

- A) gross private domestic investment exceeds net investment by the capital consumption allowance.
- B) prices, especially the price of wages, are "sticky downward."
- C) there will never be any excess capacity in the short run.
- D) aggregate demand will always equal aggregate supply.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

18) The Keynesian portion of the short-run aggregate supply (SRAS) curve implies

- A) an upward slope.
- B) no price level changes.
- C) a downward slope.
- D) flexible prices and wages.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

19) The Keynesian short-run aggregate supply (SRAS) curve

- A) shows that real Gross Domestic Product (GDP) will increase only if the price level increases.
- B) assumes a full-employment level of real Gross Domestic Product (GDP).
- C) is horizontal.
- D) does not reflect any changes in nominal Gross Domestic Product (GDP).

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

20) In an economic downturn, sticky wages and prices reduce the economy's speed of adjustment because

- A) businesses are unable to adjust quickly to changes in aggregate demand.
- B) they cause deflation.
- C) hyperinflation will likely occur.
- D) union workers would likely quit and look for work elsewhere.

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 21) Keynes suggested that the short-run aggregate supply (SRAS) curve
- A) is vertical.
 - B) is horizontal.
 - C) slopes downward.
 - D) is not a relevant concept.

Answer: B

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 22) Keynesian economics predicts that if government policy makers deem current equilibrium real Gross Domestic Product (GDP) to be "too low," then an appropriate policy action would be to
- A) do nothing, because the economy is self-adjusting.
 - B) raise government spending, thereby increasing aggregate demand and pushing up real Gross Domestic Product (GDP) with little or no inflationary consequences.
 - C) increase taxes, thereby causing aggregate demand to increase and inducing a rise in real Gross Domestic Product (GDP) with little or no inflationary consequences.
 - D) reduce the money stock, thereby causing aggregate demand to decrease and inducing a rise in fall in the price level that generates an increase in total planned expenditures.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 23) The short-run aggregate supply (SRAS) curve represents the relationship between
- A) the price level and the real Gross Domestic Product (GDP) without full adjustment or full information.
 - B) the price level and the real Gross Domestic Product (GDP) without full adjustment but with full information.
 - C) the price level and the nominal Gross Domestic Product (GDP).
 - D) the decisions of producers and the decisions of consumers.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 24) In the short run, an increase in the price level induces firms to expand production because
- A) prices of inputs are held constant, so the higher prices for firms' products imply that it is profitable to expand production.
 - B) each firm must keep its production level up to the level of its rivals, and some firms will expand production as the price level increases.
 - C) higher prices allow firms to hire more inputs by offering higher prices for inputs, which increases productivity and profits.
 - D) they can increase profits by increasing maintenance costs.

Answer: A

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 25) The relationship between the price level and the real Gross Domestic Product (GDP) without full adjustment or full information is represented by
- A) the long-run aggregate supply curve.
 - B) the short-run aggregate supply curve.
 - C) the aggregate demand curve.
 - D) the distance between the long-run aggregate supply curve and the short-run aggregate supply curve.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 26) According to Keynes, the classical model could not explain
- A) a recession or depression.
 - B) periods of rising unemployment.
 - C) a long-term economic decline.
 - D) periods of rising interest rates.

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 27) In the simple Keynesian portion of the upward sloping short-run aggregate supply curve,
- A) equilibrium real GDP is demand-determined.
 - B) equilibrium real GDP is supply-determined.
 - C) equilibrium real GDP is neither determined by aggregate supply nor by aggregate demand.
 - D) equilibrium real GDP is determined by both aggregate supply and aggregate demand.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 28) The short-run aggregate supply curve is horizontal when
- A) prices are inflexible and the economy is at full employment.
 - B) there are unemployed resources and prices do not increase when aggregate demand increases.
 - C) there are unemployed resources and prices do not decrease when aggregate supply increases.
 - D) there are no unemployed resources and prices do not increase when aggregate demand or supply increases.

Answer: B

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 32) According to Keynes, wages are inflexible because
- A) of the minimum wage set by government.
 - B) of unions and long-term contracts.
 - C) workers do not behave in their own self-interest.
 - D) the economy is never in the long run.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 33) Which of the following is a true statement?
- A) A decrease in aggregate demand was not possible according to the classical economists but was possible according to Keynes.
 - B) A decrease in aggregate demand has no short-run effects according to the classical economists but had significant effects according to Keynes.
 - C) Classical economists believed real GDP adjusted more than prices when aggregate demand fell, while Keynes argued that prices adjusted more than output.
 - D) Classical economists believed price adjusted more than output when aggregate demand fell, while Keynes argued real GDP adjusted more than prices.

Answer: D

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 34) The simplified Keynesian model
- A) holds the price level constant.
 - B) holds real GDP constant.
 - C) assumes investment and saving are always equal.
 - D) assumes unemployment is unrelated to real GDP.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 35) According to Keynes,
- A) the short-run aggregate supply curve is vertical.
 - B) nominal wages and/or prices are sticky.
 - C) money illusion does not exist.
 - D) markets are perfectly competitive

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 36) The approach to understanding the determination of real GDP and the price level that emphasizes incomplete adjustment in the prices of many goods is
- A) the classical model.
 - B) the Keynesian model.
 - C) Say's Law.
 - D) the aggregate demand model.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 37) To explain the existence of excess capacity, Keynes argued that
- A) prices and wages are flexible, and eventually markets would go back to equilibrium.
 - B) the long run average cost curve should not occur at the full employment level.
 - C) the aggregate demand curve can be manipulated by advertising.
 - D) prices and wages are inflexible in the downward direction.

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 38) Which of the of the following is a basic difference between the classical model and the Keynesian model in which the Keynesian short-run aggregate supply curve exists?
- A) The classical model assumes that the long run aggregate supply curve is vertical, while the Keynesian model assumes the long run aggregate supply curve is horizontal.
 - B) The classical model assumes that the position of the long run aggregate supply curve is determined by full employment, while the Keynesian model assumes that the long run aggregate supply curve will be to the left of full employment.
 - C) The classical model assumes that the level of real GDP is supply determined, while the Keynesian model assumes that it is demand determined.
 - D) The classical model uses real GDP, while the Keynesian model uses nominal GDP.

Answer: C

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 39) The Keynesian short-run aggregate supply curve is horizontal because
- A) it represents the full employment level of real GDP.
 - B) it reflects the absence of money illusion.
 - C) it reflects wage and price inflexibility.
 - D) it represents Say's law.

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 40) In the Keynesian model in which the Keynesian short-run aggregate supply curve exists,
- A) the short-run aggregate supply curve determines real GDP.
 - B) the aggregate demand curve determines the price level.
 - C) unemployment cannot persist for long periods of time.
 - D) aggregate demand determines real GDP per year.

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Q: How many economists does it take to change a light bulb?
- A: All. Because then you will generate employment, more consumption, moving the aggregate demand curve to the right.
- This joke represents the view of
- A) classical economists.
 - B) Keynesian economists.
 - C) economists who contend that money illusion never occurs.
 - D) economists who conclude that wages and prices are very flexible.

Answer: B

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 42) Which one of the following statements is true?
- A) The classical model cannot explain periods of prolonged unemployment.
 - B) The Keynesian model cannot explain periods of prolonged unemployment.
 - C) The Keynesian model assumes complete flexibility of wages and prices.
 - D) The Keynesian model shows that the level of real GDP is supply-determined.

Answer: A

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 43) Keynes argued that because of sticky prices and wages,
- A) the short-run aggregate supply curve could be horizontal.
 - B) the short-run aggregate supply curve is probably vertical.
 - C) the long-run aggregate supply curve slopes downward.
 - D) the aggregate demand curve is vertical.

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 44) In the Keynesian model which includes the Keynesian short-run aggregate supply curve,
- A) an increase in aggregate demand would cause the price level to rise, but does not change the level of real GDP.
 - B) an increase in aggregate demand causes real GDP to rise without changing the price level.
 - C) an increase in aggregate demand changes neither the price level nor the level of real GDP.
 - D) an increase in aggregate demand causes real GDP and the price level to decrease.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 45) If the economy is operating at a point at which short-run aggregate supply is horizontal, then
- A) real GDP cannot expand.
 - B) real GDP cannot contract.
 - C) increases in aggregate demand do not increase the price level.
 - D) then increases in aggregate demand do not increase real GDP.

Answer: C

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 46) Why is persistent unemployment a possibility in the Keynesian model but NOT in the classical model?
- A) The Keynesian model assumes that people work for motives other than those of earning an income for themselves and supporting a family.
 - B) The Keynesian model assumes that nominal wages are inflexible downward.
 - C) The Keynesian model assumes that the level of real GDP is inflexible.
 - D) The Keynesian model assumes that workers can lose their jobs to foreign competition during economic downturns.

Answer: B

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 47) The Keynesian short-run aggregate supply curve
- A) is horizontal.
 - B) is vertical.
 - C) reflects the fact that real GDP is supply-determined.
 - D) reflects the fact that real GDP does not vary with changes in aggregate demand.

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

48) Which one of the following statements is true?

- A) The shape of the Keynesian short-run aggregate supply curve is based on the conclusion that domestic workers are harmed by imports.
- B) The shape of the Keynesian short-run aggregate supply curve is based on the conclusion that there is no correlation between the level of real GDP and the employment level.
- C) The shape of the Keynesian short-run aggregate supply curve is based on the conclusion that increases in aggregate demand can boost output in the short term.
- D) The shape of the Keynesian short-run aggregate supply curve is based on the conclusion that increases in aggregate demand will increase the price level, but will leave real GDP unaffected in the short term.

Answer: C

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

49) Which one of the following statements is true?

- A) The actual behavior of prices and real GDP during the decade of the 1930s is consistent with the classical model.
- B) The actual behavior of prices and real GDP during the decade of the 1930s is consistent with the Keynesian model.
- C) The actual behavior of prices and real GDP during the decade of the 1930s is consistent with the idea that increases in aggregate demand will increase the price level but will leave real GDP unchanged.
- D) The actual behavior of prices and real GDP during the decade of the 1930s is consistent with a vertical short-run aggregate supply curve.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

50) The short-run aggregate supply curve is horizontal if

- A) resources were fully utilized.
- B) there are unutilized resources in the economy.
- C) resources are perfectly adaptable between production processes.
- D) there are high inflation rates.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 51) The Keynesian contention that the short-run aggregate supply curve is horizontal is based on the assumption that there are
- A) sticky prices.
 - B) flexible prices.
 - C) real prices.
 - D) upward sloping prices.

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 52) The short-run aggregate supply curve is a relationship between
- A) unemployment and real GDP.
 - B) inflation and time.
 - C) real GDP and price level.
 - D) capital goods and consumer goods.

Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 53) The Keynesian short-run aggregate supply curve is demonstrated graphically as a
- A) vertical line.
 - B) horizontal line.
 - C) upward sloping curve.
 - D) downward sloping curve.

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 54) Keynesian economists argue that
- A) equilibrium real GDP is demand-determined.
 - B) equilibrium real GDP is supply-determined.
 - C) equilibrium real GDP can be reached only in a theoretical economy.
 - D) reaching equilibrium real GDP always results in inflation.

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 55) Keynesian economists argue that
- A) prices and wages are flexible.
 - B) prices and wages must be set by government.
 - C) prices and wages are subject to downward "stickiness."
 - D) prices and wages depend on the decisions by the Federal Reserve Bank.

Answer: C

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

56) Keynesian economists argue that

- A) the natural rate of unemployment is below the actual rate.
- B) unemployment is a long-lasting phenomenon in the economy.
- C) unemployment only exists during periods of war in the economy.
- D) the natural rate of unemployment is zero.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

57) John Maynard Keynes developed his economic theories in the

- A) 1870s.
- B) 1900s.
- C) 1930s.
- D) 1960s.

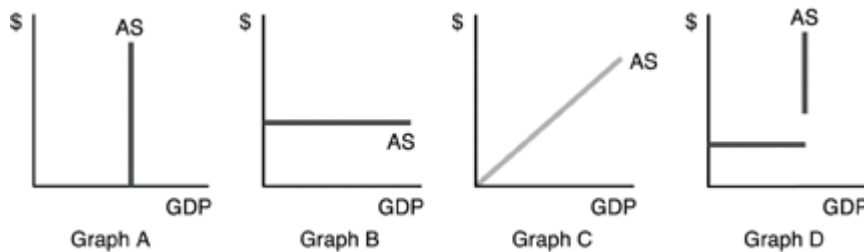
Answer: C

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB:

Question Status: Previous Edition



58) Refer to the above figure. Which of the graphs is consistent with the Keynesian short-run aggregate supply curve?

- A) Graph A
- B) Graph B
- C) Graph C
- D) Graph D

Answer: B

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

59) Refer to the above figure. Which of the graphs is consistent with the long-run aggregate supply curve?

- A) Graph A
- B) Graph B
- C) Graph C
- D) Graph D

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 60) Which of the following will NOT shift the Keynesian short-run aggregate supply curve?
- A) a change in technology
 - B) a change in profit expectations
 - C) a change in input prices
 - D) a change in the price level

Answer: D

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 61) Which of the following will shift the Keynesian short-run aggregate supply curve downward and to the right?
- A) a rise in the price level
 - B) a fall in the price level
 - C) a decrease in input costs
 - D) an increase in input costs

Answer: C

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 62) The horizontal short-run aggregate supply curve
- A) assumes that wages and all other input prices are constant.
 - B) shows that real GDP can be increased only when prices increase.
 - C) assumes that there is full employment in the economy.
 - D) assumes that opportunity cost is constant.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 63) According to Keynes, the "stickiness" of wage rates could best be explained by
- A) minimum wage laws.
 - B) unions and long-term labor contracts.
 - C) short-term labor contracts.
 - D) government interference.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 64) According to Keynesian economics, if there are unutilized resources in the economy and aggregate demand increases,
- A) real GDP will rise and price level will remain constant.
 - B) real GDP will fall and price level will remain constant.
 - C) real GDP will rise and price level will rise.
 - D) real GDP will rise and price level will fall.

Answer: A

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 65) According to Keynesian economics, if there are unutilized resources in the economy and aggregate demand decreases,
- A) real GDP will rise and price level will remain constant.
 - B) real GDP will fall and price level will remain constant.
 - C) real GDP will rise and price level will rise.
 - D) real GDP will rise and price level will fall.

Answer: B

Diff: 1

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 66) Keynesian economists would likely argue that the classical model is which of the following?
- A) a long-run theory
 - B) a short-run theory
 - C) both a long-run and short-run theory
 - D) a sticky price theory

Answer: A

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 67) Some economists believe that a positive aggregate demand shock to an economy with large amounts of excess capacity and unemployment does not necessarily cause an increase in prices. Economists who adhere to this belief are followers of
- A) classical economics.
 - B) Say's laws of economics.
 - C) Keynesian economics.
 - D) supply-side economics.

Answer: C

Diff: 1

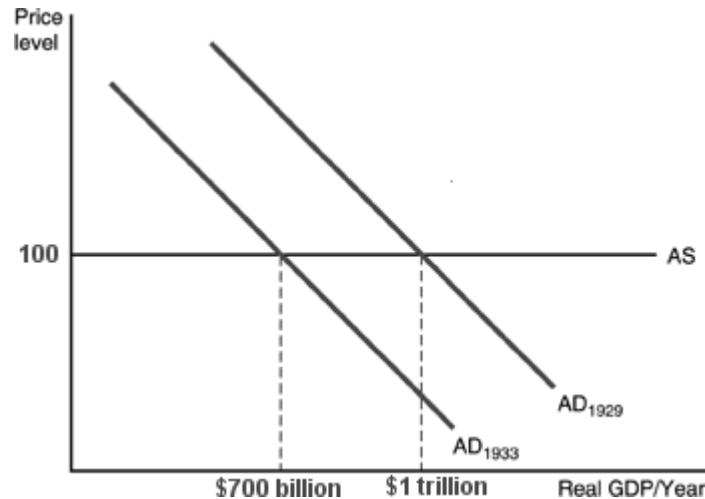
Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 68) Using a graph, analyze the Great Depression from a Keynesian perspective. What happened to unemployment?

Answer: In the below figure, the equilibrium before the depression was at a price level of 100 and real GDP of \$1 trillion. The depression was caused by a reduction in aggregate demand to AD₁₉₃₃. Because prices were not flexible, real GDP fell to \$700 billion. The reduced output would be associated with a large increase in unemployment.



Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 69) What is the major difference between the classical model and the Keynesian model? Explain.

Answer: The major difference is the shape of the aggregate supply curve. The classical view is that it is vertical, while the Keynesian view is that it is horizontal, or at least almost so. The differences in shape are due to differences in assumptions about the flexibility of prices. Classical economists assumed prices and wages were flexible and would quickly adjust to bring about a new full-employment equilibrium, while the Keynesian model assumes prices are not flexible.

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 70) For several years, the U.S. unemployment rate has been below the European unemployment rate. Offer a Keynesian explanation for this.

Answer: The aggregate supply curve in Europe is closer to horizontal than is the case in the United States. The labor market is less flexible in Europe due to higher unemployment benefits that reduce the incentive to work, and due to higher costs to firms for hiring workers.

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 71) What shape did the short-run aggregate supply curve have during the 1930s, according to Keynes? Explain.

Answer: Keynes argued the short-run aggregate supply curve was horizontal during the 1930s. There was substantial unemployment and excess capacity during the depression, so that shifts in aggregate demand would affect total output without affecting the price level. Keynes argued that prices and wages were inflexible, especially downward, and could not be relied upon to bring about a full-employment equilibrium.

Diff: 2

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 72) "According to Keynes, the economy is essentially a self-regulating system." Do you agree or disagree? Why?

Answer: Disagree. The inflexibility of prices meant that changes in aggregate demand would affect output and employment rather than the price level. Involuntary unemployment was likely when aggregate demand decreased because the wage level would not adjust to bring about a new, full-employment equilibrium. Hence, the economy is not a self-regulating system according to Keynes.

Diff: 3

Topic: 11.2 Keynesian Economics and the Keynesian Short-Run Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

- 1) What is the underlying assumption of the original, simplified Keynesian model?
- A) The relevant range of the short-run aggregate supply curve (SRAS) is vertical.
 - B) The relevant range of the aggregate supply curve (AS) is vertical.
 - C) The relevant range of the short-run aggregate supply curve (SRAS) is horizontal.
 - D) The relevant range of the long-run aggregate supply curve (LRAS) is horizontal.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 2) How does the original, simplified Keynesian model compare with modern Keynesian analysis?
- A) The original Keynesian model assumed price flexibility whereas the modern analysis does not.
 - B) In both cases, the short-run aggregate supply curve (SRAS) is horizontal.
 - C) Modern analysis shows an upward sloping SRAS to reflect some price flexibility. The original Keynesian model's SRAS is horizontal and assumes sticky prices.
 - D) All of the above.

Answer: C

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Revised

- 3) The Keynesian short-run aggregate supply curve in the simplified Keynesian model is unrealistic because
- A) a vertical curve does not make economic sense.
 - B) prices and wages will never decrease.
 - C) the classical model is better in explaining how the economy operates.
 - D) some price adjustments do take place in the short run.

Answer: D

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 4) The horizontal portion of the short-run aggregate supply curve in which there is excessive unemployment and unused capacity in the economy is
- A) Say's law.
 - B) the classical short-run aggregate supply curve.
 - C) the Keynesian short-run aggregate supply curve.
 - D) exists when prices are flexible.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 5) The short-run aggregate supply curve in modern Keynesian analysis is
- A) horizontal.
 - B) vertical.
 - C) upward sloping.
 - D) downward sloping.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 6) The short-run aggregate supply curve is positively sloped because
- A) real interest rates rather than nominal rates are used.
 - B) some price adjustments take place in the short-run.
 - C) no price adjustments take place in the short-run.
 - D) complete price adjustments take place in the short-run.

Answer: B

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 7) The short-run aggregate supply curve in modern Keynesian analysis represents the relationship between
- A) the real output of goods and services in the economy and the price level.
 - B) the real output of goods and services in the economy and the price level when people have fully adjusted their behavior.
 - C) the real output of goods and services in the economy and the price level when people have not fully adjusted their behavior.
 - D) the nominal output of goods and services and the real output of goods and services.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Along a short-run aggregate supply curve, which of the following is (are) held constant?
- A) real GDP
 - B) aggregate demand
 - C) input prices.
 - D) profits

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Revised

- 9) The full-employment rate of output can
- A) be surpassed in the long run only if input prices are flexible.
 - B) not be surpassed in either the short run or the long run.
 - C) be surpassed only when firms are not yet producing at full capacity.
 - D) be surpassed only in the short run.

Answer: D

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 10) In the short run, real GDP can increase beyond a level consistent with the long-run growth path if
- A) existing capital and labor are used more intensely.
 - B) the price level decreases accordingly.
 - C) we measure in nominal terms instead of real terms.
 - D) there is an increase in marginal tax rates.

Answer: A

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Revised

- 11) Which of the following is NOT a reason why real GDP can be expanded beyond a level consistent with its long-run growth path in modern Keynesian analysis?
- A) In the short run, existing workers can work more hours.
 - B) Prices and wages are flexible, allowing for needed adjustments.
 - C) The existing capital stock can be used more intensively.
 - D) Higher prices induce firms to hire more workers.

Answer: B

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 12) If short-run aggregate supply is upward sloping, the assumption is that
- A) prices are perfectly sticky.
 - B) prices are set by government mandate.
 - C) prices are constant.
 - D) prices adjust gradually.

Answer: D

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 13) An upward sloping short-run aggregate supply curve suggests that
- A) real GDP is determined by aggregate supply.
 - B) prices and wages are completely inflexible.
 - C) prices and wages are completely flexible.
 - D) prices and wages adjust in part to short-run demand changes.

Answer: D

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 14) In the *modern* Keynesian model, over much of its range the short-run aggregate supply (SRAS) curve is
- A) horizontal.
- B) vertical.
- C) upward sloping.
- D) downward sloping.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 15) The short-run aggregate supply curve in modern Keynesian analysis
- A) is a horizontal line the same as in the Keynesian model.
 - B) is a vertical line the same as in the classical model.
 - C) is an upward sloping curve.
 - D) is a negatively sloped curve.

Answer: C

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 16) There is a distinction between the long-run aggregate supply (LRAS) curve and the short-run aggregate supply (SRAS) curve. In the long run,
- A) technology is fixed, but not in the short run.
 - B) the price level is constant in the long run, but fluctuates in the short run.
 - C) the aggregate supply curve is horizontal, while in the short run it is upward sloping.
 - D) all adjustments to changes in the price level have been made, but in the short run all changes in the price level do not occur.

Answer: D

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Revised

- 17) If the price level kept increasing, the short-run aggregate supply (SRAS) curve would get steeper because
- A) all the unemployed would eventually be hired.
 - B) there are limits to how long workers can work long hours and capital can go without proper maintenance.
 - C) the rate at which capacity can be expanded increases indefinitely.
 - D) the long-run aggregate supply curve is horizontal.

Answer: B

Diff: 3

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 18) In the short run, if the price level rises, then the overall economy can temporarily produce beyond its nominal capacity. One reason for this is that
- A) workers can be switched from counted to uncounted production.
 - B) existing capital equipment can be used more intensively.
 - C) wage rates rise almost simultaneously with the price level.
 - D) the unemployment rate usually rises dramatically along with the price level.

Answer: B

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 19) The long-run aggregate supply curve is vertical at \$10 trillion, but the short-run aggregate supply curve intersects the aggregate demand curve at \$12 trillion. From this, we know that
- A) the economy is operating below full capacity in the short run, and will have to adjust by hiring more workers, thus reducing unemployment.
 - B) the price level is too high. The only way long-run equilibrium can be restored is to lower the price level.
 - C) adjustments will have to occur so that the long-run aggregate supply equals \$12 trillion.
 - D) adjustments will have to occur so that the short-run aggregate supply intersects the aggregate demand curve at \$10 trillion.

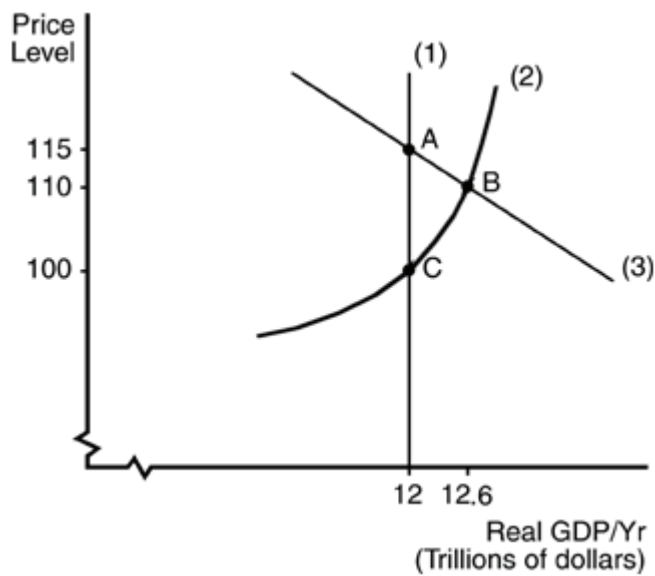
Answer: D

Diff: 3

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition



20) Identify the 3 curves in the above figure.

- A) (1) is long-run aggregate supply, (2) is short-run aggregate supply, (3) is aggregate demand.
- B) (1) is aggregate demand, (2) is short-run aggregate supply, (3) is long-run aggregate supply.
- C) (1) is short-run aggregate supply, (2) is long-run aggregate supply, (3) is aggregate demand.
- D) (1) is long-run aggregate supply, (2) is aggregate demand, (3) is short-run aggregate supply.

Answer: A

Diff: 1

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

21) Which point or points on the above figure illustrate a short-run equilibrium?

- A) Point A
- B) Point B
- C) Point C
- D) Points A and C

Answer: B

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 22) According to the above figure, what will the price level be in the new long-run equilibrium?
 A) 115 B) 110 C) 100 D) Less than 100

Answer: A

Diff: 2

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 23) What is the shape of the *modern* short-run aggregate supply (SRAS) curve? Why?

Answer: The short-run aggregate supply curve is initially horizontal, then upward sloping. If the price level increases in the short run, some costs for firms stay constant. The higher product price leads to higher profits, and the firms expand production. Hence, aggregate output can increase in the short run.

Diff: 2

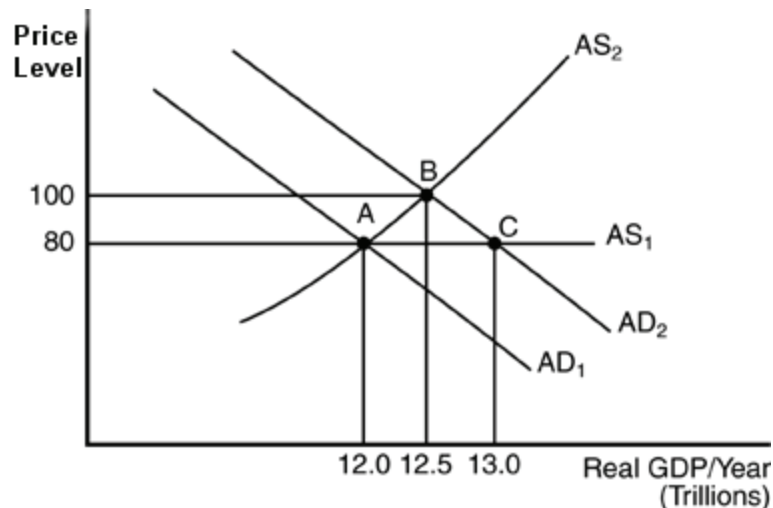
Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Compare the effects of an increase in aggregate demand when the price level is fixed versus when it can change.

Answer:



The above figure shows the effects. An increase in aggregate demand from AD_1 to AD_2 causes real Gross Domestic Product (GDP) to increase, but the size of the increase is greater for AS_1 than for AS_2 . When the price level can change, some of the impact of the increase in aggregate demand falls on the price level instead of output, whereas all of the impact is on output when the price level is fixed.

Diff: 2

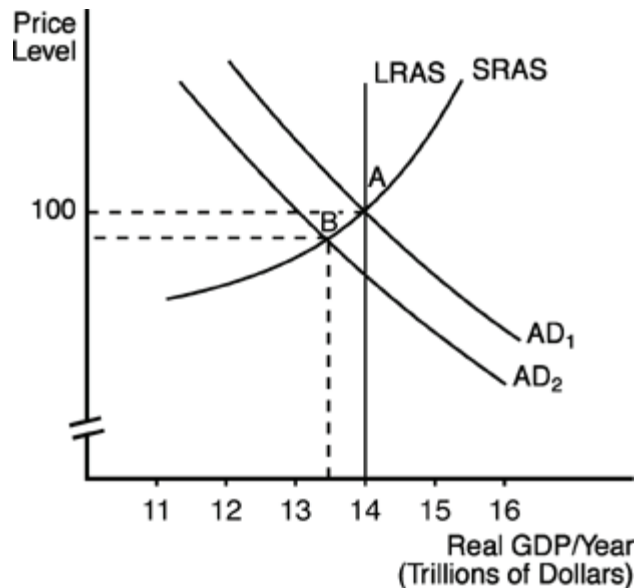
Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

- 25) Suppose the economy in the diagram below is in long-run equilibrium. If government spending decreases and causes a movement from point A to point B in the diagram below, what are the short-run effects? Explain fully.

Answer:



In the above figure, point A is the original equilibrium, with a price level of 100 and total planned expenditures on final goods and services equal to \$14 trillion. A decrease in government spending causes the aggregate demand curve to shift to the left. In the short run, total planned expenditures and equilibrium real Gross Domestic Product (GDP) falls to \$13.5 trillion. The price level falls to 90.

Diff: 3

Topic: 11.3 Output Determination Using Aggregate Demand and Aggregate Supply: Fixed versus Changing Price Levels in the Short Run

AACSB: Analytic skills

Question Status: Previous Edition

11.4 Shifts in the Aggregate Supply Curve

- 1) Economic growth due to labor force expansion or capital investments will result in
- A leftward shift of short-run aggregate supply.
 - A rightward shift in long-run aggregate supply.
- A) I only B) II only C) Both I and II D) Neither I nor II

Answer: B

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 2) Which of the following will cause an increase in aggregate supply?
- A) Decreased competition
 - B) An increase in the price level
 - C) An increase in marginal tax rates
 - D) A decrease in input prices

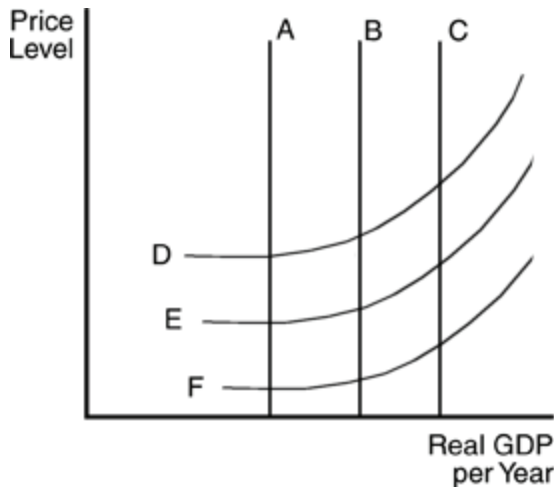
Answer: D

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition



- 3) Refer to the above figure. Assume that B is the current long-run aggregate supply (LRAS) curve and that E is the current short-run aggregate supply (SRAS) curve. If a new discovery of large oil fields in Florida led to an increase in the nation's productive capacities, then we could expect the LRAS curve and the SRAS curve to
- A) remain B and E.
 - B) move to A and D.
 - C) move to C and F.
 - D) move to A and F.

Answer: C

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 4) Refer to the above figure. Assume that B is the current long-run aggregate supply (LRAS) curve and E is the current short-run aggregate supply (SRAS) curve. If a 90-day embargo of oil from the Middle East to the United States were announced, and if after that 90-day period oil prices were expected to return to normal pre-embargo prices, then you would expect
- A) the LRAS and the SRAS to remain at B and E, respectively.
 - B) the LRAS to remain at B, but the SRAS to shift to D.
 - C) the LRAS to remain at B, but the SRAS to shift to F.
 - D) the LRAS to shift to C, and the SRAS to shift to F.

Answer: B

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 5) Which of the following is NOT an event that causes BOTH the short-run aggregate supply (SRAS) curve and the long-run aggregate supply (LRAS) curve to shift?
- A) A change in an economy's endowments of the factors of production
 - B) Technological changes
 - C) A change in an economy's labor supply
 - D) A temporary change in the price of a key input

Answer: D

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 6) Which of the following will NOT shift the short-run aggregate supply (SRAS) curve?
- A) A change in the wage rate
 - B) Technological progress
 - C) A reduction in the price of a raw material
 - D) A change in the price level

Answer: D

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 7) All of the following will shift the short-run aggregate supply (SRAS) curve EXCEPT
- A) a change in the price level.
 - B) a change in the price of labor.
 - C) a change in the price of a needed raw material.
 - D) technological progress.

Answer: A

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 8) As real GDP per year increases along the short-run aggregate supply (SRAS) curve, the SRAS curve
- A) becomes increasingly steep.
 - B) begins to level out.
 - C) shifts inward.
 - D) does not change.

Answer: A

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Both the long-run and short-run aggregate supply curves will shift when
- A) the government increases defense spending.
 - B) an event occurs which is expected to last only a short period of time.
 - C) they are both upward sloping.
 - D) the endowments of the factors of production change.

Answer: D

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 10) Which of the following would increase aggregate supply?
- A) increased training and education
 - B) a reduction in input prices
 - C) a discovery of new raw materials
 - D) all of the above

Answer: D

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 11) The discovery of new iron ore fields will cause
- A) the long-run aggregate supply curve to shift to the right and the short-run aggregate supply curve to shift to the left.
 - B) the long-run aggregate supply curve to shift to the right, but not the short-run aggregate supply.
 - C) the short-run aggregate supply curve to shift to the right, but not the long-run aggregate supply curve.
 - D) both the long-run and the short-run aggregate supply curves to shift to the right.

Answer: D

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 12) A major hurricane causes production problems in Gulf Coast region of the United States. This would cause
- A) the short-run aggregate supply curve to shift to the left, but there would be no effect on the long-run aggregate supply curve.
 - B) the short-run aggregate supply curve to shift to the left, and the long-run aggregate supply curve would shift to the right.
 - C) both the short-run and the long-run aggregate supply curves to shift to the right in equal amounts.
 - D) both the short-run and the long-run aggregate supply curves to shift to the left, but the long-run aggregate supply curve would shift more than the short-run curve.

Answer: A

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 13) The short-run aggregate supply curve would shift and the long-run aggregate supply curve would remain fixed if
- A) there was a temporary shock to aggregate demand.
 - B) there was a temporary shock that influenced the supply side.
 - C) there was a permanent increase in aggregate demand along with a permanent decrease in aggregate supply.
 - D) there was a permanent increase in aggregate demand.

Answer: B

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Revised

- 14) The short-run aggregate supply curve would shift and the long-run aggregate supply curve would remain fixed if
- A) transportation workers went on strike for a month.
 - B) there was an increase in immigration.
 - C) the retirement age increased by two years.
 - D) tough new environmental laws were passed.

Answer: A

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 15) A reduction in nominal wages will cause which of the following?
- A) a movement along the short-run aggregate supply curve
 - B) a shift of both the short-run and long-run aggregate supply curves
 - C) a rightward shift in the short-run aggregate supply curve
 - D) a leftward shift in the short-run aggregate supply curve to shift to the left

Answer: C

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 16) A permanent reduction in international trade barriers would
- A) decrease long-run aggregate supply.
 - B) increase long-run aggregate supply.
 - C) decrease aggregate demand.
 - D) increase aggregate demand.

Answer: B

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 17) A short-lived increase in oil prices caused by destruction of oil-producing and oil-refining facilities by a large hurricane will
- A) shift the SRAS curve to the right.
 - B) shift the LRAS curve to the right.
 - C) shift the SRAS curve to the left.
 - D) shift the AD curve to the right.

Answer: C

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 18) If there is a change in the U.S. endowment of factors of production, then there would be
- A) a shift in just LRAS.
 - B) a shift in both LRAS and SRAS.
 - C) shifts in just SRAS.
 - D) a movement along the SRAS curve.

Answer: B

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 19) All items below will decrease short-run aggregate supply EXCEPT
- A) a decrease in the marginal tax rates.
 - B) an increase in the prices of inputs.
 - C) a decrease in training and education.
 - D) a decrease in labor supply.

Answer: A

Diff: 1

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 20) Which of the following decreases aggregate supply?
- A) discoveries of new raw materials
 - B) an increase in competition
 - C) an increase in training and education
 - D) a decrease in labor supply

Answer: D

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 21) A temporary embargo on oil from the Middle East going in to the United States would
- A) shift both the short-run and long-run aggregate supply curves to the left.
 - B) shift only the long-run aggregate supply curve to the left.
 - C) shift the long-run aggregate supply curve to the right.
 - D) shift only the short-run aggregate supply curve to the left.

Answer: D

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 22) A new discovery of large volumes of previously unknown deposits of natural gas in Pennsylvania would
- A) shift the short-run and long-run aggregate supply curves to the right.
 - B) shift only the short-run aggregate supply curve to the right.
 - C) shift only the long-run aggregate supply curve to the right.
 - D) not affect either the short-run or long-run aggregate supply curves.

Answer: A

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 23) Consider a nation in which most workers are unionized. If all the nation's unions band together and succeed in boosting wages established by long-term labor contracts, then
- A) there is a leftward shift in just LRAS.
 - B) there is a leftward shift in both LRAS and SRAS.
 - C) there is a rightward shift in just SRAS.
 - D) there is a rightward movement along the SRAS curve.

Answer: B

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 24) All of the following will cause the aggregate supply curve to shift to the right EXCEPT
- A) discoveries of raw materials.
 - B) a reduction in input prices.
 - C) an increase in marginal tax rates.
 - D) a reduction in international trade barriers.

Answer: C

Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

- 25) A temporary increase in the price of oil would
- A) increase both short-run and long-run aggregate supply.
 - B) increase short-run aggregate supply and decrease long-run aggregate supply.
 - C) decrease short-run aggregate supply and leave long-run aggregate supply unchanged.
 - D) decrease both short-run and long-run aggregate supply.

Answer: C

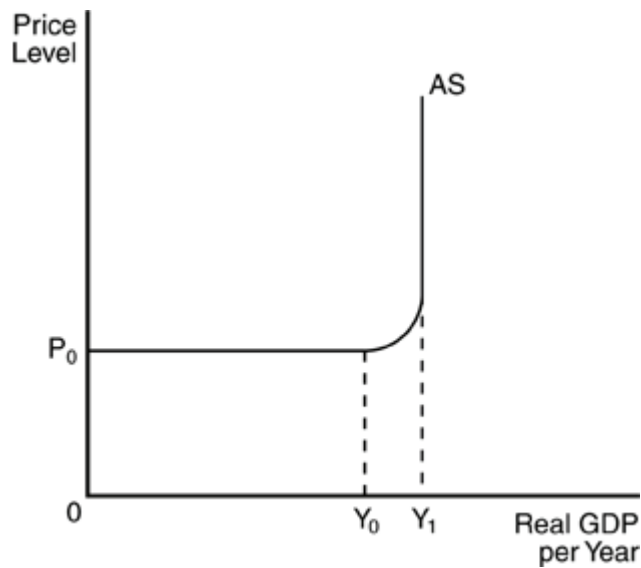
Diff: 2

Topic: 11.4 Shifts in the Aggregate Supply Curve

AACSB: Analytic skills

Question Status: Previous Edition

11.5 Consequences of Changes in Aggregate Demand



- 1) Refer to the above figure. An increase in aggregate demand between real Gross Domestic Product (GDP) levels Y_0 and Y_1
- A) would most likely result in some inflation.
 - B) would not increase output since the economy is already working at full capacity.
 - C) would have no effect on the price level.
 - D) would cause price levels to fall.

Answer: A

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 2) Refer to the above figure. An increase in aggregate demand beyond real Gross Domestic Product (GDP) level Y_1 would result in
- A) higher real GDP but not a higher price level.
 - B) a lower price level but no change in real GDP.
 - C) a higher price level but no change in real GDP.
 - D) a lower price level and an increases in real GDP.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

- 3) The gap that exists when equilibrium real Gross Domestic Product (GDP) is greater than full employment real Gross Domestic Product (GDP) is called a(n)
- A) employment gap.
B) inflationary gap.
C) recessionary gap.
D) demand gap.

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 4) Economic growth will NOT result in deflation if aggregate demand shifts
- A) outward to the right at the same speed as aggregate supply.
 - B) inward to the left at the same speed as aggregate supply.
 - C) outward to the right as aggregate supply shifts inward to the left.
 - D) inward to the left as aggregate supply shifts outward to the right.

Answer: A

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 5) An unexpected event that causes the aggregate demand curve to shift inward or outward is an
- A) aggregate demand shock.
B) aggregate supply shock.
C) aggregate supply increase.
D) aggregate supply decrease.

Answer: A

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 6) If the economy is near full capacity, the effect of a negative aggregate demand shock is to
- A) increase the level of aggregate demand.
 - B) cause the price level to fall.
 - C) increase the firm's cost of producing at every level of output.
 - D) increase the level of employment.

Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 7) One possible result of a fall in aggregate demand coupled with a stable short-run aggregate supply is
- A) a recession.
- B) an increase in employment levels.
- C) an economic expansion.
- D) a rise in the stock market.

Answer: A

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 8) If equilibrium level of real Gross Domestic Product (GDP) is less than the full-employment real Gross Domestic Product (GDP) consistent with the position of the economy's long-run aggregate supply (LRAS) curve, then the difference between full-employment real Gross Domestic Product (GDP) and current equilibrium real Gross Domestic Product (GDP) is
- A) an aggregate demand shock.
 - B) an aggregate supply shock.
 - C) a recessionary gap.
 - D) an inflationary gap.

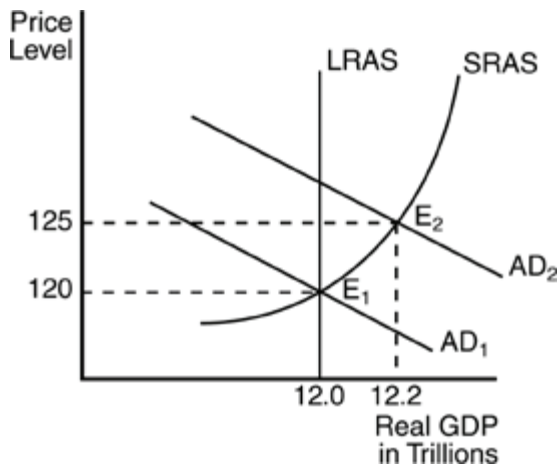
Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition



- 9) In the above figure, the inflationary gap can correctly be identified as
- A) the difference between 125 and 120.
 - B) the difference between 12.2 trillion and 12 trillion.
 - C) LRAS minus SRAS.
 - D) AD₁.

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 10) In the above figure, an increase in aggregate demand has resulted in
- A) a decline in the price level.
 - B) economic growth.
 - C) an inflationary gap.
 - D) a recessionary gap.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 11) The reason that it is possible for the economy in the above figure to be at E_2 rather than at E_1 is that
- A) in the long run there is always less than full employment.
 - B) in the short run the economy can produce more than it can in a long-run full-adjustment situation.
 - C) AD always shifts outward and never shifts inward.
 - D) the economy must be in a recession.

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 12) In the above figure, the economy would most likely move from AD_1 to AD_2 because of
- A) an aggregate supply shock.
 - B) an aggregate demand shock.
 - C) a recession.
 - D) a depression.

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 13) A short-run equilibrium occurs
- A) at the intersection of the long-run aggregate supply curve and the aggregate demand curve.
 - B) at the intersection of the short-run aggregate supply curve and the long-run aggregate supply curve.
 - C) at the intersection of the short-run aggregate supply curve and the aggregate demand curve.
 - D) at the real GDP associated with full employment.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 14) Assume equilibrium real GDP per year is equal to full-employment real GDP. Which of the following will cause a recessionary gap?
- A) an increase in aggregate demand
 - B) a reduction in aggregate demand
 - C) a discovery of a new raw material
 - D) a temporary reduction in the price of oil

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 15) In the Keynesian model, an aggregate demand shock
- A) will cause the aggregate demand curve to shift, leading to a change in the price level and real GDP.
 - B) will cause the aggregate demand curve to shift, leading to a change in the price level but not real GDP.
 - C) will cause the aggregate demand curve to shift, leading to a change in real GDP but not the price level.
 - D) will not lead to a shift of the aggregate demand curve.

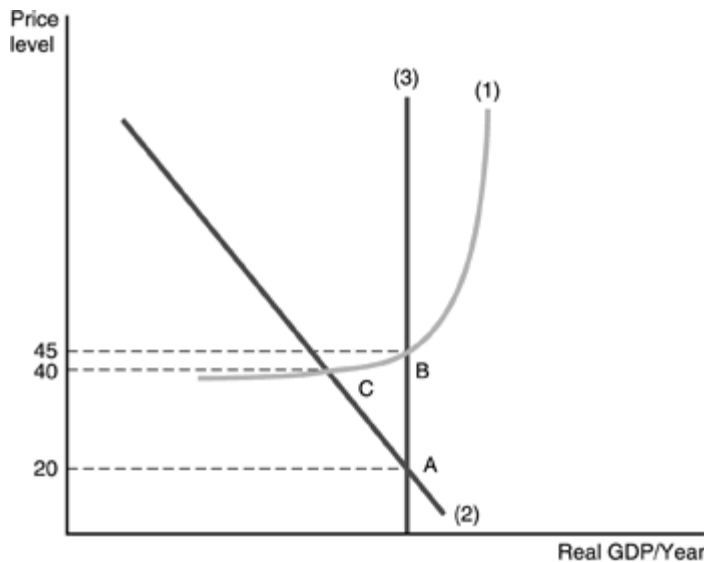
Answer: A

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition



- 16) The three curves in the above figure are
- A) (1) the long-run aggregate supply curve, (2) the aggregate demand curve, and (3) the short-run aggregate supply curve.
 - B) (1) the long-run aggregate supply curve, (2) the short-run aggregate supply curve, and (3) the aggregate demand curve.
 - C) (1) the short-run aggregate supply curve, (2) the aggregate demand curve, and (3) the long-run aggregate supply curve.
 - D) (1) the aggregate supply curve, (2) the short-run aggregate demand curve, and (3) the long-run aggregate demand curve.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 17) Refer to the above figure. Which point or points represent(s) a short-run equilibrium?
 A) A only B) B only C) C only D) both A and B

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 18) Refer to the above figure. Which point or points represent(s) a long-run equilibrium?
 A) A only B) B only C) C only D) both A and B

Answer: A

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 19) Refer to the above figure. At the initial long-run equilibrium, the price level is _____, and at the new long-run equilibrium, the price level will be _____.
 A) 20; 45 B) 20; 40 C) 40; 45 D) 20; 20

Answer: D

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 20) Refer to the above figure. Suppose the original long-run equilibrium was at point B. What could have caused the move to the current equilibrium?
 A) Decreases in the price level caused short-run aggregate supply to fall.
 B) Input prices must have increased, causing long-run aggregate supply to increase.
 C) Aggregate demand must have decreased.
 D) A temporary reduction in production due to bad weather.

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 21) Suppose the current situation is such that the price level is 120, real GDP is \$14 trillion, and long-run aggregate supply is \$13.6 trillion. We can conclude that
 A) the price level will fall until long-run aggregate supply shifts to \$14 trillion.
 B) the price level will fall and input prices will rise until real GDP pulls long-run aggregate supply up to \$14 trillion.
 C) input prices will rise until real GDP is \$13.6 trillion.
 D) aggregate demand will increase until both short-run and long-run aggregate supply equal \$14 trillion.

Answer: C

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 22) Holding the level of prices fixed implies that a given increase in aggregate demand
- A) will have a smaller effect on real GDP than would be the case if prices were more flexible.
 - B) will have a larger effect on real GDP than would be the case if prices were more flexible.
 - C) has the same effect on real GDP as when prices are more flexible.
 - D) has a smaller effect on nominal GDP than when prices are more flexible.

Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 23) Suppose we observe rising nominal GDP, a rising price level, and constant unemployment as a result of an increase in aggregate demand. We would conclude that the aggregate supply curve is

- A) upward sloping.
- B) downward sloping.
- C) vertical.
- D) horizontal.

Answer: C

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

- 24) If aggregate demand and nominal GDP increase while the price level is constant, we would conclude that

- A) the economy is already at full employment.
- B) the aggregate supply curve is upward sloping.
- C) the aggregate supply curve is horizontal.
- D) the aggregate demand curve is vertical.

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 25) If we observe an increase in real GDP and an increase in the price level after an increase in aggregate demand, we can conclude that

- A) the aggregate supply curve is upward sloping.
- B) the aggregate supply curve is horizontal.
- C) the aggregate supply curve is vertical.
- D) the economy is now at full employment.

Answer: A

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 26) A change in tastes for U.S. produced goods will
- A) shift both the aggregate demand curve and the long-run aggregate supply curve.
 - B) shift the aggregate demand curve.
 - C) shift the short-run aggregate supply curve.
 - D) shift the long-run aggregate supply curve.

Answer: B

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

- 27) Assume equilibrium real GDP per year is equal to full-employment real GDP. If aggregate demand falls, then
- A) the price level will increase in the short run and decrease in the long run.
 - B) there will be an expansionary gap.
 - C) there will be a recessionary gap.
 - D) long-run aggregate supply will eventually decrease too.

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

- 28) The short-run and long-run aggregate supply curves remain stable, and a decrease in aggregate demand occurs. What is the result in the short run?
- A) An increase in the price level and real GDP will occur.
 - B) A period of expansion and a rise in the unemployment rate could occur.
 - C) A period of recession and a rise in the unemployment rate could occur.
 - D) The price level will fall but real GDP will remain the same.

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 29) An inflationary gap occurs when
- A) aggregate demand falls, but other things remain constant.
 - B) short-run aggregate supply falls, but other things remain constant.
 - C) the short-run equilibrium level of real GDP is greater than long-run aggregate supply.
 - D) the short-run equilibrium level of real GDP is less than long-run aggregate supply.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 30) The gap that exists when equilibrium real GDP is less than full-employment real GDP is
- A) the short-run aggregate supply curve.
 - B) money illusion.
 - C) a recessionary gap.
 - D) an inflationary gap.

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

- 31) The gap that exists when equilibrium real GDP is greater than the level of real GDP shown by the position of the long-run aggregate supply curve is
- A) the short-run aggregate supply curve.
 - B) money illusion.
 - C) a recessionary gap.
 - D) an inflationary gap.

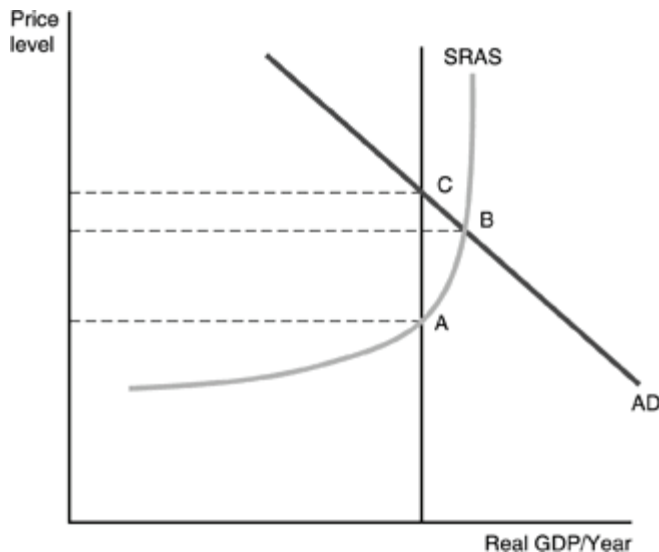
Answer: D

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised



- 32) Refer to the above figure. Suppose the economy had been at point A and now is at B. What could have caused the movement to B?
- A) Unusually good weather causes the wheat crop to be larger than normal.
 - B) Government spending increased causing aggregate demand to increase.
 - C) Winter storms cause factories in the north to be shut down for several weeks.
 - D) Both the labor force and the population increased.

Answer: B

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

33) A recessionary gap occurs when

- A) aggregate demand falls, but other things remain constant.
- B) short-run aggregate supply falls, but other things remain constant.
- C) the short-run equilibrium level of real GDP is greater than the level consistent with the long-run aggregate supply curve.
- D) the short-run equilibrium level of real GDP is less than the level consistent with the long-run aggregate supply curve.

Answer: D

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

34) An example of an aggregate supply shock is

- A) inflation caused by a surge in demand.
- B) the cutoff of oil by the OPEC nations in the early 1970s.
- C) the increase in the labor force due to the baby-boomer generation reaching working age.
- D) the increase in candy sales every February.

Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

35) A recessionary gap is the amount by which

- A) total planned real expenditures exceed total planned production in the long run.
- B) the short-run equilibrium level nominal GDP is above the short-run real GDP.
- C) the short-run equilibrium level nominal GDP is below the short-run real GDP.
- D) the short-run equilibrium level of real GDP is below the full-employment level of real GDP.

Answer: D

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

36) An inflationary gap is the amount by which

- A) total planned production exceeds total planned real expenditures in the long run.
- B) the short-run equilibrium level of nominal GDP is above the short-run level of real GDP.
- C) the short-run equilibrium level of nominal GDP is below the short-run level of real GDP.
- D) the short-run equilibrium level of real GDP is above the full-employment level of real GDP.

Answer: D

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 37) If the U.S. government were to relax its restrictions on offshore oil well drilling and open drilling in Alaskan national parks, the result to aggregate supply would be to
- A) cause a shift in the SRAS to the left.
 - B) cause a shift in the LRAS to the left.
 - C) cause no long-term shifts in AS.
 - D) cause a shift in both LRAS and SRAS to the right.

Answer: D

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 38) In the short run, if aggregate demand shifts to the left while the position of the short-run aggregate supply curve does NOT change, then
- A) the level of economic activity rises.
 - B) a recessionary gap occurs.
 - C) there is no change in real GDP and the price level.
 - D) an inflationary gap occurs.

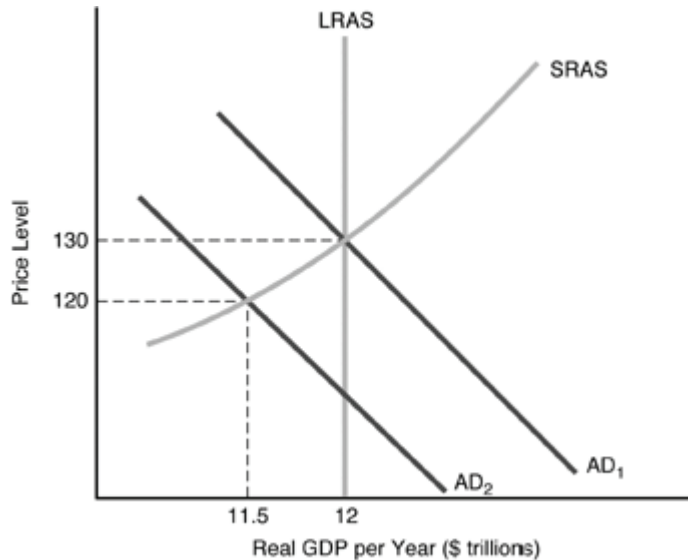
Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition



- 39) In the above figure, what are the long-run equilibrium price level and real GDP?
- A) 130 and \$12 trillion
 - B) 130 and \$11.5 trillion
 - C) 120 and \$11.5 trillion
 - D) 120 and \$12 trillion

Answer: A

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

40) In the above figure, if the relevant aggregate demand curve is AD₂, what are the short-run equilibrium price level and real GDP?

- A) 130 and \$12 trillion
- B) 130 and \$11.5 trillion
- C) 120 and \$11.5 trillion
- D) 120 and \$12 trillion

Answer: C

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

41) In the above figure, if the relevant aggregate demand curve is AD₂, what type of gap exists and how large is it?

- A) inflationary gap of \$500 billion
- B) inflationary gap of \$1 trillion
- C) recessionary gap of \$1 trillion
- D) recessionary gap of \$500 billion

Answer: D

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

42) In the above figure, what could cause the shift of aggregate demand from AD₁ to AD₂?

- A) depletion of raw materials
- B) an increase in input prices
- C) a decrease in consumer confidence
- D) an increase in international trade barriers

Answer: C

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

43) If the equilibrium level of real GDP per year is greater than the full-employment level of GDP, then

- A) a recessionary gap occurs.
- B) the economy is at full employment with no price changes.
- C) the economy expands the level of real GDP.
- D) an inflationary gap occurs.

Answer: D

Diff: 1

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 44) Which of the following actions would cause the aggregate demand curve to shift to the left?
- A) an increase in consumer spending caused by a cut in the personal income tax rate
 - B) an increase in government spending caused by increased spending on highways and bridge construction
 - C) a decrease net export spending caused by an appreciation of the home currency
 - D) an increase in exports caused by an increase in economic activity in the European Union

Answer: C

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 45) A recessionary gap results when
- A) aggregate demand is below the level consistent with full employment.
 - B) aggregate demand is above the level consistent with full employment.
 - C) aggregate supply and aggregate demand are not in short-run equilibrium.
 - D) aggregate supply decreases.

Answer: A

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 46) If the full-employment level of real GDP is greater than the equilibrium level of real GDP, the nation would be experiencing a(n)
- A) inflationary gap.
 - B) recessionary gap.
 - C) demand-pull inflation.
 - D) rising prices.

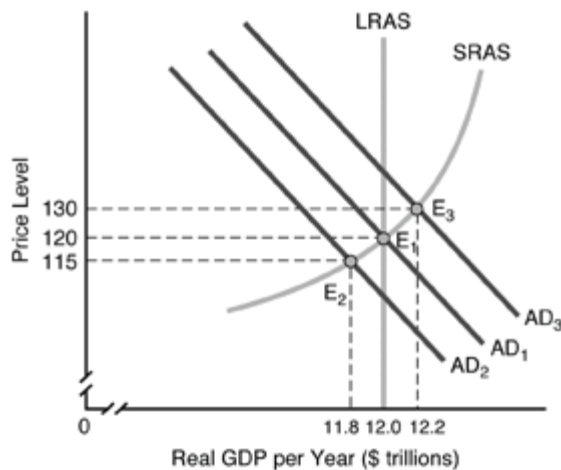
Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised



- 47) Consider the above figure. If the aggregate demand fell from AD_1 to AD_2 , our nation would be experiencing
- A) an inflationary gap.
 - B) a recessionary gap.
 - C) overemployment.
 - D) rising prices.

Answer: B

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 48) Consider the above figure. If the aggregate demand curve rose from AD_1 to AD_3 , our nation would be experiencing
- A) an inflationary gap.
 - B) a recessionary gap.
 - C) unemployment.
 - D) falling prices.

Answer: A

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

- 49) Consider the above figure. If the aggregate demand went from AD_2 to AD_3 , our nation would have gone from
- A) a recessionary gap to an inflationary gap.
 - B) a recessionary gap to full-employment real GDP.
 - C) an inflationary gap to full-employment GDP.
 - D) full-employment real GDP to an inflationary gap.

Answer: A

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

50) According to modern Keynesian analysis, an increase in aggregate demand leads to a higher price level because the

- A) aggregate demand curve is upward sloping.
- B) short-run aggregate supply curve is upward sloping.
- C) aggregate demand curve is upward horizontal.
- D) short-run aggregate supply curve is vertical.

Answer: B

Diff: 2

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Revised

51) Suppose aggregate demand is increasing over time. Would the modern Keynesian model assume that the price level would always be constant? Explain.

Answer: No. Eventually full employment would be reached and firms would be producing at full capacity. The price level would adjust as prices would increase. That is, the short-run aggregate supply curve cannot be horizontal at all possible values of real Gross Domestic Product (GDP).

Diff: 3

Topic: 11.5 Consequences of Changes in Aggregate Demand

AACSB: Analytic skills

Question Status: Previous Edition

11.6 Explaining Short-Run Variations in Inflation

1) Inflation that is caused by an increase in aggregate demand which is not matched by an increase in aggregate supply is called

- A) demand-push inflation.
- B) demand-pull inflation.
- C) cost-push inflation.
- D) cost-pull inflation.

Answer: B

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

2) The significant run-up in oil prices during the latter 2000s was an example of

- A) an aggregate demand shock that increased the price level and increased the rate of growth of real Gross Domestic Product (GDP).
- B) an aggregate demand shock that reduced the price level and reduced the rate of growth of real Gross Domestic Product (GDP).
- C) an aggregate supply shock that increased the price level and reduced the rate of growth of real Gross Domestic Product (GDP).
- D) an aggregate supply shock that reduced the price level and increased the rate of growth of real Gross Domestic Product (GDP).

Answer: C

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 3) Suppose that last year \$1 U.S. exchanged for 1 euro. If this year \$1 exchanges for 0.75 euro, then we can conclude that
- A) the dollar is weaker this year than it was last year and this will cause the United States' short-run aggregate supply (SRAS) curve to shift to the left.
 - B) the dollar is weaker this year than it was last year and this will cause the United States' short-run aggregate supply (SRAS) to shift to the right.
 - C) the dollar is stronger this year than it was last year and this will cause the United States' short-run aggregate supply (SRAS) curve to shift to the left.
 - D) the dollar is weaker this year than it was last year but this will have no impact on the United States' short-run aggregate supply (SRAS) curve.

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

- 4) If the U.S. dollar becomes weaker in international foreign exchange markets, imported goods become more expensive. One result of this is that
- A) net exports decrease.
 - B) net exports increase.
 - C) domestic employment rises.
 - D) real Gross Domestic Product (GDP) increases.

Answer: B

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 5) A weaker U.S. dollar simultaneously leads to _____ in SRAS and _____ in AD.
- A) a leftward shift ; a rightward shift
 - B) a rightward shift; a leftward shift
 - C) an outward shift; an outward shift
 - D) an inward shift; an inward shift

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 6) If the U.S. dollar becomes weaker in international markets, the net effects will include
- A) a decrease in short-run aggregate supply (SRAS) and an increase in aggregate demand.
 - B) an increase in short-run aggregate supply (SRAS) and a decrease in aggregate demand.
 - C) a decrease in both short run aggregate supply (SRAS) and aggregate demand.
 - D) an increase in both short run aggregate supply (SRAS) and aggregate demand.

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

7) Demand-pull inflation is

- A) inflation caused by increases in aggregate demand that generate an even larger increase in aggregate supply.
- B) inflation caused by increases in aggregate demand that are not matched by increases in aggregate supply.
- C) inflation caused by reductions in short-run aggregate supply.
- D) inflation caused by reductions in long-run aggregate supply.

Answer: B

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

8) Cost-push inflation is

- A) inflation caused by increases in aggregate demand that generate an even larger increase in aggregate supply.
- B) inflation caused by increases in aggregate demand that are not matched by increases in aggregate supply.
- C) inflation caused by decreases in aggregate supply that generate an even larger decrease in aggregate demand.
- D) inflation caused by decreases in aggregate supply that are not matched by decreases in aggregate demand.

Answer: D

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

9) Which of the following can cause inflation?

- A) Increases in short-run aggregate supply
- B) Increases in long-run aggregate supply
- C) Decreases in short-run aggregate supply
- D) Decreases in aggregate demand

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

10) The inflation associated with the oil price shocks in the 1970s after OPEC restricted the supply of oil is an example of

- A) cost-push inflation due to a supply shock.
- B) cost-push inflation due to a demand shock.
- C) demand-pull inflation due to a demand shock.
- D) demand-pull inflation due to a supply shock.

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 11) After a small hurricane in Florida, unemployment is low as there is a great deal of construction work and businesses run at full capacity. This suggests that
- A) the economy is operating above the full-employment level and will eventually adjust back to long-run aggregate supply.
 - B) living standards are falling as employment and economic activity are too high.
 - C) the economy is operating below its long-run level and living standards are less than they would have been without the hurricane.
 - D) the hurricane is beneficial since it is increasing employment and replacing less efficient capital with newer and more efficient capital.

Answer: A

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

- 12) A stronger U.S. dollar in world exchange markets means that
- A) a dollar buys more units of foreign currency than it could before.
 - B) a dollar buys less units of foreign currency than it could before.
 - C) a dollar buys the same amount of foreign currency than it could before, with gold backing up the value of the dollar.
 - D) foreigners sell the dollars that they have.

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

- 13) A stronger dollar leads to cheaper input prices for U.S. firms because
- A) U.S. workers are willing to work for less pay because of the stronger dollar.
 - B) U.S. producers of intermediate goods lower prices in order to benefit from the stronger dollar.
 - C) imports of raw materials and intermediate goods are cheaper.
 - D) exports of raw materials and intermediate goods are cheaper.

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 14) One effect of a stronger dollar is
- A) an increase in U.S. exports and a reduction in U.S. imports.
 - B) a reduction in U.S. exports and an increase in U.S. imports.
 - C) an increase in net exports.
 - D) an increase in both imports and exports. The effect on net exports is uncertain.

Answer: B

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 15) The net effect of a stronger dollar on real GDP is
- A) an increase in real GDP.
 - B) a decrease in real GDP.
 - C) an increase in the price level.
 - D) dependent on whether the increase in aggregate supply is more or less than the decrease in aggregate demand.

Answer: D

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 16) Suppose we observe the price level increasing and real GDP decreasing. An explanation for this is that
- A) the dollar weakened and the effect on aggregate supply was less than the effect on aggregate demand.
 - B) the dollar weakened and the effect on aggregate supply was greater than the effect on aggregate demand.
 - C) the dollar strengthened and the effect on aggregate supply was less than the effect on aggregate demand.
 - D) the dollar strengthened and the effect on aggregate supply was greater than the effect on aggregate demand.

Answer: B

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 17) Equilibrium real GDP rises after the dollar strengthened. From this, we can conclude that
- A) the increase in aggregate demand was greater than the decrease in aggregate supply.
 - B) the decrease in aggregate demand was less than the increase in aggregate supply.
 - C) the decrease in aggregate demand was more than the increase in aggregate supply.
 - D) the increase in aggregate demand was less than the decrease in aggregate supply.

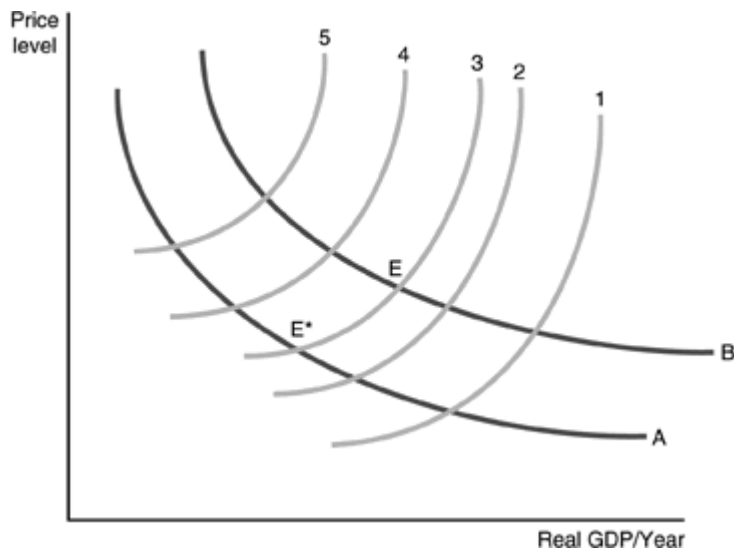
Answer: B

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition



- 18) Refer to the above figure. Suppose the economy is at E. A stronger dollar leads to a lower real GDP. Which of the aggregate supply curves must be the relevant curve after the change in the value of the dollar?

A) 1 B) 2 C) 4 D) 5

Answer: B

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 19) Refer to the above figure. Suppose the economy is at E originally, when the dollar increases in value. Which aggregate supply curve applies if the value of real GDP increases?

A) 1 B) 2 C) 4 D) 5

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 20) Refer to the above figure. Suppose we are at E* and the dollar weakens. Which aggregate supply curve must apply if the price level increases?

A) 3 only B) 4 only C) 5 only D) 4 or 5

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 21) Suppose the Japanese yen increases in its value relative to the U.S. dollar. In the U.S. economy,
- A) the price level will increase and real GDP will fall if the increase in aggregate demand is less than the decrease in aggregate supply.
 - B) the price level will increase and real GDP will fall if the decrease in aggregate demand is more than the increase in aggregate supply.
 - C) the price level will fall and real GDP will increase if the increase in aggregate supply is greater than the decrease in aggregate demand.
 - D) the price level will fall and real GDP will decrease if the decrease in aggregate demand is less than the increase in aggregate supply.

Answer: A

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

- 22) Cost-push inflation occurs
- A) when the aggregate supply curve shifts to the left, while aggregate demand remains stable.
 - B) when the aggregate supply curve shifts to the right, while aggregate demand remains stable.
 - C) when the aggregate demand curve shifts to the left, while aggregate supply remains stable.
 - D) when the aggregate demand curve shifts to the right, while aggregate supply remains stable.

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 23) Demand-pull inflation occurs
- A) when the aggregate supply curve shifts to the left, while aggregate demand remains stable.
 - B) when the aggregate supply curve shifts to the right, while aggregate demand remains stable.
 - C) when the aggregate demand curve shifts to the left, while aggregate supply remains stable.
 - D) when the aggregate demand curve shifts to the right, while aggregate supply remains stable.

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

24) If the price level should increase in the near term due to decreases in the short-run aggregate supply, the result would be

- A) demand-pull inflation.
- B) demand-pull recession.
- C) cost-push inflation.
- D) cost-pull expansion.

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

25) Suppose the Federal Reserve increases the money supply. Which of the following will tend to occur as a result of this policy in a Keynesian model?

- A) an inflationary gap
- B) demand-pull inflation
- C) a movement along the short-run aggregate supply curve
- D) all of the above

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

26) Other things being equal, if input prices rise in a country, then there would be

- A) cost-push inflation.
- B) demand-pull inflation.
- C) cost-push deflation.
- D) more production and a lower price level.

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

27) An increase in aggregate demand will tend to cause which of the following?

- A) a deflationary gap
- B) a recessionary gap
- C) cost-push inflation
- D) none of the above

Answer: D

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

28) Inflation caused by continually decreasing short-run aggregate supply is

- A) cost-pull inflation.
- B) cost-push inflation.
- C) demand-pull inflation.
- D) demand-push inflation.

Answer: B

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 29) Oil prices increased significantly in 2008. According to the Keynesian model, this increase in oil prices should have caused which of the following to occur?

A) demand-pull inflation B) demand-push inflation
C) cost-push inflation D) cost-pull inflation

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 30) Cost-push inflation can be shown on an aggregate supply aggregate demand diagram as
- A) a rightward shift of the aggregate supply curve with no change in aggregate demand.
B) a rightward shift in the aggregate demand curve with no change in aggregate supply.
C) a leftward shift in the aggregate demand curve with no change in aggregate supply.
D) a leftward shift in the aggregate supply curve with no change in aggregate demand.

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 31) Demand-pull inflation is caused by
- A) aggregate demand increasing along a horizontal aggregate supply curve.
B) aggregate demand decreasing along a horizontal aggregate supply curve.
C) aggregate demand decreasing along an upward sloping or a vertical aggregate supply curve.
D) aggregate demand increasing along an upward sloping or a vertical aggregate supply curve.

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 32) In the original *Austin Powers*, Dr. Evil is cryogenically frozen for thirty years (from the late 1960s to the late 1990s). Upon his return he hatches a plan to extort one million dollars from various world governments. His henchmen are unimpressed. What type(s) of inflation have made Dr. Evil's proposed blackmail amount seem too small?
- A) cost-push inflation
B) demand-pull inflation
C) both cost-price and price-pull inflation
D) both cost-push and demand-pull inflation

Answer: D

Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

33) Natural disasters like severe earthquakes are devastating to the economy as well as to the individuals harmed due to

- A) supply shocks.
- B) demand shocks.
- C) demand-pull inflation.
- D) demand-pull deflation.

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

34) Suppose the U.S. dollar gains strength against the euro (and against other major currencies).

This strengthening of the dollar will cause which of the following to occur?

- A) The aggregate demand curve will shift to the right and the short-run aggregate supply will shift to the right.
- B) The aggregate demand curve will shift to the left and the short-run aggregate supply will shift to the right.
- C) The aggregate demand curve will shift to the right and the short-run aggregate supply will shift to the left.
- D) the aggregate demand curve will shift to the left and the short-run aggregate supply will shift to the left.

Answer: B

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

35) Suppose the U.S. dollar weakens against the euro (and against other major currencies). This weakening of the dollar will cause which of the following to occur?

- A) The aggregate demand curve will shift to the right and the short-run aggregate supply will shift to the right.
- B) The aggregate demand curve will shift to the left and the short-run aggregate supply will shift to the right.
- C) The aggregate demand curve will shift to the right and the short-run aggregate supply will shift to the left.
- D) The aggregate demand curve will shift to the left and the short-run aggregate supply will shift to the left.

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 36) The exchange rate last month was \$1 = 3.2 Swiss francs. This month it is \$1 = 3.12 Swiss francs.

We can say that the value of the dollar

- A) fell, causing net exports to increase and aggregate demand to rise.
- B) fell, causing net exports to decrease and aggregate demand to fall.
- C) increased, causing net exports to decrease and aggregate demand to fall.
- D) increased, causing net exports to decrease and aggregate demand to rise.

Answer: A

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 37) The exchange rate last month was \$1 = 3.12 Swiss francs. This month it is \$1 = 3.21 Swiss francs.

We can say that the value of the dollar

- A) fell; causing net exports to increase and aggregate demand to rise.
- B) fell; causing net exports to decrease and aggregate demand to fall.
- C) increased; causing net exports to decrease and aggregate demand to fall.
- D) increased; causing net exports to decrease and aggregate demand to rise.

Answer: C

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 38) An appreciation of the U.S. dollar _____ the price of U.S. imports, and _____ the price of U.S. exports.

- A) lowers, lowers
- B) increases, increases
- C) increases, lowers
- D) lowers, increases

Answer: D

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 39) Suppose the U.S. dollar weakens against the euro (and against other major currencies). We know with certainty that this weakening of the dollar will cause which of the following to occur?

- A) a recessionary gap
- B) an inflationary gap
- C) a deflationary gap
- D) none of the above

Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 40) Suppose the euro appreciates against the dollar. This causes U.S. exports to become less expensive for consumers in the European Union, which would likely cause the U.S.
- A) aggregate supply to shift leftward.
 - B) aggregate supply to shift rightward.
 - C) aggregate demand to shift leftward.
 - D) aggregate demand to shift rightward.

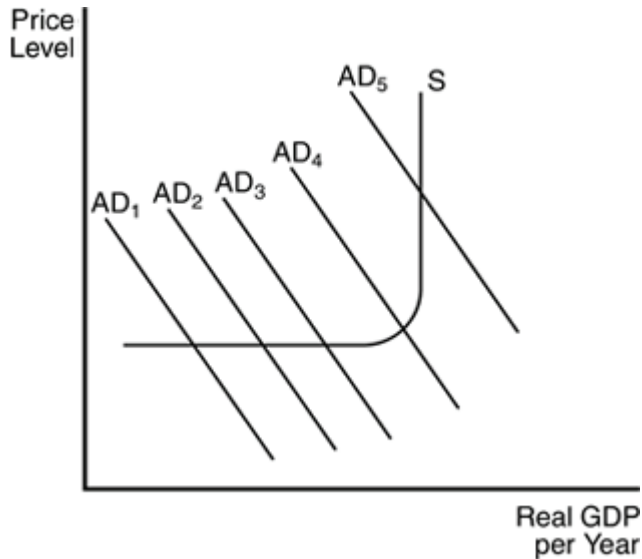
Answer: D

Diff: 2

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition



- 41) Refer to the above figure. If the aggregate demand curve shifts beyond AD₅, which of the following would we NOT expect?
- A) Strong demand-pull inflation
 - B) No increase in real Gross Domestic Product (GDP)
 - C) Strong and rapid increases in the price level
 - D) Increases in real net domestic product

Answer: D

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 42) Refer to the above figure. If the aggregate demand curve shifts beyond AD₅, then the economy will experience
- A) demand-pull inflation.
 - B) cost-push inflation.
 - C) structural inflation.
 - D) stagflation.

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Revised

- 43) When the value of the dollar increases, the net effect on the economy
- A) will be an increase in short-run aggregate supply and a decrease in aggregate demand.
 - B) will be decrease in short-run aggregate supply and an increase in aggregate demand.
 - C) will be an increase in both aggregate demand and aggregate supply.
 - D) will be a decrease in both aggregate demand and aggregate supply.

Answer: A

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 44) When the value of the dollar decreases, the net effect on the economy
- A) will be an increase in short-run aggregate supply and a decrease in aggregate demand.
 - B) will be decrease in short-run aggregate supply and an increase in aggregate demand.
 - C) will be an increase in both aggregate demand and aggregate supply.
 - D) will be a decrease in both aggregate demand and aggregate supply.

Answer: B

Diff: 1

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

- 45) What effect does a stronger dollar have on aggregate supply? Why?

Answer: A stronger dollar means that U.S. residents can buy foreign goods more cheaply. Since some of the foreign goods will be raw materials and partially processed goods, input prices fall, which causes aggregate supply to increase.

Diff: 1

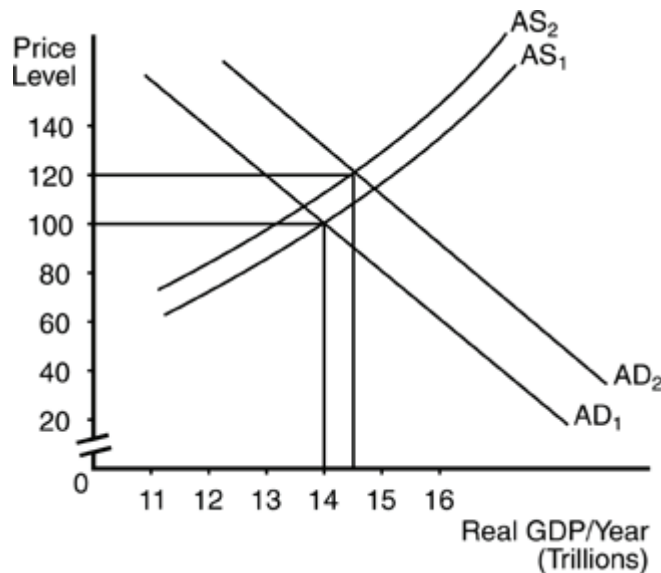
Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition

46) Using a graph, show the effects of a weaker dollar on the economy. Explain.

Answer: The original equilibrium is E_1 . A weaker dollar causes aggregate supply to decrease, represented by a shift from AS_1 to AS_2 . But the weaker dollar makes imports more expensive and exports cheaper, so aggregate demand increases from AD_1 to AD_2 . The new equilibrium is E_2 , with an increase in real Gross Domestic Product (GDP) and a rise in the price level. This result is due to the fact that aggregate demand shifted further than aggregate supply. Real Gross Domestic Product (GDP) would have fallen if the shift in aggregate supply had been greater than the shift in aggregate demand.



Diff: 3

Topic: 11.6 Explaining Short-Run Variations in Inflation

AACSB: Analytic skills

Question Status: Previous Edition