MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

1) Which of the following are aggregate demand theories of the business cycle?
   A) I and III  B) I, II and III  C) I only  D) I and II
   I. Keynesian theory
   II. real business cycle theory
   III. rational expectations theory

2) Keynesian theory explains business cycles as being the result of changes in
   A) firms’ expectations of future sales and profits.
   B) the growth rate of the quantity of money.
   C) expected consumption both now and in the future.
   D) government purchases of goods and services.

3) Keynes felt that expectations were
   A) volatile with future events hard to predict.
   B) constant with future events easy to predict.
   C) constant with future events hard to predict.
   D) volatile with future events easy to predict.

4) The Keynesian cycle can be characterized by ________money wage rate which results in a ________ short run aggregate supply curve.
   A) flexible; horizontal  B) sticky; horizontal
   C) flexible; vertical  D) sticky; vertical

5) The Keynesian view of the business cycle proposes that the money wage rate
   A) symmetrically responds to changes in aggregate demand.
   B) does not respond to changes in aggregate demand.
   C) always changes in response to changes in aggregate demand.
   D) responds only to increases in aggregate demand.

6) For monetarists the main cause of economic fluctuations is changes in
   A) the growth rate of the quantity of money.
   B) consumption.
   C) investment.
   D) the levels of household debt.

7) According to monetarists, the key determinant of expansions and recessions is
   A) the ineptitude of politicians to enact appropriate fiscal policies.
   B) the rate of change in interest rates.
   C) the rate of growth of the quantity of money.
   D) All of the above answers are correct.

8) According to monetarists, the money wage rate is
   A) flexible in the long run only.  B) always sticky.
   C) always flexible.  D) not discussed in monetarist theories.
9) Consider an economy at full employment, which then experiences an increase in the growth rate of the quantity of money. The monetarist business cycle predicts that in the long run, A) flexible money wage rates will bring equilibrium output back to its original level. B) sticky money wage rates will bring equilibrium output back to its original level. C) flexible money wage rates will bring the equilibrium price level back to its original level. D) sticky money wage rates will bring the equilibrium price level back to its original level.

10) Rational expectations theories of the business cycle predict that an unanticipated increase in aggregate demand will A) create an expansion, whereas an anticipated increase in aggregate demand would not. B) create an expansion, just as an anticipated increase in aggregate demand would. C) Either answer A or B could be true, depending on whether new classical or new Keynesian assumptions are held. D) Neither new classical nor new Keynesian theories would predict answers A or B, so both answers are incorrect.

11) The difference between the two rational expectations theories (new classical and new Keynesian) is that new classical puts more emphasis on A) unanticipated fluctuations in aggregate demand as the factor that changes real GDP. B) rational expectations. C) anticipated fluctuations in aggregate demand as the factor that changes real GDP. D) the Phillips curve.

12) Assume an increase in aggregate demand is less than expected. According to the new classical theory A) both real GDP and potential GDP decrease. B) neither real GDP nor potential GDP decrease. C) actual real GDP decreases and potential GDP does not change. D) real GDP does not change and potential GDP decreases.

13) Which theory emphasizes because of long-term wage agreements, both anticipated and unanticipated fluctuations in aggregate demand can change real GDP? A) Keynesian theory B) the new Keynesian theory of the business cycle C) monetarist theory D) the new classical theory of the business cycle

14) Which theory views fluctuations in productivity growth as the main source of economic fluctuations? A) Keynesian theory B) monetarist theory C) real business cycle theory D) rational expectations theory

15) Real business cycle economists claim that the intertemporal substitution effect A) plays a large role in the economy only during expansions. B) plays a small role in the labor market. C) has unpredictable effects on the economy. D) depends on the real interest rate.
16) Fiscal policy can be defined as
A) government policy with respect to transfer payments such as unemployment compensation and welfare.
B) government spending and tax decisions accomplished using automatic stabilizers.
C) government policy to retire the federal government debt.
D) use of the federal budget to reach macroeconomic objectives.

17) The Employment Act of 1946 made it the responsibility of the federal government to
A) promote maximum employment.
B) provide full employment and a stable balance of payments.
C) balance its budget because that policy would create the maximum level of employment.
D) improve the distribution of income.

18) A government surplus is defined as
A) interest payments on the federal government debt.
B) the government printing money to pay its bills.
C) an excess of government revenues relative to government expenditures.
D) on-budget expenditures.

19) The federal government debt is equal to the
A) cumulative sum of annual federal deficits minus surpluses.
B) annual difference between federal revenues and expenditures.
C) sum of all annual federal expenditures.
D) obligations of benefits from federal taxes and expenditures.

20) If a tax cut increases people's labor supply, then
A) tax cuts decrease aggregate demand.
B) tax cuts cannot affect aggregate demand.
C) tax cuts increase potential GDP.
D) Both answers A and B are correct.

21) The income tax ______ potential GDP by shifting the labor ______ curve ______.
A) increases; demand; rightward
B) decreases; demand; leftward
C) decreases; supply; leftward
D) increases; supply; rightward

22) The crowding out effect refers to
A) private investment crowding out government saving.
B) private saving crowding out government saving.
C) government spending crowding out private spending.
D) government investment crowding out private investment.

23) According to the Ricardo-Barro effect,
A) government budget deficits increase households' expected future disposable income.
B) government deficits raise the real interest rate.
C) households increase their personal saving when governments run budget deficits.
D) taxpayers fail to foresee that government deficits imply higher future taxes.

24) The difference between automatic fiscal policy and discretionary fiscal policy is that
A) the President has nothing to do with discretionary fiscal policy.
B) Congress initiates automatic fiscal policy.
C) Congress must pass laws implementing discretionary fiscal policy.
D) the President initiates discretionary fiscal policy.
25) Suppose the government increases taxes. This change decreases
   A) disposable income, which decreases consumption expenditure and aggregate expenditure.
   B) consumption expenditure and spending on imports. The effect on aggregate expenditure
      depends on whether domestic spending or spending on imports decreases the most.
   C) disposable income, which decreases aggregate supply.
   D) government spending, which decreases aggregate expenditure.
Answer Key
Testname: MACRO QUIZ 6

1) A
2) A
3) A
4) B
5) D
6) A
7) C
8) A
9) A
10) C
11) A
12) C
13) B
14) C
15) D
16) D
17) A
18) C
19) A
20) C
21) C
22) D
23) C
24) C
25) A