

## Macro final exam test bank – T/F questions

Note that these are questions -- not always true statements.

You will have to supply the reason why a false statement is false on the final for credit.

### Case, Fair, Oster

#### Chapter 8 – Aggregate Expenditure and Equilibrium Output

1. Firms react to unplanned inventory investment by increasing output.
2. If actual investment is greater than planned investment, inventories decrease more than planned.
3. Disposable income is the major determinant of consumption spending in classical thought (for example, in the economics of Jean-Baptiste Say).
4. The marginal propensity to consume is the change in consumption expenditure divided by the change in income.
5. If the MPC is 0.8, the marginal propensity to save will be 0.4.
6. In a Keynesian macroeconomic model, private savings will equal the sum of private investment, the government budget deficit, and the international current account surplus.
7. When the economy is in Keynesian macroeconomic equilibrium, planned investment is equal to actual investment.
8. The larger the MPS, the smaller the Keynesian government spending multiplier.
9. If the MPC is 0.75, the Keynesian government spending multiplier will be 4/3
10. If the MPC is 0.75, the lump-sum tax multiplier will be -4
11. If an economy shifts from lump-sum taxes to income taxes, an increase in government spending will result in a smaller increase in GDP.
12. If the marginal propensity to save increases, the multiplier will decrease.
13. If everyone increases their marginal propensity to save, the Keynesian model predicts that total saving will not increase, and may decline.

#### Chapter 9 – The Government and Fiscal Policy

1. Disposable income is income minus taxes plus transfer payments.
2. When actual investment is greater than planned investment, the economy will grow.
3. When  $G - T$  is positive, the government budget is in deficit.
4. If investment increases, the planned aggregate expenditure line on the Keynesian cross diagram shifts upward.
5. If the MPC increases, the planned aggregate expenditure line on the Keynesian cross diagram becomes flatter.
6. In a simple Keynesian model (with lump-sum taxes and a MPC of 0.8), if the government increases spending by \$400 billion and increases taxes by \$400 billion, output will increase by \$2000 billion.
7. In a simple Keynesian model (with lump-sum taxes and a MPC of 0.8), a tax cut of \$ 10 billion will have more of an impact on GDP than an increase in government spending of \$ 10 billion.
8. When taxes are given as a percentage of income, a higher tax rate implies a smaller government spending multiplier.
9. In an open economy, the government spending multiplier will be higher than in an economy without international trade.

## **Chapter 10. The Money Supply and the Federal Reserve System**

1. The most important role of money is to serve as a store of value.
2. Only items defined by the government as legal tender count as M1.
3. The major problem of barter is the need for a double coincidence of wants.
4. When you take \$ 100 from your savings account and deposit it in your checking account, M1 increases.
5. When you take \$ 100 from your savings account and deposit it in your checking account, M2 stays the same.
6. If a bank sells a \$ 10,000 Treasury bill to the Federal Reserve, and receives a credit in its account with the Fed, the money supply will increase by more than \$ 10,000.
7. If a bank sells a \$ 10,000 Treasury bill to the Federal Reserve, and receives a credit in its account with the Fed, the money supply will decrease by exactly \$ 10,000.
8. If a bank has liabilities of \$ 3 million and a net worth of \$ 1 million, its assets will be \$ 4 million.
9. A bank will list the mortgage loans it makes as assets.
10. A bank is said to have a "liquidity problem" when its capital is too low to cover likely losses on bad loans.
11. The Federal Reserve will act as a "lender of last resort" if a bank runs into liquidity problems.
12. The required reserve ratio is 0.25 (twenty-five percent) and a bank has \$ 800 in deposits. Its actual reserves are \$ 300, so it will have excess reserves of \_\_\_\_\_.
13. The policy making body of the Federal Reserve System is known as the \_\_\_\_\_.
14. The one Federal Reserve Bank that is automatically a member of the policy making body of the Fed is the Washington, DC bank.
15. Most \$ 100 dollar bills issued in the US are issued by the Federal Reserve Bank of Chicago.
16. The Federal Reserve is headed by the Secretary of the Treasury.
17. A decrease in the required reserve ratio will normally increase the money supply.
18. The most commonly used tool of monetary policy by the Federal Reserve system is to change the required reserve ratio.
19. An open market purchase of government securities (such as Treasury Bills) by the Fed will increase the money supply and raise the interest rate.
20. The most commonly used tool of monetary policy by the Fed is open market operations..

## **Chapter 11. The Demand for Money**

1. The rate of interest is the opportunity cost of holding money.
2. More frequent switching from bonds to money will result in a higher opportunity cost of holding money and lower money management costs.
3. The optimal money balance desired will be lower if the CPI is higher.
4. The optimal money balance desired will be lower if the inflation rate is higher.
5. The optimal money balance desired will be lower if the interest rate is higher.
6. The optimal money balance desired will be lower if the level of real income is higher.
7. If people think that interest rates are above normal levels, they will want to hold bonds in anticipation of a rise in bond prices.
8. Investors will probably wish to hold bonds when interest rates are low in the hope of selling them at higher prices when interest rates increase.
9. If the money supply increases, and the price level is unchanged, interest rates will fall.
10. If the money supply and the price level both increase by 10 percent, interest rates will not change.
11. The Fed has more control over short-term interest rates than long-term interest rates.
12. "Federal funds" are the interest rates charged by the Fed on its loans to commercial banks.

## **Chapter 12. Aggregate Demand in the Goods and the Money Markets.**

1. The axes of the goods market-money market graph in Chapter 12 (the IS-LM graph) are real GDP or income on the horizontal axis and the interest rate on the vertical axis.
2. An increase in the money supply will lead to a shift down and to the right of the money-market (LM) curve.
3. The study by Gilchrist, Natalucci and Zakrajsek finds that investment spending is highly responsive to interest rates, and will drop by more than one percent when interest rates increase by one percent.
4. The tendency for increases in government spending to cause decreases in private saving is known as the crowding out effect.
5. If investment is less responsive to changes in interest rates, the crowding-out effect will be greater, and therefore fiscal policy will be less effective in increasing GDP.
6. A decrease in government spending and an increase in investment will, unambiguously, lead to higher interest rates, according to the goods-money-market graph (IS-LM graph).
7. A policy mix of an expansionary fiscal policy and a contractionary monetary policy will, unambiguously, result in a higher interest rate.
8. A policy mix of a contractionary fiscal policy and an expansionary monetary policy, will, unambiguously, result in a lower interest rate.
9. GDP will decrease due to a movement along the aggregate demand curve when the price level rises because the increase in price level causes the demand for money to increase and hence the interest rate to rise.
10. Each point along the aggregate demand curve represents a point at which the goods market and money market are in equilibrium, given the money supply, the level of government spending, taxes and investment demand.
11. Only the goods market is in equilibrium at any point along the AD curve; the money market may or may not be in equilibrium.
12. An increase in the money supply will shift the AD curve upwards and to the right.
13. When the overall price level rises, consumption falls due to the real wealth effect.
14. An increase in taxes will shift the AD curve upwards and to the right.
15. An increase in the overall price level causes the AD curve to shift up and to the right.

## **Chapter 13. Aggregate Supply and the Equilibrium Price Level**

1. An increase in prices will cause an increase in the amount supplied, according to the AD-AS graph of chapter 13.
2. An increase in the price of a key input in production, such as oil, will cause the AS curve to shift down and to the right.
3. The long-run aggregate supply curve is vertical because wages and other input prices eventually fully adjust to changes in prices.
4. The short-run aggregate supply curve is not vertical because wages and other input prices do not fully adjust to changes in prices.
5. Rising output coupled with falling prices is called stagflation.
6. Expansionary monetary policy when the economy is operating with a good deal of excess capacity will likely result in more inflation than increase in GDP.
7. The Fed is said to be “leaning against the wind” when it raises its discount rate in response to inflation.

## **Chapter 14. (More questions to come)**

## **Chapter 15. Policy Timing, Deficit Targeting, and Stock Market Effects.**

1. Monetary policy has a shorter “implementation lag” than does fiscal policy.
2. The time it takes policymakers to realize that the economy is going into a recession is known as the “recognition lag”
3. The NBER sometimes does not declare the official end of a contraction for more than a year.
4. Fiscal policy has a longer implementation lag than monetary policy, but a shorter response lag.
5. Milton Friedman thought that monetary and fiscal policy could often be counter-productive because of the time lags involved in recognition, implementation and response.
6. The deficit will decrease during recessions and increase during expansions.
7. The federal debt is the total of all accumulated deficits (minus surpluses) over time