Name: ________________________ Class: ___________________ Date: __________ ID: A

CH 31 sample questions

Multiple Choice
Identify the choice that best completes the statement or answers the question.

____ 1. The federal budget is defined as
a. a monthly statement of expenditure laws passed by the U.S. government.
b. a monthly statement of whether the U.S. government is in deficit or surplus.
c. an annual statement of U.S. government violations of international laws.
d. an annual statement of expenditures and tax revenues of the U.S. government.
e. an annual statement of what policy actions the U.S. government has pursued.

____ 2. In the United States for the year 2005, the federal government had a ____ so the national debt was ____.
a. budget deficit; increasing
b. balanced budget; not changing
c. budget surplus; decreasing
d. budget deficit; decreasing
e. budget surplus; increasing

____ 3. If the federal government has a budget surplus, then it is definitely the case that
a. tax receipts exceed government expenditures.
b. tax receipts and government expenditures are equal.
c. tax receipts are falling and government expenditures are rising.
d. government expenditures exceed tax receipts.
e. tax receipts are rising and government expenditures are falling.

____ 4. When government expenditures exceed tax receipts, the situation is called a budget
a. with a negative balance.
b. deficit.
c. surplus.
d. debt.
e. with no balance.

____ 5. The national debt is the amount
a. by which government tax receipts exceed expenditure in a given year.
b. of debt outstanding that arises from past budget deficits.
c. by which government expenditure exceeds tax receipts in a given year.
d. of government expenditures summed over time.
e. of all future entitlement spending.

____ 6. The annual federal budget is decided upon by the
a. President of the United States and the Federal Reserve system.
b. President of the United States and the United States Treasury.
c. President of the United States and the United States Congress.
d. United States Congress and the Federal Reserve System.
e. the United States Treasury alone.

____ 7. Determining the federal budget
  a. is done solely by the President of the United States.
  b. is done solely by Congress.
  c. starts with a proposal from the President of the United States with tough choices made by Congress.
  d. starts with proposals from the Senate and House and tough choices made by the President of the United States.
  e. is done solely by the United States Treasury.

____ 8. Discretionary fiscal policy is defined as fiscal policy
  a. left to the discretion of military authorities.
  b. initiated by an act of Congress.
  c. initiated by a Presidential proclamation.
  d. triggered by the state of the economy.
  e. with multiplier effects.

____ 9. In 2001, Congress passed tax laws to reduce income tax rates for all taxpayers. This action is called
  a. a discretionary fiscal policy.
  b. a discretionary revenue policy.
  c. an automatic fiscal policy.
  d. an annual tax policy.
  e. induced tax policy.

____ 10. The government expenditure multiplier is used to determine the
  a. extra scrutiny government action receives.
  b. amount aggregate demand is affected by a change in government expenditures.
  c. amount aggregate supply is affected by a change in government expenditures.
  d. amount private consumption is decreased by government expenditures.
  e. extent to which automatic stabilizers must be changed in order to avoid recessions.

____ 11. The magnitude of the government expenditure multiplier is ____ the magnitude of the tax multiplier.
  a. greater than
  b. equal to
  c. less than
  d. not comparable to
  e. greater than for expansionary policy and less than for contractionary policy

____ 12. If the government reduces expenditures on goods and services by $30 billion, then aggregate demand
  a. decreases and real GDP decreases.
  b. decreases and potential GDP decreases.
  c. increases and real GDP increases.
  d. increases and potential GDP increases.
  e. increases and potential GDP decreases.

____ 13. The magnitude of the tax multiplier is smaller than the magnitude of the government expenditure multiplier because
  a. a change in taxes does not change expenditures.
  b. an increase in taxes decreases expenditures.
  c. a decrease in government expenditures decreases tax revenue.
  d. a change in taxes does not change expenditures by as much as the same size change in government expenditures.
  e. a change in taxes creates additional induced taxes.

____ 14. The balanced budget multiplier is
a. equal to zero because taxes and government expenditures are changed to leave the budget balanced.
b. misnamed because it does not leave the budget balanced.
c. greater than zero and less than the government expenditure multiplier.
d. greater than zero and greater than the government expenditure multiplier.
e. less than zero, that is, it is negative.

____ 15. When comparing a $100 billion increase in government spending to a $100 billion decrease in tax revenue, the effect of the increase in government expenditure on aggregate demand is ____
a. greater than the effect of the tax decrease.
b. equal to the effect of the tax decrease.
c. less than the effect of the tax decrease.
d. positive whereas the effect of the tax decrease is negative.
e. negative whereas the effect of the tax decrease is positive.

____ 16. The balanced budget multiplier applies when a $50 billion increase in government expenditure is financed by a $50 billion ____ in tax revenue and the balanced budget multiplier shows that in this case there is ____ effect on aggregate demand.
a. decrease; no
b. decrease; a positive
c. increase; no
d. increase; a positive
e. increase; a negative

____ 17. If the economy is in equilibrium with real GDP less than potential GDP, there is ____ gap and a fiscal policy that ____ is appropriate.
a. an inflationary; increases aggregate demand
b. an inflationary; decreases aggregate demand
c. a recessionary; increases aggregate demand
d. a recessionary; decreases aggregate demand
e. a recessionary; increases potential GDP

____ 18. Suppose the economy is in an equilibrium in which real GDP is less than potential GDP. To increase real GDP, the government can use a discretionary fiscal policy of
a. increasing taxes only.
b. decreasing government expenditures only.
c. decreasing taxes and/or increasing government expenditures.
d. decreasing government expenditures and simultaneously increasing taxes.
e. increasing the quantity of money.

____ 19. If the economy is in an equilibrium with real GDP less than potential GDP, discretionary fiscal policy could move the economy toward potential GDP by simultaneously ____ taxes and ____ government expenditures on goods and services.
a. raising; increasing
b. raising; decreasing
c. cutting; increasing
d. cutting; decreasing
e. raising; not changing

____ 20. To eliminate a recessionary gap, the government can ____ government expenditures on goods and services or ____ taxes.
a. increase; increase
b. increase; decrease
c. decrease; increase
d. decrease; decrease
e. increase; not change

____ 21. When an economy faces an inflationary gap, an appropriate fiscal policy is to
a. decrease government expenditure.
b. decrease taxes.
c. increase aggregate demand.
d. increase the quantity of money.
e. decrease the quantity of money.

____ 22. If an economy is in an equilibrium with an inflationary gap, policy-makers can use
a. discretionary fiscal policy and increase government expenditure.
b. automatic fiscal policy and increase government expenditure.
c. automatic fiscal policy and cut taxes.
d. discretionary fiscal policy and decrease government expenditure.
e. discretionary fiscal policy and cut taxes.

____ 23. A decrease in taxes should be applied in a situation with
a. a recessionary gap.
b. a inflationary gap.
c. low unemployment.
d. high demand for goods and services.
e. no tax multiplier.

____ 24. How could an expansionary fiscal policy increase real GDP and lower the price level?
a. if aggregate supply decreases more than aggregate demand increases
b. if aggregate supply increases more than aggregate demand increases
c. if the aggregate supply increases equals the aggregate demand increase
d. if aggregate supply decreases more than aggregate demand decreases
e. if aggregate supply decreases less than aggregate demand decreases

____ 25. A reason why discretionary fiscal policy might move the economy away from potential GDP instead of toward potential GDP is that
a. economic forecasts consistently underestimate the impact of fiscal policy.
b. it is difficult to know whether real GDP is above or below potential GDP.
c. during a recession, politicians prefer increases in government spending over decreasing taxes.
d. government programs automatically move real GDP away from potential GDP.
e. government programs are always expansionary.

____ 26. Automatic stabilizers are defined as
a. actions taken by the President without Congressional consent to stabilize the economy.
b. actions taken by an act of Congress to stabilize the economy.
c. policy that stabilizes without the need for action by the government.
d. discretionary policy taken to stabilize the economy.
e. policy that has no multiplier effects.

____ 27. An example of automatic fiscal policy is
a. Congress passing a tax rate reduction package.
b. the federal government expanding spending at the Department of Education.
c. expenditures for unemployment compensation increasing as economic growth slows.
d. the Federal Reserve reducing interest rates as economic growth slows.
e. a change in taxes that has no multiplier effect.

____ 28. Automatic changes in tax revenues and expenditures that occur as a result of fluctuations in real GDP are referred to as automatic
a. taxes and expenditures.
b. discretionary taxes and expenditures.
c. government.
d. stabilizers.
e. discretionary policy.

____ 29. Taxes that vary with real GDP are called
a. customs taxes.
b. induced taxes.
c. property taxes.
d. automatic taxes.
e. variable taxation.

____ 30. Government spending on programs that pay suitably qualified people and business benefits are called
a. suitable programs.
b. entitled people.
c. suitable spending.
d. needs-tested spending.
e. induced spending.

____ 31. Needs-tested spending is defined as
a. spending by Congress on its own perks of office.
b. taxes paid by those qualified by their income.
c. spending on programs for people qualified to receive benefits.
d. spending by the President on the White House.
e. spending that increases in expansions and decreases in recessions.

____ 32. Needs-tested spending
a. increases as real GDP increases.
b. increases as unemployment increases.
c. decreases as unemployment increases.
d. decreases in recession.
e. makes recessions more severe.

____ 33. Needs-tested spending
a. increases in recessions and decreases in expansions.
b. decreases in recessions and increases in expansions.
c. does not change with the level of economic activity.
d. is always increasing regardless of whether we are in an expansion or a recession.
e. cannot be changed unless the government changes the spending laws.

____ 34. Needs-tested spending
- a. is directing government spending and taxes to states that need the most help.
- b. is giving tax cuts to wealthy people so they will increase their spending.
- c. includes transfer payments such as food stamps and unemployment benefits.
- d. includes homeland defense spending.
- e. cannot be changed without changes in the laws.

____ 35. Automatic stabilizers include
- a. changes in induced taxes and changes in needs-tested spending.
- b. increases or decreases of tax rates and changes in needs-tested spending.
- c. changes in induced taxes and changes in discretionary spending.
- d. changes in discretionary spending and changes in needs-tested spending.
- e. changes in the federal funds interest rate brought about by Fed policy.

____ 36. In a recession, needs-tested spending ____ and induced taxes ____.
- a. increases; increase
- b. increases; decrease
- c. decreases; increase
- d. decreases; decrease
- e. increase; do not change

____ 37. An economic expansion leads to ____ needs-tested spending and ____ induced taxes.
- a. higher; lower
- b. lower; higher
- c. higher; higher
- d. lower; lower
- e. lower; no change in

____ 38. The Beige Book is
- a. a periodic report on the current economic conditions of the country.
- b. a periodic set of goals and policies that Congress sets for the Fed.
- c. the instruction manual to conduct monetary policy that only the chairman of the Fed can read.
- d. the book that contains the top-secret codes for changing the quantity of money.
- e. a report on current income tax rates and other aspects of the tax code.

____ 39. Monetary policy decisions are made by the
- a. Federal Reserve Economic Committee.
- b. Federal Open Market Committee.
- c. Council of Economic Advisors.
- d. Congress of the United States.
- e. U.S. Mint.

____ 40. Monetary policy decisions in the United States are made by the
- a. Federal Reserve in consultation with the U.S. Treasury.
- b. Federal Reserve in consultation with Congress.
- c. Federal Reserve.
- d. Congress and the President.
- e. U.S. mint.

____ 41. In the United States,
a. Congress must approve monetary policy changes.
b. Congress initializes changes in monetary policy and the Fed approves the changes.
c. the Federal Reserve sets monetary policy.
d. the Federal Reserve sets monetary and fiscal policies.
e. the President initializes changes in monetary policy and the Fed approves the changes.

____ 42. To change the federal funds rate, the Fed
a. tells banks how much to charge.
b. coordinates with banks on establishing the new rate.
c. increases or removes money from the stock market.
d. uses open market operations to change the quantity of money.
e. changes the income tax rate on interest income.

____ 43. In the short run, if the Fed wants to raise the interest rate, it
a. instructs large commercial banks to sell government securities in the open market.
b. instructs the New York Fed to sell government securities in the open market.
c. tells large commercial banks to raise their interest rates.
d. instructs the New York Fed to sell government securities in the foreign exchange market
.
e. instructs the New York Fed to buy government securities in the open market.

____ 44. The Fed ____ influence the real interest rate in the short run and ____ influence the real interest rate in the long run.
a. can; can
b. can; cannot
c. cannot; can
d. cannot; cannot
e. might be able to; might be able to

____ 45. In the short run, when the Fed raises the nominal interest rate,
a. the real interest rate is unchanged so investment and consumption expenditure are not changed.
b. the real interest rate temporarily increases, thereby decreasing investment and consumption expenditure.
c. the real interest rate temporarily falls, thereby increasing investment and consumption expenditure.
d. investment and consumption expenditure increase, thereby raising the real interest rate temporarily.
e. the real interest rate temporarily increases, thereby decreasing investment and increasing consumption expenditure.

____ 46. In the long run, the real interest rate is determined by
a. Fed actions.
b. the expected inflation rate.
c. the nominal interest rate.
d. saving supply and investment demand.
e. the multiplier effect.

____ 47. In the long run, the Federal Reserve influences the
- a. real interest rate by the effects of its tax policies.
- b. nominal interest rate by the effects of its policies on the inflation rate.
- c. real interest rate by the effects of its policies on the inflation rate.
- d. nominal interest rate by the effects of its tax policies.
- e. real interest rate by buying and selling government securities.

____ 48. In the short run, to decrease the interest rate the Federal Reserve ____ the quantity of money by ____ government securities.
- a. increases; selling
- b. increases; buying
- c. decreases; selling
- d. decreases; buying
- e. None of the above answers are correct because in the short run the Federal Reserve cannot change the interest rate.

____ 49. A change in monetary policy affects
- a. consumption expenditure, government expenditures on goods and services, and net exports.
- b. consumption expenditure, investment, and net exports.
- c. investment, government expenditures on goods and services, and net exports.
- d. consumption expenditure, productivity, and net exports.
- e. government expenditures on goods and services because it affects the government's budget balance.

____ 50. If the Fed increases interest rates, other things remaining the same, foreigners demand ____ dollars thereby ____ the price of the dollar on the foreign exchange market.
- a. more; increasing
- b. more; decreasing
- c. fewer; increasing
- d. fewer; decreasing
- e. the same number of; not affecting

____ 51. When the price of the dollar decreases on the foreign exchange market, imports ____ and exports ____.
- a. increase; increase
- b. increase; decrease
- c. decrease; increase
- d. decrease; decrease
- e. decrease; do not change

____ 52. If the Fed buys government securities, other things the same, the price of the dollar on the foreign exchange market ____ and U.S. exports ____.
- a. rises; increase
- b. rises; decrease
- c. falls; increase
- d. falls; decrease
- e. falls; do not change because they are autonomous expenditure

____ 53. As the interest rate increases in the United States, the demand for U.S. dollars in the foreign exchange markets
- a. decreases and exports increase.
- b. increases and exports decrease.
- c. decreases and exports decrease.
- d. increases and exports increase.
- e. increases and imports increase.

____ 54. If the Fed decreases the interest rate, exports ____ and imports ____.
- a. increase; increase
- b. increase; decrease
- c. decrease; increase
- d. decrease; decrease
- e. do not change because they are autonomous; decrease

____ 55. If the Fed decreases the quantity of money,
- a. investment increases.
- b. real GDP increases.
- c. exports increase and imports decrease.
- d. exports decrease and imports increase.
- e. in the short run the interest rate falls.

____ 56. To curb inflation, the Fed ____ the quantity of money and, in the short run, ____ the interest rate.
- a. increases; raises
- b. increases; lowers
- c. decreases; raises
- d. decreases; lowers
- e. does not change; the Fed raises

____ 57. The Fed is concerned that inflation might occur. To help eliminate this possibility, the Fed could ____ government securities to ____ the interest rate in the short run.
- a. buy; lower
- b. buy; raise
- c. sell; lower
- d. sell; raise
- e. sell; not change

____ 58. When the Fed worries about inflation, it ____ the quantity of money and, in the short run, ____ the interest rate.
- a. increases; lowers
- b. increases; raises
- c. decreases; lowers
- d. decreases; raises
- e. does not change; the Fed raises

____ 59. If real GDP exceeds potential GDP, to move the economy to potential GDP the Fed
- a. raises the interest rate to increase potential GDP but not real GDP.
- b. lowers the interest rate to decrease real GDP but not potential GDP.
- c. raises the interest rate to decrease real GDP but not potential GDP.
- d. lowers the interest rate to increase potential GDP but not real GDP.
- e. raises the interest rate to decrease both real GDP and potential GDP.

____ 60. If the Fed raises the interest rate, initially the
a. *AD* curve shifts rightward and real GDP increases.
b. *AD* curve shifts leftward and real GDP decreases.
c. *AS* curve shifts rightward and real GDP increases.
d. *AS* curve shifts leftward and real GDP decreases.
e. *AD* curve shifts rightward and real GDP decreases.

____ 61. If the Fed raises the interest rate, initially the
a. *AD* curve shifts leftward, decreasing real GDP and increasing the price level.
b. *AS* curve shifts leftward, decreasing real GDP and increasing the price level.
c. *AD* curve shifts rightward, increasing real GDP and the price level.
d. *AD* curve shifts leftward, decreasing real GDP and the price level.
e. *AS* curve shifts rightward, decreasing real GDP and increasing the price level.

____ 62. If the Fed's policies aim to increase aggregate demand, the Fed must fear
a. inflation.
b. recession.
c. stagflation.
d. a supply shock that decreases potential GDP.
e. a supply shock that increases aggregate supply.

____ 63. If the Fed fears a recession, it
a. sells government securities.
b. decreases the quantity of money.
c. buys government securities.
d. decreases aggregate demand.
e. decreases aggregate supply.

____ 64. During 2002, the Federal Reserve feared that the United States economy was growing too slowly and was stuck in a recession. To move the economy back to its potential GDP, the most likely policy action was for the Fed to ____ the quantity of money and thus ____.
a. increase; increase aggregate demand
b. increase; decrease aggregate demand
c. decrease; increase aggregate supply
d. decrease; decrease aggregate supply
e. increase; increase aggregate supply

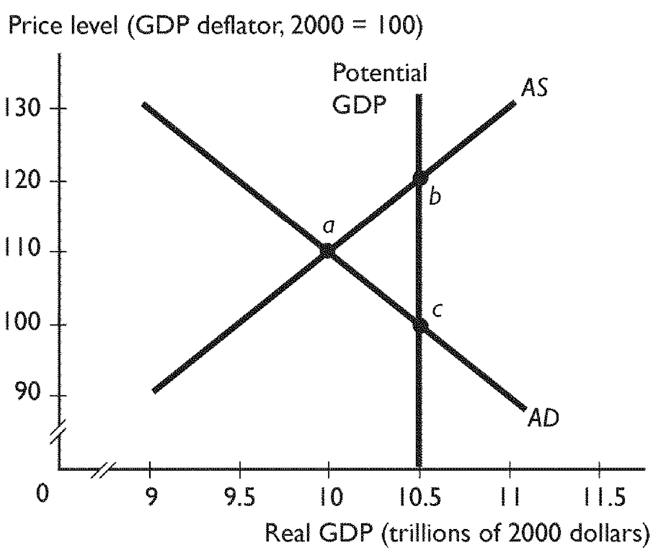
____ 65. As the Fed lowers the interest rate,
a. aggregate demand increases.
b. real GDP decreases.
c. the price level falls.
d. aggregate income decreases.
e. aggregate supply increases.

____ 66. If the Fed increases the quantity of money and lowers the interest rate, real GDP ____ and the price level ____.
a. increases; increases
b. increases; decreases
c. decreases; increases
d. decreases; decreases
e. increases; does not change

____ 67. If the Federal Reserve uses open market operations to offset a recession, the Fed ____ government securities in order to ____ the interest rate.
a. sells; raise
b. sells; lower
c. buys; raise
d. buys; lower
e. buys; not change

____ 68. In a recession, the Fed's monetary policy aims to ____ the interest rate, ____ aggregate demand, and ____ aggregate supply.
a. increase; decrease; not change.
b. decrease; increase; not change
c. increase; not change; increase
d. decrease; increase; increase
e. increase; increase; increase

____ 69. To fight a recession, an appropriate monetary policy would be that the Fed conducts an open market operation that ____ government securities, ____ the interest rate, and ____ aggregate demand.
a. sells; raises; increases
b. sells; raises; decreases
c. buys; lowers; increases
d. buys; lowers; decreases
e. sells; lowers; increases



____ 70. The economy is at the equilibrium shown as point *a* in the above figure. To restore the economy to potential GDP, the Fed should
a. buy government securities and thereby increase aggregate demand.
b. sell government securities and thereby increase aggregate demand.
c. sell government securities and thereby decrease aggregate demand.
d. buy government securities and thereby decrease aggregate demand.
e. buy government securities and thereby increase aggregate supply.

____ 71. The economy is at the equilibrium shown at point *a* in the above figure. If the Fed
a. buys government securities, the economy moves to an equilibrium at point *c*.
b. buys government securities, the economy moves to an equilibrium at point *b*.
c. sells government securities, the economy moves to an equilibrium at point *c*.
d. sells government securities, the economy moves to an equilibrium at point *b*.
e. None of the above are correct because the economy will remain at point *a* if the Fed buys or if the Fed sells government securities.

____ 72. Which of the following statements is true?
a. Monetary policy has an advantage over fiscal policy because monetary policy does not have a law-making time lag.
b. Fiscal policy has an advantage over monetary policy because fiscal policy does not have a law-making time lag.
c. Monetary policy has an advantage over fiscal policy because monetary policy does not need to estimate potential GDP.
d. Fiscal policy has an advantage over monetary policy because fiscal policy does not need to estimate potential GDP.
e. Fiscal policy has an advantage over monetary policy because fiscal policy has a multiplier effect whereas monetary policy does not.

____ 73. The limitations shared by both monetary policy and fiscal policy are
a. economic forecasting difficulties and law-making time lags.
b. estimating potential GDP and economic forecasting difficulties.
c. estimating potential GDP difficulties and law-making time lags.
d. estimating potential GDP difficulties, economic forecasting difficulties and law-making time lags.
e. only the economic forecasting difficulties.

____ 74. If we compare monetary policy to fiscal policy we see that
a. monetary policy suffers from a worse law-making lag than fiscal policy.
b. they both have limitations of estimating potential GDP and forecasting future economic activity.
c. monetary policy has precisely the same limitations as fiscal policy.
d. monetary policy can only be conducted once every eight weeks whereas fiscal policy can be conducted more frequently.
e. monetary policy has no limitations.

____ 75. Do automatic fiscal stabilizers eliminate business cycles?
a. Yes.
b. No, because they have no effect if the business cycle is the result of some unanticipated change.
c. No, but they do moderate business cycles.
d. No, they increase the likelihood that a business cycle occurs.
e. No, they make business cycle fluctuations more severe.

____ 76. In the long run, the Fed
- i. directly controls the real interest rate.
- ii. has no control over the inflation rate.
- iii. influences the nominal interest rate.

- a. i only.
- b. ii only.
- c. iii only.
- d. i and iii.
- e. i, ii, and iii.

____ 77. The Fed decreases the quantity of money to counteract
- a. a recessionary gap.
- b. a federal budget deficit.
- c. positive net exports.
- d. an inflationary gap.
- e. a rise in the unemployment rate.

____ 78. The Fed increases the quantity of money to counteract
- a. a recessionary gap.
- b. a federal budget surplus.
- c. negative net exports.
- d. an inflationary gap.
- e. inflation.

____ 79. During the Great Depression, real GDP decreased, unemployment soared, and the inflation rate was negative. Which would have been the appropriate federal government policy combination to improve economic performance?
- a. increase government expenditure, decrease taxes, increase the quantity of money
- b. increase government expenditure, decrease taxes, decrease the quantity of money
- c. decrease government expenditure, increase taxes, decrease the quantity of money
- d. do not change government expenditures or taxes , increase the quantity of money
- e. decrease government expenditures, increase taxes, do not change the quantity of money

____ 80. President Reagan often stated he preferred supply side policies. Which of the following federal government policies would be considered supply side?
- i. decrease the quantity of money
- ii. lower taxes
- iii. lower the interest rate.

- a. i only.
- b. ii only.
- c. iii only.
- d. i and iii.
- e. i, ii, and iii.