ECO 120: Global Macroeconomics **Name: (5 points)** ____________________
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Spring 2022
Practice Exam 3

Multiple-choice questions: 2 points each. Choose the best response to each prompt.

1. Suppose when consumers receive an additional \$100 of income, on average they increase their spending by \$85. What is the marginal propensity to save?

   (a) \$15

   (b) 0.15

   (c) 0.85

   (d) \$100

2. Which of the following leads to a higher expenditure multiplier effect?

   (a) Increase in the marginal propensity to import

   (b) Increase in aggregate supply

   (c) Decrease in the marginal propensity to save

   (d) Decrease in the marginal propensity to consumer

3. When consumers decide to spend more of their additional income on imports, what happens to the expenditure multiplier?

   (a) Multiplier decreases

   (b) Multiplier increases

   (c) Multiplier stays the same because additional expenditure stays the same

   (d) The multiplier may increase or decrease

4. Suppose consumers expect higher income in the future? What would be the effect of the expectation on aggregate expenditure plans in the present period?

   (a) Increase in aggregate expenditure

   (b) No change in aggregate expenditure until income increases

   (c) Aggregate expenditure may increase or decrease.

   (d) Decrease in aggregate expenditure until income increases

5. Suppose a gloomy economic outlook causes businesses' investment spending to decrease by \$150bn. Which of the following is an accurate description of the expenditure multiplier effect?

   (a) In the short-run, real GDP will decrease by more than \$150bn

   (b) In the long-run, real GDP will decrease by more than \$150bn.

   (c) In the short-run, real GDP will decrease by less than \$150bn

   (d) Real GDP will not change until the long-run

6. Suppose interest rates decrease. Which of the following changes in expenditure plans are likely as a result?
   (a) Decrease in consumption
   (b) Increase in aggregate supply
   (c) Increase in consumption
   (d) Increase in saving

7. Suppose interest rates decrease. Which of the following changes in expenditure plans are likely as a result?
   (a) Decrease in real GDP
   (b) Decrease in savings
   (c) Decrease in consumption
   (d) Increase in investment spending

8. Suppose there is an unexpected decrease in business inventories. What will be the impact on inventory investment?
   (a) Inventory investment will only change when inventories are gone
   (b) Inventory investment spending decreases
   (c) Inventory investment may increase or decrease
   (d) Inventory investment spending increases

9. Which of the following leads to an increase in business inventories?
   (a) Unexpected decrease in sales
   (b) Increase in inflation
   (c) Unexpected drop in production
   (d) Unexpected increase in sales

10. Suppose when consumers receive $120 of additional income, consumption spending increases by $95 and import spending increases by $15. What is the expenditure multiplier?
    (a) 0.21
    (b) 1.11
    (c) 0.79
    (d) 3

11. Suppose when consumers increase the fraction of income that they save. What is the impact on the expenditure multiplier?
    (a) The expenditure multiplier decreases
    (b) The expenditure multiplier increases
    (c) The expenditure multiplier is unaffected
    (d) The expenditure multiplier increases, but only in the long-run

12. Suppose a war ends leading to a decrease in expenditures on military equipment and weapons. How does this affect government spending and aggregate demand?
    (a) Government spending decreases and aggregate demand shifts to the right.
    (b) Government spending decreases and aggregate demand shifts to the left.
    (c) Government spending increases and aggregate demand shifts to the left.
    (d) Government spending increases and aggregate demand shifts to the right.

13. Which of the following is upward sloping with respect to the aggregate price level?
    (a) Aggregate demand
    (b) Long-run aggregate supply
    (c) Short-run aggregate supply
    (d) Both short-run and long-run aggregate supply

14. Which of the following could lead to a rightward shift in the aggregate supply curve?
    (a) Increase in aggregate demand
    (b) Increase in energy prices
    (c) Decrease in wages
    (d) Increase in wages

15. Suppose consumers expect taxes to decrease in the future. Which of the following would happen in the present as a result?
    (a) Nothing
    (b) Aggregate demand shifts to the right.
    (c) Aggregate demand shifts to the left.
    (d) Aggregate supply shifts to the right.

16. Why does the short-run aggregate supply curve shift to the right in the long run, following a decrease in aggregate demand?

    (a) Workers and firms adjust their expectations of wages and prices upward and they accept lower wages and prices.

    (b) Workers and firms adjust their expectations of wages and prices upward and they push for higher wages and prices.

    (c) Workers and firms adjust their expectations of wages and prices downward and they accept lower wages and prices.

    (d) Workers and firms adjust their expectations of wages and prices downward and they push for higher wages and prices.

17. To stimulate the economy in 2020 in response to the COVID-19 health and economic crisis, Congress passed a stimulus package resulting in government spending increases and tax reductions for consumers. Which of the following should be the result?

    (a) Aggregate supply shifts to the right and real GDP decreases.

    (b) Aggregate demand shifts to the left and real GDP decreases.

    (c) Aggregate demand shifts to the right and real GDP increases.

    (d) Aggregate supply shifts to the right and real GDP increases.

18. Which of the following results in a rightward shift in real money demand?

    (a) Increase in income

    (b) Improvement in financial technology

    (c) Increase in interest rate

    (d) Increase in price level

19. Which of the following monetary policies lead to a decrease in the interest rate?

    (a) Increase in money supply

    (b) Decrease in taxes

    (c) Increase in government expenditures

    (d) Decrease in money demand

20. If the central bank wishes to decrease the price level, which monetary policy should it use?

    (a) Increase money supply

    (b) Increase taxes

    (c) Decrease taxes

    (d) Decrease money supply

21. Suppose the interest rate increases. Which of the following would be the effect on the market for final goods and services?

    (a) Consumption demand and investment demand both decrease, causing both the aggregate demand and aggregate supply curves to shift to the left.

    (b) Consumption demand and investment demand both increase, causing both the aggregate demand and aggregate supply curves to shift to the right.

    (c) Consumption demand and investment demand both decrease, causing the aggregate supply curve to shift to the left.

    (d) Consumption demand and investment demand both decrease, causing the aggregate demand curve to shift to the left.

22. Which of the following variables do not change in response to the interest rate?

    (a) Money demand

    (b) Money supply

    (c) Aggregate demand

    (d) Consumption demand

23. Suppose consumers decide to decrease their expenditures on imports. All other things remaining the same, what is the short-run impact on the market for final goods and services?

    (a) Price level decreases and real GDP decreases.

    (b) Price level increases and real GDP increases.

    (c) Price level increases and real GDP decreases.

    (d) Price level decreases and real GDP increases.

24. Suppose incomes decrease abroad leading to a decrease in sales abroad. All other things remaining the same, what is the impact on the market for final goods and services?

    (a) Exports decrease, aggregate supply decreases, and real GDP decreases

    (b) Imports decrease, aggregate demand decreases, and real GDP decreases

    (c) Exports decrease, aggregate demand decreases, and real GDP decreases

    (d) Exports increase, aggregate demand increases, and real GDP increases

25. Suppose the economy is at the long-run equilibrium when a drop in consumer confidence leads to a decrease in consumption demand. What are the short-run and long-run effects on real GDP?

    (a) Real GDP decreases in both the short-run and the long-run.

    (b) Real GDP decreases in the short-run and increases back to its previous level in the long-run.

    (c) Real GDP increases in the short-run but decreases in the long-run.

    (d) Real GDP increases in the short-run and increases back to its previous level in the long-run.

Short-answer problem-solving questions: 5 points each. Answer the questions in the space provided.

26. Suppose the marginal propensity to consume is 0.8 and the marginal propensity to import is 0.15. Suppose a drop in consumer confidence results in a decrease in consumer spending by \$220 billion. Compute the short-run impact on real GDP.

27. Suppose the marginal propensity to save is 0.15 and the marginal propensity to import is 0.20. Suppose an increase in incomes abroad results in an increase in demand for exports by \$50 billion. Compute the short-run impact on real GDP.

28. Suppose the economy is in recession, where real GDP is currently \$6.5 trillion and potential GDP is \$7 trillion. The government would like to pass a stimulus package that increases government spending in order to increase real GDP back to potential GDP. The marginal propensity to consume is 0.85 and the marginal propensity to import is 0.10. How much should the increase in government expenditures be?

29. Suppose the economy is at the long-run equilibrium when a change in exchange rates leads to an increase in imports. Describe and illustrate the ***short-run*** impact on equilibrium real GDP and price level.

30. Suppose the economy is at the long-run equilibrium when there is a disruption in global supply chains, making it difficult for producers to get parts and raw materials to produce products and offer services. Describe and illustrate the ***short-run*** impact on equilibrium real GDP and price level.

31. Suppose the economy is initially at the long-run equilibrium when there is a decrease in government expenditures. Describe and illustrate ***both*** the ***short-run and long-run*** effects on equilibrium real GDP and price level.

32. Suppose the economy is experiencing a recession. Suggest how the government might change in government spending to bring real GDP back to potential GDP. Describe and illustrate the short-run equilibrium impact real GDP, and price level.

33. Suppose the economy is initially at the long-run equilibrium when the Fed decides to decrease the money supply. Describe and illustrate the ***short-run*** effects on the equilibrium interest rate, real GDP, and price level.

34. Suppose the economy is experiencing inflation. Suggest a monetary policy to put downward pressure on the price level. Describe and illustrate the impact on the equilibrium quantity of money, interest rate, real GDP, and price level.