CHAPTER 8

1) The level of GDP, the overall price level, and the level of employment are influenced by events in this market:
a) The financial (money) markets.
b) The goods-and-services market.
c) The labor markets.
d) All of the above.

2) Aggregate output (Y) is the same as:
a) Aggregate quantity supplied.
b) Aggregate income.
c) The total quantity of goods and services produced in an economy in a given period.
d) All of the above.

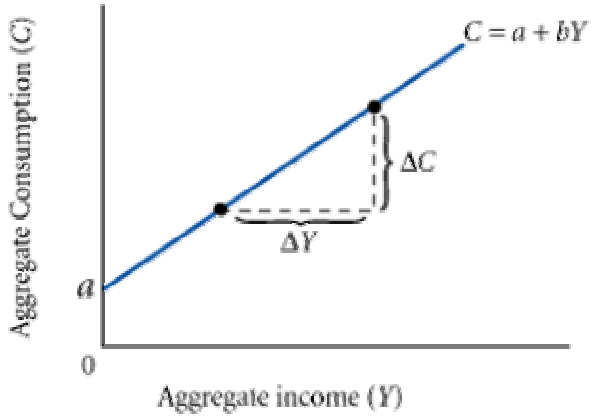
3) In economics, to think in real terms about output means to pay attention to:
a) The dollar value of output, or the dollars circulating in the economy.
b) Nominal output.
c) The quantities of goods and services produced.
d) All of the above.

4) Which of the following statements is correct?
a) Saving is a flow variable; savings is a stock variable.
b) Savings is the amount added to accumulated saving.
c) Out of disposable income, households consume, save, and pay taxes.
d) All of the above statements are correct.

5) To explain aggregate spending behavior, economists speculate that an increase in aggregate income in a given period will result in an increase in aggregate consumption in all of the following instances, except:
a. When households form positive expectations about the future.
b. When household wealth increases.
c. When interest rates rise.
d. None of the above. In all of the cases above, aggregate consumption will rise.

6) The relationship between consumption and income is called:
a. The paradox of thrift.
b. The income function.
c. The household wealth function.
d. The consumption function.

7) Refer to the figure below. The segment illustrated along the line between the two points is an explanation of:



a) How consumption could possibly decrease with increases in the level of income.
b) The marginal propensity to save.
c) Why a portion of aggregate consumption does not depend on income.
d) The marginal propensity to consume.

8) When aggregate consumption is plotted along a straight line, C = a + bY, an increase in income results in an increase in consumption equal to:
a) b.
b) a + b.
c) a times ΔY.
d) b times ΔY.

9) The sum of the marginal propensity to consume and the marginal propensity to save equals:
a) One.
b) Aggregate consumption plus aggregate saving.
c) Zero.
d) Aggregate income.

10) Fill in the blanks. Where the consumption function is below the 45° line, consumption is _____ than income, and saving is _____.
a) more; positive
b) more; negative
c) less; positive
d) less; negative

11) Which of the following is considered investment?
a) The creation of capital stock.
b) Purchases by firms of new buildings and equipment and inventories.
c) The production of something that is used to create value in the future.
d) All of the above.

12) The reason why firms do not have complete control of investment focuses on:
   a) Changes in inventory.
   b) The fact that investment is a flow variable.
   c) Purchases of physical capital.
   d) Differences between planned consumption and actual consumption.

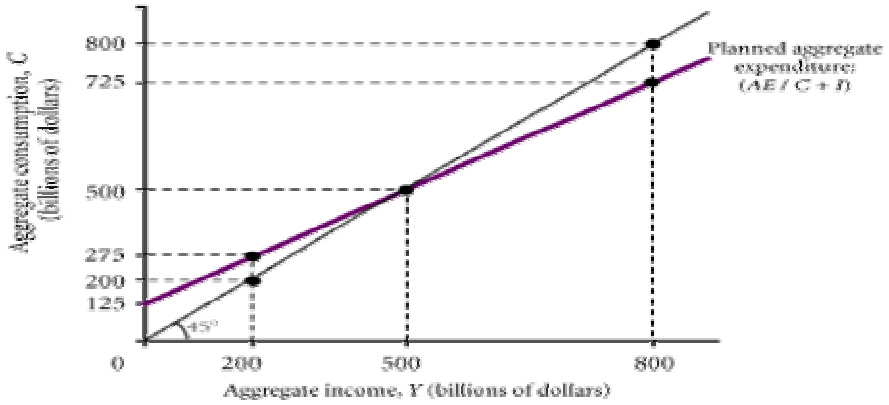
13) When inventories rise,
   a) Actual investment falls, while planned investment remains the same.
   b) Actual investment is less than planned investment.
   c) Both actual investment and planned investment rise.
   d) Actual investment is greater than planned investment.

14) In the simple model of aggregate expenditure, the planned investment function is:
   a) An upward-sloping line.
   b) An upward-sloping line.
   c) A horizontal line.
   d) An upward-sloping curve.

15) Which of the following conditions describes equilibrium in the goods market?
   a) Y = C + I
   b) AE ≡ C + I
   c) aggregate output ≡ Y
   d) All of the above describe equilibrium in the goods market.

16) When some unplanned inventory investment exists, which of the following is true?
   a) Y < C + I
   b) Y = C + I.
   c) Y > C + I
   d) AE ≡ C + I.

17) Refer to the figure below. When aggregate output equals $800 billion, which of the following happens?

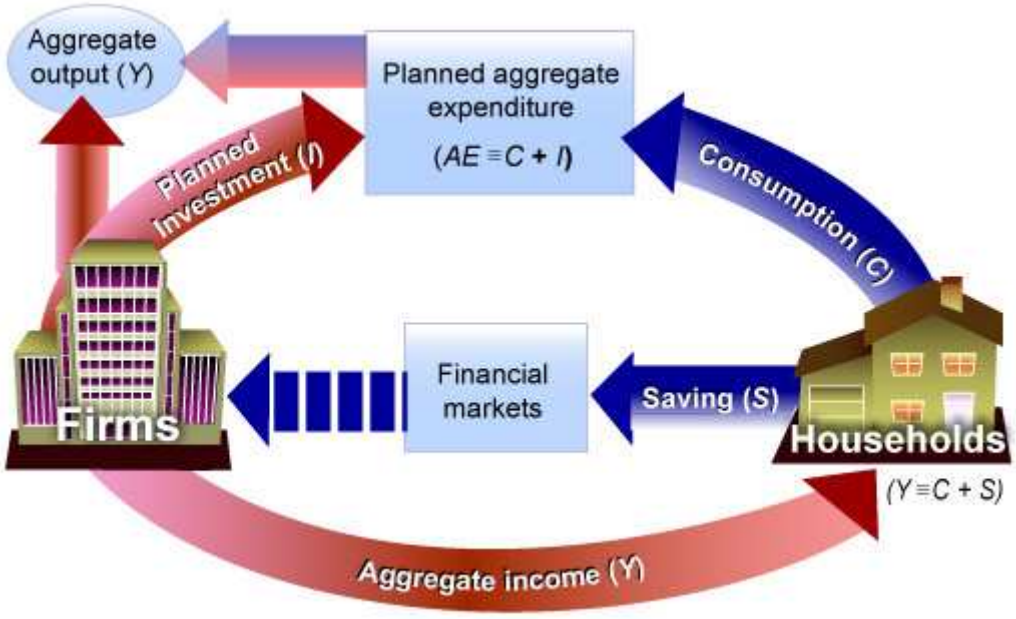


   a) Unplanned inventory is falling, and output will tend to fall.
   b) Unplanned inventory is falling, and output will tend to rise.
   c) Unplanned inventory is rising, and output will tend to fall.
   d) Unplanned inventory is rising, and output will tend to rise.

18) Consider a closed economy without government, where the consumption function is C = 100 + .8Y, and planned investment is I = 50. At what value of output is Y = C + I?

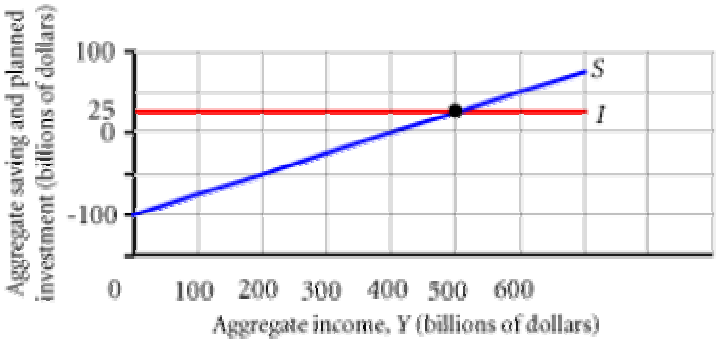
a) 500.
b) 750.
c) 187.5
d) 150.

19) Refer to the figure below. Which of the flows in the figure is a leakage?



a) Aggregate output (Y).
b) Saving (S).
c) Consumption (C).
d) Planned investment (I).

20) Refer to the figure below. At what level of output will firms respond to unplanned inventory reductions by increasing output?

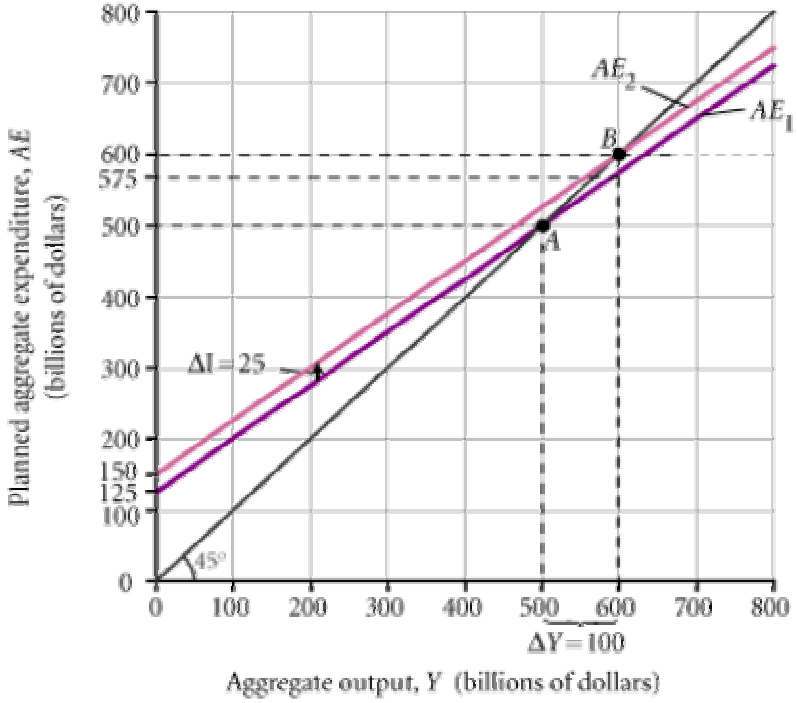


a) When the level of output is exactly 500.
b) At levels of output above 500.
c) At levels of output below 500.
d) Anywhere throughout the entire range of output.

21) The multiplier autonomous planned investment shows:

a) The change in equilibrium output given an initial change in planned investment.
b) Why planned investment is one of those variables that does not change in response to changes in the economy.
c) The ratio of the change in investment to a change in autonomous planned investment.
d) How planned investment changes by a multiple of a change in government spending.

22) Refer to the figure below. In this example, the size of the multiplier equals:



a) 1.33
b) 4
c) 100.
d) 25

23) In each round of the multiplier process in our simple, close economy without government, successive increases in income become:

a) larger and larger.
b) smaller and smaller.
c) smaller, then larger.
d) larger, then smaller.

24) In our simple economy (Y = C + I), the size of the multiplier depends on:

a) The marginal propensity to consume.
b) The magnitude of changes in aggregate output (income).
c) Aggregate expenditure.
d) The magnitude of changes in an autonomous variable.

25) In our simple economy (Y = C + I), how will equilibrium be restored after an increase in planned investment (I)?

a) Equilibrium will be restored once consumption stops rising.
b) Equilibrium will be restored only when saving has increased by exactly the amount of the initial increase in I.
c) Equilibrium will be restored only when the marginal propensity to save becomes zero.
d) Equilibrium will be restored only when inventory adjustments are made.

26) In our simple economy (Y = C + I), when investment rises, equilibrium income will change by:

a) $\frac{\Delta S}{\Delta Y}$
b) $\Delta I \times \frac{\Delta S}{\Delta Y}$
c) $\frac{1}{MPS}$
d) $\Delta I \times \frac{1}{MPS}$

27) In our simple economy (Y = C + I), which of the following is the expression for the multiplier?

a) $\frac{1}{1 - MPC}$
b) $\frac{\Delta S}{\Delta Y}$
c) $\Delta I \times \frac{1}{MPS}$
d) $\Delta I \times \frac{\Delta S}{\Delta Y}$

28) The paradox of thrift explains how:

a) An increase in saving, which requires a decrease in consumption, may result in a decrease in income, and consequently no greater saving than before.
b) An increase in consumption leads to a decrease in saving, an increase in income, and even greater saving than anticipated.
c) An increase in saving may increase income but not consumption.
d) An increase in investment can compensate for a decrease in saving; thus, with higher investment, it is possible to achieve a higher level of income with a higher level of saving.

29) In reality, the size of the multiplier in the U.S. economy is 1.4, which means that:
a) Each dollar of additional income increases consumption and saving by an additional 1.4 dollars.
b) Each dollar of additional income results in 1.4 additional dollars of consumption.
c) A sustained increase in autonomous spending of $10 billion can be expected to raise real GDP over time by $14 billion.
d) An increase in real GDP by $10 billion would increase autonomous spending by $14 billion.

30) Which of the following causes the multiplier to change?
a) Interest rates.
b) Taxes.
c) Imports.
d) All of the above.

31) Consumption is a highly volatile component of aggregate expenditure.
a) True
b) False

32) The marginal propensity to consume is the slope of the aggregate expenditure function (C + I).
a) True
b) False

33) An increase in income causes an upward shift of the consumption function.
a) True
b) False

34) The term autonomous planned investment means that changes in income have no impact on the level of planned investment expenditures.
a) True
b) False

35) The multiplier is a concept used to describe the impact of a change in autonomous expenditures on equilibrium income.
a) True
b) False

36) When aggregate expenditure is greater than aggregate income, unplanned investment is positive, and firms will plan to decrease production in the next period.
a) True
b) False

37) The sum of planned investment plus unplanned investment always equals saving.
a) True
b) False

38) The larger the marginal propensity to consume, the smaller the resulting multiplier.
a) True
b) False

39) Our analysis of production and spending assumes that firms do not have complete control over their investment decisions, but households have complete control over their consumption decisions.

a) True
b) False

40) Our analysis of production and spending assumes that firms have more control over inventory investment than over physical investment.

a) True
b) False

41) Fill in the blanks in the table below, and provide a graphical representation of consumption and saving.

a =	50
b =	0,75

Aggregate Income Y	*Consumption* C	*Saving* S
0		
50		
100		
150		
200		
250		
300		

42) Fill in the blanks in the table below.

a =	50			
b =	0.75			
I =	100			
Aggregate Income	*Consumption*	*Investment*	*Aggregate Expenditure*	*Saving*
Y	C	I	$C + I$	S
0				
200				
400				
600				
800				
1000				
1200				

43) Fill in the blanks in the table below to prove that actual investment (I_a) always equals saving (S).

a =	50		$I_a = I_p + I_u$			
c =	0.75					
I_p =	100					
Aggregate Income	*Consumption*	*Planned Investment*	*Planned Aggregate Expenditure*	*Unplanned Investment*	*Saving*	*Actual Investment*
Y	C	I_p	$C + I_p$	I_u	S	I_a
0						
200						
400						
600						
800						
1000						
1200						

44) Fill in the blanks in the table below, and provide a graphical description of the impact of higher investment.

a =	50	a =	50
b =	0.75	b =	0.75
I =	**100**	I' =	**200**
Aut. =		*Aut.* =	
Mult. =		*Mult.* =	
Y^* =		Y^* =	
Y	$C + I$		$C + I'$
0			
200			
400			
600			
800			
1000			
1200			