

## I. Multiple Choice

1. Which of the following is included in the formula for aggregate demand?
  - a) Wages
  - b) Investments
  - c) Inventories
  - d) Productivity
  
2. A decrease in interest rates will most likely:
  - a) Decrease consumer spending
  - b) Increase investment spending
  - c) Decrease government spending
  - d) Reduce net exports
  
3. Which event would shift AD to the right?
  - a) Increase in household debt
  - b) Higher taxes
  - c) Rise in foreign incomes
  - d) Appreciation of the domestic currency
  
4. The interest rate effect refers to:
  - a) Lower prices increasing exports
  - b) Higher prices reducing purchasing power
  - c) Higher prices increasing interest rates and reducing investment
  - d) Sticky wages affecting production
  
5. SRAS slopes upward primarily because:
  - a) Wages change instantly
  - b) Sticky input costs make production cheaper in the short run
  - c) Firms lose profit at high price levels
  - d) Technology improves
  
6. LRAS is vertical because:
  - a) Prices are flexible in the long run
  - b) AD no longer affects output
  - c) Input prices remain fixed
  - d) Government spending increases
  
7. A recessionary gap exists when:
  - a) AD intersects SRAS right of LRAS
  - b) AD intersects SRAS left of LRAS
  - c)  $AD = SRAS = LRAS$

- d) LRAS shifts left
8. A negative demand shock leads to:
- a) Higher real GDP
  - b) Higher unemployment
  - c) Higher inflation
  - d) Lower saving
9. A sudden oil price increase is an example of:
- a) Demand-side shock
  - b) Positive supply shock
  - c) Negative supply shock
  - d) Automatic stabilizer
10. Stagflation is caused by:
- a) Positive demand shock
  - b) Negative supply shock
  - c) Expansionary fiscal policy
  - d) Lower taxes
11. Expansionary fiscal policy includes:
- a) Raising taxes
  - b) Reducing government spending
  - c) Increasing interest rates
  - d) Cutting taxes
12. A progressive tax system acts as an automatic stabilizer because:
- a) Taxes rise in recessions
  - b) Taxes fall during expansions
  - c) Tax revenue increases long-term growth
  - d) Tax rates change automatically with income
13. The spending multiplier increases when:
- a) MPC increases
  - b) MPS increases
  - c) MPT increases
  - d) MPM increases
14. A decrease in government spending will:
- a) Shift AD right
  - b) Shift AD left
  - c) Shift SRAS right
  - d) Shift LRAS left

15. Higher corporate taxes will:
- a) Shift AD right
  - b) Shift SRAS right
  - c) Shift SRAS left
  - d) Shift LRAS right
16. Net exports increase when:
- a) Domestic currency appreciates
  - b) Foreign incomes fall
  - c) Domestic goods become more attractive
  - d) Imports rise
17. A positive supply shock causes:
- a) Higher inflation
  - b) Lower unemployment
  - c) Lower real GDP
  - d) Stagflation
18. Transfer payments act as stabilizers because:
- a) They increase during expansions
  - b) They decrease in recessions
  - c) They rise automatically when unemployment rises
  - d) They raise LRAS
19. The tax multiplier is always:
- a) Positive
  - b) Negative
  - c) Zero
  - d) Greater than the spending multiplier
20. Which factor increases LRAS?
- a) Higher income taxes
  - b) Population growth
  - c) Higher consumer debt
  - d) Higher interest rates
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## II. True / False

21. Aggregate demand includes exports but excludes imports.

22. Lower interest rates increase investment.
  23. Sticky wages adjust instantly in the short run.
  24. LRAS shifts right when technology improves.
  25. A negative demand shock causes inflation.
  26. Stagflation involves both high inflation and high unemployment.
  27. Transfer payments decrease automatically during recessions.
  28. A recessionary gap means the economy is producing above potential output.
  29. Expansionary fiscal policy increases AD.
  30. The spending multiplier is larger when MPC is high.
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### III. Fill in the Blank

31. Aggregate demand is calculated using the formula \_\_\_\_\_.
  32. Consumer spending increases when taxes \_\_\_\_\_.
  33. Sticky wages contribute to the upward slope of \_\_\_\_\_.
  34. LRAS represents the economy's \_\_\_\_\_ level of output.
  35. A sudden rise in oil prices is a \_\_\_\_\_ supply shock.
  36. Raising government spending causes AD to shift \_\_\_\_\_.
  37. The tax multiplier is always \_\_\_\_\_ in value.
  38. Automatic stabilizers require \_\_\_\_\_ new government action.
  39. A recessionary gap occurs when equilibrium output is \_\_\_\_\_ LRAS.
  40. The marginal propensity to consume plus the marginal propensity to save equals \_\_\_\_\_.
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## IV. Matching

Match each item in Column A with the correct item in Column B.

Concept	Definition
41. Real wealth effect	A. Welfare payments
42. Sticky input costs	B. Shifts SRAS left
43. LRAS	C. Sudden stimulus package
44. Transfer payments	D. Total exports minus import
45. Positive demand shock	E. Long-run potential output
46. MPS	F. Purchasing power changes when price level changes
47. Negative supply shock	G. Part of multiplier components
48. Fiscal policy	H. Leads to inflation & lower unemployment
49. Net exports	I. Production costs slow to adjust
50. Government spending shock	J. Taxes and spending

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## V. Short Answer

51. Define aggregate demand.
52. Explain why the AD curve slopes downward.
53. Identify three determinants of consumer spending.
54. Describe why SRAS slopes upward.
55. What factors shift SRAS?
56. What causes LRAS to shift?
57. Define a recessionary gap.
58. Explain the effect of a positive demand shock on unemployment.
59. What is stagflation?
60. Explain one cause of a negative supply shock.

61. Define fiscal policy.
  62. How can taxes be used as expansionary fiscal policy?
  63. What is the spending multiplier?
  64. Describe one purpose of automatic stabilizers.
  65. Explain how transfer payments stabilize the economy in a recession.
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## VI. Calculations

66. If  $MPC = 0.8$ , calculate the spending multiplier.
  67. If  $MPC = 0.75$ , calculate the tax multiplier.
  68. If  $MPS = 0.20$ ,  $MPT = 0.10$ , and  $MPM = 0.10$ , find the multiplier.
  69. If the government increases spending by \$50 billion and spending multiplier 4, how much does AD increase?
  70. If taxes rise by \$10 billion and the tax multiplier is  $-3$ , what is the total impact on GDP?
  71. If  $MPC = 0.6$ ,  $MPS = ?$ , find  $MPS$ .
  72. If  $MPM$  increases from 0.1 to 0.3, what happens to the multiplier?
  73. If  $MPC = 0.9$ , what is the spending multiplier?
  74. If the government cuts taxes by \$25 billion and  $MPC = 0.8$ , find change in GDP.
  75. If consumption rises by \$40 when income rises by \$50, calculate  $MPC$ .
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## VII. Graphing Practice

76. Draw an AD/AS diagram showing a recessionary gap.
77. Draw an AD/AS diagram showing an inflationary gap.

78. Show the effect of higher consumer confidence on the graph.
  79. Show a negative supply shock and label stagflation effects.
  80. Illustrate LRAS shifting right due to improved technology.
  81. Draw the result of expansionary fiscal policy on AD.
  82. Show how a sudden fall in interest rates affects AD.
  83. Draw the effect of a major oil price spike.
  84. Show the impact of increased taxes on AD.
  85. Draw how a positive supply shock affects price level and output.
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## **VIII. Long Answer Questions**

86. Explain how fiscal policy can be used to close a recessionary gap
87. Explain how automatic stabilizers reduce fluctuations in the business cycle
88. Explain how the multiplier effect influences the overall impact of fiscal policy
89. Evaluate the effectiveness of expansionary fiscal policy in increasing economic output
90. Evaluate the impact of supply-side shocks on inflation and unemployment