

## **Chapter 5—An Introduction to Macroeconomics**

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### **TRUE/FALSE**

1. The key characteristic of macroeconomics is the process of aggregation.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

2. Someone who studies the pricing policies of the Microsoft Corporation would be a microeconomist.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

3. Economic aggregates are not observable in the "real world."

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

4. Aggregation involves adding together different products and services.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

5. Abstract terms like "cost of living" and "price level" are meaningless to ordinary individuals.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

6. Macroeconomists pay little attention to the composition of aggregate output.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

7. During economic fluctuations, individual markets usually move in different directions.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Markets, market failure, and externalities  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

8. From 2000 to 2001, the U.S. economy's annual growth rate slowed down abruptly.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

9. Individuals live and work in both individual and aggregate economic entities.

ANS: T                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

10. Two of the most important macroeconomic issues are unemployment and inflation.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

11. An increase in aggregate demand will result in inflation.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Supply and Demand in Macroeconomics

12. Supply and demand provides the basic explanatory framework for constructing both microeconomic and macroeconomic models.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Supply and demand                      TOP: Supply and Demand in Macroeconomics

13. In macroeconomics, the vertical axis in a supply-demand model measures the price level rather than a particular product's price.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Supply and demand                      TOP: Supply and Demand in Macroeconomics

14. If aggregate demand keeps shifting rightward month after month and aggregate supply remains constant, the economy will experience a recession.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Supply and Demand in Macroeconomics

15. Gross Domestic Product represents the money value of all final goods and services produced in the domestic economy within the year.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

16. Nominal GDP includes the current value of services produced in the economy.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

17. Real GDP values current output of goods and services at their current prices.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

18. GDP in 2011 would not include the resale of a house built in 2000.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

19. Gross Domestic Product includes the sale of intermediate goods and services.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

20. If a woman marries her housekeeper, GDP would remain constant.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

21. Cars produced by General Motors in Mexico would be included in U.S. Gross Domestic Product.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

22. When the Art Institute of Chicago purchases a painting by Mary Cassatt that she produced in Paris in 1885, this would not be included in the U.S. GDP for 2011.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

23. Illegal gambling on the NCAA Final Four would be included in GDP.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

24. GDP consistently measures the output of goods and services in all countries.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

25. The existence of the "underground economy" causes measured GDP to overestimate actual output.

ANS: F                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

26. Gross Domestic Product accurately measures the environmental costs of producing all goods and services.
- ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product
27. Changes in nominal GDP always reflect changes in real output.
- ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product
28. Production for war and environmental clean-up services are not included in GDP.
- ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product
29. In the United States, GDP has grown slower than the population since 1870.
- ANS: F                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster
30. Business cycles are a persistent feature of the U.S. economy.
- ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster
31. Economic fluctuations in the United States have been less extreme since the 1950s.
- ANS: T                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster
32. In terms of macroeconomic conditions, the 1930s were the "good old days."
- ANS: F                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster
33. John Maynard Keynes wrote that economies can suffer recession or depression for many years if the government does not intervene.
- ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics  
 TOP: The Economy on a Roller Coaster
34. If aggregate demand shifts outward, the result will be inflation.
- ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Aggregate demand and aggregate supply  
 TOP: The Economy on a Roller Coaster

35. Stagflation is the simultaneous occurrence of inflation and high unemployment.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: The Economy on a Roller Coaster

36. In the early 1980s, the economy experienced high unemployment with falling inflation.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

37. One of the initial problems facing the newly elected President Clinton was a large budget deficit.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

38. Part of the good economic performance of the United States in the 1990s can be explained by a rightward-shifting aggregate supply curve.

ANS: T                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

39. Stabilization policy often faces a trade-off between inflation and unemployment.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Monetary and fiscal policy                      TOP: The Economy on a Roller Coaster

40. In 2001, the first year of the Bush administration, Americans learned that recessions were a thing of the past.

ANS: F                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

41. In response to the "Great Depression" the Obama administration responded with more tax cuts, increased federal spending, and aid to state and local governments.

ANS: T                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

## **MULTIPLE CHOICE**

1. A macroeconomist would concentrate on which of the following issues?
  - a. the price of pizzas
  - b. the profits of the IBM Corporation
  - c. the unemployment rate in Germany
  - d. the market for hot dogs

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

2. In economics, aggregation refers to
- collecting sample specimens for reclassification.
  - using small stones to pave an artistic walkway.
  - combining many markets into one overall economy.
  - using large computers to solve economic problems.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

3. Macroeconomists are distinguished from microeconomists because macroeconomists are more interested in
- inflation and unemployment than in individual markets.
  - large corporations rather than small businesses.
  - inflation in the United States rather than inflation in Costa Rica.
  - the demand for oil rather than the demand for corn.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

4. Macroeconomists think that
- most questions about individual markets are more important than the overall economy.
  - questions of overall unemployment are less important than the jobs of particular workers.
  - the details of resource allocation and individual market prices are less important than the amount of national output.
  - the causes of unemployment usually lie with the personalities of individual workers.
  - the price of particular products is more important than the overall price level.

ANS: C                      PTS: 1                      DIF: Difficult                      NAT: Reflective  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

5. An economist who studies the sales and profits of a large corporation would be classified as a(n)
- macroeconomist.
  - equity analyst.
  - stock broker.
  - microeconomist.
  - social economist.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

6. Combining various goods and services into a convenient grouping is called
- conglomeration.
  - blending.
  - congregation.

- d. agglomeration.
- e. aggregation.

ANS: E                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

7. Macroeconomics stresses
- a. resource allocation and income distribution.
  - b. inflation and unemployment.
  - c. resource allocation and inflation.
  - d. unemployment and income distribution.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

8. How do macroeconomists differ from microeconomists?
- a. the basic tools of analysis
  - b. the underlying principles
  - c. the use of abstractions and models
  - d. the problems studied
  - e. All of the above are correct.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

9. Microeconomics focuses on \_\_\_\_; macroeconomics concentrates on \_\_\_\_.
- a. the basic tools of analysis; the use of abstractions and models
  - b. the economies of various countries; the decisions of individual companies
  - c. the decisions of individual units; the behavior of entire economies
  - d. the economic aggregates; the decisions of individual units

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

10. Economists define an aggregate as
- a. a concrete object.
  - b. a specific principle.
  - c. a representative good or service.
  - d. a useful abstraction.
  - e. something immeasurable.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

11. If a macroeconomist aggregates many markets into one, then
- a. individual market differences are eliminated.

- b. one must not confuse ravioli and hot dogs.
- c. she is performing a meaningless exercise.
- d. differences between products must still be noted.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

12. China is the world's largest wheat producer. If China's domestic product grew by eleven percent in the previous year, it implies that
- a. production of wheat grew by more than eleven percent.
  - b. products other than wheat grew by less than eleven percent.
  - c. China's overall output grew by eleven percent.
  - d. production of wheat is declining in China.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

13. During economic fluctuations, markets tend to move
- a. together.
  - b. in random directions.
  - c. in opposite directions.
  - d. in many different directions.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

14. For a macroeconomist, the case for aggregation is based on two principles—1) the composition of demand and supply may not matter for some purposes, and 2)
- a. during fluctuations markets normally move together.
  - b. individual markets allocate resources efficiently.
  - c. inflation, unemployment, and growth never go together.
  - d. individual markets distribute income efficiently.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

15. During the first year of the Bush administration in 2001, the American economy
- a. increased its already rapid growth rate.
  - b. experienced high levels of inflation.
  - c. slowed in its rate of economic growth.
  - d. experienced a decrease in the rate of unemployment.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy  
TOP: Drawing a Line Between Macroeconomics and Microeconomics



16. It might be useful to think of macroeconomics as a study of \_\_\_\_ and microeconomics as a study of \_\_\_\_.
- a. big corporations, small businesses
  - b. oceans, fish
  - c. the long run, the short run
  - d. abstract, concrete
  - e. theory, reality

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

17. An example of an abstraction used in macroeconomics is
- a. the price level.
  - b. total costs.
  - c. the tax rate.
  - d. the treasury bill rate.
  - e. proprietor's income.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Drawing a Line Between Macroeconomics and Microeconomics

18. While their respective subject matters differ greatly, both microeconomists and macroeconomists rely on the same basic tools; that is, both rely on
- a. government contracts to promote research and publications.
  - b. demand-and-supply analysis.
  - c. the economic theory of John Maynard Keynes.
  - d. consumer protection laws and antitrust legislation.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: Supply and Demand in Macroeconomics

19. The horizontal axis on the aggregate demand-aggregate supply model measures
- a. the price of the specific product produced.
  - b. the level of total output.
  - c. the price level.
  - d. the level of employment.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Supply and Demand in Macroeconomics

20. The aggregate demand curve shows the quantity of domestic product
- a. produced at each possible price level.
  - b. demanded and produced at each possible price level.
  - c. that is exported at each possible price level.
  - d. demanded at each possible price level.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: Supply and Demand in Macroeconomics

21. The basic organizing framework for both microeconomic and macroeconomic models is
- purely competitive markets.
  - government planning of the economy.
  - demand and supply.
  - democratic socialism.
  - all of the above.

ANS: C

PTS: 1

DIF: Easy

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Supply and Demand in Macroeconomics

22. If aggregate demand shifts outward over a long period of time, with aggregate supply held constant, the economy should experience
- unemployment.
  - recession.
  - budget surpluses.
  - inflation.

ANS: D

PTS: 1

DIF: Difficult

NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: Supply and Demand in Macroeconomics

23. If aggregate demand shifts inward over a long period of time, with aggregate supply held constant, the economy should experience
- unemployment.
  - recession.
  - stagflation.
  - inflation.
  - budget surpluses.

ANS: B

PTS: 1

DIF: Difficult

NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: Supply and Demand in Macroeconomics

24. A recession is a period during which
- aggregate demand, production, and unemployment rises.
  - aggregate demand, production, and unemployment falls.
  - aggregate demand, production, and unemployment remain the same.
  - aggregate demand and production rises while unemployment remains the same.
  - aggregate demand and production falls while unemployment rises.

ANS: E

PTS: 1

DIF: Difficult

NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: Supply and Demand in Macroeconomics

25. The vertical axis of the aggregate demand-aggregate supply model measures the amount of
- total employment.
  - total final output.

- c. the price level.
- d. net exports.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Supply and Demand in Macroeconomics

26. In the aggregate demand-aggregate supply model, economic growth can be illustrated by an
- a. outward shift of the aggregate demand curve.
  - b. inward shift of the aggregate demand curve.
  - c. inward shift of the aggregate supply curve.
  - d. All of the above.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: Supply and Demand in Macroeconomics

27. The clearest sign of inflation would be a(n)
- a. increase in the price level.
  - b. increase in the quantity of total final output.
  - c. decrease in the quantity of total final output.
  - d. simultaneous increase in both output and prices.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Supply and demand                      TOP: Supply and Demand in Macroeconomics

28. Gross Domestic Product is best described as the
- a. measure of a nation's total economic welfare.
  - b. national income, including nonmarket income.
  - c. sum of money values of all final output produced in the domestic economy within the year.
  - d. national output minus environmental damage.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

29. Nominal GDP is
- a. also called real GDP.
  - b. a more accurate measure than real GDP.
  - c. real GDP adjusted for changes in the price level.
  - d. GDP measured in current prices.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

30. Real GDP
- a. is nominal GDP adjusted for changes in the price level.
  - b. is also called nominal GDP.
  - c. measures GDP minus depreciation of capital.
  - d. will always change when prices change.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

31. Which of the following is a true measure of national output?
- a. GDP at market price
  - b. Nominal GDP
  - c. GDP in current dollars
  - d. GDP in constant dollars

ANS: D

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

32. Gross Domestic Product is the
- a. least inclusive aggregate used to measure the economy.
  - b. total of goods and services desired by consumers.
  - c. most comprehensive measure of total output in the United States.
  - d. most accurate measure of the trade balance of the United States.

ANS: C

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

33. Gross Domestic Product is calculated by adding together
- a. the number of goods and services produced in the economy.
  - b. money value of final goods and services.
  - c. number of workers employed in national production.
  - d. all commodities but not services produced in the economy.

ANS: B

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

34. If the prices of all goods and services rise during the year,
- a. real GDP may fall.
  - b. nominal GDP must rise.
  - c. nominal GDP may increase.
  - d. real GDP must rise.

ANS: C

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

35. The clearest sign of economic growth is a(n)
- a. increase in nominal GDP.
  - b. increase in real GDP.
  - c. decrease in nominal GDP.
  - d. increase in nominal GDP.

ANS: B

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: Measuring the Economy

TOP: Gross Domestic Product

36. A good produced in 2009 and held in inventory until it is sold in 2010 would be included in which measure of GDP?
- a. Half the value in 2009 and half the value in 2010
  - b. In 2010 GDP

- c. In both 2009 and 2010 GDP
- d. In 2009 GDP

ANS: D                      PTS: 1                      DIF: Moderate           NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

37. A real estate salesperson sells a house in 2011 that was built in 2005. How does this transaction get counted in the GDP statistics?
- a. The price of the house and the real estate salesperson's commission are both included in 2011's GDP.
  - b. Neither the price of the house or the commission is included in 2011's GDP.
  - c. The real estate salesperson's commission but not the price of the house is included in 2011's GDP.
  - d. The price of the house would be included in both 2005's GDP and the GDP for 2011.

ANS: C                      PTS: 1                      DIF: Difficult           NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

38. In 2011, you buy a beautiful vintage 1965 Thunderbird convertible. This purchase would
- a. be included in the GDP for 2011.
  - b. not be included in the GDP for 2011.
  - c. be included in both the GDP for 1965 and 2011.
  - d. be in the GDP for 2011 at a depreciated value.

ANS: B                      PTS: 1                      DIF: Moderate           NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

39. Macroeconomic models use abstract concepts such as "price level" and "national income" that are calculated by combining many markets into one. This process is known as
- a. analysis and synthesis.
  - b. integration and derivation.
  - c. conceptualization.
  - d. aggregation.

ANS: D                      PTS: 1                      DIF: Moderate           NAT: Analytic  
LOC: Aggregate demand and aggregate supply                      TOP: Gross Domestic Product

40. You are a collector of antique coins. You purchase a silver dollar minted in 1898. Is this sale included in GDP for the current year?
- a. Yes, provided the coin is in mint condition.
  - b. No, it is not.
  - c. No, unless the coin has been in circulation.
  - d. Yes, it is.
  - e. Only if it is part of the current money supply.

ANS: B                      PTS: 1                      DIF: Moderate           NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

41. Aneta has owned an Italian sports car for several years and now she wants to sell it. She paid \$8,500 for it in 1993 and she has just sold it for \$39,000 in 2011. How is this sale included in the GDP for 2011?
- a. \$8,500 is included in 2011 GDP

- b. \$39,000 is included in 2011 GDP
- c. The increase in value of \$10,500 is included in 2011 GDP
- d. It is not included in 2011 GDP

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

42. Real GDP differs from nominal GDP in that nominal GDP measures
- a. output adjusted for inflation.
  - b. real output of goods and services.
  - c. output of goods and services at current prices.
  - d. real income adjusted for changes in the price level.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

43. Intermediate goods, like milk sold by a farmer to a supermarket, are
- a. included in GDP.
  - b. included in GDP at market value.
  - c. included if it is imported.
  - d. are not included in GDP.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

44. General Motors Corporation (a U.S.-based firm) produces a Saab vehicle in Sweden, and sells it in the United States. In which country's GDP is it included?
- a. Sweden and the United States
  - b. The United States because it was sold there
  - c. The United States because GM is a U.S. company
  - d. Sweden because it was produced there

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

45. If Honda (a Japan-based firm) produces a car in Ohio and exports it to Japan, in which country's GDP will the car be counted?
- a. Japan's, because Honda is a Japanese company
  - b. Japan's because that is where the car is purchased
  - c. The GDP of the United States because that is where it was built
  - d. Both Japan and the United States

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

46. Which of the following transactions would be included in GDP for 2011?
- a. On January 5, 2011, Chris Carter sold 100 shares of stock in IBM Corporation.
  - b. Bonita Delgado purchases a new 2011 Chevrolet on March 10, 2011.
  - c. Nadav Daniel buys a used desk from the "Struggling Students Used Furniture" store on May 9, 2011.
  - d. Levi Lathan purchases a 75-year-old penthouse on Lake Shore Drive in Chicago, Illinois, on

June 23, 2011.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

47. If hot dogs cost \$2 this year and \$3 next year, then 100 hotdogs will contribute
- \$200 to this year's nominal GDP and \$166 to next year's nominal GDP.
  - \$200 to this year's real GDP and \$300 to next year's real GDP.
  - the same dollar amount to each year's nominal GDP because hotdogs are intermediate goods.
  - \$200 to this year's nominal GDP and \$300 to next year's nominal GDP.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

48. E&S Cooling Co. installs air conditioning systems in new houses for homebuilders, and replacement systems for homeowners. Sales of which systems are included in this year's GDP?
- Sales of replacement systems
  - Sales of both systems
  - Sales of systems in new houses
  - Neither system would be included, because they are always intermediate goods.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

49. In periods of generally rising prices,
- real GDP will grow faster than nominal GDP.
  - nominal GDP will grow slower than real GDP.
  - real GDP will grow slower than nominal GDP.
  - real GDP and nominal GDP will grow at the same rate.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

50. Inflation refers to an increase in the
- price level.
  - rate of inflation.
  - total income.
  - real GDP.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

51. The major difference between nominal GDP and real GDP is that
- real GDP is the absolute value of goods and services and nominal GDP is a relative value.
  - real GDP refers to products made in the United States and nominal GDP refers to both exports and imports.
  - nominal GDP is the market value and real GDP has been adjusted for inflation.
  - real GDP is a relative value and nominal GDP is an absolute value.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: The Study of economics, and definitions in economics      TOP: Gross Domestic Product

52. Suppose that in 2011 you paid \$150,000 for a house that was built in 2005 and sold that year for \$210,000. The amount this transaction would add to the GDP in 2011 is
- \$0.
  - \$60,000.
  - \$210,000.
  - \$60,000

ANS: A      PTS: 1      DIF: Easy      NAT: Analytic  
LOC: Measuring the Economy      TOP: Gross Domestic Product

53. Which of the following would tend to increase the value of officially measured GDP?
- decriminalization of drugs such as marijuana and cocaine
  - decriminalization of prostitution
  - decriminalization of gambling on basketball and football
  - all of the above

ANS: D      PTS: 1      DIF: Moderate      NAT: Analytic  
LOC: Measuring the Economy      TOP: Gross Domestic Product

54. Gross Domestic Product is a monetary measure of
- total consumption in the economy.
  - the total value of all final goods and services.
  - total industrial output.
  - the total value of all foreign sales and purchases.

ANS: B      PTS: 1      DIF: Easy      NAT: Analytic  
LOC: The Study of economics, and definitions in economics      TOP: Gross Domestic Product

55. An example of an intermediate good would be a(n)
- new car.
  - used car.
  - new tire for a used car.
  - tire for a new car.
  - All of the above.

ANS: D      PTS: 1      DIF: Moderate      NAT: Analytic  
LOC: The Study of economics, and definitions in economics      TOP: Gross Domestic Product

56. Real GDP is another term for
- current dollar GDP.
  - actual GDP.
  - constant dollar GDP.
  - tangible GDP.

ANS: C      PTS: 1      DIF: Easy      NAT: Analytic  
LOC: The Study of economics, and definitions in economics      TOP: Gross Domestic Product

57. Nominal GDP is another term for
- current dollar GDP.



- b. constant dollar GDP.
- c. adjusted dollar GDP.
- d. relative value GDP.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

58. The definition of Gross Domestic Product is
- a. the total value of all sales in the economy.
  - b. the total value of production in the domestic economy plus the production of domestic firms in foreign countries.
  - c. the total value of all sales of final and intermediate goods in the domestic economy.
  - d. the total of the money values of all final goods and services produced in the domestic economy within a specific time period.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

59. Does GDP for a particular year include items produced in a previous year?
- a. Nominal GDP will not and real GDP will
  - b. Real GDP will and nominal GDP will not
  - c. Yes for both nominal and real GDP
  - d. No for both nominal and real GDP

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

60. A product that is produced in 2010 and not sold until 2011 will be counted in the GDP for
- a. both 2010 and 2011.
  - b. neither 2010 nor 2011.
  - c. 2010.
  - d. 2011.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

61. Trish grows oregano in her backyard to use in her homemade pesto sauce. How is this gardening included in GDP?
- a. It is included in real GDP.
  - b. It is included in nominal GDP.
  - c. It is not included in GDP.
  - d. It is included as an intermediate good.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

62. Dissatisfaction with public school education has led many parents to try home schooling for their children. If parents cut back on their jobs outside the home in order to spend time teaching their children at home, how will this affect GDP?
- a. GDP will increase.
  - b. Real GDP will increase and nominal GDP will decrease.

- c. Both real and nominal GDP will increase.
- d. GDP will decrease.

ANS: D                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

63. Which of the following is counted in GDP?
- a. the cost of the reconstruction and cleanup following September 11, 2001.
  - b. the value of leisure time
  - c. the value of a househusband's work at home
  - d. the value of your do-it-yourself work

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

64. Which of the following is included in GDP?
- a. the value of illegally produced goods
  - b. the value of housework by a stay-at-home dad
  - c. the value of volunteer work done at a local homeless shelter
  - d. the cost of government-provided social services

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

65. In 2011, Richard buys a 2003 Chevrolet minivan from a neighbor. Will this be counted in the GDP for 2011?
- a. Yes
  - b. No
  - c. Yes, if sales tax is paid
  - d. No, because the purchase was from an individual not a dealer

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

66. Amazon.com, an Internet retailer of books, buys a shipment of economics textbooks from a publisher. Is this included in GDP?
- a. Yes
  - b. No
  - c. It depends on how the payment is made
  - d. Yes, in real but not nominal GDP
  - e. Yes, in nominal but not real GDP

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

67. In March 2011 many college students bet on the NCAA finals in dorm gambling pools. This is an example of
- a. real vs. nominal GDP.
  - b. the assumed value of household production.
  - c. underground economic activity.
  - d. the implicit value of leisure time.

e. a "bad" versus a "good."

ANS: C

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: Measuring the Economy

TOP: Gross Domestic Product

68. Mitsubishi Corporation of America builds a car in Normal, Illinois, and ships it to Japan for sale. In which country's GDP is this production included?

- a. Japan
- b. both Japan and the United States
- c. in Japan as retail value and the United States as wholesale value
- d. half the value in Japan and half in the United States
- e. the United States

ANS: E

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: Measuring the Economy

TOP: Gross Domestic Product

69. Gross Domestic Product is an economic aggregate that represents the

- a. potential output of a country.
- b. total product of a nation's economy.
- c. total income earned from all sales.
- d. total product that a country exports.

ANS: B

PTS: 1

DIF: Easy

NAT: Analytic

LOC: Measuring the Economy

TOP: Gross Domestic Product

70. Gross Domestic Product is a dollar measure of

- a. total gross investment in an economy.
- b. total industrial sales in a particular time period.
- c. the total physical product of the economy.
- d. the value of all final goods and services produced in one time period.

ANS: D

PTS: 1

DIF: Easy

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

71. Nominal GDP is calculated by using

- a. prices set in a base year.
- b. average prices in all major cities.
- c. current prices
- d. prices charged by initial producers.

ANS: C

PTS: 1

DIF: Easy

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: Gross Domestic Product

72. Phoebe and Rachel quit running in Central Park and join a health club to run on treadmills. This decision

- a. has no effect on GDP.
- b. increases GDP.
- c. decreases GDP.
- d. increases nominal but not real GDP.

ANS: B

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: Measuring the Economy

TOP: Gross Domestic Product

73. Poor Asian countries may have per-capita GDP's that may be less than \$250. Why is this somewhat misleading for comparative purposes?
- a. Most rich country GDP is nonmarket activity.
  - b. A significant amount of poor country GDP is nonmarket activity.
  - c. Poor countries do not use dollars.
  - d. Poor countries have few resources.

ANS: B                      PTS: 1                      DIF: Difficult                      NAT: Reflective  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

74. Is GDP an accurate measure of a country's well being?
- a. Yes, it is the best measure of national well being.
  - b. Yes, provided we use real GDP and not nominal GDP.
  - c. The answer is uncertain, depending on whether GDP is rising or falling.
  - d. No, it is not.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

75. The Italian government collects a smaller amount of the taxes it is owed than the U.S. government. Other things being equal,
- a. U.S. and Italian GDP should be equal.
  - b. U.S. GDP should be higher than Italian GDP.
  - c. U.S. GDP should be lower than Italian GDP.
  - d. U.S. residents are better off than Italian residents.

ANS: B                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

76. Growth in GDP systematically understates the growth in national well being because
- a. ecological costs are netted out of GDP.
  - b. "bads" as well as "goods" get included in GDP.
  - c. investment is not included in GDP.
  - d. as a country gets richer, leisure time increases.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

77. Consider the economic effects of the September 11, 2001 terrorist attacks. Which of the following statements is correct?
- a. Reconstruction would lead to an increase in GDP.
  - b. Increased government spending on relief efforts in the U.S. would decrease GDP.
  - c. Lost items and buildings would lead to a decrease in GDP.
  - d. U.S. well-being was improved, despite the loss in GDP.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

78. International per capita GDP comparisons are misleading when countries involved differ greatly in
- a. the type of economic system each country uses to solve its economic problem.

- b. the freedom of their election processes.
- c. the percentage of economic activity that is transacted in organized markets.
- d. the quantity of human and natural resources they possess.

ANS: C                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

79. Since countries differ in the amount of economic activity that is transacted in organized markets,
- a. some countries are more productive than others.
  - b. persons live better in some countries than others.
  - c. international comparisons of per capita GDP are often misleading.
  - d. comparisons between countries are totally impossible.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

80. "Underground" economic activity can best be described as
- a. the construction of subway transportation.
  - b. the building of foundation structures for skyscrapers.
  - c. the mining and oil industries.
  - d. barter or cash activity that is not reported as income.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics                      TOP: Gross Domestic Product

81. In her book on the American work week, economist Juliet Schorr argues that Americans work too much. Her argument may be interpreted as concluding that this behavior
- a. increases GDP but decreases well being.
  - b. increases GDP and increases well-being.
  - c. decreases GDP and decreases well being.
  - d. decreases GDP but increases well being.

ANS: A                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

82. In 2001 the United States and its NATO allies dropped millions of dollars' worth of bombs on Afghanistan. These bombs and the aircraft from which they were dropped
- a. were netted out of GDP.
  - b. increased GDP and increased personal welfare.
  - c. decreased GDP and decreased personal welfare.
  - d. were added to GDP.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: Gross Domestic Product

83. When people smoke cigarettes, their friends and family members may become sick. This affects GDP by
- a. reducing GDP by the amount of medical care needed.
  - b. reducing GDP by the cost of the cigarettes purchased.
  - c. increasing GDP by the cost of the medical care and the cost of the cigarettes purchased.
  - d. decreasing GDP by the cost of the medical care and increasing GDP by the cost of the cigarettes purchased.

ANS: C                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

84. Large sport utility vehicles (SUVs) add significantly to air pollution because they do not have to meet passenger auto emission standards. The purchase of an SUV
- adds less to GDP since the pollution costs are subtracted from GDP.
  - adds to nominal but not real GDP because of the pollution costs.
  - is a net loss to GDP because the pollution costs are so large.
  - increases GDP.

ANS: D                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

85. How does the calculation of GDP include the costs of natural resource depletion that occurs when output is produced?
- The value of resource depletion is added to GDP.
  - The cost of resource depletion is not measured in GDP.
  - The cost of resource depletion is added to real but not nominal GDP.
  - Resource depletion causes GDP to overstate well being.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: Gross Domestic Product

86. The Great Depression of the 1930s
- confirmed the value of a "hands off" policy for governments.
  - was exacerbated by an expansionary monetary policy.
  - was a worldwide event.
  - continued throughout the 1940s without any interruption.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

87. One major effect of the Great Depression was
- it reaffirmed everyone's faith that capitalism was a self-correcting system.
  - it encouraged voters to limit the role of government.
  - the creation of the rational expectations school of economic theory.
  - a decreased faith in the ability of economies to automatically correct major problems.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Markets, market failure, and externalities  
TOP: The Economy on a Roller Coaster

88. In the 1960s, U.S. economy experienced
- a substantial decline in real GDP but limited inflation.
  - a substantial decline in real GDP coupled with significant inflation.
  - substantial real GDP growth coupled with significant inflation.
  - substantial real GDP growth with limited inflation.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

89. In the past 100 years the U.S. economy has primarily experienced
- deflation.
  - unemployment.
  - inflation.
  - depression.

ANS: C

PTS: 1

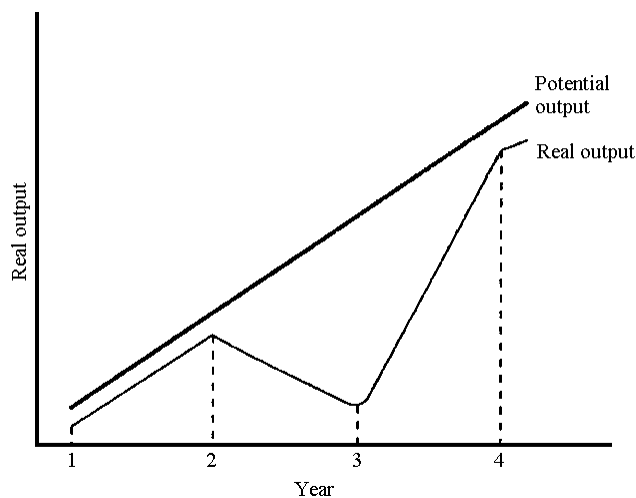
DIF: Easy

NAT: Analytic

LOC: Measuring the Economy

TOP: The Economy on a Roller Coaster

**Figure 5-1**



90. Figure 5-1 plots potential and real output for a hypothetical economy. Based on this graph, the recession occurred
- between years 1 and 2.
  - between years 2 and 3.
  - between years 3 and 4.
  - after year 4.

ANS: B

PTS: 1

DIF: Moderate

NAT: Analytic

LOC: Measuring the Economy

TOP: The Economy on a Roller Coaster

91. A period in which the price level is rising is experiencing
- inflation.
  - reflation.
  - deflation.
  - deconstruction.

ANS: A

PTS: 1

DIF: Easy

NAT: Analytic

LOC: The Study of economics, and definitions in economics

TOP: The Economy on a Roller Coaster

92. In the United States during the period from 1870 to 1940, the price level was most likely to
- fluctuate.
  - increase.

- c. decrease.
- d. trend generally upward.

ANS: A                      PTS: 1  
LOC: Measuring the Economy

DIF: Easy                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

93. In the period of U.S. economic history known as the Great Depression, the rate of inflation was generally
- a. trending upward.
  - b. positive.
  - c. uncertain.
  - d. negative.

ANS: D                      PTS: 1  
LOC: Measuring the Economy

DIF: Easy                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

94. Before the Great Depression of the 1930s, most economists believed that
- a. only active government policy could prevent recessions or inflation.
  - b. a capitalist economy had a natural tendency to cure recessions or inflation.
  - c. a capitalist economy had a natural tendency to inflation.
  - d. recessions and depressions were inevitable until the economy broke down completely.

ANS: B                      PTS: 1  
LOC: Measuring the Economy

DIF: Moderate                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

95. John Maynard Keynes wrote *The General Theory of Employment, Interest, and Money* (1936) to
- a. improve the gold supply balances of the British government.
  - b. prove that the punitive nature of the Treaty of Versailles would ultimately lead to recession in Europe.
  - c. prove that active government policy would produce unemployment and high rates of inflation.
  - d. demonstrate that pessimistic consumers and businesspersons could reduce their spending and condemn the economy to long-run stagnation.

ANS: D                      PTS: 1  
LOC: The Study of economics, and definitions in economics  
TOP: The Economy on a Roller Coaster

DIF: Difficult                      NAT: Analytic

96. During the Great Depression of the 1930s, how much did output fall between 1929 and 1933?
- a. 5 percent
  - b. 10 percent
  - c. 20 percent
  - d. 30 percent
  - e. 50 percent

ANS: D                      PTS: 1  
LOC: Measuring the Economy

DIF: Easy                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

97. In *The General Theory of Employment, Interest, and Money*, Keynes rejected the idea that
- a. a capitalist economy always gravitates toward high levels of employment.
  - b. budget deficits necessarily cause recessions and inflation.
  - c. the ultimate breakdown of the capitalist system is inevitable.



d. international trade always helps to achieve economic stability.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

98. According to Keynes, a pessimistic outlook causes consumers and businesspersons to \_\_\_\_, and a recession could occur.
- increase planned investment
  - decrease planned spending
  - increase exports
  - decrease imports
  - decrease saving

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

99. The Great Depression of the 1930s led to a revolution in macroeconomic thinking, following the work of
- Arthur Laffer.
  - Milton Friedman.
  - Adam Smith.
  - John Maynard Keynes.
  - David Ricardo.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

100. The most severe depression in the United States was the 30 percent decrease in real GDP that occurred between
- 1899 and 1913.
  - 1929 and 1933.
  - 1959 and 1963.
  - 1979 and 1983.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

101. Keynes' great book offered the promise of ending depressions through
- investors reacting to lower interest rates.
  - consumers taking over the ownership of factories.
  - government nationalizing key industries.
  - government influencing aggregate demand.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

102. Technically speaking, in what year did the "Great Recession" end?
- 1933

- b. 1935
- c. 2007
- d. 2009
- e. It had not ended as of 2011.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: The Economy on a Roller Coaster

103. The Great Depression ended in the United States when
- a. the New Deal reforms were initiated by President Roosevelt.
  - b. deficit spending ended in 1937.
  - c. the United States returned to the gold standard in 1940.
  - d. the United States began to mobilize for war in the early 1940s.
  - e. the German economy suffered hyperinflation in the 1920s.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

104. Which of the following would be counted in the U.S. GDP for 2011?
- a. a Ford Fiesta made in Mexico
  - b. the \$5,000 an investor used to purchase stock in Home Depot
  - c. Ford buying tires from Goodyear for new Ford Mustangs
  - d. none of the above

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: What Gets Counted in GDP

105. What was suggested by Keynes to move the economy out of a depressed state?
- a. The invisible hand
  - b. The price mechanism
  - c. Monetary and fiscal policy
  - d. Zero government intervention

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Monetary and fiscal policy                      TOP: The Economy on a Roller Coaster

106. The human consequences of the Great Depression included
- a. homeless families.
  - b. closed factories.
  - c. bankrupt farmers.
  - d. soup lines.
  - e. all of the above conditions.

ANS: E                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

107. The price controls on consumer goods during World War II led to
- a. permanent surpluses.
  - b. stable long-term prices.
  - c. a burst of inflation when they were ended.

d. increased production of consumer goods to satisfy demand.

ANS: C                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Supply and demand                      TOP: The Economy on a Roller Coaster

108. The 1960s are remembered by most economists as a period of
- a. very high rates of inflation.
  - b. very high rates of unemployment.
  - c. price controls and low inflation.
  - d. noninflationary growth.
  - e. all of the above.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

109. The successes of the 1960s were ascribed to the effects of
- a. classical policies from the 1800s.
  - b. classical policies from the 1930s.
  - c. classical policies from the 1950s.
  - d. Keynesian policies from the 1930s.
  - e. Keynesian policies from the 1950s.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: The Economy on a Roller Coaster

110. Usually, increased government spending for war increases inflationary pressures. The principal reason that inflation occurred during the Vietnam War and not during World War II was the existence, during World War II, of
- a. full employment.
  - b. government ownership of factories.
  - c. full production.
  - d. wage and price controls.
  - e. high levels of patriotism.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

111. In contrast to the typical Republican Party laissez-faire policies, President Richard Nixon in 1971 introduced
- a. mandatory drug testing of cabinet officers.
  - b. monetary targets for the Federal Reserve Board.
  - c. wage and price controls.
  - d. mandatory gold purchases by the U.S. Treasury.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Monetary and fiscal policy                      TOP: The Economy on a Roller Coaster

112. The international organization most responsible for rising prices during the 1970s was
- a. the WTO.
  - b. OPEC.

- c. the CIA.
- d. the World Bank.
- e. the Trilateral Commission.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

113. The recession of 1973-1975 was unusual in that both inflation and unemployment increased at the same time. This suggests that the primary cause of the recession was an
- a. inward shift of the aggregate demand curve.
  - b. outward shift of the aggregate supply curve.
  - c. inward shift of the aggregate supply curve.
  - d. outward shift of the aggregate demand curve.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Aggregate demand and aggregate supply  
 TOP: The Economy on a Roller Coaster

114. The movements of real GDP and inflation during the 1973-1975 recession can be best explained by a
- a. rightward shift of the aggregate demand curve.
  - b. leftward shift of the aggregate demand curve.
  - c. rightward shift of the aggregate supply curve.
  - d. leftward shift of the aggregate supply curve.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Aggregate demand and aggregate supply  
 TOP: The Economy on a Roller Coaster

115. The period of 1973 to 1980 can best be described as a time of
- a. deflation.
  - b. reflation.
  - c. unflation.
  - d. stagflation.
  - e. disflation.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

116. The term "stagflation" was invented in the 1970s to describe an economy experiencing both
- a. deflation and economic stagnation.
  - b. inflation and economic stagnation.
  - c. high inflation and high employment.
  - d. high inflation and high levels of economic growth.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics  
 TOP: The Economy on a Roller Coaster

117. The stagflation in the United States during the 1974-1975 period can be attributed to
- a. increases in real GDP due to high levels of defense spending.
  - b. tight monetary and fiscal policies of the Nixon-Ford administrations.

- c. rapid increases in petroleum prices, poor harvests, and the removal of wage and price controls.
- d. budget deficits by the federal government and increasing trade deficits by the United States.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

118. Stagflation can be defined as a combination of \_\_\_\_.

- a. economic migration and inflation
- b. economic aggregation and deflation
- c. economic stagnation and inflation
- d. economic aggregation and inflation

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: The Economy on a Roller Coaster

119. The significantly high rates of inflation in the 1970s occurred, in part,

- a. because of increased petroleum prices.
- b. due to high unemployment.
- c. despite falling gasoline prices.
- d. due to restrictive monetary policies.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

120. The Iranian Revolution in 1979 led to another interruption of oil supplies to the United States. This caused the reoccurrence of

- a. deflation.
- b. full-employment.
- c. trade surpluses.
- d. stagflation.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

121. The worst post-World War II recession in the United States occurred in

- a. 1964.
- b. 1973.
- c. 1981.
- d. 2007.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Measuring the Economy                      TOP: The Economy on a Roller Coaster

122. In 1981, the Reagan administration employed a policy that included tax \_\_\_\_ while at the same time the Federal Reserve's strategy was to combat \_\_\_\_.

- a. cuts; unemployment
- b. cuts; inflation

- c. hikes; unemployment
- d. hikes; inflation

ANS: B                      PTS: 1  
LOC: The role of government

DIF: Easy                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

123. The period from 1983 to 1990 was characterized by
- a. decreasing budget deficits and increasing trade surpluses.
  - b. persistently high inflation.
  - c. below average rates of real GDP growth.
  - d. consistent growth of real GDP and decreasing rates of inflation.

ANS: D                      PTS: 1  
LOC: Measuring the Economy

DIF: Moderate                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

124. The supply-side policies of the Reagan and Bush administrations led to high levels of
- a. budget surpluses.
  - b. unemployment.
  - c. inflation.
  - d. budget deficits.

ANS: D                      PTS: 1  
LOC: Measuring the Economy

DIF: Moderate                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

125. The election campaign of George Bush to succeed Ronald Reagan as president was
- a. hindered due to high levels of unemployment in 1988.
  - b. hindered by the increasing inflationary problems of the late 1980s.
  - c. helped by the budget surpluses generated in the last years of the Reagan administration.
  - d. helped by the continuing low levels of unemployment and inflation in 1988.

ANS: D                      PTS: 1  
LOC: Measuring the Economy

DIF: Difficult                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

126. The main reason that President Clinton was forced to revise his campaign promise to cut taxes was that, in 1993, he faced a large
- a. balance of payments surplus.
  - b. balance of payments deficit.
  - c. federal budget deficit.
  - d. federal budget surplus.

ANS: C                      PTS: 1  
LOC: Measuring the Economy

DIF: Moderate                      NAT: Analytic  
TOP: The Economy on a Roller Coaster

127. The macroeconomic conditions during the mid-1990s confounded many economists because of the simultaneous occurrence of
- a. low unemployment and decreasing inflation rates.
  - b. low unemployment and increasing budget deficits.
  - c. low unemployment and increasing interest rates.
  - d. high unemployment and increasing inflation rates.

ANS: A                      PTS: 1

DIF: Moderate                      NAT: Analytic

128. The first year of the Bush administration in 2001 could be represented as a(n)
- increase in the aggregate demand curve.
  - decrease in the aggregate demand curve.
  - increase in the aggregate supply curve.
  - decrease in the aggregate supply curve.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

129. The tax cut of 2001 turned out to be well-timed because it caused a
- rightward shift of the aggregate demand curve.
  - rightward shift of the aggregate supply curve.
  - leftward shift of the aggregate demand curve.
  - leftward shift of the aggregate supply curve.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Economy on a Roller Coaster

130. The name given to government programs implemented to prevent or shorten recessions and counteract inflation is
- supply-side economics.
  - contractionary policy.
  - monetary policy.
  - stabilization policy.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

131. Government policy to reduce unemployment and increase national output can be illustrated by an
- outward shift of the aggregate demand curve caused by an increase in government spending.
  - outward shift of the aggregate supply curve caused by a reduction in government spending.
  - inward shift of the aggregate demand curve caused by an increase in government spending.
  - inward shift of the aggregate supply curve caused by a reduction in government spending.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

132. The primary benefit to the macroeconomy of increasing government spending is a(n)
- decrease in the price level.
  - decrease in real GDP.
  - increase in the price level.
  - decrease in the unemployment rate.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: The role of government

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

133. If the government uses stabilization policies to reduce inflation, the economy may have to suffer
- higher rates of real GDP growth.
  - higher rates of unemployment.
  - lower rates of unemployment.
  - higher rates of price level growth.

ANS: B PTS: 1 DIF: Moderate NAT: Analytic

LOC: Monetary and fiscal policy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

134. Combating recession may require the government to
- decrease aggregate supply.
  - increase aggregate demand.
  - decrease aggregate demand.
  - decrease government spending.

ANS: B PTS: 1 DIF: Moderate NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

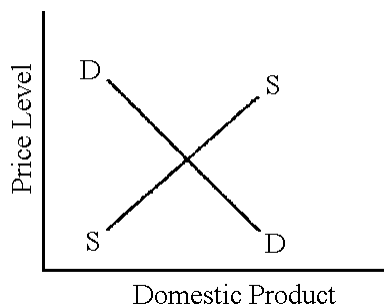
135. In response to significant economic problems, the Obama administration recommended
- more tax cuts.
  - increased government spending.
  - substantial aid to state and local governments.
  - all of the above

ANS: D PTS: 1 DIF: Moderate NAT: Analytic

LOC: Measuring the Economy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

**Figure 5-2**



136. In Figure 5-2, if the aggregate demand curve shifts outward over time, the economy will
- experience inflation.
  - see a sustained decrease in the price level.
  - experience a significant decrease in unemployment.
  - experience economic recession.

ANS: A PTS: 1 DIF: Moderate NAT: Analytic



LOC: Aggregate demand and aggregate supply  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

137. In Figure 5-2, an increase in government spending would cause
- an outward shift in the aggregate supply curve and an increase in the price level.
  - an outward shift in the aggregate demand curve and an increase in the price level.
  - an inward shift of the aggregate demand curve and an increase in the price level.
  - an inward shift of the aggregate demand curve and a decrease in the price level.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

138. In Figure 5-2, if the aggregate demand curve moves to the right less rapidly than the aggregate supply curve, then
- the price level should decline over time.
  - the price level should remain stable.
  - the price level will tend to increase.
  - the level of real GDP should decrease.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

139. The economy in the period 1950 to 1998 behaved differently than the economy in the 1870 to 1940 time period. Economists explain this difference
- in part because of the use of stabilization policy.
  - because of increases in U.S. population due to the "baby boom."
  - in part because of the globalization of the economy.
  - in part because of the use of competition policy.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
LOC: Measuring the Economy  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

140. To fight inflation, the government may
- decrease aggregate demand, which will also lead to lower unemployment rates.
  - increase aggregate demand, which will also lead to lower unemployment rates.
  - increase aggregate demand, which will also lead to higher unemployment rates.
  - decrease aggregate demand, which will also lead to higher unemployment rates.

ANS: D                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply  
TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

141. To fight recession, the government may
- decrease aggregate demand, which will also lead to lower unemployment rates.
  - increase aggregate demand, which will also lead to higher price levels.
  - increase aggregate demand, which will also lead to lower price levels.
  - decrease aggregate demand, which will also lead to higher unemployment rates.

ANS: B                      PTS: 1                      DIF: Difficult                      NAT: Analytic  
 LOC: Aggregate demand and aggregate supply  
 TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

142. Stabilization policy is the name given to government economic policies designed to
- stabilize the price level.
  - shorten and/or prevent recessions.
  - diminish unemployment.
  - All of the above are correct.

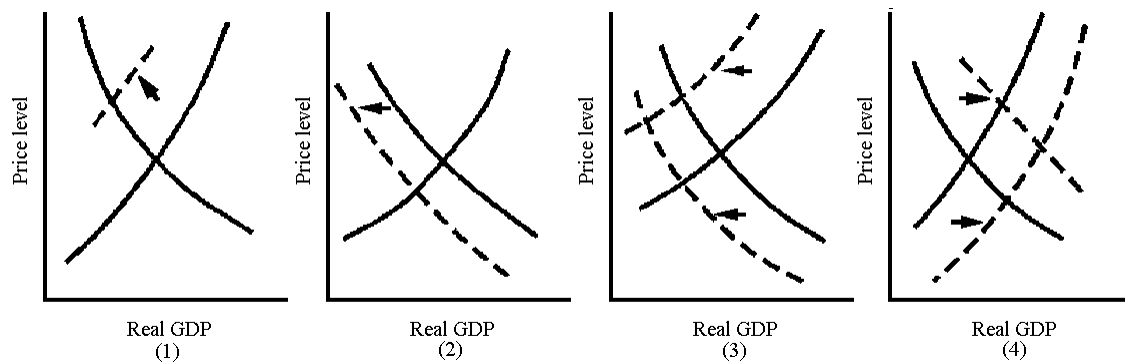
ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: Monetary and fiscal policy  
 TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

143. In contrast to the post-World War II period, before 1940 the government
- actively intervened in the economy for stabilization purposes.
  - used aggregate demand management to avoid recessions.
  - rarely intervened in the economy to influence inflation or unemployment rates.
  - used government ownership to guarantee full employment.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The role of government  
 TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

Aggregate demand and supply curves have been widely used to analyze the performance of the macroeconomy. Figure 5-3 shows four diagrams that represent different changes in the macroeconomy. Choose the diagram that best represents the situations described in the following questions.

**Figure 5-3**



144. Which graph in Figure 5-3 best represents the aggregate demand-induced Great Depression of the 1930s?
- 1
  - 2
  - 3
  - 4

ANS: B                      PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

145. Which graph in Figure 5-3 best represents the supply-side shock of the 1970s oil crisis?
- a. 1
  - b. 2
  - c. 3
  - d. 4

ANS: A                      PTS: 1                      DIF: Easy                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

146. Which graph in Figure 5-3 best represents the favorable macroeconomy of the late 1990s?
- a. 1
  - b. 2
  - c. 3
  - d. 4

ANS: D                      PTS: 1                      DIF: Easy                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

147. Which graph in Figure 5-3 best represents the economic conditions of the American economy in 2001?
- a. 1
  - b. 2
  - c. 3
  - d. 4

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

148. An increase in aggregate demand is most likely to result in
- a. inflation.
  - b. recession.
  - c. economic stagnation.
  - d. a decrease in real GDP.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

149. A rightward shift in the aggregate demand curve is most likely to result in
- a. inflation.
  - b. recession.
  - c. economic growth.
  - d. an increase in real GDP.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

150. Recessions

- a. almost never occur in the American economy.
- b. follow a regular and predictable cycle.
- c. are common features of the American economy.
- d. have been abolished by wise macroeconomic policy.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: Analytic

LOC: Measuring the Economy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

151. From the end of World War II until the present, the price level has

- a. slowly fallen over time.
- b. fluctuated around a downward trend.
- c. remained stable throughout the period.
- d. fluctuated around an upward trend.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Markets, market failure, and externalities

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

152. Business cycles in the United States after World War II have been

- a. more severe than before the war.
- b. less severe than before the war.
- c. the same as the pre-war cycles.
- d. easier to predict than the pre-war cycles.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Measuring the Economy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

153. You can generally distinguish an aggregate supply-caused recession from an aggregate demand-caused recession because

- a. real GDP will rise in an aggregate supply recession.
- b. the price level will fall in an aggregate supply recession.
- c. the price level will fall in an aggregate demand recession.
- d. real GDP will rise in an aggregate demand recession.

ANS: C                      PTS: 1                      DIF: Difficult                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

154. What makes the macroeconomic performance of the 1993 to 1998 period so unusual is the

- a. simultaneous occurrence of unemployment and inflation increases.
- b. simultaneous occurrence of real GDP decreases and inflation rate increases.
- c. occurrence of real GDP decreases while the unemployment rate increases.
- d. simultaneous occurrence of reduced unemployment rates and falling inflation rates.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Measuring the Economy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

155. According to the text, the government can use aggregate demand management policies to reduce unemployment rates. A byproduct of this policy will be
- an increase in the price level.
  - a decrease in real GDP.
  - a decrease in the price level.
  - an increase in the budget surplus.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

156. If the aggregate demand curve shifts to the left and the aggregate supply curve shifts to the right, the result will be a
- decrease in the level of output.
  - decrease in the price level.
  - higher price level.
  - higher unemployment rate.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

157. Technological change, such as the information technology revolution of the 1990s can shift the aggregate supply curve outward. If, at the same time, the government is decreasing spending, the most likely outcome of these two factors is a(n)
- increase in the price level.
  - decrease in the price level.
  - increase in real GDP.
  - decrease in real GDP.

ANS: B                      PTS: 1                      DIF: Difficult                      NAT: Analytic

LOC: Aggregate demand and aggregate supply

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

158. Since the end of World War II, the economy of the United States has been more influenced by stabilization policy. One of the undesirable side effects of this has been that the economy now has a greater tendency to suffer from
- more severe recessions and depressions.
  - higher levels of unemployment and lower rates of employment growth.
  - lower rates of growth in real and nominal GDP.
  - more persistent periods of inflation.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: Analytic

LOC: Monetary and fiscal policy

TOP: The Problem Of Macroeconomic Stabilization: A Sneak Preview

## ESSAY

- Define the following terms and explain their importance to the study of macroeconomics:

- a. aggregation
- b. recession
- c. gross domestic product
- d. final goods and services
- e. stabilization policy

ANS:

- a. *Aggregation* means combining many individual markets into one overall market. Economists use aggregation in studying macroeconomics. It is not usually used in microeconomics. One important issue is whether such a procedure can produce a meaningful number, i.e., can you add together dissimilar categories like apples and oranges.
- b. A *recession* is a period of time during which total production of goods and services in the economy declines. The technical definition of a recession is when real GDP falls for two successive calendar quarters. Recessions are a major problem in macroeconomic analysis that macroeconomists try to cure and prevent.
- c. *Gross domestic product* is the sum of the money value of all final goods and services produced in the domestic economy during a specific time period. GDP is the single most important statistic used to measure overall macroeconomic conditions.
- d. A *final good or service* is one purchased by the ultimate user. Final is used to contrast intermediate goods and services that are bought by another producer or distributor. The GDP includes only final goods and services and excludes intermediate goods and services.
- e. *Stabilization policy* is the name given to government programs designed to prevent or shorten recessions and to counteract inflation (that is, to stabilize prices). Macroeconomists who advise governments engage in stabilization policy. During presidential elections, alternative or competing stabilization policies of the candidates often are key issues in the campaign.

PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics

2. Discuss some of the fundamental differences between microeconomics and macroeconomics.

ANS:

Microeconomics studies the decisions of individuals and firms, the ways in which these decisions interact, and their influence on the allocation of a nation's resources and the distribution of income. Macroeconomics looks at how entire economies behave and studies the pressing social problems of economic growth, inflation, and unemployment. In short, whereas microeconomics focuses on the decisions of individual units, no matter how large, macroeconomics concentrates on the behavior of entire economies, no matter how small. Although they focus on different subjects, microeconomics and macroeconomics rely on virtually identical tools.

PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics

3. What is an aggregate? How is it used in macroeconomics? Give two examples of specific aggregates that are used in the study of macroeconomics.

ANS:

An "aggregate" is an abstraction that macroeconomists find convenient to use in describing some important feature of the overall economy. Aggregates are used in macroeconomics as simplifications to focus on the total of economic activity in contrast to the activity of one part of the economy. The aggregates described in the text were Gross Domestic Product (the sum of the total production of the nation's economy); aggregate demand (the sum of total demand for all the final goods and services); aggregate supply (the sum total of all the output offered for sale at various price levels); and the price level or price index (a number that serves as a measure of the average price of all final goods and services in the economy for some time period).

PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: Aggregate demand and aggregate supply

4. What are the two basic principles of aggregation?

ANS:

The two principles are:

1. Although the composition of demand and supply in the various markets may be terribly important for some purposes (such as how income is distributed and the diets people enjoy), it may be of little consequence for the economy-wide issues of growth, inflation, and unemployment—the issues that concern macroeconomists.
2. During economic fluctuations, markets tend to move up or down together.

PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics

5. What is Gross Domestic Product? What is included in this statistic? What is excluded? Give two examples of goods or services that are included in GDP and two examples of goods or services that are excluded.

ANS:

Gross Domestic Product is an aggregate and therefore an abstraction. It is the sum of the money values of all final goods and services produced in the domestic economy during a specific time period, usually a calendar quarter or year. GDP excludes goods and services produced in another quarter or year and it excludes intermediate goods and services. It includes final goods and services produced in the United States, regardless of the ownership of the facility producing the goods or services. It excludes goods and services produced outside the United States, even if they are produced by subsidiaries or branches of U.S. firms. GDP includes only goods and services that are bought and sold in organized markets. Examples of items included in GDP are anything newly produced in the specified time period. It is important that the item be produced in the period and not "new" items that may have been in storage or inventory for a long time before being sold. Items excluded from GDP are any intermediate good or service, any used good, any good or service produced outside the United States, and any good or service that does not pass through an organized market.

PTS: 1                      DIF: Easy                      NAT: Analytic  
LOC: The Study of economics, and definitions in economics

6. Which of the following items are included in GDP? For those items not included, explain why they are not included in GDP.
- a. Jane buys newly issued shares of stock in Macro.com, Inc.

- b. Ross buys a new pair of jeans at a local department store.
- c. Joey has his mustache trimmed at his hair salon.
- d. Rachel buys an antique chest at a resale shop.
- e. Monica makes her own pasta sauce in her apartment.
- f. Phoebe grows her own herbs on her apartment balcony.
- g. Michael travels to Austria and buys wine and cheese.

ANS:

- a. This is not included in GDP. No good or service has been produced.
- b. Included.
- c. Included.
- d. Not included. Produced in a previous year.
- e. Not included. Does not pass through an organized market; would be considered "household production."
- f. Not included. "Household production."
- g. Not included. The goods were produced in a foreign country.

PTS: 1                      DIF: Easy                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics

7. Define and distinguish between real and nominal GDP. Explain why the distinction is important to economists.

ANS:

Real GDP (or GDP in constant dollars) is a measure of the output of final goods and services produced in the domestic economy during a specific time period. It measures output in dollars of constant value. Therefore, it corrects for the effects of inflation. Real GDP will increase if there is an increase in the actual output of goods and services, such as more automobiles, more computers, more Internet access time, or more new economic textbooks. Nominal GDP (or GDP in current dollars, or money GDP) is a measure of output of final goods and services at current prices produced in the domestic economy during a specific time period. It measures final sales using dollars of current (non-inflation corrected) spending power. It can increase because of an increase in real output or because of an increase in the prices of final goods and services. Economists use real GDP as a more accurate measure of the true state of the economy, in that it tells us whether there are more or fewer actual final goods and services in the economy. Nominal GDP can be misleading in this regard. An example of this is the case of stagflation; rising prices, combined with falling output of final goods and services, may result in rising nominal GDP and falling real GDP. The decrease in real GDP is a better indicator of the sluggish economy.

PTS: 1                      DIF: Moderate                      NAT: Analytic  
 LOC: The Study of economics, and definitions in economics

8. What are intermediate goods? Why do economists exclude the value of intermediate goods while calculating national income?

ANS:



Intermediate goods are goods used as inputs in the production of other goods. There would be a problem of multiple counting if we include the value of both intermediate goods and final goods. For example, if chips sold to computer manufacturers were included in GDP, we would count the same chip when it was sold to the computer maker and then again as a component of the computer when it was sold to a consumer. Only final goods and services count in the GDP.

PTS: 1                      DIF: Moderate              NAT: Analytic  
LOC: The Study of economics, and definitions in economics

9. Compare and contrast the U.S. economic record prior to 1940 and after 1950. How do the two time periods differ? What best explains the differences according to a macroeconomist?

ANS:

The economy experienced business cycles of greater magnitude before 1940. Cycles after 1950 have been much less extreme. Before 1940, both inflation and deflation occurred. After 1950, inflation was a fairly constant condition and deflation never occurred over a prolonged period. Unemployment rates have been, on the average, much lower during the post-1950 time period. Most economists explain the superior economic performance of the post-1950 period to the use of Keynesian demand management stabilization policies that were implemented after World War II. The economy prior to 1940 could be described as "natural" or unmanaged. The economy after 1950 could be described as actively managed or stabilized.

PTS: 1                      DIF: Moderate              NAT: Analytic              LOC: Measuring the Economy

10. Why do price levels increase when government adopts fiscal or monetary policy to correct the economy when it faces a recession and high unemployment?

ANS:

Recession and unemployment are often caused by insufficient aggregate demand. Policy makers can use monetary and fiscal policy tools to stimulate aggregate demand during recession. The aggregate demand curve will shift to the right leading to an increase in general price levels.

PTS: 1                      DIF: Moderate              NAT: Analytic              LOC: Monetary and fiscal policy

11. Describe some of the steps used to combat inflation. What are their side-effects?

ANS:

Inflation is frequently caused by aggregate demand racing ahead too fast. Government policies that reduce demand can keep prices down and thereby reduce inflation. Some examples are reducing government spending or raising taxes, as done by the Clinton administration in the 1990s, or raising interest rates, which the Federal Reserve did in 2005-2006. Thus, fiscal or monetary policies that reduce aggregate demand can be effective anti-inflationary devices. But such policies also decrease real GDP and raise unemployment.

PTS: 1                      DIF: Moderate              NAT: Analytic              LOC: Monetary and fiscal policy

12. Contrast the economic performance of the American economy of 2001 with the economic performance of the 1996 to 2001 period. Use the appropriate aggregate demand and aggregate supply curves to distinguish the differing economic condition of the two periods.

ANS:

The economic performance of the 1996 to 2000 period could be characterized as a fortuitous combination of increasing aggregate demand at the same time the aggregate supply curve was shifting out as well. This created both economic growth and a fairly stable price level. The American economy experienced both low inflation and decreasing rates of unemployment. The year 2001 represents a classic aggregate demand-caused recession. A decrease in investment spending caused a decrease in aggregate demand. This caused a decrease in output and employment while putting downward pressure on prices. The American economy suffered the usual effects of recession, proving that the United States is not immune from the normal vicissitudes of the business cycle and that the U.S. had not entered a "new paradigm."

PTS: 1                      DIF: Difficult                      NAT: Reflective

LOC: Aggregate demand and aggregate supply