Principles of Macroeconomics
Homework Assignment 9
Answer Sheet

Name _______________________ Class Day/Time ____________________

Questions of this homework are in the next few pages. Please find the answer of the questions and fill in the blanks below. Turn in this answer sheet on the due date in class. Keep the remaining pages to study.

1. ________	**11. ________**
2. ________	**12. ________**
3. ________	**13. ________**
4. ________	**14. ________**
5. ________	**15. ________**
6. ________	**16. ________**
7. ________	**17. ________**
8. ________	**18. ________**
9. ________	**19. ________**
10. ________	**20. ________**

Principles of Macroeconomics
Homework 9

Name________________________
Multiple Choice

____ 1. Fiscal policy refers to the idea that aggregate demand is changed by changes in
   a. the money supply.
   b. trade policy.
   c. government spending and taxes.
   d. all of the above.

____ 2. An increase in government spending shifts
   a. aggregate demand left.
   b. aggregate demand right.
   c. aggregate supply right.
   d. neither aggregate demand nor aggregate supply.

____ 3. An economy is in full employment state. An enormous increase in government expenditures
   a. would raise the price level, but not real GDP at all.
   b. would raise real GDP, but not the price level.
   c. would raise the price level, and a relatively small amount of real GDP.
   d. would raise neither real GDP nor the price level.

____ 4. The government builds a bridge. The owner of the company that builds the bridge pays her workers. The workers increase their spending on consumer goods. The sales of the firms that sells those consumer goods increases. This type of effect on spending illustrates
   a. the wealth effect.
   b. the income effect.
   c. the substitution effect.
   d. the multiplier effect.

____ 5. The marginal propensity to consume (*MPC*) is defined as the fraction of
   a. extra income that a household either consumes or saves.
   b. extra income that a household consumes rather than saves.
   c. total income that a household consumes rather than saves.
   d. total income that a household either consumes or saves.

____ 6. Which of the following statements is true about Keynesian multiplier theory?
   a. If the government increases spending by $10 million, real GDP will eventually decrease by more than $10 million.
   b. If the government increases spending by $10 million, real GDP will eventually decrease by $10 million.
   c. If the government increases spending by $10 million, real GDP will eventually increase by $10 million.
   d. If the government increases spending by $10 million, real GDP will eventually increase by more than $10 million.

____ 7. If the *MPC* = 0.6, then the government spending multiplier is

a. 1.6667
b. 1.5
c. 0.6
d. 2.5
e. none of the above

____ 8. Expansionary fiscal policy includes

a. reduction of government spending and increase in tax.
b. reduction of both government spending and tax.
c. increase in government spending and tax cuts.
d. increase in both government spending and tax.

____ 9. Assume that the *MPC* is 0.7. An increase in government spending of $500 billion will

a. increase aggregate demand by $1666.67 billion.
b. increase aggregate demand by $120 billion.
c. increase aggregate demand by $500 billion.
d. increase aggregate demand by $333.33 billion.

____ 10. If taxes

a. increase, consumption increases, aggregate demand shifts right.
b. increase, consumption decreases, aggregate demand shifts left.
c. decrease, consumption increases, aggregate demand shifts left.
d. decrease, consumption decreases, aggregate demand shifts right.

____ 11. Suppose an economy is in recession with a negative GDP gap of $800 billion. If MPC is 0.9, how much should the government spend to eliminate the negative GDP gap?

a. $800 billion
b. $40 billion
c. $160 billion
d. $80 billion

____ 12. Which of the followings is not included in fiscal policy?

a. federal spending on security
b. households spending on consumption
c. Georgia state income tax
d. Coffee county sales tax

______ 13. The economy is operating at full employment. To maintain steady growth,

a. the government should increase spending and cut tax.
b. the government should decrease spending and cut tax.
c. the government should not do anything to this economy.
d. the government should increase both spending and tax.

______ 14. Suppose the Economic Advisor of the President believes in the Keynesian theory. Also suppose the economy is in recession. What fiscal policy will he/she recommend to the President?

a. cut tax and increase government spending
b. cut tax and cut government spending
c. raise tax and cut government spending
d. raise tax and government spending

______ 15. Suppose the households in an economy tend to spend $92 on consumption whenever they receive $100 increase in income. This economy's marginal propensity to consume is

a. 0.92
b. 0.8
c. 0.7
d. 0.08

______ 16. If the spending multiplier for an economy is 15, it means

a. every dollar the government spent would increase GDP by $10.
b. every dollar the government spent would increase GDP by $9.
c. every dollar the government spent would increase GDP by $1.5.
d. every dollar the government spent would increase GDP by $15.

______ 17. According to the Keynesian theory, if an economy's MPC is 0.6 and if there is a tax cut of $40 million, the real GDP in the economy would

a. decrease by $30 million.
b. increase by $30 million.
c. increase by $60 million.
d. not change.

______ 18. If an economy is overheated, which of the following fiscal policy should be used to subside the inflation?

a. Contractionary fiscal policy, such as cutting government spending and raise tax
b. Contractionary fiscal policy, such as increasing government spending and cutting tax
c. Supply-side policy, such as increasing government spending and cutting tax
d. Expansionary fiscal policy, such as increasing government spending and cutting tax

______19. Budget deficit occurs when

a. government tax revenue exceeds government expenditure.
b. government expenditures match government tax revenue.
c. government expenditures exceed government tax revenue.
d. none of the above.

______ 20. Which of the following is the Keynesian argument about fiscal policy?

a. Keynes suggests, the government cuts tax and raise government spending during recession, and therefore his theory is all about running deficit.
b. Keynes explains, the budget would be balanced in the long run because the budget deficit occurring during recession would be offset by the budget surplus during expansion.
c. Keynes suggests, the government cuts tax and raise government spending to stimulate the economy, and therefore his theory brings a country into national debt.
d. Keynes argues, during recession the government should still run a balanced budget.