

Practice AP Macroeconomics Test

1. Which of the following correctly describes the components of Aggregate Demand?
 - A. Consumption expenditures + Investment expenditures + Government expenditures + Exports + Imports
 - B. Consumption expenditures + Investment expenditures + Government expenditures + Exports - Imports
 - C. Consumption expenditures + Investment expenditures + Government expenditures - Exports - Imports
 - D. Consumption expenditures + Investment expenditures + Government expenditures + Savings + Exports - Imports
 - E. Consumption expenditures + Investment expenditures + Government expenditures + Business expenditures + Savings + Exports + Imports

2. Which of the following formulas is correctly stated?
 - A. Real interest rate = nominal interest rate + anticipated inflation.
 - B. Nominal interest rate = real interest rate + anticipated inflation.
 - C. Real interest rate = nominal interest rate + actual inflation.
 - D. Nominal interest rate = real interest rate + actual inflation.
 - E. Nominal interest rate = real interest rate - actual inflation.

3. Which of the following would not affect the size of real GDP?
 - A. Consumer purchase of a new car for personal use.
 - B. Government purchase of a new car for the military.
 - C. Business purchase of a new car for a delivery vehicle.
 - D. Consumer purchase of a rare renaissance painting.
 - E. Consumer purchase of a haircut.

4. If an autonomous increase in spending in an economy of 100 leads to an increase in real GDP of 500 then for that economy the marginal propensity to consume must have been:
 - A. 4/5
 - B. 5
 - C. 100
 - D. 400
 - E. 500

5. If the government increased spending by 10 and increased taxes by 10 to pay for the increased spending then which of the following combinations would correctly explain the effect on the budget and GDP?

	<u>Budget</u>	<u>GDP</u>
A.	unchanged	decrease
B.	surplus	decrease
C.	unchanged	no change
D.	surplus	increase
E.	unchanged	increase

 - A. A
 - B. B
 - C. C
 - D. D
 - E. E.

6. If a 100 deposit in a bank leads to a 1000 increase in the money supply, the reserve requirement must have been:
 - A. .10%
 - B. 10%
 - C. 100%
 - D. 1000%
 - E. cannot be determined from the information given.

7. Long run economic growth in a country would be encouraged through which of the following combinations of events?

	<u>Investment</u>	<u>interest rates</u>	<u>savings rate</u>
A.	high	high	high
B.	high	high	low
C.	high	low	low
D.	low	low	low
E.	high	low	high

 - A. A
 - B. B
 - C. C
 - D. D
 - E. E

8. Which of the following people would be considered structurally unemployed?
 - A. Unemployed auto assembly line factory worker during a recession.
 - B. Unemployed auto assembly line factory worker who was replaced with a robot.
 - C. An auto assembly line worker who quit her job to go back to school full-time to improve her job skills.
 - D. A high school student who mows lawns during the summer, but is out of work because it is winter.
 - E. A high school economics teacher who is not working during the summer, but plans to go back and teach in the fall.

9. Which combination of events described below would be the most expansionary for an economy, assuming that they all happened at the same time?

	<u>Taxes</u>	<u>Government spending</u>	<u>Net exports</u>	<u>reserve requirement</u>
A.	decrease	increase	increase	decrease
B.	increase	increase	increase	decrease
C.	decrease	increase	decrease	decrease
D.	decrease	decrease	decrease	decrease
E.	increase	decrease	decrease	increase

10. If an economy is suffering from inflation, what fiscal policy measure could be taken to help alleviate the problem?
 - A. Increase money supply
 - B. Increase government spending
 - C. Increase taxes
 - D. Increase the reserve requirement
 - E. Increase deficit spending

11. Which of the following would be an appropriate monetary policy measure to combat inflation?
- increase taxes
 - decrease taxes
 - sell bonds
 - buy bonds
 - lower the reserve requirement

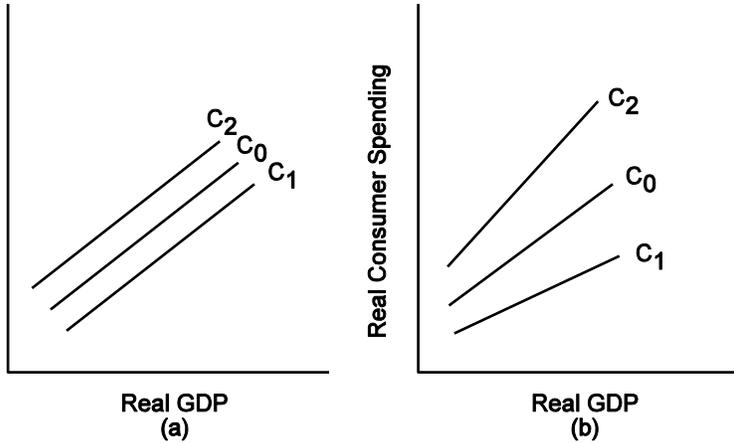


Figure 1

12. Based on Figure 1 a movement from C0 to C2, in both diagrams, would be consistent with which of the following?
- fixed tax cut and cut in tax rate
 - fixed tax increase and increase in tax rate
 - fixed tax cut and increase in tax rate
 - fixed tax increase and decrease in tax rate
 - none of the above correctly describe the movement from C0 to C2

13. Over the long run, the rate of growth of real wages is approximately equal to the rate of:
- inflation.
 - unemployment.
 - growth of labor productivity plus the rate of inflation.
 - growth of labor productivity minus the rate of inflation.
 - growth of labor productivity.

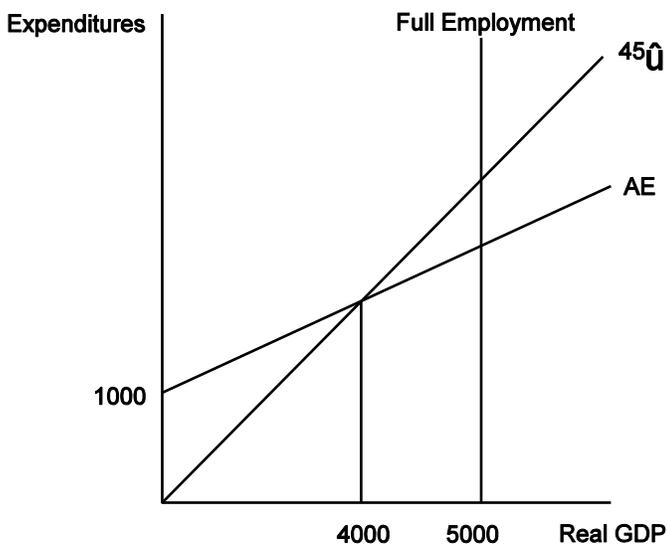


Figure 2

14. Based on Figure 2 the size of the simple multiplier is:
- one
 - two
 - three
 - four
 - five
15. Based on Figure 2 the economy shown is experiencing a/an:
- inflationary gap
 - recessionary gap
 - unemployment gap
 - stagflation
 - disinflation
16. Based on Figure 2 the MPC is:
- 0%
 - 25%
 - 50%
 - 75%
 - 100%
17. A production possibility curve is most closely related to which of the following?
- short run aggregate supply curve
 - long run aggregate supply curve
 - aggregate demand curve
 - aggregate expenditure diagram
 - Keynesian cross diagram
18. Which of the following combinations of policy moves would be recommended for an economy experiencing an annual increase in the inflation rate of 6% and an unemployment rate of 5%?
- increase government spending and increase the discount rate
 - decrease government spending and decrease the reserve requirement
 - increase income tax rates and sell bonds
 - decrease income tax rates and buy bonds
 - increase government transfer payments and increase the reserve requirement
19. The Keynesian monetary policy transmission mechanism would correctly be described in which of the following?

	<u>Money supply</u>	<u>Interest rate</u>	<u>Investment</u>	<u>GDP</u>
A.	increase	increase	increase	increase
B.	increase	increase	increase	decrease
C.	increase	decrease	increase	increase
D.	increase	decrease	decrease	decrease
E.	decrease	decrease	decrease	decrease

20. Crowding out describes a relationship among deficits, interest rates, and private spending. Which of the following describe that relationship?

	<u>Deficit</u>	<u>interest rate</u>	<u>private spending</u>
A.	increase	increase	increase
B.	decrease	decrease	decrease
C.	increase	increase	decrease
D.	increase	decrease	increase
E.	increase	decrease	decrease

21. Which of the following correctly describe the concept of the multiplier?

- I. It takes time for the multiplier to work. The impact of an independent change in investment during the first six months will be considerably smaller than the multiplier analysis implies.
 - II. When the marginal propensity to consume is 0.8, an independent increase in investment of \$10 billion will cause the aggregate income **of a fully employed economy** to rise to \$50 billion.
 - III. The multiplier effect may be even larger over time as its effect is supported by the interest rate and foreign purchases effect.
- A. I, II, and III are all true
 - B. I is true, II and III are false
 - C. I and II are true, III is false
 - D. I and III are true, II is false
 - E. I, II, and III are all false

22. "In the first half of 1973, prices rose at an annual rate of 8 percent and real output at 4.5 percent, while unemployment fell from 5.0 percent to 4.8 percent. From June 1972 to June 1973, the money supply increased 11 percent, while the U.S. government ran a deficit equal to 2 percent of GDP." Since unemployment was already at or near its natural rate during 1972-73,

- A. greater monetary expansion was necessary to stabilize prices.
- B. monetary and fiscal policy of the period added to the inflationary pressure already plaguing the economy.
- C. \$14 billion budget deficit probably caused unemployment to fall and real income to expand without adding to the inflation problem.
- D. monetary and fiscal policy of the period probably helped stabilize the growth rate of aggregate demand and promote price stability in the long run.
- E. Expansionary fiscal policy was necessary to stabilize prices

23. In a typical circular flow model describing the interaction of businesses and households, which of the following is/are true?

- I. Households buy factors of production and goods
- II. Firms buy factors of production and goods
- III. Households buy factors of production
- IV. Firms buy factors of production
- V. Firms buy goods
- VI. Households buy goods

- A. I only
- B. II only
- C. III and IV only
- D. IV and VI only
- E. V and VI only

24. If Americans suddenly decide to hold more cash for carrying on transactions and for precautionary reasons, which of the following is most likely to result?

- A. Increase in interest rates
- B. Decrease in interest rates
- C. Dollar depreciates in value
- D. Exports will rise
- E. Gross private domestic investment will rise

25. If the federal government and the Federal Reserve both attempt to contract the economy, which of the following sets correctly describes the probable results of these actions? (FP = fiscal policy, MP = monetary policy)

	<u>Interest rates</u>		<u>Price level</u>		<u>Output</u>	
	<u>FP</u>	<u>MP</u>	<u>FP</u>	<u>MP</u>	<u>FP</u>	<u>MP</u>
A.	increase	increase	increase	increase	increase	increase
B.	decrease	decrease	decrease	decrease	decrease	decrease
C.	increase	decrease	decrease	decrease	decrease	decrease
D.	decrease	increase	decrease	decrease	decrease	decrease
E.	decrease	increase	decrease	increase	decrease	increase

26. The Keynesian model would find monetary policy to be less effective if:

- A. Interest rates fell
- B. Interest rates rose
- C. Investment demand is elastic
- D. Investment demand is inelastic
- E. Fiscal policy remains neutral

27. Banks create money when they:

- A. collect interest on loans to the public
- B. buy government securities from the Federal Reserve
- C. allow customers to transfer money from time accounts to demand accounts
- D. keep required reserves as vault cash
- E. loan excess reserves to the public

28. Which of the following would be hurt the most by unanticipated inflation?

- A. borrowers with fixed rate loans
- B. borrowers with variable rate loans
- C. creditors
- D. both borrowers and creditors are hurt the same
- E. neither borrowers nor creditors are hurt by unanticipated inflation, they both benefit

29. A graphical representation with unemployment on the horizontal axis and inflation on the vertical axis is known as:
- Okun's law
 - Stagflation
 - Long run equilibrium
 - Natural rate of unemployment and inflation
 - Phillips curve

30. Stagflation could be caused by which of the following?
- Increase in aggregate supply
 - Decrease in aggregate supply
 - Increase in aggregate demand
 - Decrease in aggregate demand
 - Any of these has an equal chance of creating stagflation

31. If interest rates rise, growth will be slowed because;
- Firms will invest in more projects with future payoffs thus limiting growth.
 - Firms will invest in fewer projects with future payoffs thus limiting growth.
 - Firms will invest the same amount in projects with future payoffs at all interest levels thus leaving growth unaffected.
 - Firms will pay more in dividends and as a result retained earnings will fall.
 - Firms will pay less in dividends and as a result retained earnings will fall.

32. If inflation is 5% and nominal GDP grew by 4% then during the same period real GDP grew by:

- 9%
- 5%
- 4%
- 1%
- 1%

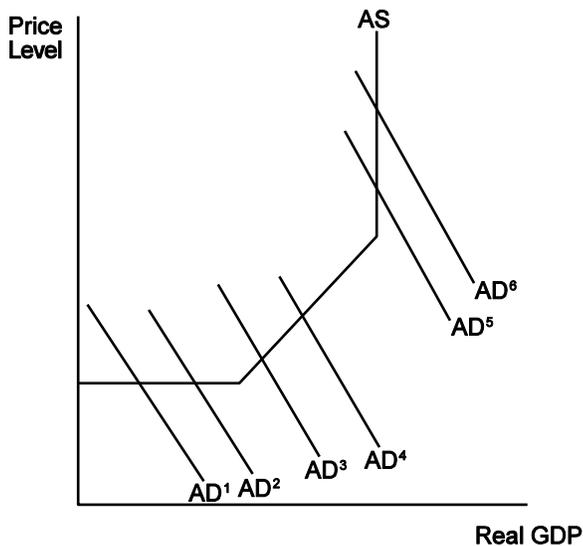


Figure 3

33. Based on Figure 3, a movement from _____ to _____ will result in a non-inflationary expansion of real output.

- AD1 to AD2
- AD2 to AD3
- AD3 to AD4
- AD4 to AD5
- AD5 to AD6

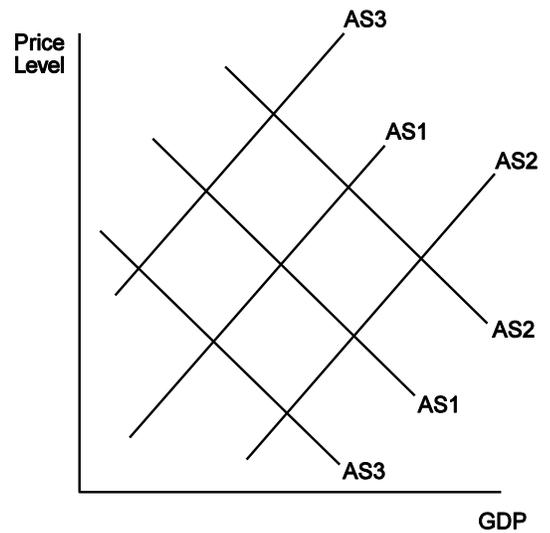


Figure 4

34. Beginning at the equilibrium position shown by AS1 and AD1, in Figure 4, which single movement could account for stagflation?

- AS1 to AS2
- AS1 to AS3
- AD1 to AD2
- AD1 to AD3
- None of the above would explain stagflation

35. Which of the following is a basic part of the Classical School of economic thought?

- Market systems may reach equilibrium at any level of output.
- Short-run inflation is unlikely to occur.
- Short-run unemployment is unlikely to occur.
- Prices and wages are flexible.
- Long-run equilibrium at full employment is unlikely to occur.

36. In the crude equation of exchange where $MV=PY$:

- Monetarists believe V is stable.
- Classical economists believe V is unstable.
- Keynesians believe V is stable.
- Monetarists believe that P is stable.
- Keynesians believe that P is stable

37. Which of the following is most likely to cause an increase in the long run aggregate supply curve?

- An increase in government spending.
- An increase in interest rates.
- An increase in taxes.
- An increase in literacy levels of the population.
- An increase in aggregate demand.

38. If an economy was operating at an equilibrium level of output at \$3,000 billion and full employment equilibrium was \$4,000 billion, with a marginal propensity to save of .2, a Keynesian economist would recommend:

- Increase government spending by \$1,000 billion
- Increase government spending by \$500 billion
- Increase government spending by \$250 billion
- Decrease taxes by \$1,000 billion
- Decrease taxes by \$250 billion

39. An adverse supply shock:
- Can be anticipated and decreases aggregate supply
 - Can be anticipated and increases aggregate supply
 - Cannot be anticipated but decreases aggregate supply
 - Cannot be anticipated but increases aggregate supply
 - Cannot be anticipated but decreases aggregate demand

40. All of the following are currently part of the United States money supply, EXCEPT:
- Coins
 - Currency
 - Checkable accounts
 - Credit cards
 - Demand deposits

41. If the Federal Reserve sells bonds in the open market, which of the following will result?
- Decreased demand for money and lower interest rates
 - Increased demand for money and higher interest rates
 - Increased money supply and lower interest rates
 - Decreased money supply and higher interest rates
 - Increased demand for and supply of money and an increase in interest rates

42. Based on the data from table below we can conclude that:

	Output Per Unit of Labor Input	
	England	Portugal
Cloth	20	24
Wine	2	12

- Portugal has a comparative advantage in the production of cloth and wine
 - England has a comparative advantage in the production of cloth and wine
 - Portugal has a comparative advantage in cloth and England has a comparative advantage in wine
 - England has a comparative advantage in cloth and Portugal has a comparative advantage in wine
 - England has an absolute advantage in the production of cloth and wine
43. On day 1, it cost \$.7354 U.S. to buy one Canadian dollar. How many Canadian dollars would \$1 U.S. buy?
- 1.36
 - 1.27
 - 1.11
 - 0.84
 - 0.73
44. On the next day (see Question 43) it cost \$.845 U.S. to buy one Canadian dollar. From this information we can conclude that:
- The U.S. dollar got stronger and U.S. exports will rise
 - The U.S. dollar got weaker and U.S. exports will rise
 - The U.S. dollar got stronger and U.S. exports will fall
 - The U.S. dollar got weaker and U.S. exports will fall
 - The U.S. dollar got stronger and U.S. exports will be unaffected

45. Suppose that the Fed decides to decrease the growth rate of the money supply in the U.S. What is most likely to happen to the U.S. trade deficit, and to GDP?
- The trade deficit will rise, GDP will rise.
 - The trade deficit will fall, GDP will rise.
 - The trade deficit will rise, GDP will fall.
 - The trade deficit will fall, GDP will fall.
 - The trade deficit will rise, GDP will be unaffected.

46. Gross domestic product (GDP)
- is the sum of all exchanges of goods and services during a period.
 - includes financial transactions such as the purchase of stocks or bonds traded during a period.
 - includes the purchases of goods at intermediate stages of production.
 - is the sum of the total spending on all final-user goods and services produced domestically during a period.
 - includes all goods and services exchanged during a period.

47. Which of the following is/are correct?

- (X) Your spouse cleans your house every Thursday.
 (Y) You sell your old economics book for \$25.
 (Z) Your economic textbook is revised and you buy a new edition.

- All three events increase GDP.
- Only (X) increases GDP
- Only (Y) increases GDP
- Only (Z) increases GDP
- (X) and (Y) increase GDP, (Z) reduces GDP

48. Which of the following best illustrates the difference between GDP and GNP?
- GDP measures the goods and services consumed by the citizens of a country, while GNP measures output exported to other countries.
 - GDP measures output produced by the citizens within a country, while GNP measures output produced by non-citizens within a country.
 - GDP measures the output produced by the citizens of a country, while GNP measures output produced within the borders of a country.
 - GDP measures the output produced within the borders of a country, while GNP measures output produced by the citizens of a country.
 - GDP measures goods produced by the citizens of a country, while GNP measures the output of goods and services produced by the citizens of a country.

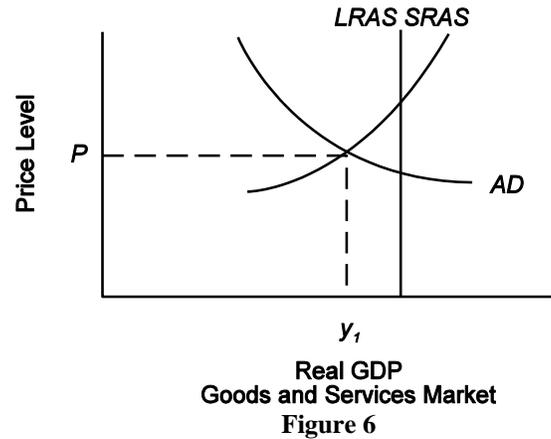
49. If decision makers underestimate inflation, the real wage will
- rise, increasing unemployment
 - rise, reducing unemployment
 - fall, increasing unemployment
 - fall, reducing unemployment
 - Is as likely to rise or fall making the effect on unemployment indeterminate

50. Which of the following will most likely occur during the expansionary phase of the business cycle?
- Real GDP rises and unemployment falls.
 - Real GDP rises and unemployment rises.
 - Real GDP declines and inflation rises.
 - Interest rates rise and the number of business failures rise.
 - Inflation rises and employment falls
51. Frictional unemployment
- would be eliminated if the economy were operating at full employment levels of GDP.
 - would be eliminated if the minimum wage were raise.
 - is the result of worker skills not matching the jobs available.
 - is zero when we have achieved the Natural rate of unemployment.
 - is present even when labor markets are working well.

FIGURE 5

Population	50 million
Number in the labor force	30 million
Number employed full time	20 million
Number unemployed	2 million

52. Based on the data in Figure 5, what is the labor force participation rate of the economy?
- 40 percent
 - 56 percent
 - 60 percent
 - 66.7 percent
 - 93.3 percent
53. Based on the data in Figure 5, what is the unemployment rate of the economy?
- 4 percent
 - 6.7 percent
 - 7.1 percent
 - 10.0 percent
 - 60 percent



54. Given the aggregate demand and aggregate supply conditions depicted in Figure 6, which of the following is most likely?
- an increase in resource prices, which will stimulate aggregate demand and direct the economy to potential capacity
 - a decrease in resource prices, which will increase costs and shift SRAS to the left, directing the economy to its potential capacity
 - lower resource prices, which will reduce costs and shift SRAS to the right until full-employment is achieved
 - a shift in LRAS to the left as the result of an increase in the expected inflation rate
 - a shift in LRAS to the right as a result of higher inflationary expectations for the future
55. If the consumer price index (CPI) were 131 at year-end 1999 and 125 at year-end 1998, then inflation during 1999 was
- zero; prices were stable during 1999
 - 4.8 percent
 - 6.0 percent
 - 31 percent
 - 125 percent
56. Which of the following best expresses the central idea of countercyclical fiscal policy?
- Planned deficits are experienced during economic booms and planned surpluses during economic recessions.
 - The balanced-budget approach is the proper criterion for determining annual budget policy.
 - Deficits are planned during economic recessions, and surpluses are utilized to restrain inflationary booms.
 - Deficits are planned during inflationary booms, and surpluses are utilized to restrain economic recessions.
 - Actual deficits should equal actual surpluses during a period of deflation.

57. Although the economy was in the Great Depression, the Hoover administration followed a fiscal policy of balancing the budget. A Keynesian would have found this policy
- A. inappropriate, because it probably would have inflationary consequences that might serve to further the people's reluctance to hold money.
 - B. appropriate, because it probably would have led to a significant increase in the money supply and thereby increased employment.
 - C. appropriate, because it probably would have stimulated economic activity and helped end the depression.
 - D. appropriate, because a balanced budget is always appropriate.
 - E. inappropriate, because it probably would further depress aggregate demand, economic activity, and employment.
58. If debit cards become more widely used by consumers and businesses, which of the following is most likely to happen?
- A. Currency holdings will remain the same, but M1 money supply will fall.
 - B. The amount of currency held by the public will increase.
 - C. Less money will be held as currency and more money will be held in bank accounts, which will increase the reserves of banks unless the Fed takes offsetting actions.
 - D. Less money will be held as currency and more money will be held in bank accounts, which will decrease the reserves of banks unless the Fed takes offsetting actions.
 - E. The money supply will be unaffected because debit card expenditures are considered the equivalent of cash.
59. International trade can be mutually advantageous because it
- A. allows each trading partner to specialize more fully in the production of those things that it does best.
 - B. reduces the competitiveness of domestic industries and thereby makes it easier for the domestic producers to raise prices.
 - C. permits the trading partners to expand their joint output.
 - D. All of the above are true.
 - E. Both A and C are true; B is false.
60. Compared to the no-trade situation, when a country imports a good
- A. domestic consumers gain, domestic producers lose, and the gains outweigh the losses.
 - B. domestic consumers lose, domestic producers gain, and the gains outweigh the losses.
 - C. domestic consumers gain, domestic producers lose, and the losses outweigh the gains.
 - D. domestic consumer gain, but domestic producers lose an equal amount.
 - E. Both domestic consumers and domestic producers lose.

Answers

1. B	11. C	21. B	31. B	41. D	51. E
2. B	12. A	22. B	32. E	42. D	52. C
3. D	13. E	23. D	33. A	43. A	53. B
4. A	14. D	24. A	34. B	44. B	54. C
5. E	15. B	25. D	35. D	45. C	55. B
6. A	16. D	26. D	36. A	46. D	56. C
7. E	17. B	27. E	37. D	47. D	57. E
8. B	18. C	28. C	38. E	48. D	58. C
9. A	19. C	29. E	39. C	49. D	59. E
10. C	20. C	30. B	40. D	50. A	60. A