1. With an MPS of .4, the MPC will be:
A) 1.0 minus .4.
B) .4 minus 1.0.
C) the reciprocal of the MPS.
D) .4.

2. As income increases consumption will:
A) be unaffected.
B) increase absolutely, but remain constant as a percentage of income.
C) increase absolutely, but decline as a percentage of income.
D) increase both absolutely and as a percentage of income.

3. The size of the MPC is assumed to be:
A) less than zero.
B) greater than one.
C) greater than zero, but less than one.
D) two or more.

4. The relationship between consumption and disposable income is such that:
A) an inverse and stable relationship exists between consumption and income.
B) a direct, but very volatile, relationship exists between consumption and income.
C) a direct and quite stable relationship exists between consumption and income.
D) the two are always equal.

5. The biggest component of Aggregate Expenditure is
A) Investment
B) Consumption
C) Government Spending
D) Net Export

6. If Ben's MPC is .80, this means that he will:
A) spend eight-tenths of any increase in his disposable income.
B) spend eight-tenths of any level of disposable income.
C) break even when his disposable income is $8,000.
D) save two-tenths of any level of disposable income.

7. (Advanced analysis) If the equation C = 20 + .6Y , where C is consumption and Y is disposable income, were graphed:

A) the vertical intercept would be +.6 and the slope would be +20.
B) it would reveal an inverse relationship between consumption and disposable income.
C) the vertical intercept would be negative, but consumption would increase as disposable income rises.
D) the vertical intercept would be +20 and the slope would be +.6.

8. If the NRU = 2%, the unemployment rate is 12%, actual GDP is $1 Trillion, and the MPC is 0.75, Investment should increase by _____ in order to reach potential GDP.

A) $200 Billion
B) $50 Billion
C) $1.2 Trillion
D) $7

9. If the NRU = 2%, the unemployment rate is 12%, actual GDP is $1 Trillion, and the MPC is 0.75, In order to reach potential GDP, Government should cut taxes by:

A) $200 Billion
B) $50 Billon
C) $66.67 Billion
D) $12

10. The most important determinant of consumption and saving is the:

A) level of bank credit.
B) level of income.
C) interest rate.
D) price level.

11. Assume a machine which has a useful life of only one year costs $2,000. Assume, also, that net of such operating costs as power, taxes, and so forth, the additional revenue from the output of this machine is expected to be $2,300. The expected rate of return on this machine is:

A) 7.5 percent.
B) 10 percent.
C) 15 percent.
D) 20 percent.

12. A decline in the real interest rate will:

A) increase the amount of investment spending.
B) shift the investment schedule downward.
C) shift the investment-demand curve to the right.
D) shift the investment-demand curve to the left.

13. If business taxes are reduced and the real interest rate increases:
A) consumption and saving will necessarily increase.
B) the level of investment spending might either increase or decrease.
C) the level of investment spending will necessarily increase.
D) the level of investment spending will necessarily decrease.

14. If the NRU = 2%, the unemployment rate is 12%, actual GDP is $1 Trillion, and the MPC is 0.75, In order to reach potential GDP and keep the it's budget balanced, the Government should tax people and increase Govt spending by:
A) $50 Billion
B) $1.2 Trillion
C) $20 Billion
D) $200 Billion

15. Assume a machine, which has a useful life of only one year costs $1,000. Assume, also, that net of such operating costs as power, taxes, and so forth, the additional revenue from the output of this machine is expected to be $1,500. The expected rate of return on this machine is:
A) 10%
B) 5%
C) 50%
D) 100%

16. If the nominal interest rate is 6% and prices rise by 8%. The real interest rate is:
A) 2%
B) Can't be determined
C) 0%
D) -2%

17. If the MPC = 0.95 in an economy, the multiplier equals
A) 95
B) 20
C) 5
D) 1/20

18. The multiplier is defined as:
A) 1 - MPS.
B) change in GDP × initial change in spending.
C) change in GDP/initial change in spending.
D) change in GDP - initial change in spending.

19. The multiplier can be calculated as:
A) 1/(MPS + MPC)
B) MPC/MPS
C) 1/(1 - MPC)
D) 1 - MPC = MPS

20. The multiplier:
A) varies directly with the slope of the investment-demand schedule.
B) will be greater, the smaller MPC.
C) will be greater, the smaller the MPS.
D) will be greater, the larger the MPS

21. Other things equal, if a change in the tastes of American consumers causes them to purchase more foreign goods at each level of U.S. GDP:
A) unemployment will decrease domestically.
B) U.S. GDP will fall.
C) inflation will occur domestically.
D) U.S. real GDP will rise.

22. When computing the GDP in an economy using the expenditure approach:
A) net exports may be either positive or negative.
B) imports will always exceed exports.
C) exports will always exceed imports.
D) exports and imports will be equal.

23. If the dollar appreciates relative to foreign currencies, we would expect:
A) the multiplier to decrease.
B) a country's exports and imports to both fall.
C) a country's net exports to rise.
D) a country's net exports to fall.

24. If a lump-sum income tax of $25 billion is levied and the MPS is 0.20, the:
A) saving will increase by $5 billion.
B) consumption decrease $25 billion.
C) consumption decrease by $20 billion.
D) consumption will increase by $25 billion.

25. Suppose the economy is operating at its full-employment-noninflationary GDP and the MPC is 0.75. The Federal government now finds that it must increase spending on military goods by $21 billion in response to a

deterioration in the international political situation. To sustain full-employment-noninflationary GDP government must:

A) reduce taxes by $28 billion.
B) reduce transfer payments by $21 billion.
C) increase taxes by $21 billion.
D) increase taxes by $28 billion.

26. A $1 increase in government spending on goods and services will have a greater impact on the equilibrium GDP than will a $1 decline in taxes because:

A) government spending is more employment-intensive than is either consumption or investment spending.
B) government spending increases the money supply and a tax reduction does not.
C) a portion of a tax cut will be saved.
D) taxes vary directly with income.

27. Which of the following is correct?

A) Government expenditures and taxes both increase GDP.
B) Government expenditures and taxes both decrease GDP.
C) Government expenditures increase, but taxes decrease, GDP.
D) Government expenditures decrease, but taxes increase, GDP.

28. If APC = .6 and MPC = .5, a simultaneous increase in both taxes and government spending of $20 will:

A) decrease GDP by $20.
B) decrease GDP by $40.
C) increase GDP by $20.
D) increase GDP by $40.

Answer key:

1. A 2.C 3.C 4.C 5.B 6.A 7.D 8.B 9.C 10.B 11.C 12.A
13. B 14.D 15. C. 16.D 17.B 18.C 19.C 20.C 21.B 22.A 23.D 24.C
25.D 26.C 27.C 28.C