

Name: _____ Date: _____

1. Short-run fluctuations in output and employment are called:
 - A) sectoral shifts.
 - B) the classical dichotomy.
 - C) business cycles.
 - D) productivity slowdowns.

2. A 5-percent reduction in the money supply will, according to most economists, reduce prices 5 percent:
 - A) in both the short and long runs.
 - B) in neither the short nor long run.
 - C) in the short run but lead to unemployment in the long run.
 - D) in the long run but lead to unemployment in the short run.

3. The aggregate demand curve is the _____ relationship between the quantity of output demanded and the _____.
 - A) positive; money supply
 - B) negative; money supply
 - C) positive; price level
 - D) negative; price level

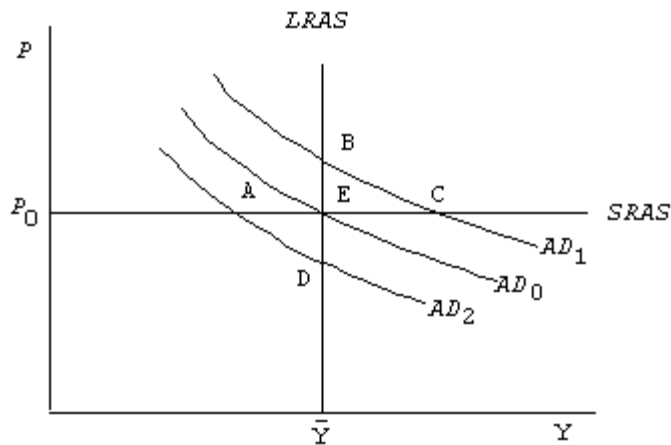
4. If an aggregate demand curve is drawn with real GDP (Y) along the horizontal axis and the price level (P) along the vertical axis, using the quantity theory of money as a theory of aggregate demand, this curve slopes _____ to the right and gets _____ as it moves further to the right.
 - A) downward; steeper
 - B) downward; flatter
 - C) upward; steeper
 - D) upward; flatter

5. Along an aggregate demand curve, which of the following are held constant?
 - A) real output and prices
 - B) nominal output and velocity
 - C) the money supply and real output
 - D) the money supply and velocity

6. According to the quantity theory of money, if output is higher, _____ real balances are required, and for fixed M this means _____ P .
- A) higher; lower
 - B) lower; higher
 - C) higher; higher
 - D) lower; lower
7. Aggregate supply is the relationship between the quantity of goods and services supplied and the:
- A) money supply.
 - B) unemployment rate.
 - C) interest rate.
 - D) price level.
8. A short-run aggregate supply curve shows fixed _____, and a long-run aggregate supply curve shows fixed _____.
- A) output; output
 - B) prices; prices
 - C) prices; output
 - D) output; prices
9. If the long-run aggregate supply curve is vertical, then changes in aggregate demand affect:
- A) neither prices nor level of output.
 - B) both prices and level of output.
 - C) level of output but not prices.
 - D) prices but not level of output.
10. If the short-run aggregate supply curve is horizontal, then the:
- A) classical dichotomy is satisfied.
 - B) money supply cannot affect prices in the short run.
 - C) money supply cannot affect output in the short run.
 - D) money supply is irrelevant in the short run.
11. Starting from long-run equilibrium, if the velocity of money increases (due to, for example, the invention of automatic teller machines) and no action is taken by the government:
- A) prices will rise both in the short run and the long run.
 - B) output will rise both in the short run and the long run.
 - C) prices will rise in the short run and output will rise in the long run.
 - D) output will rise in the short run and prices will rise in the long run.

12. Starting from long-run equilibrium, if the velocity of money increases (due to, for example, the invention of automatic teller machines), the Fed might be able to stabilize output by _____ the rate of growth of the money supply.
- A) permanently decreasing
 - B) permanently increasing
 - C) temporarily decreasing
 - D) temporarily increasing

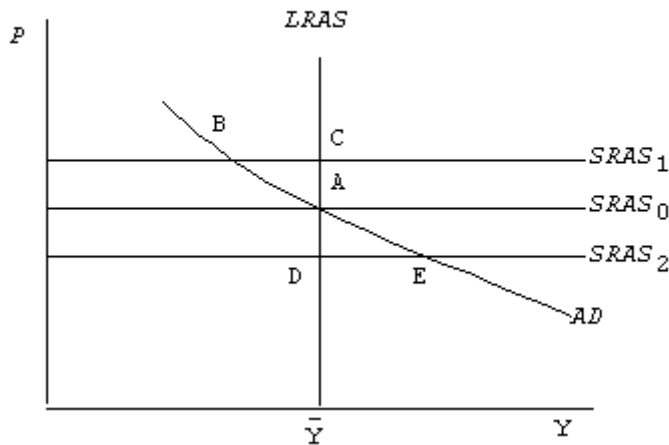
Use the following to answer question 13:



13. In this graph, initially the economy is at point E, with price P_0 and output Y . Aggregate demand is given by curve AD_0 , and $SRAS$ and $LRAS$ represent, respectively, short-run and long-run aggregate supply. Now assume that the aggregate demand curve shifts so that it is represented by AD_1 . The economy moves first to point _____ and then, in the long run, to point _____.
- A) A; D
 - B) D; A
 - C) C; B
 - D) B; C

Use the following to answer question 14:

Exhibit: Supply Shock



14. Assume that the economy starts at point A and there is a drought that severely reduces agricultural output in the economy for just one year. In this situation, point _____ represents the short-run equilibrium immediately following the drought and point _____ represents the eventual long-run equilibrium.
- A) B; C
 B) B; A
 C) E; D
 D) D; A
15. Starting from long-run equilibrium, without policy intervention, the long-run impact of an adverse supply shock is that prices will:
- A) be permanently higher and output will be restored to the natural rate.
 B) return to the old level and output will be restored to the natural rate.
 C) be permanently higher and output will be permanently lower.
 D) return to the old level, but output will be permanently lower.
16. Starting from long-run equilibrium, if a drought pushes up food prices throughout the economy, the Fed could move the economy more rapidly back to full employment output by:
- A) increasing the money supply, but at the cost of permanently higher prices.
 B) decreasing the money supply, but at the cost of permanently lower prices.
 C) increasing the money supply, which would restore the original price level.
 D) decreasing the money supply, which would restore the original price level.

Answer Key

1. C
2. D
3. D
4. B
5. D
6. A
7. D
8. C
9. D
10. B
11. D
12. C
13. C
14. B
15. B
16. A