Week #10 Worksheet – Loanable F.M. ~ Classical vs. Keynesian

1. If aggregate demand and supply are both increasing,
   - **a.** real GDP will not change.
   - **b.** the price level may not change.
   - **c.** real GDP will definitely be decreasing.
   - **d.** the price level will definitely be decreasing.
   - **e.** the price level will definitely be increasing.

2. An increase in aggregate quantity demanded could be caused by
   - **a.** a decrease in liquid assets held by households (caused, for example, by a boom in stock market prices).
   - **b.** an increase in oil prices.
   - **c.** a decrease in personal income.
   - **d.** consumer expectations of lower prices in the future.
   - **e.** a decline in the price level.

3. An economic contraction can be caused by an increase in
   - **a.** household wealth.
   - **b.** investment demand.
   - **c.** real interest rates.
   - **d.** government purchases.

4. Consumers decide to increase their level of saving to repay a larger portion of household debt. What happens?
   - **a.** Aggregate supply decreases, causing equilibrium GDP to decline.
   - **b.** Aggregate demand increases, causing the recessionary GDP gap to diminish.
   - **c.** Aggregate demand shifts to the right, causing a higher equilibrium real GDP.
   - **d.** Aggregate demand declines, resulting in lower levels of real output and employment.
   - **e.** Aggregate supply and aggregate demand both decrease, causing equilibrium GDP to decline.

5. If aggregate supply decreases while aggregate demand simultaneously increases,
   - **a.** the price level will decline, but we cannot predict what will happen to equilibrium real GDP.
   - **b.** equilibrium real GDP will increase, but we cannot predict what will happen to the price level.
   - **c.** the price level will rise.
   - **d.** equilibrium real GDP will decline and the price level will remain unchanged.
   - **e.** the price level and equilibrium real GDP will both remain unchanged.

6. A rise in input prices will cause
   - **a.** an outward shift in aggregate supply.
   - **b.** a downward movement along the aggregate supply curve.
   - **c.** an inward shift in aggregate supply.
   - **d.** an upward movement along the aggregate supply curve.
   - **e.** None of the above

7. An increase in productivity will most likely
- **a.** cause an increase in aggregate demand and aggregate supply.
- **b.** cause an increase in aggregate demand.
- **c.** have no effect on aggregate supply or aggregate demand.
- **d.** cause an increase in aggregate supply.
- **e.** None of the above.

8. Starting initially at potential real GDP, an increase in aggregate demand shifts the aggregate demand curve _________, causing real GDP to _________and the price level to _________.
- **a.** outward, rise, fall
- **b.** inward, fall, fall
- **c.** inward, fall, rise
- **d.** outward, fall, fall
- **e.** outward, rise, rise

9. If the stock market crashes, reducing real wealth, at the same time that energy prices are falling, what will likely happen to real GDP and the price level?
- **a.** The price level falls, but the change in real GDP is indeterminate.
- **b.** Real GDP and the price level fall.
- **c.** Real GDP rises, but the price level falls.
- **d.** Real GDP falls, but the change in the price level is indeterminate.

10. The classicists argued that an increase in aggregate demand would ___________ in the short run, but in the long run real GDP would ___________.
- **a.** decrease aggregate supply, rise
- **b.** increase real GDP, return to its potential level
- **c.** increase real GDP, rise further causing inflation
- **d.** decrease real GDP, increase

11. John Maynard Keynes argued that
- **a.** downward nominal-wage rigidity prevented the classical self-correction mechanism from working to eliminate recessionary GDP gaps.
- **b.** the automatic forces of the market would restore the economy to full employment very quickly.
- **c.** the classical macroeconomic argument that government spending should be used in recessions wouldn't eliminate a recessionary GDP gap.
- **d.** fluctuations in aggregate demand were the primary cause of recessions.
- **e.** Both (a) and (d).

12. If an economy is currently operating at its potential level of real GDP, an increase in aggregate demand will
- **a.** increase the price level and produce an inflationary gap.
- **b.** cause stagflation.
- **c.** produce long-run economic growth.
- **d.** decrease the price level and produce a recessionary gap.

13. Which of the following shift the long-run aggregate supply curve rightward?
- **a.** Improvements in technology
- **b.** Improvements in the efficiency with which resources are used
- **c.** Increases in the quantity of resources available to a nation
- **d.** Increases in the productivity of productive resources
- **e.** All of the above.