University of Lethbridge — Department of Economics
ECON 1012 — Introduction to Microeconomics
Instructor: Michael G. Lanyi

Chapter 29 — Fiscal Policy

1) If revenues exceed outlays, the government's budget balance is ________, and the government has a budget ________.

A) positive; deficit
B) negative; surplus
C) positive; surplus
D) negative; deficit
E) zero; deficit

Topic: Government Budgets

2) If outlays exceed revenues, the government's budget balance is ________, and the government has a budget ________.

A) negative; surplus
B) negative; deficit
C) zero; surplus
D) positive; surplus
E) positive; deficit

Topic: Government Budgets

3) Government debt is

A) always increasing.
B) the result of a rising price level.
C) the total amount of government borrowing.
D) a phenomena that occurs only during times of war.
E) equal to revenues minus outlays.

Topic: Government Budgets

4) All of the following statements are true *except*

A) revenues include corporate income taxes, personal income taxes; indirect taxes and investment income.
B) the main source of fluctuations in revenues is corporate income taxes.
C) total revenues have no strong trends.
D) indirect taxes decreased during the 1990s due to the introduction of the GST.
E) total revenues increased through the 1960s and 1980s.

Topic: Government Budgets

5) All of the following statements are true *except*

A) outlays increased steadily from 1971 through 1985.
B) the three components of government outlays are transfer payments, expenditures on goods and services, and debt interest.
C) debt interest has been steadily increasing since 1960.
D) expenditures on goods and services have a downward trend.
E) transfer payments decreased sharply during the 1990s.

Topic: Government Budgets

6) Choose the correct statement
   A) The debt-to-GDP ratio was 18 percent in 1974 .
   B) The debt-to-GDP ration increased dramatically between 1981 and 1986 .
   C) The government debt increases when the government has a budget deficit.
   D) The federal government debt was 113 percent of GDP in 1945.
   E) All of the above.

Topic: Government Budgets

7) During the 1980s and 1990s in Canada,
   A) personal income taxes as a percentage of GDP decreased.
   B) total revenues as a percentage of GDP increased by over 5 percent.
   C) indirect taxes as a percentage of GDP increased steadily.
   D) investment income as a percentage of GDP increased.
   E) none of the above.

Topic: Government Budgets

8) Between 1981 and 1986, the federal government debt
   A) averaged 80 percent of GDP.
   B) fluctuated widely in value, but exhibited no trend.
   C) fell substantially.
   D) remained constant.
   E) rose dramatically in value.

Topic: Government Budgets

9) The main components of government revenues are
   A) corporate income taxes, indirect taxes, and transfer payments.
   B) debt interest, corporate income taxes, and income taxes.
   C) transfer payments, investment income, and indirect taxes.
   D) personal income taxes, corporate income taxes, indirect taxes, and investment income.
   E) debt interest, expenditures on goods and services, and income taxes.

Topic: Government Budgets

10) The category of federal government revenues that fluctuates the most is
   A) investment income.
   B) debt interest.
   C) personal income taxes.
   D) indirect taxes.
   E) transfer payments.

Topic: Government Budgets

11) Suppose the government starts with a debt of $0. Then in year 1, there is a deficit of $100 billion, in year 2 there is a deficit of $60 billion, in year 3 there is a surplus of $40 billion, and in year 4 there is a deficit of $20 billion. What is government debt at the end of year 4?
   A) $140 billion.
   B) $180 billion.
   C) Somewhat greater than $140 billion, depending on the interest rate.
   D) Somewhat greater than $220 billion, depending on the interest rate.
   E) $20 billion.

Topic: Government Budgets

12) Which of the following would *not* increase the budget deficit?
A) an increase in government transfer payments
B) an increase in indirect taxes
C) an increase in government expenditures on goods and services
D) an increase in interest on the government debt
E) a decrease in investment income

Topic: Government Budgets

13) Fiscal policy is
A) any policy by the Bank of Canada.
B) effective only when the federal government has a budget surplus.
C) the use of the federal budget to achieve macroeconomic objectives.
D) budgeting policy by aggregate households.
E) any attempt by the federal government or Bank of Canada to control inflation.

Topic: Government Budgets

14) Which of the following is *not* a source of government revenues?
A) transfer payments
B) corporate income taxes
C) investment income
D) indirect taxes
E) personal income taxes

Topic: Government Budgets

15) Which of the following is *not* a source of government revenues?
A) personal income taxes
B) indirect taxes
C) corporate income taxes
D) investment income
E) transfer payments

Topic: Government Budgets

16) Which of the following is a government outlay?
A) investment income
B) corporate income taxes
C) indirect taxes
D) debt interest
E) personal income taxes

Topic: Government Budgets

17) As a percentage of provincial GDP, provincial government outlays are highest in
A) Alberta.
B) the Yukon Territory.
C) Quebec.
D) Newfoundland and Labrador.
E) Nunavut.

Topic: Government Budgets

18) What are the main categories of the federal government outlays?
   A) investment income, debt interest and transfer payments
   B) transfer payments, expenditures on goods and services, and debt interest
   C) indirect taxes, farmers' subsidies, and debt interest
   D) personal income taxes, expenditures on goods and services, and debt interest
   E) none of the above

Topic: Government Budgets

19) Outlays as a percentage of provincial GDP are the highest in ________, whereas the largest transfers from the federal government are made to ________.
   A) Northern Canada; Northern Canada and the Atlantic provinces
   B) Northern Canada and the Atlantic provinces; Quebec
   C) British Columbia; Northern Canada and the Atlantic provinces
   D) Ontario; Northern Canada and the Atlantic provinces
   E) Alberta; Northern Canada and the Atlantic provinces

Topic: Government Budgets

20) The government of Ricardia's budget lists the following projected revenues and outlays: $25 million in personal income taxes, $15 million in corporate income taxes, $5 million in indirect taxes, $2 million in investment income, $30 million in transfer payments, $12 million in government expenditure, and $8 million in debt interest. Ricardia has a government budget
   A) surplus of $3 million.
   B) deficit of $3 million.
   C) deficit of $13 million.
   D) surplus of $57 million.
   E) surplus of $13 million.

Topic: Government Budgets

21) The largest source of revenues for the federal government is
   A) expenditures on goods and services.
   B) indirect taxes such as the GST.
   C) corporate income taxes.
   D) personal income taxes.
   E) transfer payments.

Topic: Government Budgets

22) An increase in income taxes
   A) decreases potential GDP because workers' incentives to work are weakened.
   B) does not affect potential GDP because the potential GDP depends on technology only.
   C) decreases potential GDP because real GDP decreases when households have less disposable income to spend.
   D) does not affect potential GDP as long as the economy's endowments of resources and the state of technology remain unchanged.
   E) increases potential GDP because workers have to work longer hours to maintain the same standard of living before the tax increase.

Topic: Supply Side Effects of Fiscal Policy

23) A tax cut on capital income
   A) does not affect potential GDP because it has no impact on the supply of labour.
   B) increases potential GDP because the supply of loanable funds increases.
   C) does not affect potential GDP because the interest rate affects aggregate expenditure only.
   D) increases potential GDP because households have more disposable income to spend.
   E) increases potential GDP because workers have greater incentives to work.

Topic: Supply Side Effects of Fiscal Policy

24) Consider all the effects of fiscal policy. A cut in the income tax
A) shifts the *AD* curve rightward but does not shift either the *LAS* or *SAS* curve.
B) shifts the *LAS* curve rightward but does not shift either the *AD* or *SAS* curve.
C) shifts the *SAS* curve rightward but does not shift either the *AD* or *LAS* curve.
D) shifts both the *SAS* and *LAS* curves rightward but does not shift the *AD* curve.
E) shifts the *AD*, *SAS*, and *LAS* curves rightward.

Topic: Supply Side Effects of Fiscal Policy

25) Consider all the effects on fiscal policy. A cut in the tax on capital income
A) shifts the AD curve rightward.
B) shifts the SAS curve rightward.
C) shifts the LAS curve rightward.
D) all of the above.
E) only B and C.

Topic: Supply Side Effects of Fiscal Policy

26) Consider all the effects of fiscal policy. An income tax cut
A) increases real GDP but decreases the price level.
B) increases real GDP but leaves the price level unchanged.
C) increases real GDP and the price level may rise or fall.
D) increases both real GDP and the price level.
E) does not change real GDP or the price level.

Topic: Supply Side Effects of Fiscal Policy

27) An income tax cut that provides a greater incentive to work than an alternative tax cut will result in comparatively
A) the same level of long-run real GDP and a lower price level.
B) the same level of long-run real GDP and price level.
C) higher long-run real GDP and a lower price level.
D) the same level of long-run real GDP and a higher price level.
E) higher long-run real GDP and a higher price level.

Topic: Supply Side Effects of Fiscal Policy

28) If the nominal interest rate is 11%, the inflation rate is 4% and the tax rate is 25%, what is the real after-tax interest rate?
A) 4.25%
B) -1.25%
C) 5.25%
D) 10%
E) 8%

Topic: Supply Side Effects of Fiscal Policy

29) The Laffer Curve has been criticized by mainstream economists because
A) tax cuts are just spent, not saved as predicted by the theory.
B) empirically, tax cuts have not led to higher tax revenues.
C) higher tax rates do not create negative incentive effects.
D) there is no theoretical possibility of higher tax rates leading to lower tax revenues.
E) savers look only at real interest rates, not nominal interest rates.

Topic: Supply Side Effects of Fiscal Policy

30) An income tax ________ potential GDP by shifting the labour ________ curve ________.
A) decreases; supply; leftward
B) increases; supply curve and labour demand curve; rightward
C) increases; demand; rightward
D) increases; supply; rightward
E) decreases; demand; rightward
Topic: Supply Side Effects of Fiscal Policy

31) If we compare Canada to France and the United Kingdom, Canada's tax wedge is ________ the French tax wedge and ________ the U.K. tax wedge.
A) smaller than; smaller than
B) larger than; larger than
C) smaller than; larger than
D) equal to; larger than
E) larger than; smaller than
Topic: Supply Side Effects of Fiscal Policy

32) The difference between the before-tax and after-tax rates is the
A) tax plug.
B) deadweight loss.
C) taxation penalty.
D) deadweight gain.
E) tax wedge.
Topic: Supply Side Effects of Fiscal Policy

33) If we compare the United States to France, we see that potential GDP per person in France is ________ than that in the United States because the French tax wedge is ________ than the U.S. tax wedge.
A) greater; larger
B) greater; smaller
C) less; smaller
D) less; larger
E) none of the above
Topic: Supply Side Effects of Fiscal Policy

34) Suppose the tax rate on interest income is 50 percent, the real interest rate is 3 percent, and the inflation rate is 4 percent. The real after-tax interest rate is
A) 3.5 percent.
B) 3.0 percent.
C) 4.0 percent.
D) -3.5 percent.
E) -0.5 percent.
Topic: Supply Side Effects of Fiscal Policy

35) Suppose the tax rate on interest income is 25 percent, the real interest rate is 4 percent, and the inflation rate is 4 percent. The real after-tax interest rate is
A) 0.5 percent.
B) -0.5 percent.
C) 2.0 percent.
D) 3.5 percent.
E) 4.0 percent.
Topic: Supply Side Effects of Fiscal Policy

36) The Laffer curve is the relationship between
A) government outlays and revenues.
B) the tax rate and potential GDP.
C) the tax rate and the amount of tax revenue.
D) government expenditure and potential GDP.
E) tax revenue and potential GDP.

Topic: Supply Side Effects of Fiscal Policy

37) According to the Laffer curve, raising the tax rate
A) might increase, decrease, or not change the amount of tax revenue.
B) always increases the amount of tax revenue.
C) has no effect on the amount of tax revenue.
D) always decreases the amount of tax revenue.
E) does not change the amount of tax revenue.

Topic: Supply Side Effects of Fiscal Policy

38) The Laffer curve shows that increasing ________ increases ________ when ________ low.
A) potential GDP; tax revenue; tax revenue is
B) tax revenue; potential GDP; tax revenue is
C) investment; potential GDP; the interest rate is
D) the tax rate; tax revenue; the tax rate is
E) government outlays; the budget deficit; government expenditure is

Topic: Supply Side Effects of Fiscal Policy

39) An increase in the tax on capital income ________ the supply of loanable funds and ________ investment.
A) decreases; decreases
B) increases; increases
C) decreases the demand for loanable funds; decreases or increases
D) increases; decreases
E) decreases; increases

Topic: Supply Side Effects of Fiscal Policy

40) Suppose that in China, investment is $400 billion, saving is $400 billion, tax revenues are $500 billion, exports are $300 billion, and imports are $200 billion. The government budget ________ the supply of loanable funds, which ________ the real interest rate and ________ investment.
A) deficit decreases; raises; decreases
B) surplus decreases; raises; increases
C) surplus increases; raises; decreases
D) surplus increases; lowers; decreases
E) surplus increases; lowers; increases

Topic: Supply Side Effects of Fiscal Policy

41) Suppose that in China, investment is $400 billion, saving is $400 billion, tax revenues are $500 billion, exports are $300 billion, and imports are $200 billion. ________ in government expenditure or ________ in taxes will further increase China's budget ________, increase investment and speed economic growth.
A) An increase; an increase; surplus
B) A decrease; an increase; deficit
C) An increase; a decreases; deficit
D) A decrease; an increase; surplus
E) A decrease; a decrease; deficit

Topic: Supply Side Effects of Fiscal Policy

42) The government is proposing to increase the tax rate on labour income and asks you to report on the supply-side effects of such an action. According to the research of Edward C. Prescott, cross-country evidence for Canada, the United States, the United Kingdom, and France shows all of the following *except* ________.

A) potential GDP per person in France is 14 percent below that of the United States (per person) and the entire difference can be attributed to the difference in the tax wedge in the two countries
B) between Canada, the United States, France, and the United Kingdom, the tax wedge is greatest in the United Kingdom, and the country with the smallest tax wedge has the smallest potential GDP
C) potential GDP per person in Canada is 16 percent below that of the United States but this difference is due to different productivities
D) the greater the tax wedge, the smaller the level of employment and the smaller the potential GDP
E) potential GDP per person in the United Kingdom is 41 percent below that of the United States (per person) and about a third of the difference arises from the different tax wedges

Topic: Supply Side Effects of Fiscal Policy

43) The government increases the tax rate on labour income and at the same time cuts the rate of sales tax to keep the amount of tax collected constant. As a result, the supply of labour ________, the demand for labour ________, and the equilibrium level of employment ________. The before-tax wage rate ________, and the after-tax wage rate ________. Potential GDP ________.

A) decreases; does not change; decreases; rises; falls; decreases
B) decreases; increases; does not change; rises; falls; does not change
C) decreases; decreases; decreases; rises; falls; decreases
D) does not change; increases; increases; does not change; decreases; increases
E) does not change; does not change; does not change; does not change; does not change; does not change

Topic: Supply Side Effects of Fiscal Policy

44) The government increases the tax rate on labour income. As a result, the supply of labour ________ and the demand for labour ________. The equilibrium level of employment ________.

A) decreases; does not change; decreases
B) does not change; decreases; decreases
C) does not change; decreases; decreases
D) decreases; decreases; decreases
E) decreases; increases; does not change

Topic: Supply Side Effects of Fiscal Policy

45) The government increases the tax rate on labour income. At the equilibrium level of employment, the before-tax wage rate ________ and the after-tax wage rate ________. Potential GDP ________.

A) falls; rises; does not change
B) rises; falls; decreases
C) rises; falls; does not change
D) falls; rises; decreases
E) rises; falls; increases

Topic: Supply Side Effects of Fiscal Policy

46) Which one of the following statements is true, using absolute values? The autonomous tax multiplier

A) is larger than the government expenditure multiplier.
B) is smaller than the government expenditure multiplier.
C) always equals the government expenditure multiplier.
D) is larger than the government expenditure multiplier during expansions.
E) has the same value as the government expenditure multiplier except during recessions.

Topic: Stabilizing the Business Cycle

47) Which of the following are automatic stabilizers?
A) induced taxes
B) transfer payments
C) exports
D) investment
E) A and B

Topic: Stabilizing the Business Cycle

48) An automatic stabilizer works by
A) decreasing fluctuations in aggregate expenditure and decreasing fluctuations in real GDP.
B) increasing fluctuations in aggregate expenditure and decreasing fluctuations in real GDP.
C) making the aggregate supply curve steeper which decreases fluctuations in real GDP.
D) decreasing fluctuations in aggregate expenditure and increasing fluctuations in real GDP.
E) increasing fluctuations in aggregate expenditure and increasing fluctuations in real GDP.

Topic: Stabilizing the Business Cycle

49) Due to automatic stabilizers, when income rises
A) government outlays fall and revenues rise.
B) the economy will automatically move to full employment.
C) government outlays rise and revenues fall.
D) the economy will automatically return to its original level of real GDP.
E) government outlays equal revenues.

Topic: Stabilizing the Business Cycle

50) Due to automatic stabilizers, when real GDP increases, the
A) government budget deficit increases or the government budget surplus decreases.
B) the economy will automatically move to full employment.
C) the price level remains constant.
D) government budget remains in balance.
E) government budget deficit decreases or the government budget surplus increases.

Topic: Stabilizing the Business Cycle

51) Currently the government of Ricardia has outlays equal to \$100 billion, and a tax scheme that is related positively to real GDP by the following equation: Taxes = \$25 billion + 0.1(real GDP). What are autonomous taxes in Ricardia?
A) \$25 billion
B) It depends on the level of real GDP.
C) \$2.5 billion
D) \$250 billion
E) 0.1

Topic: Stabilizing the Business Cycle

52) Currently the government of Ricardia has outlays equal to \$100 billion, and a tax scheme that is related positively to real GDP by the following equation: Taxes = \$25 billion + 0.1(real GDP). What is the real GDP when the government has a balanced budget?
A) \$250
B) \$100
C) \$1,250 billion
D) \$750 billion
E) \$1,000 billion

Topic: Stabilizing the Business Cycle

53) If the economy is in a recession, and the government has a budget deficit, then there
A) may be either a structural surplus or deficit.
B) must be a structural surplus.
C) may be a structural deficit, but not a structural surplus.
D) may be a structural surplus, but not a structural deficit.
E) must be a structural deficit.

Topic: Stabilizing the Business Cycle

54) The structural deficit is the deficit
A) that would occur at the trough of the business cycle.
B) in a recession.
C) caused by the business cycle.
D) that would occur at potential GDP.
E) in an expansion.

Topic: Stabilizing the Business Cycle

55) The cyclical deficit
A) arises purely because real GDP does not equal potential GDP.
B) occurs when the economy is at full employment.
C) is a persistent economic phenomenon.
D) is an accumulation of the government debt.
E) none of the above.

Topic: Stabilizing the Business Cycle

56) Norland has the budget deficit of $15 billion. According to the government economists, Norland has a structural deficit of $3 billion. What is a cyclical deficit in Norland?
A) $12 billion
B) $18 billion
C) $15 billion
D) $10 billion
E) zero

Topic: Stabilizing the Business Cycle

57) Everything else remaining the same, as the economy enters a recession,
A) government outlays tend to fall and induced taxes fall.
B) induced taxes and transfer payments rise.
C) induced taxes rise and interest payments on the debt rise.
D) government outlays rise and induced taxes fall.
E) interest payments on the debt rise and induced taxes fall.

Topic: Stabilizing the Business Cycle

58) Everything else remaining the same, as the economy enters an expansion,
A) transfer payments and interest on the debt rise.
B) induced taxes rise and transfer payments fall.
C) induced taxes fall and transfer payments remain constant.
D) induced taxes and transfer payments fall.
E) induced taxes and transfer payments rise.

Topic: Stabilizing the Business Cycle

59) If the economy is in an expansion, and the federal government is running a deficit, then a recession would automatically
A) increase taxes.
B) decrease the deficit.
C) increase government outlays.
D) increase the deficit.
E) C and D.

Topic: Stabilizing the Business Cycle

60) If the economy is in a recession and the federal government is running a deficit, then an expansion would
A) leave the deficit unchanged.
B) automatically balance the budget.
C) automatically increase the deficit.
D) automatically decrease the deficit.
E) increase the deficit only if the interest rate rises.

Topic: Stabilizing the Business Cycle

61) Consider the economy of NoTax, where the multiplier is 2.5. If the government desires to shift the *AD* curve rightward by $5 billion, the correct increase in government expenditure is
A) $8.33 billion.
B) $2.5 billion.
C) $2 billion.
D) $7.5 billion.
E) $3 billion.

Topic: Stabilizing the Business Cycle

62) A cyclical deficit occurs when
A) government outlays are less than revenues.
B) there is a deficit even when real GDP equals potential GDP.
C) there is a deficit due to the fact real GDP is greater than potential GDP.
D) there is a deficit due to the fact real GDP is less than potential GDP.
E) government outlays are greater than revenues.

Topic: Stabilizing the Business Cycle

63) A structural deficit
A) equals the cyclical deficit plus the actual deficit.
B) is present only if real GDP is greater than potential.
C) is greater than a cyclical deficit.
D) exists even if real GDP equals potential.
E) none of the above.

Topic: Stabilizing the Business Cycle

64) The presence of induced taxes means that
A) the government expenditure multiplier is less than the autonomous tax multiplier.
B) fluctuations in aggregate expenditure are reduced.
C) a structural deficit always exists.
D) a cyclical deficit always exists.
E) discretionary fiscal policy is unnecessary.

Topic: Stabilizing the Business Cycle

Use the figure below to answer the following questions.

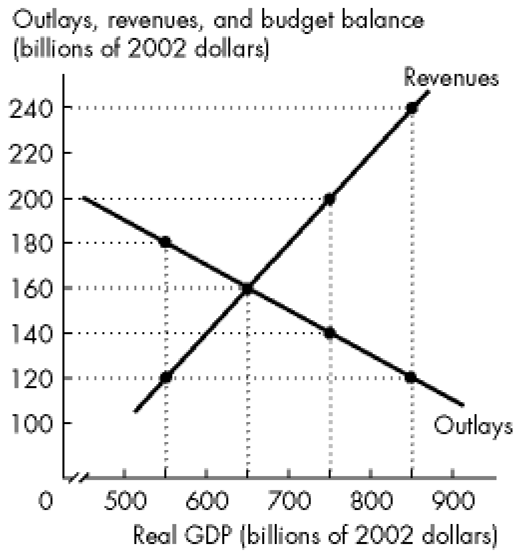

Figure 29.3.1

65) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. The budget is balanced when real GDP equals ________.
A) $550 billion
B) $750 billion
C) $600 billion
D) $650 billion
E) $700 billion

Topic: Stabilizing the Business Cycle

66) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If real GDP equals $550 billion, the budget is
A) a surplus of $40 billion.
B) a deficit of $40 billion.
C) a deficit of $60 billion.
D) a surplus of $60 billion.
E) in balance.

Topic: Stabilizing the Business Cycle

67) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If real GDP equals $550 billion, the structural deficit is
A) a surplus of $40 billion.
B) $60 billion.
C) zero.
D) a surplus of $60 billion.
E) unknown given the available information.

Topic: Stabilizing the Business Cycle

68) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If potential GDP is $750 billion,

A) the structural deficit is $60 billion.
B) the structural surplus is $60 billion.
C) the structural deficit is $40 billion.
D) neither a structural surplus nor a structural deficit exists.
E) the structural surplus is $40 billion.

Topic: Stabilizing the Business Cycle

69) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If potential GDP is $750 billion, and actual real GDP is $650 billion, the cyclical deficit is

A) $40 billion.
B) equal to the structural deficit.
C) $60 billion.
D) $180 billion.
E) zero.

Topic: Stabilizing the Business Cycle

70) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Automatic fiscal policy would be shown as a movement

A) from left to right along the outlays curve.
B) from right to left along the revenues curve.
C) from right to left along the outlays curve.
D) from left to right along the revenues curve.
E) all of the above.

Topic: Stabilizing the Business Cycle

71) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Discretionary fiscal policy would be shown as a movement

A) from left to right along the outlays curve.
B) from right to left along the outlays curve.
C) from left to right along the revenues curve.
D) from right to left along the revenues curve.
E) none of the above.

Topic: Stabilizing the Business Cycle

72) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Discretionary contractionary fiscal policy would be shown as

A) a movement from left to right along the outlays curve.
B) an upward shift of the outlays curve.
C) an upward shift of the revenues curve.
D) a movement from left to right along the revenues curve.
E) both A and C.

Topic: Stabilizing the Business Cycle

73) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Discretionary expansionary fiscal policy would be shown as

A) a movement from left to right along the outlays curve.
B) an upward shift of the outlays curve.
C) a movement from left to right along the revenues curve.
D) an upward shift of the revenues curve.
E) both A and C.

Topic: Stabilizing the Business Cycle

74) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. An increase in induced taxes would be shown as a
A) movement from left to right along the revenues curve.
B) movement from left to right along the outlays curve.
C) shift upwards in the the outlays curve.
D) shift upwards in the revenues curve.
E) both A and C.

Topic: Stabilizing the Business Cycle

75) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. A change in autonomous taxes would be shown as
A) an upward shift of the outlays curve.
B) a movement from left to right along the outlays curve.
C) a movement from left to right along the revenues curve.
D) an upward shift of the revenues curve.
E) both A and C.

Topic: Stabilizing the Business Cycle

76) Automatic fiscal policy
A) is triggered by the state of the economy.
B) occurs during recessions but not during expansions.
C) involves only a change in government outlays and no change in revenues.
D) involves only a change in personal income tax rates.
E) requires action by Parliament.

Topic: Stabilizing the Business Cycle

77) Discretionary fiscal policy
A) is triggered by the state of the economy.
B) involves only a change in government outlays and no change in revenues.
C) requires action by Parliament.
D) occurs during recessions but not during expansions.
E) involves only a change in personal income tax rates.

Topic: Stabilizing the Business Cycle

78) Which one of the following happens automatically if the economy goes into a recession?
A) Revenues decrease and government outlays do not change.
B) Both government outlays and revenues increase, and the deficit stays the same.
C) The government budget deficit increases or the government budget surplus decreases.
D) Government outlays increase and revenues do not change.
E) The government budget deficit decreases.

Topic: Stabilizing the Business Cycle

79) During an expansion, revenues
A) and government outlays decrease.
B) decrease and government outlays increase.
C) remain constant and government outlays increase.
D) and government outlays increase.
E) increase and government outlays decrease.

Topic: Stabilizing the Business Cycle

80) During a recession, revenues
A) increase and government outlays decrease.
B) and government outlays increase.
C) decrease and government outlays increase.
D) remain constant and government outlays increase.
E) and government outlays decrease.

Topic: Stabilizing the Business Cycle

81) Which of the following is an example of a fiscal policy designed to counter a recessionary gap?
A) decreasing government expenditures on goods and services
B) increasing taxes
C) increasing debt interest payments
D) decreasing transfer payments
E) increasing transfer payments

Topic: Stabilizing the Business Cycle

82) Which of the following is an example of a contractionary fiscal policy?
A) increasing government expenditure
B) increasing taxes
C) cutting transfer payments
D) A and B
E) B and C

Topic: Stabilizing the Business Cycle

83) Contractionary fiscal policy is usually not used in practice to fight inflation because
A) the fiscal multipliers are zero in the long run.
B) politicians do not want to cut their own salaries and benefits.
C) there is a time lag due to the legislative process before the fiscal policy takes action.
D) the fiscal multipliers affect real GDP but not the price level.
E) the automatic stabilizers will offset the policy effects.

Topic: Stabilizing the Business Cycle

84) Which of the following quotations correctly refers to an autonomous tax multiplier in the short run?
A) "The increase in taxes will raise prices only."
B) "The increase in taxes will lower real GDP."
C) "A change in the budget has no impact on real GDP unless it changes aggregate supply."
D) "A change in the budget has no impact on real GDP."
E) All of the above.

Topic: Stabilizing the Business Cycle

85) Expansionary fiscal policy
A) increases aggregate demand.
B) decreases aggregate demand.
C) increases short–run aggregate supply.
D) increases long–run aggregate supply.
E) A, C, and D are correct.

Topic: Stabilizing the Business Cycle

86) Which of the following policies will *not* shift the *AD* curve rightward?

A) increasing autonomous transfer payments
B) increasing government expenditure on goods and services
C) decreasing government expenditures on goods and services *and* decreasing autonomous taxes by the same amount
D) decreasing autonomous taxes
E) increasing government expenditures on goods *and* services and increasing autonomous taxes by the same amount

Topic: Stabilizing the Business Cycle

87) In the short run, an increase in government expenditure will

I. shift the aggregate demand curve rightward.
II. increase real GDP.
III. increase the government expenditure multiplier.
IV. increase the autonomous tax multiplier.

A) I and III are correct.
B) I, II and III are correct.
C) II and IV are correct.
D) I and II are correct.
E) III and IV are correct.

Topic: Government Expenditure Multiplier

88) The effects of a change in government expenditure has a multiplier effect

A) only when there is a decrease in expenditure.
B) because the resulting change in disposable income generates changes in consumption expenditure.
C) because taxes are left unchanged.
D) only when there is an increase in expenditure.
E) because a change in government expenditure changes potential GDP.

Topic: Government Expenditure Multiplier

89) A change in autonomous taxes ________ a multiplier effect because it ________ which, in turn, ________ consumption expenditure.

A) creates; changes investment; changes
B) creates; changes the supply of labour; increases
C) cannot create; cannot change investment; cannot change
D) cannot create; does not affect disposable income; cannot change
E) creates; changes disposable income; changes

Topic: Tax Multiplier

90) The magnitude of the autonomous tax multiplier ________ the magnitude of the government expenditure multiplier.

A) is always larger than
B) is always equal to
C) cannot be compared to
D) could be smaller, larger, or equal to
E) is always smaller than

Topic: Tax Multiplier

91) Suppose the government increases autonomous taxes. This change decreases

A) disposable income, which decreases potential GDP.
B) disposable income, which decreases consumption expenditure and aggregate expenditure.
C) consumption expenditure and spending on imports. The effect on aggregate expenditure depends on whether domestic spending or spending on imports decreases the most.
D) disposable income, which decreases short-run aggregate supply.
E) government expenditure, which decreases aggregate expenditure.

Topic: Tax Multiplier

92) In the short run, an increase in autonomous taxes will

I. shift the aggregate demand curve leftward.
II. decrease real GDP.
III. increase the government expenditure multiplier.
IV. increase the autonomous tax multiplier.

A) I, II, and III are correct.
B) I and III are correct.
C) II and IV are correct.
D) I and II are correct.
E) only I is correct.

Topic: Tax Multiplier

93) The effect of a change in taxes is less than the same sized change in government expenditure because

A) the amount by which consumption initially changes is equal to *MPC* times the tax change.
B) tax rates are the same regardless of income levels.
C) some people do not pay their taxes.
D) none of the above.
E) changes in government expenditure do not directly affect consumption.

Topic: Tax Multiplier

94) An advantage of automatic stabilizers over discretionary fiscal policy is that

A) automatic stabilizers work in recessions and expansions but discretionary fiscal policy works only in a recession.
B) automatic stabilizers are not subject to all the same time lags that discretionary fiscal policy is.
C) automatic stabilizers can be easily fine-tuned to move the economy to full employment.
D) only Parliament is involved in implementing automatic stabilizers instead of both Parliament and the Bank of Canada.
E) automatic stabilizers require only a simple majority of Parliament to pass whereas discretionary fiscal policy requires a two-thirds majority to pass.

Topic: Limitations of Fiscal Policy

95) If the budget deficit is $50 billion and the structural deficit is $10 billion, the cyclical deficit is

A) $50 billion
B) $60 billion.
C) $40 billion.
D) $20 billion.
E) $10 billion.

Topic: Cyclical and Structural Deficits

96) If the economy has a structural deficit of $25 billion and a cyclical deficit of $75, we can conclude that the current budget deficit is ________ billion.

A) $75
B) $50
C) $125
D) $100
E) $25

Topic: Cyclical and Structural Deficits

97) When real GDP equals potential GDP of $12 trillion, the budget deficit is $1 trillion. Real GDP actually equals $14 trillion and the budget surplus is $3 trillion. The economy has a structural ________ and a cyclical ________.

A) deficit of $4 trillion; surplus of $1 trillior
B) deficit of $1 trillion; surplus of $2 trillior
C) surplus of $3 trillion; surplus of $2 trillior
D) deficit of $1 trillion; surplus of $4 trillior
E) surplus of $4 trillion; deficit of $1 trillior

Topic: Cyclical and Structural Deficits

98) Choose the correct statement.

A) Eliminating an inflationary gap is very simple – calculate the size of the gap and the size of the multiplier, then change government expenditure for an immediate decrease in real GDP.
B) When an economy is in an above full-employment equilibrium, an equal decrease in government expenditure and autonomous taxes cannot return the economy to full employment.
C) When an economy is in an above full-employment equilibrium, an increase in taxes will decrease aggregate demand, but because the autonomous tax multiplier is smaller than the government expenditure multiplier, the economy will not return to potential GDP.
D) Contractionary fiscal policy can eliminate inflationary pressure.
E) All of the above.

Topic: Cyclical and Structural Deficits

99) A budget deficit that needs government action to remove it is a ________ deficit. A ________ deficit will disappear when the economy moves back to full employment. The economic forecast for Canada in 2009 moves the budget into a ________.

A) structural; cyclical; structural surplus
B) cyclical; structural; cyclical surplus
C) structural; cyclical; cyclical deficit
D) structural; cyclical; cyclical surplus
E) cyclical; structural; structural deficit

Topic: Cyclical and Structural Deficits

100) The economy is in a recession and the recessionary gap is large. Discretionary fiscal policy that might occur is ________. Automatic fiscal policy that might occur is ________. A discretionary fiscal stimulation package that would avoid a budget deficit is a simultaneous and equal ________.

A) an increase in government expenditure and a cut in taxes; an increase in transfer payments and a fall in induced taxes; increase in government expenditure and taxes
B) a decrease in transfer payments and an increase in induced taxes; a decrease in government expenditure and an increase in taxes; decrease in transfer payments and induced taxes
C) a decrease in government expenditure and an increase in taxes; a decrease in transfer payments and an increase in induced taxes; decrease in government expenditure and taxes
D) an increase in transfer payments and a fall in induced taxes; an increase in government expenditure and a cut in taxes; increase in transfer payments and induced taxes
E) none of the above

Topic: Cyclical and Structural Deficits

Answer Key
Testname: 029 FISCAL POLICY

1) C
2) B
3) C
4) B
5) C
6) E
7) E
8) E
9) D
10) C
11) A
12) B
13) C
14) A
15) E
16) D
17) E
18) B
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26) C
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37) A
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42) B
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