INSTITUTE OF ACTUARIAL & QUANTITATIVE STUDIES

Subject: Macro Economics

Chapter: Unit 4

Category: Practice Questions

1. Subject CT7 April 2018 Question 20

Other things being equal, an increase in the level of real output in an economy will result in:

A. a rise in the value of the fiscal multiplier.
B. a decrease in the transactions demand for money.
C. a rise in the rate of interest.
D. an increase in the speculative demand for money.

2. Subject CT7 April 2018 Question 23

As a result of a change in economic policy, interest rates and consumption rise but investment falls. The new policy is most likely to have been:

A. an expansionary fiscal policy.
B. an expansionary monetary policy.
C. a contractionary fiscal policy.
D. a contractionary monetary policy.

3. Subject CT7 April 2018 Question 24

The introduction of an expansionary monetary policy in an open economy operating with a flexible exchange rate would most likely lead to:

A. higher domestic interest rates and an appreciation of the domestic currency.
B. higher domestic interest rates and a depreciation of the domestic currency.
C. lower domestic interest rates and an appreciation of the domestic currency.
D. lower domestic interest rates and a depreciation of the domestic currency.

4. Subject CT7 April 2018 Question 25

Which of the following is a supply side economic policy aimed at promoting economic growth?

A. increases in social security benefits designed to increase expenditures of unemployed workers
B. measures designed to increase trade union powers so that real wage rises can increase expenditures of employed workers
C. increases in Tariffs designed to increase production of domestic goods
D. reduction in corporate taxation

5. Subject CT7 September 2018 Question 20

Money that is held because of possible unforeseen events is held because of the:

A. speculative motive for holding money.
B. transactions motive for holding money.
C. precautionary motive for holding money.
D. asset motive for holding money.

6. Subject CT7 September 2018 Question 21

Which of the following policies undertaken by the central bank will have an expansionary effect on the broad money supply measure other things being equal?

A. The sale of Treasury Bills in the financial markets.
B. A demand for special deposits from the commercial banks to be placed with the central bank.
C. A rise in the central bank lending rate.
D. A lowering of the reserve requirements on commercial banks.

7. Subject CT7 September 2018 Question 24

Which of the following is NOT a problem associated with the active management of fiscal policy?

A. Time lags.
B. Uncertainty.
C. Crowding out.
D. The accelerator.

8. Subject CT7 September 2018 Question 25

The adoption of an expansionary fiscal policy will result in:

A. an increase in aggregate demand and a reduction in real output and unemployment.
B. an increase in aggregate demand, real output and unemployment.
C. an increase in aggregate demand and real output and a reduction in unemployment.
D. a reduction in aggregate demand and real output and an increase in unemployment.

9. Subject CT7 September 2018 Question 26

The “crowding out” effect associated with an increase in government borrowing could be reduced or eliminated by an accommodating increase in:

A. government expenditure.
B. taxation.
C. money supply.
D. transfer payments.

10. Subject CT7 April 2017 Question 16

Which of the following is least likely to lead to an increase in long run economic growth?

A. An increase in the money supply.
B. An increase in capital investment expenditure.
C. An increase in education expenditure.
D. An increase in research and development expenditure.

11. Subject CT7 April 2017 Question 22

A government's attempts to increase the monetary base (narrow money supply) through open market operations are likely to cause short term interest rates to:

A. fall and reduce money demand.
B. fall and raise money demand.
C. rise and reduce money demand.
D. rise and raise money demand.

12. Subject CT7 April 2017 Question 23

Consider an economy where the demand for real money balances is interest inelastic and the demand for investment is interest elastic. A change in the money supply will result in a relatively:

A. small change in the rate of interest and the level of investment.
B. large change in the rate of interest and the level of investment.
C. small change in the rate of interest and a relatively large change in the level of investment

D. large change in the rate of interest and a relatively small change in the level of investment.

13. Subject CT7 April 2017 Question 25

The introduction of a restrictive monetary policy in an open economy operating with a flexible exchange rate would most likely lead to:

A. higher domestic interest rates and an exchange rate appreciation.

B. higher domestic interest rates and an exchange rate depreciation.

C. lower domestic interest rates and an exchange rate appreciation.

D. lower domestic interest rates and an exchange rate depreciation.

14. Subject CT7 April 2017 Question 26

A central bank's use of the "Taylor Rule" attempts to take which of the following two macroeconomic objectives into account?

A. inflation and the exchange rate

B. economic growth and unemployment

C. inflation and economic growth

D. unemployment and the exchange rate

15. Subject CT7 October 2017 Question 15

Which one of the following will occur, assuming spare capacity within the economy, if both government spending and the money supply are increased:

A. national income and interest rates will both rise
B. national income and interest rates will both fall
C. the effect on both national income and interest rates is uncertain
D. national income will rise but the effect on interest rates is uncertain

16. Subject CT7 October 2017 Question 16

Which one of the following is NOT a "crowding out" effect resulting from a fiscal expansion?

A. a fall in investment due to the associated rise in the interest rate
B. a fall in consumer demand due to the fear of higher future taxes
C. reduced import expenditure due to increased government demand for domestically produced goods
D. a fall in demand for exports due to an exchange rate appreciation as a result of the associated rise in the interest rate

17. Subject CT7 October 2017 Question 18

Which of the following would constitute a supply side economic policy for reducing unemployment?

A. increasing social security benefits
B. increasing the money supply
C. reducing corporate and personal taxation
D. increasing government expenditure aimed at exploiting the multiplier effect

18. Subject CT7 October 2017 Question 19

A government's attempts to increase the monetary base (narrow money supply) through open market operations are likely to cause short term interest rates to:

A. rise and reduce money demand.
B. rise and raise money demand.
C. fall and reduce money demand.
D. fall and raise money demand.

19. Subject CT7 October 2017 Question 20

The nominal rate of interest is 2% and the expected rate of inflation is positive at 3%. Which one of the following is TRUE?

A. The real rate of interest is positive.
B. The expected rate of inflation is less than the real rate of interest.
C. The real rate of interest is greater than the nominal rate of interest.
D. The real rate of interest is –1%.

20. Subject CT7 April 2016 Question 17

Which one of the following will have a negative impact upon money demand?

A. a fall in the rate of interest
B. a rise in the real Gross Domestic Product
C. the rise in the frequency with which people are paid
D. a higher expectation that stock prices will fall

21. Subject CT7 April 2016 Question 21

Which of the following would constitute a supply side economic policy for raising employment?

A. decreasing social security benefits
B. decreasing the money supply
C. increasing corporate and personal taxation
D. increasing government expenditure aimed at exploiting the multiplier effect

22. Subject CT7 September 2016 Question 23

Consider an economy where the demand for real money balances and the demand for investment are both highly interest elastic. A change in the money supply will give:

A. a relatively small change in both the rate of interest and the level of investment.
B. a relatively large change in both the rate of interest and the level of investment.
C. a relatively large change in the rate of interest and a relatively small change in the level of investment.

D. a relatively small change in the rate of interest and a relatively large change in the level of investment.

23. Subject CT7 September 2016 Question 24

Which one of the following statements about the demand for money is TRUE?

A. The demand for money is negatively related to the interest rate.
B. The demand for money is negatively related to wealth.
C. The demand for money is negatively related to the general price level.
D. The demand for money is negatively related to real income.

24. Subject CT7 September 2016 Question 25

The direct impact of open market operations, where the central bank purchases government securities, is to:

A. reduce the cash reserves of commercial banks and reduce the monetary base.
B. reduce the cash reserves of commercial banks and increase the monetary base.
C. increase the cash reserves of commercial banks and reduce the monetary base.
D. increase the cash reserves of commercial banks and increase the monetary base.

25. Subject CT7 September 2016 Question 26

An increase in government expenditure financed by government borrowing from the non-bank private sector is most likely to:

A. reduce the demand for money, reduce interest rates and cause investment to rise.
B. increase the demand for money, reduce interest rates and cause investment to rise.
C. reduce the demand for money, increase interest rates and cause investment to fall.
D. increase the demand for money, increase interest rates and cause investment to fall.

26. Subject CT7 April 2015 Question 22

The overall money multiplier effect might be smaller than the full bank deposits multiplier because:

A. governments are pursuing an expansionary monetary policy.
B. high rates of interest are discouraging borrowing.
C. banks are not holding excess cash reserves.
D. all proceeds of loans are re-deposited with banks.

28. Subject CT7 April 2015 Question 25

The introduction of a restrictive monetary policy in an open economy operating with a flexible exchange rate would most likely lead to:

A. higher domestic interest rates and an exchange rate appreciation.
B. higher domestic interest rates and an exchange rate depreciation.
C. lower domestic interest rates and an exchange rate appreciation.
D. lower domestic interest rates and an exchange rate depreciation.

29. Subject CT7 April 2015 Question 26

The "Taylor Rule" attempts to take which of the following two macroeconomic objectives into account?

A. inflation and the exchange rate
B. economic growth and unemployment
C. inflation and economic growth
D. unemployment and the exchange rate

30. Subject CT7 April 2015 Question 16

Other things remaining the same, the effect of an increase in the budget deficit is to:

A. lower short term interest rates because the aggregate demand curve shifts to the left.
B. raise short term interest rates because the aggregate demand

curve shifts to the left.

C. lower short term interest rates because the aggregate demand curve shifts to the right.
D. raise short term interest rates because the aggregate demand curve shifts to the right.

31. Subject CT7 April 2015 Question 22

As a result of an economic policy change, interest rates and consumption rise but investment falls. The new policy was:

A. an expansionary fiscal policy.
B. an expansionary monetary policy.
C. a contractionary fiscal policy.
D. a contractionary monetary policy.

33. Subject CT7 September 2014 Question 17

Which of the following could explain why a country's aggregate demand curve might shift inwards to the left?

A. A decrease in interest rates.
B. A rise in exchange rates.
C. A rise in government expenditure.
D. An increase in business confidence.

34. Subject CT7 September 2014 Question 20

The monetary base is increased when:

A. the government spends more money.
B. the government buys Treasury bills from the public.
C. a citizen buys a newly issued corporate bond.

D. a firm obtains an overdraft from a bank.

35. Subject CT7 September 2014 Question 21

The adoption of an expansionary fiscal policy will result in:

A. an increase in aggregate demand and a reduction in real output and unemployment.
B. an increase in aggregate demand, real output and unemployment.
C. an increase in aggregate demand and real output and a reduction in unemployment.
D. a reduction in aggregate demand and real output and an increase in unemployment.

36. Subject CT7 September 2014 Question 24

Which of the following is likely to be the most effective method of reducing the natural rate of unemployment?

A. Increase unemployment benefit
B. Increase government expenditure
C. Increase the money supply
D. Increase information flows on job availability

37. Subject CT7 September 2014 Question 26

The Central Bank conducts an open market sale of bonds equivalent to £20 million. The commercial banks hold reserves equivalent to 5 per cent of their deposits. What is the maximum that the broad money supply may fall as a result of the open market operation?

A. £1 million
B. £20 million

C. £200 million
D. £400 million

38. Subject CT7 April 2013 Question 20

Which of the following is NOT a supply side economic policy aimed at promoting economic growth?

A. Cuts in social security benefits designed to encourage more workers to take work
B. Measures designed to reduce trade union powers
C. Deregulation
D. Tariffs designed to increase production of domestic goods

39. Subject CT7 April 2013 Question 21

Which of the following will increase the demand to hold money?

A. A fall in the national income
B. A rise in the rate of interest
C. A rise in the expectation of a stock market crash
D. An increase in the frequency with which people are paid, for example, a switch from monthly to weekly payments

41. Subject CT7 April 2013 Question 23

Which ONE of the following would be observed following a contractionary open market operation by the central bank?

A. A fall in the money supply, a fall in the short term rate of interest and a fall in the price of treasury bills
B. A fall in the money supply, a fall in the short term rate of interest and a rise in the price of treasury bills
C. A fall in the money supply, a rise in the short term rate of interest

and a fall in the price of treasury bills

D. A fall in the money supply, a rise in the short term rate of interest and a rise in the price of treasury bills

42. Subject CT7 April 2012 Question 20

Which of the following statements about the demand for money is FALSE?

A. The demand for money is negatively related to the interest rate.
B. The demand for money is positively related to the level of national income.
C. The demand for money is negatively related to the price level.
D. The demand for money can be divided into speculative, precautionary and transactions motives.

43. Subject CT7 April 2012 Question 21

Which one of the following would NOT constitute a demand side economic policy for reducing unemployment?

A. Increased government expenditure on domestically produced goods.
B. Increased money supply.
C. Reduced corporate and personal taxation.
D. A privatization programme.

44. Subject CT7 April 2012 Question 22

The adoption of a policy to reduce the government's budget deficit will involve:

A. an increase in aggregate demand and a reduction in real output.

B. an increase in aggregate demand and an increase in real output.

C. a reduction in aggregate demand and a reduction in real output.
D. a reduction in aggregate demand and an increase in real output.

45. Subject CT7 September 2012 Question 17

If the money supply decreases due to a contractionary open market operation by the central bank then the price of treasury bills will:

A. fall as the short term interest rate rises.
B. fall as the short term interest rate falls.
C. rise as the short term interest rate rises.
D. rise as the short term interest rate falls.

47. Subject CT7 October 2015 Question 22

The direct impact of open market operations, where the central bank purchases government securities, is to:

A. reduce the cash reserves of commercial banks and reduce the monetary base.
B. reduce the cash reserves of commercial banks and increase the monetary base.
C. increase the cash reserves of commercial banks and reduce the monetary base.
D. increase the cash reserves of commercial banks and increase the monetary

48. Subject CT7 October 2015 Question 24

The adoption of an expansionary fiscal policy will result in:

A. an increase in aggregate demand, real output and unemployment.
B. an increase in aggregate demand and a reduction in real output and unemployment.
C. an increase in aggregate demand and real output and a reduction in unemployment.
D. a reduction in aggregate demand and real output and an increase in unemployment.

49. Subject CT7 October 2015 Question 25

The introduction of a restrictive monetary policy in an open economy operating with a flexible exchange rate would most likely lead to:

A. lower domestic interest rates and an exchange rate appreciation.
B. lower domestic interest rates and an exchange rate depreciation.
C. higher domestic interest rates and an exchange rate appreciation.
D. higher domestic interest rates and an exchange rate depreciation.

50. Subject CT7 October 2015 Question 26

"Crowding out" describes the:

A. increase in consumption expenditure caused by lower taxes.
B. increase in interest rates caused by contractionary monetary policy.
C. extent to which government expansionary policy is counteracted by lower private spending resulting from higher interest rates.
D. extent to which government contractionary policy is counteracted by lower private spending resulting from lower interest rates.

51. Subject CT7 April 2017 Question 34

Explain, using an aggregate supply and aggregate demand diagram, the likely impact of an increase in aggregate demand due to a monetary expansion in both the short and longer run. In your answer consider any relevant aggregate supply side effects.

52. Subject CT7 April 2018 Question 36

Discuss the advantages, disadvantages and potential problems associated with using fiscal policy and monetary policy to boost economic activity in an open economy.

53. Subject CT7 September 2018 Question 35

i. Describe TWO methods that can be used to control the money supply.

ii. Show using a money market equilibrium diagram, the effect of an increase in the money supply.

54. Subject CT7 October 2017 Question 36

Banks in country X operate a simple liquidity ratio of 15%. Initially $150 million is deposited with banks. Assume that the public do not hold any cash.

i. Prepare a table showing:

	$m		*$m*
Banks receive	150	Retain	……..
	……..	Lend	
Second round deposits rise by	……..	Retain	……..
		Lend	
Third round deposits rise by	……..	Retain	……..
		Lend	
Fourth round deposits rise by	……..	Retain	……..
		Lend	

ii. Determine how much credit will have been created after four rounds.

iii. Calculate the total value that deposits will eventually reach.

55. Subject CT7 April 2016 Question 32

i. Describe what is meant by discretionary fiscal policy.

ii. Assess why discretionary fiscal policy may not be effective in smoothing fluctuations in the business cycle.

56. Subject CT7 April 2016 Question 34

i. Describe how a central bank conducts a contractionary monetary policy designed to slow down the economy, making clear the implications of the operation for the short term rate of interest.
ii. Discuss THREE reasons why a central bank would wish to pursue a contractionary monetary policy.

57. Subject CT7 April 2015 Question 37

i. Discuss governments' use of discretionary fiscal policy in controlling substantial fluctuations in national income.
ii. Discuss the difficulty in predicting the effect of the policy.
iii. With the aid of a diagram, explain how time lags present an additional problem in using fiscal policy.

58. Subject CT7 October 2015 Question 35

Assume that initial deposits are £185 million and banks wish to hold 20% of deposits as cash.

i. Calculate the bank deposits multiplier.
ii. Calculate, showing all workings, the level that total deposits will eventually rise to and the total amount of credit created.
iii. Describe TWO complications that banks may experience in practice when seeking to create credit.

59. Subject CT7 April 2013 Question 36

i. Explain how an expansionary monetary policy and the associated low short term interest rates can be useful in expanding economic activity in an open economy.
ii. Discuss the potential problems that may undermine the effectiveness of such a policy

60. Subject CT7 September 2012 Question 34

Draw a diagram representing equilibrium in the money market showing both the real money supply (MS1) and real money demand (MD1) at an interest rate r_1 that clears the money market.

i. Explain and show on your diagram how a reduction in the real money supply to MS2 would affect the market rate of interest in the short run.

61. Subject CT7 April 2011 Question 23

The use of debit cards and cash withdrawal machines will have the following effect on a bank:

A. Lower the bank's liquidity ratio and increase the bank deposits multiplier.
B. Increase the bank's liquidity ratio and lower the bank deposits multiplier.
C. Lower the bank's liquidity ratio and leave the bank deposits multiplier unchanged.
D. The effect on the bank's liquidity ratio and the bank deposits multiplier will be uncertain.

62. Subject CT7 April 2011 Question 24

Which of the following would cause the demand for money curve to shift inwards to the left?

A. An increase in the frequency of payments to individuals.
B. An increase in real Gross Domestic Product.
C. A decrease in the rate of interest.
D. An increase in prices.

63. Subject CT7 April 2011 Question 26

The overall money multiplier effect might be smaller than the full bank deposits multiplier because:

A. governments are pursuing an expansionary monetary policy.
B. high rates of interest are discouraging borrowing.
C. banks are not holding excess cash reserves.
D. all proceeds of loans are re-deposited with banks.

64. Subject CT7 April 2011 Question 33

Identify and explain three functions of money.

65. Subject CT7 April 2011 Question 38

i. Identify alternative types of supply side policy.

ii. Discuss the effectiveness of supply side policies.

66. Subject CT7 September 2011 Question 23

A tightening of monetary policy in an open economy operating with a flexible exchange rate would most likely lead to:

A. higher domestic interest rates and an exchange rate appreciation.
B. higher domestic interest rates and an exchange rate depreciation.
C. lower domestic interest rates and an exchange rate appreciation.
D. lower domestic interest rates and an exchange rate depreciation.

66. Subject CT7 September 2011 Question 35

i. Explain how the general government debt may be linked to this year's budget deficit and how a rising general government debt can impact on next year's budget deficit.

ii. Explain why it is that countries with a high general government debt tend to have to pay a higher rate of interest on their debt, other things being equal, than countries with a low general government debt.

67. Subject CT7 April 2010 Question 7

The transactions demand for money will be greater the:

A. higher the price level.
B. lower the level of real income.
C. higher the rate of interest.
D. higher the speculative (asset) demand for money.

68. Subject CT7 April 2010 Question 8

If an excess demand for money exists in the economy, then as the money market moves towards equilibrium we would expect the short term interest rate to:

A. rise as Treasury bill prices rise.
B. fall as Treasury bill prices rise.
C. fall as Treasury bill prices fall.
D. rise as Treasury bill prices fall.

69. Subject CT7 April 2010 Question 10

In the event of a recession in the economy, automatic fiscal stabilizers:

A. raise government expenditure and reduce tax revenue.
B. raise government expenditure and raise tax revenue.
C. reduce government expenditure and raise tax revenue.
D. reduce government expenditure and reduce tax revenue.

70. Subject CT7 September 2010 Question 33

A bank's liquidity ratio is 10 per cent, and the bank's deposits increase by £25 billion.

i. Calculate the increase in total deposits.
ii. Explain the circumstances in which the overall multiplier effect could be smaller than that shown by your result in (i) above.

71. Subject CT7 April 2009 Question 28

i. Define the money multiplier.

ii. Provide, using the following notation, an equation for the money multiplier:

m = the money multiplier
c = the proportion of deposits held by the public as cash
r = the proportion of deposits held by the banks as cash

iii. Calculate the value of the money multiplier given the following data:
   i. $c = 0.5$ and $r = 0.2$.

iv. Calculate the resulting increase in the total quantity of money (M4) if the monetary base (MO) increased by £200m.

72. Subject CT7 September 2009 Question 18

Which one of the following situations will lead to the most crowding out following an increase of government expenditure?

A. The demand for money is interest elastic and private investment is interest inelastic.
B. The demand for money is interest inelastic and private investment is interest elastic.
C. The demand for money and private investment are both interest inelastic.
D. The demand for money and private investment are both interest elastic.

73. Subject CT7 September 2009 Question 19

Government attempts to increase the money supply through open market operations are likely to cause short term interest rates to:

A. rise and reduce money demand.

B. rise and raise money demand.

C. fall and reduce money demand.

D. fall and raise money demand.

74. Subject CT7 September 2009 Question 21

Other things being equal, an increase in the fiscal surplus will lead to a:

A. rise in long term interest rates.

B. increase in the money supply.

C. a fall in bond prices.

D. none of the above.

75. Subject CT7 September 2009 Question 23

In IS/LM analysis an increase in government spending may be illustrated as follows:

A. The IS curve shifts left and the LM curve remains in the same place.

B. The IS curve shifts right and the LM curve remains in the same place.

C. The LM curve shifts left and the IS curve remains in the same place.

D. The LM curve shifts right and the IS curve remains in the same place.

UNIT 4

PRACTICE QUESTIONS

UNIT 4

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