

**Handout 19-1 (concluded)**

**PART II**

**Instructions:** Test your understanding of fiscal policy by completing the first four questions in the table below. All your choices for each situation must be consistent, that is, you should choose either an expansionary or contractionary fiscal policy. Fill in the spaces as follows:

*Column A: Objective for Aggregate Demand*

Write "increase" if you wish to increase aggregate demand.  
Write "decrease" if you wish to decrease aggregate demand.

*Column B: Action on Taxes*

Write "increase" if you wish to increase taxes.  
Write "decrease" if you wish to decrease taxes.

*Column C: Action on Government Spending*

Write "increase" if you wish to increase government spending.  
Write "decrease" if you wish to decrease government spending.

*Column D: Effect on Budget*

Write "toward deficit" if you wish to increase the deficit (or reduce the surplus).  
Write "toward surplus" if you wish to reduce the deficit (or increase the surplus).

	(A) Objective for Aggregate Demand	(B) Action on Taxes	(C) Action on Government Spending	(D) Effect on Budget
1. The national unemployment rate rises to 12%				
2. Inflation is strong and its rate is now 14% per year				
3. Surveys show consumers are losing confidence in the economy, retail sales are weak, and business inventories are increasing rapidly.				
4. Business sales and investment are expanding rapidly, and economists believe a strong inflation lies ahead.				
5. Inflation persists while unemployment stays high.				