Money and Banking

1. The conversion of a barter economy to one that uses money increases efficiency by reducing
   a. the need to exchange goods.
   b. the need to specialize.
   c. the need to employ team production methods.
   d. transactions costs.

2. Although not a unique store of value, people find money a convenient store of value because
   a. it does not decline in value when prices rise.
   b. its value remains fixed to the price level: that is, if prices double so does the value of money.
   c. it is the most liquid asset.
   d. of all of the above.
   e. of none of the above.

3. The _____ is a better approximation for the _____, the nearer the bond’s price is to the bond’s par value and the longer the maturity of the bond
   a. current yield: yield to maturity
   b. current yield: coupon rate
   c. yield to maturity: current yield
   d. yield to maturity: coupon rate

4. When real income increases, the demand curve for money shifts to the ____ and the interest rate _____.
   a. right: rises
   b. right: fall
   c. left: falls
   d. left: rises

5. The risk premium on corporate bonds becomes smaller if
   a. the riskiness of corporate bonds increase.
   b. the liquidity of corporate bonds increase.
   c. the liquidity of corporate bonds decreases.
   d. the riskiness of corporate bonds decreases.
e. both (b) and (d) occur.

6. According to the preferred habitat theory of the term structure, a slightly upward sloping yield curve indicates that
   a. short-term interest rates are expected to rise in the future.
   b. short-term interest rates are expected to remain unchanged in the future.
   c. short-term interest rates are expected to decline moderately in the future.
   d. short-term interest rates are expected to decline sharply in the future.

7. According to the interest parity condition, the domestic interest rate is equal to
   a. the foreign interest rate plus the expected appreciation of the domestic currency.
   b. the foreign interest rate less the expected appreciation of the domestic currency.
   c. the foreign interest rate less the expected depreciation of the domestic currency.
   d. the foreign interest rate less the expected depreciation of the domestic currency weighted by the domestic interest rate.

8. A decrease in the domestic interest rate shifts the expected return schedule for domestic deposits to the _____ and causes the domestic currency to depreciate.
   a. right
   b. left
   c. right
   d. left

9. Banks face the problem of _____ in loan markets because bad credit risks are the ones most likely to seek bank loans.
   a. adverse selection
   b. moral hazard
   c. moral suasion
   d. intentional fraud

10. If the required reserve ratio is equal to 20 percent, a single bank can increase its loans up to a maximum amount equal to
    a. 5 times its excess reserves
    b. 2.5 times its excess reserves
    c. its excess reserves
    d. 20 percent of its excess reserves

11. A simple deposit multiplier equal to four implies a required reserve ratio equal to
a. 100 percent  
b. 50 percent  
c. 25 percent  
d. 0 percent

12. The money multiplier is smaller than the simple deposit multiplier when  
a. the excess reserves ratio is zero.  
b. the currency-checkable deposit ratio is zero.  
c. the excess reserves ratio is greater than zero.  
d. only (a) and (b) of the above are true.

13. Other things equal, rising market interest rates encourage banks to  
a. increase discount borrowings from the Central Bank.  
b. hold more excess reserves.  
c. hold fewer excess reserves.  
d. do both (a) and (b) of the above.  
e. do both (a) and (c) of the above.

14. The money supply is ____ related to excess reserves ratio, and is ____ related  
to the currency ratio.  
a. negatively; negatively  
b. negatively; positively  
c. positively; negatively  
d. positively; positively

15. Discount policy affects the money supply by affecting the volume of ____ and  
the ____ .  
a. excess reserves; monetary base  
b. discount loans; monetary base  
c. excess reserves; money multiplier  
d. discount loans; money multiplier

16. Keynes’s liquidity preference theory indicates that the demand for money  
a. is purely a function of income, and interest rates have no effect on the demand  
for money.  
b. is purely a function of interest rates, and income has no effect on the demand for  
money.  
c. is both a function of income and interest rates.
d. is both a function of government spending and income.

17. The expenditure multiplier is the ratio of
a. the change in equilibrium output to a change in the monetary base.
b. the change in the money supply to a change in the monetary base.
c. the change in the money supply to a change in the autonomous expenditure.
d. the change in equilibrium output to a change in the autonomous expenditure.

18. If the economy is on the IS curve, but is to the right of the LM curve, aggregate output will _____ and the interest rate will _____.
   a. rise; rise
   b. rise; fall
   c. fall; rise
   d. fall; fall

19. In the IS-LM framework, an expansionary monetary policy will cause aggregate output to _____ and the interest rate to _____.
   a. increase; increase
   b. increase; decrease
   c. decrease; decrease
   d. decrease; increase

20. The LM curve will be vertical and fiscal policy ineffective when
   a. the demand for money is unaffected by changes in the interest rate.
   b. the demand for money is unaffected by changes in the income.
   c. investment is unaffected by changes in the interest rate.
   d. investment is unaffected by changes in the income.

21. If the ____ curve is more unstable than the ____ curve, an interest rate target is preferred.
   a. IS; IS
   b. IS; LM
   c. LM; IS
   d. LM; LM

22. An autonomous rise in ____ (not caused by a change in the price level, aggregate output, or the interest rate) shifts the ____ curve to the _____.
   a. net exports; LM; right
b. net exports; LM: left

c. money demand; IS: right

d. money demand; LM: left

23. According to the monetarists an increase in the money supply, other things equal, will shift the aggregate _____ curve to the _____.
   a. demand; right
   b. demand; left
   c. supply; left
   d. supply; right

24. Keynesians believe that
   a. the aggregate demand curve is downward-sloping.
   b. a change in the quantity of money causes the aggregate demand curve to shift.
   c. changes in government spending and taxes cause the aggregate demand curve to shift.
   d. all of the above.
   e. only (a) and (b) of the above.

25. While the initial effect of a _____ shift in the aggregate _____ curve is a rise in both the price level and the output, the ultimate effect is only a rise in the price level.
   a. leftward; supply
   b. leftward; demand
   c. rightward; supply
   d. rightward; demand