

Sample Final Exam

Name _____

Id # _____

Instructions: Please mark your answer on the exam paper as well as on the scantron sheet and turn the exam in at the end.

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

- 1) Federal Reserve independence is thought to
- A) lead to better fiscal and monetary policy coordination.
 - B) introduce a short-term bias to monetary policymaking.
 - C) introduce longer-run considerations to monetary policymaking.
 - D) do both A and B of the above.

Answer: C

- 2) If the Fed decides to reduce bank reserves, it can
- A) purchase foreign currency.
 - B) purchase government bonds.
 - C) sell government bonds.
 - D) extend discount loans to banks.
 - E) print more currency.

Answer: C

- 3) Two ways in which the Fed can provide additional reserves to the banking system are by _____ government bonds or by _____ foreign currency deposits.
- A) selling; purchasing
 - B) purchasing; purchasing
 - C) selling; selling
 - D) issuing; purchasing
 - E) purchasing; selling

Answer: B

- 4) The four players in the money supply process include
- A) banks, depositors, borrowers, and the U.S. Treasury.
 - B) banks, borrowers, the central bank, and the U.S. Treasury.
 - C) banks, depositors, the central bank, and borrowers.
 - D) banks, depositors, the central bank, and the U.S. Treasury.

Answer: C

- 5) Part of the increase in currency holdings in the 1960s and 1970s can be attributed to
- A) bracket creep due to inflation and progressive income taxes.
 - B) the switch from progressive to proportional income taxes.
 - C) the adoption of regressive taxes.
 - D) increases in income tax rates.
 - E) none of the above.

Answer: A

- 6) Assuming initially that $r = 10\%$, $c = 40\%$, and $e = 0$, an increase in c to 50% causes
- A) the money multiplier to decrease from 2.8 to 2.33.
 - B) the money multiplier to increase from 2.5 to 2.8.
 - C) the money multiplier to decrease from 2.8 to 2.5.
 - D) the money multiplier to increase from 2.33 to 2.8.
 - E) no change in the money multiplier.

Answer: C

- 7) Open market operations as a monetary policy tool have the advantages that
- A) they can be implemented quickly without administrative delays.
 - B) they are easily reversed if mistakes are made.
 - C) they are flexible and precise.
 - D) all of the above.
 - E) only A and B of the above.

Answer: D

- 8) The primary indicator of the Fed's stance on monetary policy is
- A) the growth rate of M2.
 - B) the discount rate.
 - C) the Treasury bill rate.
 - D) the federal funds rate.
 - E) the growth rate of the monetary base.

Answer: D

- 9) Velocity, over the business cycle, tends to
- A) fall during economic expansion.
 - B) fall during economic contractions.
 - C) stay constant.
 - D) rise during economic contractions.

Answer: B

- 10) The money market is in equilibrium
- A) at any point on the IS curve.
 - B) at any point on the LM curve.
 - C) at any point on the ISLM diagram.
 - D) at only one point on the LM curve.
 - E) only at the intersection of the IS and LM curves.

Answer: B

- 11) An increase in government spending causes the equilibrium level of aggregate output to _____ at any given interest rate and shifts the _____ curve to the _____.
- A) fall; IS; left
 - B) rise; LM; right
 - C) rise; IS; right
 - D) fall; LM; left
 - E) rise; LM; left

Answer: C

- 12) If nominal GDP is \$8 trillion, and the money supply is \$2 trillion, velocity is
- A) 0.25.
 - B) 8.
 - C) 16.
 - D) 4.
 - E) none of the above.

Answer: D

- 13) The majority of members of the Federal Open Market Committee are
- A) Federal Reserve Bank presidents.
 - B) presidents of member banks.
 - C) the seven Federal Reserve governors.
 - D) members of the Federal Advisory Council.
 - E) none of the above.

Answer: C

- 14) When the Fed acts as a lender or last resort, the type of loan it extends is
- A) installment credit.
 - B) seasonal credit.
 - C) primary credit.
 - D) emergency credit.
 - E) secondary credit.

Answer: E

- 15) The velocity of money is
- A) the average number of times that a dollar is spent in buying the total amount of final goods and services.
 - B) the ratio of the money stock to interest rates.
 - C) the ratio of the money stock to high-powered money.
 - D) none of the above.

Answer: A

- 16) Which of the following statements concerning Keynesian analysis are true?
- A) Keynes recognized that equilibrium would occur in the economy when total quantity of output supplied (aggregate output produced) equals quantity of output demanded (Y^{ad}), that is, when $Y = Y^{ad}$.
 - B) Keynes's analysis started with the recognition that the total quantity demanded of an economy's output was the sum of four types of spending: consumer expenditure, planned investment spending, government spending, and net exports.
 - C) Keynes's analysis involves explaining why aggregate output is at a certain level by understanding what factors affect each component of aggregate demand and how the sum of these components could add up to an output smaller than the economy is capable of producing, resulting in less than full employment.
 - D) All of the above are true.

Answer: D

- 17) A monetary expansion is characterized by
- A) rising output and falling interest rates.
 - B) falling output and rising interest rates.
 - C) constant output and falling interest rates.
 - D) falling output and interest rates.
 - E) rising output and interest rates.

Answer: A

- 18) When a member of the nonbank public deposits currency into her bank account, then the monetary base will _____, but reserves will _____.
- A) fall; remain unchanged
 - B) remain unchanged; fall
 - C) rise; remain unchanged
 - D) remain unchanged; rise

Answer: D

- 19) The monetary base consists of
- A) currency in circulation and discount loans.
 - B) reserves and government securities.
 - C) currency in circulation and government securities.
 - D) currency in circulation and Federal Reserve notes.
 - E) currency in circulation and reserves.

Answer: E

- 20) The quantity theory of money is a theory of
- A) how the nominal value of aggregate income is determined.
 - B) how the money supply is determined.
 - C) how interest rates are determined.
 - D) all of the above.

Answer: A

- 21) Tobin's model of the speculative demand for money shows that people hold money as a store of wealth
- A) as a way of reducing income.
 - B) as a way of avoiding taxes.
 - C) as a way of reducing risk.
 - D) for each of the above reasons.

Answer: C

- 22) The risk structure of interest rates is
- A) the relationship among interest rates of different bonds with the same maturity.
 - B) the relationship among the term to maturity of different bonds.
 - C) the structure of how interest rates move over time.
 - D) the relationship among interest rates on bonds with different maturities.

Answer: A

- 23) The spread between the interest rates on bonds with default risk and default-free bonds is called the
- A) junk margin.
 - B) default premium.
 - C) bond margin.
 - D) risk premium.

Answer: D

- 24) If 1-year interest rates for the next two years are expected to be 4 and 2 percent, and the 2-year term premium is 1 percent, then the 2-year bond rate will be
- A) 1 percent.
 - B) 2 percent.
 - C) 3 percent.
 - D) 4 percent.
 - E) 5 percent.

Answer: D

- 25) According to the liquidity premium theory
- A) a flat yield curve indicates that short-term interest rates are expected to rise moderately in the future.
 - B) a steeply rising yield curve indicates that short-term interest rates are expected to remain unchanged in the future.
 - C) a moderately rising yield curve indicates that short-term interest rates are not expected to change much in the future.
 - D) only A and B of the above are true.

Answer: C

- 26) Using the one-period valuation model, assuming a year-end dividend of \$0.50, an expected sales price of \$50, and a required rate of return of 10%, the current price of the stock would be
- A) \$50.50.
 - B) indeterminate.
 - C) \$45.00.
 - D) \$45.91.
 - E) \$50.00.

Answer: D

- 27) In rational expectations theory, the term "optimal forecast" is essentially synonymous with
- A) the best guess.
 - B) the correct guess.
 - C) correct forecast.
 - D) the actual outcome.

Answer: A

- 28) Which of the following types of information most likely allows the exploitation of a profit opportunity?
- A) Hot tips from a stockbroker
 - B) Technical analysis
 - C) Financial analysts' published recommendations
 - D) Insider information

Answer: D

29) Which of the following is the primary source of external funds used by American businesses to finance their activities?

A) Stock

B) Bonds and commercial paper

C) Other loans

D) Bank loans

Answer: D

30) Adverse selection is a problem associated with equity and debt contracts arising from

A) the borrower's lack of incentive to seek a loan for highly risky investments.

B) the lender's inability to legally require sufficient collateral to cover a 100% loss if the borrower defaults.

C) the lender's relative lack of information about the borrower's potential returns and risks of his investment activities.

D) none of the above.

Answer: C