CHAPTER **13**

# Money and Banking

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**Multiple Choice Questions**

**Functions of money**

1. To say money is socially defined means that:
   A) money has been defined in a Constitutional amendment.
   B) whatever performs the functions of money to a high degree is included in the money supply.
   C) the money supply includes all public and private securities purchased by society.
   D) society, acting through Congress, specifies what shall be included in the money supply.

2. Money functions as:
   A) a store of value.
   B) a unit of account.
   C) a medium of exchange.
   D) all of the above.

3. If you are estimating your total expenses for school next semester, you are using money primarily as:
   A) a medium of exchange.
   B) a store of value.
   C) a unit of account.
   D) an economic investment.

4. If you place a part of your summer earnings in a savings account, you are using money primarily as a:
   A) medium of exchange.
   B) store of value.
   C) unit of account.
   D) standard of value.

5. If you write a check on a bank to purchase a used Honda Civic, you are using money primarily as:
   A) a medium of exchange.
   B) a store of value.
   C) a unit of account.

D) an economic investment.

6. A $200 price tag on a cashmere sweater in a department store window is an example of money functioning as a:
   A) unit of account.
   B) standard of deferred payments.
   C) store of value.
   D) medium of exchange.

7. Stock market price quotations best exemplify money serving as a:
   A) store of value.
   B) unit of account.
   C) medium of exchange.
   D) index of satisfaction.

8. Purchasing common stock by writing a check best exemplifies money serving as a:
   A) store of value.
   B) unit of account.
   C) medium of exchange.
   D) index of satisfaction.

9. When economists say that money serves as a medium of exchange, they mean that it is:
   A) a way to keep wealth in a readily spendable form for future use.
   B) a means of payment.
   C) a monetary unit for measuring and comparing the relative values of goods.
   D) declared as legal tender by the government.

10. When economists say that money serves as a unit of account, they mean that it is:
   A) away to keep wealth in a readily spendable form for future use.
   B) a means of payment.
   C) a monetary unit for measuring and comparing the relative values of goods.
   D) declared as legal tender by the government.

11. When economists say that money serves as a store of value, they mean that it is:
   A) a way to keep wealth in a readily spendable form for future use.
   B) a means of payment.
   C) a monetary unit for measuring and comparing the relative values of goods.
   D) declared as legal tender by the government.

**Supply of money**

12. The paper money used in the United States is:
   A) National Bank Notes.
   B) Treasury Notes.
   C) United States Notes.
   D) Federal Reserve Notes.

13. The largest component of the money supply (*M*1) is:

A) gold certificates.
B) checkable deposits.
C) paper money in circulation.
D) coins.

14. In the United States, the money supply ($M$1) is comprised of:
A) coins, paper currency, and checkable deposits.
B) currency, checkable deposits, and Series E bonds.
C) coins, paper currency, checkable deposits, and credit balances with brokers.
D) paper currency, coins, gold certificates, and time deposits.

15. Fiat money is:
A) composed only of checkable deposits.
B) money because the government asserts that it is.
C) money that is "resting" in a commercial bank vault.
D) money that can be redeemed for an intrinsically valuable commodity such as gold.

16. The purchasing power of the dollar:
A) has been increasing in recent years because of economic growth.
B) varies directly with the cost-of-living index.
C) is inversely related to the level of aggregate demand.
D) is the reciprocal of the price level.

17. The money supply is backed:
A) by the government's ability to control the supply of money and therefore to keep its value relatively stable.
B) by government bonds.
C) dollar-for-dollar with gold and silver.
D) dollar-for-dollar with gold bullion.

18. Checkable deposits are classified as money because:
A) they can be readily used in purchasing goods and paying debts.
B) banks hold currency equal to the value of their checkable deposits.
C) they are ultimately the obligations of the Treasury.
D) they earn interest income for the depositor.

19. The value of money varies:
A) inversely with the price level.
B) directly with the volume of employment.
C) directly with the price level.
D) directly with the interest rate.

20. Currency (paper money plus coins) constitutes about:
A) 81 percent of the U.S. $M$l money supply.
B) 48 percent of the U.S. $M$1 money supply.
C) 92 percent of the U.S. $M$1 money supply.
D) 11 percent of the U.S. $M$1 money supply.

21. In 2000, the supply of money ($M$1) in the United States was about:

A) \$247 billion.
B) \$1600 billion.
C) \$203 billion.
D) \$1100 billion.

22. More than one-half the money in the U.S. economy is created by:
A) the receipt of gold bullion through international trade and finance.
B) commercial banks and thrift institutions.
C) the Federal mint.
D) the Federal Treasury.

23. In defining money as *M*1 economists exclude time deposits because:
A) the intrinsic value of time deposits is nil.
B) the purchasing power of time deposits is much less stable than that of checkable deposits and currency.
C) they are not directly or immediately a medium of exchange.
D) they are not recognized by the Federal government as legal tender.

24. The purchasing power of money and the price level vary:
A) inversely.
B) directly during recessions, but inversely during inflations.
C) directly, but not proportionately.
D) directly and proportionately.

25. If the price index rises from 100 to 120, the value of the dollar:
A) may either rise or fall.
B) will rise by one-sixth.
C) will fall by one-sixth.
D) will rise by 20 percent.

26. Other things equal, an excessive increase in the money supply will :
A) increase the purchasing power of each dollar.
B) decrease the purchasing power of each dollar.
C) have no impact on the purchasing power of the dollar.
D) reduce the price level.

27. If $P$ equals the price level expressed as an index number and $D$ equals the value of the dollar, then:
A) $P = D - 1$.
B) $D = 1/P$.
C) $1 = D/P$.
D) $D = P - 1$.

Use the following to answer questions 28-30:

Answer the next question(s) on the basis of the following table:

| Year | Price level | Value of dollar |
|---|---|---|
| 1 | 1.00 | $1.00 |
| 2 | 1.25 | |
| 3 | .80 | |
| 4 | .50 | |

28. Refer to the above table. The value of the dollar in year 2 is:
    A) $1.25.
    B) $1.33.
    C) $.80.
    D) $1.00.

29. Refer to the above table. The value of the dollar in year 3 is:
    A) $1.00.
    B) $1.25.
    C) $.80.
    D) $.50.

30. Refer to the above table. The value of the dollar in year 4 is:
    A) $.25.
    B) $.33.
    C) $.50.
    D) $2.00.

31. Which of the following is *not* part of the *M*2 money supply?
    A) money market mutual fund balances
    B) money market deposit accounts
    C) currency
    D) large ($100,000 or more) time deposits

32. The *M*2 money supply includes:
    A) stock certificates.
    B) corporate bond certificates.
    C) the cash value of life insurance policies.
    D) individual shares in money market mutual funds.

33. A checking account entry is money because it:
    A) is ensured by the Federal Deposit Insurance Corporation.
    B) has been declared as such by the Federal government.
    C) performs the functions of money.
    D) can be "sold" for currency.

34. Currency in circulation is part of:
    A) M1 only.
    B) M2 only.
    C) M3 only.
    D) M1, M2, and M3.

35. Money market deposit accounts are included in:
   A) *M*1 only.
   B) both *M*1 and *M*2.
   C) both *M*2 and *M*3.
   D) *M*3 only.

36. Checkable deposits are:
   A) included in *M*1.
   B) not included in either *M*l or *M*2.
   C) considered to be a near money.
   D) also called time deposits.

37. Checkable deposits are:
   A) included in *M*1 but not in *M*2.
   B) considered to be a near-money.
   C) included in *M*1 and in *M*2.
   D) also called time deposits.

38. The amount of money reported as *M*2:
   A) is smaller than the amount reported as *M*1.
   B) is larger than the amount reported as *M*1.
   C) excludes coins and currency.
   D) includes large ($100,000 or more) certificates of deposit.

39. The largest component of the money supply is:
   A) coins.
   B) paper money.
   C) bank debt.
   D) stock certificates.

40. Paper money (currency) in the United States is issued by the:
   A) United States Mint.
   B) Federal Reserve Banks.
   C) United States Treasury.
   D) national banks.

41. A $20 bill is a:
   A) gold certificate.
   B) Treasury note.
   C) Treasury bill.
   D) Federal Reserve Note.

42. Coins in people's pockets and purses are:
   A) included in *M*1, but not in *M*2.
   B) included in both *M*1 and in *M*2.
   C) included in *M*2, but not in *M*1.
   D) excluded from *M*1 and *M*2 because people can exchange them for Federal Reserve notes.

43. Coins held in commercial banks are:
   A) included in $M1$, but not in $M2$.
   B) included both in $M1$ and in $M2$.
   C) included in $M2$, but not in $M1$.
   D) not part of the nation's money supply.

44. Checkable deposits include:
   A) both large and small time deposits.
   B) the deposits of banks and thrifts on which checks can be written.
   C) only the checkable deposits of commercial banks.
   D) only the checkable deposits of commercial banks.

45. The difference between $M1$ and $M2$ is that:
   A) the former includes time deposits.
   B) the latter includes small time deposits, noncheckable savings accounts, money market deposit accounts, and money market mutual fund balances.
   C) the latter includes negotiable government bonds.
   D) the latter includes cash held by commercial banks and the U.S. Treasury.

46. Other things equal, if checkable deposits increase by $40 billion and currency and coins in circulation decrease by $40 billion, the:
   A) $M1$ money supply will decline.
   B) $M1$ money supply will not change.
   C) $M2$ money supply will decline.
   D) $M3$ money supply will increase.

47. Other things equal, if checkable deposits decrease by $40 billion and balances in money market mutual funds increase by $40 billion, the:
   A) $M1$ money supply will decline and $M2$ money supply will remain unchanged.
   B) $M1$ and $M2$ money supplies will not change.
   C) $M2$ and $M3$ money supplies will increase.
   D) $M1$, $M2$, and $M3$ money supplies will decline.

48. Other things equal, if balances in money market mutual funds increase by $40 billion and large time deposits decrease by $40 billion, the:
   A) $M1$ and $M2$ money supplies will not change.
   B) $M2$ and $M3$ money supplies will increase.
   C) $M1$, $M2$, and $M3$ money supplies will decline.
   D) $M2$ money supply will increase and $M3$ money supply will remain unchanged.

Use the following to answer questions 49-51:

| | |
|---|---|
| Money market mutual fund balances | $220 |
| Currency and coins in banks | 10 |
| Currency and coins in circulation | 60 |
| Saving deposits, including money market deposit accounts | 50 |
| Large ($100,000 or more) time deposits | 180 |
| Small (less than $100,000) time deposits | 80 |
| Checkable deposits | 70 |

49. Refer to the above information. Money supply *M*1 for this economy is:
    A) $60.
    B) $70.
    C) $130.
    D) $140.

50. Refer to the above information. Money supply *M*2 for this economy is:
    A) $480.
    B) $130.
    C) $490.
    D) $660.

51. Refer to the above information. Money supply *M*3 for this economy is:
    A) $480.
    B) $130.
    C) $490.
    D) $660.

Use the following to answer questions 52-55:

Answer the next question(s) on the basis of the following list of assets:
1. Large ($100,000 and over) time deposits
2. Noncheckable savings deposits
3. Currency (coins and paper money)
4. Small (under $100,000) time deposits
5. Stock certificates
6. Checkable deposits
7. Money market deposit accounts
8. Money market mutual fund balances

52. Refer to the above list. The *M*1 definition of money comprises item(s):
    A) 6 only.
    B) 3, 4, and 6.
    C) 3 and 6.
    D) 2, 3, and 6.

53. Refer to the above list. The *M*2 definition of money comprises:
    A) items 1, 2, 3, and 6.
    B) items 3, 4, 5, and 6.
    C) items 2, 3, 4, 6, 7, and 8.

D) items 1, 2, 3, and 4.

54. Refer to the above list. The *M*3 definition of money comprises:
   A) items 1, 2, 3, 4, 6, 7, and 8.
   B) items 2, 3, 4, 6, 7, and 8.
   C) items 1, 3, 4, 6, 7, and 8.
   D) all of the eight items listed.

55. Refer to the above list. Which of the following is *not* included in any of the three official definitions of money?
   A) item 2
   B) item 5
   C) item 4
   D) items 1 and 4

56. Credit card balances are:
   A) a component of *M*1.
   B) a component of *M*2, but not of *M*1.
   C) a component of *M*3, but not of *M*2.
   D) not a component of *M*1, *M*2, or *M*3.

57. A basic argument for using the *M*1 concept of money is that:
   A) it includes all of the important financial assets that have any degree of liquidity.
   B) the government collects data for the components of *M*1, but does not do so for *M*2 and *M*3.
   C) its components are superior to other financial assets as a store of value.
   D) its components are directly and immediately spendable.

58. Currency and coins held within banks are part of:
   A) the *M*3 definition of the money supply.
   B) the *M*2 definition of the money supply.
   C) the *M*1 definition of the money supply.
   D) none of the above definitions of the money supply.

**Demand for money**

59. The transactions demand for money is most closely related to money functioning as a:
   A) unit of account.
   B) medium of exchange.
   C) store of value.
   D) measure of value.

60. The asset demand for money is most closely related to money functioning as a:
   A) unit of account.
   B) medium of exchange.
   C) store of value.
   D) measure of value.

61. The asset demand for money:

A) is unrelated to both the interest rate and the level of GDP.
B) varies inversely with the rate of interest.
C) varies inversely with the level of real GDP.
D) varies directly with the level of nominal GDP.

62. On a diagram where the interest rate and the quantity of money demanded are shown on the vertical and horizontal axes respectively, the transactions demand for money can be represented by:
A) a line parallel to the horizontal axis.
B) a vertical line.
C) a downsloping line or curve from left to right.
D) an upsloping line or curve from left to right.

63. On a diagram where the interest rate and the quantity of money demanded are shown on the vertical and horizontal axes respectively, the asset demand for money can be represented by:
A) a line parallel to the horizontal axis.
B) a vertical line.
C) a downsloping line or curve from left to right.
D) an upsloping line or curve from left to right.

64. On a diagram where the interest rate and the quantity of money demanded are shown on the vertical and horizontal axes respectively, the total demand for money can be found by:
A) horizontally adding the transactions and the asset demand for money.
B) vertically subtracting the transactions demand from the asset demand for money.
C) horizontally subtracting the asset demand from the transactions demand for money.
D) vertically adding the transactions and the asset demand for money.

65. The total demand for money curve will shift to the right as a result of:
A) an increase in nominal GDP.
B) an increase in the interest rate.
C) a decline in the interest rate.
D) a decline in nominal GDP.

66. Which of the following statements is correct? Other things equal:
A) a decline in real output will shift both the transactions demand curve for money and the total money demand curve to the right.
B) a decline in the interest rate will shift the asset demand curve for money to the right, but leave the total money demand curve unchanged.
C) deflation will shift both the transactions demand curve for money and the total money demand curve to the left.
D) inflation will shift the transactions demand curve for money to the right, but leave the total money demand curve unchanged.

67. If the money GDP is $600 billion and, on the average, each dollar is spent three times per year, then the amount of money demanded for transactions purposes will be:
A) $1800 billion.
B) $600 billion.
C) $200 billion.
D) $1200 billion.

68. In which of the following instances can we be certain that the quantity of money demanded by the public will decrease?

A) nominal GDP decreases and the interest rate decreases
B) nominal GDP increases and the interest rate decreases
C) nominal GDP decreases and the interest rate increases
D) nominal GDP increases and the interest rate increases

69. It is costly to hold money because:
A) deflation may reduce its purchasing power.
B) in doing so one sacrifices interest income.
C) bond prices are highly variable.
D) the velocity of money may decline.

70. An increase in nominal GDP increases the demand for money because:
A) interest rates will rise.
B) more money is needed to finance a larger volume of transactions.
C) bond prices will fall.
D) the opportunity cost of holding money will decline.

71. Which of the following is *correct*?
A) The asset demand for money is downsloping because the opportunity cost of holding money declines as the interest rate rises.
B) The asset demand for money is downsloping because the opportunity cost of holding money increases as the interest rate rises.
C) The transactions demand for money is downsloping because the opportunity cost of holding money varies inversely with the interest rate.
D) The asset demand for money is downsloping because bond prices and the interest rate are directly related.

72. The transactions demand for money will shift to the:
A) right when the interest rate increases.
B) left when the interest rate decreases.
C) right when aggregate income increases.
D) right when aggregate income decreases.

73. The opportunity cost of holding money:
A) is zero because money is not an economic resource.
B) varies inversely with the interest rate.
C) varies directly with the interest rate.
D) varies inversely with the level of economic activity.

74. The total demand for money will shift to the left as a result of:
A) a decline in nominal GDP.
B) an increase in the price level.
C) a change in the interest rate.
D) an increase in nominal GDP.

75. The asset demand for money is downsloping because:
A) the opportunity cost of holding money increases as the interest rate rises.
B) it is more attractive to hold money at high interest rates than at low interest rates.
C) bond prices rise as interest rates rise.
D) the opportunity cost of holding money declines as the interest rate rises.

76. (Advanced analysis) Assume the equation for the total demand for money is $L = 0.4Y + 80 - 4\,i$, where $L$ is the amount of money demanded, $Y$ is gross domestic product, and $i$ is the interest rate. If gross domestic product is $200 and the interest rate is 10 (percent), what amount of money will society want to hold?
A) $200
B) $120
C) $320
D) $160

**Money market**

77. If the quantity of money demanded exceeds the quantity supplied:
A) the supply-of-money curve will shift to the left.
B) the demand-for-money curve will shift to the right.
C) the interest rate will rise.
D) the interest rate will fall.

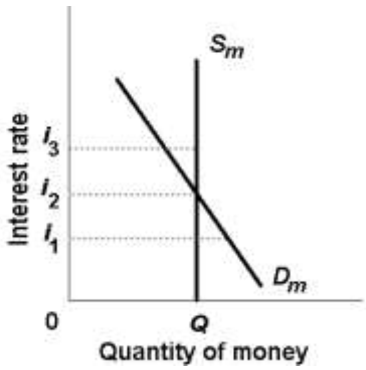
78. The equilibrium rate of interest in the money market is determined by the intersection of the:
A) supply of money curve and the asset demand for money curve.
B) supply of money curve and the transactions demand for money curve.
C) supply of money curve and the total demand for money curve.
D) investment demand curve and total demand for money curve.

79. If the demand for money and the supply of money both decrease, the equilibrium:
A) interest rate will decline, but we cannot predict the change in the equilibrium quantity of money.
B) quantity of money and the equilibrium interest rate will both increase.
C) quantity of money will increase, but we cannot predict the change in the equilibrium interest rate.
D) quantity of money will decline, but we cannot predict the change in the equilibrium interest rate.

80. If in the money market the quantity of money demanded exceeds the money supply, the interest rate will:
A) fall, causing households and businesses to hold less money.
B) rise, causing households and businesses to hold less money.
C) rise, causing households and businesses to hold more money.
D) fall, causing households and businesses to hold more money.

81. If in the money market the amount of money supplied exceeds the amount of money households and businesses want to hold, the interest rate will:
A) fall, causing households and businesses to hold less money.
B) rise, causing households and businesses to hold less money.
C) rise, causing households and businesses to hold more money.
D) fall, causing households and businesses to hold more money.

Use the following to answer questions 82-86:




82. Refer to the above diagram of the money market. The downward slope of the money demand curve $D_m$ is best explained in terms of the:
A) transactions demand for money.
B) direct or positive relationship between bond prices and interest rates.
C) asset demand for money.
D) wealth or real-balances effect.

83. Refer to the above diagram of the money market. The vertical money supply curve $S_m$ reflects the fact that:
A) bond prices and interest rates are inversely related.
B) the stock of money is determined by the Federal Reserve System and does not change when the interest rate changes.
C) the velocity of money is zero.
D) lower interest rates result in lower opportunity costs of supplying money.

84. Refer to the above diagram of the money market. The equilibrium interest rate is:
A) $i_1$.
B) $i_2$.
C) $i_3$.
D) not determinable without additional information.

85. Refer to the above diagram of the money market. Given $D_m$ and $S_m$, an interest rate of $i_3$ is not sustainable because the:
A) supply of bonds in the bond market will decline and the interest rate will rise.
B) supply of bonds in the bond market will increase and the interest rate will decline.
C) demand for bonds in the bond market will decline and the interest rate will rise.
D) demand for bonds in the bond market will rise and the interest rate will fall.

86. Refer to the above diagram of the money market. Other things equal, the money demand curve in the diagram would shift leftward if:
A) the asset demand for money increased.
B) the transactions demand for money increased.
C) nominal GDP decreased.
D) the overall price level rose.

Use the following to answer questions 87-88:

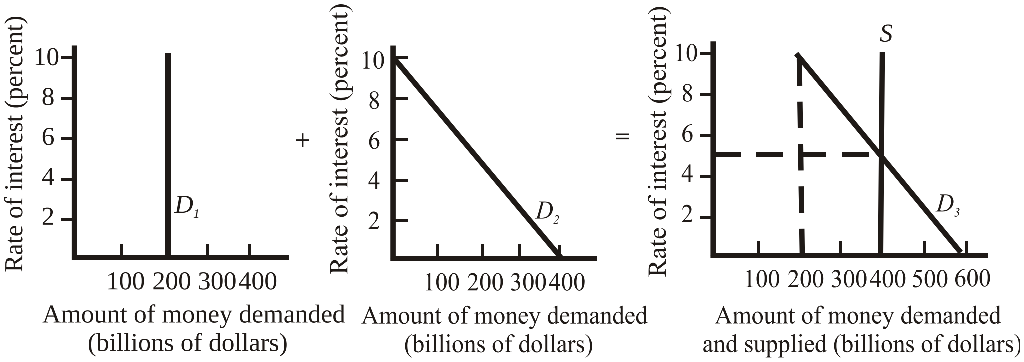
Answer the next question(s) on the basis of the following information for a bond having no expiration date: bond price = $1000; bond fixed annual interest payment - $100; bond annual interest rate = 10 percent.

87. Refer to the above information. If the price of this bond falls by $200, the interest rate will:
A) rise by 2.5 percentage points.
B) rise by 5 percentage points.
C) fall by 2.5 percentage points.
D) fall by 5 percentage points.

88. Refer to the above information. If the price of this bond increases to $1250, the interest rate will:
A) fall to 9 percent.
B) fall to 8 percent.
C) rise to 11 percent.
D) rise to 12 percent.

89. Which of the following statements is *correct*?
A) Interest rates and bond prices vary directly.
B) Interest rates and bond prices vary inversely.
C) Interest rates and bond prices are unrelated.
D) Interest rates and bond prices vary directly during inflations and inversely during recessions.

Use the following to answer questions 90-96:




90. Refer to the above money market diagrams. The asset demand for money is shown by:
A) $D_1$.
B) $D_2$.
C) $D_3$.
D) $S$.

91. Refer to the above money market diagrams. Curve $D_1$ represents the:
A) speculative demand for money.
B) transactions demand for money.
C) asset demand for money.
D) stock of money.

92. Refer to the above money market diagrams. The total demand for money is shown by:
A) $D_1$.
B) $D_2$.

C) $D_3$.
D) $S$.

93. Refer to the above money market diagrams. If each dollar held for transactions is spent four times per year on the average, we can infer that the:
A) real GDP is $800.
B) nominal GDP is $800.
C) money supply must be $800.
D) nominal GDP is $1200.

94. Refer to the above money market diagrams. If the interest rate was at 3 percent, people would:
A) sell bonds, which would cause bond prices to fall and the interest rate to rise.
B) buy bonds, which would cause bond prices to fall and the interest rate to rise.
C) sell bonds, which would cause bond prices to rise and the interest rate to rise.
D) buy bonds, which would cause bond prices to rise but have an uncertain effect upon the interest rate.

95. Refer to the above money market diagrams. If the interest rate was at 8 percent, people would:
A) sell bonds, which would cause bond prices to fall and the interest rate to fall.
B) buy bonds, which would cause bond prices to rise and the interest rate to fall.
C) have insufficient liquidity, which would cause them to reduce their spending on consumer goods.
D) buy bonds, which would cause bond prices to fall and the interest rate to rise.

96. Refer to the above money market diagrams. If the Federal Reserve increased the stock of money, the:
A) $S$ curve would shift leftward and the equilibrium interest rate would rise.
B) $S$ curve would shift rightward and the equilibrium interest rate would fall.
C) $D_3$ would shift leftward and the equilibrium interest rate would fall.
D) $D_3$ curve would shift leftward and the equilibrium interest rate would rise.

97. Suppose the demand for money and the supply of money increase simultaneously. We can:
A) expect the interest rate to rise and bond prices to fall.
B) expect the interest rate to fall and bond prices to rise.
C) the nominal GDP to expand.
D) not predict what will happen to interest rates or bond prices.

98. When the money market is in equilibrium:
A) the quantity of money demanded equals the quantity of money supplied.
B) the interest rate is increasing.
C) bond prices are falling.
D) the interest rate is declining.

99. Other things equal, if there is an increase in nominal GDP:
A) the demand for money will decrease.
B) the interest rate will rise.
C) bond prices will rise.
D) consumption spending will fall.

100. Other things equal, if the supply of money is reduced:

A) the demand for money will increase.
B) the interest rates will fall.
C) bond prices will fall.
D) investment spending will increase.

Use the following to answer questions 101-103:

Answer the next question(s) on the basis of the following table in which columns (1) and (2) indicate the transactions demand ($D_t$) for money and columns (1) and (3) show the asset demand ($D_a$) for money:

| **(1) Interest rate** | **(2) $D_t$** | **(3) $D_a$** |
|---|---|---|
| 12% | $100 | $ 0 |
| 10 | 100 | 20 |
| 8 | 100 | 40 |
| 6 | 100 | 60 |
| 4 | 100 | 80 |
| 2 | 100 | 100 |

101. The above data suggest that the amount of money demanded for transactions:
A) varies directly with the interest rate.
B) varies inversely with the interest rate.
C) varies inversely with nominal GDP.
D) is independent of the interest rate.

102. The above data suggest that the amount of money that society wishes to hold as an asset:
A) varies directly with the interest rate.
B) varies inversely with the interest rate.
C) varies inversely with nominal GDP.
D) is independent of the interest rate.

103. Refer to the above data. If the money supply is $160, the equilibrium interest rate will be:
A) 10 percent.
B) 8 percent.
C) 6 percent.
D) 4 percent.

Use the following to answer questions 104-105:

Answer the next question(s) on the basis of the following information. For transactions, households and businesses want to hold an amount of money equal to one half of nominal GDP. The table shows the amounts of money they want to hold as an asset at various interest rates.

| **Interest rate** | **Amount of money demanded** |
|---|---|
| 10% | $ 20 |
| 8 | 40 |
| 6 | 60 |
| 4 | 80 |
| 2 | 100 |

104. Refer to the above information. If nominal GDP is $200 and the interest rate is 6 percent, the total amount of money that households and businesses will want to hold is:
   A) $120
   B) $140
   C) $160
   D) $180

105. Refer to the above information. If nominal GDP is $300 and the supply of money is $230, the equilibrium interest rate will be:
   A) 8 percent.
   B) 6 percent.
   C) 4 percent.
   D) 2 percent.

106. The price of a bond having no expiration date is originally $8,000 and has a fixed annual interest payment of $800. A fall in the price of the bond by $3,000 will provide a new buyer of the bond an interest rate of:
   A) 10 percent.
   B) 12 percent.
   C) 14 percent.
   D) 16 percent.

Use the following to answer questions 107-112:

Answer the next question(s) on the basis of the following table:

| **Interest rate** | **Transaction demand for money** | **Asset demand for money** | **Money supply** |
|---|---|---|---|
| 2% | $220 | $300 | $460 |
| 4 | 220 | 280 | 460 |
| 6 | 220 | 260 | 460 |
| 8 | 220 | 240 | 460 |
| 10 | 220 | 220 | 460 |

107. The transactions demand for money in the above money market would graph as a:
   A) vertical line.
   B) horizontal line.
   C) line sloping downward and to the right.
   D) line sloping upward and to the right.

108. The total demand for money curve in the above money market would graph as a:
   A) vertical line.
   B) horizontal line.
   C) line sloping upward to the right.
   D) line sloping downward to the right.

109. At equilibrium in the above money market, the total amount of money demanded is:
   A) $500.
   B) $480.

C) $460.
D) $440.

110. Refer to the above table. The equilibrium interest rate is:
A) 2 percent.
B) 4 percent.
C) 6 percent.
D) 8 percent.
E) 10 percent.

111. Refer to the above table. An increase in the money supply of $20 billion will cause the equilibrium interest rate to:
A) fall by 4 percentage points.
B) fall by 2 percentage points.
C) rise by 4 percentage points.
D) rise by 2 percentage points.

112. All else equal, the transaction demand for money in the above table would increase if:
A) nominal GDP increased.
B) the interest rate fell.
C) the supply of money increased.
D) the economy's MPC declined.

**U.S. financial system**

113. The basic policy-making body in the U.S. banking system is:
A) the Federal Open Market Committee (FOMC).
B) the Board of Governors of the Federal Reserve.
C) the Federal Advisory Council.
D) the Council of Economic Advisers.

114. The twelve Federal Reserve Banks:
A) are owned and operated by the U.S. Treasury.
B) were created in 1776.
C) hold the reserve deposits of commercial banks.
D) are also known as national banks.

115. When was the Federal Reserve System created?
A) 1926
B) 1946
C) 1895
D) 1913

116. In the U.S. economy the money supply is controlled by the:
A) U.S. Treasury.
B) Federal Reserve System.
C) Senate Committee on Banking and Finance.
D) Congress.

117. The three formal Advisory Councils to the Board of Governors are the:
   A) Federal Advisory Council, Thrift Institutions Advisory Council, and the Council of Economic Advisers.
   B) Office of Management of the Budget, Congressional Budget Office, and the Consumer Advisory Council.
   C) Federal Advisory Council, Thrift Institutions Advisory Council, and the Consumer Advisory Council.
   D) Federal Advisory Council, Federal Open Market Committee, and the Council of Economic Advisers.

118. The group that sets the Federal Reserve Systems policy on buying and selling government securities (bills, notes, and bonds) is the:
   A) Federal Advisory Council.
   B) Consumer Advisory Council.
   C) Council of Economic Advisers.
   D) Federal Open Market Committee (FOMC).

119. How many commercial banks are now operating in the United States?
   A) about 140,000
   B) about 8,600
   C) about 2,000
   D) about 6,000

120. Which one of the following is true about the U. S. Federal Reserve System?
   A) There are 10 regional Federal Reserve Banks.
   B) The head of the U.S. Treasury also chairs the Federal Reserve Board.
   C) There are seven members of the Federal Reserve Board.
   D) The Open Market Committee is smaller in size than the Federal Reserve Board.

121. Which one of the following is true about the U. S. Federal Reserve System?
   A) The head of the U.S. Treasury also chairs the Federal Reserve Board.
   B) There are 10 regional Federal Reserve Banks.
   C) There are 14 members of the Federal Reserve Board.
   D) The Federal Open Market Committee (FOMC) has more members than does the Federal Reserve Board.

122. Which one of the following is true about the U. S. Federal Reserve System?
   A) There are 12 regional Federal Reserve Banks.
   B) The head of the U.S. Treasury also chairs the Federal Reserve Board.
   C) There are 14 members of the Federal Reserve Board.
   D) The Open Market Committee is smaller in size than the Federal Reserve Board.

123. In which of the following U. S. cities is one of the twelve Federal Reserve Banks located?
   A) Miami
   B) New Orleans
   C) San Francisco
   D) Denver

124. In which of the following U. S. cities is one of the twelve Federal Reserve Banks located?
   A) New York City
   B) Seattle
   C) Miami
   D) Denver

125. The Board of Governors of the Federal Reserve has ____ members.
A) 5
B) 7
C) 9
D) 14

126. The members of the Federal Reserve Board:
A) serve seven-year terms.
B) are appointed by the American Economic Association.
C) are elected by votes of the 12 presidents of the Federal Reserve Banks.
D) serve 14-year terms.

127. An important routine function of the Federal Reserve Bank is to:
A) supervise the liquidation of the assets of bankrupt state banks.
B) help large commercial banks develop correspondent relationships with smaller commercial banks.
C) advise commercial banks as to the most profitable ways of reinvesting profits.
D) provide facilities by which commercial banks and thrift institutions may collect checks.

128. Which of the following statements best describes the twelve Federal Reserve Banks?
A) They are privately owned and privately controlled central banks whose basic goal is to provide an ample and orderly market for U.S. Treasury securities.
B) They are privately owned and publicly controlled central banks whose basic function is to minimize the risks in commercial banking in order to make it a reasonably profitable industry.
C) They are privately owned and publicly controlled central banks whose basic goal is to control the money supply and interest rates in promoting the general economic welfare.
D) They are privately owned and publicly controlled central banks whose basic goal is to earn profits for their owners.

129. The seven members of the Board of Governors of the Federal Reserve System are:
A) appointed by the President with the confirmation of the Senate.
B) elected by Congress from a slate of nominees provided by the President.
C) appointed by the Senate Finance Committee.
D) appointed by the presidents of the twelve Federal Reserve Banks.

130. To say that the Federal Reserve Banks are quasi-public banks means that:
A) they are privately owned, but managed in the public interest.
B) they deal only with banks of foreign nations and do not have direct business contact with U.S. banks.
C) they deal only with commercial banks, and not the public.
D) they are publicly owned, but privately managed.

131. Which of the following is the basic economic policy function of the Federal Reserve Banks?
A) holding the deposits or reserves of commercial banks
B) acting as fiscal agents for the Federal government
C) regulating the supply of money
D) the collection or clearing of checks among commercial banks

132. The Federal Reserve System:
A) is basically an independent agency.

B) has the same status as the Supreme Court.
C) has the status of a Congressional committee.
D) is an agency of the executive branch of the Federal government.

133. Research for industrially advanced countries indicates that:
A) the more independent the central bank, the lower the average annual rate of inflation.
B) the more independent the central bank, the higher the average annual rate of inflation.
C) there is no relationship between the degree of independence of a country's central bank and its inflation rate.
D) the more independent the central bank, the higher the average annual rate of unemployment.

134. Research involving industrially advanced countries suggests that:
A) the more independent the central bank, the lower the average annual growth of real GDP.
B) the more independent the central bank, the higher the average annual growth of real GDP.
C) there is no relationship between the degree of independence of a country's central bank and the growth rate of its real GDP.
D) the less independent the central bank, the higher the average annual rate of inflation.

135. Commercial banks and thrift institutions:
A) differ because thrifts cannot make loans.
B) differ because thrifts cannot offer checkable deposits.
C) have become less similar in recent years.
D) have become increasingly similar in recent years.

136. The traditional role of savings and loan associations has been to:
A) finance business purchases of capital goods.
B) purchase corporate stocks on behalf of their depositors.
C) make installment loans to consumers.
D) make mortgage loans on houses.

137. The term thrift institution or thrifts includes:
A) savings and loan associations, mutual savings banks, and credit unions.
B) savings and loan associations, mutual savings banks, credit unions, and commercial banks.
C) commercial banks and the twelve Federal Reserve Banks.
D) any institution offering savings accounts.

**Recent developments and reform**

138. Firms whose central business is to offer security advice and buy and sell individual stocks and bonds for clients are known as:
A) thrifts.
B) pension fund companies.
C) securities firms.
D) insurance companies.

139. Firms whose central business is providing individual account shares of collections of stocks, bonds, or both are known as:
A) insurance companies.
B) thrifts.
C) commercial banks.
D) mutual funds companies.

140. Which of these pairs of financial institutions are most alike in terms of their main lines of business?
A) commercial banks and thrifts
B) insurance companies and mutual fund companies.
C) thrifts and securities firms.
D) pension fund companies and commercial banks.

141. The Federal Deposit Insurance Corporation (FDIC) insures deposits up to $100,000 in:
A) mutual fund companies and pension fund companies.
B) thrifts and insurance companies.
C) commercial banks and thrifts.
D) securities firms and insurance companies.

142. Banks and thrifts have responded to their relative declines by:
A) expanding their services and merging with one another.
B) merging with computer and software manufacturers.
C) selling their ATMs to new startup firms.
D) asking for trade protection against imported of financial services.

143. Relatively recently, Congress has:
A) permitted banks and thrifts to "self-insure" rather than participate in the FDIC system.
B) allowed holders of government bonds to add these bonds to their insured checking accounts.
C) ended restrictions on banks' merging with insurance companies, securities firms, and other firms offering financial services..
D) ended restrictions on banks' buying of nonbank firms such as manufacturers, corporate farms, and real estate companies.

144. The bank and thrift share of total financial assets has:
A) declined significantly since 1980.
B) increased significantly since 1980.
C) remained quite constant since the Second World War.
D) increased in the United States but declined abroad.

145. The share of total financial assets held by insurance companies, pension funds, mutual funds companies, and security-related firms has:
A) declined significantly since 1980.
B) increased significantly since 1980.
C) has remained quite constant since the Second World War.
D) decreased in the United States but increased abroad.

146. Which of the following is a *true* statement?
A) The bank and thrift share of total financial assets has increased dramatically since 1980.
B) The vast bulk of investment in the major nations is financed, not from internal saving, but from funds from abroad.
C) The world's financial markets have become increasingly integrated.
D) International stock and bond funds cannot be sold in the United States.

147. Relatively recently, Congress passed legislation that:
A) will eventually replace the $1 bill with a $1 coin.
B) allows nonbank firms such as Chrysler and IBM to own large commercial banks or thifts.
C) replaces the twelve Federal Reserve Banks with a single Central Bank.

D) ends the legal separation of the banking industry and securities firms.

148. The Financial Services Modernization Act of 1999:
   A) set limits on the fees that banks can charge for automatic teller machine (ATM) withdrawals.
   B) established a new dollar coin that will replace the dollar bill in 2005.
   C) permitted banks, thrifts, pension companies, and securities firms to merge and to sell each other's products.
   D) outlawed "payday loans" that are advanced against forthcoming payroll checks.

149. Electronic money is:
   A) closely associated with smart cards.
   B) issued in real terms so that it is immune from the effects of inflation.
   C) the money dispensed by automatic teller machines (ATMs).
   D) also called share-draft money.

150. Plastic cards that contain computer chips that store account balances are known as:
   A) credit cards.
   B) smart cards.
   C) debit cards.
   D) E-cards.

**Last Word Questions**

151. (Last Word) The major countries in which citizens hold and use large quantities of U.S. dollars are:
   A) Germany, England, and France.
   B) Russia, Argentina, and Poland.
   C) Canada, Australia, and New Zealand.
   D) Egypt, Spain, and Italy.

152. (Last Word) The use of U.S. dollars in foreign countries:
   A) is illegal under international law.
   B) helps foreign buyers and sellers overcome problems with their domestic currencies.
   C) varies directly (positively) with U.S. interest rates.
   D) is less in volume than the use of foreign currencies in the United States.

153. (Last Word) The use of U.S. dollars in foreign countries:
   A) is illegal under international law.
   B) actually benefits the United States because each dollar costs less than a dollar to produce.
   C) varies directly (positively) with U.S. interest rates.
   D) is less in volume than the use of foreign currencies in the United States.

**True/False Questions**

154. The $M2$ money supply is larger than the $M1$ money supply.

155. Fiat money refers to all near monies.

156. The twelve Federal Reserve Banks are governmentally owned but privately controlled.

157. The United States Treasury is the basic source of money in the U.S. economy.

158. The higher the interest rate, the larger will be the amount of money demanded for transaction purposes.

159. The asset demand for money varies inversely with the nominal GDP.

160. Depository institutions are the major source of money in the U. S. economy.

161. Checkable deposits held in saving and loan institutions, mutual savings banks, and credit unions are part of the *M*1 definition of the money supply.

162. Bond prices and interest rates are directly or positively related.

163. Currency and coins held by banks are part of the *M*1 definition of money supply.

164. The percentage share of total U.S. financial assets held by commercial banks and thrifts has increase since 1980.

165. The number of U.S. banks has increased since 1990.

166. Fidelity, Putnam, Dreyfus, and Kemper are examples of mutual fund companies.

167. Thrifts are known as "banker's banks" because they lend money to commercial banks.