

# Chapter 15

## Money, Banking, and Central Banking

### 15.1 The Functions of Money

- 1) In a barter system, we would expect to see
- A) many different units of money.
  - B) money and goods exchanged for each other.
  - C) wide-spread financial institutions.
  - D) goods traded directly for other goods and services.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

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

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 3) A barter arrangement essentially means
- A) a cashless transaction.
  - B) a credit deal.
  - C) buying with an I.O.U.
  - D) swapping goods for cash.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 4) For barter to occur there must be
- A) hyperinflation.
  - B) a double coincidence of wants for each good to be exchanged.
  - C) one person who pays cash.
  - D) two people willing to pay with credit.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 5) A barter arrangement simply means
- A) a direct exchange of goods without the use of money.
  - B) a promise to pay in the future.
  - C) that gold must be offered from one party.
  - D) the government has paid for the goods.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 6) The direct exchange of goods and services for other goods and services is known as
- A) barter.
  - B) purchasing power.
  - C) intermediation.
  - D) wholesale trade.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 7) Without an accepted medium of exchange, people
- A) have to specialize in one area of production.
  - B) have to rely on gold or silver in order to exchange goods and services.
  - C) have to resort to barter in order to exchange goods and services.
  - D) can efficiently obtain goods and services.

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 8) As a result of money in an economy,
- A) people are greedier than in a barter economy.
  - B) stealing exists and people have to find ways to prevent theft.
  - C) transaction costs are higher than would be the case in a barter economy.
  - D) real Gross Domestic Product (GDP) and economic growth are greater than they would be in a barter economy.

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Which of the following represents a function of money?
- A) medium of exchange
  - B) unit of accounting
  - C) standard of deferred payment
  - D) all of the above

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Revised

10) Money is defined as

- A) a person's net worth.
- B) anything people generally accept in exchange for goods and services.
- C) a by product of a barter economy.
- D) any financial instrument that is backed by gold.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

11) Which of the following statements does NOT describe a function of money?

- A) A store of value
- B) A hedge against inflation
- C) A standard of deferred payment
- D) A unit of accounting

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

12) When you buy a hamburger for lunch, you are using money as a

- A) store of value.
- B) standard of deferred payment.
- C) medium of exchange.
- D) unit of accounting.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

13) When money is accepted as payment in a market transaction, it is functioning as a

- A) store of value.
- B) unit of accounting.
- C) medium of exchange.
- D) unit of investment.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

14) Money as a medium of exchange

- I. Facilitates the exchange of goods
- II. Reduces the incentive to barter
- A) I only
- B) II only
- C) Both I and II
- D) Neither I nor II

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

15) The use of money as a medium of exchange

I. lowers transaction costs.

II. permits more specialization.

A) I only

B) II only

C) Neither I nor II

D) Both I and II

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

16) A \$35,000 price tag on a new car is an example of money as

A) a medium of exchange.

B) a unit of accounting.

C) a store of value.

D) a time deposit.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

17) When money provides a yardstick that allows individuals to compare the relative values of goods and services, it is functioning as a

A) medium of exchange.

B) unit of accounting.

C) store of value.

D) standard of deferred payment.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

18) When money serves as a standard for comparing values of different things, it is functioning as a

A) store of value.

B) hedge against inflation.

C) standard of deferred payment.

D) unit of accounting.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

19) To function as money, something must hold its purchasing power over time. That is, it must be a

A) store of value.

B) standard of deferred payment.

C) unit of accounting.

D) medium of exchange.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 20) If you save \$2,500 for a down payment on a new car, you are using money as
- A) a store of value.
  - B) a unit of account.
  - C) a medium of exchange.
  - D) a standard of deferred payment.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 21) To be accepted as money, an item must perform all of the following functions EXCEPT
- A) serve as a store of value.
  - B) be easily reproduced.
  - C) be a medium of exchange.
  - D) serve as a standard of deferred payment.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 22) In economics, money is
- A) another term for income.
  - B) a financial instrument backed by some precious metal such as gold or silver.
  - C) anything that people generally accept in exchange for goods and services.
  - D) whatever the government defines it to be.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Revised

- 23) When you set aside the money you have today in order to purchase goods and services later on, you are using money as a
- A) medium of exchange.
  - B) standard of deferred payment.
  - C) unit of accounting.
  - D) store of value.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 24) The most important function of money is when money is used as a
- A) medium of exchange.
  - B) standard of deferred payment.
  - C) unit of accounting.
  - D) store of value.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 25) For something to serve as money, it must be
- A) backed by the authority of the government.
  - B) generally accepted by buyers and sellers.
  - C) light, durable, and common.
  - D) convertible to gold.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 26) Which of the following is NOT one of the functions of money?
- A) Medium of exchange
  - B) Source of wealth
  - C) Unit of accounting
  - D) Store of value

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 27) The function of money as a store of value diminishes if
- A) prices of goods and services increase.
  - B) interest rates increase.
  - C) people begin to barter.
  - D) money is no longer backed by gold.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: New

- 28) Which of the following statements is NOT true about money?
- A) Anything that serves as a medium of exchange, as a unit of accounting, as a store of value, and as a standard of deferred payment can be called money.
  - B) Money is any medium that is universally accepted by sellers and creditors.
  - C) Money is a standard of deferred payment.
  - D) Money can only be coins and paper.

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 29) A medium of exchange is
- A) any asset that sellers will accept as payment.
  - B) a measure by which prices are expressed.
  - C) an asset that is used to settle future debts.
  - D) the thing traded when barter takes place.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

30) Any asset that sellers will accept as payment is a(n)

- A) medium of exchange.
- B) unit of accounting.
- C) store of value.
- D) standard of deferred payment.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

31) Without an accepted medium of exchange

- A) there would be no trade.
- B) people would have to rely on gold or silver in order to exchange goods and services.
- C) goods and services would be exchanged by barter.
- D) prices are very difficult to determine.

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

32) One of the benefits of money as a medium of exchange is that

- A) it allows for private transactions such as trading vegetables for medical services.
- B) it allows individuals to compare the relative value of goods.
- C) over time it will become more valuable so that individuals can purchase more goods and services.
- D) it allows for specialization that leads to economic efficiencies.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

33) The direct exchange of goods and services for other goods and services is known as

- A) primitive trade.
- B) nonmarket trade.
- C) barter.
- D) purchasing power parity.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

34) The direct exchange of goods and services for other goods and services without the use of money is

- A) a standard of deferred payment.
- B) barter.
- C) a store of value.
- D) financial intermediaries.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

35) Which function of money allows people to specialize in areas in which they have a comparative advantage?

- A) Medium of exchange
- B) Unit of accounting
- C) Store of value
- D) Standard of deferred payment

Answer: A

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

36) Compared to a barter economy, an economy that uses money will

- A) be greedier.
- B) be poorer.
- C) have more corruption.
- D) have more output.

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

37) Which of the following is NOT a benefit of money when used as a medium of exchange?

- A) Allowing individuals to specialize
- B) Allowing individuals to pay off debts
- C) Allowing for some economic efficiencies
- D) Providing economic growth

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

38) As a unit of account, money is used

- A) to define prices of all other goods.
- B) to pay off future debts.
- C) to hold purchasing power over time.
- D) to exchange for goods and services.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

39) The function of money that allows individuals a method to compare the relative value of goods and services is

- A) medium of exchange.
- B) unit of accounting.
- C) store of value.
- D) liquidity.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

40) A measure by which prices are expressed is a(n)

- A) medium of exchange.
- B) unit of accounting.
- C) store of value.
- D) standard of deferred payment.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

41) The function of money that provides for a commonly recognized measure of value for the price system is a(n)

- A) medium of exchange.
- B) unit of accounting.
- C) store of value.
- D) standard of deferred payment.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

42) Camels have been used as money. Which function of money would this type of money perform least well?

- A) Medium of exchange
- B) Unit of accounting
- C) Store of value
- D) Standard of deferred payment

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

43) Which term below fits closest to money functioning as a unit of accounting?

- A) Exchange
- B) Specialization
- C) Yardstick
- D) Liquid

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

44) Which function of money allows for comparison shopping?

- A) Medium of exchange
- B) Unit of accounting
- C) Store of value
- D) Standard of deferred payment

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 45) Money serves as a standard of value, which is another way of saying that money functions as
- A) a medium of exchange.
  - B) a unit of accounting.
  - C) a store of value.
  - D) standard of deferred payment.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 46) Cigarettes served as money in some prisoner of war (POW) camps during World War II. Given this, we would expect to observe
- A) no one ever smoking a cigarette.
  - B) people usually resorting to barter rather than using cigarettes as money.
  - C) prices of other goods expressed in terms of cigarettes.
  - D) only government-issued cigarettes being accepted as money.

Answer: C

Diff: 3

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 47) If something serves as a store of value, we expect it to be
- A) divisible.
  - B) durable.
  - C) of intrinsic value.
  - D) light.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 48) The ability to hold value over time is a(n)
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred payment.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 49) If something is to serve as money it must be a store of value. This means that it must
- A) be divisible.
  - B) be the standard by which all goods are compared in setting prices.
  - C) hold its purchasing power over time.
  - D) be liquid.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition



- 55) What characteristic defines something as money?
- A) assets declared by the government to be of value
  - B) a medium of exchange universally accepted in an economy
  - C) notes you can deposit in a savings account
  - D) an asset that earns interest

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 56) The requirement for a double coincidence of wants occurs when
- A) there is inflation.
  - B) there is deflation.
  - C) a system of barter is used.
  - D) the medium of exchange is liquid.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 57) To the extent that money serves as a store of value, it allows you to
- A) transfer wealth into the future.
  - B) comparison shop.
  - C) be an effective negotiator.
  - D) find good bargains.

Answer: A

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 58) To the extent that money serves as a medium of exchange
- A) it benefits both buyers and sellers.
  - B) it reduces transaction costs.
  - C) it eliminates the need for barter.
  - D) All of the above are correct.

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 59) The advantage of holding money as an asset is that
- A) money earns interest.
  - B) money is liquid.
  - C) money is safe from thievery.
  - D) the value of money appreciates over time.

Answer: B

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 60) The existence of money in an economy promotes efficiency by
- A) creating an equal distribution of income.
  - B) creating incentives to be self-sufficient.
  - C) facilitating trade, thereby allowing for greater specialization.
  - D) allowing for the formation of corporations as legal entities.

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 61) Which of the following is NOT a function of money?
- A) medium of exchange
  - B) form of credit
  - C) store of value
  - D) standard of deferred payment

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 62) When comparing the price of a mountain bike with the price of a street bike, Sam discovered the mountain bike was more expensive. This is an example of using money as
- A) a store of value.
  - B) a medium of exchange.
  - C) a unit of accounting.
  - D) a standard of deferred payment.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 63) If Joe buys a Mocha at Starbucks, his money is acting as a
- A) unit of accounting.
  - B) standard of deferred payment.
  - C) store of value.
  - D) medium of exchange.

Answer: D

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 64) When Kate and Sam use dollars to compare the market values of their automobiles, money is acting as a
- A) unit of accounting.
  - B) standard of deferred payment.
  - C) store of value.
  - D) medium of exchange.

Answer: A

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 65) When Annie puts her money in her sock drawer for purchases later on, money is acting as a
- A) unit of accounting.
  - B) standard of deferred payment.
  - C) store of value.
  - D) medium of exchange.

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 66) A monetary system is preferable over the barter system because of the problems associated with
- A) cash leakages.
  - B) the double coincidence of wants.
  - C) the law of diminishing marginal utility.
  - D) the law of increasing relative costs.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 67) A monetary system is preferable over the barter system because it
- A) reduces transaction costs.
  - B) is easier to track by the government.
  - C) limits cash leakages.
  - D) is determined by the Congress.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 68) The direct exchange of one good or service for another is called
- A) a token exchange.
  - B) a standard of deferred payment.
  - C) the exchange of purchasing power.
  - D) barter.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 69) For barter to occur there has to be
- A) a commodity to serve as a medium of exchange.
  - B) a formal market where prices are quoted.
  - C) a double coincidence of wants.
  - D) a single coincidence of wants.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 70) A \$100 price tag on a sweater in a department store is an example of money serving as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred value.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 71) Giving the store clerk a \$100 bill for a sweater priced at \$100 is an example of money serving as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred value.

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 72) If a friend of yours keeps cash hidden under the mattress, he is using money as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred value.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 73) You go to work today, but will get your paycheck at the end of the month. This is an example of money serving as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred payment.

Answer: D

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 74) Which of the following is NOT a function of money?
- A) medium of stored value
  - B) standard of deferred payment
  - C) unit of accounting
  - D) store of value

Answer: A

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 75) The price tag on a pair of Nike shoes illustrates how money performs the function of a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred payment.

Answer: B

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 76) Perishable goods such as milk or fruit are never used as money, because they cannot function as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred payment.

Answer: C

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 77) Suppose you are offered a new iPod in exchange for thirty hours of your work in your friend's garden. This is an example of
- A) money as a medium of exchange.
  - B) money as a store of value.
  - C) barter.
  - D) money as a standard of deferred payment.

Answer: C

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 78) Suppose you pay \$490.00 for a new iPad. This is an example of
- A) money as a medium of exchange.
  - B) money as a store of value.
  - C) barter.
  - D) money as a standard of deferred payment.

Answer: A

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Revised

- 79) What is money?

Answer: Money is any medium that is universally accepted in an economy by sellers of goods and services as payments for the goods and services and by creditors as payment for debts.

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

80) Why is money as a medium of exchange important in an economy?

Answer: Money permits more specialization and reduces the transaction costs associated with means-of-payment uncertainty. Under barter, one might be uncertain as to what the other party might be willing to accept. With money, this uncertainty is greatly reduced.

Diff: 2

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

81) What are the functions of money?

Answer: Money serves as a medium of exchange, which means it is accepted as payment. It serves as a unit of account in which prices are expressed. It also serves as a store of value and as a standard of deferred payment.

Diff: 1

Topic: 15.1 The Functions of Money

AACSB: Analytic skills

Question Status: Previous Edition

## 15.2 Properties of Money

1) Given the list of assets below, which is the most liquid?

- A) \$500 worth of General Motors common stock
- B) \$500 worth of General Motors bonds
- C) A \$500 travelers check
- D) A one-ounce gold coin

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

2) The degree to which an asset can be acquired or disposed of without much loss of nominal value or transaction costs is known as

- A) fiat money.
- B) liquidity.
- C) fiducia.
- D) credit.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

3) An individual who desires the most liquid asset possible will hold

- A) currency.
- B) a savings account.
- C) checkable deposits at a bank.
- D) U.S. government bonds.

Answer: A

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 4) The ability to quickly convert an asset into cash is
- A) disintermediation.
  - B) the standard of deferred payment.
  - C) financial intermediation.
  - D) liquidity.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 5) When an asset is described as being highly liquid, which one of the following characteristics does it possess?
- A) It earns a high rate of interest, so its purchasing power is maintained when prices rise.
  - B) It is easily and readily converted into money without any loss in purchasing power.
  - C) The face value of the asset is somewhat less than its value when converted into currency.
  - D) The asset holds its value over time.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 6) Liquidity refers to
- A) the ease with which an asset can be acquired or disposed of without incurring high transaction costs.
  - B) the expected return from an asset.
  - C) the amount of indebtedness held against an asset.
  - D) the net worth of the individual in question.

Answer: A

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 7) Which of the following is the most liquid asset?
- A) small denomination time deposits
  - B) currency
  - C) short-term treasury bonds
  - D) shares of stock

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 8) A highly liquid asset
- A) has high transaction costs associated with its sale.
  - B) must be held for a substantial period of time.
  - C) generally has a very limited market for its resale.
  - D) can be disposed of easily without loss of value.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 9) The cost of holding money is best described as
- A) the cost of printing money.
  - B) the cost which price decreases impose on money holders.
  - C) the yield which is paid to money holders by the U.S. government.
  - D) the yield that could have been earned had the asset been held in another form.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 10) A corporate bond is not as liquid as cash because the bond
- A) cannot be converted to spendable dollars either until it matures or is sold to another investor.
  - B) can be exchanged only for the goods or services produced by the company that issued the bond.
  - C) must be exchanged for a stock certificate before it can be converted to spendable funds.
  - D) represents an exchange for gold only.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 11) If an asset can be obtained or disposed of without much risk of losing its nominal value, it is said to be
- A) fiduciary.
  - B) liquid.
  - C) wealth.
  - D) valuable.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Revised

- 12) The opportunity cost of holding money is measured by
- A) a dollar.
  - B) the price of government bonds.
  - C) the interest yield that could have been earned by holding some other asset.
  - D) the liquidity of interest-bearing assets.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 13) The most liquid asset is
- A) gold.
  - B) silver.
  - C) money.
  - D) blue-chip stocks.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 14) The reason we are willing to accept money with no intrinsic value is that
- A) paper currency may be exchanged for full-bodied money.
  - B) the money supply is backed by an equal amount of gold and silver.
  - C) we have a fiduciary monetary system in which currency has both acceptability and predictability of value.
  - D) the value of the money varies directly with changes in the price level.

Answer: C

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 15) In a fiduciary monetary system, the value of the money issued by a government is based on
- A) the gold held in that government's vaults.
  - B) public confidence in that currency's acceptability and predictability of value.
  - C) the ability to convert it to some asset of value, like silver.
  - D) its being made out of some material with a market value equal to a bill's face value.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 16) Checkable and debitable accounts in commercial banks and other financial institutions are classified as money because

A) they are not liabilities of the banks.  
B) they sometimes earn an interest income for the depositor.  
C) they are generally acceptable in the payment of debt.  
D) banks hold currency in their vaults equal to the value of demand deposits.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 17) A fiduciary monetary standard exists when the value of a currency

A) is determined by law.  
B) is convertible to a fixed quantity of gold.  
C) depends upon the public's confidence that the currency can be exchanged for goods and services.  
D) increases with inflation.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 18) Which of the following is a correct reason for stating that the United States has a fiduciary monetary system?

I. Our money is convertible to a fixed amount of silver or gold.

II. Our money has a predictable value.

A) I only                      B) II only                      C) Both I and II                      D) Neither I nor II

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 19) A system in which the value of currency issued by the government is based entirely on public faith that the currency will be acceptable in trade is

A) a fiduciary system.                      B) a private property system.  
C) a Gresham system.                      D) a socialistic system.

Answer: A

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 20) A checkable and debitable account
- A) is a very illiquid asset.
  - B) is one on which the holder can write checks.
  - C) must be traded on the stock exchange.
  - D) cannot serve as a store of value.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 21) Which of the following is a checkable and debitable account?
- A) A brokerage account with your stockbroker
  - B) A savings account
  - C) A checking account
  - D) All of the above are checkable and debitable accounts.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 22) A fiduciary monetary system is
- A) fully backed by gold.
  - B) dependent on barter for exchanges of goods and services.
  - C) one which cannot have any inflation.
  - D) dependent on the public's faith to accept the currency.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 23) Transactions deposits include
- A) credit cards.
  - B) certificates of deposit.
  - C) lines of credit.
  - D) checkable and debitable accounts.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Money in a fiduciary monetary system is backed by
- A) gold.
  - B) the public's confidence that the assets will continue to serve as money.
  - C) the intrinsic value of the materials used to make the assets that serve as money.
  - D) assets owned by the government that are intrinsically valuable.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 25) The purchasing power or value of money
- A) is determined by law.
  - B) varies inversely with the price level.
  - C) depends on the value of gold.
  - D) varies inversely with the interest rate.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 26) The purchasing power of the dollar
- A) varies directly with the price of gold.
  - B) varies directly with the purchasing power of other major currencies such as the euro and the Japanese yen.
  - C) varies directly with the price level.
  - D) varies inversely with the price level.

Answer: D

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 27) When the price level goes up, the purchasing power of the dollar
- A) also increases.
  - B) falls.
  - C) remains constant.
  - D) varies directly with the value of the euro.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 28) Money is still useful during times of inflation because
- A) it still retains the characteristic of predictability of value.
  - B) more money can be made so people can still purchase the goods and services they want.
  - C) it is not a liquid asset.
  - D) its opportunity cost falls as inflation rises.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 29) An asset is liquid if it
- A) is of intrinsic value.
  - B) can be exchanged for other goods and services.
  - C) is a store of value.
  - D) can be obtained or disposed of without losing much of its nominal value.

Answer: D

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 30) Which of the following is the most liquid?
- A) certificate of deposit
  - B) cash
  - C) checkable and debitable account
  - D) stocks and bonds

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 31) The liquidity of money refers to
- A) the amount of gold it is backed by.
  - B) the standard of deferred payments and how quickly those payments can be made.
  - C) how quickly it can be disposed of without high transaction costs.
  - D) asymmetric information.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Revised

32) The opportunity cost of holding money

- A) is measured by the alternative interest yield obtainable by holding some other asset.
- B) is based on the fiduciary monetary system.
- C) refers to the amount of paper currency held by the Fed.
- D) refers to the Fed's role as the lender of last resort.

Answer: A

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

33) The cost of holding money is

- A) transactions accounts.
- B) the opportunity cost.
- C) the liquidity approach.
- D) capital controls.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

34) The opportunity cost of holding a dollar is

- A) a dollar.
- B) the price of a government bond.
- C) less than a dollar.
- D) the interest yield that could have been earned by holding some other asset.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

35) An increase in the interest rate would induce people to

- A) sell shares of stock and buy bonds, but would have no effect on their desire to hold money.
- B) get rid of all their money and buy stocks with it.
- C) sell their least liquid assets and hold more money in case interest rates go up again.
- D) hold a smaller fraction of their wealth in the form of money.

Answer: D

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

36) The degree to which an asset can be acquired or disposed of without much danger of any intervening loss in nominal value is known as

- A) transaction deposits.
- B) a time deposit.
- C) liquidity.
- D) M2.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB:

Question Status: Previous Edition

- 37) An asset that can be easily disposed of without high transactions costs and with relative certainty as to its value is

A) solid.                      B) liquid.                      C) M1.                      D) M2.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 38) In a fiduciary monetary system, money is backed by

A) the public's confidence that the assets will continue to be accepted as money.  
 B) the intrinsic value of the materials used to make the assets.  
 C) the assets of the institutions that issue the various assets used as money.  
 D) gold.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 39) A system in which money is issued by the government and its value is based uniquely on the public's faith that the currency represents command over goods and services is the

A) transactions approach.                      B) liquidity approach.  
 C) fiduciary monetary system.                      D) transaction deposits.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 40) The U.S. fiduciary monetary system

A) is the one agency responsible for providing coins and paper currency.  
 B) is one where money is not convertible to a fixed quantity of gold.  
 C) puts capital controls in place.  
 D) controls the private banking system.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 41) The essential difference between paper money and coins as forms of money is that

A) the metallic content of coins makes them more acceptable as money.  
 B) paper money issued by the Federal Reserve Board is backed by gold while coins are not.  
 C) paper money serves as a unit of account while coins do not.  
 D) paper is paper and not metal. The metal is more durable.

Answer: D

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 42) Even when a particular monetary asset is not performing one of the functions of money well, people still use the asset because
- A) it is still easier than relying on barter.
  - B) they have no choice.
  - C) once an asset is defined as money it is always money.
  - D) people expect money will come back at a later date.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 43) A fiduciary monetary system ultimately rests on
- A) the value of the metal backing up the system.
  - B) the public's confidence in the system.
  - C) the value of the assets backing up the system.
  - D) the difficulty of counterfeiting the currency.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 44) The value of a dollar varies
- A) inversely with the price of gold.
  - B) inversely with the price level.
  - C) directly with the price level.
  - D) directly with the purchasing power of other major currencies.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 45) Even when people know the purchasing power of the currency is declining, they continue to use the currency because
- A) they have no other choice.
  - B) its value is holding better than any other asset.
  - C) its value is still predictable.
  - D) it still has some intrinsic value.

Answer: C

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 46) Which of the following would be considered the *least* liquid asset?
- A) currency
  - B) checkable deposits
  - C) travelers checks
  - D) shares of stock

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 47) Which of the following assets is the most liquid in the United States?
- A) U.S. Treasury Bonds
  - B) U.S. currency
  - C) corporate bonds
  - D) an antique car

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 48) Which of the following is the *most* liquid?
- A) real estate
  - B) currency.
  - C) U.S. treasury bonds.
  - D) shares of stock.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 49) An asset is liquid if
- A) it earns interest.
  - B) it is backed by a government guarantee.
  - C) it can be exchanged for other items of value without high transaction costs.
  - D) All of the above are correct.

Answer: C

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 50) Of the items in the following lists, which go from most liquid to least liquid?
- A) a checking account, a house, a six-month certificate of deposit, shares of stock
  - B) a six-month certificate of deposit, shares of stock, a house, a checking account
  - C) a checking account, a certificate of deposit, shares of stock, a house
  - D) a house, a six-month certificate of deposit, shares of stock, a checking account

Answer: C

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 51) In a fiduciary monetary system,
- A) coins get their value from the precious metals of which they are made.
  - B) money gets its value from the confidence that the public has in its acceptability.
  - C) paper currency does not have value, but balances in checking accounts do.
  - D) checking account balances do not have value, but paper currency does.

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 52) The term "fiduciary" comes from the Latin *fiducia*, which means
- A) value.
  - B) gold.
  - C) money.
  - D) trust or confidence.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 53) A fiduciary monetary system means
- A) that the value of each currency is determined by the amount of gold held by each nation.
  - B) that the currency is backed by implicit faith in government.
  - C) that money is legal tender.
  - D) that money has commodity value.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 54) A fiduciary monetary system has to have all of the following EXCEPT
- A) trust.
  - B) the Federal Reserve System.
  - C) acceptability.
  - D) predictability of value.

Answer: B

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 55) Which one of the following statements is true?
- A) Not all forms of currency are accepted equally well by the public as a medium of exchange.
  - B) Checkable and debitable account balances are not money, but currency is.
  - C) Checkable and debitable accounts are considered money by law in only 15 states.
  - D) The value of the dollar rises along with the increases in the consumer price index.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 56) To the extent that the value of money is less predictable, it becomes
- A) more acceptable as a standard of deferred payment.
  - B) more acceptable as a unit of account.
  - C) more acceptable as a store of value.
  - D) less acceptable as a medium of exchange.

Answer: D

Diff: 3

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 57) Which of the following would be considered a transaction deposit?
- A) passbook savings account
  - B) checking account
  - C) credit card account
  - D) 401(k) retirement account

Answer: B

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 58) What type of intrinsic value or backing does U.S. currency have today?
- A) gold
  - B) government bonds
  - C) none
  - D) silver

Answer: C

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 59) The money supply in the United States is backed by
- A) faith.
  - B) gold.
  - C) silver.
  - D) platinum.

Answer: A

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 60) United States coins and currency are backed by
- A) silver.
  - B) gold.
  - C) reserves of foreign currencies.
  - D) confidence that they will retain their value.

Answer: D

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 61) Stock market price quotations are an example of money serving as a
- A) store of value.
  - B) medium of exchange.
  - C) unit of accounting.
  - D) economic value.

Answer: C

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 62) A fiduciary monetary system is dependent on
- A) acceptability and predictability of value.
  - B) precious metals backing fiat money.
  - C) Congressional monetary support.
  - D) a negative inflation rate.

Answer: A

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 63) What is liquidity? Why is money the most liquid of all assets? What is the cost of this liquidity?

Answer: Liquidity is the degree to which an asset can be acquired or disposed of without much danger of any loss in nominal value and with small transaction costs. Money is the most widely and readily accepted asset that can be exchanged for other goods and services, so it is the most liquid asset. The cost of this liquidity is the interest yield given up that was available by holding another asset.

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 64) What is a fiduciary monetary system?

Answer: A fiduciary monetary system is a system in which currency is issued by the government and its value is based on the public's confidence that the currency represents command over goods and services. The currency used in the system has no intrinsic value.

Diff: 1

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

- 65) Savings accounts, certificates of deposit, and bonds pay interest and stocks pay dividends. Why does anyone hold on to currency or other forms of money and lose this extra income?

Answer: Money is more liquid than these other assets and this liquidity is often valuable. If one wants to purchase something, stocks cannot be used. The stock must be sold and payment to the broker must be paid. The transaction costs will be greater than the costs of holding the money balances.

Diff: 2

Topic: 15.2 Properties of Money

AACSB: Analytic skills

Question Status: Previous Edition

66) Why might people in a country refuse to accept the fiduciary money in the country?

Answer: If people believed the government was about to fail or believed the currency was becoming worthless because of inflation, they may decide to use other things as money. These might include gold or currencies from other countries that are seen as more stable.

*Diff: 3*

*Topic: 15.2 Properties of Money*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

## 15.3 Defining Money

1) The two basic ways to define money are

- A) the transactions approach and the fiduciary approach.
- B) the transactions approach and the M1 approach.
- C) the transactions approach and the liquidity approach.
- D) the liquidity approach and the store of value approach.

Answer: C

*Diff: 2*

*Topic: 15.3 Defining Money*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

2) Which of the following institutions has responsibility for distributing currency and coins to the U.S. banking system?

- A) The Office of the Comptroller of the Currency
- B) The Federal Reserve System
- C) The U.S. Bureau of Engraving and Printing
- D) The U.S. Mint

Answer: B

*Diff: 2*

*Topic: 15.3 Defining Money*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

3) Which of the following institutions has responsibility for producing the coins that are distributed in the United States?

- A) The Office of the Comptroller of the Currency
- B) The Federal Reserve System
- C) The U.S. Bureau of Engraving and Printing
- D) The U.S. Mint

Answer: D

*Diff: 2*

*Topic: 15.3 Defining Money*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 4) Which approach to measuring money focuses on the value of currency, transaction deposits, and travelers checks?
- A) The transactions approach
  - B) The liquidity approach
  - C) Near moneys
  - D) M2

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 5) The transactions approach to measuring money stresses the role of money as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) store of value.
  - D) standard of deferred payment.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 6) Which of the following is NOT included using the transactions approach to measuring the money supply (M1)?
- A) Currency
  - B) Certificates of deposit
  - C) Transaction deposits
  - D) Traveler's checks

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 7) The designate M1 measure of money consists of
- A) the most liquid types of money in the U.S. system.
  - B) small time deposits only.
  - C) credit cards and ATM cards.
  - D) gold and gold coins.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Checkable deposit account balances are
- A) counted in the calculation of the money supply.
  - B) part of M2 but not part of M1.
  - C) considered credit, but not money.
  - D) only a small component of the money supply.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

9) Which of the following is NOT part of M1?

- A) Credit cards
- B) Checking accounts
- C) Currency
- D) Traveler's checks

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

10) Which one of the following is NOT a part of the M1 definition of money?

- A) Paper currency (i.e., Federal Reserve notes)
- B) Coins
- C) Savings accounts
- D) Checkable and debitable accounts

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

11) When we examine the U.S. money supply, the smallest component of M1 is

- A) currency and coins.
- B) transaction deposits.
- C) certificates of deposit.
- D) traveler's checks.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

12) The transactions approach to measuring money includes

- A) government bonds.
- B) the value of shares of stock in commercial banks.
- C) traveler's checks.
- D) all of these.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

13) The transactions approach to measuring money (M1) includes all of the following EXCEPT

- A) traveler's checks.
- B) certificates of deposit.
- C) checking accounts.
- D) currency.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

14) All of the following are included in M1 EXCEPT

- A) coin and currency.
- B) money market mutual fund shares.
- C) traveler's checks.
- D) checking account balances.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

15) Which of the following is NOT part of M1?

- A) Money market deposit accounts
- B) Coin and currency
- C) Checking deposits
- D) Traveler's checks

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

16) Thrift institutions

- A) receive most of their funds from the public's savings deposits.
- B) include commercial banks and investment firms.
- C) include credit unions but not savings and loan associations.
- D) do not offer transaction deposits.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

17) A time deposit with a fixed maturity date offered by banks is called a

- A) checking account.
- B) savings deposit.
- C) small-denomination certificate of deposit.
- D) corporate bond.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

18) Which of the following is NOT part of M1 but is included in M2?

- A) Currency
- B) Small-denomination certificates of deposits
- C) Traveler's checks
- D) Cash

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

19) Assets that can be easily converted into money without significant loss of value are

- A) transactions balances.
- B) near monies.
- C) currencies.
- D) liabilities.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

20) Small-denomination time deposits are

- A) considered part of near money.
- B) included in the definition of both M1 and M2.
- C) included in the definition of M1, but not in M2.
- D) the same as transaction deposits.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

21) Which of the following is included in M2?

- I. money market mutual funds
  - II. small-denomination certificates of deposit
- A) I only                      B) II only                      C) Both I and II                      D) Neither I nor II

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

22) Which of the following could least reasonably be included in the liquidity approach to defining the money supply?

- A) Savings deposits
- B) Money market mutual fund accounts
- C) Corporate bonds
- D) Traveler's checks

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

23) Which of the following is true of M2?

- A) It is larger than M1.
- B) It excludes savings deposits.
- C) It does not include highly liquid components of the money supply.
- D) It is less than M1.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 24) The liquidity approach to measuring money stresses the role of money as a
- A) medium of exchange.
  - B) unit of accounting.
  - C) temporary store of value.
  - D) standard of deferred payment.

Answer: C

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 25) Since 1982, banks and thrift institutions have offered a type of savings account that yields a market rate of interest with a minimum balance and a limit on transactions. These accounts, which have no minimum maturity, are known as
- A) certificates of deposit.
  - B) money market mutual funds.
  - C) mutual funds.
  - D) repurchase agreements.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB:

Question Status: Revised

- 26) What differentiates a savings deposit from a small-denomination certificate of deposit (CD)?
- A) A CD has a fixed maturity date; a savings deposit can be withdrawn at any time.
  - B) A savings deposit cannot be withdrawn before its maturity date without incurring a penalty; funds in a CD are available at any time with no interest penalty.
  - C) Only a savings deposit is a time deposit.
  - D) All depository institutions accept savings deposits, whereas only a thrift institution can issue a CD.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

- 27) All transaction deposits are included in
- A) M1 only.
  - B) M2 only.
  - C) both M1 and M2.
  - D) savings balances only.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 28) Which of the following is NOT included in the MZM definition of money?
- A) currency.
  - B) money market funds.
  - C) travelers checks.
  - D) small-denomination time deposits.

Answer: D

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

| Component                        | Amount<br>(Billions of dollars) |
|----------------------------------|---------------------------------|
| Currency                         | \$600                           |
| Coins                            | 35                              |
| Transaction Deposits             | 570                             |
| Saving Deposits                  | 416                             |
| Travelers' Checks                | 8                               |
| Small Denomination Time Deposits | 2,144                           |
| Money Market Mutual Fund Shares  | 1,430                           |
| Overnight Eurodollars            | 16                              |
| Overnight Repurchase             |                                 |
| Agreements at Commercial Banks   | 63                              |
| Money Market Deposit Accounts    | 500                             |
| Available Credit on Credit Cards | 675                             |

29) According to the above table, the value of M1 is

- A) \$1,888 billion.      B) \$1,629 billion.      C) \$1,213 billion.      D) \$1,205 billion.

Answer: C

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

30) According to the above table, the value of M2 is

- A) \$5,303 billion.      B) \$5,782 billion.      C) \$5,325 billion.      D) \$9,000 billion.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

31) The money supply is

- A) the rate at which the Federal Reserve Board prints currency.  
B) limited to currency and coins.  
C) the amount of money in circulation.  
D) the rate at which the Federal Reserve Board creates money.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

32) The largest component of M1 is

- A) currency and coins.
- B) traveler's checks.
- C) transaction deposits.
- D) time deposit.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

33) The best measure of money is

- A) coins and currency.
- B) the one based on the transactions approach.
- C) the one based on the liquidity approach.
- D) something economists have never agreed on.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

34) The transactions approach to measuring money relies on the role of money primarily as a

- A) medium of exchange.
- B) unit of account.
- C) temporary store of value.
- D) standard of deferred payment.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

35) A method of measuring the money supply by looking at money as a medium of exchange is the

- A) fiduciary monetary system.
- B) capital control.
- C) transactions approach.
- D) liquidity approach.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

36) A method of measuring the money supply by looking at money as a temporary store of value is the

- A) fiduciary monetary system.
- B) capital control.
- C) transactions approach.
- D) liquidity approach.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 37) The liquidity approach to measuring money stresses the role of money as a
- A) medium of exchange.
  - B) unit of account.
  - C) temporary store of value.
  - D) standard of deferred payment.

Answer: C

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 38) The key official definition of the money supply is
- A) only coins and paper currency in circulation.
  - B) only transactions deposits at banks.
  - C) MZM.
  - D) M2.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 39) The money supply that consists of currency, transaction deposits, and traveler's checks is
- A) M1.
  - B) M2.
  - C) the fiduciary monetary system.
  - D) the liquidity approach.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 40) Transaction deposits
- A) are deposits in a thrift institution or a commercial bank on which a check may be written.
  - B) are only deposits that you can check on through the Internet.
  - C) include savings accounts.
  - D) are accounts that pay interest to the depositor.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Traveler's check are
- A) part of M1 only.
  - B) part of M2 only.
  - C) part of M1 and M2.
  - D) not part of M1 or M2.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 42) If the transactions approach to measuring money is used, then the money supply consists of
- A) currency only.
  - B) transaction deposits only.
  - C) currency and transaction deposits only.
  - D) currency, checkable and debitable deposits, and traveler's checks.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 43) Which of the following is NOT included in the money supply when the transactions approach is used?
- A) Money market deposit accounts.
  - B) Traveler's checks.
  - C) Transaction deposits.
  - D) Currency.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 44) Which of the following is NOT included in M1?
- A) Currency.
  - B) Transaction deposits.
  - C) Saving deposits.
  - D) Traveler's checks.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 45) Currency consists of
- A) only coins minted by the U.S. Treasury.
  - B) only Federal Reserve notes.
  - C) coins minted by the U.S. Treasury and Federal Reserve notes.
  - D) coins, Federal Reserve Notes and traveler's checks.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

| Component                                               | Amount<br>(Billions of Dollars) |
|---------------------------------------------------------|---------------------------------|
| Currency                                                | \$250                           |
| Coins                                                   | 50                              |
| Transaction Deposits                                    | 600                             |
| Savings Deposits                                        | 450                             |
| Traveler's Checks                                       | 10                              |
| Small Denomination Time Deposits                        | 1,200                           |
| Money Mkt Mutual Fund Shares                            | 500                             |
| Over Night Eurodollars                                  | 20                              |
| Over Night Repurchase<br>Agreements at Commercial Banks | 65                              |
| Available Credit on Credit Cards                        | 900                             |
| Large Time Deposits                                     | 2,500                           |

46) Refer to the above table. The value of M1 is

- A) \$860 billion.      B) \$910 billion.      C) \$1,360 billion.      D) \$2,560 billion.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

47) The liquidity approach to measuring the money supply uses

- A) M1 only.      B) near moneys only.  
C) M1 plus some highly liquid assets.      D) M2 plus some highly liquid assets.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

48) An interest-earning account that can be withdrawn at any time without payment of a penalty is  
a

- A) savings deposit.      B) money market deposit account.  
C) time deposit.      D) certificate of deposit.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 49) An account issued by banks yielding a market rate of interest with a minimum balance requirement and a limit on transactions is a
- A) savings deposit.
  - B) money market deposit account.
  - C) time deposit.
  - D) certificate of deposit.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 50) A deposit in a financial institution that requires notice of intent to withdraw is a
- A) savings deposit.
  - B) money market deposit account.
  - C) time deposit.
  - D) certificate of deposit.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 51) Which of the following is a time deposit with a fixed maturity date offered by banks and other financial institutions?
- A) Savings deposit
  - B) Money market deposit account
  - C) Time deposit
  - D) Small-denomination certificate of deposit

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

- 52) Small-denomination time deposits are less than
- A) \$1 million.
  - B) \$100,000.
  - C) \$10,000.
  - D) \$1,000.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB:

Question Status: Previous Edition

- 53) U.S. paper currency is issued by the
- A) United States Mint.
  - B) Federal Reserve System.
  - C) U.S. Treasury.
  - D) largest commercial banks.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB:

Question Status: Previous Edition

|                                       |         |
|---------------------------------------|---------|
| Outstanding U.S. Treasury Bills       | \$900   |
| Currency in Circulation               | \$500   |
| Money Market Deposits Accounts        | \$300   |
| Small Denomination Time Deposits      | \$600   |
| Transaction Deposits                  | \$1,000 |
| Stock Market Shares                   | \$1,000 |
| Money Market Mutual Funds Balances    | \$500   |
| Savings Deposits                      | \$400   |
| Traveler's Checks Not Issued by Banks | \$200   |

54) Based on the information in the above table, the value of M1 is

- A) \$2,100.                      B) \$1,700.                      C) \$3,000.                      D) \$3,100.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

55) Using the information in the above table, the value of M2 is

- A) \$3,500.                      B) \$2,100.                      C) \$4,500.                      D) \$5,400.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

56) The M1 definition of the money supply includes all of the following EXCEPT

- A) currency.                                              B) transaction deposits.  
C) savings accounts.                                              D) travelers checks.

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

57) In defining money as M1, economists exclude time deposits because

- A) they have no intrinsic value.  
B) they do not directly serve as a medium of exchange.  
C) they are not recognized as legal tender.  
D) they earn an interest for their holders.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 58) If people withdraw \$10 million from the nation's money market mutual funds and redeposit the funds in various checkable and debitable accounts, then
- A) M1 and M2 will remain unchanged.
  - B) M1 will increase, M2 will remain unchanged.
  - C) M1 will increase, M2 will decrease.
  - D) M1 and M2 will increase.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

- 59) In defining money according to the transactions approach, you would want to include
- A) those assets that are used as a store of value.
  - B) those assets that are used as a medium of exchange.
  - C) those assets that are used as a unit of account.
  - D) those assets that are used as a standard of deferred payment.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 60) Which one of the following is true?
- A) Transaction deposits are counted in M2 but are not included in M1.
  - B) Most of the U.S. currency in existence circulates outside U.S. borders.
  - C) Traveler's checks are not considered to be money because they are not valid unless signed.
  - D) Balances in money market deposit accounts are counted in M1 but are not included in M2.

Answer: B

Diff: 3

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 61) The M1 measure of money is suggested by the \_\_\_\_\_ approach to measuring money.
- A) investment
  - B) liquidity
  - C) transactions
  - D) security

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

- 62) The M2 measure of money is suggested by the \_\_\_\_\_ approach to measuring money.
- A) investment
  - B) liquidity
  - C) transactions
  - D) security

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

63) Which one of the following is included in M2 but NOT in M1?

- A) coins and currency
- B) transaction deposits
- C) a savings deposit without a set maturity
- D) large-denomination time deposits

Answer: C

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

64) Which of the following is NOT included in the M1 money supply?

- A) currency
- B) passbook savings accounts
- C) checkable and debitable accounts
- D) traveler's checks

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

65) Which of the following is included in M2 but NOT in M1?

- A) small-denomination time deposits
- B) transaction deposits
- C) currency
- D) traveler's checks

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

66) The M2 money supply is equal to the M1 money supply plus

- A) small time deposits, savings deposits, and retail money market mutual fund shares.
- B) all credit card balances and retail money market mutual fund shares.
- C) large time deposits and retail money market mutual fund shares.
- D) every account held by commercial banks.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

67) Small-denomination certificates of deposits are

- A) included in M1 but not M2.
- B) included in M1 and M2.
- C) included only in M1.
- D) included in M2 but not M1.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

68) The narrowest definition of the money supply is

- A) M1.
- B) M2.
- C) the difference between M2 and M1.
- D) the sum of M1 and M2.

Answer: A

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

69) Money market mutual funds are funds pooled by

- A) a group of people to buy shares of stocks.
- B) a group of people to buy stock market funds.
- C) a group of people to buy short maturity credit instruments.
- D) a group of people to buy U.S. Treasury bonds.

Answer: C

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

70) For a small-denomination certificate of deposit to be included in M2 it must be a denomination of less than

- A) \$1,000,000.
- B) \$100,000.
- C) \$10,000.
- D) \$1,000.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Revised

71) Which of the following assets are counted in M1?

- A) transaction deposits
- B) mutual funds accounts
- C) bonds
- D) line of credit

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

72) Which of the following assets are counted in M2?

- A) gold
- B) balances in retail mutual funds accounts
- C) value of outstanding bonds
- D) lines of credit offered by commercial banks

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

73) Suppose your \$50,000 certificate of deposit matures and you transfer the funds to your checking account. This causes

- A) M1 to decrease by \$50,000 and M2 to increase by \$50,000.
- B) M1 to increase by \$50,000 and M2 to remain the same.
- C) both M1 and M2 to increase by \$50,000.
- D) no change to either M1 or M2.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

74) Which of the following is NOT included in M1?

- A) transaction deposits
- B) currency
- C) small time deposits
- D) travelers checks

Answer: C

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

75) The largest component of M1 is

- A) transaction deposits.
- B) currency and coins.
- C) travelers checks.
- D) savings accounts.

Answer: B

Diff: 2

Topic: 15.3 Defining Money

AACSB:

Question Status: Previous Edition

76) Checking accounts are included in

- A) certificates of deposit.
- B) currency.
- C) lines of credit.
- D) M1.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

77) A checking account balance in a commercial bank is

- A) part of the currency supply.
- B) a time deposit.
- C) not liquid enough to be considered money.
- D) an asset readily usable for most transactions.

Answer: D

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

78) A transaction deposit is

- A) a fiduciary monetary system.
- C) opportunity cost.

- B) a checkable and debitable account.
- D) the liquidity approach.

Answer: B

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

79) Federal Reserve notes are

- A) paper currency.
- C) checks issued by the U.S. government.

- B) savings bonds.
- D) travelers' checks.

Answer: A

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

80) For the United States, what is money based on the transactions approach to measuring money?

Answer: The transactions approach looks at what is used as a medium of exchange. For the United States, this includes currency, transaction deposits, and traveler's checks.

Diff: 1

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

81) How does the liquidity approach to measuring the money supply differ from the transaction approach?

Answer: The liquidity approach focuses on assets that can be converted into money quickly and without loss of nominal value while the transaction approach only looks at assets that are used as a medium of exchange. People can earn some interest with these assets and still convert them to money easily and cheaply.

Diff: 2

Topic: 15.3 Defining Money

AACSB: Analytic skills

Question Status: Previous Edition

## 15.4 Financial Intermediation and Banks

1) The financial institutions in our banking system are all in the business of transferring funds from savers to investors. This process is known as

- A) lobbying.
- C) money laundering.

- B) parachuting.
- D) financial intermediation.

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 2) Suppose you place your savings in a time deposit at the bank, and that bank lends some of those funds to a business that desires a loan. This is an example of
- A) direct finance.  
B) indirect finance.  
C) asymmetric information.  
D) adverse selection.

Answer: B

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Revised

- 3) An item to which a business holds legal claim is called a(n)  
A) asset. B) liability. C) loan. D) time deposit.

Answer: A

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 4) A checkable and debitable account is
- A) a liability to a commercial bank.
  - B) an asset to a commercial bank.
  - C) a liability to the household or firm that has the account.
  - D) an asset for the Federal Reserve System.

Answer: A

*Diff: 2*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 5) Financial institutions participate in which of the following activities?
- A) financial intermediation                      B) indirect finance  
C) the issuance of loans                        D) all of the above

Answer: D

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 6) Financial intermediation is best defined as the process by which
- A) inflation is controlled.
  - B) corporations issue new stock.
  - C) liabilities are liquidated.
  - D) financial institutions accept savings from savers and make loans to investors.

Answer: D

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

*Question Status: Previous Edition*

- 7) Financial intermediaries are institutions that
- A) produce money for the federal government.
  - B) regulate the activities of stock and bond markets.
  - C) act as middlemen in the process of directing funds from savers to investors.
  - D) oversee the activities of government institutions such as the Federal Reserve.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Financial intermediaries are important because
- A) they bring lenders and borrowers together in a way that lowers transaction costs.
  - B) they provide large funds to the stock market.
  - C) they employ large numbers of people.
  - D) they increase costs for banks.

Answer: A

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Suppose that a new customer opens a checking account and a saving account, placing \$50,000 in each. Later, the bank makes a loan of \$100,000 to a business firm. For this bank,
- A) assets increased by \$50,000 because the saving account is an asset, while liabilities increased by \$50,000 because the checking account is a liability.
  - B) assets increased by \$100,000 because the checking and saving accounts are assets, and liabilities increased by \$100,000 because the loan is a liability.
  - C) assets increased by \$100,000 because the loan is an asset, and liabilities increased by \$100,000 because the checking and saving accounts are liabilities.
  - D) assets remained unchanged but liabilities increased by \$100,000 because of the loan.

Answer: C

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 10) Which of the following is NOT an example of a financial intermediary?
- A) A credit union
  - B) A pension fund
  - C) The Internal Revenue Service
  - D) An insurance company

Answer: C

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 11) The term "depository institution" refers to
- A) commercial banks only.
  - B) credit unions only.
  - C) savings and loan associations only.
  - D) commercial banks, credit unions, and savings and loan associations.

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 12) A business owner applies for a bank loan to launch a fairly low-risk project. After receiving the loan, she cancels the low-risk project and instead uses the borrowed funds for a high-risk venture. This is an example of
- A) financial intermediation.
  - B) the transactions approach.
  - C) moral hazard.
  - D) capital controls.

Answer: C

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 13) If knowledge possessed by one party in a financial transaction is not known to the other party, \_\_\_\_\_ exists.
- A) disintermediation
  - B) asymmetric information
  - C) fraud
  - D) no financial intermediation

Answer: B

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 14) Who benefits from the process of financial intermediation?
- A) Savers only.
  - B) Borrowers only.
  - C) Both savers and borrowers.
  - D) There is no benefit, because money does not create wealth.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 15) Asymmetric information is a situation in which
- A) information possessed by one party in a transaction is not known by another party.
  - B) information possessed by one party in a transaction is also known by another party.
  - C) the government has information that it chooses to pass along to private firms.
  - D) private firms have information that they choose to pass along to the government.

Answer: A

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 16) The process in which financial institutions accept savings from businesses, households, and governments and lend the funds to other businesses, households, and governments is called
- A) central banking system.
  - B) financial intermediation.
  - C) moral hazard.
  - D) adverse selection.

Answer: B

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 17) A central bank is
- A) the largest bank in the country.
  - B) the largest bank in the country's capital.
  - C) a banker's bank.
  - D) an international bank.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 18) Financial intermediaries are institutions that
- A) create money.
  - B) provide checking accounts.
  - C) set interest rates.
  - D) transfer funds in the form of loans from savers to investors.

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 19) All of the following are examples of financial intermediaries EXCEPT
- A) credit unions.
  - B) insurance companies.
  - C) retirement funds.
  - D) stock exchanges.

Answer: D

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 20) Possession of information by one party in a financial transaction but not by the other party is
- A) asymmetric information.
  - B) symmetric information.
  - C) informational hazard.
  - D) financial intermediation.

Answer: A

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 21) Two people are involved in a borrower/lender situation, and one person has superior knowledge of its own current and future prospects over the other person. This is known as
- A) preventable information.
  - B) symmetric information.
  - C) asymmetric information.
  - D) deceptive knowledge.

Answer: C

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 22) The likelihood that individuals who seek to borrow money may use the funds for unworthy, high-risk projects is
- A) asymmetric information.
  - B) adverse selection.
  - C) moral hazard.
  - D) financial intermediation.

Answer: B

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 23) The possibility that a borrower might engage in riskier behavior after a loan has been obtained is
- A) asymmetric information.
  - B) adverse selection.
  - C) moral hazard.
  - D) financial intermediation.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Russia borrowed funds from the International Monetary Fund in 1989 in exchange for agreeing to undertake certain changes. However, after receiving the funds, Russia spent the funds on other things, making the loan repayment more unlikely to occur. This situation is referred to as
- A) adverse selection.
  - B) moral hazard.
  - C) asymmetric information.
  - D) deceptive knowledge.

Answer: B

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 25) The process by which financial institutions accept savings from businesses, households and governments and lend the savings to other businesses, households and governments is

A) asymmetric information.                      B) adverse selection.  
C) moral hazard.                                  D) financial intermediation.

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 26) When you deposit funds in a bank and then the bank lends these funds to a borrower, the bank is engaged in

A) fiduciary investment.                      B) fraudulent behavior.  
C) universal banking.                          D) financial intermediation.

Answer: D

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 27) Which of the following is NOT an asset of commercial banks?

A) consumer loans                              B) business loans  
C) savings deposits                              D) home mortgages

Answer: C

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 28) People with savings often deposit their funds in a commercial bank, rather than investing them directly with business enterprises, in order to

A) avoid the problems associated with financial intermediation.  
B) avoid the problems associated with asymmetric information.  
C) earn the highest possible return for taking on the riskiest investments.  
D) All of the above are correct.

Answer: B

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 29) From an accounting point of view, a checking account should be considered part of a bank's

A) assets.                                          B) liabilities.                                          C) profits.                                          D) reserves.

Answer: B

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

30) Which of the following is NOT a description of indirect finance?

- A) You take out a student loan from your bank.
- B) An insurance company lends funds to IBM.
- C) You borrow \$500 from your best friend.
- D) You buy shares in a mutual fund.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Revised

31) Which of the following is a financial intermediary?

- A) the Red Cross
- B) the Internal Revenue Service
- C) a share of corporate stock
- D) an insurance company

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

32) Which of the following is NOT a financial intermediary?

- A) commercial banks
- B) a savings and loan association
- C) the Federal Reserve Bank of New York
- D) the Internal Revenue Service

Answer: D

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

33) Let us suppose that you apply for a loan with a bank. You tell the bank that you are going to remodel your kitchen, but after you get the loan you go to Las Vegas to gamble with the money. Your behavior is an example of

- A) adverse selection.
- B) direct credit allocation.
- C) moral hazard.
- D) indirect credit allocation.

Answer: C

Diff: 3

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

34) The function that banks perform by obtaining funds from households, businesses, and governments and lending these funds to other households, businesses, and governments is known as

- A) financial intermediation.
- B) lending intermediation.
- C) fiscal intermediation.
- D) liquidity intermediation.

Answer: A

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

35) Which of the following is NOT a reason that people tend to deposit their funds with banks rather than lend their funds directly to other individuals?

- A) adverse selection problems
- B) asymmetric information problems
- C) moral hazard problems
- D) liquidity problems

Answer: D

Diff: 3

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Revised

36) Adverse selection refers to the

- A) possibility that the borrower may engage in riskier behavior after the loan is obtained.
- B) likelihood that a potential borrower may use the funds that he receives for unworthy, high risk projects.
- C) possession of information by one party in a financial transaction not known by the other party.
- D) use of statistical discrimination in making loans.

Answer: B

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

37) The possibility that a borrower might engage in riskier behavior after a loan is made is called

- A) adverse selection.
- B) liability aversion.
- C) moral hazard.
- D) the risk of default.

Answer: C

Diff: 1

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

38) Which of the following describes a moral hazard problem?

- A) a process by which individuals have substantial resources devoted to the exchange process and need to make a profit or they will be adversely affected
- B) a post-contractual problem that may result because participants to the exchange process have information that allows them to act in an opportunistic manner
- C) a process by which individual buyers or sellers with better information are more likely to participate in voluntary exchange
- D) a contractual problem that results because monopolies exist in all economies

Answer: B

Diff: 3

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 39) Suppose you and a friend are shopping at a swap meet and you borrow \$500 from your friend to pay for a guitar that you see there. This is an example of
- A) direct financing.
- B) indirect financing.
- C) moral hazard.
- D) transaction costs.

Answer: A

*Diff:* 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 40) Suppose you borrow \$500 from your bank to pay for a guitar. This is an example of
- A) direct financing.  
B) indirect financing.  
C) moral hazard.  
D) transaction costs.

Answer: B

*Diff: 2*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Financial institutions that receive most of their funds from the savings of the public are
- A) the fiduciary monetary system.                      B) the world index fund.
- C) universal banking.                                        D) thrift institutions.

Answer: D

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

*AACSB:*

Question Status: Previous Edition

- 42) When you use a debit card to purchase a pair of jeans, you are
- A) creating a 30-day loan from your bank to the seller.
  - B) creating a 30-day loan from the seller to your bank.
  - C) giving your bank an instruction to transfer funds directly from your bank account to the store's bank account.
  - D) creating an overnight repurchase agreement between your bank and the store.

Answer: C

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

*Question Status: Previous Edition*

- 43) When you make a purchase at a retail store by giving your bank an instruction to transfer funds directly from your bank account to the store's bank account, you have most likely made the purchase using
- A) cash.                      B) a loan.                      C) a debit card.                      D) credit.

Answer: C

*Diff: 1*

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: New

44) Explain the role of financial intermediation.

Answer: Financial intermediation is the process by which financial institutions accept savings from households and lend the savings to households, businesses, and the government. It is a middleman role that brings savers and borrowers together.

Diff: 2

Topic: 15.4 Financial Intermediation and Banks

AACSB: Analytic skills

Question Status: Previous Edition

## 15.5 The Federal Reserve System: The U.S. Central Bank

1) The central bank for the United States is

A) Chase Manhattan Bank.

B) the Congressional Bank.

C) the Federal Reserve System.

D) First National Bank of New York.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

2) The current chair of the Board of Governors of the Federal Reserve is

A) Alan Greenspan.

B) John Snow.

C) Ben Bernanke.

D) Henry Paulson.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

3) Which of the following is true of the Federal Reserve System?

I. It was established in the early 1980s.

II. It serves as the central bank of the United States.

A) I only

B) II only

C) Both I and II

D) Neither I nor II

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

4) The Federal Open Market Committee (FOMC)

A) determines the tax policy of the government.

B) influences the future growth of the money supply.

C) oversees all transactions on the stock market.

D) lends to the least credit-worthy customers.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 5) The part of the Federal Reserve System that determines monetary policy actions is the
- A) District Bank Board.
  - B) Federal Deposit Insurance Corporation (FDIC).
  - C) Federal Open Market Committee.
  - D) Comptroller's Office.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 6) The Board of Governors of the Federal Reserve System is
- A) elected by the general public.
  - B) composed of seven members who are appointed by the President and approved by the Senate.
  - C) composed of representatives from the country's 12 largest commercial banks.
  - D) composed of 12 members of the Senate and the U.S. House of Representatives.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 7) Monetary policy actions are determined by the
- A) Federal Open Market Committee.
  - B) New York Federal Reserve Bank.
  - C) President of the United States.
  - D) U.S. Congress.

Answer: A

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Who appoints the Federal Reserve System's Board of Governors?
- A) The Secretary of the Treasury
  - B) The President of the United States
  - C) The Speaker of the House of Representatives
  - D) The American Banking Association

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

9) Which of the following is NOT a part of the Federal Reserve System?

- A) The Twelve District Federal Reserve banks
- B) The Federal Open Market Committee
- C) The Federal Deposit Insurance Corporation
- D) The Board of Governors

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

10) The Board of Governors of the Federal Reserve System is

- A) appointed by the Congress.
- B) elected by the public.
- C) appointed by the President with approval of the U.S. Senate.
- D) elected by members of the American Banking Association.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

11) Which of the following is NOT a function of the Federal Reserve System?

- A) The Fed holds reserves of depository institutions.
- B) The Fed supplies the economy with fiduciary currency.
- C) The Fed determines government spending and taxation policies.
- D) The Fed acts as fiscal agent for the United States Department of the Treasury.

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

12) Which of the following is NOT a function of the Fed?

- A) Regulating the money supply in the economy
- B) Offering checking accounts to the U.S. public
- C) Acting as government's fiscal agent
- D) Providing a system of check collection and clearing for depository institutions

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

13) Which of the following is NOT a function of the Fed?

- A) Holding reserves for depository institutions
- B) Supervising member banks
- C) Regulating the money supply
- D) Lending funds to credit-worthy private firms

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

14) Which of the following is NOT a function of the Federal Reserve System?

- A) Providing for check collection and clearing
- B) Holding deposits of member banks
- C) Supervising member banks
- D) Making loans to college students

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

15) Regarding the nation's money supply, the Federal Reserve

- A) has no ability to influence its magnitude or its rate of growth.
- B) precisely sets the amount of money in circulation in consultation with the Congress.
- C) can influence its future growth.
- D) gives the U.S. Treasury the authority to print as much as it wishes.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

16) Which of the following statements is correct?

- I. The Fed can periodically and without warning examine member commercial banks to ensure that they are conforming to current banking standards.
- II. The Fed helps the government collect certain tax revenues and aids in the purchase and sale of government securities.

- A) I only
- B) II only
- C) Both I and II
- D) Neither I nor II

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 17) The Fed is said to be the "lender of last resort" in that
- A) it stands ready to lend to any depository institution that it has decided should not fail.
  - B) it makes loans to individuals whom commercial banks do not believe are credit-worthy.
  - C) it charges a higher interest rate to borrowers than does any other bank.
  - D) it functions as the government's bank only when commercial banks fail to do so.

Answer: A

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 18) All of the following are functions of the Federal Reserve System EXCEPT
- A) supplying the economy with fiduciary currency.
  - B) providing a system of check collection and clearing.
  - C) acting as the government's fiscal agent.
  - D) lending funds to risky customers denied credit by commercial banks.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 19) It is widely believed that the Federal Reserve's most important function is
- A) to provide loans to the federal government.
  - B) to regulate the money supply.
  - C) to set the legal, controlled consumer interest rates.
  - D) to lend to risky customers.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

- 20) Which of the following is NOT a function of the Federal Reserve System?
- A) Regulating the money supply
  - B) Making loans to households and businesses
  - C) Acting as the fiscal agent of the federal government
  - D) Supervising member banks

Answer: B

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

- 21) The Federal Reserve System acts as the government's fiscal agent by
- A) auditing taxpayers.
  - B) providing checking account services for the government.
  - C) preparing the budget the President presents to Congress every year.
  - D) determining how to finance a deficit.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 22) Which of the following is NOT a correct statement about the Federal Reserve banks?
- A) They supervise member banks within the Federal Reserve System.
  - B) They provide a system of check collection and clearing.
  - C) They provide the economy with gold backed currency.
  - D) They act as banker and fiscal agent for the U.S. government.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 23) A "banker's bank" is another name for
- A) a financial intermediary.
  - B) a government bank.
  - C) a central bank.
  - D) the Federal Depository Insurance Agency.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Which of the following is the central bank for the United States?
- A) the Federal Deposit Insurance Corporation (FDIC)
  - B) the United States Treasury
  - C) the Comptroller of the Currency
  - D) none of the above

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

25) The U.S. central bank performs all the following roles for the nation EXCEPT

- A) performing banking functions for their nations' governments.
- B) lending funds directly to the public.
- C) providing financial services for private banks.
- D) conducting their nations' monetary policies.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

26) The Federal Reserve System was established in which year?

- A) 1865.
- B) 1913.
- C) 1929.
- D) 1941.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

27) The Board of Governors of the Federal Reserve System has how many governors?

- A) 1.
- B) 5.
- C) 7.
- D) 12.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

28) All of the following are functions of the Federal Reserve System EXCEPT

- A) to provide loans to developing countries.
- B) to supply the economy with fiduciary currency.
- C) to hold depository institutions' reserves.
- D) to act as the government's fiscal agent.

Answer: A

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

29) By serving as the lender of last resort,

- A) the Fed provides check clearing services.
- B) the Fed supervises depository institutions.
- C) the Fed can prevent bank failures.
- D) the Fed aids in the sale of government securities.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

30) The Federal Reserve System is divided into how many districts?

- A) 1                      B) 5                      C) 7                      D) 12

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

31) Control of the money supply is handled by

- A) Congress.  
B) the Federal Reserve System.  
C) all commercial banks.  
D) Congress and all member commercial banks.

Answer: B

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

32) Depository institutions must

- A) use and pay for the services of the Federal Reserve System.  
B) set their interest rates according to schedules established by the Federal Reserve System.  
C) keep a certain percentage of their deposits as reserves.  
D) turn over a percentage of their profits to the Federal Reserve System as payment for services provided by the Fed.

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

33) The Fed

- A) is responsible for minting coins.  
B) distributes Federal Reserve notes, which are paper currency.  
C) is responsible for conducting U.S. fiscal policy.  
D) has 15 Federal Reserve banks and governing boards in New York and Chicago.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 34) Which of the following is responsible for the distribution of paper currency in the United States?
- A) the U.S. Treasury
  - B) the Office of the Comptroller of the currency
  - C) the Federal Reserve
  - D) all of the above

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 35) Check collection and clearing happen
- A) at the bank where the check was written.
  - B) only at private clearing centers.
  - C) at the Fed and at private clearing centers.
  - D) only at the Fed.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 36) Which of the following is NOT true about the duties the Fed performs for the federal government?
- A) The Federal Reserve is the banker and fiscal agent of the federal government.
  - B) The U.S. Treasury controls the Fed.
  - C) The Federal Reserve aids in the purchase and sale of certain government securities.
  - D) The U.S. Treasury has a checking account at the Fed.

Answer: B

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 37) As a "lender of last resort," the Fed
- A) is obligated to bail out any depository institution in the country that is in financial difficulty.
  - B) protects the deposits of \$100,000 or less in all commercial banks in the country.
  - C) provides loans to banks experiencing temporary liquidity problems.
  - D) bails out any corporation the government has decided should not fail.

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 38) The most important function of the Fed is to
- A) provide a system for collecting and clearing checks.
  - B) collect taxes.
  - C) support the federal government's deficit spending by buying government securities.
  - D) regulate the money supply.

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Revised

- 39) All of the following are functions of the Fed EXCEPT
- A) providing paper currency.
  - B) enforcing international trade agreements.
  - C) serving as a mechanism for clearing checks.
  - D) the banker and fiscal agent for the government.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 40) Which of the following depository institutions is NOT regulated by a government agency?
- A) Savings and loan associations
  - B) Credit unions
  - C) Commercial banks that are not part of the Federal Reserve System
  - D) None of the above: All depository institutions are regulated by some government agency

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Which of the following is solely responsible for determining changes in the money supply in the United States?
- A) the U.S. Treasury
  - B) the Comptroller of the Currency
  - C) the Federal Open Market Committee
  - D) the chairman of the Federal Reserve

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 42) Which one of the following is a function of the Federal Reserve System?
- A) providing the economy with currency
  - B) providing a system for check clearing
  - C) serving as a lender of last resort
  - D) all of the above

Answer: D

Diff: 3

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

43) Why might the Federal Reserve intervene in foreign currency markets?

- A) to ensure the safety of overseas investments for banks
- B) to ensure the safety of overseas investments for private investors
- C) to ensure the safety of overseas investments for pension funds
- D) to maintain a desired exchange rate for the dollar

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

44) The Federal Reserve Bank was first established in the U.S. by an Act of Congress passed in

- A) 1789.
- B) 1861.
- C) 1913.
- D) 1947.

Answer: C

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

45) The Board of Governors of the Federal Reserve System has

- A) 7 members serving 14 year terms.
- B) 7 members serving 4 year terms.
- C) 12 members serving 14 year terms.
- D) 12 members serving 4 year terms.

Answer: A

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

46) The Federal Reserve System has

- A) 7 district banks.
- B) 12 district banks.
- C) 24 district banks.
- D) 50 district banks.

Answer: B

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

47) How many Federal Reserve district banks are there in the United States?

- A) 1
- B) 5
- C) 7
- D) none of the above.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

48) The fiscal agent for the federal government is

- A) the United States Treasury.
- B) the United States Treasurer.
- C) the Comptroller of Currency.
- D) the Federal Reserve System.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

49) A major function of the Federal Reserve System is

- A) the implementation of fiscal policy for the federal government.
- B) the control of the money supply.
- C) the control of government spending.
- D) the control of taxing policy.

Answer: B

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

50) Which of the following is NOT a function of the Federal Reserve System?

- A) supply fiduciary currency to the economy
- B) provide a system for check collection and clearing
- C) implement fiscal policy
- D) regulate the money supply

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

51) Who appoints the chair of the Federal Reserve System?

- A) the Senate and Congress
- B) member banks of the Federal Reserve System
- C) the President of the United States
- D) the Federal Open Market Committee (FOMC)

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

52) The part of the Federal Reserve System (the Fed) that sets reserve requirements is

- A) the Federal Open Market Committee.
- B) the Federal Advisory Committee.
- C) the Federal Reserve district banks.
- D) the Board of Governors.

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 53) The part of the Federal Reserve System (the Fed) that holds the reserve balances of depository institutions is

A) the Federal Open Market Committee.                      B) the Federal Advisory Committee.  
C) the Federal Reserve district banks.                      D) the Board of Governors.

Answer: C

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 54) The part of the Federal Reserve System (the Fed) that directs the buying and selling of U.S. government securities is

A) the Federal Open Market Committee.                      B) the Federal Advisory Committee.  
C) the Federal Reserve district banks.                      D) the Board of Governors.

Answer: A

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 55) The part of the Federal Reserve System (the Fed) that supervises and regulates member banks is

A) the Federal Open Market Committee.                      B) the Federal Advisory Committee.  
C) the Federal Reserve district banks.                      D) the Board of Governors.

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 56) All of the following are functions of the Federal Reserve System (the Fed) EXCEPT

A) supplying currency.                      B) check clearing.  
C) regulation of the money supply.                      D) lender of last resort for consumers.

Answer: D

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 57) Federal Reserve notes are

A) a liability of the Federal Reserve System.  
B) an asset to the Federal Reserve System.  
C) both an asset and a liability to the Federal Reserve System.  
D) a liability to the United States Treasury.

Answer: A

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

58) The potential for a financial breakdown at large institutions to spread throughout the financial system is called

- A) a systemic risk.
- B) a too-large-to-fail problem.
- C) an adverse selection problem.
- D) a moral hazard.

Answer: A

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: New

59) After the financial crisis of the late 2000s, President Obama and Congress considered adding to the Federal Reserve's functions by making it the nation's primary regulator of

- A) systemic risk.
- B) default risk.
- C) credit risk.
- D) investment risk.

Answer: A

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: New

60) What is the typical role of a central bank?

- A) It serves as a bank for the national treasury.
- B) It regulates depository institutions.
- C) It serves as a lender of last resort.
- D) All of the above.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

61) The potential for a financial breakdown at one financial institution to spread throughout the financial system is known as a

- A) lending risk.
- B) moral hazard.
- C) liquidity risk.
- D) systemic risk.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

62) In 2010, President Obama signed into law that made the Federal Reserve as the nation's

- A) largest private bank.
- B) federal income tax collector.
- C) fiscal policy making unit.
- D) regulator of systemic financial risk.

Answer: D

Diff: 1

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 63) The members of the Federal Open Market Committee are
- A) the Treasury secretary, the head of the Federal Deposit Insurance Corporation, and the Comptroller of the Currency.
  - B) the seven members of the Fed's Board of Governors and five of the Federal Reserve bank presidents.
  - C) the President, the Speaker of the House of Representatives, and the Senate Majority Leader.
  - D) the five top officials at the Federal Reserve Bank of New York's Trading Desk.

Answer: B

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB:

Question Status: Previous Edition

- 64) The Fed is the bankers' bank. What functions of the Fed are involved in this role? What are the other important functions of the Fed?

Answer: The Fed holds reserves of banks, lends to banks when their reserves are low, and provides a system for check collecting and clearing. Other important functions include providing fiduciary currency, acting as the government's fiscal agent, supervising member banks, and regulating the money supply.

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

- 65) In the United States, who determines monetary policy? What is the major tool used to determine monetary policy?

Answer: The Federal Reserve Bank's Federal Open Market Committee determines monetary policy. The committee is made up of the Board of Governors and 5 reserve bank presidents. Their main tool is buying and selling existing U.S. government securities in open markets.

Diff: 2

Topic: 15.5 The Federal Reserve System: The U.S. Central Bank

AACSB: Analytic skills

Question Status: Previous Edition

## 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

- 1) Goldsmiths were able to practice an early form of fractional reserve banking because they knew that
- A) people were relatively unsophisticated in their financial transactions.
  - B) gold was the major form of money.
  - C) not all depositors would claim their gold at the same time.
  - D) gold did not serve as a unit of account.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 2) A system in which depository institutions hold reserves that are less than the amount of total deposits is called
- A) fiat money banking.  
B) fractional reserve banking.  
C) central banking system.  
D) required reserve banking.

Answer: B

*Diff: 1*

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 3) Fractional reserve banking refers to a banking system in which
- A) bank deposits are less than bank reserves.
  - B) bank reserves are only a fraction of total deposits.
  - C) bank reserves are only a fraction of required reserves.
  - D) bank loans are less than bank reserves.

Answer: B

*Diff: 1*

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 4) If banks engage in fractional reserve banking, it means that
- A) they never run short of currency.
  - B) they hold less than 100 percent of their deposits as reserves.
  - C) a fraction of their legal reserves are held as top-grade government securities.
  - D) they do not hold any excess reserves.

Answer: B

*Diff: 1*

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 5) Fractional reserve banking can be thought of as a bank
- A) withholding a portion of its total deposits that are not loaned out.
  - B) holding deposits equal to its net worth.
  - C) paying a fraction of its profit to depositors.
  - D) loaning out all of its reserves.

Answer: A

*Diff: 2*

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 6) In the United States, where do depository institutions hold their reserves?
- A) In their own vaults in the form of precious metals such as gold and silver
  - B) In accounts with the U.S. Department of the Treasury
  - C) Either as vault cash or on reserve with Federal Reserve district banks
  - D) All reserves must be held at a Federal Reserve district bank

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 7) A fractional reserve banking system is a system whereby
- A) banks keep at least 100 percent of their deposits on hand as reserves.
  - B) banks keep only a fraction of their deposits on hand as reserves.
  - C) a central bank tells all banks what fraction of the population they can serve.
  - D) banks specialize so that one type of bank handles one kind of deposit and another type of bank handles another type of deposit.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 8) With fractional reserve banking,
- A) banks can not generate profits.
  - B) monetary policy will be ineffective.
  - C) banks retain only a portion of their deposits in their vaults or at Federal Reserve banks.
  - D) banks can act as securities brokers.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 9) A bank with \$200 million in transaction deposits keeps \$20 million in cash in the bank vault, \$10 million in deposits at the Fed, and \$5 million in government securities in the bank vault. Its total reserves equal
- A) \$10 million.
  - B) \$20 million.
  - C) \$30 million.
  - D) \$35 million.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 10) Banks do not need to keep all of their deposits on hand as reserves because
- A) only a fraction of deposits are withdrawn at any one time.
  - B) FDIC protects banks from excessive withdrawal demands.
  - C) there is too much risk of bank robberies.
  - D) they can always generate new reserves through the money creation process.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 11) Total reserves are
- A) deposits held by Federal Reserve district banks for depository institutions, plus depository institutions' vault cash.
  - B) reserves that a depository institution must hold in the form of vault cash.
  - C) reserves that depository institutions are allowed to claim as reserves.
  - D) any item that legally functions as money.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 12) Deposits held by Federal Reserve district banks for depository institutions, plus depository institutions' vault cash are known as
- A) reserves.
  - B) a sweep account.
  - C) adverse selection.
  - D) the discount rate.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 13) Total reserves of private banks are
- A) all customer deposits.
  - B) deposits held at the Fed and vault cash.
  - C) the minimum amount banks need to hold against time deposits.
  - D) federal reserve notes.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

14) Total reserves are

- A) required reserves plus vault cash.
- B) required reserves plus excess reserves.
- C) required reserves.
- D) excess reserves.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

15) The reserve ratio is 10% and a bank has \$600,000 in transaction deposits. The amount of reserves equals

- A) \$6,000.
- B) \$60,000.
- C) \$600,000.
- D) undeterminable without information on cash reserves.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

16) A bank with \$100 million in deposits has \$15 million of cash in the bank, \$10 million in deposits with the Fed, and \$15 million in government securities in its vault. Its total reserves equal

- A) \$10 million.
- B) \$15 million.
- C) \$25 million.
- D) \$40 million.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

17) Under a fractional reserve banking system,

- A) banks keep a fraction of their deposits on hand as reserves.
- B) banks keep a fraction of their reserves on hand as deposits.
- C) banks keep all of their deposits on hand as reserves.
- D) banks keep all of their reserves on hand as deposits.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

18) A system in which depository institutions hold reserves that are less than the amount of total deposits is

- A) the Federal Reserve System.
- B) the federal funds market.
- C) sweep accounts.
- D) fractional reserve banking.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 19) Jane has just deposited \$2,000 in her checking account. She knows that the bank will keep part of these funds on hand and loan out the rest. This is an example of

A) the Federal Reserve System.                      B) a sweep account.  
C) fractional reserve banking.                      D) excess reserves.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 20) In a fractional reserve banking system,

A) banks are required to keep all deposits on hand so that they can pay their depositors when they desire to withdraw funds.  
B) banks are required to keep a fraction of deposits in bonds.  
C) banks are required to keep a fraction of all deposits on hand and send the rest to the Fed.  
D) banks do not keep sufficient reserves on hand to cover 100 percent of their depositors' accounts.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 21) Fractional reserve banking began

A) in the early twentieth century.                      B) in the early nineteenth century.  
C) in the Middle Ages.                      D) in ancient Greece.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 22) A system in which depository institutions hold reserves that are less than the amount of total deposits is

A) a fractional reserve banking system.                      B) a percentage reserve banking system.  
C) a ratio reserve banking system.                      D) a legal reserve banking system.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 23) The concept of holding reserves, such as gold, that are less than the value of the total deposits
- A) is known as fractional reserve banking.
  - B) has been illegal since the passage of the Financial Services Modernization Act of 1999.
  - C) is known as non-credit banking.
  - D) None of the above are correct.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Fractional reserve banking is a system in which
- A) depository institutions pay a fraction of advertised interest rates.
  - B) a fraction of banking services must be provided by depository institutions.
  - C) depository institutions hold a fraction of total deposits in reserve.
  - D) the money supply is a set fraction of the U.S. gold reserves.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 25) Fractional reserve banking refers to a system in which the depository institution
- A) holds reserves equal to its deposits.
  - B) holds reserves greater than its deposits.
  - C) holds reserves less than its deposits.
  - D) holds zero reserves.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 26) A statement of assets and liabilities of any business entity is called
- A) an income statement.
  - B) a cash flow statement.
  - C) a balance sheet.
  - D) a statement of net worth.

Answer: C

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 27) Which of the following would NOT be an asset on a bank's balance sheet?
- A) Loans outstanding
  - B) Bank building
  - C) Cash in the vault
  - D) Transactions deposits

Answer: D

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 28) Which of the following actions has *no* effect on the total money supply?
- A) The Federal Open Market Committee buys government securities.
  - B) The Federal Open Market Committee sells government securities.
  - C) There is a transfer of deposits from one bank to another bank.
  - D) There is change in the money multiplier.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 29) Given a required reserve ratio of 20 percent, a commercial bank that has received a new deposit of \$100 can make additional loans of
- A) \$0.
  - B) \$20.
  - C) \$80.
  - D) \$400.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 30) Following a new deposit of \$500, the loans of a commercial bank increase by \$400. In this situation, the reserve ratio is most likely
- A) 0 percent.
  - B) 20 percent.
  - C) 80 percent.
  - D) 180 percent.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 31) The reserve ratio is 10 percent. If the bank receives a customer deposit of \$100,000, then an immediate effect is
- A) a reduction in the bank's total assets of exactly \$10,000.
  - B) a reduction in the bank's total liabilities of exactly \$10,000.
  - C) no change in the bank's total assets or total liabilities.
  - D) an increase in the bank's reserves of exactly \$10,000.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: New

- 32) Other things being equal, if the reserve ratio is raised from 10 percent to 20 percent,
- A) minimum potential value of the money multiplier rises from 0.10 to 0.20.
  - B) minimum potential value of the money multiplier falls from 100 to 50.
  - C) maximum potential value of the money multiplier rises from 10 to 20.
  - D) maximum potential value of the money multiplier falls from 10 to 5.

Answer: D

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 33) To reach the maximum money multiplier, it is assumed that
- A) commercial banks keep the amount of reserves. equal to total bank deposits.
  - B) all loans get redeposited in a checkable account.
  - C) there is insufficient loan demand.
  - D) loans are diverted into circulating currency.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 34) Which of the following will limit the expansion of the money supply following a new deposit?
- A) Failure of banks to voluntarily hold excess reserves
  - B) A strong demand for new loans
  - C) A re-depositing of all loan proceeds
  - D) A strong demand for holding currency outside of commercial banks

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 35) A statement of assets and liabilities of any business entity is
- A) a sweep account.
  - B) a balance sheet.
  - C) net worth.
  - D) legal reserves.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 36) The difference between assets and liabilities is
- A) a sweep account.
  - B) a balance sheet.
  - C) net worth.
  - D) legal reserves.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 37) A bank currently has \$50 million in deposits, \$6 million in cash in the vault, \$4 million on deposit with the Fed, and \$5 million in government securities. The reserve ratio is 20 percent. A new deposit is made of \$1 million. What is the maximum size loan the bank can make once the check clears?
- A) 0
  - B) \$800,000
  - C) \$1 million
  - D) \$5.8 million

Answer: B

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 38) The reserve ratio is 20 percent. A check for \$1 million is deposited in Bank A, written on an account from Bank B. After the check clears what are the new excess reserves at Bank A, and by how much does the money supply change if all banks make loans so that they have zero excess reserves?

A) \$200,000; \$800,000  
 B) \$800,000; \$1 million  
 C) \$800,000; \$800,000  
 D) \$800,000; 0

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 39) If all of a bank's depositors showed up on one day requesting cash withdrawals of all their deposited funds,

A) the bank would pay them all, although reluctantly.  
 B) the bank would likely fail to have sufficient reserves to honor their requests.  
 C) the bank could lawfully refuse their demands.  
 D) the bank would immediately call all outstanding loans.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 40) Among the liabilities of a bank are its

A) transaction deposits.  
 B) total reserves.  
 C) excess reserves.  
 D) loans.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 41) The balance sheet of a bank shows its

A) profits and losses.  
 B) assets and liabilities.  
 C) earnings and expenses.  
 D) revenues and costs.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 42) If a bank receives a new transaction deposit of \$100,000 and the reserve ratio is 20 percent, then the bank could expand its loans by as much as

A) \$20,000.  
 B) \$80,000.  
 C) \$100,000.  
 D) \$400,000.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

43) If a check written on one bank is deposited in another bank

- A) the money supply increases.
- B) the money supply remains unchanged.
- C) the money supply decreases.
- D) new reserves are created for the banking system.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

44) Which of the following is a liability to a bank?

- A) total reserves
- B) transaction deposits
- C) government securities
- D) loans

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

45) If a check was written on Bank A for \$100 and Bank B presented the check to Bank A for payment, what will happen to the required reserves for each respective bank after payment is made?

- A) Bank A's required reserves increase; Bank B's decrease.
- B) Bank B's required reserves increase; Bank A's decrease.
- C) Both banks will see an increase in their required reserves.
- D) Both banks will see a decrease in their required reserves.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

46) Which of the following is NOT an asset of a bank?

- A) cash
- B) loans
- C) total reserves
- D) transaction deposits

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

| Assets       |                    | Liabilities          |                    |
|--------------|--------------------|----------------------|--------------------|
| Reserves     | \$200,000          | Transaction Deposits | \$2,000,000        |
| Securities   | \$200,000          |                      |                    |
| Loans        | \$1,600,000        |                      |                    |
| Total Assets | <u>\$2,000,000</u> | Total Liabilities    | <u>\$2,000,000</u> |

- 47) Based on the above table, the reserve ratio for the banking system is
- A) 20 percent.                      B) 10 percent.                      C) 15 percent.                      D) 1 percent.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 48) Based on the above table, an open market operation in which the Fed purchased \$100,000 of government securities would
- A) create a reserve deficiency for the banking system.  
 B) lead to a maximum potential expansion of the money supply of \$100,000.  
 C) lead to a maximum potential expansion of the money supply of \$1 million.  
 D) cause demand deposits to fall by \$100,000.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 49) The potential money multiplier for the banking system in the above table is
- A) 5.                                      B) 9.                                      C) 1.                                      D) 10.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 50) When the Federal Reserve sells a government security to a commercial bank,
- A) the cash reserves of the commercial bank decrease.  
 B) the net worth of the commercial bank increases.  
 C) the loans of the commercial bank will increase.  
 D) the balance sheet of the commercial bank is thrown off balance.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 51) If a \$1 million open market purchase by the Fed generates a new deposit at a bank that immediately causes the bank's reserves held at the Fed to increase by \$1 million, then the T-account effects are that the bank's assets and liabilities \_\_\_\_\_ by \$1 million and that the Fed's assets and liabilities \_\_\_\_\_ by \$1 million.

A) decline; decline  
B) increase; decline  
C) decline; increase  
D) increase; increase

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 52) The Fed sells a U.S. government security and a bank dealer writes a check for the amount. When the check clears,

A) reserves remain unchanged because the decrease of reserves at the dealer's bank is offset by an increase in the reserves at the Fed.  
B) reserves have fallen by the amount of the check because the Fed clears the check by reducing the bank's deposits at the Fed.  
C) reserves increase by the amount of the check because the Fed clears the check by increasing the amount of the bank's deposits with the Fed.  
D) reserves have fallen by the amount of the reserves times the reserve ratio, and the money supply falls by the difference between the amount of the check and the fall in the reserves.

Answer: B

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 53) The reserve ratio is 10 percent and all loan proceeds are deposited in transactions accounts. A bond dealer has \$100 million in deposits, \$8 million in vault cash, and \$7 million in deposits at the Fed. The Fed sells \$1 million in securities to the bond dealer. As a result, of this transaction alone,

A) the money supply falls by \$1 million and total reserves fall by \$1 million.  
B) the money supply falls by \$1 million and total reserves rise by \$1 million.  
C) the money supply rises by \$1 million, total reserves fall by \$900,000.  
D) the money supply rises by \$1 million, but reserves do not change.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 54) Suppose that the actual money multiplier equals the maximum potential money multiplier. If the reserve ratio is 10 percent, in order for the banking system to increase deposits by \$2.5 million, the Fed must
- A) permit the system to have prolonged reserve deficiencies.
  - B) sell \$2.5 million of government securities to the general public.
  - C) sell \$250,000 of government securities to the general public.
  - D) buy \$250,000 of government securities from the public.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 55) The Federal Open Market Committee has responsibility for
- A) appointing members to the Board of Governors of the Federal Reserve system.
  - B) printing money.
  - C) issuing orders to buy or sell government securities for the Fed.
  - D) advising the Treasury Department on monetary policy.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 56) When the Fed wants to undertake open market operations, it
- A) can require all commercial banks to buy from or sell to it.
  - B) can require all member banks to buy from or sell to it.
  - C) buys or sells securities through the trading desk at the New York Federal Reserve Bank.
  - D) buys from or sells to the U.S. Treasury.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 57) Open market operations are
- A) the buying of existing corporate securities in secondary markets by private citizens, banks and the Fed.
  - B) the buying and selling of existing U.S. government securities in open private markets by the Fed.
  - C) the actions of the Fed that are used to finance deficit financing by the government.
  - D) the selling of new government securities in order to increase the money supply.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 58) The level of reserves in the banking system is determined by
- A) the American Banking Association.
  - B) the Federal Open Market Committee.
  - C) bond dealers.
  - D) the Treasury Department.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 59) When the Fed buys a U.S. bond in the open market
- A) its action has no effect on the total reserves or the money supply because the check it writes increases reserves at one bank but they fall at another.
  - B) total reserves increase by the amount of the purchase but the money supply stays the same.
  - C) its action expands total reserves and the money supply.
  - D) its action contracts total reserves and the money supply.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 60) Open market operations are conducted by the Fed
- A) in the private secondary U.S. securities market.
  - B) in the New York Stock Exchange.
  - C) through the Bureau of Engraving.
  - D) through the Washington location of the Federal Reserve's Bank of Governors.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 61) The initial impact of the Fed's open market sale of government securities by the Federal Reserve is
- A) an increase in the money supply by some multiple of the dollar volume of the sale.
  - B) an increase in commercial bank deposits at the Fed.
  - C) a fall in the money supply by some multiple of the dollar volume of the sale.
  - D) a reduction of the commercial banking system's reserve deposits at the Fed.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 62) A sale of securities by the Fed causes
- A) a contraction of the money supply equal to the amount of the securities sold.
  - B) an expansion of the money supply equal to the amount of the securities sold.
  - C) a multiple expansion of the money supply greater than the amount of the securities sold.
  - D) a multiple contraction of the money supply greater than the amount of the securities sold.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 63) If the actual money multiplier equals the potential money multiplier and if the Federal Reserve wishes to increase the money supply by \$500 when the reserve ratio is 10 percent, it should
- A) sell \$50 of government bonds.
  - B) buy \$50 of government bonds.
  - C) sell \$5000 of government bonds.
  - D) buy \$5000 of government bonds.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 64) If the actual money multiplier equals the potential money multiplier and if the Fed wishes to reduce the money supply by \$1 million when the reserve ratio is 20 percent, then the Fed should
- A) sell \$200,000 of government securities.
  - B) buy \$200,000 of government securities.
  - C) sell \$500,000 of government securities.
  - D) buy \$500,000 of government securities.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 65) When the Fed buys U.S. government securities, the money supply
- A) increases because there is an increase in transaction deposits at the bank of the bond dealer but there is no decrease in transaction deposits at any other bank.
  - B) decreases because there is an increase in the reserves of the bond dealer's bank.
  - C) remains unchanged because the increase in transaction deposits at the bond dealer's bank is offset by a reduction in transaction deposits at the Fed.
  - D) remains unchanged because the increase in transaction deposits at the bond dealer's bank is offset by a fall in transaction deposits at another bank.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

66) Open market operations are

- A) the buying and selling of existing U.S. government securities in open private markets by the Fed in order to change the money supply.
- B) the buying and selling of existing U.S. government securities in open private markets by citizens.
- C) the selling of new government securities by banks in order to increase the money supply.
- D) the selling of new government securities in open private markets by banks in order to finance the deficit.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

67) Assuming a reserve ratio of 10 percent, if a bank sells \$100,000 in securities how much can the bank loan out?

- A) \$90,000
- B) \$100,000
- C) \$110,000
- D) \$10,000

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

68) Assuming a reserve ratio of 10 percent, if a bank receives \$100,000 in deposits how much can the bank loan out?

- A) \$90,000
- B) \$100,000
- C) \$110,000
- D) \$10,000

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

69) The Federal Reserve will engage in open market operations when

- A) it wants to punish private banks because they are not keeping the required level of reserves.
- B) it wants to change the money supply.
- C) it wants to change the reserve ratio.
- D) it wants to increase the total amount of reserves since government securities are considered a reserve.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 70) The level of reserves in the monetary system is determined by
- A) the Federal Open Market Committee.
  - B) the Treasury Department.
  - C) Congress.
  - D) the President of the United States.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 71) When the Fed sells a U.S. bond in the open market
- A) total reserves will increase.
  - B) total reserves will decrease.
  - C) total reserves do not change but the money supply increases.
  - D) total reserves do not change but the money supply decreases.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 72) When the Fed buys a U.S. bond in the open market
- A) total reserves will increase.
  - B) total reserves will decrease.
  - C) total reserves do not change but the money supply increases.
  - D) total reserves do not change but the money supply decreases.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 73) The Fed sells \$1 million in bonds to a bond dealer. The bond dealer's bank experiences
- A) a decrease in assets of \$1 million as its reserves decrease and an increase in liabilities of \$1 million as its deposits rise.
  - B) a decrease in assets of \$1 million as its reserves decrease and a decrease in liabilities of \$1 million as its deposits fall.
  - C) an increase in assets of \$1 million as its deposits fell by \$1 million, and a decrease in liabilities as its reserves fell by \$1 million.
  - D) no change in assets or liabilities.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 74) If a bank's deposits at the Fed increase by \$10 million, then
- A) both the bank's assets and the Fed's assets increase by \$10 million.
  - B) both the bank's liabilities and the Fed's liabilities increase by \$10 million.
  - C) the bank's assets increase by \$10 million and the Fed's liabilities increase by \$10 million.
  - D) the bank's assets increase by \$10 million, but there is no change at the Fed since it does not really have assets or liabilities.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 75) The Fed buys securities and gives a bond dealer a check for the amount. After the check has cleared,
- A) reserves remain unchanged because the increase of reserves at the dealer's bank are offset by an increase in reserves at the Fed.
  - B) reserves have fallen by the amount of the check because the Fed clears the check by reducing the bank's deposits at the Fed.
  - C) reserves have risen by the amount of the check because the Fed clears the check by increasing the amount of the bank's deposits with the Fed.
  - D) reserves have fallen by the amount of the reserves times the reserve ratio and the money supply increases by the difference between the amount of the check and the increase in the reserves.

Answer: C

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 76) When the Fed sells government securities,
- A) reserves increase, leading to a decrease in the money supply by an amount more than the sale of the government securities.
  - B) reserves decrease, leading to an increase in the money supply by an amount more than the sale of the government securities.
  - C) reserves increase, leading to an increase in the money supply by an amount more than the sale of the government securities.
  - D) reserves decrease, leading to a decrease in the money supply by an amount more than the sale of the government securities.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 77) When the Fed buys government securities,
- A) reserves increase, leading to a decrease in the money supply by an amount more than the purchase of the government securities.
  - B) reserves decrease, leading to a increase in the money supply by an amount more than the purchase of the government securities.
  - C) reserves increase, leading to a increase in the money supply by an amount more than the purchase of the government securities.
  - D) reserves decrease, leading to a decrease in the money supply by an amount more than the purchase of the government securities.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 78) Mary decides to buy a bond from Joe for \$100. The money supply will
- A) neither increase nor decrease.
  - B) increase by \$100.
  - C) increase by more than \$100.
  - D) decrease by \$100.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 79) The reserve ratio is 20 percent. If the Fed buys \$1 million of U.S. government securities and the check is deposited in Bank A, but Bank A increases its vault cash by the entire amount, then the money supply
- A) does not increase.
  - B) increases by \$800,000.
  - C) increases by \$1 million.
  - D) increases by more than \$1 million.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 80) A purchase of U.S. government securities by the Fed causes
- A) an expansion of the money supply equal to the amount of the securities purchased.
  - B) a contraction of the money supply equal to the amount of the securities purchased.
  - C) an expansion of the money supply of more than the amount of the securities purchased.
  - D) a contraction of the money supply of more than the amount of the securities purchased.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 81) A sale of U.S. government securities by the Fed causes a(n)
- A) expansion of the money supply equal to the amount of the securities sold.
  - B) contraction of the money supply equal to the amount of the securities sold.
  - C) expansion of the money supply of more than the amount of the securities sold.
  - D) contraction of the money supply of more than the amount of the securities sold.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 82) The reserve ratio is 20 percent. If the Fed buys \$1 million of U.S. government securities from a bond dealer by transmitting the funds to the dealer's deposit account at Bank ABC, then
- A) Bank ABC can make no additional loans.
  - B) Bank ABC can make additional loans up to \$800,000.
  - C) Bank ABC can make additional loans up to \$1 million.
  - D) Bank ABC cannot make any additional loans, but the system as a whole can make additional loans up to \$1 million.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 83) The reserve ratio is 20 percent. After the Fed buys \$1 million in U.S. government securities from a bond dealer by transmitting the funds to the dealer's deposit account at Bank A, Bank A lends a construction company an amount equal to its excess reserves. The construction company spends the entire amount on lumber from a lumber yard, which deposits the construction company's check in its deposit account with Bank A. The maximum loan Bank A can now make is
- A) \$0.
  - B) \$640,000.
  - C) \$800,000.
  - D) \$1 million.

Answer: B

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 84) The reserve ratio is 20 percent. The Fed buys \$1 million in government securities from a bond dealer by transmitting the funds to the dealer's deposit account at Bank A. Bank A loans the maximum amount possible to a construction company, which buys materials from a lumber yard. The lumberyard deposits the construction company's check in Bank B. What is the maximum loan Bank A can now make and the maximum loan Bank B can now make?

- A) Bank A: 0; Bank B: \$640,000
- B) Bank A: 0; Bank B: \$800,000
- C) Bank A: \$800,000; Bank B: \$640,000
- D) Bank A: \$800,000; Bank B: 0

Answer: A

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 85) The reserve ratio is 20 percent. The Fed buys \$1 million in government securities from a bond dealer by transmitting the funds to the dealer's deposit account at Bank A. Bank A makes the maximum loan possible to a construction company, which buys materials with the loan. The check is deposited in Bank B, which loans out all it can to a car dealership. To this point, the money supply has increased by

A) \$1 million.                      B) \$1.8 million.                      C) \$2.44 million.                      D) \$3 million.

Answer: C

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 86) Suppose that the reserve ratio is 20 percent. A bank's customer deposits into her account \$100,000 in funds from a check written on an account at another bank. The maximum potential increase in the money supply resulting from this transaction is equal to

A) \$0.                      B) \$20,000.                      C) \$200,000.                      D) \$500,000.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 87) When the Fed buys a \$10,000 bond from a bond dealer,

A) reserves of the banking system increase by \$10,000, but the money supply will only be able to increase by something less than this amount.  
B) reserves of the banking system increase by \$10,000, but the money supply can increase by more than \$10,000.  
C) reserves of the banking system remain unchanged, but the money supply increases by \$10,000.  
D) reserves of the banking system remain unchanged, but the money supply decreases by \$10,000.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 88) If a bond dealer sells a government bond to the Fed for \$100,000, and the reserve ratio is 10 percent, then the bank that receives a \$100,000 deposit from the dealer can expand its loans by \_\_\_\_\_, and the money supply can increase by as much as \_\_\_\_\_.

A) \$80,000; \$800,000                      B) \$10,000; \$100,000  
C) \$90,000; \$1,000,000                      D) \$90,000; \$900,000

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 89) For the money expansion process to produce the maximum potential multiplier effect,
- A) all loans of a given bank have to be deposited in that bank.
  - B) the required reserve ratio has to be 100 percent.
  - C) the Fed has to sell government bonds to back up the loans.
  - D) all loans from banks have to be redeposited throughout the banking system.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 90) Open market operations are
- A) the procedures for approving loans at commercial banks.
  - B) the procedures of applying for loans at commercial banks.
  - C) the Federal Reserve's purchase and sale of existing U.S. government securities.
  - D) steps a bank must complete before it can invest in stocks on the open market.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 91) When the Fed buys U.S. government securities on the open market,
- A) the reserves of the banking system expand.
  - B) the reserves of the banking system contract.
  - C) the money supply contracts.
  - D) the total reserves of the banking system will fall below required reserves.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 92) Which one of the following would increase reserves for the banking system?
- A) The Fed sells government securities on the open market.
  - B) The Fed buys government securities on the open market.
  - C) You purchase a newly-issued U.S. Treasury bond.
  - D) You purchase a U.S. Treasury bond from a bond dealer.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

93) Open market operations involve

- A) the buying and selling of existing corporate bonds.
- B) the buying and selling of existing corporate stocks.
- C) the buying and selling of existing federal government bonds.
- D) the buying and selling of Federal Reserve bonds.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

94) If the Fed purchases \$100,000 in government bonds from a bank, then the

- A) liabilities of the bank rise by \$100,000.
- B) reserves of the bank rise by \$100,000.
- C) assets of the bank rise by \$100,000.
- D) reserves of the bank rise by \$100,000.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

95) If the FOMC decides to engage in the selling of government bonds, what is the effect on the money supply?

- A) a decrease
- B) an increase
- C) no change
- D) an initial increase followed by an additional rise when the bonds mature

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

96) The Fed's buying and selling of existing government securities is called

- A) market interventions.
- B) open market operations.
- C) changes in the reserve requirement ratio.
- D) changes in the difference between the discount rate and the federal funds rate.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

97) When a bank sells a bond to the Fed,

- A) its liabilities decrease.
- B) its liabilities increase.
- C) its reserves initially decrease.
- D) its reserves initially increase.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 98) When a bank buys a bond from the Fed,  
A) its liabilities decrease. B) its liabilities increase.  
C) its reserves initially decrease. D) its reserves initially increase.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 99) If the FOMC decides that the Fed should buy bonds it  
A) instructs the New York Federal Reserve Bank's trading desk to buy them.  
B) asks the Congress for permission to buy them.  
C) requires the President's signature on the buy order.  
D) requires the permission of the Financial Oversight Committee.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 100) If the money multiplier is 2.4 and the Fed buys \$8 million in securities on the open market, transaction deposits could potentially  
A) increase by \$19.2 million. B) increase by \$8 million.  
C) decrease by \$19.2 million. D) decrease by \$16.5 million.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 101) Suppose that the reserve ratio is 5%. What is the value of the potential money multiplier?  
A) 2 B) 5 C) 10 D) 20

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 102) The Fed buys \$1 million in bonds from a bond dealer. The bond dealer's bank experiences
- A) an increase in assets of \$1 million as its reserves increase and a decrease in liabilities as its transactions deposits fall.
  - B) no change in assets or liabilities. Assets both increased and decreased by the amount of the check.
  - C) a decrease in assets of \$1 million as the checking account of the bond dealer increased, and a decrease in liabilities as the bank's deposits with the Fed increased by \$1 million.
  - D) an increase in assets of \$1 million as its reserves increase and an increase in liabilities of \$1 million as the deposits in the bond dealer's transactions account increases by \$1 million.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 103) Other things being equal, when the Fed buys U.S. government securities,
- A) the U.S. Treasury must immediately issue new securities to replace the securities that the Fed has removed from the market.
  - B) the Fed's total assets and total liabilities immediately expand by exactly the amount of the Fed's purchase.
  - C) the quantity of deposits in the U.S. banking system expands by less than the amount of the Fed's purchase.
  - D) the quantity of paper currency and coins in circulation expands by more than the amount of the Fed's purchase.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 104) A purchase of U.S. government securities by the Fed causes
- A) a multiple contraction of the money supply because deposits fall by more than the amount of the securities purchased.
  - B) a contraction of the money supply equal to the amount of the securities because all other transactions occur within the banking system.
  - C) a multiple expansion of the money supply because the reserve ratio is less than one.
  - D) an expansion of the money supply equal to the amount of the securities because all other transactions occur within the banking system.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 105) The reserve ratio is 10 percent. Depositors regularly keep 10 percent of their deposits as cash. If the Fed buys \$1 million of U.S. government securities, excess reserves
- A) increase by \$800,000.
  - B) increase by \$810,000.
  - C) increase by \$900,000.
  - D) increase by \$1 million.

Answer: B

Diff: 3

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 106) To expand the money supply, the Fed should
- A) buy U.S. government securities.
  - B) sell U.S. government securities.
  - C) raise the required reserve ration.
  - D) cut taxes.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 107) To contract the money supply, the Fed should
- A) reduce the differential between the discount rate and the federal funds rate.
  - B) increase government spending and cut taxes.
  - C) lower the required reserve ratio.
  - D) sell U.S. government securities.

Answer: D

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 108) The reserve ratio equals 20 percent. The Fed buys \$1 million in U.S. government securities. The most the money supply can increase is
- A) \$1 million.
  - B) \$4 million.
  - C) \$5 million.
  - D) \$10 million.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 109) To increase the money supply,
- A) the Federal Reserve should sell government securities.
  - B) the commercial banks should reduce their loans.
  - C) the Federal Reserve should buy government securities.
  - D) the Federal Reserve should reduce its loans to banks.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 110) A decrease in the reserve ratio will
- A) cause the money supply to decrease.
  - B) cause the money supply to increase.
  - C) not affect the money supply.
  - D) decrease the money multiplier.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 111) The reason that the commercial banking system can generate a multiple expansion or contraction of the money supply is that
- A) banks are required to hold only a fraction of their deposit liabilities as reserves.
  - B) most banks maintain a relatively large stock of reserves.
  - C) banks hold reserves equal to their net worth.
  - D) banks generally are required to hold surplus funds on deposit with other banks.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 112) If the reserve ratio is raised, the money multiplier
- A) is lowered.
  - B) is increased.
  - C) stays the same.
  - D) is doubled.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 113) The maximum potential money multiplier is equal to
- A) the reserve ratio.
  - B) the inverse of the required reserve ratio.
  - C) one minus the reserve ratio
  - D) the number of dollars on reserve.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 114) If the reserve ratio is 25 percent, the maximum potential money multiplier is
- A) 1.
  - B) 4.
  - C) 8.
  - D) 25.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 115) With a reserve ratio of 10 percent, the maximum potential money multiplier is  
A) 1.                                      B) 5.                                      C) 10.                                      D) 100.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 116) For the past several decades, the U.S. M1 multiplier has been between \_\_\_\_\_.  
A) 1.0 and 2.0.                              B) 2.5 and 3.0.                              C) 3.0 and 6.0.                              D) 6.5 and 10.0.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 117) The larger is the reserve ratio,  
A) the greater is the increase in the money supply for an increase in bank deposits.  
B) the more likely it is there will be currency drains.  
C) the smaller is the maximum potential money multiplier.  
D) the more difficult it is for the Federal Reserve to control the money supply.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 118) By affecting the amount of reserves in the banking system, the Fed can  
A) affect the size of the money supply.                              B) change the marginal tax rates.  
C) increase government purchases.                              D) reduce government purchases.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 119) Initially, the reserve ratio is 10 percent. Now banks decide they want an additional 10 percent of deposits as reserves. There are no currency drains. If the Fed buys \$1 million of U.S. government securities, the money supply will  
A) not change because of the excess reserves banks keep on hand.  
B) increase by \$1 million.  
C) increase by \$5 million.  
D) increase by \$10 million.

Answer: C

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 120) Following a new deposit of \$50 at a bank, drawn on funds previously held on deposit at another bank, when the reserve ratio is 10 percent, the maximum potential increase in the money supply will be

A) \$0.                                      B) \$50.                                      C) \$400.                                      D) \$500.

Answer: A

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 121) If the reserve ratio is 10 percent and reserves in the commercial banking system increase by \$10,000, the maximum possible expansion of demand deposits is

A) \$10,000.                                      B) \$90,000.                                      C) \$100,000.                                      D) \$1,000,000.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 122) When the Federal Reserve sells a government security to a bond dealer, which transmits payment from a transactions deposit account at a bank,

A) the cash of the Federal Reserve will decrease.  
 B) the net worth of the commercial bank will decrease.  
 C) the loans of the commercial bank will increase.  
 D) the money supply will decrease.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 123) If the Federal Reserve sells \$100 of securities through a commercial bank when the reserve requirement is 10 percent, the maximum potential change in the money supply is

A) a \$100 increase.                                      B) a \$1,000 increase.  
 C) a \$100 decrease.                                      D) a \$1,000 decrease.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 124) If the Federal Reserve buys \$500 of government securities when the required reserve ratio is 20 percent, the maximum potential change in the money supply is a(n)

A) increase by \$100.                                      B) increase by \$2,500.  
 C) decrease by \$100.                                      D) decrease by \$2,500.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

125) Which of the following would reduce the money multiplier?

- A) Reducing the reserve ratio
- B) Bond purchases by the Fed
- C) Cash drains from banks
- D) Bank reductions in desired reserve holdings

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

126) Which of the following would reduce the money multiplier?

- A) The purchase of bonds by the Fed
- B) Lowering the reserve ratio
- C) Increases in the reserve ratio
- D) A flow of currency into the banking system

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

127) According to the text, the actual M1 multiplier in the U.S. today is

- A) between 0 and 1.
- B) between 1.5 and 2.0.
- C) negative.
- D) over 10.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: New

128) According to the text, the actual M2 multiplier in the United States today is

- A) about 5.
- B) between 1.0 and 2.0.
- C) negative.
- D) over 10.

Answer: B

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: New

129) The formula  $\frac{1}{\text{required reserve ratio}}$  is the

- A) federal funds rate.
- B) discount rate.
- C) potential money multiplier.
- D) actual change in the money supply.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB:

Question Status: Previous Edition

- 130) The actual money multiplier multiplied by the change in total reserves is the
- A) federal funds rate.
  - B) discount rate.
  - C) potential money multiplier.
  - D) actual change in the money supply.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 131) The potential money multiplier gives us
- A) the growth in real national income when the money supply increases.
  - B) the growth in the money supply when income increases.
  - C) the maximum potential change in the money supply due to a change in reserves.
  - D) the maximum potential change in the money supply due to a change in income.

Answer: C

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 132) When people decide to increase the amount of currency they are currently holding
- A) the potential money multiplier will increase.
  - B) the potential money multiplier will decrease.
  - C) the actual money multiplier will increase.
  - D) the actual money multiplier will decrease.

Answer: D

Diff: 1

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 133) When banks reduce the reserve ratio, the potential money multiplier
- A) increases.
  - B) decreases.
  - C) remains unchanged.
  - D) sometimes increases, and sometimes decreases depending on the rate of inflation.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 134) If proceeds from loans are NOT deposited back in the banking system, then
- A) the magnitude of the multiplier process is reduced.
  - B) there is no effect on the magnitude of the multiplier process.
  - C) the magnitude of the multiplier process is increased.
  - D) the Fed intervenes by selling more Federal government bonds.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

- 135) The value of the money multiplier depends on
- A) the reserve ratio.
  - B) the ratio of total assets to total liabilities for the banking system as a whole.
  - C) the interest rate offered on bonds currently being sold by the Fed.
  - D) the interest rate offered on bonds currently being purchased by the Fed.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 136) If the reserve ratio decreases from 20 percent to 10 percent, then the potential money multiplier
- A) increases from 5 to 10.
  - B) decreases from 10 to 5.
  - C) does not change.
  - D) decreases from 20 to 10.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 137) An increase in the reserve ratio
- A) has an expansionary effect on the money supply.
  - B) has a contractionary effect on the money supply.
  - C) increases the money multiplier.
  - D) will cause banks to make more loans.

Answer: B

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 138) Suppose that the Fed purchases \$1,000,000 worth of bonds and that the reserve ratio is 25 percent. Then, the maximum potential expansion of deposits is
- A) \$4,000,000.
  - B) \$10,000,000.
  - C) \$400,000.
  - D) \$25,000,000.

Answer: A

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Revised

- 139) What is a fractional reserve banking system? How long has the fractional reserve banking system been in existence?

Answer: A fractional reserve banking system is a system in which depository institutions hold reserves that are less than the amount of total deposits. They have been in existence at least 2,500 years.

*Diff: 1*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 140) What are reserves? Discuss the various types of reserves used in the U.S. banking system.

Answer: Reserves are assets held by a depository institution that are used to meet withdrawal demands. In the U.S. Federal Reserve System, reserves include deposits held by Federal Reserve district banks for depository institutions plus the vault cash in the depository institution. Total reserves are anything that the law allows banks to claim as reserves. Required reserves are the value of reserves the depository institution must hold and excess reserves are the reserves the institution holds in excess of the required reserves.

*Diff: 1*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 141) As far as reserves and deposits are concerned, describe the assets and liabilities of a bank.

Answer: The major liabilities of a bank are the deposits they hold. Transaction deposits are drawn down every time a depositor writes a check. The assets are the reserves the bank has and any loans they have made.

*Diff: 1*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 142) Explain what happens to the money supply when the Fed sells bonds on the open market. What happens to the assets and liabilities of the Fed?

Answer: The money supply falls when the Fed sells bonds on the open market, because the purchaser pays for the bonds by transmitting funds from a transactions deposit. The reserves of the bank fall by the amount of the funds transfer. The assets of the Fed fall, because the bonds sold had been assets and the liabilities of the Fed. The liabilities of the Fed decrease, because the purchaser's bank's reserves declined by the amount of the transfer.

*Diff: 3*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 143) Suppose the Fed purchases \$1 million in bonds in the open market. Explain how the money supply can increase by more than \$1 million.

Answer: Transaction deposits and reserves increase by \$1 million as a result of the purchase. Since the reserve ratio is less than one, the bank now can loan some of the reserves to someone. If it does, then the transaction deposits of the borrower increase by the amount of the loan, so the money supply has increased further.

*Diff: 2*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Revised*

- 144) Why does the money supply increase when the Fed buys a bond but does not change when a business buys a bond?

Answer: The reserves in the banking system increase when the Fed buys bonds but remain unchanged when a business buys bonds. When a business buys bonds, a check is written on one bank and deposited in another. The reserves of one bank increase but fall in the other, so there is no net change. When the Fed buys bonds, reserves increase in a bank but don't decrease anywhere else since the Fed can add to the reserves of a member bank.

*Diff: 3*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 145) Explain how the Fed increases the money supply when it buys bonds in the open market.

Answer: The Fed buys bonds in the open market and pays for the bonds by transmitting funds to the bond dealer's deposit account in a bank, at which point it becomes part of the money supply. The Fed has just created money, because it has added to the reserve account of the bond dealer's bank, and the money supply increases by the amount of the purchase.

*Diff: 2*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Previous Edition*

- 146) How are the assets and liabilities changed for a bond dealer, the bond dealer's bank, and the Fed when the Fed buys \$100,000 in bonds?

Answer: The bond dealer trades a bond for a transactions deposit of \$100,000. That is, the form of the assets change but not the total value. Assets and liabilities of the bank increase by \$100,000 since transaction deposits increase when the Fed deposits the funds, and the bank's reserves increase by the same amount. The assets of the Fed increase by \$100,000 when it buys the bond and its liabilities increase by \$100,000 because reserves of the bank on deposit with the Fed increase. The money supply increases as the bond is converted into money.

*Diff: 3*

*Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply*

*AACSB: Analytic skills*

*Question Status: Revised*

- 147) Suppose a person deposits a paycheck in a bank. The transaction deposits are money, so has the money supply increased? Explain.

Answer: No. The check was drawn on the employer's account. Transaction deposits fell in that bank by the same amount transaction deposits increased in this bank, so the total money supply has not changed.

Diff: 2

Topic: 15.6 Fractional Reserve Banking, the Federal Reserve, and the Money Supply

AACSB: Analytic skills

Question Status: Previous Edition

## 15.7 Federal Deposit Insurance

- 1) The Federal Deposit Insurance Corporation insures

- A) banks against lawsuits.
- B) the federal funds market.
- C) the deposits held in member banks.
- D) the deposits held in the Fed.

Answer: C

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 2) The FDIC was created because

- A) banks failed to create money the way the Fed wanted them to.
- B) people worried about bank failures after World War I, even though very few banks actually failed.
- C) there were so many bank failures in the 1930s.
- D) the Fed kept the required reserve ratio too low.

Answer: C

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 3) Which of the following has been a problem faced by the FDIC in its provision of federal deposit insurance?

- A) Moral hazard arising from the tendency for the highest-risk banks to be those most interested in obtaining deposit insurance in the first place
- B) Adverse selection arising from the tendency for banks to take on more risk after they receive deposit insurance
- C) Moral hazard arising from the tendency for banks to take on more risk after they receive deposit insurance
- D) A relatively low number of bank failures each year, which has reduced the need for deposit insurance

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

4) Which of the following statements about the FDIC is correct?

- I. The deposit insurance premiums charged by the FDIC to a member bank fully reflect the riskiness of that bank's assets
- II. The manner in which the FDIC is set up helps protect depository institutions from the rigors of true market competition

A) I only                      B) II only                      C) Both I and II                      D) Neither I nor II

Answer: B

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

5) Bank runs are a possibility because

- A) the FDIC is inefficient.
- B) bankers are often poor businesspeople.
- C) in difficult times people want currency instead of demand deposits.
- D) banks do not keep enough reserves to cover all their depository liabilities.

Answer: D

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

6) The manner in which FDIC deposit insurance is set up in the United States encourages banks to

- A) be too conservative in their lending practices.
- B) maintain excess reserves that are too great.
- C) make riskier loans than they otherwise would.
- D) reject some loans that probably would be profitable.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

7) If the FDIC eliminated its insurance program for deposits, then

- A) the banking system would probably fail.
- B) individual depositors would have more incentive to ascertain the soundness and solvency of the bank.
- C) banks would probably hold fewer reserves.
- D) moral hazard would be increased.

Answer: B

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Asymmetric information before a transaction takes place generates the problem of
- A) flawed bank regulation.
  - B) intermediation.
  - C) adverse selection.
  - D) bank runs.

Answer: C

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Deposit insurance shields depositors from the adverse effects of risky decisions and thereby
- A) encourages riskier behavior on the part of managers of depository institutions.
  - B) encourages depositors to monitor the managers of depository institutions more closely.
  - C) encourages moral hazard on the part of depositors.
  - D) generates a more efficient banking system.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 10) The fact that individuals whose credit worthiness is less than it appears to be are those who are most willing to borrow funds at any given interest rate is an example of
- A) adverse selection.
  - B) symmetric information.
  - C) moral bonuses.
  - D) diverse origins.

Answer: A

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 11) Which of the following statements is/are correct?
- I. Depository institution managers undertake riskier actions than they otherwise would because of the existence of deposit insurance
  - II. Because of the existence of deposit insurance, depositors in savings and loans and other banks have little incentive to investigate the financial stability of these institutions
- A) I only
  - B) II only
  - C) Both I and II
  - D) Neither I nor II

Answer: C

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

- 12) Lenders generally want borrowers to agree to invest prudently, yet once a loan is made borrowers may use the funds in a highly risky fashion. This leads to the problem of
- A) critical mass.
  - B) deposit insurance.
  - C) investor selection.
  - D) moral hazard.

Answer: D

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

## 13) The Federal Deposit Insurance Corporation

- A) insures the deposits held by the Fed.
- B) insures the deposits held in banks.
- C) insures banks against lawsuits by depositors.
- D) insures the open market operations of the Fed.

Answer: B

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

## 14) As of 2010, the FDIC insured deposit accounts up to which of the following amounts?

- A) \$10,000.
- B) \$25,000.
- C) \$100,000.
- D) \$250,000.

Answer: D

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Revised

## 15) The FDIC helps prevent

- A) risky behavior on the part of bankers.
- B) inflation.
- C) bank runs.
- D) risky behavior on the part of depositors.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

## 16) The FDIC fee system encourages depository institutions to

- A) make riskier loans than they would otherwise.
- B) reject loans that probably would have been profitable.
- C) seek only a modest rate of return.
- D) operate their institutions in too conservative a fashion.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

## 17) Asymmetric information before a transaction takes place generates the problem of

- A) bank runs.
- B) irrational behavior.
- C) moral hazard.
- D) adverse selection.

Answer: D

Diff: 1

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

18) If depository insurance exists, bank managers may make riskier loans than they would have otherwise, which is an example of

- A) regulatory lag.
- B) irrational behavior.
- C) moral hazard.
- D) adverse selection.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

19) Which of the following is NOT a potential problem due to federal depository insurance?

- A) Banks have an incentive to make riskier loans than they would otherwise.
- B) Depositors have little incentive to monitor the behavior of the managers of the depository institutions.
- C) Depositors demand greater interest rates on their deposits to compensate them for the riskier behavior of the managers of the depository institutions.
- D) Lenders have less incentive to investigate the credit-worthiness of borrowers.

Answer: C

Diff: 3

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

20) Bank examinations by the FDIC help reduce the \_\_\_\_\_ problem, by preventing bank managers from allocating funds already obtained from depositors to non-creditworthy loans.

- A) moral hazard
- B) principled hazard
- C) adverse selection
- D) contrary selection

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

21) In addition to insuring accounts, the FDIC today has the additional power of

- A) setting reserve requirements.
- B) establishing FOMC goals.
- C) establishing the discount rate.
- D) establishing higher capital requirements for banks.

Answer: D

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

22) The Federal Deposit Insurance Corporation

- A) increases the stability of the banking system by reducing the likelihood of bank runs.
- B) discourages banks from engaging in excessive risk taking.
- C) only insures deposits in money-center banks.
- D) was established after the Panic of 1907.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

23) Because deposits are insured by the FDIC, most of us do not look at the lending behavior of our banks. This creates a(n) \_\_\_\_\_ problem.

- A) moral hazard
- B) principled hazard
- C) adverse selection
- D) contrary selection

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

24) Bank X had a reputation for asking few questions when it provided loans. Five years later, the majority of the loans were not repaid. This is because the bank had failed to address the

- A) adverse selection problem.
- B) moral hazard problem.
- C) contrary selection problem.
- D) free-rider problem.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

25) Which of the following represents a preventative measure against bank runs?

- A) The President of the United States can order banks to pay depositors.
- B) The Federal Reserve can lower reserve requirements to ensure that banks have sufficient funds.
- C) The FDIC provides deposit insurance.
- D) None of the above is correct.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

26) What would cause a bank run?

- A) Depositors feel that the bank does not have sufficient assets to cover their deposits.
- B) Depositors feel that they are earning too low of a return on their deposits.
- C) Borrowers feel that they are being charged too high of an interest rate on their loans.
- D) Bank managers choose to hold more excess reserves.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

27) What effect has the presence of federal deposit insurance had on the banking industry?

- A) Banks now hold more excess reserves.
- B) Banks have made it more difficult for customers to qualify for loans.
- C) Banks have made riskier loans.
- D) Depositors have become more vigilant in monitoring the decisions made by managers of their banks.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

28) The government agency that insures deposits held in banks in the United States is

- A) the Federal Reserve System.
- B) the Federal Bank Insurance Corporation.
- C) the Federal Asset Insurance Corporation.
- D) the Federal Deposit Insurance Corporation.

Answer: D

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB:

Question Status: Previous Edition

29) Due to the existence of the FDIC, banks

- A) may make riskier loans knowing that their depositors are insured.
- B) have not changed their behavior even with the existence of insurance.
- C) become more cautious in making loans.
- D) are no longer concerned about net worth.

Answer: A

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

30) In which year was the Federal Deposit Insurance Corporation (FDIC) established?

- A) 1913                      B) 1929                      C) 1933                      D) 1951

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Revised

31) The primary purpose of the FDIC is to reduce the potential for

- A) government regulations.                      B) reserve cheating.  
C) bank runs.                      D) excessive interest rates.

Answer: C

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition

32) Explain the forces that caused the savings and loan debacle in the latter half of the 1980s.

Answer: Deposit insurance created a moral hazard problem in which savings institutions had an incentive to make riskier loans than they would have made in the absence of deposit insurance. In addition, because their deposits were federally insured, depositors of savings institutions had less incentive to monitor the risks incurred by the managers. As a result, the institutions extended large amounts of high-risk loans, many of which generated losses that resulted in failures by numerous institutions.

Diff: 2

Topic: 15.7 Federal Deposit Insurance

AACSB: Analytic skills

Question Status: Previous Edition