

Note: Submit your answers using Blackboard Learn. Notice that the order in which the answers appear [i.e., A), B), C), and D)] are different in this PDF file and in Blackboard Learn.

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

- 1) A financial crisis is _____
A) not possible in the modern financial environment.
B) a feature of developing economies only.
C) a major disruption in the financial markets.
D) typically followed by an economic boom.

- 2) A situation in which the quantity of bonds supplied exceeds the quantity of bonds demanded is called a condition of excess supply; because people want to sell _____ bonds than others want to buy, the price of bonds will _____.
A) more; rise B) fewer; fall C) fewer; rise D) more; fall

- 3) Money is _____
A) a flow of earnings per unit of time.
B) always based on a precious metal like gold or silver.
C) the total collection of pieces of property that are a store of value.
D) anything that is generally accepted in payment for goods and services or in the repayment of debt.

- 4) A lower level of income causes the demand for money to _____ and the interest rate to _____, everything else held constant.
A) decrease; decrease B) increase; decrease
C) increase; increase D) decrease; increase

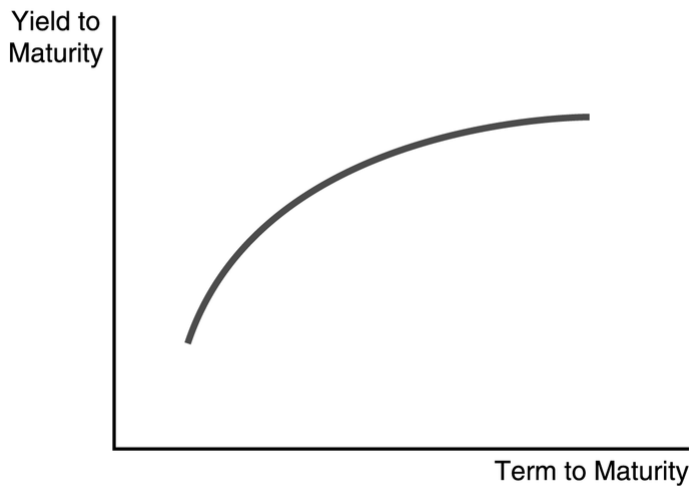
- 5) According to the liquidity premium theory of the term structure, a slightly upward sloping yield curve indicates that short-term interest rates are expected to _____
A) rise in the future. B) remain unchanged in the future.
C) decline moderately in the future. D) decline sharply in the future.

- 6) Dennis notices that jackets are on sale for \$99. In this case money is functioning as a _____.
A) payments-system ruler B) unit of account
C) store of value D) medium of exchange

- 7) An example of economies of scale in the provision of financial services is _____
A) providing depositors with a variety of savings certificates.
B) investing in a diversified collection of assets.
C) spreading the cost of writing a standardized contract over many borrowers.
D) spreading the cost of borrowed funds over many customers.

- 8) Every financial market has the following characteristic: _____
A) It allows loans to be made.
B) It channels funds from lenders-savers to borrowers-spenders.
C) It determines the level of interest rates.
D) It allows common stock to be traded.

- 9) Everything else held constant, abolishing all taxes will _____
 A) increase the interest rate on corporate bonds.
 B) reduce the interest rate on municipal bonds.
 C) increase the interest rate on municipal bonds.
 D) increase the interest rate on Treasury bonds.
- 10) If a \$10,000 face-value discount bond maturing in one year is selling for \$5,000, then its yield to maturity is _____
 A) 5 percent. B) 10 percent. C) 50 percent. D) 100 percent.
- 11) With an interest rate of 6 percent, the present value of \$100 next year is approximately _____
 A) \$106. B) \$100. C) \$94. D) \$92.
- 12) When the price level falls, the _____ curve for nominal money _____, and interest rates _____, everything else held constant. _____
 A) demand; increases; rise B) demand; decreases; fall
 C) supply; decreases; fall D) supply; increases; rise
- 13) The demand curve for bonds has the usual downward slope, indicating that at _____ prices of the bond, everything else equal, the _____ is higher. _____
 A) lower; quantity demanded B) lower; demand
 C) higher; quantity demanded D) higher; demand

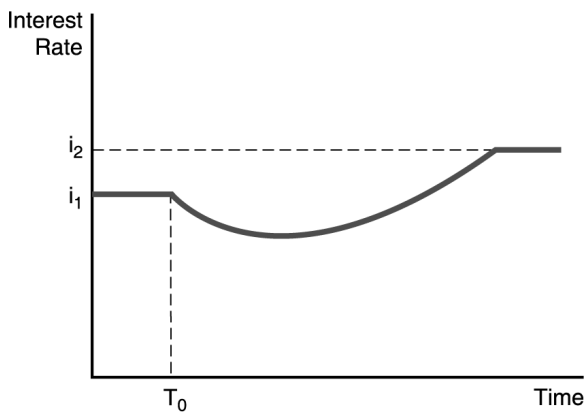


- 14) The steeply upward sloping yield curve in the figure above indicates that _____
 A) short-term interest rates are expected to remain unchanged in the future.
 B) short-term interest rates are expected to fall moderately in the future.
 C) short-term interest rates are expected to rise in the future.
 D) short-term interest rates are expected to fall sharply in the future.

- 15) Which of the following can be described as involving indirect finance? 15) _____
 A) You make a deposit at a bank.
 B) You make a loan to your neighbor.
 C) You buy a U.S. Treasury bill from the U.S. Treasury.
 D) A corporation buys a share of common stock issued by another corporation in the primary market.
- 16) Economies of scale enable financial institutions to 16) _____
 A) reduce moral hazard.
 B) avoid the asymmetric information problem.
 C) avoid adverse selection problems.
 D) reduce transactions costs.
- 17) Which of the following bonds are considered to be default-risk free? 17) _____
 A) U.S. Treasury bonds
 B) Investment-grade bonds
 C) Municipal bonds
 D) Junk bonds
- 18) The management of money and interest rates is called _____ policy and is conducted by a nation's _____ bank. 18) _____
 A) monetary; superior
 B) fiscal; central
 C) fiscal; superior
 D) monetary; central
- 19) Financial institutions that accept deposits and make loans are called _____. 19) _____
 A) exchanges
 B) finance companies
 C) over-the-counter markets
 D) banks
- 20) The riskiness of an asset's returns due to changes in interest rates is 20) _____
 A) interest-rate risk.
 B) asset risk.
 C) exchange-rate risk.
 D) price risk.
- 21) According to the segmented markets theory of the term structure 21) _____
 A) the interest rate for each maturity bond is determined by supply and demand for that maturity bond.
 B) investors' strong preferences for short-term relative to long-term bonds explains why yield curves typically slope downward.
 C) because of the positive term premium, the yield curve will not be observed to be downward-sloping.
 D) bonds of one maturity are close substitutes for bonds of other maturities, therefore, interest rates on bonds of different maturities move together over time.
- 22) The opportunity cost of holding money is 22) _____
 A) the interest rate.
 B) the price level.
 C) the discount rate.
 D) the level of income.
- 23) An increase in the time to the promised future payment _____ the present value of the payment. 23) _____
 A) decreases
 B) is irrelevant to
 C) has no effect on
 D) increases

- 24) According to the liquidity premium theory of the term structure, a downward sloping yield curve indicates that short-term interest rates are expected to _____ 24) _____
 A) rise in the future. B) remain unchanged in the future.
 C) decline moderately in the future. D) decline sharply in the future.
- 25) In Keynes's liquidity preference framework, individuals are assumed to hold their wealth in two forms: 25) _____
 A) money and bonds. B) stocks and bonds.
 C) real assets and financial assets. D) money and gold.
- 26) Collateral is _____ the lender receives if the borrower does not pay back the loan. 26) _____
 A) a liability B) a present C) an asset D) an offering
- 27) The problem created by asymmetric information before the transaction occurs is called _____, while the problem created after the transaction occurs is called _____. 27) _____
 A) moral hazard; adverse selection B) free-riding; costly state verification
 C) costly state verification; free-riding D) adverse selection; moral hazard
- 28) Since it does not have to be converted into anything else to make purchases, _____ is the most liquid asset. 28) _____
 A) money B) stock C) artwork D) gold
- 29) _____ markets transfer funds from people who have an excess of available funds to people who have a shortage. 29) _____
 A) Derivative exchange B) Commodity
 C) Financial D) Fund-available
- 30) If a \$5,000 coupon bond has a coupon rate of 13 percent, then the coupon payment every year is 30) _____
 A) \$13. B) \$130. C) \$650. D) \$1,300.
- 31) When tax revenues are greater than government expenditures, the government has a budget _____ 31) _____
 A) deficit B) revision C) surplus D) crisis
- 32) A credit market instrument that requires the borrower to make the same payment every period until the maturity date is known as a 32) _____
 A) simple loan. B) fixed-payment loan.
 C) discount bond. D) coupon bond.
- 33) The concept of _____ is based on the common-sense notion that a dollar paid to you in the future is less valuable to you than a dollar today. 33) _____
 A) present value B) interest C) future value D) deflation
- 34) _____ work in the secondary markets matching buyers with sellers of securities. 34) _____
 A) Claimants B) Dealers C) Underwriters D) Brokers
- 35) When the Fed decreases the money stock, the money supply curve shifts to the _____ and the interest rate _____, everything else held constant. 35) _____
 A) right; falls B) left; falls C) right; rises D) left; rises

- 36) Everything else held constant, if interest rates are expected to fall in the future, the demand for long-term bonds today _____ and the demand curve shifts to the _____. 36) _____
 A) falls; left B) rises; right C) falls; right D) rises; left
- 37) Typically, borrowers have superior information relative to lenders about the potential returns and risks associated with an investment project. The difference in information is called 37) _____
 A) moral selection. B) risk sharing.
 C) asymmetric information. D) adverse hazard
- 38) The risk structure of interest rates is 38) _____
 A) the relationship among the term to maturity of different bonds.
 B) the relationship among interest rates of different bonds with the same maturity.
 C) the relationship among interest rates on bonds with different maturities.
 D) the structure of how interest rates move over time.



- 39) The figure above illustrates the effect of an increased rate of money supply growth at time period T_0 . From the figure, one can conclude that the 39) _____
 A) liquidity effect is smaller than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
 B) liquidity effect is larger than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
 C) liquidity effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
 D) liquidity effect is larger than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
- 40) The M1 measure of money includes 40) _____
 A) money market mutual fund shares. B) traveler's checks.
 C) money market deposit accounts. D) small denomination time deposits.
- 41) What is the return on a 5 percent coupon bond that initially sells for \$1,000 and sells for \$1,200 next year? 41) _____
 A) 5 percent B) -5 percent C) 25 percent D) 10 percent
- 42) Everything else held constant, an increase in the liquidity of bonds results in a _____ in demand for bonds and the demand curve shifts to the _____. 42) _____
 A) fall; right B) rise; left C) rise; right D) fall; left

- 43) A plot of the interest rates on default-free government bonds with different terms to maturity is called _____ 43) _____
 A) an interest-rate curve. B) a risk-structure curve.
 C) a default-free curve. D) a yield curve.
- 44) Of the following, the largest is _____ 44) _____
 A) demand deposits. B) M2.
 C) money market deposit accounts. D) M1.
- 45) When yield curves are downward sloping, _____ 45) _____
 A) medium-term interest rates are above both short-term and long-term interest rates.
 B) short-term interest rates are above long-term interest rates.
 C) short-term interest rates are about the same as long-term interest rates.
 D) long-term interest rates are above short-term interest rates.
- 46) Financial markets promote greater economic efficiency by channeling funds from _____ to _____ 46) _____
 A) savers; borrowers B) borrowers; savers
 C) investors; savers D) savers; lenders
- 47) Typically, yield curves are _____ 47) _____
 A) bowl shaped. B) gently upward sloping.
 C) mound shaped. D) flat.
- 48) A financial market in which only short-term debt instruments are traded is called the _____ market. 48) _____
 A) bond B) capital C) money D) stock
- 49) Everything else held constant, a decrease in wealth _____ 49) _____
 A) reduces the demand for silver. B) increases the demand for bonds.
 C) increases the demand for stocks. D) increases the demand for gold.
- 50) The _____ states that the nominal interest rate equals the real interest rate plus the expected rate of inflation. 50) _____
 A) Fisher equation B) Monetarist equation
 C) Marshall equation D) Keynesian equation
- 51) The interest rate that equates the present value of payments received from a debt instrument with its value today is the _____ 51) _____
 A) yield to maturity. B) real interest rate.
 C) current yield. D) simple interest rate.
- 52) Financial markets improve economic welfare because _____ 52) _____
 A) they allow consumers to time their purchase better.
 B) eliminate the need for indirect finance.
 C) they weed out inefficient firms.
 D) they channel funds from investors to savers.
- 53) If peanuts serve as a medium of exchange, a unit of account, and a store of value, then peanuts are _____ 53) _____
 A) bank deposits. B) loanable funds. C) reserves. D) money.

- 54) In the bond market, the bond demanders are the _____ and the bond suppliers are the _____. 54) _____
 A) borrowers; lenders B) lenders; advancers
 C) borrowers; advancers D) lenders; borrowers
- 55) Compared to checks, paper currency and coins have the major drawbacks that they 55) _____
 A) must be backed by gold. B) are hard to counterfeit.
 C) are not the most liquid assets. D) are easily stolen.
- 56) If a \$5,000 face-value discount bond maturing in one year is selling for \$5,000, then its yield to 56) _____
 maturity is
 A) 0 percent. B) 5 percent. C) 10 percent. D) 20 percent.
- 57) _____ is a flow of earnings per unit of time. 57) _____
 A) Income B) Money C) Currency D) Wealth
- 58) The upward and downward movement of aggregate output produced in the economy is referred to 58) _____
 as the _____.
 A) roller coaster B) shock wave C) see saw D) business cycle
- 59) The present value of a fixed-payment loan is calculated as the _____ of the present value of all 59) _____
 cash flow payments.
 A) difference B) sum C) log D) multiple
- 60) All of the following are necessary criteria for a commodity to function as money except 60) _____
 A) it must be widely accepted. B) it must be divisible.
 C) it must deteriorate quickly. D) it must be easy to carry.
- 61) A movement along the bond demand or supply curve occurs when _____ changes. 61) _____
 A) income B) wealth C) expected return D) bond price
- 62) When yield curves are flat, 62) _____
 A) short-term interest rates are about the same as long-term interest rates.
 B) medium-term interest rates are above both short-term and long-term interest rates.
 C) short-term interest rates are above long-term interest rates.
 D) long-term interest rates are above short-term interest rates.
- 63) A consol paying \$20 annually when the interest rate is 5 percent has a price of 63) _____
 A) \$100. B) \$200. C) \$400. D) \$800.
- 64) When the price of a bond is above the equilibrium price, there is an excess _____ bonds and 64) _____
 price will _____.
 A) demand for; rise B) supply of; fall
 C) demand for; fall D) supply of; rise
- 65) Which of the following can be described as involving indirect finance? 65) _____
 A) You buy a U.S. Treasury bill from the U.S. Treasury.
 B) You buy shares in a mutual fund.
 C) A corporation buys a short-term security issued by another corporation in the primary
 market.
 D) You make a loan to your neighbor.

- 66) The preferred habitat theory of the term structure is closely related to the _____
 A) expectations theory of the term structure.
 B) liquidity premium theory of the term structure.
 C) segmented markets theory of the term structure.
 D) the inverted yield curve theory of the term structure.
- 67) Of the four effects on interest rates from an increase in the money supply, the one that works in the opposite direction of the other three is the _____
 A) expected inflation effect. B) price level effect.
 C) income effect. D) liquidity effect.
- 68) Everything else held constant, when bonds become less widely traded, and as a consequence the market becomes less liquid, the demand curve for bonds shifts to the _____ and the interest rate _____.
 A) right; rises B) left; rises C) right; falls D) left; falls
- 69) Everything else held constant, during a business cycle expansion, the supply of bonds shifts to the _____ as businesses perceive more profitable investment opportunities, while the demand for bonds shifts to the _____ as a result of the increase in wealth generated by the economic expansion.
 A) left; left B) left; right C) right; right D) right; left
- 70) An increase in interest rates might _____ saving because more can be earned in interest income. _____
 A) disallow B) encourage C) discourage D) invalidate