

NAME: \_\_\_\_\_ Student ID: \_\_\_\_\_

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College of Business Administration  
Department of Economics  
Principles of Macroeconomics  
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ECO 2013 - 0008  
Spring 2004

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## QUIZ IV – Version 2

- This closed book QUIZ is worth 100 points.  
The exam totals 45 Multiple-Choice questions and 1 Short-Essay question.  
Each Multiple-Choice question is worth 2 points.  
The Short-Essay question is worth 10 points.  
Allocate your time accordingly.
- Including the cover page, the exam totals 12 pages.
- DO NOT forget to write your name and your student id on the exam booklet.
- Non-Programmable calculators and language dictionaries are allowed.
- At the end of the exam, hand-in the exam booklet and the computer sheet to the examiner.

**March 24, 2004**

**4:35 p.m. – 5:40 p.m.**

**BA 2-210**

## Multiple-Choice Questions (90 points)

1. After the Federal Reserve increases reserves in the banking system through open-market purchases, banks create new deposits through multiple rounds of lending and accepting deposits until the:
  - a) deposit insurance limit is reached.
  - b) actual reserve/deposit ratio is less than the desired reserve/deposit ratio.
  - c) Federal Reserve requires them to stop.
  - d) actual reserve/deposit ratio is greater than the desired reserve/deposit ratio.
  - e) actual reserve/deposit ratio is equal to the desired reserve/deposit ratio.
  
2. Precautionary saving is saving:
  - a) for protection against unexpected setbacks, such as the loss of a job or a medical emergency.
  - b) to smooth income over one's lifetime.
  - c) to meet long-term objectives, such as retirement, college attendance, or the purchase of a home.
  - d) done in anticipation of sales or bargain in the future.
  - e) for the purpose of leaving an inheritance.
  
3. If consumption spending decreases by \$5 million with no changes in net transfer payments, then:
  - a) public saving decreases.
  - b) private saving does not change.
  - c) private saving decreases.
  - d) public saving increases.
  - e) private saving increases.
  
4. When money is the basic measure of economic value, it serves as a:
  - a) double coincidence of wants.
  - b) store of value.
  - c) unit of account.
  - d) financial intermediary.
  - e) medium of exchange.
  
5. Money serves as a basic yardstick for measuring economic value (i.e., a unit of account), allowing:
  - a) private money to be issued for local use.
  - b) people to hold their wealth in a liquid form.
  - c) governments to restrict the issuance of private monies.
  - d) easy comparison of the relative prices of goods and services.
  - e) goods and services to be exchanged with a double coincidence of wants.

6. When the Federal Reserve sells government bonds to the public, this is an example of a(n):
- a) discount loan.
  - b) change in reserve requirements.
  - c) bank panic.
  - d) open-market sale.
  - e) open-market purchase.
7. During the bank panic of 1930-33, the public withdrew deposits from the bank preferring to hold currency. As a result,:
- a) bank reserves increased by less than the increase in currency causing the money supply to decrease.
  - b) bank reserves decreased by less than the increase in currency causing the money supply to increase.
  - c) bank reserves decreased but were offset by an equal increase in currency with no net effect on the money supply.
  - d) bank reserves decrease by an amount equal to the increase in currency causing the money supply to decrease.
  - e) bank reserves decreased by more than the increase in currency causing the money supply to decrease.
8. The builder of a new movie theater complex is trying to decide how many screens she wants. Below are her estimates of the number of patrons the complex will attract each year, depending on the number of screens available:

Number of Screens	Total number of patrons
1	50,000
2	90,000
3	120,000
4	140,000

After paying the movie distributor and meeting all other non-interest expenses, the owner expects to net \$2.00 per ticket sold. Construction costs are \$1,000,000 per screen. How many screens should be built if the real interest rate is 5%

- a) 5   b) 3   c) 4   d) 1   e) 2
9. If banks' desired reserve ratio increases from .10 to .15, the public still desires to hold the same amount of currency, and the Fed takes no actions, the money supply will:
- a) equal the quantity of currency that is still in use.
  - b) either increase or decrease.
  - c) decrease.
  - d) increase.
  - e) not change.

- 10.** Barter is:
- a) a means of channeling funds from savers to borrowers with productive investment opportunities.
  - b) the extension of credit to borrowers using funds raised from savers.
  - c) the direct trade of goods and services for other goods and services.
  - d) an asset used in purchasing goods and services.
  - e) an equity claim to ownership.
- 11.** The money supply in Econland is 1,500, and currency held by the public equals bank reserves. The desired reserve/deposit ratio is 0.20. Bank reserves equal \_\_\_\_.
- a) 250   b) 500   c) 1500   d) 300   e) 200
- 12.** The most important tool of monetary policy is:
- a) the minimum net worth required of banks.
  - b) reserve requirement ratios.
  - c) the discount rate.
  - d) market interest rates.
  - e) open market operations.
- 13.** Holding other factors constant, a decline in the price of new capital goods will:
- a) decrease investment
  - b) increase national saving
  - c) decrease national saving
  - d) increase the value of the marginal product of capital.
  - e) increase investment
- 14.** Liabilities are:
- a) the debts one owes.
  - b) anything of value one owns.
  - c) current income minus spending on current needs.
  - d) stocks, bonds, and credit card balances.
  - e) saving minus investment.
- 15.** The direct trade of goods and services for other goods and services is called:
- a) barter.
  - b) using a medium of exchange.
  - c) the efficient allocation of resources.
  - d) financial intermediation.
  - e) diversification.



- 23.** In an open-market sale the Federal Reserve \_\_\_ government bonds and the supply of bank reserves \_\_\_\_.
- a)** buys; decreases
  - b)** sells; does not change
  - c)** buys; increases
  - d)** sells; decreases
  - e)** sells; increases
- 24.** Banks hold reserves:
- a)** to meet depositor withdrawals and payments.
  - b)** to earn interest.
  - c)** only because the government requires them to hold reserves.
  - d)** to escape the double coincidence of wants.
  - e)** to increase profits.
- 25.** Double coincidence of wants is avoided if money is used as a:
- a)** store of value
  - b)** tool of monetary policy.
  - c)** measure of value.
  - d)** standard of deferred payment.
  - e)** medium of exchange.
- 26.** The most important, most convenient, and most flexible way in which the Federal Reserve affects the supply of bank reserves is through:
- a)** changing bank reserve requirement ratios.
  - b)** conducting open-market operations.
  - c)** changing interest rates.
  - d)** conducting bank examinations.
  - e)** changing the Federal Reserve discount rate.
- 27.** If the saving rate in an economy decreases and capital gains (net of capital losses) are earned of an amount equal, the economy's:
- a)** assets will decrease.
  - b)** wealth will decrease.
  - c)** liabilities will decrease.
  - d)** wealth will remain unchanged.
  - e)** wealth will increase.



- 34.** Money is:
- a) the market value of all final goods and services produced in a country in a year.
  - b) any asset used to make purchases.
  - c) the sum of assets minus debts.
  - d) the same as income.
  - e) all financial assets.

- 35.** If the Federal Reserve wants to increase the money supply, it should:
- a) conduct open-market sales.
  - b) increase reserve requirements.
  - c) increase the discount rate.
  - d) raise interest rates.
  - e) conduct open-market purchases.

- 36.** If net taxes paid by households increase,:
- a) public saving will decrease.
  - b) private saving will decrease.
  - c) transfer payments to households will increase.
  - d) private saving will increase.
  - e) transfer payments to households will decrease.

- 37.** You are given the following information about the economy:

Household saving	300
Business saving	700
Government purchases	1,000
Government transfers and interest payments	500
Government tax collections	1,500
GDP	5,000

Private saving is \_\_\_\_\_ and national saving is \_\_\_\_\_.

- a) 700; 0    b) 1,000; 1,500    c) 1,000; 2,000    d) 1,000; 1,000    e) 300; -200

- 38.** Social Security benefits, welfare payments, and farm support payments are examples of:
- a) public interest payments
  - b) consumption spending
  - c) transfer payments
  - d) government spending
  - e) investment spending

- 39.** In Macroland, currency held by the public is 2,000 econs, bank reserves are 300 econs, and the desired reserve/deposit ratio is 10 percent. If the Central Bank raises the required reserve/deposit ratio making the new desired ratio equal to 15 percent, then the money supply in Macroland will \_\_\_\_\_ to \_\_\_\_\_ econs, assuming that the public does not wish to change the amount of currency it holds.
- a) increase; 5,000
  - b) decrease; 4,000
  - c) decrease; 5,000
  - d) decrease; 2,300
  - e) increase; 4,000
- 40.** The opportunity cost of capital investment is the:
- a) value of the marginal product of labor.
  - b) real interest rate.
  - c) price of new capital goods.
  - d) value of the marginal product of capital.
  - e) price of the firm's output.
- 41.** If the reserve/deposit ratio is less than 100%, then the banking system engages in:
- a) 100% reserve banking.
  - b) capital investment.
  - c) credit allocation.
  - d) fractional-reserve banking.
  - e) the double coincidence of wants.
- 42.** Holding other factors constant, if new environmental regulations increase firms' cost of operating capital, then the real interest rate will \_\_\_\_\_ and the equilibrium quantity of national saving and investment will \_\_\_\_\_.
- a) increase; not change
  - b) increase; increase
  - c) decrease; increase
  - d) decrease; decrease
  - e) increase; decrease
- 43.** To the extent that households are target savers, who save to reach a specific goal, a decrease in the interest rate \_\_\_\_\_ household saving.
- a) may either increase or decrease
  - b) increases
  - c) decreases
  - d) does not affect
  - e) cuts in half

**44.** You are given the following information about the economy:

Consumption	3000
Government budget surplus	500
Government transfers and interest payments	750
Government tax collections	1,750
GDP	6,000

Public saving is \_\_\_\_\_ and national saving is \_\_\_\_\_.

- a)** 500; 2,500    **b)** 750; 2,750    **c)** 500; 500    **d)** 1,250; 2,000    **e)** 500; 3,500

**45.** The introduction of credit cards and debit cards has \_\_\_\_\_ velocity.

- a)** had no impact on    **b)** increased    **c)** doubled    **d)** decreased    **e)** eliminated

### Answer Key

1. e
2. a
3. e
4. c
5. d
6. d
7. d
8. b
9. c
10. c
11. a
12. e
13. e
14. a
15. a
16. a
17. c
18. b
19. b
20. d
21. c
22. e
23. d
24. a
25. e
26. b
27. d
28. c
29. d
30. d
31. b
32. e
33. d
34. b
35. e
36. b
37. d
38. c
39. b
40. b
41. d
42. d
43. b
44. a
45. b

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**Short-Essay Question (10 points)**

**Answer in the given space below each question.**

“A high rate of money growth generally leads to inflation.”

- A. Using the quantity equation, show that the rate of growth of the money supply equals the rate of inflation.
- B. Now, if you are in charge of the Federal Reserve System, what are the three tools that you can use to change the money supply?
- C. What would the Fed do with each tool if it wanted to increase the money supply?

Solution

- A. Quantity Equation  $M \times V = P \times Y$   
If V and Y are constant, then the percentage increase in the money supply leads to the same percentage increase in the price level.
- B. Open market operations, the reserve requirement, and discount window lending.
- C. Make open market purchases, lower the reserve requirement, lower the discount rate to increase discount window lending.