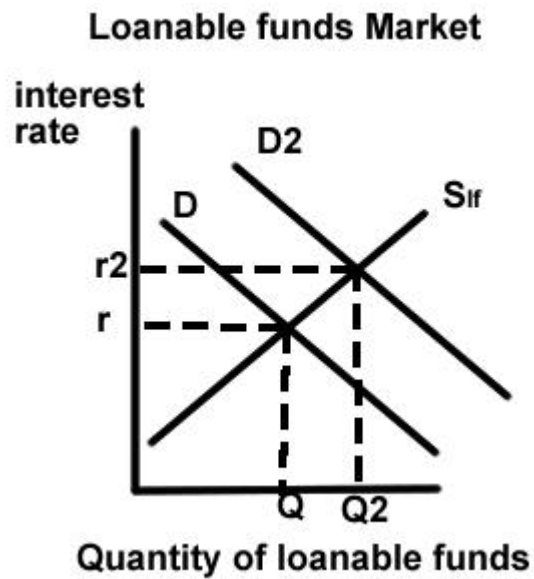


Financial Sector 40 Question Multiple Choice
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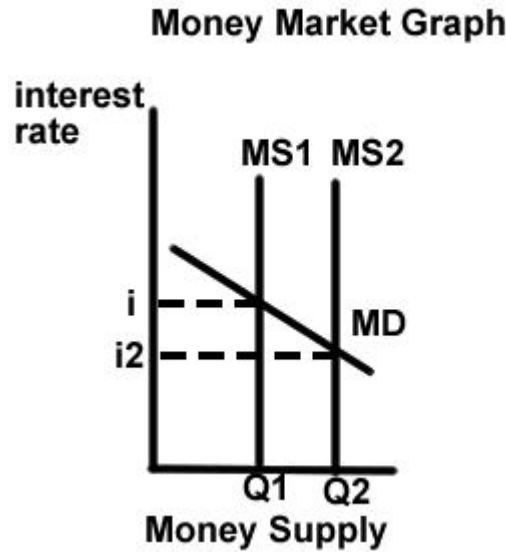
Financial Sector

1. Refer to the graph. Which of the following would most likely cause an increase in real interest rates illustrated on this graph?



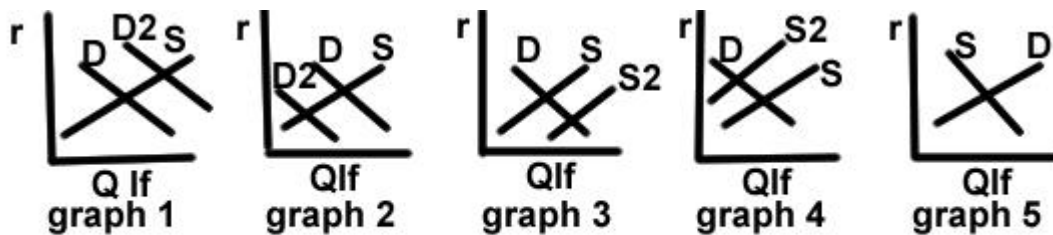
- (A) expectations of economic growth
- (B) expectations of inflation
- (C) a decrease in consumption
- (D) a decrease in budget deficits
- (E) an increase in savings

2. Which of the following would explain a shift in the money supply from MS1 to MS2?



- (A) an increase in the interest rates at the Federal Reserve Bank's discount window
- (B) a decrease in bank reserves
- (C) an increase in bond purchases by the Federal Reserve Bank's open market operations
- (D) an increase in the supply of U.S. dollars in the foreign currency exchange
- (E) a decrease in demand to hold currency

3. Refer to the graphs. Assume that the loanable funds market is initially in equilibrium at $S = D$. Now suppose that new energy technology encourages the construction of new buildings and the renovation of old building. Which graph would best illustrate the initial effect of the new technology?



LOANABLE FUNDS GRAPHS

- (A) graph 1
- (B) graph 2
- (C) graph 3
- (D) graph 4
- (E) graph 5

4. Refer to the Refbrun CB Balance Sheet. The bank lends \$10,000 to a local business. What two accounting entries must be made?

Refbrun Community Bank Balance Sheet			
(\$millions)			
Assets		Liabilities	
Reserves	20	Deposits	160
Loans	120	Other Liabilities	20
Securities	50	Total Liability	180
Physical Assets	10	Net Worth	20
Total Assets	200	Total Liabilities and Net Worth	200

- (A) Add \$10,000 to Loans and \$10,000 to Investments.
- (B) Add \$10,000 to Loans and subtract \$10,000 from Reserves.
- (C) Add \$10,000 to Investments and subtract \$10,000 from Loans.
- (D) Add \$10,000 to Loans and add \$10,000 to Reserves.
- (E) Subtract \$10,000 from Loans and subtract \$10,000 from Reserves.

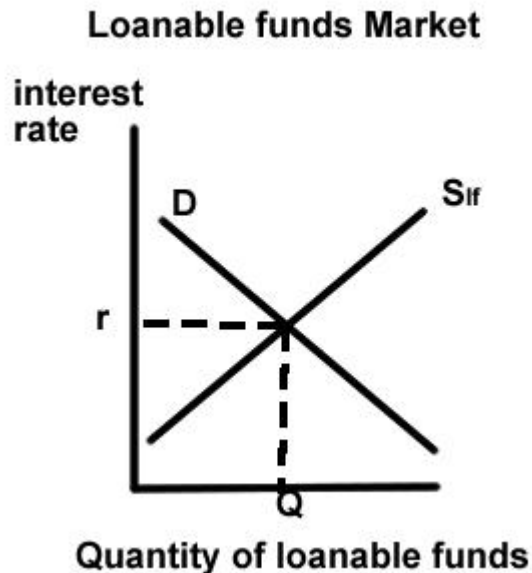
5. Which of the following best describes the monetary base of an economy?

- (A) the currency in circulation
- (B) the currency in circulation and reserves held by banks
- (C) the currency in circulation, reserves held by banks, loans made by banks
- (D) the currency in circulation, reserves held by banks, loans made by banks and currency held by the treasury.
- (E) reserves held by banks

6. Velocity is calculated by dividing

- (A) real GDP by the price level
- (B) nominal GDP by the price level
- (C) real GDP by the money supply
- (D) nominal GDP by the money supply
- (E) real GDP by Nominal GDP

7. Refer to the graph. The supply of loanable funds (S_{lf}) illustrated on this graph refers to



- ___ (A) the supply of money entering the currency exchange market
- ___ (B) the money supply created by the Federal Reserve Bank
- ___ (C) the supply of money held in reserves.
- ___ (D) the savings of households
- ___ (E) the monetary base

8. If Betty Sue deposits her \$500 dollar paycheck into the Refbrun Bank, the bank will not

- ___ (A) have an increase in reserves.
- ___ (B) have an increase in assets.
- ___ (C) have an increase in liabilities.
- ___ (D) have an increase in net worth.
- ___ (E) have an increase in excess reserves.

9. Which of the following would diminish the affect of the money multiplier?

- ___ (A) an expansionary monetary policy
- ___ (B) an increase in household incomes
- ___ (C) an increase in spending
- ___ (D) an increase in excess reserves held by banks
- ___ (E) a decrease in cash held by the public

10. Excess reserves are:

- (A) Reserves that banks are required to hold
- (B) Total reserves that banks hold
- (C) Reserves that cannot be used for loans
- (D) Reserves that banks hold that are greater than the legally required reserves
- (E) Reserves that have not created a liability to the banks

11. Refer to the Balance Sheet for the Refbrun Community Bank. The Federal Reserve Bank requires all banks to keep 10% of Transaction deposits that exceed \$50 million as required reserves. What are the required reserves for the Refbrun community Bank?

Assets		Liabilities	
Reserves	20	Deposits	160
Loans	120	Other Liabilities	20
Securities	50	Total Liability	180
Physical Assets	10	Net Worth	20
Total Assets	200	Total Liabilities and Net Worth	200

- (A) \$10 million
- (B) \$11 million
- (C) \$16 million
- (D) \$8 million
- (E) \$ 4 million

12. If banks charge 5% nominal interest on loans made and the expected rate of inflation is 2%, then the real interest rate is:

- (A) 5%
- (B) 7%
- (C) 3%
- (D) not part of the nominal interest rate
- (E) less than expected rate of inflation

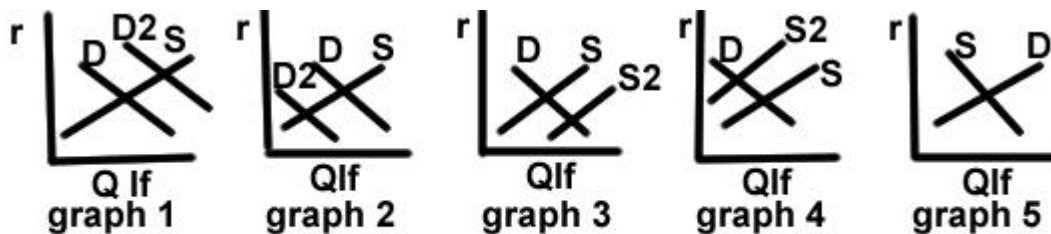
13. The Banking (Money) multiplier is calculated by the formula:

- (A) $1/1-mpc$ (mpc =marginal propensity to consume)
- (B) $1/mps$ (mps = marginal propensity to save)
- (C) $1/IR$ (IR = Interest rate)
- (D) $1/RR$ (RR = reserve requirement)
- (E) $1/DR$ (DR = discount rate)

14. Which of the following would most likely have a negative effect on the velocity of money?

- (A) An increase in the marginal propensity to consume
- (B) An increase in the number of consumers
- (C) An increase in price level
- (D) An increase in hoarding
- (E) An increase in national income

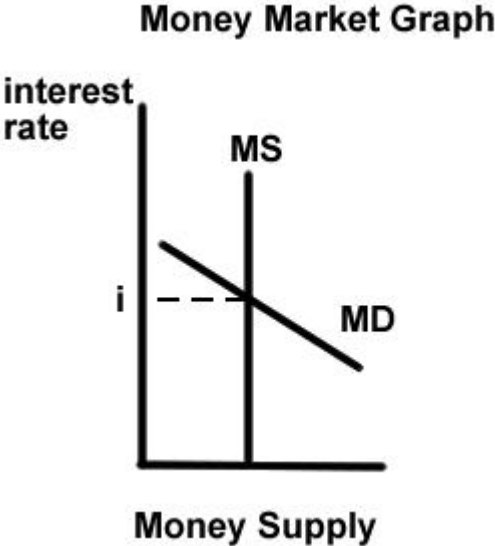
15. Refer to the loanable funds graphs. Begin with the loanable funds market in equilibrium at $S = D$. Then assume that the marginal propensity to save increases. Which graph would best illustrate the effect of this change?



LOANABLE FUNDS GRAPHS

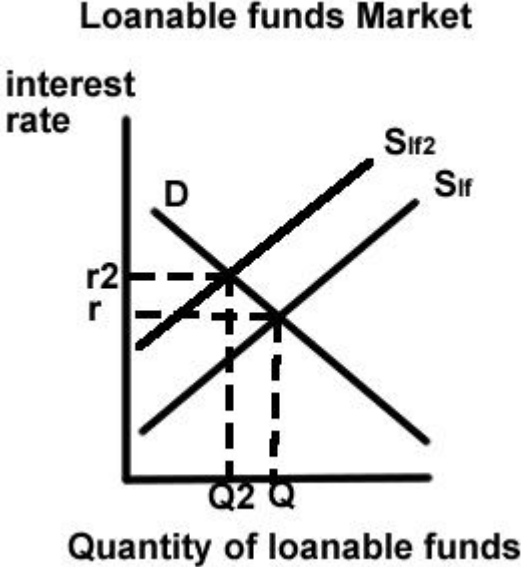
- (A) graph 1
- (B) graph 2
- (C) graph 3
- (D) graph 4
- (E) graph 5

16. Refer to the money graph. The money demand (MD) represents



- ___ (A) the demand to borrow money
- ___ (B) the demand to hold money as an asset
- ___ (C) the demand to increase the money supply
- ___ (D) the demand to save money in a bank
- ___ (E) the demand to purchase goods

17. Refer to the graph. Which of the following would best explain the increase in interest rates illustrated by this graph?



- ___ (A) a decrease in the marginal propensity to consume
- ___ (B) an increase in the marginal propensity to save
- ___ (C) an increase in Investment demand
- ___ (D) an increase in financial capital leaving the country
- ___ (E) a decrease in Investment demand

18. If the Federal Reserve Bank increases the reserve requirement, what would be the most likely effect on money supply and interest rates?

- ___ (A) money supply would increase and interest rates would increase
- ___ (B) money supply would increase and interest rates would decrease
- ___ (C) money supply would decrease and interest rates would increase
- ___ (D) money supply would decrease and interest rates would decrease
- ___ (E) money supply and interest rates would remain constant

19. Refer to the balance sheet for the Refbrun Community Bank. The bank recognizes a default on a loan of \$20,000 that cannot be recovered. What two accounting entries should be made?

Refbrun Community Bank Balance Sheet
(\$millions)

Assets		Liabilities	
Reserves	20	Deposits	160
Loans	120	Other Liabilities	20
Securities	50	Total Liability	180
Physical Assets	10	Net Worth	20
Total Assets	200	Total Liabilities and Net Worth	200

- ___ (A) Subtract \$20,000 from Loans and subtract 20,000 from Reserves.
- ___ (B) Subtract \$20,000 from Loans and subtract 20,000 from Investment.
- ___ (C) Subtract \$20,000 from Loans and subtract \$20,000 from Other Liabilities
- ___ (D) Subtract \$20,000 from Loans and add \$20,000 from Other Liabilities.
- ___ (E) Subtract \$20,000 from Loans and subtract \$20,000 from Net Worth.

20. The country of Alpha is experiencing 7% inflation. If this rate of inflation continues for the next 20 years, we can expect the price level to double in approximately:

- (A) 20 years
- (B) 5 years
- (C) 15 years
- (D) 3 years
- (E) 10 years

21. Which of the following would not be considered a form of money?

- (A) currency
- (B) checking accounts
- (C) debit cards
- (D) credit cards
- (E) none of the above

22. Using money as a medium of exchange replaces the need to

- (A) save
- (B) work
- (C) barter
- (D) borrow
- (E) use checks

23. Which of the following is included in M2 but not M1

- (A) currency in circulation
- (B) demand deposits
- (C) money market accounts
- (D) traveler's checks
- (E) repurchase agreements

24. Which of the following is not accurate?

- (A) Money is used as a medium of exchange.
- (B) Money is a real asset.
- (C) Money is used as a standard of value.
- (D) Money definitions include M1, M2, and M3.
- (E) Money is used as a store of value.

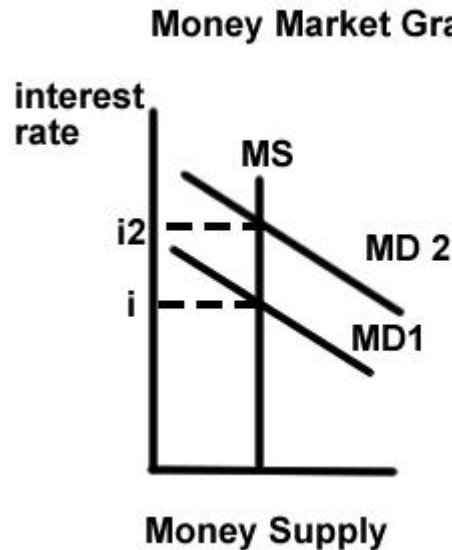
25. If a bond with duration of 1 yr is purchased for \$1,000 and at the end of the year the purchaser receives \$1,100 the interest rate paid on the bond was?

- ___ (A) 1%
- ___ (B) 10%
- ___ (C) 100%
- ___ (D) 11%
- ___ (E) 110%

26. The federal funds rate is the interest rate that

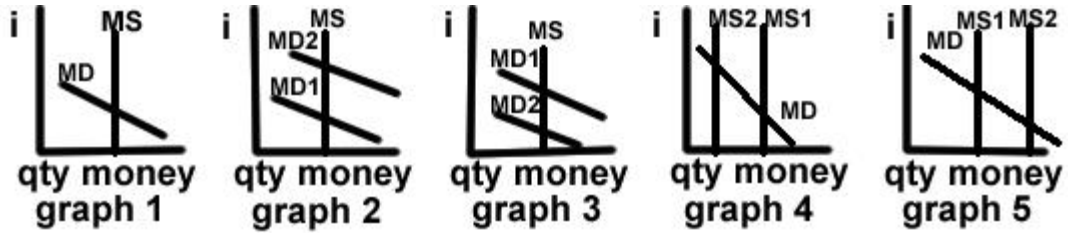
- ___ (A) the interest rate that Federal Reserve Bank charges other banks
- ___ (B) the interest rate that banks charge the government to borrow money
- ___ (C) the interest rate that banks charge their prime customers
- ___ (D) the interest rate that a bank charges another bank to borrow funds overnight
- ___ (E) the interest rate that the Federal Reserve Bank charges state institutions

27. Refer to the graph. Which of the following would explain the shift in money demand from MD1 to MD2?



- ___ (A) a decrease in incomes
- ___ (B) an increase in expectations for higher bond values
- ___ (C) an increase in price level
- ___ (D) a decrease in price level
- ___ (E) a decrease in the opportunity cost of holding money

28. Refer to the graphs. Assume that the money market is initially in equilibrium where $MD = MS$. Then the Federal Reserve Bank buys bonds in the open market. Which graph best illustrates the effect of these purchases?

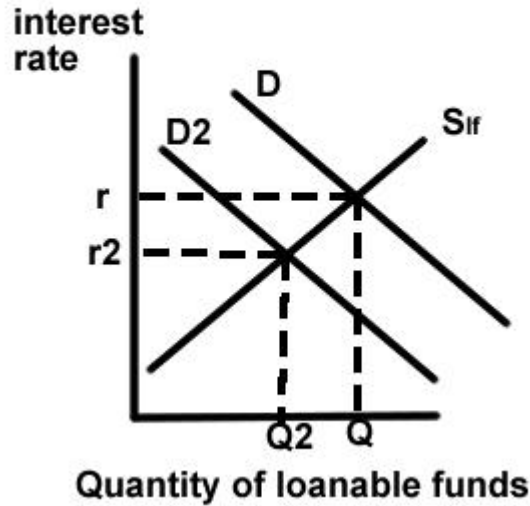


Money Market Graphs

- ___ (A) graph 1
- ___ (B) graph 2
- ___ (C) graph 3
- ___ (D) graph 4
- ___ (E) graph 5

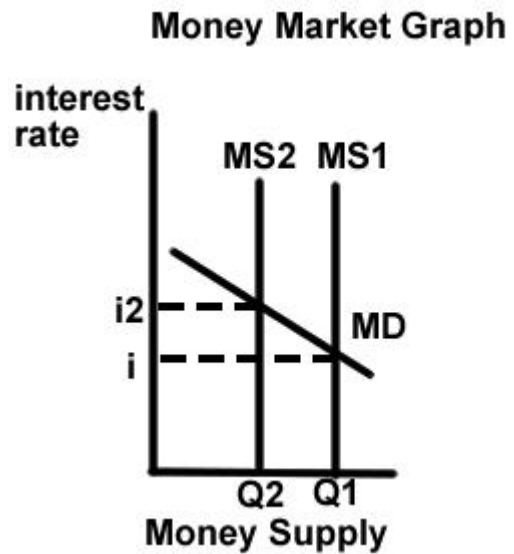
29. Refer to the graph. Which of the following would most likely decrease the interest rate illustrated by this graph?

Loanable funds Market



- ___ (A) Expectations of an economic boom
- ___ (B) An increase in Investment demand
- ___ (C) Expectations of a severe recession
- ___ (D) A decrease in savings
- ___ (E) An increase in consumption

30. Refer to the money market graph. Which of the following is true if the money supply changes from MS1 to MS2?



- (A) The Federal Reserve Bank has increased the money supply.
- (B) The opportunity cost of holding cash has increased.
- (C) The Federal Reserve Bank has decreased the reserve requirement.
- (D) Household incomes have increased.
- (E) Preferences for liquidity have increased.

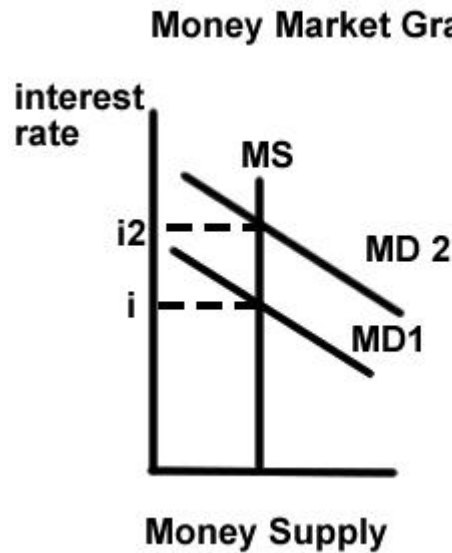
31. Refer to the Refbrun Community Bank Balance Sheet. If Lola Paloosa deposits \$1,000 into the Refbrun Community Bank, what two accounting entries should be made?

Refbrun Community Bank Balance Sheet
(\$millions)

Assets		Liabilities	
Reserves	20	Deposits	160
Loans	120	Other Liabilities	20
Securities	50	Total Liability	180
Physical Assets	10	Net Worth	20
Total Assets	200	Total Liabilities and Net Worth	200

- ___ (A) Subtract \$1,000 from Deposits and add \$1,000 to Loans.
- ___ (B) Add \$1,000 to Deposits and subtract \$1,000 from Reserves.
- ___ (C) Add \$1,000 to Deposits and add \$1,000 to Reserves.
- ___ (D) Subtract \$1,000 from Deposits and add \$1,000 to Loans.
- ___ (E) Add \$1,000 to Deposits and add \$1,000 to Investments.

32. Refer to the graph. Which of the following would cause a increase in interest rates from i to i_2 illustrated by this graph?



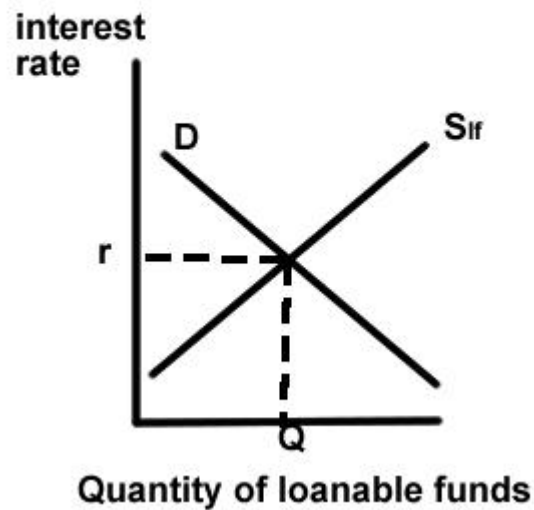
- (A) A decrease in household incomes
- (B) An increase in the price level
- (C) An increase in the money supply
- (D) An increase in bank reserves
- (E) An increase in unemployment.

33. In the secondary bond market where already issued bonds are traded, an increase in the interest rate will lead to

- (A) an increase in interest payments on these already issued bonds
- (B) a decrease in the price of these already issued bonds
- (C) an increase obligation for the companies that have already issued these bonds
- (D) an increase in the interest payments on bonds that will be issued in the near future
- (E) an increase in the price of these already issued bonds

34. Refer to the graph. The demand (D) illustrated on this graph refers to the

Loanable funds Market



- (A) demand to hold bonds
- (B) demand to finance real investment
- (C) demand to finance consumption
- (D) demand to save money
- (E) demand to increase liquidity

35. When the U.S. Economy is experiencing a high rate of inflation; the Federal Reserve Bank can try to lower inflation by

- (A) increasing the sale of bonds
- (B) decreasing the reserve requirement
- (C) decreasing the interest rates at the discount window
- (D) putting more currency in circulation
- (E) decreasing the sale of bonds

36. Refer to the Refbrun Community Bank Balance Sheet. This bank borrows \$2,000 overnight from another bank. What two accounting entries should be made?

Refbrun Community Bank Balance Sheet			
(\$millions)			
Assets		Liabilities	
Reserves	20	Deposits	160
Loans	120	Other Liabilities	20
Securities	50	Total Liability	180
Physical Assets	10	Net Worth	20
Total Assets	200	Total Liabilities and Net Worth	200

- (A) Add \$2,000 to Loans and add \$2000 to Other Liabilities.
- (B) Add \$2,000 to Loans and subtract \$2,000 from Other Liabilities.
- (C) Add \$2,000 to Reserves and subtract \$2,000 from Investments.
- (D) Add \$2,000 to Reserves and add \$2,000 to Other Liabilities.
- (E) Add \$2,000 to Investments and add \$2,000 to Other Liabilities.

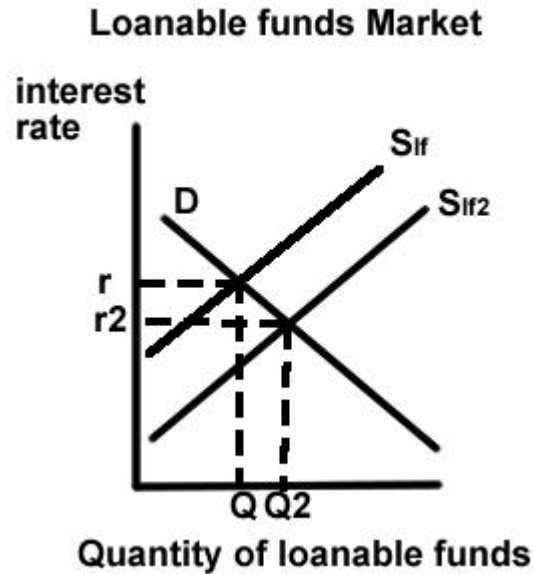
37. In the basic quantity equation of money: $M \cdot V = P \cdot Q$, the right hand side of the equation represents:

- (A) price level
- (B) bank reserves
- (C) real GDP
- (D) nominal GDP
- (E) monetary base

38. Which of the following statements accurately describes the difference between a stock and a bond?

- (A) A bond represents an owner's share of a business and a stock represents a liability of a business.
- (B) A bond holder is paid a dividend and a stock holder receives interest payments.
- (C) A stock is considered an asset and a bond is not considered an asset.
- (D) A bond represents a liability of a business and a stock represents ownership of a corporation.
- (E) A bond can be resold in a secondary market and a stock cannot be resold.

39. Refer to the graph. Which of the following would most likely explain the decrease in interest rates illustrated on this graph?



- (A) Expectations of a recession
- (B) An increase in the marginal propensity to consume
- (C) A decrease in Investment
- (D) A decrease in financial capital flows into the country
- (E) A decrease in the marginal propensity to consume

40. In the quantity equation of money: $M \cdot V = P \cdot Q$
 V represents:

- (A) the speed at which money circulates in the economy
- (B) the value of the dollar
- (C) the real GDP
- (D) the money that is supplied in the money market
- (E) the money that is supplied in the loanable funds market