

Name _____

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Section Number _____

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

- 1) If housing prices are expected to increase, then, other things equal, the demand for houses will _____ and that of Treasury bills will _____. 1) _____
 A) increase; decrease B) increase; increase
 C) decrease; decrease D) decrease; increase
- 2) Using the Gordon growth formula, if D_1 is \$1.00, k_e is 10% or 0.10, and g is 5% or 0.05, then the current stock price is 2) _____
 A) \$10. B) \$20. C) \$30. D) \$40.
- 3) If \$22,050 is the amount payable in two years for a \$20,000 simple loan made today, the interest rate is 3) _____
 A) 5 percent. B) 10 percent. C) 22 percent. D) 25 percent.
- 4) According to the expectations theory of the term structure 4) _____
 A) investors have strong preferences for short-term relative to long-term bonds, explaining why yield curves typically slope upward.
 B) when the yield curve is downward sloping, short-term interest rates are expected to remain relatively stable in the future.
 C) yield curves should be equally likely to slope downward as slope upward.
 D) when the yield curve is steeply upward sloping, short-term interest rates are expected to remain relatively stable in the future.
- 5) When the price of a bond is _____ the equilibrium price, there is an excess demand for bonds and price will _____. 5) _____
 A) below; rise B) below; fall C) above; rise D) above; fall
- 6) A monetary expansion _____ stock prices due to a decrease in the _____ and an increase in the _____, everything else held constant. 6) _____
 A) increases; required rate of return; dividend growth rate
 B) reduces; future sales price; expected rate of return
 C) increases; required rate of return; future sales price
 D) reduces; current dividend; expected rate of return
- 7) Bonds issued by state and local governments are called _____ bonds. 7) _____
 A) commercial B) Treasury C) corporate D) municipal
- 8) The demand for gold increases, other things equal, when 8) _____
 A) interest rates are expected to rise.
 B) interest rates are expected to fall.
 C) the market for silver becomes more liquid.
 D) real estate prices are expected to increase.

- 9) Which of the following are true concerning the distinction between interest rates and returns? 9) _____
- A) The return can be expressed as the sum of the discount yield and the rate of capital gains.
 - B) The rate of return on a bond will not necessarily equal the interest rate on that bond.
 - C) The rate of return will be greater than the interest rate when the price of the bond falls between time t and time $t + 1$.
 - D) The return can be expressed as the difference between the current yield and the rate of capital gains.
- 10) Countries that experience very high rates of inflation may also have 10) _____
- A) falling money supplies.
 - B) constant money supplies.
 - C) rapidly growing money supplies.
 - D) balanced budgets.
- 11) The demand for silver decreases, other things equal, when 11) _____
- A) wealth grows rapidly.
 - B) interest rates are expected to rise.
 - C) the gold market is expected to boom.
 - D) the market for silver becomes more liquid.
- 12) Banks, savings and loan associations, mutual savings banks, and credit unions 12) _____
- A) are no longer important players in financial intermediation.
 - B) have been adept at innovating in response to changes in the regulatory environment.
 - C) since deregulation now provide services only to small depositors.
 - D) produce nothing of value and are therefore a drain on society's resources.
- 13) An increase in the liquidity of corporate bonds will _____ the price of corporate bonds and _____ the yield of Treasury bonds, everything else held constant. 13) _____
- A) reduce; increase
 - B) increase; reduce
 - C) increase; increase
 - D) reduce; reduce
- 14) When the total value of final goods and services is calculated using current prices, the resulting measure is referred to as 14) _____
- A) real GDP.
 - B) nominal GDP.
 - C) the index of leading indicators.
 - D) the GDP deflator.
- 15) If fluctuations in interest rates become smaller, then, other things equal, the demand for stocks _____ and the demand for long-term bonds _____. 15) _____
- A) increases; decreases
 - B) decreases; decreases
 - C) decreases; increases
 - D) increases; increases
- 16) If bad credit risks are the ones who most actively seek loans and, therefore, receive them from financial intermediaries, then financial intermediaries face the problem of 16) _____
- A) moral hazard.
 - B) adverse selection.
 - C) free-riding.
 - D) costly state verification.
- 17) Using the Gordon growth model, a stock's price will increase if 17) _____
- A) the growth rate of dividends falls.
 - B) the required rate of return on equity rises.
 - C) the dividend growth rate increases.
 - D) the expected sales price rises.

- 18) If the expected path of 1-year interest rates over the next five years is 1 percent, 2 percent, 3 percent, 4 percent, and 5 percent, the expectations theory predicts that the bond with the highest interest rate today is the one with a maturity of _____ 18) _____
 A) two years. B) three years. C) four years. D) five years.
- 19) Using the one-period valuation model, assuming a year-end dividend of \$0.11, an expected sales price of \$110, and a required rate of return of 10%, the current price of the stock would be _____ 19) _____
 A) \$121.12. B) \$110.11. C) \$100.10. D) \$100.11
- 20) An \$8,000 coupon bond with a \$400 coupon payment every year has a coupon rate of _____ 20) _____
 A) 5 percent. B) 8 percent. C) 10 percent. D) 40 percent.
- 21) Banks and other financial institutions engage in financial intermediation, which _____ 21) _____
 A) can hurt the performance of the economy.
 B) involves borrowing from investors and lending to savers.
 C) can benefit economic performance.
 D) has no effect on economic performance.
- 22) The total collection of pieces of property that serve to store value is a person's _____ 22) _____
 A) credit. B) wealth. C) money. D) income.
- 23) If there are five goods in a barter economy, one needs to know ten prices in order to exchange one good for another. If, however, there are ten goods in a barter economy, then one needs to know _____ prices in order to exchange one good for another. _____ 23) _____
 A) 20 B) 25 C) 30 D) 45
- 24) If the interest rates on all bonds rise from 5 to 6 percent over the course of the year, which bond would you prefer to have been holding? _____ 24) _____
 A) A bond with ten years to maturity B) A bond with one year to maturity
 C) A bond with five years to maturity D) A bond with twenty years to maturity
- 25) Securities are _____ for the person who buys them, but are _____ for the individual or firm that issues them. _____ 25) _____
 A) liabilities; assets B) negotiable; nonnegotiable
 C) assets; liabilities D) nonnegotiable; negotiable
- 26) The organization responsible for the conduct of monetary policy in the United States is the _____ 26) _____
 A) U.S. Treasury. B) Comptroller of the Currency.
 C) Federal Reserve System. D) Bureau of Monetary Affairs.
- 27) During a "flight to quality" _____ 27) _____
 A) the spread between Treasury bonds and Baa bonds increases.
 B) the spread between Treasury bonds and Baa bonds decreases.
 C) the spread between Treasury bonds and Baa bonds is not affected.
 D) the change in the spread between Treasury bonds and Baa bonds cannot be predicted.
- 28) The supply curve for bonds has the usual upward slope, indicating that as the price _____, ceteris paribus, the _____ increases. _____ 28) _____
 A) rises; supply B) falls; supply
 C) falls; quantity supplied D) rises; quantity supplied

- 29) A consol paying \$20 annually when the interest rate is 5 percent has a price of _____
A) \$100. B) \$200. C) \$400. D) \$800.
- 30) Equity instruments are traded in the _____ market. _____
A) capital B) commodities C) bond D) money
- 31) Assuming the same coupon rate and maturity length, the difference between the yield on a Treasury Inflation Protected Security and the yield on a non-indexed Treasury security provides insight into _____
A) the nominal interest rate. B) the real interest rate.
C) the nominal exchange rate. D) the expected inflation rate.
- 32) Which of the following sequences accurately describes the evolution of the payments system? _____
A) Barter, coins made of precious metals, paper currency, checks, electronic funds transfers
B) Barter, checks, paper currency, coins made of precious metals, electronic funds transfers
C) Barter, checks, paper currency, electronic funds transfers
D) Barter, coins made of precious metals, checks, paper currency, electronic funds transfers
- 33) If a security pays \$55 in one year and \$133 in three years, its present value is \$150 if the interest rate is _____
A) 5 percent. B) 10 percent. C) 12.5 percent. D) 15 percent.
- 34) In which of the following situations would you prefer to be the borrower? _____
A) The interest rate is 4 percent and the expected inflation rate is 1 percent.
B) The interest rate is 9 percent and the expected inflation rate is 7 percent.
C) The interest rate is 13 percent and the expected inflation rate is 15 percent.
D) The interest rate is 25 percent and the expected inflation rate is 50 percent.
- 35) A key assumption in the segmented markets theory is that bonds of different maturities _____
A) are substitutes only if the investor is given a premium incentive.
B) are perfect substitutes.
C) are not substitutes at all.
D) are substitutes but not perfect substitutes.
- 36) U.S. dollar deposits in foreign banks outside the U.S. or in foreign branches of U.S. banks are called _____. _____
A) Eurodollars B) outside dollars C) foreign dollars D) Atlantic dollars
- 37) People hold money even during inflationary episodes when other assets prove to be better stores of value. This can be explained by the fact that money is _____
A) a unique good for which there are no substitutes.
B) extremely liquid.
C) the only thing accepted in economic exchange.
D) backed by gold.
- 38) Which of the following is not included in the M1 measure of money but is included in the M2 measure of money? _____
A) Small-denomination time deposits B) Demand deposits
C) Traveler's checks D) Currency

- 39) The primary purpose of deposit insurance is to _____
 A) improve the flow of information to investors.
 B) protect bank employees from unemployment.
 C) prevent banking panics.
 D) protect bank shareholders against losses.
- 40) The difference between money and income is that _____
 A) there is no difference□money and income are both stocks.
 B) money is a stock and income is a flow.
 C) money is a flow and income is a stock.
 D) there is no difference□money and income are both flows.
- 41) A discount bond selling for \$15,000 with a face value of \$20,000 in one year has a yield to maturity of _____
 A) 3 percent. B) 20 percent. C) 25 percent. D) 33.3 percent.
- 42) Suppose you are holding a 5 percent coupon bond maturing in one year with a yield to maturity of 15 percent. If the interest rate on one-year bonds rises from 15 percent to 20 percent over the course of the year, what is the yearly return on the bond you are holding? _____
 A) 5 percent B) 10 percent C) 15 percent D) 20 percent
- 43) Budget deficits are important because deficits _____
 A) always cause prices to fall.
 B) always cause interest rates to fall.
 C) cause bank failures.
 D) can result in higher rates of monetary growth.
- 44) If ten years ago the prices of the items bought last month by the average consumer would have been much higher, then one can likely conclude that _____
 A) the aggregate price level has declined during this ten-year period.
 B) the average rate of money growth for this ten-year period has been positive.
 C) the aggregate price level has risen during this ten-year period.
 D) the average inflation rate for this ten-year period has been positive.
- 45) The present value of a fixed-payment loan is calculated as the _____ of the present value of all cash flow payments. _____
 A) difference B) multiple C) sum D) log
- 46) If you expect the inflation rate to be 12 percent next year and a one-year bond has a yield to maturity of 7 percent, then the real interest rate on this bond is _____
 A) -5 percent. B) -2 percent. C) 2 percent. D) 12 percent.
- 47) If an individual moves money from a money market deposit account to currency, _____
 A) M1 increases and M2 stays the same.
 B) M1 stays the same and M2 increases.
 C) M1 stays the same and M2 stays the same.
 D) M1 increases and M2 decreases.

- 48) Bonds with relatively low risk of default are called _____ securities and have a rating of Baa (or BBB) and above; bonds with ratings below Baa (or BBB) have a higher default risk and are called _____. 48) _____
- A) investment grade; junk bonds B) high quality; lower grade
 C) high quality; junk bonds D) investment grade; lower grade
- 49) If prices in the bond market become more volatile, everything else held constant, the demand curve for bonds shifts _____ and interest rates _____. 49) _____
- A) left; rise B) right; rise C) right; fall D) left; fall
- 50) The primary assets of a finance company are _____ 50) _____
- A) corporate stocks and bonds. B) municipal bonds.
 C) mortgages. D) consumer and business loans.

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