

Name \_\_\_\_\_

ID Number \_\_\_\_\_

Section Number \_\_\_\_\_

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

- 1) There are \_\_\_\_\_ members of the Board of Governors of the Federal Reserve System. 1) \_\_\_\_\_  
A) 5                      B) 7                      C) 12                      D) 19
- 2) Measuring the sensitivity of bank profits to changes in interest rates by multiplying the gap times the change in the interest rate is called 2) \_\_\_\_\_  
A) gap-exposure analysis.                      B) basic gap analysis.  
C) interest-exposure analysis.                      D) basic duration analysis.
- 3) Assuming initially that  $r = 10\%$ ,  $c = 40\%$ , and  $e = 0$ , an increase in  $r$  to 15% causes the M1 money multiplier to \_\_\_\_\_, everything else held constant. 3) \_\_\_\_\_  
A) decrease from 2.8 to 2.55                      B) increase from 2.55 to 2.8  
C) increase from 1.82 to 2                      D) decrease from 2 to 1.82
- 4) As the costs associated with deposit outflows \_\_\_\_\_, the banks willingness to hold excess reserves will \_\_\_\_\_. 4) \_\_\_\_\_  
A) increase; decrease                      B) increase; increase  
C) decrease; increase                      D) decrease; not be affected
- 5) Which of the following is NOT an entity of the Federal Reserve System? 5) \_\_\_\_\_  
A) The Board of Governors  
B) Federal Reserve Banks  
C) The Federal Open Market Committee  
D) The Comptroller of the Currency
- 6) Each Federal Reserve bank has nine directors. Of these \_\_\_\_\_ are appointed by the member banks and \_\_\_\_\_ are appointed by the Board of Governors. 6) \_\_\_\_\_  
A) four; five                      B) six; three                      C) five; four                      D) three; six
- 7) The difference of rate-sensitive liabilities and rate-sensitive assets is known as the 7) \_\_\_\_\_  
A) rate-risk index.                      B) duration.  
C) interest-sensitivity index.                      D) gap.
- 8) Everything else held constant, in the market for reserves, when the federal funds rate is 3%, raising the discount rate from 5% to 6% 8) \_\_\_\_\_  
A) has an indeterminate effect on the federal funds rate.  
B) has no effect on the federal funds rate.  
C) lowers the federal funds rate.  
D) raises the federal funds rate.

- 9) Because borrowers, once they have a loan, are more likely to invest in high-risk investment projects, banks face the \_\_\_\_\_  
 A) adverse selection problem. B) moral hazard problem.  
 C) lemon problem. D) adverse credit risk problem.
- 10) In order to reduce the \_\_\_\_\_ problem in loan markets, bankers collect information from prospective borrowers to screen out the bad credit risks from the good ones. \_\_\_\_\_  
 A) moral hazard B) adverse selection  
 C) moral suasion D) adverse lending
- 11) Because \_\_\_\_\_ are less liquid for the depositor than \_\_\_\_\_, they earn higher interest rates. \_\_\_\_\_  
 A) money market deposit accounts; time deposits  
 B) time deposits; passbook savings  
 C) passbook savings; time deposits  
 D) money market deposit accounts; passbook savings
- 12) If a bank has \$100,000 of checkable deposits, a required reserve ratio of 20 percent, and it holds \$40,000 in reserves, then the maximum deposit outflow it can sustain without altering its balance sheet is \_\_\_\_\_  
 A) \$20,000. B) \$25,000. C) \$10,000. D) \$30,000.
- 13) The excess reserves ratio is \_\_\_\_\_ related to expected deposit outflows, and is \_\_\_\_\_ related to the market interest rate. \_\_\_\_\_  
 A) positively; negatively B) positively; positively  
 C) negatively; negatively D) negatively; positively
- 14) If a bank has \_\_\_\_\_ rate-sensitive assets than liabilities, a \_\_\_\_\_ in interest rates will reduce bank profits, while a \_\_\_\_\_ in interest rates will raise bank profits. \_\_\_\_\_  
 A) fewer; decline; decline B) fewer; rise; rise  
 C) more; rise; decline D) more; decline; rise
- 15) Suppose, at a given federal funds rate, there is an excess demand for reserves in the federal funds market. If the Fed wants the federal funds rate to stay at that level, then it should undertake an open market \_\_\_\_\_ of bonds, everything else held constant. If the Fed does nothing, however, the federal funds rate will \_\_\_\_\_. \_\_\_\_\_  
 A) purchase; increase B) purchase; decrease  
 C) sale; decrease D) sale; increase
- 16) Suppose that from a new checkable deposit, First National Bank holds eight million dollars on deposit with the Federal Reserve, nine million dollars in excess reserves, and faces a required reserve ratio of ten percent. Given this information, we can say First National Bank has \_\_\_\_\_ million dollars in vault cash. \_\_\_\_\_  
 A) one B) two C) nine D) ten

- 17) Which of the following is an entity of the Federal Reserve System? 17) \_\_\_\_\_
- A) The FDIC
  - B) The Comptroller of the Currency
  - C) The FOMC
  - D) The U.S. Treasury Secretary
- 18) A \$5 million deposit outflow from a bank has the immediate effect of 18) \_\_\_\_\_
- A) reducing deposits and reserves by \$5 million.
  - B) reducing deposits and loans by \$5 million.
  - C) reducing deposits and securities by \$5 million.
  - D) reducing deposits and capital by \$5 million.
- 19) If a person selling bonds to the Fed cashes the Fed's check, then reserves \_\_\_\_\_ and currency in circulation \_\_\_\_\_, everything else held constant. 19) \_\_\_\_\_
- A) remain unchanged; increases
  - B) increase; remains unchanged
  - C) remain unchanged; declines
  - D) decline; remains unchanged
- 20) If, after a deposit outflow, a bank has a reserve deficiency of \$ 3 million, it can meet its reserve requirements by 20) \_\_\_\_\_
- A) selling \$3 million of securities.
  - B) repaying its discount loans from the Fed.
  - C) increasing loans by \$3 million.
  - D) reducing deposits by \$3 million.
- 21) Each governor on the Board of Governors can serve 21) \_\_\_\_\_
- A) only one nonrenewable fourteen-year term.
  - B) one full nonrenewable eight-year term plus part of another term.
  - C) only one nonrenewable eight-year term.
  - D) one full nonrenewable fourteen-year term plus part of another term.
- 22) When a \$10 check written on the First National Bank of Chicago is deposited in an account at Citibank, then 22) \_\_\_\_\_
- A) the reserves of the First National Bank increase by \$ 10.
  - B) the liabilities of Citibank increase by \$10.
  - C) the assets of Citibank fall by \$10.
  - D) the liabilities of the First National Bank increase by \$10.
- 23) If a banker expects interest rates to fall in the future, her best strategy for the present is 23) \_\_\_\_\_
- A) to increase the duration of the bank's assets.
  - B) to increase the duration of the bank's liabilities.
  - C) to sell long-term certificates of deposit.
  - D) to buy short-term bonds.
- 24) Having interest rate stability 24) \_\_\_\_\_
- A) guarantees full employment.
  - B) allows for less uncertainty about future planning.
  - C) leads to demands to curtail the Fed's power.
  - D) leads to problems in financial markets.

- 25) Which of the following bank assets is the most liquid? 25) \_\_\_\_\_  
 A) Consumer loans  
 B) Cash items in process of collection  
 C) Reserves  
 D) U.S. government securities
- 26) What makes the Federal Reserve so unique compared to other central banks around the world is its 26) \_\_\_\_\_  
 A) decentralized structure. B) regulatory functions.  
 C) centralized structure. D) monetary policy functions.
- 27) The relationship between borrowed reserves, the nonborrowed monetary base, and the monetary base is 27) \_\_\_\_\_  
 A)  $BR = MB - MB_n$ . B)  $MB = BR - MB_n$ .  
 C)  $MB = MB_n - BR$ . D)  $BR = MB_n - MB$ .
- 28) In the market for reserves, a \_\_\_\_\_ in the reserve requirement \_\_\_\_\_ the demand for reserves, lowering the federal funds interest rate, everything else held constant. 28) \_\_\_\_\_  
 A) rise; increases B) rise; decreases  
 C) decline; decreases D) decline; increases
- 29) Banks that actively manage liabilities will most likely meet a reserve shortfall by 29) \_\_\_\_\_  
 A) calling in loans. B) borrowing federal funds.  
 C) selling municipal bonds. D) seeking new deposits.
- 30) When the Federal Reserve purchases a government bond from a bank, reserves in the banking system \_\_\_\_\_ and the monetary base \_\_\_\_\_, everything else held constant. 30) \_\_\_\_\_  
 A) decrease; decreases B) increase; increases  
 C) decrease; increases D) increase; decreases
- 31) Because of an expected rise in interest rates in the future, a banker will likely 31) \_\_\_\_\_  
 A) buy long-term rather than short-term bonds.  
 B) buy short-term rather than long-term bonds.  
 C) make either short or long-term loans; expectations of future interest rates are irrelevant.  
 D) make long-term rather than short-term loans.
- 32) Banks earn profits by selling \_\_\_\_\_ with attractive combinations of liquidity, risk, and return, and using the proceeds to buy \_\_\_\_\_ with a different set of characteristics. 32) \_\_\_\_\_  
 A) loans; deposits B) assets; liabilities  
 C) liabilities; assets D) securities; deposits

- 33) All \_\_\_\_\_ are required to be members of the Fed. 33) \_\_\_\_\_  
 A) banks with assets less than \$100 million  
 B) nationally chartered banks  
 C) banks with assets less than \$500 million  
 D) state chartered banks
- 34) The Federal Reserve Bank of \_\_\_\_\_ plays a special role in the Federal Reserve System because it houses the open market desk. 34) \_\_\_\_\_  
 A) San Francisco B) New York  
 C) Boston D) Chicago
- 35) Suppose that from a new checkable deposit, First National Bank holds two million dollars in vault cash, eight million dollars on deposit with the Federal Reserve, and one million dollars in required reserves. Given this information, we can say First National Bank faces a required reserve ratio of \_\_\_\_\_ percent. 35) \_\_\_\_\_  
 A) ten B) twenty C) eighty D) ninety
- 36) \_\_\_\_\_ the Federal Reserve earn income while \_\_\_\_\_ the Federal Reserve cost nothing. 36) \_\_\_\_\_  
 A) Reserves of; assets of  
 B) Assets of; liabilities of  
 C) Liabilities of; assets of  
 D) Currency in circulation by; assets of
- 37) The fraction of checkable deposits that banks are required by regulation to hold are 37) \_\_\_\_\_  
 A) excess reserves. B) total reserves.  
 C) required reserves. D) vault cash.
- 38) During the bank panics of the Great Depression the currency ratio 38) \_\_\_\_\_  
 A) increased sharply. B) increased slightly.  
 C) decreased sharply. D) decreased slightly.
- 39) Everything else held constant, in the market for reserves, when the federal funds rate equals the discount rate, lowering the discount rate 39) \_\_\_\_\_  
 A) increases the federal funds rate.  
 B) has no effect on the federal funds rate.  
 C) lowers the federal funds rate.  
 D) has an indeterminate effect of the federal funds rate.
- 40) Bank loans from the Federal Reserve are called \_\_\_\_\_ and represent a \_\_\_\_\_ of funds. 40) \_\_\_\_\_  
 A) fed funds; source B) discount loans; use  
 C) fed funds; use D) discount loans; source
- 41) Large-denomination CDs are \_\_\_\_\_, so that like a bond they can be resold in a \_\_\_\_\_ market before they mature. 41) \_\_\_\_\_  
 A) nonnegotiable; primary B) nonnegotiable; secondary  
 C) negotiable; primary D) negotiable; secondary



- 49) Using Taylor's rule, when the equilibrium real federal funds rate is 2 percent, there is no output gap, the actual inflation rate is zero, and the target inflation rate is 2 percent, the nominal federal funds rate should be \_\_\_\_\_
- A) 0 percent.                      B) 1 percent.  
C) 2 percent.                      D) 3 percent.
- 50) The money supply is \_\_\_\_\_ related to the nonborrowed monetary base, and \_\_\_\_\_ related to the level of borrowed reserves.      50) \_\_\_\_\_
- A) negatively; negatively              B) positively; negatively  
C) positively; positively              D) negatively; not

1. B
2. B
3. A
4. B
5. D

6. B
7. D
8. B
9. B
10. B

11. B
12. B
13. A
14. D
15. A

16. B
17. C
18. A
19. A
20. A

21. D
22. B
23. A
24. B
25. C

26. A
27. A
28. C
29. B
30. B

31. B
32. C
33. B
34. B
35. A

36. B
37. C
38. A
39. C
40. D

41. D
42. C
43. A
44. A
45. D

46. A
47. A
48. A
49. B
50. C