

**VERSION A – ANSWER OUTLINE (Answers at End)**

**ECONOMICS 353**

**L. Tesfatsion/Spring 2011**

**FINAL EXAM–VERSION A: 70 Questions Total (1 Point Each)**

**2 May 2011**

Please write on side 1 of your answer bubble sheet your FIRST AND LAST NAME together with your STUDENT ID NUMBER, and write ECON 353: FINAL EXAM–VERSION A on the top margin of side 1.

Answer all 70 questions below by marking answers on your answer bubble sheet using a number 2 pencil **\*\*ONLY\*\***. Each question is worth 1 point. Read each question carefully before answering.

**USE OF ANY ELECTRONIC OR MECHANICAL DEVICE DURING THE EXAM IS STRICTLY PROHIBITED.**

At the end of the exam, please turn in your bubble sheet and be prepared to show an official photo ID of yourself (e.g., student ID, driver's license) if asked.

**CAUTION:** Do your own work, do not assist others in any way during the exam, and keep your eyes focused only on your own exam. Any behavior to the contrary will be considered cheating and will not be tolerated. Cheating will result in an automatic F on the exam, and further sanctions may be applied in line with university policy.

**\*\*OPPORTUNITY TO COMMENT ON QUESTIONS:\*\*** If you wish to comment on a question you believe is unclear or ambiguous, please do the following:

- (1) Write your specific comments on the following pages along side the statement(s) of the question(s) about which you have concerns.
- (2) Indicate here the numbers of the questions you have commented on:  
\_\_\_\_\_
- (3) Write your name and student ID number where indicated below.

STUDENT NAME \_\_\_\_\_

STUDENT ID NUMBER \_\_\_\_\_

- (4) At the end of the exam, give this exam question packet to the instructor for special handling.

**Q1.** By definition, the GROSS DOMESTIC PRODUCT (GDP) for an economy during some year T measures the total value of \_\_\_\_\_

- A. all final goods and services consumed within the economy during year T.
- B. all final goods and services produced by the economy's citizens during year T.
- C. all final goods and services produced within the economy's borders during year T.
- D. all production taking place within the economy's borders during period T.

**Q2.** By definition, the INFLATION RATE is \_\_\_\_\_

- A. the rate of change of the aggregate price level.
- B. a continual increase in the aggregate price level.
- C. an increase in the value of a country's currency.
- D. an increase in the value of a country's nominal GDP.
- E. none of the above.

**Q3.** The U.S. INFLATION RATE from 1952 through present times \_\_\_\_\_

- A. has steadily trended downward.
- B. has steadily trended upward.
- C. has typically been positive.
- D. has fluctuated around its "natural rate" level of 0 percent.

**Q4.** Since 1970 the U.S. DOLLAR \_\_\_\_\_

- A. has steadily declined in value against all major foreign currencies.
- B. has steadily increased in value against all major foreign currencies.
- C. has slowly replaced IMF "special drawing rights" (SDRs) as the reserve currency of choice throughout the world.
- D. has experienced substantial fluctuations in value in relation to major foreign currencies.

**Q5.** The US GOVERNMENT BUDGET since 1950 has largely been \_\_\_\_\_

- A. in deficit, meaning government expenditures have exceeded tax revenues.
- B. in deficit, meaning government expenditures have been less than tax revenues.
- C. in surplus, meaning government expenditures have exceeded tax revenues.
- D. in surplus, meaning government expenditures have been less than tax revenues.

**Q6.** By definition, examples of FINANCIAL assets include \_\_\_\_\_

- A. ATM machines.
- B. special financial knowledge acquired through working as a bank manager.
- C. 100 shares of General Motors stock.
- D. all of the above.
- E. only A and B above.

**Q7 (1 Point).** Which (if any) of the following statements describing dealers, brokers, and financial intermediaries are TRUE?

- A. Brokers acquire inventories of assets in preparation for any gaps that arise between asset demands and asset supplies, a process known as “brokerage commissioning.”
- B. Financial intermediaries sell lower-risk assets with short maturities to savers and then use these funds to buy higher-risk assets with longer maturities from borrowers, a process known as “asset transformation.”
- C. Dealers sell lower-risk assets with short maturities to buyers and then use these funds to buy higher-risk assets with longer maturities from sellers, a process known as “making the market.”
- D. none of the above.

**Q8.** By definition, instances of DIRECT FINANCE include: \_\_\_\_\_

- A. the signing of a loan contract with Wells Fargo Bank.
- B. the purchase of a share of Whirlpool Corporation on the New York Stock Exchange.
- C. a swap of U.S. dollars for yen on the Foreign Exchange Market.
- D. the purchase of newly issued LDK Solar Company stock shares in an initial public offering (IPO).
- E. none of the above.

**Q9.** By definition, a EURODOLLAR is \_\_\_\_\_

- A.** one euro in the form of paper currency rather than coinage.
- B.** a U.S. dollar deposited in foreign banks outside the U.S. or in foreign branches of U.S. banks.
- C.** a U.S. dollar that is being held by the European Central Bank (ECB) specifically as currency reserves for Europe-U.S. trade transactions.
- D.** any U.S. dollar that has been purchased by euros in the foreign currency market.
- E.** the number of U.S. dollars that can be obtained in exchange for one euro.

**Q10.** A CORPORATE BOND issued by John Deere and purchased by you is \_\_\_\_\_ for John Deere and \_\_\_\_\_ for you.

- A.** a liability; an asset
- B.** an asset; a liability
- C.** a real asset; a financial asset
- D.** a financial asset; a real asset

**Q11.** The organization responsible for the conduct of MONETARY POLICY in the United States is \_\_\_\_\_

- A.** the executive branch (the President and his administration).
- B.** the Federal Reserve System.
- C.** the Office of the Comptroller.
- D.** the U.S. Treasury.
- E.** the U.S. Congress.

**Q12.** CHECKABLE DEPOSIT ACCOUNTS supplied by reputable U.S. commercial banks such as the First National Bank in Ames \_\_\_\_\_

- A.** are legal tender in the U.S.
- B.** are a generally accepted means of payment for goods and services and for repayment of debts in the U.S., by social custom.
- C.** constitute part of M1, a commonly used measure of money in the U.S.
- D.** All of the above.
- E.** Only B and C.

**Q13.** When compared to exchange systems that rely on money, DISADVANTAGES of a barter payment system include: \_\_\_\_\_

- A. lower transactions costs.
- B. the discouragement of labor specialization.
- C. the encouragement of labor specialization.
- D. the requirement that there be no double-coincidence-of-wants in order for the system to work.
- E. both C and D.

**Q14.** U.S. MONETARY POLICY makers routinely induce changes in the money supply held by the private sector in an attempt to exert control over \_\_\_\_\_

- A. the government budget deficit.
- B. prices through “printing press” operations.
- C. short-term interest rates.
- D. the balance of payments.

**Q15.** Which of the following statements are TRUE:

- A. Initial estimates of the aggregate money measures M1 and M2 are rarely revised, so they are reliable guides to short-run movements in the money supply.
- B. M1 and M2 always move closely together, so it does not matter which measure is used.
- C. M1 is the narrowest aggregate money measure used in the U.S. in the sense that it consists of financial instruments that are most liquid and hence most “money like.”
- D. All of the above.
- E. Only B and C above.

**Q16.** By definition, which of the following statements are TRUE for COUPON BONDS?

- A. The borrower is required to make only one contract-specified “coupon payment,” to be paid at the bond’s maturity date.
- B. Mortgages are examples of coupon bonds.
- C. The borrower makes a contract-specified “coupon payment” in every payment period until the bond’s maturity date, at which time the borrower also pays the face value of the bond.
- D. Only A and B above.
- E. Only B and C above.

- Q17.** The CURRENT YIELD on a coupon bond with a \$100 face value, a coupon rate equal to .20 (20 percent), and a current purchase price of \$200 is \_\_\_\_
- A. 20 percent
  - B. 10 percent
  - C. 8 percent
  - D. 5 percent
  - E. None of the above
- Q18.** Letting “ \* ” denote multiplication, if the annual interest rate is 4 percent, then the PRESENT VALUE TODAY of a payment stream (\$50, \$80) with \$50 to be received at the end of the first year and \$80 to be received at the end of the second year is given by \_\_\_\_
- A.  $\$50 * (1 + 0.04) + \$80 * (1 + 0.04)^2$
  - B.  $\$50 / (1 + 0.04) + \$80 / (1 + 0.04)$
  - C.  $\$50 / (1 + 0.04) + \$80 / (1 + 0.04)^2$
  - D.  $\$50 + [\$80 / (1 + 0.04)^2]$
- Q19.** The (ANNUAL) YIELD TO MATURITY  $i$  on a COUPON BOND with a purchase price \$600, a face value \$200, a 3-year coupon payment stream (\$60, \$20, \$100), and a 3-year maturity is calculated as follows: \_\_\_\_
- A.  $i$  equals the annual interest rate that, when used to calculate the present value of the income stream (\$60, \$20, \$100), results in a present value equal to \$600.
  - B.  $i$  equals the annual interest rate that, when used to calculate the present value of the income stream (\$60, \$20, \$100), results in a present value equal to \$200.
  - C.  $i$  equals the annual interest rate that, when used to calculate the present value of the income stream (\$60, \$20, \$300), results in a present value equal to \$600.
  - D.  $i$  equals the annual interest rate that, when used to calculate the present value of the income stream (\$60, \$20, \$300), results in a present value equal to \$200.
- Q20.** Letting  $i$  denote the current nominal market interest rate (yield to maturity), in which of the following situations should a rational investor prefer to be a LENDER: \_\_\_\_
- A.  $i = 4$  percent and the expected inflation rate = 3 percent
  - B.  $i = 13$  percent and the expected inflation rate = 11 percent
  - C.  $i = 25$  percent and the expected inflation rate = 20 percent
  - D.  $i = 5$  percent and the expected inflation rate = -1 percent

- Q21.** INTEREST RATE RISK is the risk faced by \_\_\_\_ in the form of \_\_\_\_.
- A. a potential lender; fluctuations in the purchase price of bonds.
  - B. a bond owner; fluctuations in the yield to maturity, hence in the period-by-period return rate on the bond.
  - C. a person who has re-sold a bond in a secondary market; fluctuations in the interest payments the seller will have to make to the buyer.
  - D. a potential borrower; fluctuations in the interest payments the borrower will have to make to the lender.
  - E. a borrower who has already issued a bond; fluctuations in the interest payments the borrower will have to make to the bond holder.
- Q22.** Treasury Inflation Protection Securities (TIPS) generate useful information for monetary policy makers because \_\_\_\_
- A. the interest rate on TIPS always closely tracks the Federal Funds Rate.
  - B. the interest and principal payments on TIPS are adjusted for changes in the price level, hence the interest rate on TIPS provides a measure of the real interest rate.
  - C. the difference between the current market interest rate and the TIPS interest rate provides a measure of expected inflation.
  - D. all of the above.
  - E. only B and C above.
- Q23.** In the treatment of bond markets in Mishkin Chapter 5, several important assumptions are maintained about supply curves. These assumptions include: \_\_\_\_
- A. the Yield-to-Maturity  $i$  moves directly with the bond price  $P$  along each supply curve, in the sense that  $P$  increases if and only if  $i$  increases (and vice versa).
  - B. all economic variables APART from the bond quantity supplied and the bond price  $P$  (hence the Yield-to-Maturity  $i$ ) are assumed to take on constant values along each supply curve.
  - C. supply curves slope up.
  - D. only B and C above
- Q24.** As discussed in Mishkin (Chapter 5), a supply curve plotted with price  $P$  on the vertical axis and quantity  $B$  on the horizontal axis is said to SHIFT TO THE RIGHT if \_\_\_\_
- A. for every given price  $P$ , the amount  $B$  of quantity supplied increases.
  - B. the price  $P$  and the amount  $B$  of quantity supplied both decrease.
  - C. for every given price  $P$ , the amount  $B$  of quantity supplied decreases.
  - D. the price  $P$  and the amount  $B$  of quantity supplied both increase.
  - E. the price  $P$  decreases and the amount  $B$  of quantity supplied increases.

- Q25.** According to Mishkin (Chapter 5), a decrease in the bond price  $P$  will result in \_\_\_\_\_ the bond DEMAND curve, and an increase in the expected inflation rate will result in \_\_\_\_\_ the bond DEMAND curve.
- A. a downward movement along; a rightward shift of
  - B. a leftward shift of; a downward movement along
  - C. a rightward shift of; a downward movement along
  - D. a downward movement along; a leftward shift of
- Q26.** According to Mishkin (Chapter 5), key factors that are likely to cause the SUPPLY curve for bonds to SHIFT TO THE LEFT include \_\_\_\_\_
- A. a higher government budget deficit.
  - B. a decrease in the expected profitability of capital investment.
  - C. a decrease in the expected inflation rate.
  - D. all of the above.
  - E. only B and C above.
- Q27.** Suppose the market for U.S. Treasury bonds is currently in equilibrium. However, new data showing an increased weakness of the dollar against the euro convinces people to revise UPWARD their expectations TODAY regarding the inflation rate in the U.S. OVER THE NEXT COMING YEAR. Then the theory in Mishkin Chapter 5 predicts that (all else equal) the effect on the U.S. Treasury bond market TODAY will be \_\_\_\_\_ in the equilibrium price of U.S. Treasury bonds and \_\_\_\_\_ in the equilibrium quantity of U.S. Treasury bonds sold.
- A. either an increase or decrease; a definite increase
  - B. a definite decrease; either an increase or decrease
  - C. a definite increase; either an increase or decrease
  - D. a definite decrease; a definite decrease
- Q28.** The ONE-PERIOD VALUATION MODEL FOR COMMON STOCKS presented in Mishkin, Chapter 7, implies that the current share price of a stock  $S$  equals \_\_\_\_\_
- A. the average expected dividend payment per period.
  - B. the average expected dividend payment plus capital gains (or losses) per period.
  - C. the sum of next period's expected dividend payment and next period's expected share price, divided by  $[1 + i]$  (where  $i$  is the yield to maturity).
  - D. the sum of next period's expected dividend payment and next period's expected share price, divided by  $[1 + k_e]$  (where  $k_e$  is the required return on equity investment).



- Q29.** The GENERALIZED DIVIDEND VALUATION MODEL presented in Mishkin Chapter 7 implies that the share price  $P_n$  of a stock S in a distant time period  $n$  will NOT have any significant effect on the current share price for S \_\_\_\_
- A. under any circumstances.
  - B. if investors have rational expectations.
  - C. if the price  $P_n$  increases more slowly than  $[1 + k_e]^n$  as  $n$  increases, where  $k_e$  is the required return on equity investment.
  - D. if the stock S pays a positive dividend in each period.
- Q30.** By definition, a BUBBLE is said to exist on a stock S if \_\_\_\_
- A. the stock S is expected to pay a positive dividend to its shareholders in each future time period.
  - B. the share price of the stock S exceeds the present value of its future expected dividend stream, where the discount rate used to calculate the present value is the required return on equity investment.
  - C. the share price of stock S exhibits a dramatic rise in value followed by an abrupt fall.
  - D. all of the above.
  - E. only A and B above.
- Q31.** As explained in Mishkin Chapter 7, the GORDON GROWTH MODEL is derived from the generalized dividend valuation model under the special assumption that \_\_\_\_
- A. expected dividend payments are constant over time.
  - B. the required return on equity investment  $k_e$  increases at a constant rate.
  - C. expected dividend payments grow at a constant rate.
  - D. expected dividend payments are zero over time.
  - E. none of the above.
- Q32.** The view that expectations are formed from past experience as some kind of weighted average of past observations, known as \_\_\_\_\_, implies that \_\_\_\_\_.
- A. optimal statistical forecasting; information is used optimally.
  - B. adaptive expectations; expectations tend to change slowly over time.
  - C. rational expectations; all relevant information is taken into account.
  - D. perfect foresight expectations; forecast errors have small standard deviations.
  - E. extrapolative expectations; forecast errors are sequentially independent.

- Q33.** The key assumption characterizing RATIONAL EXPECTATIONS is that \_\_\_\_
- A. people do not make use of past observations because these observations are out-of-date.
  - B. people make optimal use of their information when forming their expectations.
  - C. people do not make sudden changes in their expectations.
  - D. people are able to forecast future events without error.
  - E. only B and D above.
- Q34.** An important implication of the strongest version of the EFFICIENT MARKET HYPOTHESIS presented in Mishkin Chapter 7 is that stock market investors \_\_\_\_
- A. should pay close attention to “hot tips” in published reports by investment advisors.
  - B. should pay close attention to trends and patterns in past stock price data.
  - C. should not expect to be able to earn returns in the stock market that are persistently higher than the average return for the stock market as a whole.
  - D. should not follow a “buy and hold” strategy since such an overly cautious approach will leave unexploited profit opportunities.
  - E. should never buy into a mutual fund, because such funds cannot consistently outperform the market.
- Q35.** As discussed in Mishkin Chapter 7, the Efficient Market Hypothesis (EMH) remains controversial because of the persistence of stock market ANOMALIES that appear to contradict the predictions of the EMH. Examples of these anomalies include: \_\_\_\_
- A. Stock prices tend to fluctuate more than their associated dividend payment streams.
  - B. Stock prices sometimes fall after the announcement of good news.
  - C. Stock prices do not always immediately adjust to new (unanticipated) profit announcements.
  - D. All of the above.
  - E. Only A and C above.
- Q36.** In a world divided between HC and ROW, multiplying any valuation  $V$  measured in HC currency units by the HC NOMINAL EXCHANGE RATE  $E$  \_\_\_\_.
- A. corrects  $V$  for changes in the HC price level
  - B. corrects  $V$  for changes in the HC inflation rate
  - C. transforms  $V$  into a valuation measured in ROW currency units
  - D. transforms  $V$  into pure quantity terms

- Q37.** In a world divided between HC and ROW, the conditions needed in order for the PURCHASING POWER PARITY (PPP) CONDITION to reduce to a straightforward application of the Law of One Price include the following: \_\_\_\_\_
- A. the HC and ROW inflation rates must equal each other over time.
  - B. the HC and ROW aggregate price levels must equal each other over time.
  - C. HC and ROW must produce the same bundle of goods and services.
  - D. all of the above.
- Q38.** Suppose the inflation rate in Sweden is 5 percent during 2011 and the inflation rate in South Korea is 3 percent during 2011. Then the PURCHASING POWER PARITY CONDITION predicts that, during 2011, the value of the Swedish currency (kronas) measured in terms of the South Korean currency (wons) – i.e., the number of won per krona – will \_\_\_\_\_
- A. fall by 2 percent
  - B. rise by 2 percent
  - C. rise by 8 percent
  - D. fall by 8 percent
- Q39.** Suppose the average nominal interest rate on bank deposit accounts across foreign countries who are major trading partners of the U.S. is 5 percent, and the U.S. effective exchange rate index for these countries (i.e., a weighted average of their exchange rates measured in foreign currency units per U.S. dollar) is expected to depreciate by 2 percent. Then INTEREST PARITY predicts that, on average, nominal interest rates on U.S. bank deposit accounts should be about \_\_\_\_\_
- A. 3 percent.
  - B. 7 percent.
  - C. -3 percent
  - D. 3.5 percent
- Q40.** Potential BENEFITS to European Union member countries from joining the eurozone include: \_\_\_\_\_
- A. an increased ability to pursue independent monetary policies.
  - B. the possibility that the euro will some day match or exceed the U.S. dollar as a reserve currency held around the world.
  - C. a more flexible system of exchange rates between their national currencies.
  - D. avoidance of the 3% deficit-to-GDP ratio imposed on EU member countries that do not participate in the eurozone.
  - E. none of the above.

**Q41.** In a two-country world (HC and ROW), by definition ROW saving in relation to the HC is \_\_\_\_\_

- A. ROW imports minus ROW exports.
- B. ROW GDP minus ROW consumption.
- C. Total income received by ROW from the HC, minus HC exports to ROW.
- D. Total income received by the HC from ROW, minus HC imports from ROW.

**Q42.** Which item(s) below would appear as items in the 2011 U.S. CURRENT ACCOUNT: \_\_\_\_\_

- A. Interest payments received in 2011 by U.S. holders of Belgium bonds.
- B. Purchases by Japan in 2011 of soybeans harvested in 2011 by Iowan farmers.
- C. The purchase by citizens of Iceland in 2011 of 200 newly issued stock shares in the Great Tan Now Corporation based in Los Angeles, California.
- D. All of the above.
- E. Only A and B above.

**Q43.** If the U.S. is running a CURRENT ACCOUNT DEFICIT, then U.S. national saving is \_\_\_\_\_ U.S. total investment, and the U.S. is \_\_\_\_\_ the rest-of-the-world.

- A. greater than; a net lender to
- B. greater than; a net borrower from
- C. less than; a net lender to
- D. less than; a net borrower from

**Q44.** According to post-1999 U.S. balance of payments accounting, which items below would appear in the U.S. CAPITAL AND FINANCIAL ACCOUNT KFA for 2011:

- A. a purchase in 2011 by U.S. citizen Bill Gates of the New York Empire State Building constructed in 1931.
- B. interest income received in 2011 by U.S. holders of a Russian bond issue.
- C. a Nigerian citizen's purchase in 2011 of a newly issued U.S. Treasury bond.
- D. a purchase in 2011 by U.S. citizen Donald Trump of a casino in Las Vegas, Nevada, constructed in 2011.
- E. all of the above.

- Q45.** Suppose the world is divided between HC and ROW, and all international reserves take the form of currency reserves held by the HC central bank. If the HC is in a BALANCE OF PAYMENTS EQUILIBRIUM, this means \_\_\_\_\_
- A. the HC current account is zero.
  - B. the HC central bank is actively intervening in the foreign exchange market to ensure demand equals supply.
  - C. the net change in HC official reserve assets is equal to zero.
  - D. the sum of the HC current account plus the HC capital and financial account equals the net change in HC official reserve assets.
  - E. in net terms the HC is neither borrowing from nor lending to ROW.
- Q46** According to Mishkin Chapter 8, during 1970-2000 \_\_\_\_\_ was a more important source of EXTERNAL FUNDS for U.S. corporations than \_\_\_\_\_.
- A. revenues from stock and bond issues; loans from financial intermediaries
  - B. loans from foreign financial intermediaries; loans from domestic financial intermediaries
  - C. loans from financial intermediaries; revenues from stock and bond issues
  - D. loans from government agencies; loans from financial intermediaries
- Q47.** Some of the key reasons why banks and other financial intermediaries are able to reduce or eliminate information problems and transaction costs include: \_\_\_\_\_
- A. banks can spread their loan costs over large pools of depositors (lenders).
  - B. bank loans are typically made in private, which gives bankers a greater incentive to engage in information gathering.
  - C. banks can include collateral requirements in loan contracts, which can act as a signal regarding the type of borrower (high or low risk).
  - D. all of the above.
- Q48.** Corporate BONDHOLDERS are generally LESS likely to be concerned about moral hazard problems than corporate SHAREHOLDERS because \_\_\_\_\_
- A. corporate bondholders have priority over stockholders in case of bankruptcy.
  - B. corporate bonds include restrictive covenants that condition payments on corporate profit performance.
  - C. corporate bond payments are not conditioned on corporate profit performance (except in extreme circumstances such as bankruptcy).
  - D. only A and B above.
  - E. only A and C above.

- Q49.** ADVERSE SELECTION PROBLEMS are said to occur in financial markets when \_\_\_\_
- A. ownership of assets is separated from the control of these assets.
  - B. people who do not pay for information take advantage of the information that other people have paid for by observing their behavior.
  - C. high-risk borrowers are successfully able to pass themselves off as low-risk borrowers when applying for loans.
  - D. the cost per dollar loaned declines as the size of the loan increases.
- Q50.** The SARBANES-OXLEY ACT OF 2002, introduced in the wake of \_\_\_\_, increased \_\_\_\_.
- A. the dot.com bubble burst; Congressional authority to oversee initial public offerings (IPOs).
  - B. the Enron crisis; regulatory oversight of firm accounting and audit practices.
  - C. the U.S. savings and loan crisis; regulatory oversight of firms to reduce principle-agent problems.
  - D. the U.S. twin deficit problem; reporting requirements on the U.S. Federal Government.
- Q51.** The ECONOMIC GROWTH of a country refers to \_\_\_\_.
- A. changes in its balance of payments.
  - B. changes in the infrastructure, organization, and governance of its economy.
  - C. changes in its money supply.
  - D. changes in the size of its economy, often measured by changes in GDP.
- Q52.** According to Mishkin (Chapter 9), most U.S. FINANCIAL CRISES have been preceded by one or more “trigger events”. These trigger events include: \_\_\_\_
- A. an increase in interest rates.
  - B. a decline in asset prices.
  - C. a deterioration in the balance sheets of financial institutions.
  - D. an increase in uncertainty resulting, for example, from the failure of a prominent firm.
  - E. all of the above

- Q53.** According to Mishkin (Chapter 9), a key way in which U.S. financial crises have DIFFERED from financial crises in emerging economies such as Mexico is that \_\_\_\_
- A. U.S. regulators have not permitted insolvent financial institutions to stay in operation.
  - B. foreign exchange crises (e.g., speculative currency attacks) have not played a dominant role in U.S. financial crises.
  - C. U.S. financial crises tend to be of far shorter duration.
  - D. U.S. financial crises have not resulted in substantial bank failures.
- Q54.** Which of the following events (all else equal) results in an INCREASE in the REAL net worth of a U.S. corporation that has outstanding loans denominated in U.S. dollars: \_\_\_\_
- A. a large purchase by investors of the corporation's outstanding stock shares on the New York Stock exchange at a market price higher than the price at which the shares were originally sold at first issue.
  - B. an increase in the U.S. aggregate price level.
  - C. a decline in the U.S. exchange rate relative to its major trading partners.
  - D. all of the above.
  - E. only A and B above.
- Q55.** According to Mishkin (Chapter 9), one of the key factors that worsened and prolonged the U.S. Great Depression was \_\_\_\_, which resulted in \_\_\_\_.
- A. a severe deflation; increased debt burdens.
  - B. a sharp contraction in the real money supply; a sharp rise in interest rates.
  - C. a sharp drop in real government spending; a sharp drop in real GDP.
  - D. a sharp increase in inflation; a sharp decrease in the real money supply.
- Q56.** According to the ppt notes on Mishkin (11/12:Part A), key factors that led to the U.S. financial crisis in the early 1980s included: \_\_\_\_
- A. increased competition for deposits from financial innovations (e.g., money market mutual funds) led banks to offer higher interest rates on their deposits.
  - B. higher deposit interest costs forced banks to seek out non-traditional lending and investment activities offering higher return rates (but also higher risks).
  - C. increased provision of government-backed deposit insurance in 1980 encouraged banks to diversify into higher return (but riskier) activities such as real estate loans and junk bonds (moral hazard problems).
  - D. All of the above.
  - E. only A and B above.

- Q57.** According to the ppt/html notes on Mishkin (11/12:Part A), a key reason why the U.S. has a large number of commercial banks in comparison with other industrialized countries is \_\_\_\_\_
- A. consumer protection laws.
  - B. vigorous competition within the U.S. commercial banking industry.
  - C. past U.S. regulations that restricted bank branching across state lines.
  - D. strong U.S. consumer preference for small community banks.
- Q58.** According to the html notes on Mishkin (11/12:Part A), the following financial innovations were an attempt to get around the branching restrictions imposed by the 1863 National Banking Act and the 1927 McFadden Act: \_\_\_\_\_
- A. junk bonds and money market mutual funds.
  - B. bank holding companies and automated teller machines.
  - C. adjustable-rate mortgages and NOW accounts.
  - D. virtual banks and electronic money.
- Q59.** According to the ppt/html notes on Mishkin (11/12:Part A), an important provision of the 1933 Glass-Steagall Act is that it \_\_\_\_\_
- A. prohibited commercial banks from underwriting or dealing in corporate securities.
  - B. permitted commercial banks to pay interest on checkable deposit accounts.
  - C. prohibited commercial banks from purchasing any debt securities.
  - D. prohibited commercial banks from engaging in risky loans.
- Q60.** According to the ppt/html notes on Mishkin (11/12:Part A), the 1933 Glass-Steagall Act was significantly weakened by the \_\_\_\_\_.
- A. 1994 by the Riegle-Neal Interstate Banking and Branching Efficiency Act.
  - B. 1999 Gramm-Leach-Bliley Act.
  - C. 2002 Sarbanes-Oxley Act.
  - D. 2010 by the Dodd-Frank Act.



- Q61.** According to Charles Jones (Global Financial Crisis, 2009), a key innovation in finance known as \_\_\_\_\_ enabled the hidden build-up of \_\_\_\_\_ during the years leading up to the subprime financial crisis.
- A. junk bonds; credit (default) risk
  - B. bank holding companies; large too-big-to-fail banking institutions
  - C. securitization; aggregate (“systemic”) risk
  - D. money market mutual funds; large pools of funds for speculative investments
- Q62.** A key aspect of the 2010 Dodd-Frank Act, legislated in direct response to the subprime financial crisis, is that it \_\_\_\_\_.
- A. bans the sale of collateralized debt obligations.
  - B. establishes a new agency to monitor and prevent the build-up of aggregate (“systemic”) risk in the financial sector.
  - C. bans the advertisement and issuing of subprime mortgages.
  - D. fully reinstates the 1933 Glass-Steagall provision prohibiting commercial banks from engaging in securities activities.
- Q63.** When Dr. Yunus first organized the Grameen Bank (GB) Project in 1976, commentators thought he would surely fail because of the unusual and seemingly incompatible nature of the three lending principles he strove to enforce. These three principles included: \_\_\_\_\_.
- A. Loans were to be repaid, and on time.
  - B. Only the poorest people were eligible for loans.
  - C. Loans were to be directed primarily towards women.
  - D. All of the above.
  - E. Only B and C above.
- Q64.** Recent criticisms of microcredit and the Grameen Bank include: \_\_\_\_\_.
- A. charges that Dr. Yunus is making inappropriate use of Grameen Bank profits to fund his political campaign to be prime minister of India.
  - B. charges that the tremendous surge in microcredit lending has led to lax oversight of borrowers, hence moral hazard problems (e.g., use of funds for consumption rather than business investment).
  - C. charges that strong-arm tactics employed by aggressive microlending firms have led to inappropriate lending to subprime borrowers who cannot repay, causing tremendous family stresses (e.g., increased suicide rates).
  - D. All of the above.
  - E. Only B and C above.

- Q65.** In the 1990s, Enron created many special-purpose entities (SPEs) specifically to \_\_\_\_.
- A.** hide Enron's risky investments and, later, the losses incurred by these investments.
  - B.** hide Enron's profits from lucrative investments, thus avoiding tax obligations.
  - C.** hide Enron's use of illegal electronic trading strategies, such as "death star."
  - D.** bulk up the asset side of Enron's balance sheets when these SPEs were consolidated into Enron's financial statements.
- Q66.** The International Monetary Fund (IMF) was originally organized \_\_\_\_.
- A.** in 1965 as a development agency whose construction loans were to be primarily funded through donations received from the more developed countries of the world.
  - B.** in 1971 as an international regulatory agency whose primary mission was support of fixed exchange rates and the gold standard.
  - C.** in 1933 as a regulatory agency tasked with restoring order to the international monetary system by imposition of appropriate rules and regulations.
  - D.** in 1945 as a financially self-sufficient lending agency whose annual expenses were to be primarily met by the difference between its interest receipts on its loans and its interest payments on the "quota" deposits received from its member countries.
- Q67.** Since 2007 the IMF has experienced a sharp resurgence in prestige and importance (and a decline in criticism), primarily due to the fact that \_\_\_\_.
- A.** the IMF has ceded more control of its lending operations to emerging market IMF member countries, a key demand of its critics.
  - B.** the resources of the IMF have been needed to help bail out several IMF member countries in serious financial trouble, including "developed" countries such as Greece and Ireland.
  - C.** the IMF has forgiven the loans of many of the poorer IMF member countries, a key demand of its critics.
  - D.** the IMF is now beginning to provide low-interest development loans financed by donations from developing countries, a key demand of its critics.

- Q68.** Commentators have long wondered if the European Union can survive in its current organizational form: namely, as a collection of sovereign countries \_\_\_\_.
- A. all operating under a single currency (the euro).
  - B. attempting to form a political union while retaining their economic autonomy.
  - C. attempting to form an integrated economy without first forming a political union.
  - D. attempting to form a unified culture that blends both “European” and “non-European” cultural attributes.
- Q69.** The global financial crisis beginning in 2007 is sorely testing the organizational structure of the eurozone, in particular, the strict fiscal stability rules imposed as a precondition of admittance to the eurozone. These fiscal stability rules include the following: \_\_\_\_.
- A. the government debt of a country must not be in excess of 3% of the country’s GDP.
  - B. the gross debt to GDP ratio of a country must not exceed 60%.
  - C. the government of a country must keep the country’s tax rates at or below the average levels currently prevailing among eurozone member countries.
  - D. all of the above.
  - E. only A and B above.
- Q70.** According to required readings for Ex 7 (Mishkin Chapter 7), Facebook (like Google) might ultimately end up offering its shares publicly through an Initial Public Offering (IPO). The reason given for this assertion is that Goldman Sachs’ planned “special purpose vehicle” for permitting its super-wealthy clients to acquire privately-held Facebook shares is possibly in violation of the Security and Exchange Commission’s 1964 500-PERSON RULE requiring that \_\_\_\_.
- A. any corporation that distributes stock shares has to have at least 500 shareholders.
  - B. any entity specializing in the provision of a “public good” (such as social network services) that has 500 or more persons as shareholders must be registered as a non-profit corporation.
  - C. any entity with total assets exceeding \$10 million and securities held of record by 500 or more persons has to register these securities with the SEC and file regular reports with the SEC (and the public) on its financial condition.
  - D. all corporations specializing in “public goods” (such as social networking services) that have 500 or more equity investors must be publicly held.

## Answers to Multiple Choice Questions

Q1-C,  
Q2-A,  
Q3-C,  
Q4-D,  
Q5-A,  
Q6-C,  
Q7-B,  
Q8-D,  
Q9-B,  
Q10-A,

Q11-B,  
Q12-E,  
Q13-B,  
Q14-C,  
Q15-C,  
Q16-C,  
Q17-B,  
Q18-C,  
Q19-C,  
Q20-D,

Q21-B,  
Q22-E,  
Q23-D,  
Q24-A,  
Q25-D,  
Q26-E,  
Q27-B,  
Q28-D,  
Q29-C,  
Q30-B,

Q31-C,  
Q32-B,  
Q33-B,  
Q34-C,  
Q35-E,

Q36-C,  
Q37-C,  
Q38-A,  
Q39-B,  
Q40-B,

Q41-C,  
Q42-E,  
Q43-D,  
Q44-C,  
Q45-C,  
Q46-C,  
Q47-D,  
Q48-E,  
Q49-C,  
Q50-B,

Q51-D,  
Q52-E,  
Q53-B,  
Q54-B,  
Q55-A,  
Q56-D,  
Q57-C,  
Q58-B,  
Q59-A,  
Q60-B,

Q61-C,  
Q62-B,  
Q63-D,  
Q64-E,  
Q65-A,  
Q66-D,  
Q67-B,  
Q68-C,  
Q69-B,  
Q70-C