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

1) A corporation acquires new funds only when its securities are sold in the
A) primary market by an investment bank.
B) secondary market by a stock exchange broker.
C) secondary market by an investment bank.
D) secondary market by a commercial bank.

2) Currency includes
A) paper money, coins, and checks.
B) paper money and checks.
C) paper money and coins.
D) paper money, coins, checks, and savings deposits.

3) When money prices are used to facilitate comparisons of value, money is said to function as a
A) store of value. B) unit of account.
C) medium of exchange. D) payments-system ruler.

4) Which of the following can be described as direct finance?
A) You borrow $2500 from a friend.
B) You buy shares in a mutual fund.
C) You take out a mortgage from your local bank.
D) You buy shares of common stock in the secondary market.

5) The currency component includes paper money and coins held in ________.
A) bank vaults B) the central bank
C) the hands of the nonbank public D) ATMs

6) The agency that was created to protect depositors after the banking failures of 1930–1933 is the
A) Office of the Comptroller of the Currency.
B) Treasury Department.
C) Federal Deposit Insurance Corporation.
D) Federal Reserve System.

7) Which of the following statements uses the economists’ definition of money?
A) The job with New Company gave me the opportunity to earn more money.
B) I hope that I have enough money to buy my lunch today.
C) Betsy is rich—she has a lot of money.
D) I plan to earn a lot of money over the summer.

8) You can borrow $5000 to finance a new business venture. This new venture will generate annual earnings of $251. The maximum interest rate that you would pay on the borrowed funds and still increase your income is
A) 25%. B) 12.5%. C) 10%. D) 5%. 
9) The upward and downward movement of aggregate output produced in the economy is referred to as the _______.
   A) business cycle    B) see saw   C) roller coaster    D) shock wave

10) The evolution of the payments system from barter to precious metals, then to fiat money, then to checks can best be understood as a consequence of
   A) government regulations designed to promote the safety of the payments system.
   B) innovations that reduced the costs of exchanging goods and services.
   C) competition among firms to make it easier for customers to purchase their products.
   D) government regulations designed to improve the efficiency of the payments system.

11) An important function of secondary markets is to
   A) make it easier to sell financial instruments to raise funds.
   B) create a market for newly constructed houses.
   C) make it easier for governments to raise taxes.
   D) raise funds for corporations through the sale of securities.

12) Bonds that are sold in a foreign country and are denominated in a currency other than that of the country in which it is sold are known as

13) Economists group commercial banks, savings and loan associations, credit unions, mutual funds, mutual savings banks, insurance companies, pension funds, and finance companies together under the heading financial intermediaries. Financial intermediaries
   A) can hurt the performance of the economy.
   B) produce nothing of value and are therefore a drain on society’s resources.
   C) provide a channel for linking those who want to save with those who want to invest.
   D) hold very little of the average American’s wealth.

14) In the United States, loans from _______ are far _______ important for corporate finance than are securities markets.
   A) financial intermediaries; less    B) government agencies; less
   C) financial intermediaries; more    D) government agencies; more

15) Financial markets promote economic efficiency by
   A) creating inflation.
   B) channeling funds from investors to savers.
   C) reducing investment.
   D) channeling funds from savers to investors.

16) The higher a security’s price in the secondary market the _______ funds a firm can raise by selling securities in the _______ market.
   A) more; secondary    B) less; secondary
   C) more; primary    D) less; primary

17) A professional baseball player may be contractually restricted from skiing. The team owner includes this clause in the player’s contract to protect against
   A) moral hazard.    B) risk sharing.
   C) adverse selection.    D) regulatory circumvention.
18) If peanuts serve as a medium of exchange, a unit of account, and a store of value, then peanuts are
A) bank deposits. B) loanable funds. C) money. D) reserves.

19) A sharp increase in the growth of the money supply is likely followed by
A) an increase in the inflation rate. B) a recession. C) no change in the economy. D) a depression.

20) Which of the following can be described as involving indirect finance?
A) You make a loan to your neighbor. B) You make a deposit at a bank. C) You buy a U.S. Treasury bill from the U.S. Treasury. D) A corporation buys a share of common stock issued by another corporation in the primary market.

21) Budgets deficits can be a concern because they might
A) lead to higher bond prices. B) lead to a slower rate of money growth. C) ultimately lead to higher inflation. D) lead to lower interest rates.

22) Poorly performing financial markets can be the cause of

23) Which of the following statements about the characteristics of debt and equities is true?
A) Bonds pay dividends. B) They can both be long-term financial instruments. C) Bond holders are residual claimants. D) The income from bonds is typically more variable than that from equities.

24) Which of the following statements best explains how the use of money in an economy increases economic efficiency?
A) Money cannot have an effect on economic efficiency. B) Money increases economic efficiency because it decreases transactions costs. C) Money increases economic efficiency because it is costless to produce. D) Money increases economic efficiency because it discourages specialization.

25) The process where financial intermediaries create and sell low-risk assets and use the proceeds to purchase riskier assets is known as

26) Well-functioning financial markets
A) produce an efficient allocation of capital. B) eliminate the need for indirect finance. C) cause financial crises. D) cause inflation.
27) When I purchase __________, I own a portion of a firm and have the right to vote on issues important to the firm and to elect its directors.
   A) bills   B) notes   C) bonds   D) stock

28) All but the most primitive societies use money as a medium of exchange, implying that
   A) barter exchange is economically efficient.
   B) the use of money is economically efficient.
   C) barter exchange cannot work outside the family.
   D) inflation is not a concern.

29) Which of the following is a true statement?
   A) The aggregate price level is measured as the rate of change in the inflation rate.
   B) The average price of goods and services in an economy is called the aggregate price level.
   C) The inflation rate is measured as the rate of change in the federal government budget deficit.
   D) Money or the money supply is defined as Federal Reserve notes.

30) Securities are ________ for the person who buys them, but are ________ for the individual or firm that issues them.
    A) liabilities; assets   B) assets; liabilities
    C) negotiable; nonnegotiable   D) nonnegotiable; negotiable

31) U.S. Treasury bills are considered the safest of all money market instruments because there is no risk of ________.
    A) default   B) defeat   C) demarkation   D) desertion

32) The bond markets are important because they are
    A) the markets where interest rates are determined.
    B) the markets where foreign exchange rates are determined.
    C) easily the most widely followed financial markets in the United States.
    D) the markets where all borrowers get their funds.

33) Which of the following instruments is not traded in a money market?
    C) Residential mortgages.   D) Eurodollars.

34) Money is defined as
    A) anything that is generally accepted in payment for goods and services or in the repayment of debt.
    B) the unrecognized liability of governments.
    C) a risk-free repository of spending power.
    D) bills of exchange.

35) A financial market in which previously issued securities can be resold is called a ________ market.
    A) primary   B) used securities   C) tertiary   D) secondary

37) GDP measured with constant prices is referred to as A) the GDP deflator. B) real GDP. C) nominal GDP. D) industrial production.

38) Everything else held constant, a decline in interest rates will cause spending on housing to A) remain unchanged. B) rise. C) fall. D) either rise, fall, or remain the same.

39) If an individual moves money from a demand deposit account to a money market deposit account, A) M1 stays the same and M2 stays the same. B) M1 stays the same and M2 increases. C) M1 increases and M2 decreases. D) M1 decreases and M2 stays the same.

40) Economists find no completely satisfactory way to measure money because A) economists find disagreement interesting and refuse to agree for ideological reasons. B) money supply statistics are a state secret. C) the Federal Reserve does not employ or report different measures of the money supply. D) the "moneyness" or liquidity of an asset is a matter of degree.

41) If the maturity of a debt instrument is less than one year, the debt is called _______. A) short-term B) long-term C) intermediate-term D) prima-term.

42) Bonds issued by state and local governments are called _______ bonds. A) Treasury B) commercial C) corporate D) municipal.

43) Fear of a major recession causes stock prices to fall, everything else held constant, which in turn causes consumer spending to A) increase. B) decrease. C) remain unchanged. D) cannot be determined.

44) Federal funds are A) loans made by banks to the Federal Reserve System. B) loans made by the Federal Reserve System to banks. C) loans made by banks to each other. D) funds raised by the federal government in the bond market.

45) The stock market is important because it is A) where foreign exchange rates are determined. B) the most widely followed financial market in the United States. C) the market where most borrowers get their funds. D) where interest rates are determined.
46) Evidence from the United States and other foreign countries indicates that
   A) there is a strong positive association between inflation and growth rate of money over
       long periods of time.
   B) money growth is clearly unrelated to inflation.
   C) there is little support for the assertion that "inflation is always and everywhere a
       monetary phenomenon."
   D) countries with low monetary growth rates tend to experience higher rates of inflation, all
       else being constant.

47) Typically, borrowers have superior information relative to lenders about the potential returns
   and risks associated with an investment project. The difference in information is called
   _______, and it creates the _______ problem.
   A) adverse selection; risk sharing
   B) asymmetric information; adverse selection
   C) adverse selection; moral hazard
   D) asymmetric information; risk sharing

48) Equity instruments are traded in the _______ market.
   A) money  B) commodities  C) capital  D) bond

49) A disadvantage of _______ is that it is very heavy and hard to transport from one place to
   another.
   A) electronic money  B) fiat money
   C) commodity money  D) paper money

50) 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.
   A) 20  B) 25  C) 30  D) 45
Answer Key
Testname: EXAM1_SPRING_2013

1) A
2) C
3) B
4) A
5) C
6) C
7) B
8) D
9) A
10) B
11) A
12) A
13) C
14) C
15) D
16) C
17) A
18) C
19) A
20) B
21) C
22) C
23) B
24) B
25) D
26) A
27) D
28) B
29) B
30) B
31) A
32) A
33) C
34) A
35) D
36) A
37) B
38) B
39) D
40) D
41) A
42) D
43) B
44) C
45) B
46) A
47) B
48) C
Answer Key
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49) C
50) D