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

1) When a new depositor opens a checking account at the First National Bank, the bank’s assets ____ and its liabilities _____.
   A) increase; increase  
   B) decrease; decrease  
   C) decrease; increase  
   D) increase; decrease

2) Modern liability management has resulted in
   A) failure by banks to coordinate management of assets and liabilities.
   B) increase importance of deposits as a source of funds.
   C) increased sales of certificates of deposits to raise funds.
   D) reduced borrowing by banks in the overnight loan market.
   E) all of the above.

3) In the absence of regulation, banks would probably hold
   A) too little capital.
   B) too much capital, reducing the efficiency of the payments system.
   C) too much capital, reducing the profitability of banks.
   D) none of the above.

4) Which of the following are not reported as assets on a bank’s balance sheet?
   A) Borrowings  
   B) Savings deposits  
   C) Reserves  
   D) Only A and B of the above

5) Credit rationing occurs when a bank
   A) refuses to make a loan of any amount to a borrower, even when she is willing to pay a higher interest rate.
   B) restricts the size of the loan to less than the borrower would like.
   C) does either A or B of the above.
   D) does neither A nor B of the above.

6) A bank will want to hold more excess reserves (everything else equal) when
   A) it expects to have deposit inflows in the near future.
   B) the cost of selling loans falls.
   C) brokerage commissions on selling bonds increase.
   D) all of the above situations occur.
7) Which of the following statements most accurately describes the task of bank asset management?

A) Banks seek to have the highest liquidity possible subject to earning a positive rate of return on their operations.
B) Banks seek to prevent bank failure at all cost; since a failed bank earns no profit, liquidity needs supersede the desire for profits.
C) Banks seek the highest returns possible subject to minimizing risk and making adequate provisions for liquidity.
D) None of the above accurately describes the task of asset management.

8) Which of the following are reported as assets on a bank’s balance sheet?

A) Cash items in the process of collection
B) Deposits with other banks
C) Bank capital
D) Checkable deposits
E) Only A and B of the above

9) Which of the following statements is false?

A) The expenses involved in servicing accounts (salaries, building rent, etc.) make up over half the costs of running a bank.
B) Technically, savings deposits are not payable on demand.
C) Demand deposits are checkable deposits that pay no interest.
D) Nontransaction deposits are the primary source of bank funds.

10) If borrowers with the most risky investment projects seek bank loans in higher proportion to those borrowers with the safest investment projects, banks are said to face the problem of

A) adverse credit risk.
B) lemon lenders.
C) moral hazard.
D) adverse selection.

11) Banks acquire the funds that they use to purchase income-earning assets from such sources as

A) bank capital.
B) reserves.
C) cash items in the process of collection.
D) all of the above.
E) only A and B of the above.
12) If a bank has $100,000 of deposits, a required reserve ratio of 20 percent, and it holds $30,000 in reserves, then it need not rearrange its balance sheet if there is a deposit outflow of
A) $20,000.
B) $8,000.
C) $5,000.
D) either A or B of the above.
E) either B or C of the above.

13) A bank’s balance sheet
A) lists sources and uses of bank funds.
B) shows that total assets equals total liabilities plus equity capital.
C) indicates whether or not the bank is solvent.
D) does all of the above.
E) does only A and B of the above.

14) Holding all else constant, when a bank receives the funds for a deposited check,
A) cash items in the process of collection fall by the amount of the check.
B) bank assets remain unchanged.
C) bank liabilities decrease by the amount of the check.
D) all of the above.
E) only A and B of the above.

15) Which of the following are reported as liabilities on a bank’s balance sheet?
A) Nontransaction deposits
B) Bank capital
C) Loans
D) Only A and B of the above
E) Only B and C of the above

16) Secondary reserves are so called because
A) they are not easily converted into cash, and are, therefore, of secondary importance to banking firms.
B) 50% of these assets count toward meeting required reserves.
C) they can be converted into cash with low transactions costs.
D) of none of the above.
17) A bank facing a reserve deficiency will first
   A) borrow from the Fed.
   B) sell securities.
   C) borrow from other banks.
   D) call in loans.
   E) all of the above.

18) The likelihood of bank failure increases when
   A) a bank has more capital.
   B) a bank holds more U.S. government securities.
   C) a bank suffers large deposit outflows.
   D) a bank holds more excess reserves.
   E) all of the above.

19) Large-denomination CDs are _____, so that like a bond they can be resold in a _____ market before they mature.
   A) negotiable; primary
   B) nonnegotiable; primary
   C) nonnegotiable; secondary
   D) negotiable; secondary

20) When $1 million is deposited at a bank, the required reserve ratio is 20 percent, and the bank chooses not to hold any excess reserves but makes loans instead, then, in the bank’s final balance sheet,
   A) the liabilities of the bank increase by $1,000,000.
   B) the assets at the bank increase by $1,000,000.
   C) reserves increase by $200,000.
   D) each of the above occurs.
   E) both A and B of the above occur.
Answer Key
Testname: PRACTICE_CH09

1) A
2) C
3) A
4) D
5) C
6) C
7) C
8) E
9) A
10) D
11) A
12) E
13) D
14) E
15) D
16) C
17) C
18) C
19) D
20) D