

Financial Sector Unit Test
AP Macroeconomics
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Multiple Choice: Choose the letter of the BEST answer for each question. There is only one possible answer for each question. Do not write on the test!

1. When you use money to purchase your lunch, money is serving which role(s)?
 - I. Medium of exchange
 - II. Store of value
 - III. Standard of value
 - a. I only
 - b. II only
 - c. III only
 - d. I and III only
 - e. I, II, and III

2. When you decide you want “\$10 worth” of a product, money is serving which role(s)?
 - I. Medium of exchange
 - II. Store of value
 - III. Standard of value
 - a. I only
 - b. II only
 - c. III only
 - d. II and III only
 - e. I, II, and III

3. In the United States, the dollar is
 - a. Backed by silver.
 - b. Backed by gold and silver.
 - c. Commodity-backed money.
 - d. Commodity money.
 - e. Fiat money.

4. Bank reserves include which of the following?
 - I. Currency in bank vaults
 - II. Bank deposits held in accounts at the Federal Reserve
 - III. Customer deposits in bank checking accounts
 - a. I only
 - b. II only
 - c. III only
 - d. I and II only
 - e. I, II, and III

5. The fraction of bank deposits actually held as reserves is the
- Reserve ratio.
 - Required reserve ratio.
 - Excess reserve ratio.
 - Reserve requirement.
 - Monetary base.
6. Which of the following changes would be the most likely to increase the size of the money multiplier?
- An increase in the required reserve ratio
 - An increase in excess reserves
 - A decrease in cash holdings by consumers
 - An increase in bank runs
 - A decrease in deposit insurance
7. The monetary base equals
- Currency in circulation.
 - Reserves held by banks.
 - Currency in circulation – reserves held by banks.
 - Currency in circulation + reserves held by banks.
 - Currency in circulation/reserves held by banks.
8. Which of the following is NOT a role of the Federal Reserve System?
- Controlling bank reserves
 - Printing currency (Federal Reserve notes)
 - Carrying out monetary policy
 - Supervising and regulation banks
 - Holding reserves for commercial banks
9. Which of the following financial services does the Federal Reserve provide for commercial banks?
- Clearing checks
 - Holding reserves
 - Making loans
- I only
 - II only
 - III only
 - I and II only
 - I, II, and III
10. Which of the following is not a task of the financial system?
- Transaction costs
 - Risk
 - Liquidity
- I only
 - II only
 - III only
 - I and II only
 - I, II, and III

11. When the Fed makes a loan to a commercial bank, it charges
- No interest.
 - The prime rate.
 - The federal funds rate.
 - The discount rate.
 - The market interest rate.
12. When a member bank needs loans to cover their expenses at a bank, which interest do they choose to use even though it may be a higher interest rate.
- No interest
 - The prime rate.
 - The federal funds rate.
 - The discount rate.
 - The market interest rate.

13. If the Fed purchases U.S. Treasury bills from a commercial bank, what happens to bank reserves and the money supply?

Bank Reserves

Money Supply

- | | |
|-------------|-----------|
| a. Increase | decrease |
| b. Increase | increase |
| c. Decrease | decrease |
| d. Decrease | increase |
| e. Increase | no change |

14. A change in which of the following will shift the money demand curve?

- The aggregate price level
- Real GDP
- The interest rate

- I only
- II only
- III only
- I and II only
- I, II, and III

15. The quantity of money demanded rises (that is, there is a movement along the money demand curve) when
- The aggregate price level increases.
 - The aggregate price level falls.
 - Real GDP increases.
 - New technology makes banking easier.
 - Short-term interest rates fall.

16. The real interest rate equals the
- Nominal interest rate plus the inflation rate.
 - Nominal interest rate minus the inflation rate.
 - Nominal interest rate divided by the inflation rate.
 - Nominal interest rate time the inflation rate.
 - Federal funds rate.

17. Which of the following will increase the demand for loanable funds?
- A federal government budget surplus
 - An increase in perceived business opportunities
 - A decrease in the interest rate
 - Positive capital inflows
 - Decrease private savings rates
18. Which of the following will increase the supply of loanable funds?
- An increase in perceived business opportunities
 - Decreased government borrowing
 - An increased private saving rate
 - An increase in the expected inflation rate
 - A decrease in capital inflows
19. Suppose that a national government increased deficit spending on goods and services, increasing its demand for loanable funds. In the long run, this policy would most likely result in which of the following changes in this country?

<u>Real Interest Rate</u>	<u>Investment</u>
a. Decrease	Decrease
b. Decrease	Increase
c. Increase	Decrease
d. Increase	No change
e. No change	Increase

20. If the government increases expenditures on goods and services and increases taxation by the same amount, which of the following will occur?
- Aggregate demand will be unchanged.
 - Aggregate demand will increase.
 - Interest rates will decrease.
 - The money supply will decrease.
 - The money supply will increase.
21. Which of the following contributed to the creation of the Federal Reserve System?
- The bank panic of 1907
 - The Great Depression
 - The savings and loan crisis of the 1980's
- I only
 - II only
 - III only
 - I and II only
 - I, II, and III
22. To counteract a recession, the Federal Reserve should
- Raise the reserve requirement and the discount rate.
 - Sell securities on the open market and raise the discount rate
 - Sell securities on the open market and lower the discount rate
 - Buy securities on the open market and raise the discount rate
 - Buy securities on the open market and lower the discount rate

23. An increase in which of the following would cause an increase in aggregate supply?
- Labor productivity
 - The wage rate
 - Prices of imports
 - Consumer spending
 - Interest rates
24. Which of the following is the most liquid monetary aggregate?
- M1
 - M2
 - M3
 - Near-moneys
 - Dollar bills
25. A financial intermediary that provides liquid financial assets in the form of deposits to lenders and uses their funds to finance the illiquid investment spending needs of borrowers is called a
- Mutual fund
 - Bank
 - Corporation
 - Pension fund
 - Life insurance company
26. Which of the following is NOT a type of financial asset?
- Bonds
 - Stocks
 - Bank deposits
 - Loans
 - Houses
27. Which of the following is the best example of using money as a store of value?
- A customer pays in advance for \$10 worth of gasoline at a gas station.
 - A babysitter puts her earning in a dresser drawer while she saves to buy a bicycle.
 - Travelers buy meals on board an airline flight.
 - Foreign visitors to the United States convert their currency to dollars at the airport.
 - You use \$1 bills to purchase soda from a vending machine.
28. Which of the following time values of money is worth the most?
- Present value
 - Future value
 - Past value
- I only
 - II only
 - III only
 - I and II only
 - I, II, and III

29. What does the acronym P.I.L.E. represent?
- Productivity, Investments, Laws, Expectations
 - Products, Inputs, Laws, Expectations
 - Productivity, Inputs, Laws, Experiences
 - Productivity, Investments, Long Run, Expectations
 - Productivity, Inputs, Laws, Expectations
30. What does the acronym C.I.G.X_n represent?
- Consumers, Inputs, Government, Net Exports
 - Consumers, Investments, Government, Exports
 - Consumers, Investments, Government, Net Exports
 - Consumers, Inputs, Government, Net Imports
 - Consumers, Investments, Government, Imports

Short Answer: Write out your answer for the following question.

31. Calculate the MS using the data below:

Checkable Deposits	\$408
Small-time Deposits	\$12
Large-time Deposits	\$2,965
Noncheckable Savings Deposits	\$386
Institutional Money Market Funds	\$4,723
Currency	\$612

M1 = _____

M2 = _____

M3 = _____

Free Response Questions: Write or graph out your answer for each question. Make sure you answer all parts of the question.

32. Assume that the United States economy is currently in long-run equilibrium.
- a. Draw a correctly labeled graph of aggregate demand and aggregate supply and show each of the following.
 - i. The long-run aggregate supply curve
 - ii. The current equilibrium output and price levels, labeled as Y_E and PL_E , respectively.
 - b. Assume that the government increases spending on national defense without raising taxes.
 - i. On your graph in part (a), show how the government action affects aggregate demand.
 - ii. How will this government action affect the unemployment rate in the short run? Explain.
 - c. Assume that the economy adjusts to a new long-run equilibrium after the increase in government spending.
 - i. How will the short-run aggregate supply curve in the new long-run equilibrium compare with that in the initial long-run equilibrium in part (a)? Explain.
 - ii. On your graph in part (a), label the new long-run equilibrium price level as PL_2 .
 - d. In order to finance the increase in government spending on national defense from part (b), the government borrows funds from the public. Using a correctly labeled graph of the loanable funds market, show the effect of the government's borrowing on the real interest rate.
 - e. Given the change in the real interest rate in part (d), what is the impact on each of the following?
 - i. Investment
 - ii. Economic growth rate. Explain.

33. Assume the economy of Andersonland is in a long-run equilibrium with full employment. In the short run, nominal wages are fixed.
- a. Draw a correctly labeled graph of short-run aggregate supply, long-run aggregate supply, and aggregate demand. Show each of the following.
 - i. Equilibrium output, labeled Y_1
 - ii. Equilibrium price level, labeled PL_1
 - b. Assume that there is an increase in exports from Andersonland. On your graph in part (a), show the effect of higher exports on the equilibrium in the short run, labeling the new equilibrium output and price level Y_2 and PL_2 , respectively.
 - c. Based on your answer in part (b), what is the impact of higher exports on real wages in the short run? Explain.
 - d. As a result of the increase in exports, export-oriented industries in Andersonland increase expenditures on new container ships and equipment.
 - i. What component of aggregate demand will change?
 - ii. What is the impact on the long-run aggregate supply? Explain.
 - e. Suppose the economy begins to experience recessionary pressures due to unforeseen stagflation. Assume that the Central Bank of Rankinland pursues an expansionary monetary policy.
 - i. Identify the open-market operation that the Central Bank would use.
 - ii. Draw a correctly labeled money market graph and show the short-run effect of the expansionary monetary policy on the nominal interest rate.
 - iii. Assuming no change to the price level, what happens to the real interest rate as a result of the monetary policy? Explain.
 - iv. Given your answers to part (e)(iii) regarding the real interest rate, what happens to the real gross domestic product in the short run? Explain.