Question #1 of 113

Question ID: 1573019

A central bank that wants to increase short-term interest rates is *most likely* to:

A) issue long-term bonds.

B) decrease bank reserve requirements.

C) sell government securities.

Explanation

Open market operations to sell securities will decrease the outstanding supply of cash balances and increase short-term interest rates. The central bank does not issue long-term bonds but may buy and sell bonds issued by the government. Decreasing reserve requirements or purchasing government securities would tend to decrease short-term interest rates.

(Module 15.1, LOS 15.b)

Question #2 of 113

Question ID: 1572972

Manufacturing and trade sales are *best* described as a:

A) lagging indicator.

B) leading indicator.

C) coincident indicator.

Explanation

Manufacturing and trade sales are a coincident indicator that generally reflects the current phase of the business cycle.

(Module 13.1, LOS 13.c)

Question #3 of 113

Question ID: 1591390

A distinction between fiscal policy and monetary policy is that fiscal policy:

A) is aimed at promoting economic growth, while monetary policy is aimed at promoting price stability.

B) concerns taxes and government spending, while monetary policy concerns the money supply.

C) is typically expansionary, while monetary policy is typically contractionary.

Explanation

The distinction between fiscal and monetary policy is that a country's government determines fiscal policy through taxes and spending, but its central bank determines monetary policy by controlling the money supply. Both fiscal and monetary policy can be used to promote economic growth and price stability. Either fiscal policy or monetary policy can be expansionary or contractionary.

(Module 14.1, LOS 14.a)

Question #4 of 113

Question ID: 1573071

Which of the following groups in the country of Minidonia would *least likely* be helped by the imposition of tariffs on Minidonian imports of transportation equipment?

A) Automotive manufacturers.

B) Trucking companies.

C) Minidonia's government.

Explanation

Tariffs on transportation equipment benefit the government in the form of tariff revenue, and benefit domestic producers and industry workers in the form of higher prices for transportation equipment. The users of transportation equipment, such as trucking companies, suffer from higher costs due to the higher prices of transportation equipment.

(Module 17.1, LOS 17.b)

Question #5 of 113

Question ID: 1572961

A peak in the business cycle is *most likely* associated with:

A) the highest level of economic output during the cycle.

B) decreasing inflation pressure.

C) payroll employment turning from positive to negative.

Explanation

The peak phase of a business cycle represents the highest level of economic output (real GDP) reached during that cycle. Inflation pressure that built during the expansion may continue into the early part of the contraction that follows the peak. Employment typically does not begin to decline until sometime after the peak.

(Module 13.1, LOS 13.a)

Question #6 of 113

Question ID: 1573054

Exogenous geopolitical risk factors are *best* described as those that are:

A) unanticipated. ✓

B) known in terms of timing but not outcome. ✗

C) known or anticipated long-term effects. ✗

Explanation

Exogenous risk refers to unanticipated geopolitical events. Thematic risk refers to factors with known or anticipated long-term effects. Event risk refers to factors that are known in terms of timing but not outcome.

(Module 16.1, LOS 16.d)

Question #7 of 113

Question ID: 1650898

Which of the following statements about credit cycles is *most accurate*?

A) Credit cycles tend to dampen business cycles. ✗

B) Credit cycles are a potential cause of asset price bubbles. ✓

C) A typical business cycle includes two or more credit cycles. ✗

Explanation

Credit cycles tend to amplify business cycles and are a potential cause of asset price bubbles. Credit cycles have tended to be longer, on average, than business cycles.

(Module 13.1, LOS 13.b)

Question #8 of 113

Question ID: 1591381

Firms' initial responses to an emerging economic contraction are *most likely* to be:

A) reducing overtime hours.

B) laying off workers.

C) deferring maintenance of machinery.

Explanation

Early in an economic contraction, firms typically reduce output by using capital and labor less intensively than during an expansion (e.g., by reducing overtime). When they believe a contraction is likely to persist, firms decrease capacity by laying off workers and reducing their physical capital, often by deferring maintenance or not replacing worn-out equipment.

(Module 13.1, LOS 13.c)

Question #9 of 113

Question ID: 1591374

Which of the following is *least likely* a characteristic of perfect competition?

A) The demand curve for an individual firm is a vertical line.

B) The size of each firm is small relative to the size of the overall market.

C) The products produced within a given market are homogenous.

Explanation

Under perfect competition individual firms have no control over price resulting in a demand schedule that is perfectly elastic or horizontal.

(Module 12.2, LOS 12.b)

Question #10 of 113

Question ID: 1572989

The crowding-out model implies that a:

A) budget deficit will increase the real interest rate and thereby retard private investment.

B) budget surplus will retard aggregate demand and trigger an economic downturn.

C) budget deficit will stimulate aggregate demand and trigger a multiplier effect which will lead to inflation.

Explanation

Increased budget deficits will increase the demand for loanable funds and lead to higher interest rates and thus lower private investment. Crowding-out implies that an increase in government spending will choke off private investment and reduce the intended impact of fiscal policy changes on aggregate demand.

(Module 14.1, LOS 14.b)

Question #11 of 113

Question ID: 1573049

A country with little or no external trade is *most likely* one that practices:

A) multilateralism.

B) autarky.

C) hegemony.

Explanation

Autarky refers to a policy of seeking self-sufficiency by engaging in little or no external trade.

(Module 16.1, LOS 16.b)

Question #12 of 113

Question ID: 1572949

A venture capitalist is interested in providing funding for a new company. The company wants to enter an industry where the market structure is best described as monopolistic competition. The venture capitalist can expect to find an industry where:

A) the costs to enter the market are low.

B) the products are homogeneous.

C) firms compete regularly on price.

Explanation

In a monopolistically competitive market structure, the products are differentiated (not homogeneous), firms compete more on feature differences and quality than on price, and the barriers to entry (the costs of entering and exiting the market) are low.

(Module 12.2, LOS 12.c)

Question #13 of 113

Question ID: 1573026

Silvano Jimenez, an analyst at Banco del Rey, is reviewing recent actions taken by the U.S. Federal Reserve (the Fed) in setting monetary policy. Recently, the Fed decided to increase the money supply, which has resulted in a decrease in real interest rates. At a staff meeting, Jimenez brings this matter to the attention of his colleagues and makes the following statements:

Statement 1: Although the money supply increase has led to a decrease in real interest rates, we should begin to see U.S. investors decrease their investments abroad and the U.S. dollar will appreciate in the foreign exchange market.

Statement 2: The Fed's increase in the money supply will increase the amount of imports into the U.S.

Are Statement 1 and Statement 2 as made by Jimenez CORRECT?

	Statement 1	Statement 2
A)	Incorrect	Correct
B)	Incorrect	Incorrect
C)	Correct	Incorrect

Explanation

If the Fed increases the money supply and real interest rates decline, U.S. investors will seek higher real rates of return abroad and the U.S. dollar will depreciate as the dollar will be exchanged for foreign currencies in order to buy the foreign investments. Likewise, the decrease in real interest rates will reduce the inflow of funds from abroad as foreign investors seek higher rates of return outside the U.S. With a dollar that has depreciated, U.S. exports should increase, as U.S. products will become cheaper for foreign buyers. As such, both statements are incorrect.

(Module 15.1, LOS 15.b)

Question #14 of 113

Question ID: 1591365

An oligopoly is *least likely* characterized by:

A) a large number of sellers.

B) barriers to entry.

C) economies of scale.

Explanation

Oligopolies consist of a small number of sellers. They tend to be characterized by barriers to entry such as significant economies of scale.

(Module 12.2, LOS 12.b)

Question #15 of 113

Question ID: 1591367

Which of the following is *most likely* to be considered a characteristic of monopolistic competition?

A) High barriers to entry and exit. ✗

B) Inelastic demand curves. ✗

C) Differentiated products. ✓

Explanation

Differentiated products are a key characteristic of monopolistic competition. Although producers have downward sloping demand curves, they are typically elastic.

(Module 12.2, LOS 12.b)

Question #16 of 113

Question ID: 1573030

What are the three essential qualities an effective central bank should possess?

A) Independence, credibility, and transparency. ✓

B) Transparency, independence, and consistency. ✗

C) Credibility, relevance, and reliability. ✗

Explanation

A central bank that is independent from political interference, possesses credibility, and exhibits transparency is more likely to achieve its monetary policy objectives than a central bank that lacks these qualities. The other characteristics listed in the answer choices relate to financial statements and financial reporting standards.

(Module 15.2, LOS 15.c)

Question #17 of 113

Question ID: 1572986

When an economy dips into a recession, automatic stabilizers will tend to alter government spending and taxation so as to:

A) enlarge the budget deficit (or reduce the surplus).

B) reduce interest rates, thus stimulating aggregate demand.

C) reduce the budget deficit (or increase the surplus).

Explanation

During a recession unemployment is high, so the government will pay out more in unemployment compensation at the exact time that tax receipts from corporations and individuals are low. This will increase the size of the deficit and also maintain aggregate demand during recessionary periods.

(Module 14.1, LOS 14.b)

Question #18 of 113

Question ID: 1591364

Monopolistic competition differs from pure monopoly in that:

A) monopolistic competitors are price takers and monopolists are not.

B) monopolistic competitors have low barriers to entry and monopolists do not.

C) monopolists maximize profits and monopolistic competitors do not.

Explanation

Another name for monopolistic competition is a competitive price searcher market. Monopolistic competition refers to a large number of independent sellers, each produces a differentiated product, each market has a low barrier to entry, and each producer faces a downward sloping demand curve.

(Module 12.2, LOS 12.b)

Question #19 of 113

Question ID: 1572945

A market structure characterized by a large number of firms all producing identical products is *best* described as:

A) perfect competition.

B) monopoly.

C) monopolistic competition.

Explanation

In a perfectly competitive economic market, there are many independent firms, each seller is small relative to the total market, and there are no barriers to entry or exit.

(Module 12.2, LOS 12.b)

Question #20 of 113

Question ID: 1573003

A government that is implementing a contractionary fiscal policy is *most likely* to:

A) increase spending on public works.

B) decrease transfer payments to households.

C) decrease income tax rates.

Explanation

Decreasing spending or increasing taxes are contractionary fiscal policy actions. Increasing spending or decreasing taxes are expansionary.

(Module 14.2, LOS 14.d)

Question #21 of 113

Question ID: 1573114

An analyst observes that one U.S. dollar is worth eight Mexican pesos (MXN) or six Polish zlotys (PLN). The value of one PLN in terms of MXN is *closest* to:

A) 0.7500.

B) 1.3333.

C) 7.0000.

Explanation

For the Level I CFA exam, we quote foreign exchange rates as units of the price currency per one unit of the base currency. Here we are given MXN/USD = 8 and PLN/USD = 6, and we are asked to calculate MXN/PLN.

The cross rate MXN/PLN = MXN/USD × USD/PLN, which equals $8 \times 1/6 = 1.3333$.

(Module 19.1, LOS 19.a)

Question #22 of 113

Question ID: 1591388

Monetary policy is *most accurately* described as actions that influence economic activity by increasing or decreasing:

A) currency exchange rates.

B) the supply of money and credit.

C) tax rates on income and consumption.

Explanation

Monetary policy attempts to influence economic growth and inflation by increasing or decreasing the money supply and the availability of credit in the economy. Taxes and government spending are tools of fiscal policy. Monetary and fiscal policy can both influence currency exchange rates, but this is not typically their primary goal or tool.

(Module 14.1, LOS 14.a)

Question #23 of 113

Question ID: 1572997

The time it takes for policy makers to enact a fiscal policy action is *best* described as:

A) implementation lag.

B) action lag.

C) legislative lag.

Explanation

The time it takes for fiscal policy actions to be proposed, approved, and implemented is referred to as action lag.

(Module 14.2, LOS 14.d)

Question #24 of 113

Question ID: 1573122

If the AUD/CAD spot exchange rate is 0.9875 and 60-day forward points are −25, the 60-day AUD/CAD forward rate is *closest to*:

A) 0.9900.

B) 1.0125.

C) 0.9850.

Explanation

For an exchange rate quoted to four decimal places, forward points are expressed in units of 0.0001. The 60-day forward rate is 0.9875 + 0.0001(−25) = 0.9850.

(Module 19.1, LOS 19.b)

Question #25 of 113

Question ID: 1572987

An argument against being concerned with the size of a fiscal deficit is that a deficit can:

A) lead to higher future taxes that will increase government revenues. ✗

B) cause government borrowing to crowd out private borrowing. ✗

C) aid in increasing GDP and employment if the economy is operating at less than potential GDP. ✓

Explanation

One potential argument against being concerned about the size of fiscal deficits is that a deficit can help increase GDP and employment if output is below potential GDP and the spending does not divert capital from productive uses. Higher deficits that lead to crowding out or higher future taxes that result in lower long-term economic growth are arguments for concern about the size of fiscal deficits.

(Module 14.1, LOS 14.b)

Question #26 of 113

Question ID: 1572958

The *most* effective way to assess the impact of a potential merger on the market structure of an industry is to:

A) calculate the n-firm concentration ratio. ✗

B) analyze barriers to entry. ✗

C) calculate the Herfindahl-Hirschman Index. ✓

Explanation

The Herfindahl-Hirschman Index is more sensitive to mergers than the n-firm concentration ratio. Although barriers to entry for an industry are important in assessing market structure, they are not necessarily related to the impact of a merger.

(Module 12.3, LOS 12.e)

Question #27 of 113

Question ID: 1573065

Which of the items below is NOT a valid reason why nations adopt trade restrictions? To:

A) prohibit foreign firms from increasing market share by selling products below cost.

B) protect industries in which they have a comparative advantage.

C) protect industries that are highly sensitive to national security.

Explanation

If a particular country enjoys a comparative advantage in a particular industry, no protection is needed.

(Module 17.1, LOS 17.b)

Question #28 of 113

Question ID: 1608852

Which one of the following Federal Reserve monetary policies, when pursued in line with the U.S. government's fiscal policies, would help increase aggregate demand during a period of high unemployment?

A) A decrease in the discount rate.

B) The sale of bonds by the Fed.

C) An increase in the reserve requirements for financial institutions.

Explanation

A decrease in the Fed's lending rate is a monetary tool that the Fed can use to increase the money supply, thereby increasing aggregate demand during recessionary times when there is high unemployment. An increase in the reserve requirements and the sale of bonds by the Fed would all be restrictive monetary policies that would reduce the amount of money in the economy and reduce aggregate demand.

(Module 15.2, LOS 15.d)

Question #29 of 113

Question ID: 1573060

Geopolitical risks are *best* described as having:

A) greater impacts during recessionary phases of business cycles.

B) broad impacts on countries or regions, rather than discrete impacts on specific companies.

C) impacts that are not typically captured by scenario analysis.

Explanation

Geopolitical risks often have greater impacts during recessions than they would likely have during expansions. Geopolitical risks may have discrete impacts on specific companies or industries as well as broad impacts on countries and regions. Scenario analysis is a technique for modeling the potential impacts of geopolitical risks.

(Module 16.1, LOS 16.f)

Question #30 of 113

Question ID: 1573048

A country whose actions reflect nationalism is *least likely* to behave in ways that exhibit:

A) autarky.

B) bilateralism.

C) hegemony.

Explanation

Hegemony refers to behavior that reflects globalization and noncooperation. Autarky and bilateralism both refer to behavior that reflects nationalism.

(Module 16.1, LOS 16.b)

Question #31 of 113

Question ID: 1573036

An analyst has determined the projected trend rate of real GDP growth is 2.5% and the central bank's inflation target is 2.5%. If the central bank policy rate is 5.0%, monetary policy is *most likely*:

A) neutral.

B) contractionary.

C) expansionary.

Explanation

The neutral rate of interest is real trend rate of economic growth plus the inflation target. In this example, the neutral rate = 2.5% + 2.5% = 5.0%. Because the policy rate is the same as the neutral rate of interest, monetary policy is neither contractionary nor expansionary.

(Module 15.2, LOS 15.c)

Question #32 of 113

Question ID: 1573011

If a monetary policy is focused on combating inflation, which open market actions by the Federal Reserve will *most* effectively accomplish this?

A) Sell Treasury securities, causing aggregate demand to decrease. ✓

B) Sell Treasury securities, causing aggregate demand to increase. ✗

C) Purchase Treasury securities, causing aggregate demand to decrease. ✗

Explanation

If the Federal Reserve wants to slow inflation, it needs to decrease aggregate demand (i.e., business investment, consumer purchases of durable goods, and exports). To accomplish this, the Federal Reserve could engage in open market sales of Treasury securities.

(Module 15.1, LOS 15.b)

Question #33 of 113

Question ID: 1572974

Average weekly initial claims for unemployment insurance are classified as a:

A) coincident indicator. ✗

B) lagging indicator. ✗

C) leading indicator. ✓

Explanation

Initial claims for unemployment insurance are considered a leading indicator.

(Module 13.1, LOS 13.c)

Question #34 of 113

Question ID: 1572956

A key difference in oligopoly price setting between the Cournot model and the Stackelberg model is that the latter assumes:

A) sequential rather than simultaneous pricing by market participants.

B) competitors' prices will not change.

C) a strategic game model versus the former, which is a rule-based model.

Explanation

The Stackelberg model assumes pricing decisions are made sequentially, where the leader firm chooses the price first, and with the other firm choosing its price based on the leader's price. The Cournot model assumes competitors' prices will not change. Both Cournot and Stackelberg models are rule-based (strategic game) models.

(Module 12.2, LOS 12.d)

Question #35 of 113

Question ID: 1573058

A geopolitical risk that will have the biggest impact in the environmental, social, and governance realm will *most likely* have a velocity classification that is:

A) low.

B) high.

C) medium.

Explanation

A low-velocity classification describes a geopolitical risk that will take a long time to impact investment values. Risks that land in the environmental, social, and governance area tend to be low-velocity risks.

(Module 16.1, LOS 16.d)

Question #36 of 113

Question ID: 1573047

A country that generally engages in bilateralism is *best* characterized as exhibiting:

A) non-cooperation and globalization.

B) cooperation and globalization.

C) cooperation and nationalism.

Explanation

Archetypes of geopolitical behavior by countries include bilateralism (cooperation and nationalism), autarky (non-cooperation and nationalism), hegemony (non-cooperation and globalization), and multilateralism (cooperation and globalization).

(Module 16.1, LOS 16.b)

Question #37 of 113

Question ID: 1573083

Two countries trade freely with each other and have agreed to specific tariffs on imports from other countries. The workers in either country may freely cross the common border to work in the other country. The two countries have agreed to common economic policies, but they use separate currencies. This type of cooperation is *best* described as a(n):

A) monetary union. ✗

B) economic union. ✓

C) customs union. ✗

Explanation

The two countries are a part of an economic union. In an economic union, there is (1) free trade among members, (2) common restrictions (tariffs) on imports from non-members, (3) free movement of production factors (labor), and (4) common economic institutions and coordination of economic policies. While a customs union has common tariffs on imports from non-union countries and free trade, it does not allow workers to cross the borders freely and does not have common economic institutions. A monetary union requires all of the listed items and a common currency.

(Module 17.1, LOS 17.c)

Question #38 of 113

Question ID: 1591389

Attempting to influence economic growth and inflation by changing tax rates and government spending is *best* described as:

A) fiscal policy. ✓

B) a combination of fiscal and monetary policy. ✗

C) monetary policy. ✗

Explanation

Fiscal policy refers to actions by a government to influence economic activity through changes in taxes and government spending.

(Module 14.1, LOS 14.a)

Question #39 of 113

Question ID: 1573066

An anti-dumping restriction on trade:

A) keeps some highly sensitive products in the country.

B) protects infant industries.

C) prohibits foreign firms from selling products below cost to gain market share.

Explanation

Firms dump their goods at a price lower than cost in order to drive out the competition. Once this is complete, they will be able to raise prices to much higher levels in order to gain abnormal profits. Of course, once prices are increased, new competitors may arise.

(Module 17.1, LOS 17.b)

Question #40 of 113

Question ID: 1573079

Which of the following lists of trading blocs is *most* accurately ordered by degree of economic integration, from least to most integrated?

A) Customs union, economic union, monetary union.

B) Free trade area, economic union, common market.

C) Free trade area, common market, customs union.

Explanation

The order by degree of economic integration (from least to most integrated) is as follows: free trade areas, customs union, common market, economic union, and monetary union.

(Module 17.1, LOS 17.c)

Question #41 of 113

Question ID: 1572946

A market has the following characteristics:

- There is a large number of independent sellers.
- Each produces a differentiated product.
- There are low barriers to entry.
- Producers face downward-sloping demand curves.
- Demand is highly elastic.

This market is *best* characterized as:

A) an oligopoly.

B) a monopoly.

C) monopolistic competition.

Explanation

These conditions characterize monopolistic competition. By contrast, monopolies and oligopolies have high barriers to entry and involve either a single seller (monopoly) or a small number of interdependent sellers (oligopoly).

(Module 12.2, LOS 12.b)

Question #42 of 113

Question ID: 1573028

Xanadu attempts to decrease its inflation rate by implementing contractionary monetary policy. Which of the following is *most likely* to be the long-run effect on Xanadu's trade balance as a result of the monetary policy change?

A) Worsen.

B) Improve.

C) Remain the same.

Explanation

Contractionary monetary policy likely will cause higher domestic interest rates and attract foreign capital. As foreign capital flows in, the currency will appreciate relative to other currencies. The higher cost of its currency will result in higher cost exports that become less attractive to other countries. Xanadu's trade balance will most likely worsen.

(Module 15.1, LOS 15.b)

Question #43 of 113

Question ID: 1573078

Which form of regional trading agreement is *least likely* to allow free movement of labor?

A) Economic union.

B) Customs union.

C) Common market.

Explanation

Economic unions and common markets remove all barriers to the movement of labor and capital among their members. Customs unions do not have this feature.

(Module 17.1, LOS 17.c)

Question #44 of 113

Question ID: 1573005

The primary objective of a central bank is typically to:

A) control inflation.

B) achieve full employment.

C) stabilize exchange rates.

Explanation

Although some central banks have other stated goals including stabilizing exchange rates and achieving full employment, the primary objective for a central bank is to control inflation and promote price stability.

(Module 15.1, LOS 15.a)

Question #45 of 113

Question ID: 1573116

If the spot exchange rate between the British pound and the U.S. dollar is GBP/USD 0.7775, and the spot exchange rate between the Canadian dollar and the British pound is CAD/GBP 1.8325, what is the USD/CAD spot cross exchange rate?

A) 0.42428.

B) 1.42477.

C) 0.70186.

Explanation

First, convert GBP/USD 0.7775 to 1/0.7775 = USD/GBP 1.28617.

Then, divide USD/GBP 1.28617 by CAD/GBP 1.8325 = USD/CAD 0.70187.

(Module 19.1, LOS 19.a)

Question #46 of 113

Question ID: 1572996

The time it takes for a fiscal policy action to affect the economy is *best* described as:

A) recognition lag.

B) action lag.

C) impact lag.

Explanation

The time it takes for a fiscal policy action, once implemented, to have its effect on the economy is referred to as impact lag. Recognition lag is the time it takes policymakers to realize a fiscal policy response is needed. Action lag is the time it takes policymakers to discuss, enact, and implement fiscal policy measures.

(Module 14.2, LOS 14.d)

Question #47 of 113

Question ID: 1573080

The form of regional trading agreement (RTA) *least likely* to have the unintended negative effect of reducing a member country's low-cost imports from a non-member country is a:

A) customs union.

B) common market.

C) free trade area.

Explanation

A free trade area removes barriers to trade among its members but does not require any of its members to change their trade policies with non-members. A common market and a customs union both impose uniformity on trade rules with non-member nations, which could restrict a member's low-cost imports from a nation that is not a member.

(Module 17.1, LOS 17.c)

Question #48 of 113

Question ID: 1572921

At a fixed level of capital, output increases as the quantity of labor increases, but at a decreasing rate. This phenomenon is an example of:

A) diminishing costs to labor.

B) diminishing returns to capital.

C) diminishing returns to labor.

Explanation

The law of diminishing returns states that at some point, as more and more of a resource (e.g., labor) is devoted to a production process, holding the quantity of other inputs constant, the output increases, but at a decreasing rate.

(Module 12.1, LOS 12.a)

Question #49 of 113

Question ID: 1572917

According to the law of diminishing returns, doubling the number of salespeople for a firm will *most likely* result in:

A) increasing the total sales of the firm and reducing the average sales per salesperson.

B) decreasing the total sales of the firm as a result of competition amongst salespeople.

C) doubling the total sales of the firm.

Explanation

The law of diminishing returns states that as more of a resource is added to a production process, holding other resource use constant, increases in output will eventually decrease. Therefore, as more salespeople are added they will generate more sales at a decreasing rate. Total sales will increase and the average sales per salesperson will decrease.

(Module 12.1, LOS 12.a)

Question #50 of 113

Question ID: 1573057

A high-net-worth investor has a long time horizon of approximately 25 years before he will shift his allocations more in favor of safer, low-risk investments. The likelihood of this investor reacting to an event categorized as a black swan risk by changing his allocations is:

A) high.

B) low.

C) moderate.

Explanation

A black swan risk is an exogenous risk with a low likelihood of occurrence, but a high short-term impact. If an investor has a long time horizon (and 25 years is considered long) before he plans to shift allocations, an event that would be categorized as a black swan risk would not cause the investor to react in any way. Reactions to these events are much more likely for investors with short time horizons.

(Module 16.1, LOS 16.d)

Question #51 of 113

Question ID: 1572982

Discretionary fiscal policy refers to:

A) buying or selling securities in the open market to influence interest rates.

B) government spending programs that counteract the business cycle without the intervention of policymakers.

C) active decisions regarding spending and taxing to affect economic growth.

Explanation

Discretionary fiscal policy, in contrast to automatic stabilizers, refers to active decisions by the government to affect economic growth through changes in government spending and taxation. Buying or selling securities in the open market is an example of monetary policy.

(Module 14.1, LOS 14.b)

Question #52 of 113

Question ID: 1573056

Black swan risk refers to exogenous geopolitical risks that have substantial:

A) long-term effects and a high probability of occurrence.

B) short-term effects and a low probability of occurrence.

C) long-term effects and a low probability of occurrence.

Explanation

Exogenous risks relate to unanticipated geopolitical risk. A black swan risk is an exogenous risk with a low likelihood of occurrence, but a high short-term impact.

(Module 16.1, LOS 16.d)

Question #53 of 113

Question ID: 1573008

Which of the following is *least likely* to be a function of the central bank?

A) Issue currency.

B) Regulate the banking system.

C) Collect tax payments.

Explanation

The three functions of a central bank are to issue a country's currency, regulate its banking system, and to manage the money supply. Tax collection is typically conducted by a government agency created specifically to carry out that function.

(Module 15.1, LOS 15.a)

Question #54 of 113

Question ID: 1591402

The sell side of the foreign exchange markets primarily consists of:

A) multinational banks that deal in currencies.

B) firms and investors that are hedging their currency risks.

C) firms and investors that require foreign currencies for transactions.

Explanation

The sell side of foreign exchange markets is primarily large multinational banks. They are the primary dealers in currencies and originators of forward foreign exchange contracts. Firms and investors that require foreign currencies for transactions or wish to hedge their currency risks comprise the buy side of the foreign exchange market.

(Module 18.1, LOS 18.a)

Question #55 of 113

Question ID: 1573052

Promoting international monetary cooperation, promoting exchange stability, and assisting members experiencing balance of payments difficulties are the goals of the:

A) World Bank.

B) World Trade Organization.

C) International Monetary Fund.

Explanation

The IMF's main goals are promoting international monetary cooperation; facilitating the expansion and balanced growth of international trade; promoting exchange stability; assisting in the establishment of a multilateral system of payments; and making resources available (with adequate safeguards) to members.

(Module 16.1, LOS 16.c)

Question #56 of 113

Question ID: 1591380

The market structure in which a firm's optimal pricing strategy depends on the responses of other firms is:

A) Oligopoly.

B) Monopolistic competition.

C) Perfect competition.

Explanation

Interdependence of firms is a characteristic of an oligopoly market. Optimal pricing for a firm in an oligopoly market depends on expectations of how its competitors will respond.

(Module 12.2, LOS 12.d)

Question #57 of 113

Question ID: 1573029

A central bank has operational independence if it can independently determine:

A) the policy rate.

B) how inflation is calculated.

C) the horizon over which to achieve its inflation target.

Explanation

A central bank is said to have operational independence if it has the authority to determine the policy rate independently. Determining how inflation is calculated and the time horizon for achieving its target rate of inflation refer to a central bank that has target independence.

(Module 15.2, LOS 15.c)

Question #58 of 113

Question ID: 1573018

If a central bank's targeted inflation rate is above the current rate, the central bank is *most likely* to:

A) increase the overnight lending rate.

B) increase the reserve requirement.

C) buy government securities.

Explanation

Buying government securities is an expansionary policy that would increase the money supply and allow the inflation rate to increase to the targeted range. Increasing reserve requirements and overnight lending rates are contractionary and would have the opposite effects.

(Module 15.1, LOS 15.b)

Question #59 of 113

Question ID: 1573059

If the country of Smithia enacts sanctions against the political leaders of Jonesia, Smithia is said to be using:

A) a financial tool of geopolitics.

B) an economic tool of geopolitics.

C) a national security tool of geopolitics.

Explanation

Sanctions refer to restrictions on the financial interests of specific geopolitical actors and are considered a financial tool of geopolitics.

(Module 16.1, LOS 16.e)

Question #60 of 113

Question ID: 1573074

Which group is *most likely* to benefit from a quota imposed on imports of a good?

A) Foreign consumers of the good.

B) Domestic producers of the good.

C) Domestic consumers of the good.

Explanation

Quotas restrict the supply of imported goods, which increases the price domestically, benefiting domestic producers but harming domestic consumers. While some specific foreign producers may also benefit from the higher prices created by the quota if they receive the revenue transfer (due to higher prices received for all goods sold under the import license), foreign producers as a whole are likely to experience decreased sales in the country that imposes a quota.

(Module 17.1, LOS 17.b)

Question #61 of 113

Question ID: 1573053

Settling trade disputes and establishing agreements between trading partners *most accurately* describe the activities of the:

A) World Bank.

B) World Trade Organization.

C) International Monetary Fund.

Explanation

The World Trade Organization (WTO) deals with the global rules of trade between nations. Its main function is to ensure that trade flows as smoothly, predictably, and freely as possible.

(Module 16.1, LOS 16.c)

Question #62 of 113

Question ID: 1591359

Monopolistic competition differs from pure monopoly in that:

A) monopolists maximize profit; monopolistic competitors do not.

B) monopolistic competitors are price takers, monopolists are not.

C) barriers to entry are high under monopoly, but low under monopolistic competition.

Explanation

Monopolistic competition is characterized by the low barriers to enter its competitive markets. In contrast, a monopoly exists only where there are high barriers to market entry.

(Module 12.2, LOS 12.b)

Question #63 of 113

Question ID: 1573064

In the context of foreign trade, limits on the amounts of imports a country allows over some period are *best* described as:

A) quotas.

B) subsidies.

C) tariffs.

Explanation

Quotas are limits on the amounts of imports allowed into a country in a period of time. Government payments to firms that export goods are known as export subsidies. Taxes on imported goods collected by the government are known as tariffs.

(Module 17.1, LOS 17.b)

Question #64 of 113

Question ID: 1591385

Increases in firms' inventory-sales ratios are *most likely* to occur:

A) just after the trough of the economic cycle.

B) during an economic contraction.

C) just before a peak in the economic cycle.

Explanation

Just before a peak in the economic cycle, sales slow, but production and inventory levels still reflect expectations of continued rapid growth. Inventory accumulates as sales slow, increasing the inventory-sales ratio until firms reduce production in response to decreased or declining sales growth.

(Module 13.1, LOS 13.c)

Question #65 of 113

Question ID: 1573109

A government that imposes restrictions on capital flows into or out of its country is *most likely* attempting to:

A) implement floating exchange rates.

B) encourage competition among domestic industries.

C) reduce the volatility of domestic asset prices.

Explanation

Reasons commonly cited by governments for imposing capital restrictions include reducing the volatility of domestic asset prices, maintaining control of exchange rates, keeping domestic interest rates low, and protecting strategic industries from foreign ownership.

(Module 18.2, LOS 18.c)

Question #66 of 113

Question ID: 1591398

Assuming no changes in the prices of a representative consumption basket in two currency areas over the measurement period, changes in the nominal exchange rate:

A) can be extrapolated to calculate interest rates.

B) are equal to changes in the real exchange rate.

C) can be converted to the real exchange rate using interest rates.

Explanation

The real interest rate = the nominal interest rate × ratio of consumption basket (or index) price levels in both countries. Assuming no price changes, the real exchange rate has remained the same as the nominal interest rate during the period.

You can think of the ratio of the consumption basket (or index) price levels in two countries as the bracketed portion of the Fisher relation for two countries. Here is the Fisher relation for two countries:

$$\frac{(1 + \mathrm{R}_{\text{nominal A}})}{(1 + \mathrm{R}_{\text{nominal B}})} = \frac{(1 + \mathrm{R}_{\text{real A}})[1 + \mathrm{E}(\text{inflation}_{\mathrm{A}})]}{(1 + \mathrm{R}_{\text{real B}})[1 + \mathrm{E}(\text{inflation}_{\mathrm{B}})]}$$

Here is the ratio of the consumption basket (or index) price levels in two countries:

$$\frac{[1 + \mathrm{E}(\text{inflation}_{\mathrm{A}})]}{[1 + \mathrm{E}(\text{inflation}_{\mathrm{B}})]}$$

If inflation in A is 10% and inflation in B is 0%, the ratio of consumption basket (or index) price levels is 1.1. If inflation in both countries is 0%, the ratio of consumption basket (or index) price levels is 1 and the nominal interest rate = the real interest rate. If the nominal interest rate = the real interest rate, changes in the nominal exchange rate = changes in the real exchange rate.

(Module 18.1, LOS 18.a)

Question #67 of 113

Question ID: 1573021

If the U.S. Federal Reserve decides to decrease the money supply, which of the following is *most likely* to occur in the short run?

A) An increase in the velocity of money similar to decrease in the money supply. ✗

B) An increase in the real rate of interest. ✓

C) A decrease in the unemployment rate. ✗

Explanation

If the U.S. Federal Reserve decreases the money supply, an increase in nominal and real interest rates will occur. Higher real rates will cause businesses to invest less, which will cause the unemployment rate to increase. Furthermore, households will decrease purchases of durable goods, automobiles, and other items that are typically financed at short-term rates. This will decrease aggregate demand. The decrease in aggregate demand and expenditures will cause incomes to go down, which further decreases consumption and investment. Moreover, this decrease in aggregate demand will decrease real GDP and the price level in the short run and the long run.

(Module 15.1, LOS 15.b)

Question #68 of 113

Question ID: 1573040

Which of the following statements regarding the monetary policy transmission mechanism is *most* accurate?

A) Central banks can control short-term interest rates by increasing the money supply to increase interest rates or by decreasing the money supply to decrease interest rates.

B) Central banks can control long-term interest rates directly because decisions by consumers and businesses are based on these rates.

C) Central banks can control short-term interest rates directly, but long-term interest rates are beyond their control.

Explanation

Central banks can control short-term interest rates directly. However, the decisions of consumers and businesses are based on long-term interest rates, which are beyond the control of central banks. Increasing the money supply will decrease interest rates and decreasing the money supply will increase interest rates.

(Module 15.2, LOS 15.c)

Question #69 of 113

Question ID: 1573070

The primary benefits derived from tariffs usually accrue to:

A) domestic suppliers of goods protected by tariffs.

B) domestic producers of export goods.

C) foreign producers of goods protected by tariffs.

Explanation

Tariffs raise domestic prices, benefiting domestic suppliers.

(Module 17.1, LOS 17.b)

Question #70 of 113

Question ID: 1591392

Promoting economic growth and price stability are the goals of:

A) monetary policy, but not fiscal policy.

B) fiscal policy, but not monetary policy.

C) both fiscal and monetary policy.

Explanation

Both monetary and fiscal policies are used by policymakers with the goals of maintaining stable prices and producing positive economic growth.

(Module 14.1, LOS 14.a)

Question #71 of 113

Question ID: 1573075

Prior to the beginning of summer, the government of Japan places a 150 percent tariff on imported chain saws. Assume for this example that this tariff has a significant impact on the supply of chain saws. The government's action:

A) will protect the jobs and high wages of Japanese chain saw industry workers.

B) is more harmful than if the government had limited the amount of chain saws imported.

C) benefits the Japanese government and domestic producers.

Explanation

The Japanese government's action is an example of a *tariff*. A tariff is a tax imposed on imports and benefits the Japanese government because it collects the tariff. Domestic producers benefit because the reduction in the supply of imported goods means a higher domestic price.

The other choices are incorrect. A tariff is considered *less* harmful than a quota (an import quantity limitation) because under a quota, the domestic government does *not* receive any funds as it would under a tariff (the foreign producers receive the revenue transfer). In the long run, trade restrictions do not protect the net number of jobs in the country. The number of jobs protected by import restrictions will be offset by jobs lost in the import/export industry. Import/export firms will be unable to sell the overpriced domestic products abroad or import and sell the lower priced restricted foreign-made product.

(Module 17.1, LOS 17.b)

Question #72 of 113

Question ID: 1573125

If the no-arbitrage forward exchange rate for a euro in Japanese yen is less than the spot rate, then the interest rate in:

A) Japan is the same as in the Eurozone.

B) the Eurozone is less than in Japan.

C) Japan is less than in the Eurozone.

Explanation

If the quote is in terms of JPY per EUR, this implies that the JPY is expected to appreciate relative to the EUR. There will be no arbitrage opportunity only if the interest rate in Japan is lower than the interest rate in the Eurozone.

(Module 19.1, LOS 19.b)

Question #73 of 113

Question ID: 1591391

When the central bank increases short-term interest rates, its monetary policy is *best* described as:

A) contractionary.

B) expansionary.

C) accommodative.

Explanation

When the central bank increases short-term interest rates, it is attempting to decrease the growth rate of money and credit in an economy, and policy is said to be contractionary, restrictive, or tight. Accommodative or expansionary monetary policy attempts to increase the growth rate of money and credit (e.g., by decreasing short-term interest rates).

(Module 14.1, LOS 14.a)

Question #74 of 113

Question ID: 1572950

A key difference between the short-run and long-run outputs under monopolistic competition is that in the long run, the price is:

A) below average total cost, such that economic profits are negative.

B) equal to average total cost, such that economic profits are zero.

C) above average total cost, such that economic profits are positive.

Explanation

In the short run, a firm in a monopolistically competitive market structure can earn a positive economic profit because the price charged exceeds average total cost. However, competitors see this opportunity and are able to enter the market because the barriers to entry are low. Over the long run, the demand curve for each individual firm falls such that price is driven down to the level of average total cost, thereby reducing economic profits down to zero.

(Module 12.2, LOS 12.c)

Question #75 of 113

Question ID: 1591373

A firm operating as a price taker will produce the quantity at which:

A) revenue is maximized.

B) it earns long-run economic profit.

C) marginal revenue equals marginal cost.

Explanation

A firm operating as a price taker will produce the quantity where MC = MR. It will maximize profit and not revenue. In the long run, it will make zero economic profit.

(Module 12.2, LOS 12.b)

Question #76 of 113

Question ID: 1573035

Which of the following is currently the most-used target for central banks?

A) Interest rate targeting.

B) Inflation targeting.

C) Money supply targeting.

Explanation

Inflation targeting is the most-used tool of central banks for making monetary policy decisions.

(Module 15.2, LOS 15.c)

Question #77 of 113

Question ID: 1573115

If the exchange rate between the U.S. dollar and the Canadian dollar is USD/CAD 0.6403, and the exchange rate between the Canadian dollar and the UK pound sterling is CAD/GBP 2.5207, the exchange rate between the U.S. dollar and the UK pound sterling, stated as GBP/USD, is *closest* to:

A) 1.6140.

B) 0.6196.

C) 3.9367.

Explanation

For currency cross rate calculations, the recommended approach is to set up the given rates such that cross-multiplying will result in the exchange rate the question is asking for. In this case, GBP/USD = GBP/CAD × CAD/USD.

GBP/CAD = 1 / 2.5207 = 0.3967

CAD/USD = 1 / 0.6403 = 1.5618

GBP/USD = 0.3967 × 1.5618 = 0.6196

Alternatively, USD/CAD 0.6403 × CAD/GBP 2.5207 = USD/GBP 1.6140, and GBP/USD = 1 / 1.6140 = 0.6196.

(Module 19.1, LOS 19.a)

Question #78 of 113

Question ID: 1591362

Which of the following is *least likely* a characteristic of an oligopoly?

A) Products can either be similar or differentiated.

B) There are few sellers.

C) Relatively small economies of scale.

Explanation

Oligopolies have large economies of scale and interdependence among competitors.

(Module 12.2, LOS 12.b)

Question #79 of 113

Question ID: 1573067

If a country imposes a tariff on an imported good, which groups will *most likely* be harmed by the tariff?

A) Foreign consumers.

B) Domestic producers.

C) Domestic consumers.

Explanation

Domestic consumers in the country that imposes a tariff are harmed because they must pay higher prices for the good. Tariffs benefit domestic producers of the good by effectively imposing a price increase on competing imports. A tariff does not affect foreign consumers of the good.

(Module 17.1, LOS 17.b)

Question #80 of 113

Question ID: 1573069

David Forsythe and Linda Novak are discussing the advantages and disadvantages of import restrictions. They state the following:

> Forsythe: One of the groups that benefits from import restrictions is often the government that imposes them.
>
> Novak: Import restrictions impose costs on specific groups, such as the country's import industries, but these costs are more than offset by the benefits to other groups and to the economy as a whole.

With respect to these statements:

A) both are correct.

B) only one is correct.

C) both are incorrect.

Explanation

Forsythe is correct. A primary reason why trade restrictions remain widespread is the revenue that governments receive from tariffs. Novak is incorrect. Trade restrictions benefit specific groups, such as workers in the protected industries, but those benefits are most often less than the costs imposed on consumers and other industries as a whole.

(Module 17.1, LOS 17.b)

Question #81 of 113

Question ID: 1573016

Which of the following policy tools is the *least likely* to be available to the U.S. Federal Reserve Board?

A) Setting the discount rate at which banks can borrow from the Federal Reserve.

B) Buying and selling Treasury securities in the open market.

C) Requiring the banking system to tighten or loosen its credit policies.

Explanation

The U.S. Federal Reserve can encourage or persuade banks as a whole to tighten or loosen their credit policies, but it cannot compel them to do so.

(Module 15.1, LOS 15.b)

Question #82 of 113

Question ID: 1572983

Unemployment compensation is an example of:

A) an automatic monetary policy stabilizer.

B) an automatic fiscal policy stabilizer.

C) a discretionary fiscal policy stabilizer.

Explanation

Unemployment compensation automatically rises and falls with the business cycle, therefore it is an example of an automatic fiscal policy stabilizer.

(Module 14.1, LOS 14.b)

Question #83 of 113

Question ID: 1591376

In which of the following industry structures is a firm *least likely* able to increase its total revenue by decreasing the price of its output?

A) Perfect competition.

B) Oligopoly.

C) Monopolistic competition.

Explanation

Under perfect competition each firm is selling all of its output at the market price. Therefore any firm that sells its output at less than the market price will decrease its total revenue. Under monopolistic competition or oligopoly, firms are price searchers. Decreasing the price will increase the quantity a firm sells and may increase or decrease total revenue.

(Module 12.2, LOS 12.b)

Question #84 of 113

Question ID: 1591384

An economy has been producing at its full-employment level of output and the price level has been stable. Businesses then begin experiencing unintended decreases in their inventory levels. What does this *most likely* imply about the short-run outlook for economic growth and inflation?

	Economic growth	Inflation
A)	Increasing	Increasing
B)	Increasing	Decreasing
C)	Decreasing	Increasing

Explanation

Starting from conditions of long-run equilibrium, unintended decreases in inventory levels suggest that aggregate demand has increased. Producers will respond in the short run by increasing output and prices, so economic growth and inflation will increase.

(Module 13.1, LOS 13.c)

Question #85 of 113

Question ID: 1573073

In what way does a tariff differ from a quota? A tariff is imposed:

A) by world organizations, and quotas are imposed by individual countries.

B) as a tax on imports, and a quota limits the quantity that can be imported.

C) by a single government, and a quota is a worldwide agreement on the total amount of trade allowed.

Explanation

The difference between a tariff and a quota is that a *tariff* is a tax imposed on imported goods, while a *quota* is an import quantity limitation. Both are imposed by individual countries.

(Module 17.1, LOS 17.b)

Question #86 of 113

Question ID: 1572951

An industry characterized by monopolistic competition contains approximately 25 different companies. Each individual company is *most likely* to:

A) attempt to engage in price-fixing, as it will generate reasonable profits. ✗

B) have significant power over pricing. ✗

C) focus on average market price rather than individual competitor prices. ✓

Explanation

In a monopolistically competitive market structure, there will be a large number of independent sellers who will each have small market shares (so no one company has a lot of power over pricing), collusion or price-fixing will not be possible because of the sheer volume of companies, and each company will focus more on average market price than on the prices individual competitors are charging.

(Module 12.2, LOS 12.c)

Question #87 of 113

Question ID: 1572957

The sale price per unit that would maximize profits for all oligopoly participants is equal to $25 per unit. The sale price that would exist in a perfectly competitive market structure is equal to $18 per unit. The most likely price for a firm in an oligopoly to charge will be *closest* to:

A) $20. ✓

B) $25. ✗

C) $30. ✗

Explanation

The limiting outcomes in an oligopoly situation mean that price will fall somewhere between where all participants would maximize profits ($25) and the price that would result from perfect competition ($18). So, the most likely price out of the options given will be $20.

(Module 12.2, LOS 12.d)

Question #88 of 113

Question ID: 1573055

With respect to analyzing geopolitical risk, velocity *most likely* refers to the speed with which:

A) geopolitical events occur. ✗

B) mitigation strategies can be put into place. ✗

C) investment values reflect the effects of a risk. ✓

Explanation

The effects of geopolitical risk on investments can be analyzed in terms of likelihood (probability of occurrence), impact (magnitude of the effects on investment outcomes), and velocity (speed with which investment values reflect these effects).

(Module 16.1, LOS 16.d)

Question #89 of 113

Question ID: 1573009

Central banks are *most likely* to pursue a target inflation rate:

A) between 0% and 2%. ✗

B) equal to 0%. ✗

C) between 2% and 3%. ✓

Explanation

Central banks typically define price stability as a stable inflation rate of about 2% to 3%. A target of zero is not typically used because it would risk deflation.

(Module 15.1, LOS 15.a)

Question #90 of 113

Question ID: 1573022

The open market sale of Treasury securities by the Federal Reserve is *least likely* to result in:

A) a decreased rate of inflation.

B) increased exports of U.S. goods.

C) increased longer-term interest rates.

Explanation

When the Fed sells Treasuries, it causes both short- and long-term interest rates to increase. This rate increase causes the dollar to appreciate, which reduces foreign demand for domestic goods, causing exports to decline. The interest rate increase also puts downward pressure on price levels, which causes inflation to slow.

(Module 15.1, LOS 15.b)

Question #91 of 113

Question ID: 1573119

The spot exchange rate for CHF/EUR is 0.8342 and the 1-year forward quotation is −0.353%. The 1-year forward exchange rate for EUR/CHF is *closest to*:

A) 1.2029.

B) 0.8313.

C) 1.2022.

Explanation

The forward rate for CHF/EUR is $0.8342 \times (1 - 0.00353) = 0.8313$. The 1-year forward EUR/CHF exchange rate is $1 / 0.8313 = 1.2030$.

(Module 19.1, LOS 19.b)

Question #92 of 113

Question ID: 1572973

The inventory-to-sales ratio for manufacturing and trade is classified as a:

A) coincident indicator.

B) leading indicator.

C) lagging indicator.

Explanation

The inventory-to-sales ratio for manufacturing and trade is considered a lagging indicator because it peaks after the economy does, even though it is sometimes used in forecasting economic activity.

(Module 13.1, LOS 13.c)

Question #93 of 113

Question ID: 1591399

An exchange rate at which two parties agree to trade a specific amount of one currency for another a year from today is *best* described as a:

A) forward exchange rate. ✔

B) future exchange rate. ✘

C) real exchange rate. ✘

Explanation

A forward exchange rate specifies the amount of two currencies that will be exchanged at a specific point of time in the future. A transaction that uses the spot exchange rate is one that would occur immediately. A real exchange rate is one that has been adjusted for the relative inflation rates in two countries, and could be referring to an exchange rate that prevails at any given time.

(Module 18.1, LOS 18.a)

Question #94 of 113

Question ID: 1591379

Which of the following is *most likely* to be a characteristic of an oligopolistic industry?

A) Many sellers. ✘

B) Interdependence among firms. ✔

C) Low barriers to entry. ✘

Explanation

An oligopolistic industry exhibits a high degree of interdependence among firms. One firm's pricing decisions or advertising activities will affect the other firms' demand curves. These industries typically consist of a small number of sellers and have significant barriers to entry.

(Module 12.2, LOS 12.d)

Question #95 of 113

Question ID: 1572952

For profitable firms in an industry characterized by monopolistic competition, over a long time period, positive economic profits will tend to:

A) decrease, even if accounting profits remain positive. ✓

B) remain constant, regardless of the trend in accounting profits. ✗

C) increase, along with accounting profits. ✗

Explanation

Accounting profit is equal to net income, or revenues less expenses on a company's income statement. Economic profit is accounting profit, less implicit (or opportunity) costs. In the short run, a firm in a monopolistically competitive market structure can have both accounting and economic profits. But in the long run, economic profit will decrease to zero as competitors take advantage of favorable market conditions and low barriers to entry.

(Module 12.2, LOS 12.c)

Question #96 of 113

Question ID: 1591368

A market that is characterized by monopolistic competition is *least likely* to feature:

A) sellers that produce a differentiated product. ✗

B) a small number of independent sellers. ✓

C) low barriers to entry. ✗

Explanation

In monopolistic competition, there is a large, not small, number of independent sellers.

(Module 12.2, LOS 12.b)

Question #97 of 113

Question ID: 1591372

Which of the following is *most likely* a characteristic of perfect competition?

A) The number of firms in the market is small. ✗

B) Different firms sell their output at different prices. ✗

C) Barriers to entry are not a significant factor. ✓

Explanation

Under perfect competition there are no significant barriers to entry into the market. An industry that can be characterized as perfect competition typically consists of a large number of firms, each of which can sell its entire output at the market price, and none of which are large enough to affect the market price.

(Module 12.2, LOS 12.b)

Question #98 of 113

Question ID: 1591393

Country P begins importing goods from Country Q. In the long run, benefits from this trade relationship will *most likely* accrue to:

A) Country Q only.

B) Country P only.

C) both Country P and Country Q.

Explanation

Both countries in an international trade relationship benefit in the long run. Costs of international trade tend to be short-run effects in specific domestic industries.

(Module 17.1, LOS 17.a)

Question #99 of 113

Question ID: 1573046

A country joins a free trade agreement with its surrounding countries. The country also enacts a law prohibiting its domestic manufacturers from exporting military technology. In terms of geopolitics, which of these actions is considered cooperative?

A) Both of these actions.

B) Only one of these actions.

C) Neither of these actions.

Explanation

In the context of geopolitics, "cooperation" refers to interaction and engagement among countries. While participating in trade agreements is considered cooperative, banning exports of a particular good is considered non-cooperative.

(Module 16.1, LOS 16.a)

Question #100 of 113

Question ID: 1573117

The Japanese yen is trading at JPY/USD 115.2200 and the Danish krone (DKK) is trading at JPY/DKK 16.4989. The USD/DKK exchange rate is:

A) 0.1432.

B) 0.5260.

C) 6.9835.

Explanation

The cross rate between USD and DKK is calculated in the following manner:

> (USD/JPY)(JPY/DKK) = (1 / 115.2200) × 16.4989 = USD/DKK 0.1432 (the Yen cancels out)

(Module 19.1, LOS 19.a)

Question #101 of 113

Question ID: 1572943

Which of the following *most accurately* describes a market with a single seller of a product that has no good substitutes?

A) Oligopoly.

B) Monopolistic competition.

C) Monopoly.

Explanation

A monopoly is characterized by one seller, a specific and well-defined product for which there is no good substitutes, and high barriers to entry.

(Module 12.2, LOS 12.b)

Question #102 of 113

Question ID: 1572955

Firm X and Firm Y are two firms in a Cournot duopoly model with identical marginal cost curves. In the long run, equilibrium will occur with both firms selling:

A) different quantities with different market shares at an equilibrium price above the price in a monopoly market structure.

B) the same quantity with differing market shares at an equilibrium price equivalent to the price in a monopoly market structure.

C) the same quantity with an equivalent market share at an equilibrium price above the price in a perfectly competitive market.

Explanation

In a Cournot duopoly model, two firms with identical marginal cost curves in the long run will sell the same quantity with equivalent market shares at an equilibrium price above the price in a perfectly competitive market (but below the price in a monopoly market structure).

(Module 12.2, LOS 12.d)

Question #103 of 113

Question ID: 1608854

Which of the following policy combinations would *most likely* lead to private sector growth and a decreasing government share of GDP?

A) Contractionary fiscal policy and contractionary monetary policy.

B) Contractionary fiscal policy and expansionary monetary policy.

C) Expansionary fiscal policy and contractionary monetary policy.

Explanation

Contractionary fiscal policy combined with expansionary monetary policy is more likely to increase private sector growth and decrease the government share of GDP than the other policy combinations.

(Module 15.2, LOS 15.d)

Question #104 of 113

Question ID: 1573113

Given the following quotes, GBP/USD 2.0000 and MXN/USD 8.0000, calculate the direct MXN/GBP spot cross exchange rate.

A) 0.6250.

B) 0.2500.

C) 4.0000.

Explanation

Invert the first quote to read USD/GBP 0.5000. Then, 0.5000 × 8.0000 = 4.0000 MXN/GBP.

(Module 19.1, LOS 19.a)

Question #105 of 113

Question ID: 1572984

Which of the following statements *best* explains how automatic stabilizers work? Even without a change in fiscal policy, automatic stabilizers tend to promote:

A) a budget surplus during a recession and a budget deficit during an inflationary expansion. ✗

B) a budget deficit during a recession but do not promote a budget surplus during an inflationary expansion. ✗

C) a budget deficit during a recession and a budget surplus during an inflationary expansion. ✓

Explanation

Automatic stabilizers such as unemployment compensation, corporate profits tax, and the progressive income tax run a deficit during a business slowdown but run a surplus during an economic expansion. Therefore, they automatically implement countercyclical fiscal policy without the delays associated with policy changes that require legislative action.

(Module 14.1, LOS 14.b)

Question #106 of 113

Question ID: 1572998

The time it takes for policy makers to determine that the economy requires a fiscal policy action is *best* described as:

A) recognition lag. ✓

B) impact lag. ✗

C) action lag. ✗

Explanation

Recognition lag refers to the time it takes for fiscal policy makers to determine the need for a policy action. Action lag is the time it takes policymakers to discuss, enact, and implement fiscal policy measures. Impact lag is the time it takes for a fiscal policy measure to have its effect on the economy.

(Module 14.2, LOS 14.d)

Question #107 of 113

Question ID: 1572963

The expansion phase of a business cycle is *most likely* characterized by:

A) the rate of economic growth changing from negative to positive.

B) decreasing inflationary pressures.

C) increasing employment.

Explanation

Employment is typically increasing during the expansion phase of a business cycle. Inflationary pressures are typically decreasing during a contraction phase. The rate of economic growth changes from negative to positive in the trough phase.

(Module 13.1, LOS 13.a)

Question #108 of 113

Question ID: 1591387

Policies used with the goal of maintaining stable prices and producing economic growth include:

A) monetary policy only.

B) fiscal policy only.

C) both fiscal policy and monetary policy.

Explanation

Both fiscal and monetary policies are used to maintain stable prices and produce economic growth. Fiscal policy does so by mechanisms that involve spending and taxation, and monetary policy uses central bank tools to modify the availability of money and credit.

(Module 14.1, LOS 14.a)

Question #109 of 113

Question ID: 1591370

Characteristics of an oligopoly *least likely* include:

A) significant barriers to entry.

B) interdependence among competitors.

C) identical products.

Explanation

In an oligopoly, a small number of producers sell products that can be similar or differentiated. An oligopoly typically features significant barriers to entry including economies of scale. Pricing and output decisions by each firm directly influence the decisions of competing firms.

(Module 12.2, LOS 12.b)

Question #110 of 113

Question ID: 1573033

If a central bank implements an exchange rate targeting policy successfully, the country's inflation rate is *most likely* to be:

A) less than that of the target currency.

B) greater than that of the target currency.

C) the same as that of the target currency.

Explanation

Successful exchange rate targeting should result in the same inflation rate in the targeting country as in the country of the target currency.

(Module 15.2, LOS 15.c)

Question #111 of 113

Question ID: 1573002

An example of a contractionary fiscal policy change is a(n):

A) increase in a fiscal deficit.

B) increase in a fiscal surplus.

C) decrease in a fiscal surplus.

Explanation

An increase in a fiscal surplus or a decrease in a fiscal deficit is contractionary. An increase in a fiscal deficit or a decrease in a fiscal surplus is expansionary.

(Module 14.2, LOS 14.d)

Question #112 of 113

Question ID: 1573006

If a bank needs to borrow funds from the Federal Reserve to fund a temporary shortage in reserves, it would borrow funds at the:

A) prime rate.

B) discount rate.

C) federal funds rate.

Explanation

Banks are able to borrow from the Fed at the discount rate. The federal funds rate is the interest rate banks charge other banks to borrow reserves from other banks. The prime rate is the rate that commercial banks charge their best customers.

(Module 15.1, LOS 15.a)

Question #113 of 113

Question ID: 1573001

The country of Zurkistan is experiencing both high interest rates and high inflation. The government passes laws that reduce government spending and increase taxes. It takes many months before interest rates fall and inflation is reduced. This is an example of:

A) recognition lag in discretionary fiscal policy.

B) action lag and automatic stabilizers.

C) impact lag in discretionary fiscal policy.

Explanation

This is an example of discretionary fiscal policy involving impact lag because it takes time for the impact of the change in taxing and spending to be felt throughout the economy.

(Module 14.2, LOS 14.d)