Money and Banking

Homework #1

Due on Nov. 15, 2021

1. What are A) money market; B) capital market; C) bond market; D) stock market? Explain the meaning of these terms with at least one example for each.
2. Financial markets promote greater economic efficiency by channeling funds from \_\_\_\_\_\_\_\_ to \_\_\_\_\_\_\_\_.
   1. investors; savers
   2. borrowers; savers
   3. savers; borrowers
   4. savers; lenders Answer:
3. The price paid for the rental of borrowed funds (usually expressed as a percentage of the rental of $100 per year) is commonly referred to as the A) inflation rate.
   1. exchange rate.
   2. interest rate.
   3. aggregate price level.

Answer:

1. High interest rates might \_\_\_\_\_\_\_\_ purchasing a house or car but at the same time high interest rates might \_\_\_\_\_\_\_\_ saving.
   1. discourage; encourage
   2. discourage; discourage
   3. encourage; encourage D) encourage; discourage Answer:
2. Stock prices are
   1. relatively stable trending upward at a steady pace.
   2. relatively stable trending downward at a moderate rate.
   3. extremely volatile.
   4. unstable trending downward at a moderate rate. Answer:
3. A rising stock market index due to higher share prices
   1. increases people's wealth, but is unlikely to increase their willingness to spend. B) increases people's wealth and as a result may increase their willingness to spend.
   2. decreases the amount of funds that business firms can raise by selling newlyissued stock.
   3. decreases people's wealth, but is unlikely to increase their willingness to spend.

Answer:

1. A financial crisis is
   1. not possible in the modern financial environment.
   2. a major disruption in the financial markets.
   3. a feature of developing economies only.
   4. typically followed by an economic boom.

Answer:

1. Financial institutions that accept deposits and make loans are called A) exchanges.
   1. banks.
   2. over-the-counter markets.
   3. finance companies.

Answer:

1. If your nominal income in 2002 was $50,000, and prices doubled between 2002 and 2011, to have the same real income, your nominal income in 2011 must be A) $50,000.
   1. $75,000.
   2. $90,000.
   3. $100,000 Answer:
2. If real GDP in 2002 is $10 trillion, and in 2003 real GDP is $9.5 trillion, then real GDP growth from 2002 to 2003 is A) 0.5%.
   1. 5%.
   2. 0%.
   3. -5%.

Answer:

1. If the aggregate price level at time t is denoted by Pt, the inflation rate from time t - 1 to t is defined as
   1. t = (Pt – Pt - 1)/ Pt - 1.
   2. t = (Pt + 1 - Pt - 1) /Pt - 1.
   3. t = (Pt + 1 - Pt) /Pt.
   4. t = (Pt - Pt - 1) /Pt.

Answer:

1. If the CPI is 120 in 1996 and 180 in 2002, then between 1996 and 2002, prices have increased by A) 180%.
   1. 80%.
   2. 60%.
   3. 50%.

Answer:

1. Every financial market has the following characteristic: A) It determines the level of interest rates.
   1. It allows common stock to be traded.
   2. It allows loans to be made.
   3. It channels funds from lenders-savers to borrowers-spenders. Answer:
2. Which of the following can be described as involving direct finance? A) A corporation issues new shares of stock.
   1. People buy shares in a mutual fund.
   2. A pension fund manager buys a short-term corporate security in the secondary market.
   3. An insurance company buys shares of common stock in the over-the-counter markets. Answer:
3. Which of the following can be described as involving indirect finance? A) You make a loan to your neighbor.
   1. A corporation buys a share of common stock issued by another corporation in the primary market.
   2. You buy a U.S. Treasury bill from the U.S. Treasury.
   3. You make a deposit at a bank.

Answer:

1. Securities are \_\_\_\_\_\_\_\_ for the person who buys them, but are \_\_\_\_\_\_\_\_ for the individual or firm that issues them.
   1. assets; liabilities
   2. liabilities; assets
   3. negotiable; nonnegotiable D) nonnegotiable; negotiable Answer:
2. Which of the following statements about the characteristics of debt and equity is false?
   1. They can both be long-term financial instruments.
   2. They can both be short-term financial instruments.
   3. They both involve a claim on the issuer's income.
   4. They both enable a corporation to raise funds.

Answer:

1. Which of the following statements about the characteristics of debt and equities is true?
   1. They can both be long-term financial instruments.
   2. Bond holders are residual claimants.
   3. The income from bonds is typically more variable than that from equities.
   4. Bonds pay dividends. Answer:
2. Long-term debt has a maturity that is A) between one and ten years.
   1. less than a year.
   2. between five and ten years.
   3. ten years or longer.

Answer:

1. Which of the following is an example of an intermediate-term debt? A) A thirty-year mortgage. B) A sixty-month car loan.
   1. A six month loan from a finance company.
   2. A Treasury bond.

Answer:

1. A financial market in which only short-term debt instruments are traded is called the \_\_\_\_\_\_\_\_ market.
   1. bond
   2. money
   3. capital D) stock Answer:
2. Equity instruments are traded in the \_\_\_\_\_\_\_\_ market.
   1. money
   2. bond
   3. capital
   4. commodities Answer:
3. Which of the following instruments are traded in a money market? A) State and local government bonds.
   1. U.S. Treasury bills.
   2. Corporate bonds.
   3. U.S. government agency securities.

Answer:

1. Financial intermediaries provide customers with liquidity services. Liquidity services
   1. make it easier for customers to conduct transactions.
   2. allow customers to have a cup of coffee while waiting in the lobby.
   3. are a result of the asymmetric information problem.
   4. are another term for asset transformation.

Answer:

1. The problem created by asymmetric information before the transaction occurs is called \_\_\_\_\_\_\_\_, while the problem created after the transaction occurs is called \_\_\_\_\_\_\_\_.
   1. adverse selection; moral hazard
   2. moral hazard; adverse selection
   3. costly state verification; free-riding D) free-riding; costly state verification Answer: