Test Bank for Financial Markets and Institutions 13th Edition by Madura

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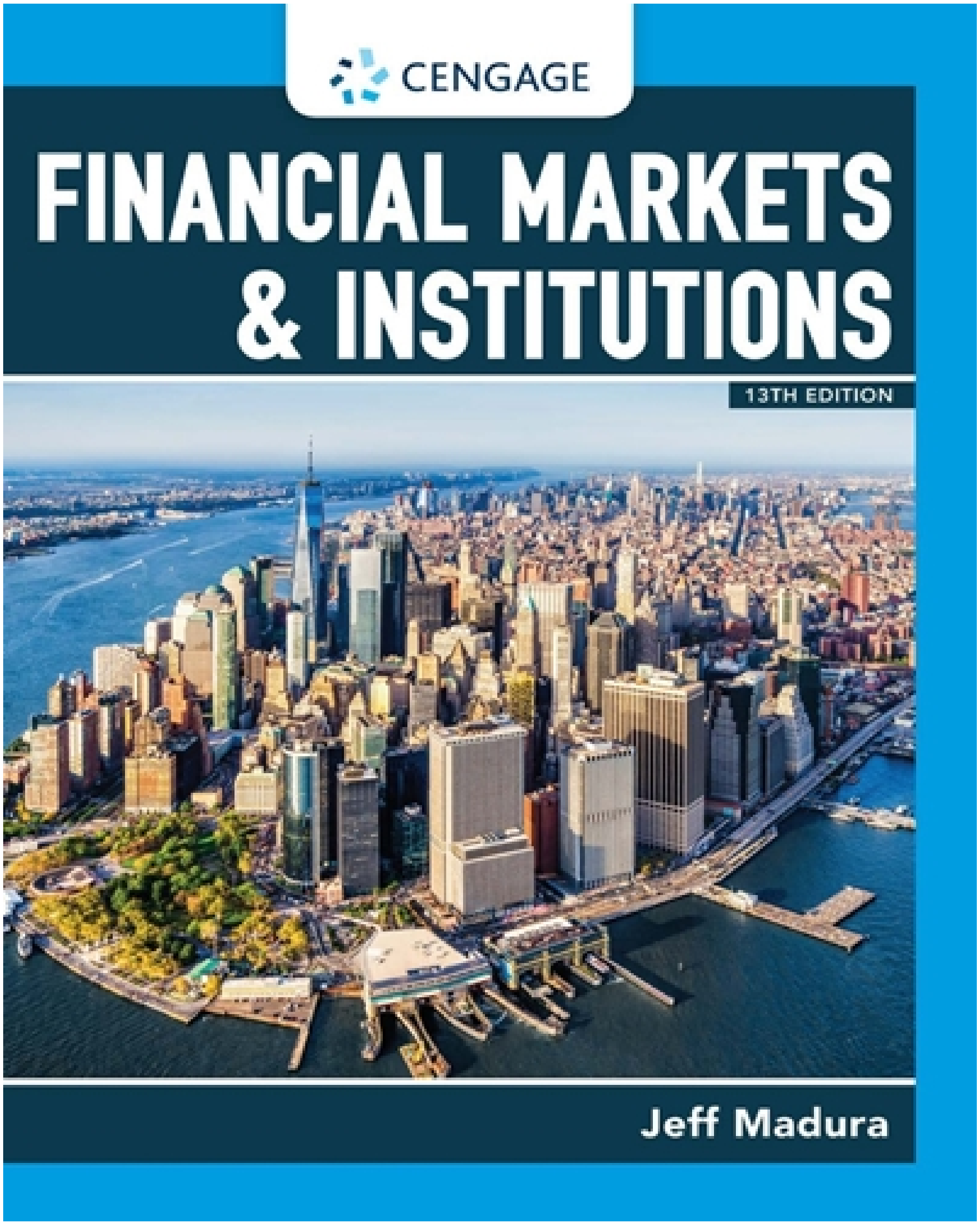

Test Bank

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TRUE/FALSE

1 : According to the loanable funds theory, market interest rates are determined by the factors that control the supply of and demand for loanable funds.
A : true
B : false

Correct Answer : A

2 : The supply of loanable funds in the United States is partly determined by the monetary policy implemented by the Federal Reserve System.
A : true
B : false

Correct Answer : A

3 : At any point in time, households and businesses demand a greater quantity of loanable funds at lower rates of interest.
A : true
B : false

Correct Answer : A

4 : The business demand for loanable funds is inversely related to the number of proposed projects implemented and inversely related to the interest rate.
A : true
B : false

Correct Answer : B

5 : Other things being equal, a smaller quantity of U.S. funds would be demanded by foreign governments and corporations if their domestic interest rates were high relative to U.S. rates.
A : true
B : false

Correct Answer : B

6 : If foreign interest rates fall, foreign firms and governments would likely reduce their demand for U.S. funds.
A : true
B : false

Correct Answer : A

7 : Since the aggregate demand for loanable funds is the sum of the quantities demanded by the separate sectors, and since most of these sectors are likely to demand a larger quantity of funds at lower interest rates (other things being equal), the aggregate demand for loanable funds is positively related to interest rates at any point in time.
A : true
B : false

Correct Answer : B

8 : In general, suppliers of loanable funds are willing to supply more funds if the interest rate is higher.
A : true

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B : false

Correct Answer : A

9 : If the aggregate demand for loanable funds increases without a corresponding increase in aggregate supply, there will be a surplus of loanable funds.

A : true

B : false

Correct Answer : B

10 : The relationship between interest rates and expected inflation is often referred to as the loanable funds theory.

A : true

B : false

Correct Answer : B

11 : According to the Fisher effect, if the real interest rate is zero, the nominal interest rate must be equal to the expected inflation rate.

A : true

B : false

Correct Answer : A

12 : To forecast the real interest rate for an upcoming period using the Fisher effect, the expected inflation rate over that period is subtracted from the nominal interest rate quoted for that period.

A : true

B : false

Correct Answer : A

13 : According to the Fisher effect, when the inflation rate is lower than anticipated, the real interest rate is relatively low.

A : true

B : false

Correct Answer : B

14 : Forecasters should consider future plans for corporate expansion and the future state of the economy when forecasting business demand for loanable funds.

A : true

B : false

Correct Answer : A

MULTIPLE CHOICE

15 : The level of installment debt as a percentage of disposable income is generally ____ during recessionary periods.?

A : ?higher

B : ?lower

C : ?zero

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D : ?negative

Correct Answer : B

16 : At any given point in time, households would demand a ____ quantity of loanable funds at ____ rates of interest.
A : greater; higher
B : greater; lower
C : smaller; lower
D : None of these are correct.

Correct Answer : B

17 : Businesses demand loanable funds to
A : finance installment debt.
B : subsidize other companies.
C : invest in long-term (fixed) assets.
D : None of these are correct.

Correct Answer : C

18 : The required return to implement a given business project will be ____ if interest rates are lower. This implies that businesses will demand a ____ quantity of loanable funds when interest rates are lower.?
A : ?greater; lower
B : ?lower; greater
C : ?lower; lower
D : ?greater; greater

Correct Answer : B

19 : If interest rates are ____, ____ projects will have expected returns that exceed a business's particular required rate of return.
A : higher; more
B : lower; more
C : lower; no
D : None of these are correct.

Correct Answer : B

20 : The demand for funds resulting from business investment in new projects is ____ related to the number of projects implemented, and is therefore ____ related to the interest rate.
A : inversely; positively
B : positively; inversely
C : inversely; inversely
D : positively; positively

Correct Answer : B

21 : If economic conditions become less favorable, then
A : expected cash flows on various projects will increase.
B : the required rate of return on projects will increase.
C : there will be additional acceptable business projects.
D : there will be a decreased demand by business for loanable funds.

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Correct Answer : D

22 : As a result of more favorable economic conditions, there is a(n) ____ demand for loanable funds, causing an ____ shift in the demand curve.?
A : ?decreased; inward
B : ?decreased; outward
C : ?increased; outward
D : ?increased; inward

Correct Answer : C

23 : The federal government’s demand for loanable funds is ____. If the budget deficit is expected to increase, the federal government’s demand for loanable funds will ____.
A : interest-elastic; decrease
B : interest-elastic; increase
C : interest-inelastic; increase
D : interest-inelastic; decrease

Correct Answer : C

24 : Other things being equal, foreign governments and corporations would demand ____ U.S. funds if their local interest rates were lower than U.S. rates. Therefore, for a given set of foreign interest rates, foreign demand for U.S. funds is ____ related to U.S. interest rates.?
A : ?less; inversely
B : ?more; positively
C : ?less; positively
D : ?more; inversely

Correct Answer : A

25 : For a given set of foreign interest rates, the quantity of U.S. loanable funds demanded by foreign governments or firms will be ____ U.S. interest rates.
A : positively related to
B : inversely related to
C : unrelated to
D : None of these are correct.

Correct Answer : B

26 : The quantity of loanable funds supplied is normally
A : highly interest-elastic.
B : more interest-elastic than the demand for loanable funds.
C : less interest-elastic than the demand for loanable funds.
D : equally as interest-elastic as the demand for loanable funds.
E : highly interest-elastic AND more interest-elastic than the demand for loanable funds.

Correct Answer : C

27 : The ____ sector is the largest supplier of loanable funds.
A : household
B : government

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C : business
D : None of these are correct.

Correct Answer : A

28 : If a strong economy allows for a large ____ in households' income, the supply curve will shift ____.
A : decrease; outward
B : increase; inward
C : increase; outward
D : None of these are correct.

Correct Answer : C

29 : The equilibrium interest rate
A : equates the aggregate demand for loanable funds with the aggregate supply of loanable funds.
B : equates the elasticity of the aggregate demand for and supply of loanable funds.
C : decreases as the aggregate supply of loanable funds decreases.
D : increases as the aggregate demand for loanable funds decreases.

Correct Answer : A

30 : The equilibrium interest rate should
A : fall when the aggregate supply of funds exceeds the aggregate demand for funds.
B : rise when the aggregate supply of funds exceeds the aggregate demand for funds.
C : fall when the aggregate demand for funds exceeds the aggregate supply of funds.
D : rise when the aggregate demand for funds equals the aggregate supply of funds.
E : rise when the aggregate supply of funds exceeds the aggregate demand for funds AND fall when the aggregate demand for funds exceeds the aggregate supply of funds.

Correct Answer : A

31 : Which of the following is likely to cause a decrease in the equilibrium U.S. interest rate, other things being equal??
A : ?a decrease in saving by foreign savers
B : ?an increase in inflation
C : ?pessimistic economic projections that cause businesses to reduce expansion plans
D : ?a decrease in saving by U.S. households

Correct Answer : C

32 : The Fisher effect states that the?
A : ?nominal interest rate equals the expected inflation rate plus the real rate of interest.
B : ?nominal interest rate equals the real rate of interest minus the expected inflation rate.
C : ?real rate of interest equals the nominal interest rate plus the expected inflation rate.
D : ?expected inflation rate equals the nominal interest rate plus the real rate of interest.

Correct Answer : A

33 : If the real interest rate was negative for a period of time, then
A : inflation is expected to exceed the nominal interest rate in the future.
B : inflation is expected to be less than the nominal interest rate in the future.

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C : actual inflation was less than the nominal interest rate during that period of time.
D : actual inflation was greater than the nominal interest rate during that period of time.

Correct Answer : D

34 : If inflation is expected to decrease, then?
A : ?savers will provide less funds at the existing equilibrium interest rate.
B : ?the equilibrium interest rate will increase.
C : ?the equilibrium interest rate will decrease.
D : ?borrowers will demand more funds at the existing equilibrium interest rate.

Correct Answer : C

35 : If inflation turns out to be lower than expected?
A : ?savers benefit.
B : ?borrowers benefit while savers are not affected.
C : ?savers and borrowers are equally affected.
D : ?savers are adversely affected but borrowers benefit.

Correct Answer : A

36 : If the economy weakens, there is ____ pressure on interest rates. If the Federal Reserve increases the money supply there is ____ pressure on interest rates (assume that inflationary expectations are not affected).?
A : ?upward; upward
B : ?upward; downward
C : ?downward; upward
D : ?downward; downward

Correct Answer : D

37 : What is the basis of the relationship between the Fisher effect and the loanable funds theory?
A : savers desire to maintain the existing real rate of interest
B : borrowers desire to achieve a positive real rate of interest
C : savers desire to achieve a negative real rate of interest
D : borrowers desire to achieve a positive real rate of interest AND savers desire to achieve a negative real rate of interest

Correct Answer : A

38 : Assume that foreign investors who have invested in U.S. securities decide to decrease their holdings of U.S. securities and increase their holdings of securities in their own countries. This should cause the supply of loanable funds in the United States to______ and should place ____ pressure on U.S. interest rates.
A : decrease; upward
B : decrease; downward
C : increase; downward
D : increase; upward

Correct Answer : A

39 : Assume that foreign investors who have invested in U.S. securities decide to increase their holdings of U.S. securities. This should cause the supply of loanable funds in the United States to ____ and should place ____ pressure on U.S. interest rates.?
A : ?decrease; upward

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B : ?decrease; downward
C : ?increase; downward
D : ?increase; upward

Correct Answer : C

40 : If the federal government needs to borrow additional funds, this borrowing reflects a(n) ____ in the supply of loanable funds and a(n) ____ in the demand for loanable funds.?
A : ?increase; no change
B : ?decrease; no change
C : ?no change; increase
D : ?no change; decrease

Correct Answer : C

41 : If the federal government reduces its budget deficit, this causes a(n) ____ in the supply of loanable funds and a(n) ____ in the demand for loanable funds.?
A : ?increase; no change
B : ?decrease; no change
C : ?no change; increase
D : ?no change; decrease

Correct Answer : D

42 : When there are expectations of higher inflation in the future, we would typically expect the supply of loanable funds to ____ and the demand for loanable funds to ____.?
A : ?increase; decrease
B : ?increase; increase
C : ?decrease; increase
D : ?decrease; decrease

Correct Answer : C

43 : If the real interest rate is expected to become negative, then the purchasing power of savings would be ____, as the inflation rate is expected to be ____ the existing nominal interest rate.?
A : ?decreasing; less than
B : ?decreasing; greater than
C : ?increasing; greater than
D : ?increasing; less than

Correct Answer : B

44 : If economic expansion is expected to decrease, the demand for loanable funds should ____ and interest rates should ____.?
A : ?increase; increase
B : ?increase; decrease
C : ?decrease; decrease
D : ?decrease; increase

Correct Answer : C

45 : The federal government’s spending policies are generally thought to be _________ interest rates, but municipal governments’ spending is somewhat ________ interest rates.?

A : ?independent of; sensitive to
B : ?sensitive to; independent of
C : ?inversely rated to; positively related to
D : ?positively related to; inversely related to

Correct Answer : A

46 : ?The federal government's _________ determines the budget deficit and therefore determines the government's demand for loanable funds.
A : ?monetary policy
B : ?fiscal policy
C : ?congressional policy
D : ?economic policy

Correct Answer : B

47 : Canada and the United States are major trading partners. If Canada experiences a major increase in economic growth, that could place ____ pressure on Canadian interest rates and ____ pressure on U.S. interest rates.?
A : ?upward; upward
B : ?upward; downward
C : ?downward; downward
D : ?downward; upward

Correct Answer : A

48 : If investors shift funds from stocks into bank deposits, this ____ the supply of loanable funds and places ____ pressure on interest rates.?
A : ?increases; upward
B : ?increases; downward
C : ?decreases; downward
D : ?decreases; upward

Correct Answer : B

49 : When Japanese interest rates rise, and exchange rate expectations remain unchanged, the most likely effect is that the supply of loanable funds provided by Japanese investors to the United States will ____, and U.S. interest rates will ____.
A : increase; increase
B : increase; decrease
C : decrease; decrease
D : decrease; increase

Correct Answer : D

50 : Which of the following will probably NOT result in an increase in the business demand for loanable funds?
A : an increase in economic growth
B : a reduction in interest rates on business loans
C : a recession
D : None of these are correct.

Correct Answer : C

51 : If the aggregate demand for loanable funds increases without a corresponding ____ in aggregate supply, there

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will be a ____ of loanable funds.?
A : ?increase; surplus
B : ?increase; shortage
C : ?decrease; surplus
D : ?decrease; shortage

Correct Answer : B

52 : A ____ federal government deficit increases the quantity of loanable funds demanded at any prevailing interest rate, causing an ____ shift in the demand schedule.
A : higher; inward
B : higher; outward
C : lower; outward
D : None of these are correct.

Correct Answer : B

53 : Which of the following is NOT true regarding foreign interest rates?
A : The large flow of funds between countries causes interest rates in any given country to become more susceptible to interest rate movements in other countries.
B : If a foreign country is experiencing high inflation, its equilibrium interest rate is likely to be higher than the U.S. equilibrium interest rate.
C : An increase in a foreign countrys interest rates will likely decrease demand for U.S. loanable funds by businesses in that country.
D : All of these are true regarding foreign interest rates.

Correct Answer : C

54 : Which of the following is least likely to affect household demand for loanable funds?
A : a decrease in tax rates
B : an increase in interest rates
C : a reduction in available projects with an expected high rate of return
D : All of these are equally likely to affect household demand for loanable funds.

Correct Answer : C

55 : Which of the following statements is incorrect?
A : The Feds monetary policy is intended to influence U.S. economic conditions.
B : The Feds monetary policy affects the supply of loanable funds, which affects interest rates.
C : By influencing interest rates, the Fed is able to influence the amount of money that corporations and households are willing to borrow and spend.
D : All of these are true.

Correct Answer : D

56 : The ____ suggests that the market interest rate is determined by factors that control the supply of and demand for loanable funds.
A : Fisher effect
B : loanable funds theory
C : real interest rate
D : None of these are correct.

Correct Answer : B

57 : When forecasting future interest rates, if the net demand for funds (ND) becomes _____, there will be ______ adjustment in interest rates.
A : negative; an upward
B : negative; no
C : positive; an upward
D : positive; a downward

Correct Answer : C

58 : Other things being equal, a ____ quantity of U.S. funds would be demanded by foreign governments and corporations if their domestic interest rates were ____ relative to U.S. rates.
A : smaller; high
B : larger; high
C : larger; low
D : None of these are correct.

Correct Answer : B

59 : The federal government's demand for funds is said to be interest-inelastic, or ____ to interest rates.
A : sensitive
B : insensitive
C : relatively sensitive as compared to other sectors
D : None of these are correct.

Correct Answer : B

60 : The required rate of return to implement a proposed project will be ______ if interest rates are _________.
A : lower; higher
B : lower; lower
C : higher; lower
D : higher; unchanged

Correct Answer : B

61 : The expected impact of an increased expansion by businesses is an ____ shift in the demand schedule and ____ in the supply schedule.?
A : ?inward; an inward shift
B : ?inward; an outward shift
C : ?outward; an inward shift
D : ?outward; no obvious change

Correct Answer : D

62 : Which of the following is a valid representation of the Fisher effect?
A : $i = E(\text{INF}) + i_R$
B : $i_R = E(\text{INF}) + i$
C : $E(\text{INF}) = i + i_R$
D : None of these are correct.

Correct Answer : A

63 : The real interest rate can be forecasted by subtracting the ___ from the ____ for that period.?

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A : ?nominal interest rate; expected inflation rate
B : ?prime rate; nominal interest rate
C : ?expected inflation rate; nominal interest rate
D : ?prime rate; expected inflation rate

Correct Answer : C

64 : According to the Fisher effect, expectations of higher inflation cause savers to require a ____ on savings.?
A : ?higher nominal interest rate
B : ?higher real interest rate
C : ?lower nominal interest rate
D : ?lower real interest rate

Correct Answer : A

65 : The federal government’s demand for funds is _________, and municipal governments’ demand for funds is _____________.
A : interest-inelastic; very interest-inelastic
B : interest-elastic; interest-elastic
C : interest-inelastic; somewhat interest-elastic
D : interest-elastic; somewhat interest-inelastic

Correct Answer : C

66 : Assume that a credit crisis causes a weak economy, and the Fed increases money supply. These conditions should cause
A : an increase in both the supply of and the demand for loanable funds.
B : a decrease in both the supply of and the demand for loanable funds.
C : a decrease in the supply of loanable funds and an increase in the demand for loanable funds.
D : an increase in the supply of loanable funds and a decrease in the demand for loanable funds.

Correct Answer : D

67 : The crowding-out effect occurs when
A : foreign investors crowd out U.S. investors in the market for loanable funds.
B : the federal government’s demand for loanable funds due to a higher budget deficit crowds out the private demand in the market for loanable funds.
C : institutional investors crowd out individual investors in the market for loanable funds.
D : firms and municipal governments crowd out households in the market for loanable funds.

Correct Answer : B