# *Test Bank for Money Banking and Financial Institutions v1 1st Edition by Carbaugh*

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Chapter 1: Introduction to Money, Banking, and Financial Markets

MULTIPLE CHOICE

1. In the financial system,
   a. business firms sell their goods in return for cash payments of buyers.
   b. the government makes expenditures and transfer payments.
   c. bank reserves are placed into circulation for households and businesses.
   d. funds are transferred to borrowers from savers.
   e. funds are transferred to savers from borrowers.

   ANS: D DIF: Moderate

2. Money is important for the economy since it affects:
   a. the business cycle
   b. the rate of interest
   c. the inflation rate
   d. the level of spending
   e! All of the above are true.

   ANS: E DIF: Easy

3. The monetary policy of the United States is carried out by the:
   a. Office of the Comptroller of the Currency
   b. Federal Deposit Insurance Corporation
   c. Federal Reserve System
   d. Securities and Exchange Commission
   e. Bureau of the Mint

   ANS: C DIF: Easy

4. For a money and banking course, budget deficits of the federal government are important to consider because
   a. depository institutions will become insolvent without budget deficits.
   b. without budget deficits, the nominal interest rate will hover around zero percent.
   c. budget deficits may affect interest rates and the behavior of monetary policy.
   d. budget deficits determine the size of a country's capital stock and economic activity.
   e. budget deficits imply that government taxes exceed government expenditures.

   ANS: C DIF: Moderate

5. If a country's money supply continually rises at a faster rate than the country can increase its production of goods and services,
   a. the rate of inflation will increase.
   b. the rate of deflation will accelerate.

c. market rates of interest will decline.
d. the standard of living will increase.
e. a balance of trade surplus will occur.

ANS: A DIF: Moderate

6. Which of the following is an example of when financial intermediation would occur?
   a. Kristy Evens makes a loan to Bill Miller for $10,000.
   b. General Motors Corporation issues common stock that is sold to people in Michigan.
   c. Microsoft Corporation borrows money by issuing a bond that is sold to a college student.
   d. Helen Miller deposits $1,000 in a bank, and the bank makes a loan to a business.
   e. Joe Smith places his wages under his pillow.

   ANS: D DIF: Hard

7. A continuing expansion of the money supply is most likely to be followed by:
   a. declining short-term and long-term interest rates
   b. an economic slump, or downturn
   c. a higher rate of inflation
   d. a decrease in industrial production and employment
   e. the bankruptcy of the federal government

   ANS: C DIF: Moderate

8. If you buy shares of Apple Corporation stock, then
   a. you have become a debtor to Apple.
   b. you have made a loan to Apple.
   c. you have become a part owner of Apple.
   d. you have provided new and temporary funds to Apple.
   e. your federal income taxes will decline.

   ANS: C DIF: Easy

9. The central bank of the United States is:
   a. the International Monetary Fund
   b. the Bank for Reconstruction and Settlements
   c. the U.S. Treasury
   d. the Federal Reserve System
   e. the Bureau of the Mint

   ANS: D DIF: Easy

10. Following World War I, the economy of Germany
    a. rebounded, and it realized substantial increases in economic activity.
    b. witnessed sharply declining interest rates that triggered speculative borrowing.

c. was destabilized by intensifying deflation.
d. was ruined due to hyperinflation.
e. encountered full employment for the first time in twenty-two years.

ANS: D DIF: Easy

11. Low growth rates in the money supply are likely to be linked to
    a. low market interest rates and low levels of inflation.
    b. low market interest rates and high levels of inflation.
    c. high market interest rates and low levels of inflation.
    d. high market interest rates and high levels of inflation.
    e. high levels of employment and falling industrial production.

ANS: A DIF: Easy

12. A rising rate of interest might cause businesses to _____, but households to ______.
    a. borrow less; save less
    b. borrow less; save more
    c. borrow more; save less
    d. borrow more; save more
    e. borrow the same amount; spend more on consumption

ANS: B DIF: Easy

13. Higher budget deficits of the federal government might be troublesome since they may
    a. lead to deflation which reduces the purchasing power of money.
    b. cause market interest rates to rise which causes business investment spending to fall.
    c. cause the dollar's exchange value to rise, then fall.
    d. may lead to a lower growth rate in the money supply which triggers recession.
    e. may encourage households to consume more and save less.

ANS: B DIF: Hard

14. A substantial contraction in the growth rate of the money supply may be followed by
    a. persistent inflation that reduces the purchasing power of fixed money incomes.
    b. a business-cycle expansion in which economic activity rises and unemployment falls.
    c. higher market rates of interest that induce increases in interest-sensitive spending.
    d. a decrease in economic activity and an increase in unemployment.
    e. tariffs being placed on imports of goods and services.

ANS: D DIF: Moderate

15. Due to expectations that the American economy will fall into a prolonged slump, suppose corporate stock prices decline 45 percent on average. Therefore, consumer spending would likely
    a. initially increase by a substantial amount, then a small amount.

b. initially increase by a moderate amount, then a substantial amount.
c. initially increase by a small amount, then a moderate amount.
d. decrease.
e. not be impacted

ANS: D DIF: Hard

16. The U.S. financial system provides all of the following services except:
    a. the provision of liquidity to households and businesses
    b. the curtailment of the federal government's debt
    c. a decrease in information costs for savers and investors
    d. a sharing of risk for savers and investors
    e. the granting of loans to individuals and businesses

    ANS: B DIF: Easy

17. If the exchange value of the U.S. dollar rises against the British pound,
    a. American goods exported to Britain become more expensive.
    b. American goods exported to Britain become cheaper.
    c. American goods imported from Britain become more expensive.
    d. British goods sold in Britain become cheaper.
    e. American goods sold in the United States become more expensive.

    ANS: A DIF: Moderate

18. The Federal Reserve System
    a. provides deposit insurance for people having checking accounts in banks.
    b. provides deposit insurance for people having savings account in banks.
    c. owns and operates the largest commercial banks of the United States.
    d. conducts the monetary policy of the United States.
    e. produces all coins used by the American public.

    ANS: D DIF: Moderate

19. A diagram illustrating the rate of inflation and the money supply growth rate for a cross-section of countries would likely suggest that
    a. countries with high money growth will likely have higher inflation.
    b. countries with high money growth will likely have lower inflation.
    c. countries with low money growth will likely have higher deflation.
    d. countries with low money growth will likely have higher consumption.
    e. there is no relationship between money growth rates and inflation/deflation rates across countries.

    ANS: A DIF: Moderate

20. The monetary policy of the Federal Reserve refers to

a. adjusting government expenditures to stabilize the economy.
b. changing tax rates to alter business and consumer spending.
c. changing interest rates to affect the availability of bank credit.
d. adjusting transfer payments to stabilize incomes of the needy
e. changing the exchange rate to encourage exports.

ANS: C DIF: Easy

21. Inflation tends to be the result of:
    a. a rapid increase in the money supply
    b. demands for lower wages by labor unions
    c. demand shocks that reduce the amount of consumer spending
    d. supply shocks that cause technological gains for the economy
    e. a sizable reduction in the demand for money

ANS: A DIF: Easy

22. Common stock that is issued by Microsoft Corporation
    a. allows the investor in stock to have a guaranteed rate of return.
    b. signifies an IOU on the part of Microsoft.
    c. permits the investor in stock to share in the earnings of Microsoft.
    d. allows the investor in stock to participate in the day-to-day operations of Microsoft.
    e. allows the investor in stock to receive a reduction in federal taxes.

ANS: C DIF: Easy

23. A continuing decrease in the growth of the money supply tends to
    a. promote deflation for the economy.
    b. reduce economic activity and the rate of inflation.
    c. increase the economy's output and rate of unemployment.
    d. increase the inflation rate and reduce the rate of unemployment.
    e. promote an inequitable distribution of income in the country.

ANS: B DIF: Moderate

24. Which of the following is <u>not</u> a financial intermediary?
    a. Yakima Federal Savings and Loan Association
    b. Boeing Credit Union
    c. Mutual Savings Bank of Pittsburgh
    d. Minneapolis Investment Advisors Inc.
    e. U.S. Bank

ANS: D DIF: Moderate

25. If the Federal Reserve decreases the growth rate of bank reserves and the money supply,
    a. the level of economic activity will likely increase.

b. the rate of inflation will likely decline.
c. the rate of unemployment will likely fall.
d. the growth in gross domestic product will remain unchanged.
e. the net exports of the United States will decrease.

ANS: B DIF: Moderate

26. Which statement is true for financial intermediaries?
a. They establish interest rates and bond prices for the economy.
b. All of their deposits are insured by the Federal Deposit Insurance Corporation.
c. All of their deposits are insured by the National Credit Union Administration.
d. They borrow from individuals who are savers and lend to household and business borrowers.
e. They include only commercial banks and savings and loan associations.

ANS: D DIF: Moderate

27. In terms of assets, which is the largest financial intermediary in the United States?
a. mutual savings banks
b. commercial banks
c. federally chartered credit unions
d. state chartered credit unions
e. savings and loan associations

ANS: B DIF: Easy

28. The process of offering shares of a private corporation to the public in a new stock issuance is carried out
a. in the NASDAQ.
b. in the New York Stock Exchange.
c. in an initial public offering.
d. in a mutual fund.
e. in the secondary market.

ANS: C DIF: Moderate

29. The Dow Jones Industrial Average is a stock market index that includes
a. the top thirty commercial banks in the United States.
b. the top thirty mutual fund companies in the United States.
c. the top thirty producers of industrial products such as steel and chemicals.
d. thirty prominent companies listed on stock exchanges in the United States.
e. thirty prominent credit unions in the United States.

ANS: D DIF: Moderate

30. Bonds are issued by ______ to finance projects and operations.

a. corporations
b. city governments
c. state governments
d. the federal government
e! All of the above are true.

ANS: E DIF: Easy

31. ______ is a digital currency designed to operate as a medium of exchange through a computer network that is not reliant on any central authority.
a. Foreign exchange
b. Cryptocurrency
c. The Federal Reserve Note
d. The Euro
e. The renminbi

ANS: B DIF: Easy

32. Which of the following is not a stock corporation whose main objective is to make a profit for its shareholders?
a. Wells Fargo Bank
b. Yakima Federal Savings and Loan Association
c. Boeing Credit Union
d. Ford Motor Company
e. Bank of America

ANS: C DIF: Moderate

33. Thrift institutions include all of the following except:
a. Yakima Federal Savings and Loan Association
b. Bank of America
c. Mutual Savings Bank of Ohio
d. Boeing Credit Union
e. Navy Federal Credit Union
ANS: B DIF: Moderate

34. Under the "dual banking system" of the United States,
a. banks have the purpose of accepting deposits and making loans.
b. banks make loans to households as well as to businesses.
c. state-chartered banks exist along with federally-chartered banks.
d. commercial banks exist along with investment banks.
e. banks have the purpose of issuing checking accounts and savings accounts.

ANS: C DIF: Easy

35. The Federal Deposit Insurance Corporation does not insure the deposits of:

a. Navy Federal Credit Union
b. Mutual Savings Bank of Iowa
c. Washington Federal Savings and Loan Association
d. U.S. Bank
e. JPMorgan Chase

ANS: A DIF: Moderate

36. The Federal Deposit Insurance Corporation (FDIC) insures the deposits of banks up to a maximum of ______ per account holder.
a! $75,000
b! $200,000
c! $250,000
d! $300,000
e! $350,000

ANS: C DIF: Easy

37. Which federal agency charters, regulates, and supervises all national banks and federal savings associations as well as federal branches and agencies of foreign banks?
a. the U.S. Treasury
b. the Federal Reserve
c. the Office of the Comptroller of the Currency
d. the Securities and Exchange Commission
e. the U.S. Bureau of the Mint

ANS: C DIF: Moderate

38. Commercial banks earn money in all of the following ways except
a. they earn interest on loans made to individuals and businesses.
b. they earn interest on the securities issued by the federal government.
c. they earn interest on the securities issued by municipal governments.
d. they earn fees for customer services such as safe deposit boxes and credit cards.
e. they earn commissions on sales of newly issued corporate stock to domestic investors

ANS: E DIF: Moderate

39. Created in 1934, the ______ protects investors, maintains fair, orderly, and efficient securities markets, and facilitates capital formation.
a. U.S. Treasury
b. Federal Reserve
c. Office of the Comptroller of the Currency
d. Bureau of the Mint
e. Securities and Exchange Commission

ANS: E DIF: Easy

40. Commercial banks include:
   a. JPMorgan Chase
   b. Bank of America
   c. Wells Fargo Bank
   d. Citigroup
   e! All of the above are true.

   ANS: E DIF: Moderate

41. An example of a digital currency is:
   a. Bitcoin
   b. the euro
   c. blockchain
   d. fiat currency
   e. credit currency

   ANS: A DIF: Easy

42. The Dow Jones Industrial Average is a stock market index of _____ blue-chip companies listed on stock exchanges in the United States.
   a! 10
   b! 20
   c! 30
   d! 40
   e! 50

   ANS: C DIF: Easy

43. Which institution supervises, regulates, and provides deposit insurance for credit unions?
   a. the Office of Thrift Supervision
   b. the Office of the Comptroller of the Currency
   c. the Bureau of the Mint
   d. the Federal Reserve System
   e. the National Credit Union Administration

   ANS: E DIF: Easy

44. Thrift institutions include all of the following except:
   a. mutual funds
   b. savings and loan associations
   c. federally-chartered credit unions
   d. state-chartered credit unions
   e. mutual savings banks

   ANS: A DIF: Easy

45. The dual mandate of the Federal Reserve means that the Federal Reserve is responsible for promoting
    a. stable exchange rates and a sound money supply.
    b. high interest rates and strong investment spending.
    c. maximum employment and stable prices.
    d. an equitable distribution of income and low inflation.
    e. zero unemployment and modest inflation.

ANS: C DIF: Moderate

46. Following World War I, the economy of Germany was greatly destabilized by:
    a. deflation
    b. hyperdeflation
    c. inflation
    d. hyperinflation
    e. zero inflation

ANS: D DIF: Moderate

47. Following World War I, the economy of _____ was greatly stabilized by hyperinflation.
    a. the United States
    b. Canada
    c. Australia
    d. New Zealand
    e. Germany

ANS: E DIF: Moderate

48. All of the following apply to deflation except
    a. it is a general decline in the prices of goods and services.
    b. it is associated with a decrease in aggregate demand in the economy.
    c. it results in a decline in the purchasing power of money.
    d. it harms borrowers who must repay debts in money worth more than the money they initially borrowed.
    e. helps creditors who receive payment in money that has more value than the money that was initially lent.

ANS: C DIF: Hard

49. Brian Moynihan worked his way up in the banking industry to become the chief executive officer of:
    a. Bank of America
    b. JPMorgan Chase
    c. Wells Fargo Bank
    d. U.S. Bank
    e. Citigroup

ANS: A DIF: Easy

50. All of the following regulators employ bank examiners except:
    a. the Federal Reserve System
    b. state banking commissions
    c. the Office of the Comptroller of the Currency
    d. the Federal Deposit Insurance Corporation
    e. the Securities and Exchange Commission

ANS: A DIF: Moderate

TRUE/FALSE

51. The National Credit Union Administration insures the share draft accounts (deposits) of credit union members up to a maximum of $250,000 per account holder in all federal credit unions and the overwhelming majority of state-chartered credit unions.

ANS: T DIF: Moderate

52. The U.S. Securities and Exchange Commission is the primary regulator of depository institutions, securities brokers and dealers, investment advisors, and mutual funds.

ANS: F DIF: Hard

53. During the early 2000s, the government of oil rich Venezuela took advantage of an oil boom to borrow, and its spending soared as well as its budget deficit. The government responded to this situation by printing more money. The result was hyperinflation.

ANS: T DIF: Moderate

54. Following World War I, the German economy quickly recovered in the 1920s, which allowed the country to regain stability and become a prominent member of the European community of nations.

ANS: F DIF: Moderate

55. Founded in 1913, the Federal Reserve System is currently owned and operated by the U.S. government to serve the public interest of the American economy.

ANS: F DIF: Moderate

56. The Federal Deposit Insurance Corporation insures the deposits of banks up to a limit of $125,000 per account holder.

ANS: F DIF: Easy

57. Deflation can hurt borrowers, who must pay their debts in money that is worth more than the money they borrowed.

ANS: T DIF: Moderate

58. Episodes of hyperinflation are generally accompanied by a rapidly increasing money supply needed to finance large fiscal deficits arising from war, revolution, the end of empires, and the establishment of new states.

ANS: T DIF: Moderate

59. The "dual mandate" of the Federal Reserve System is to achieve low short-term and long-term interest rates for the American economy.

ANS: F DIF: Moderate

60. The Office of the Comptroller of the Currency strives to ensure that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations.

ANS: T DIF: Hard

61. The dual banking system of the United States implies that state-chartered banks and federally-chartered banks accept deposits and make loans to households and businesses.

ANS: T DIF: Hard

62. Membership in the Federal Reserve System is required for national banks and is optional for state-chartered banks.

ANS: T DIF: Moderate

63. New York City is the headquarters of the global foreign exchange market.

ANS: F DIF: Moderate

64. At the New York Stock Exchange, newly issued stocks are sold for the first time.

ANS: F DIF: Easy

65. In the foreign exchange market, participants can buy, sell, hedge, and speculate on the exchange rates between currency pairs, such as the U.S. dollar and the euro.

ANS: T DIF: Moderate

66. Financial markets refer to any marketplace where the trading of securities occurs, including the stock market, bond market, foreign exchange market, and derivatives market.

ANS: T DIF: Moderate

67. The Nasdaq is a stock exchange that is located in New York City, and it has a centralized trading floor where traders gather to buy and sell securities in face-to-face negotiations.

ANS: F DIF: Difficult

68. As the economy changes over time, so does the composition of the Dow Jones Industrial Average. A component of the Dow may be dropped when a company becomes less relevant to current trends of the economy, to be replaced by a new name that better reflects the shift.

ANS: T DIF: Moderate

69. The foreign exchange market is essentially an over-the-counter-market, because trading is done directly between two parties without the supervision of a central exchange.

ANS: T DIF: Moderate

70. The growth of cryptocurrencies like Bitcoin has replaced the U.S. dollar as the world's key currency.

ANS: F DIF: Moderate

ESSAY

71. Explain the meaning of a financial market.

ANS: A financial market refers to any marketplace where the trading of securities occurs, including the stock market, bond market, foreign exchange market, and derivatives market. Financial markets are vital to the smooth operation of capitalist economies by allocating resources and creating liquidity for businesses and entrepreneurs. Financial markets create securities products that provide a return for those who have excess funds (investors/lenders) and make these funds available to those who need additional money (borrowers).

DIF: Moderate

72. What is meant by a depository institution?

ANS: A depository institution is a financial institution that obtains funds mainly through deposits of individuals and businesses. Depository institutions pay interest on that money while it is held in the institution. Commercial banks, savings and loan associations, mutual savings banks, and credit unions are examples of depository institutions.

DIF: Moderate

73. Summarize the nature of a commercial bank.

ANS: A commercial bank is a privately-owned institution that accepts deposits and make loans. It is generally a stock corporation whose main objective is to make a profit for its shareholders. A commercial bank receives checking accounts and savings accounts of its customers, and it extends credit to borrowers through loans such as short-term business loans, consumer loans, and mortgages.

DIF: Moderate

74. Describe a savings and loan association.

ANS: Operating as a thrift institution, savings and loan associations originated as part of philanthropic efforts to encourage saving among people of modest means. Although they originally offered only savings accounts and consumer loans, they now offer a wider range of financial services such as checking accounts, business loans, and mortgages. They can be owned by shareholders (stock ownership) or by their depositors and borrowers (mutual ownership).

DIF: Moderate

75. Identify the main characteristics of a credit union.

ANS: A credit union is cooperative financial institution that is established by a group of people with a common bond, such as working for the same employer. The group of people combine their funds to form the credit union's deposit base; the members of the credit union own and control the institution together. As a nonprofit institution, a credit union does not pay federal income taxes, and it strives to encourage savings and make excess funds within a community available at low cost to their members.

DIF: Moderate

76. Describe the dual banking system of the United States.

ANS: Under a dual banking system, both the fifty state governments and the federal government issue bank charters for the need and convenience of their citizens. The federal government (Office of the Comptroller of the Currency) charters national banks, and state banking departments charter state banks. Chartering agencies strive to ensure that new banks have sufficient capital and managerial expertise to safely operate.

DIF: Moderate

77. What is the dual mandate of the Federal Reserve System?

ANS: The U.S. Congress has explicitly stated that the Federal Reserve's goals should be maximum employment and stable prices. These goals have come to be known as the Federal Reserve's dual mandate. To achieve these goals, the Federal Reserve conducts monetary policy, the management of money and interest rates, and these variables are linked to changes in aggregate output, employment, and inflation.

DIF: Moderate

78. Describe the nature of hyperinflation.

ANS: Hyperinflation is a rapid and uncontrolled inflation in which prices rise by 50 percent or more per month. Episodes of hyperinflation are generally accompanied by a rapidly increasing money supply needed to finance large fiscal deficits arising from war, revolution, the end of empires, and the establishment of new states. Hyperinflation leads to sharp reductions in the purchasing power of money.

DIF: Moderate