1. In the United States saving is allocated to its most productive use by:
A. the Federal Reserve.
B. the Federal, state, and local governments.
C. regulations and laws designed to improve productivity.
D. a decentralized, market-oriented financial system.

2. Two reasons savers keep deposits at banks are to:
A. secure mortgages and to purchase stocks.
B. earn a return on their savings and to facilitate making payments.
C. lower interest rates and to increase the money supply.
D. equalize loan supply and demand and to earn interest.

3. Sydney purchases a newly-issued, two-year government bond with a principal amount of $10,000 and a coupon rate of 6% paid annually. One year before the bonds matures (and after receiving the coupon payment for the first year), Sydney sells the bond in the bond market. What price (rounded to the nearest dollar) will Sydney receive for his bond if the prevailing interest rate is 5%?
A. $9,524
B. $10,000
C. $10,095
D. $10,600

Selling a bond that will give $10,600

Price(1.05) = 10,600

Price = 10095

4. When Federal Reserve actions cause interest rates on newly issued bonds to decrease from 6% to 5%, the prices of existing bonds:
A. increase.
B. decrease.
C. remain unchanged.
D. decrease only if the coupon rate is less than 5%.

5. The current price of a stock increases when:
A. expected future dividends decrease.
B. the expected future price of the stock decreases.
C. interest rates decrease.
D. the perceived riskiness of the stock increases.

6. You expect a share of EconNews.Com to sell for $65 a year from now and to pay a $2 dividend per share in one year. What should you pay (rounded to the nearest dollar) for the stock today if you require an 8% return?
A. $60
B. $62
C. $67
D. $70

Price $(1.08) = 67$

7. Based on the following information, the value of the M1 measure of the money supply is _____ and the value of the M2 measure of the money supply is _____.

$M1 = 20 + 300 + 10 + 200 = 530$

Assets	Billions of Dollars
Currency	20
Demand deposits	300
Money market mutual funds	800
Travelers' checks	10
Savings deposits	1,800
Other checkable deposits	200
Small denomination time deposits	1,100

A. $530 billion; $3,700 billion
B. $330 billion; $4,230 billion
C. $520 billion; $4,320 billion
D. $530 billion; $4,230 billion

8. The amount of money in the United States is determined by:
A. the Federal Reserve.
B. the combined behavior of commercial banks and the public, and actions of the Federal Reserve.
C. the public
D. the combined behavior of commercial banks and the public.

9. If the desired reserve/deposit ratio equals .10, then every dollar of currency in bank vaults supports _____ of the money supply, while every dollar of currency held by the public contributes _____ to the money supply.
A. $1; $1
B. $0.10; $1
C. $1; $0.10
D. $10; $1

10. In Macroland there is $10,000,000 in currency. The public holds half of the currency and banks hold the rest as reserves. If banks' desired reserve/deposit ratio is 10%, deposits in Macroland equal _____ and the money supply equals _____.
A. 50,000,000; 60,000,000
B. 55,000,000; 55,000,000
C. 50,000,000; 55,000,000
D. 100,000,000; 100,000,000

$$Deposits = \frac{5,000,000}{0.1} = 50\,000\,000$$

$$MS = Deposits + 5,000,000$$

11. In Macroland there is $1,000,000 in currency that can either be held by the public or used by banks as reserves. Banks' desired reserve/deposit ratio is 10%. If the public of Macroland decides to hold more currency, increasing the proportion they hold from 50% to 75%, the money supply in Macroland will _____.
A. increase.
B. decrease.
C. remain the same.
D. either increase or decrease.

12. The money supply in Macroland is currently 2,500, bank reserves are 200, currency held by public is 500, and banks' desired reserve/deposit ratio is 0.10. Assuming the values of the currency held by the public and the desired reserve/deposit ratio do not change, if the Central Bank of Macroland wishes to increase the money supply to 3,000, then it should conduct an open-market _____ government bonds to/from the public.
A. purchase of 50
B. purchase of 250
C. purchase of 500
D. sale of 50

$$BD = \frac{200}{0.1} \qquad MS = 2000 + 500$$

Purchase 50, then $BD = \frac{250}{0.1}$ $MS = 3000$

13. If the money supply grows by 5 percent per year, velocity grows by 1 percent per year, and real GDP grows by 3 percent per year, then the rate of inflation is approximately _____ percent per year.
A. 1
B. 3
C. 5
D. 7

$$V = \frac{Y \times P}{M} \qquad V = (\Delta Y + \Delta P) - \Delta M$$

$$1 = 3 + P - 5$$

$$P = 3$$

14. Velocity is determined by:
A. the Federal Reserve.
B. the size of the government budget deficit.
C. average labor productivity times the population growth rate.
D. payments methods and technology.

15. If a bank's desired reserve/deposit ratio is .33 and it has deposit liabilities of $100 million and reserves of $50 million, it:
A. has too few reserves and will reduce its lending.
B. has too many reserves and will increase its lending.
C. has the correct amount of reserves and outstanding loans.
D. should increase the amount of its reserves.