Name	TestBanks Chapter 1 Multiple-Choice Questions
Description	Question pool for TestBanks Chapter 1 Multiple-Choice Questions
Instructions	

Add Question Here

Question 1 **Multiple Choice** **0 points**

Question
Financial markets contain people and firms that buy and sell two kinds of assets: ________ and ________.

Answer
- travelers checks; insurance policies
- ✓ currency; securities
- dollars; euros
- bonds; stocks

Add Question Here

Question 2 **Multiple Choice** **0 points**

Question
Financial markets are made up of people and firms that ________ assets.

Answer
- buy
- sell
- print
- ✓ buy and sell

Add Question Here

Question 3 **Multiple Choice** **0 points**

Question
A security is a claim on ________ of income.

Answer
- ✓ future flows
- the current amount
- the past flow
- the profits

Add Question Here

Question 4 **Multiple Choice** **0 points**

Question
Which of the following best defines a security?

Answer
- It is a claim on the past flow of income.
- It is a claim on the depreciation of income.
- It is a fixed payment.
- ✓ It is a claim on the future flow of income.

Add Question Here

Question 5 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A bond is an example of a:

Answer
- ✓ fixed income security.
- constant asset.
- flexible income security.
- security with an unknown payment.

Add Question Here

Question 6 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A bond pays its ________ at the time of ________.

Answer
- present value; purchase
- future value; purchase
- ✓ face value; maturity
- present value; maturity

Add Question Here

Question 7 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Consider a bond you buy for $100 which pays you $6 a year for 10 years, and then pays back the $100. The face value of the bond is ________, the ________ is $6, and the maturity is ________.

Answer
- $6; coupon payment; 10 years
- ✓ $100; coupon payment; 10 years
- $100; face value; 1 year
- $100; coupon payment; 1 year

Add Question Here

Question 8 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following institutions do *not* issue bonds?

Answer
- the Federal government
- corporations
- local governments
- ✓ None of the answers are correct.

Add Question Here

Question 9 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following institutions do *not* issue bonds?

Answer
- foreign governments
- corporations
- government agencies
- ✓ None of the answers are correct.

Add Question Here

Question 10 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Interest is best defined as:

Answer
- ✓ the payment for using funds.
- the amount of a loan.
- insurance against future disaster.
- the receipt of principle.

Add Question Here

Question 11 | **Multiple Choice** | **0 points** | Modify | Remove

Question
If a bond's face value plus all coupon payments exceeds the price a buyer pays, the bond pays:

Answer
- a discount rate.
- ✓ interest.
- a premium.
- the rate of inflation.

Add Question Here

Question 12 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A zero coupon bond pays:

Answer
- a stream of coupon payments only.
- its face value and coupon payments.
- ✓ only the face value.
- There is not enough information provided to answer the question.

Add Question Here

Question 13 | **Multiple Choice** | **0 points** | Modify | Remove

Question
To attract ________ of a zero coupon bond, the seller must ________ the bond at ________ its face value.

Answer
- ✓ buyers; sell; less than
- buyers; sell; greater than
- sellers; buy; less than
- sellers; buy; equal to

Add Question Here

Question 14 | **Multiple Choice** | **0 points** | Modify | Remove

Question
If the issuer of a bond does not pay its promised payments, the issuer:

Answer
✓ defaults.
goes bankrupt.
lacks revenues.
All of the answers are correct.

Add Question Here

Question 15 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following arranges risk from least to most risky (left to right)?

Answer
large corporations, government, small corporations
small corporations, large corporations, government
government, small corporations, large corporations
✓ government large corporations, small corporations

Add Question Here

Question 16 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A stock is:

Answer
a loan to a corporation.
a fixed-payment asset.
✓ an ownership share in a corporation.
an ownership share in a government.

Add Question Here

Question 17 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A stock entitles you to:

Answer
✓ a percentage of a firm's total profits.
one dollar for each of a firm's share you own.
a fixed payment forever.
a fixed face-value payment at the time of maturity.

Add Question Here

Question 18 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A stock entitles you to:

Answer
- charge interest to a corporation.
- a fixed payment forever.
- ✓ a percentage of a firm's total profits.
- None of the answers are correct.

Add Question Here

Question 19	Multiple Choice	0 points	Modify Remove

Question
Corporations issue stocks to:

Answer
- write off taxes on profits.
- ✓ raise funds for investment.
- enrich the owners of the corporation.
- engage in trading activities.

Add Question Here

Question 20	Multiple Choice	0 points	Modify Remove

Question
When governments don't have enough funds to make bond payments, they:

Answer
- ✓ default.
- declare bankruptcy.
- call an election.
- buy back the bonds.

Add Question Here

Question 21	Multiple Choice	0 points	Modify Remove

Question
Default risk is ____ for new corporations because they may stop making ___ payments.

Answer
- lower; dividend
- lower; bond
- higher; dividend
- ✓ higher; bond

Add Question Here

Question 22	Multiple Choice	0 points	Modify Remove

Question
A well-functioning financial market:

Answer
- transfers funds from investors to savers.
- decreases the economy's productivity.
- ✓ allows firms to fund investment projects.
- ensures that speculators always make money.

Add Question Here

Question 23 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A _____ is a security that promises to pay the buyer predetermined amounts of money at certain times in the future.

Answer
- ✓ bond
- share of common stock
- dividend
- share of preferred stock

Add Question Here

Question 24 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Suppose you pay $1000 for a bond that pays you $35 a year for five years and then pays you back $1000 at the end of the fifth year. Which of the following statements is true?

Answer
- The face value of this bond is $35.
- The bond's maturity is 10 years.
- ✓ The coupon payment is $35.
- This bond has a coupon rate of 10 percent.

Add Question Here

Question 25 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following statements about bonds is true?

Answer
- Commercial paper matures in more than five years.
- A zero-coupon bond always sells for more than its face value.
- ✓ A Treasury bill matures in less than a year.
- Commercial paper is considered long-term debt.

Add Question Here

Question 26 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The risk of default is _____ for bonds issued by the U.S. government and ____ for bonds issued by corporations losing money.

Answer
- small; about the same
- large; about the same
- ✓ small; larger
- large; smaller

Add Question Here

Question 27 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following statements about stock is true?

Answer
- Holding bonds is usually riskier than holding stock.
- If you own stock in a corporation, then you are a creditor of that corporation.
- ✓ The flow of income generated by stock is unpredictable.
- Stock prices are less volatile than bond prices.

Add Question Here

Question 28	Multiple Choice	0 points	Modify Remove

Question
Financial markets help transfer funds from the ________ to the ________.

Answer
- bankers; investors.
- depositors; bankers
- ✓ savers; investors
- investors; savers

Add Question Here

Question 29	Multiple Choice	0 points	Modify Remove

Question
Which of the following explain(s) the importance of financial markets?
I. They help channel funds from savers to investors with productive uses for the funds.
II. They help people and firms share risks.
III. They allow the rich to get richer.

Answer
- I only
- II only
- ✓ I and II
- I, II, and III

Add Question Here

Question 30	Multiple Choice	0 points	Modify Remove

Question
Which of the following definitions does the text use?

Answer
- ✓ Savers are people who spend less than they earn.
- Investors are people who make risky purchases of paper assets.
- Savers are people who spend more than they earn.
- Investors are people who purchase stocks and bonds.

Add Question Here

Question 31	Multiple Choice	0 points	Modify Remove

Question
Which of the following definitions does the text use?

Answer
- ✓ Savers are people who spend less than they earn.
- Investors are people who spend more than they earn.
- Investors are people who purchase stocks and bonds.
- Savers are people who put all their excess income in savings accounts.

Add Question Here

Question 32 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Diversification is defined as:

Answer
- spending less than is earned.
- ✓ the distribution of wealth among different assets.
- increasing the productive capacity of the economy.
- the general rising level of prices.

Add Question Here

Question 33 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Diversification allows ________ to earn healthy returns from securities while minimizing ________.

Answer
- ✓ savers; risk
- sellers; risk
- savers; inflation
- savers; unemployment

Add Question Here

Question 34 | **Multiple Choice** | **0 points** | Modify | Remove

Question
A mutual fund is an institution that:

Answer
- ✓ holds a diversified set of assets and sells shares to savers.
- holds a diversified set of assets and buys shares directly from the government.
- holds a single share and sells shares to savers.
- buys physical capital for investors.

Add Question Here

Question 35 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Employees of Enron got into trouble because:

Answer
- they could only buy Enron stock for retirement.

✓ the majority of the 401(k) fund they saved in was devoted to Enron stock.

their pension fund went bankrupt.

the majority of the 401(k) fund they saved in was devoted to Microsoft stock.

Add Question Here

Question 36 **Multiple Choice** **0 points** Modify Remove

Question
Firms which have a majority of their own stock in their employee 401(k) plans include:

Answer
General Electric.
Pfizer.
Procter & Gamble.
✓ All of the answers are correct.

Add Question Here

Question 37 **Multiple Choice** **0 points** Modify Remove

Question
Financial markets help channel ____ to ____ and help people share ____.

Answer
money; individuals; profits
profits; companies; risk
✓ savings; investors; risk
dividends; individuals; risk

Add Question Here

Question 38 **Multiple Choice** **0 points** Modify Remove

Question
Many American workers save for their retirement through a 401(k) plan with their employer. This plan is generally a good idea if the 401(k) plan is ____ because the plan will be ____ risky.

Answer
invested in company stock; less
invested in company stock; more
✓ diversified; less
diversified; more

Add Question Here

Question 39 **Multiple Choice** **0 points** Modify Remove

Question
Economic functions of financial markets include:

Answer
✓ matching savers and investors.
making sure no saver suffers a loss.
decreasing the overall efficiency of the economy.

making sure no investor suffers a loss.

Add Question Here

Question 40 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Suppose Jessica issues a bond to raise funds for her new company and that David buys some of these bonds. According to the textbook, Jessica is the ______.

Answer

- the saver and David is the investor
- ✓ the investor and David is the saver
- both the saver and the investor
- neither the saver nor the investor

Add Question Here

Question 41 | **Multiple Choice** | **0 points** | Modify | Remove

Question
According to the textbook, the old adage " Don't put all your eggs in one basket" relates to the concept of:

Answer

- ✓ diversification.
- concentration.
- risk maximization.
- risk standardization.

Add Question Here

Question 42 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Financial markets promote diversification by:

Answer

- ✓ allowing investors to issue stock or bonds and therefore avoid using only their own money to fund their projects.
- restricting savers' opportunities to choose from when deciding an asset to buy.
- preventing savers and borrowers from sharing in the risks associated with any investment.
- increasing the probability that an investor default will decrease savers' returns.

Add Question Here

Question 43 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Amy has bought stock in five different corporations, while Bob used all his savings to buy stock in only one company. According to this, Amy has a _______ diversified portfolio and therefore is facing ______ risk than Bob.

Answer

- more; more

less; more
✓ more; less
less; less

Add Question Here

Question 44 | **Multiple Choice** | **0 points** | Modify | Remove

Question
When financial markets collapse and stop matching savers with investors:

Answer
- there are no consequences for the performance of the economy.
- the economy benefits greatly from less speculation.
- ✓ the economy usually suffers: production decreases and unemployment increases.
- there are no consequences for the performance of the economy, and the economy benefits greatly from less speculation.

Add Question Here

Question 45 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Economists call the situation in which one side of an economic transaction has more information than the other:

Answer
- a negative externality.
- a fixed cost.
- a lack of diversification.
- ✓ asymmetric information.

Add Question Here

Question 46 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The problem of *adverse selection* arises when the owners of a security have a(n):

Answer
- incentive to misbehave after an asset purchase.
- incentive to behave according to expectations.
- ✓ incentive to give potential buyers bad information.
- disincentive to give potential buyers bad information.

Add Question Here

Question 47 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The problem of *moral hazard* arises when the owners of a security have:

Answer
- an incentive to give potential buyers bad information.

✓ little incentive to behave prudently after selling its asset.
a disincentive to give potential buyers bad information.
an incentive to behave according to expectations.

Add Question Here

Question 48 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Moral hazard and adverse selection are examples of:

Answer
irrational exuberance.
✓ asymmetric information.
adaptive expectations.
default risk.

Add Question Here

Question 49 | **Multiple Choice** | **0 points** | Modify | Remove

Question
One reason that investors may be unwilling to purchase securities is because:

Answer
investors believe that economic growth is going to slow down.
investors don't have enough information about the company.
the company does not share all of the information with investors.
✓ All of the answers are correct.

Add Question Here

Question 50 | **Multiple Choice** | **0 points** | Modify | Remove

Question
When the owner of a company does not act in the shareholders, best interest, the situation is known as:

Answer
✓ moral hazard.
adverse selection.
asymmetric information.
None of the answers is correct.

Add Question Here

Question 51 | **Multiple Choice** | **0 points** | Modify | Remove

Question
When one participant in an economic transaction has more information than the other participant, the situation is known as:

Answer
uncertain information.
✓ asymmetric information.
perfect information.

symmetric information.

Add Question Here

Question 52 | **Multiple Choice** | **0 points** | Modify | Remove

Question
According to the adverse selection problem, firms that are most eager to make a transaction are the ______ desirable to parties on the other side of the transaction. For example, a low-quality firm will be most eager to issue a security when its price is _______.

Answer
- most; low
- most; high
- ✓ least; low
- least; high

Add Question Here

Question 53 | **Multiple Choice** | **0 points** | Modify | Remove

Question
When adverse selection problems increase, it is likely that the quality (i.e., value, low default risk) of securities traded in the financial market will:

Answer
- ✓ decline.
- increase.
- remain about the same as if there were no adverse selection problems.
- decline, increase, or remain about the same.

Add Question Here

Question 54 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Suppose you want to buy a bond in the financial market, but you do not have enough information about bond issuers. The problem you are facing is usually known as:

Answer
- moral hazard.
- ✓ adverse selection.
- free rider.
- conflict of interest.

Add Question Here

Question 55 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The asymmetric information problem created before the transaction occurs is known as ______, while the asymmetric information problem that arises after the transaction is known as _____.

Answer
- moral hazard; adverse selection

the free-rider problem; adverse selection
adverse selection; the free-rider problem
✓ adverse selection; moral hazard

Add Question Here

Question 56	Multiple Choice	0 points	Modify Remove

Question
Suppose asymmetric information problems (i.e., adverse selection and moral hazard) decrease. As a result, the quantity of securities will ______ and the quality of these securities will _____.

Answer
increase; decrease
✓ increase; increase
decrease; decrease
decrease; increase

Add Question Here

Question 57	Multiple Choice	0 points	Modify Remove

Question
Which of the following best defines a financial institution?

Answer
an institution that only makes loans
a firm that prints money
✓ a firm that helps channel funds from savers to investors
a government agency that gives away funds to investors

Add Question Here

Question 58	Multiple Choice	0 points	Modify Remove

Question
A firm that helps channel funds from ________ to ________ is called a ________.

Answer
✓ savers; investors; financial institution
savers; investors; government agency
investors; savers; financial institution
the government; investors; bank

Add Question Here

Question 59	Multiple Choice	0 points	Modify Remove

Question
A bank:

Answer
prints money.
makes loans.
takes deposits and issues bonds.
✓ takes deposits and makes loans.

Add Question Here

Question 60 | **Multiple Choice** | **0 points** | Modify | Remove

Question
________ is defined as when savers deposit money in banks which then lend to investors, while ________ arises when savers provide funds to investors by buying securities in financial markets.

Answer
- Lending; borrowing
- ✓ Indirect finance; direct finance
- Borrowing; direct finance
- Direct finance; indirect finance

Add Question Here

Question 61 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Banks reduce ________ by screening ________.

Answer
- moral hazard; potential borrowers
- adverse selection; savers
- ✓ adverse selection; potential borrowers
- irrational exuberance; depositors

Add Question Here

Question 62 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The difference in interest rates between savings accounts and loans can be explained, in part, by the:

Answer
- cost of gathering information on potential borrowers—adverse selection.
- risk associated with making loans.
- cost of monitoring borrowers once the loan has been made—moral hazard.
- ✓ All of the answers are correct.

Add Question Here

Question 63 | **Multiple Choice** | **0 points** | Modify | Remove

Question
By requiring borrowers to sign a covenant when getting a loan, a bank is trying to minimize

Answer
- high unexpected inflation.
- ✓ moral hazard.
- adverse selection.
- irrational exuberance.

Add Question Here

Question 64 | **Multiple Choice** | **0 points** | Modify | Remove

Question
To minimize the problem of moral hazard when making a loan, a bank requires a borrower to:

Answer
- ✓ sign a covenant.
- use their car as collateral.
- put up 50 percent of their own funds as a downpayment.
- None of the answers are correct.

Add Question Here

Question 65 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Banks are the main source of funding for ________ , mainly because of ________ and ________.

Answer
- bond holders; risk; asymmetric information
- governments; adverse selection; uncertainty about the future
- ✓ small firms; adverse selection; moral hazard
- big firms; adverse selection; moral hazard

Add Question Here

Question 66 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The financial crisis of 2007–2009 was caused in part by:

Answer
- the failure of investors to purchase securities.
- investors not borrowing enough from the banks.
- ✓ the failure of banks to adequately screen borrowers before giving them loans.
- banks providing too much information to securities markets.

Add Question Here

Question 67 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Some companies are able to raise funds on the securities market rather than borrowing from a bank because:

Answer
- these companies are not very well known to the bank.
- ✓ these companies are well known to the public.
- the bank is restricted from lending to some companies.
- most banks only lend to inviduals, not to companies.

Add Question Here

Question 68 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Individuals from two different businesses apply for a loan at a bank. If the individual with the bad credit history obtains a loan rather than the individual with the good credit history, this is an example of:

Answer

- microfinance.
- direct finance.
- ✓ adverse selection.
- moral hazard.

Add Question Here

Question 69	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following can be considered a “ financial intermediary” ?

Answer

- ✓ a bank
- a stockbroker
- a securities dealer
- a member of the SEC

Add Question Here

Question 70	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following institutions accept deposits and make loans?

Answer

- investment banks
- ✓ commercial banks
- mutual funds
- pension funds

Add Question Here

Question 71	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following can be described as “ indirect finance” ?

Answer

- You buy 400 shares of IBM stock.
- You buy $5000 worth of ATT bonds.
- ✓ You deposit $1000 in your local bank.
- You lend $40 to your cousin.

Add Question Here

Question 72	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following can be considered as “ direct finance” ?

Answer

- Your friend gets a car loan from the local bank.
- ✓ You buy $3000 worth of Intel bonds.

You deposit $4000 in your savings account.
You take out a mortgage loan at a bank.

Add Question Here

Question 73 | **Multiple Choice** | **0 points** | Modify | Remove

Question
According to the textbook, the primary reason why banks exist is that:

Answer

- banks keep our money safe in their vaults.
- banks make sure our money does not lose its purchasing power.
- ✓ banks reduce asymmetric information problems.
- banks make bank managers rich.

Add Question Here

Question 74 | **Multiple Choice** | **0 points** | Modify | Remove

Question
When a bank officer asks questions about an individual's ability to repay a loan (e.g., the bank, credit history, current employment characteristics, net worth, etc.), the bank is trying to cope with the __________ problem.

Answer

- moral-hazard
- chronic-gossiper
- ✓ adverse-selection
- principal-agent

Add Question Here

Question 75 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The practice of including a covenant in a loan contract is a way of dealing with the _____ problem.

Answer

- ✓ moral-hazard
- chronic-borrower-gambler
- adverse-selection
- free-rider

Add Question Here

Question 76 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following can be defined as economic growth?
I. Growth in real GDP
II. Increases in productivity
III. Falling unemployment

Answer

- I only

II only
III only
✓ I and II

Add Question Here

Question 77 | **Multiple Choice** | **0 points** | Modify | Remove

Question
One explanation for high long-run economic growth rates is:

Answer
✓ high savings rates.
high consumption rates.
low productivity.
low rates of unemployment.

Add Question Here

Question 78 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Empirical evidence shows a positive correlation between ________ and ________.

Answer
inflation; financial development
inflation; economic growth
high rates of money growth; economic growth.
✓ financial development; economic growth

Add Question Here

Question 79 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Researchers found that countries with ________ in the 1960s had faster ________.

Answer
strong financial systems; economic growth during the 1960s
✓ strong financial systems; economic growth in the decades after the 1960s
weaker financial systems; inflation in the decades after the 1960s
strong financial systems; inflation before the 1960s

Add Question Here

Question 80 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The restriction that requires that banks operate in no more than one state is called:

Answer
asymmetric information.
✓ unit banking.
moral hazard.

a negative externality.

Add Question Here

Question 81	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following is/are arguments *against* unit banking?
I. Decreasing economies of scale
II. Decreased bank risk
III. Less competition

Answer

I only
II only
III only
✓ I and III

Add Question Here

Question 82	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following is/are arguments *against* unit banking?
I. Increasing economies of scale
II. Increased bank risk
III. More competition

Answer

I only
✓ II only
III only
I and II

Add Question Here

Question 83	**Multiple Choice**	**0 points**	Modify Remove

Question
Banks in developing economies are less willing to lend to small firms because:

Answer

✓ of higher loan default rates.
interest rates charged cover transaction costs.
of lower adverse selection.
of lower moral hazard.

Add Question Here

Question 84	**Multiple Choice**	**0 points**	Modify Remove

Question
Microfinance institutions get around the problem of moral hazard and high default rates by:

Answer

✓ lending to groups rather than individuals.
lending only to proven borrowers.
lending only to large businesses.

charging usurious interest rates.

Add Question Here

Question 85 | **Multiple Choice** | **0 points** | Modify | Remove

Question
An economy run by the government which completely decides what goods and services to produce, who receives them, and which investment projects to undertake, is called a:

Answer
✓ command economy.
market economy.
mixed economy.
socialist economy.

Add Question Here

Question 86 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Economic historians have pointed to which of the following to explain the demise of the Soviet Union?
I. Managers were evaluated based on profits rather than production quotas.
II. There was misallocation of investment, with " prestige" sectors chosen over less productive ones.
III. Planners emphasized the short run over the long run.

Answer
I only
II only
✓ III only
II and III

Add Question Here

Question 87 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The differences in the financial systems across countries help explain why some countries are richer than other countries, because:
I. richer countries tend to have stronger financial systems than poorer countries.
II. richer countries do not have a problem with asymmetric information in financial markets.
III. richer countries tend to have larger populations than poorer countries.

Answer
✓ I only
I and II
I and III
I, II, and III

Add Question Here

Question 88 | **Multiple Choice** | **0 points** | Modify

Remove

Question
Many microfinance institutions help the economies in developing countries grow by:
I. only lending to people who borrow as part of a group.
II. lending primarily to women.
III. requiring borrowers to operate as a not-for-profit business.

Answer
- I only
- ✓ II only
- III only
- I, II, and III

Add Question Here

Question 89 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Centrally planned economies often outperform market-based economies in the short run because:

Answer
- the government can identify the most productive investment projects.
- prices in market-based economies do not reflect consumer demand.
- ✓ the government controls the economy's resources and can require high levels of investment.
- government employees are very efficient.

Add Question Here

Question 90 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Many East Asian countries, such as Taiwan, Singapore, and South Korea, rapidly moved from the world's poorest countries to among the world's richest countries in three decades. The main reason for this progress was because:

Answer
- their governments directed resources to the best investment projects.
- banks in these countries were not allowed to engage in cross-border business.
- their governments did not create a strong financial system.
- ✓ these countries had high saving rates.

Add Question Here

Question 91 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following statements about the link between the savings rate and the financial system is true?

Answer
- A low savings rate and an underdeveloped financial

system will create economic growth.

✓ A high savings rate and a strong financial system can create economic growth.

A high savings rate and an underdeveloped financial system will create economic growth.

All of the answers are correct.

Add Question Here

Question 92	**Multiple Choice**	**0 points**	Modify Remove

Question
Which of the following statements about financial systems is true?

Answer

Forcing firms to provide information about their investment and expected profits results in an underdeveloped financial system.

✓ Financial systems of different countries have different regulations.

When financial systems cannot work properly, it is easy for investors to get funds.

All countries make sure that bank depositors have their deposits insured.

Add Question Here

Question 93	**Multiple Choice**	**0 points**	Modify Remove

Question
Recent research about the link between the financial system and economic growth suggests that:

Answer

✓ a strong financial system can spur economic growth.

the efficiency of the financial system is irrelevant for economic growth.

a weak financial system promotes economic growth.

there is no link at all between the financial system and economic growth.

Add Question Here

Question 94	**Multiple Choice**	**0 points**	Modify Remove

Question
According to the textbook, unit banking:

Answer

allowed banks to exploit economies of scale.

increased competition in the banking industry.

allowed banks to diversify their loans portfolio.

✓ None of the answers are correct.

Add Question Here

Question 95	**Multiple Choice**	**0 points**	Modify Remove

Question
According to the textbook, unit banking _______ competition in the banking industry and _______ banks to exploit economies of scale.

Answer
- increased; did not allow
- decreased; encouraged
- ✓ decreased; did not allow
- increased; encouraged

Add Question Here

Question 96 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following can be considered a consequence of unit banking?

Answer
- ✓ Banks usually operated as monopolists, charging high fees and providing poor service.
- Funds flowed more easily from savers to investors.
- The banking industry in the United States became more efficient.
- Unit banking promoted competition in the U.S. banking industry.

Add Question Here

Question 97 | **Multiple Choice** | **0 points** | Modify | Remove

Question
According to historical evidence, a centrally planned economy:

Answer
- efficiently allocates funds by deciding which investment project must be funded.
- ✓ shows that free financial markets are critical for the proper allocation of funds and economic growth.
- is a better alternative than free markets when considering how to allocate funds.
- always resulted in more efficient financial systems and higher economic growth than free market economies.

Add Question Here

Question 98 | **Multiple Choice** | **0 points** | Modify | Remove

Question
According to the textbook, the centrally planned economy of the Soviet Union:

Answer
- overinvested in heavy industry.
- underinvested in consumer goods.
- allowed a free financial market to allocate funds to their most productive use.
- ✓ overinvested in heavy industry and underinvested in consumer goods.

Add Question Here

Question 99 | **Multiple Choice** | **0 points** | Modify | Remove

Question
The United States experienced a financial crisis in 2007–2009 that pulled the country into an economic crisis when:

Answer
- large financial institutions failed.
- asset prices fell sharply.
- bank lending contracted.
- ✓ All of the answers are correct.

Add Question Here

Question 100 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Governments are able to stop or slow down a financial crisis by:

Answer
- imposing wage and price controls to prevent price increases.
- selling government bonds to reduce the money supply.
- ✓ making loans to families.
- purchasing financial securities.

Add Question Here

Question 101 | **Multiple Choice** | **0 points** | Modify | Remove

Question
Which of the following events is usually present during a financial crisis?

Answer
- an increase in stock prices
- ✓ a decrease in output
- a decrease in unemployment
- an increase in GDP

Add Question Here

Question 102 | **Multiple Choice** | **0 points** | Modify | Remove

Question
During the 2007–2009 financial crisis in the United States:

Answer
- the Fed pushed short-term rates to near zero.
- the unemployment rate rose to close to 4 percent.
- the Fed contracted the money supply aggressively.
- ✓ GDP increased at a 5 percent annual rate.

Add Question Here

Question 103 | **Multiple Choice** | **0 points** | Modify | Remove

Question

Inflation is defined as:

Answer

- the percentage change of the price of oil over a period of time.
- the difference in the aggregate price level over a period of time.
- ✓ the percentage increase in the aggregate price level over a period of time.
- today's aggregate price level divided by yesterday's price level.

Add Question Here

Question 104	**Multiple Choice**	**0 points**	Modify Remove

Question

Real GDP is defined as:

Answer

- ✓ nominal GDP divided by the aggregate price level.
- the total value of all goods and services produced in an economy in a given period at current prices.
- the aggregate price level divided by nominal GDP.
- the types of goods and services produced.

Add Question Here

Question 105	**Multiple Choice**	**0 points**	Modify Remove

Question

Which of the following is true?

Answer

- ✓ $$\text{real GDP} = \frac{\text{nominal GDP}}{\text{aggregate price level}}$$
- real GDP = nominal GDP × aggregate price level
- $$\text{nominal GDP} = \frac{\text{real GDP}}{\text{aggregate price level}}$$
- $$\text{aggregate price level} = \frac{\text{real GDP}}{\text{nominal GDP}}$$

Add Question Here

OK

Name	TestBanks Chapter 1 True-False Questions
Description	Question pool for TestBanks Chapter 1 True-False Questions
Instructions	Modify

Add Question Here

Question 1	**True/False**	**0 points**	Modify Remove

Question
All bonds have the same maturity.

Answer
True
✓ False

Add Question Here

Question 2 | **True/False** | **0 points** | Modify | Remove

Question
Corporations and governments issue bonds.

Answer
✓ True
False

Add Question Here

Question 3 | **True/False** | **0 points** | Modify | Remove

Question
A stockholder knows exactly how much income her share will earn.

Answer
True
✓ False

Add Question Here

Question 4 | **True/False** | **0 points** | Modify | Remove

Question
Stockholders have voting rights while bondholders do not.

Answer
✓ True
False

Add Question Here

Question 5 | **True/False** | **0 points** | Modify | Remove

Question
When a corporation or government issues bonds, it is lending money to those who buy the bonds.

Answer
True
✓ False

Add Question Here

Question 6 | **True/False** | **0 points** | Modify | Remove

Question
All bonds have the same default risk.

Answer
True
✓ False

Add Question Here

Question 7	**True/False**	**0 points**	Modify Remove

Question
In general, stocks produce higher returns than bonds.

Answer ✓ True
False

Add Question Here

Question 8	**True/False**	**0 points**	Modify Remove

Question
Financial markets are important because they help channel funds from savers to investors with productive uses for the funds.

Answer ✓ True
False

Add Question Here

Question 9	**True/False**	**0 points**	Modify Remove

Question
Financial markets transfer funds from savers to investors.

Answer ✓ True
False

Add Question Here

Question 10	**True/False**	**0 points**	Modify Remove

Question
Financial markets allow savers and investors to share risks by diversifying their portfolios.

Answer ✓ True
False

Add Question Here

Question 11	**True/False**	**0 points**	Modify Remove

Question
The fact that both savers and investors want to minimize risk also explains the existence of financial markets.

Answer ✓ True
False

Add Question Here

Question 12	**True/False**	**0 points**	Modify Remove

Question
The problem of *moral hazard* arises when the owners of a security have little incentive to behave prudently after selling its asset.

Answer

✓ True
False

Add Question Here

Question 13 | **True/False** | **0 points** | Modify | Remove

Question
The problem of *adverse selection* arises when the owners of a security have little incentive to behave prudently after selling its asset.

Answer

True
✓ False

Add Question Here

Question 14 | **True/False** | **0 points** | Modify | Remove

Question
Asymmetric information problems do not affect the performance of financial markets.

Answer

True
✓ False

Add Question Here

Question 15 | **True/False** | **0 points** | Modify | Remove

Question
The asymmetric information problem that arises after the transaction has been made is known as moral hazard.

Answer

✓ True
False

Add Question Here

Question 16 | **True/False** | **0 points** | Modify | Remove

Question
Because it is usually costly to check the amount of effort put forward by an investor, savers might be reluctant to buy securities.

Answer

✓ True
False

Add Question Here

Question 17 | **True/False** | **0 points** | Modify | Remove

Question
A bank's main role in the economy is to make loans.

Answer

True
✓ False

Add Question Here

Question 18 | **True/False** | **0 points** | Modify | Remove

Question
When economists say " bank" they are referring to investment banks.

Answer
True
✓ False

Add Question Here

Question 19 | **True/False** | **0 points** | Modify | Remove

Question
The situation in which savers deposit money in banks that then lend to investors is called indirect finance.

Answer
✓ True
False

Add Question Here

Question 20 | **True/False** | **0 points** | Modify | Remove

Question
The situation in which savers deposit money in banks that then lend to investors is called direct finance.

Answer
True
✓ False

Add Question Here

Question 21 | **True/False** | **0 points** | Modify | Remove

Question
If savers provide funds to investors by buying securities in financial markets, we call this direct finance.

Answer
✓ True
False

Add Question Here

Question 22 | **True/False** | **0 points** | Modify | Remove

Question
The difference in interest rates between savings accounts and loans can be explained, in part, by the cost of gathering information on potential borrowers—adverse selection.

Answer
✓ True
False

Add Question Here

Question 23 | **True/False** | **0 points** | Modify | Remove

Question
A bank is a financial institution that raises funds by accepting deposits and uses these funds to make private loans to individuals and companies.

Answer
✓ True
False

Add Question Here

Question 24 | **True/False** | **0 points** | Modify | Remove

Question
Savings and loan associations are usually larger than commercial banks.

Answer
True
✓ False

Add Question Here

Question 25 | **True/False** | **0 points** | Modify | Remove

Question
Through the " direct finance" channel, a saver provides funds to an investor by making use of financial markets (i.e., by buying bonds or stock issued by the investor).

Answer
✓ True
False

Add Question Here

Question 26 | **True/False** | **0 points** | Modify | Remove

Question
One explanation for high rates of economic growth is high savings rates.

Answer
✓ True
False

Add Question Here

Question 27 | **True/False** | **0 points** | Modify | Remove

Question
One explanation for high rates of economic growth is high depreciation rates.

Answer
True
✓ False

Add Question Here

Question 28 | **True/False** | **0 points** | Modify

Remove

Question
The reason for high rates of economic growth in the “ East Asian miracle” countries is relatively high rates of consumption.

Answer
True
✓ False

Add Question Here

Question 29 | **True/False** | **0 points** | Modify | Remove

Question
One reason economic historians give to explain the demise of the Soviet Union was that managers were evaluated based on profits rather than production quotas.

Answer
True
✓ False

Add Question Here

Question 30 | **True/False** | **0 points** | Modify | Remove

Question
Microfinance institutions get around the problem of moral hazard and high default rates by lending to groups rather than individuals.

Answer
✓ True
False

Add Question Here

Question 31 | **True/False** | **0 points** | Modify | Remove

Question
Microfinance institutions get around the problem of moral hazard and high default rates by charging usurious interest rates.

Answer
True
✓ False

Add Question Here

Question 32 | **True/False** | **0 points** | Modify | Remove

Question
Only with an efficient (i.e., strong) financial system will a high savings rate result in economic growth.

Answer
✓ True
False

Add Question Here

Question 33 | **True/False** | **0 points** | Modify | Remove

Question

Financial systems of all countries have the same government regulations.

Answer

True

✓ False

Add Question Here

Question 34	**True/False**	**0 points**	Modify Remove

Question

During a financial crisis, asset prices usually drop and the unemployment rate usually increases.

Answer

✓ True

False

Add Question Here

Question 35	**True/False**	**0 points**	Modify Remove

Question

Nominal GDP is the total value of all goods and services produced in an economy in a given period at constant prices.

Answer

True

✓ False

Add Question Here

Question 36	**True/False**	**0 points**	Modify Remove

Question

Economists prefer to use real GDP because it is distorted by price changes.

Answer

True

✓ False

Add Question Here

OK

Name	TestBanks Chapter 1 Short-Answer Questions
Description	Question pool for TestBanks Chapter 1 Short-Answer Questions
Instructions	Modify

Add Question Here

Question 1	**Essay**	**0 points**	Modify Remove

Question

Explain the key differences between a bond and a stock.

Answer A bond has a fixed schedule of payments, when and how much. Owners of bonds do not have a say in the way the bond issuer acts. The characteristics of a stock are: stock payments are uncertain and may change depending on the profits earned by the firm, and stockholders have voting rights. Because of uncertainty, stocks are riskier and carry higher risk premia and thus yield higher returns.

Add Question Here

Question 2	Essay	0 points	Modify Remove

Question
Describe the problem Enron employees had when the company went bankrupt.

Answer Because the overwhelming majority of the 401(k) funds of Enron's employees were devoted to Enron stock, the employees were not sufficiently diversified against risk. As the fortunes of Enron collapsed so too did the retirement funds of its employees. Many employees also lost their jobs.

Add Question Here

Question 3	Essay	0 points	Modify Remove

Question
One of the main functions of financial markets is to help people share risks. Explain why risk sharing is important to an economy?

Answer The financial markets allow investors to diversify their portfolios so if one investment does poorly, it may be offset by investments that do well. Potential investors would not want to " put all of their eggs in one basket" and potentially have large losses. At the same time, a diversified portfolio would also be expected to have smaller potentially large gains overall.

Add Question Here

Question 4	Essay	0 points	Modify Remove

Question
In 2007–2008, the U.S. financial system required substantial help from the U.S. central bank (the Fed). Explain how bailing out these financial institutions may contribute to moral hazard.

Answer When banks make loans they are implicitly willing to take on the risk associated with making those loans. Thus, if a borrower defaults, the bank should be responsible for its loan decisions. Put another way, banks must be willing to accept their mistakes. By bailing out banks that have made bad loan decisions, the Fed allows banks to dodge responsibility for their decisions. Banks may interpret this as not having to be responsible for their actions. This is one argument that was made during the U.S. subprime crisis.

Add Question Here

Question 5	Essay	0 points	Modify Remove

Question

In September 2008, the American financial system required substantial help from the U.S. government and the central bank. Most of the problems had the same root cause—asymmetric information and its twin problems of adverse selection and moral hazard. Explain how asymmetric information contributed to the financial crisis and how the government's support of the financial system addressed the problems of adverse selection and moral hazard.

Answer The financial markets experienced difficulty in the fall of September 2008 largely because shareholders and debtholders lost confidence in the ability of companies to avoid bankruptcy and to pay their debt obligations. Shareholders had less information than the companies about their future financial prospects. Adverse selection became a problem because only the firms that were desperate for funding were entering the market. Moral hazard arose when the firms engaged in behavior that was detrimental to investors, but the investors could not monitor this behavior. The government addressed these problems by providing $700 billion in financial assistance to bail out the financial firms. This financing gave investors the confidence to return to the market, since the government would bear the risk if the company would not be able to fulfill its obligations.

Add Question Here

Question 6	Essay	0 points	Modify Remove

Question

List, and explain, the basic functions of a bank.

Answer The basic functions of a bank are taking deposits and making loans. In performing these basic functions, banks must also be responsible for monitoring and screening potential borrowers to minimize problems associated with asymmetric information.

Add Question Here

Question 7	Essay	0 points	Modify Remove

Question

Explain how banks reduce adverse selection.

Answer When a potential borrower approaches a bank for a loan, the bank wants to ensure that the borrower will be able to pay back the loan. However, the bank has difficulty separating those who will pay back the loan and those who will not because it does not have the same information that the potential borrowers do. Borrowers who have a higher risk of default tend to be more eager to borrow funds than those who have a low risk. This behavior drives the good risks out of the market. Banks reduce this adverse selection by asking potential borrowers to provide information about their credit history, their business plans, and their financial status.

Add Question Here

Question 8 | **Essay** | **0 points** | Modify | Remove

Question
Explain how strong financial markets contribute to economic growth.

Answer By households having a place to save, savings rates increase and those savings can be loaned for productive purposes. Financial markets allow economies to minimize risk through screening, monitoring, and diversifying loans across a variety of firms or sectors.

Add Question Here

Question 9 | **Essay** | **0 points** | Modify | Remove

Question
A country's rate of economic growth depends on a variety of factors. Please explain how government policies toward financial markets affect economic growth.

Answer Countries with strong financial systems tend to have stronger economic growth than countries with weak financial systems. Countries with strong financial systems tend to channel savings toward its most productive uses. Governments promote strong financial systems in many ways, including (1) requiring publicly trading firms to prepare annual reports and (2) providing insurance for bank deposits.

Add Question Here

Question 10 | **Essay** | **0 points** | Modify | Remove

Question
Explain how the financial crisis of 2007–2009 affected economic growth in the United States.

Answer When the financial crisis erupted, the U.S. economy was already in a recession and the collapse of the financial markets worsened the economic downturn, as savers became unwilling to invest in the stock market. The uncertainty over the economy, combined with a reluctance of banks to make loans, led firms to scale back their investment plans and prevented small businesses from obtaining the funds needed by their businesses. These negative events reinforced one another and, when combined with the additional borrowing by the Federal government in the face of tax revenue declines due to the recession, caused economic growth to slow.

Add Question Here

OK