Reading 18: Monetary and Fiscal Policy

Question #1 of 90

Question ID: 444963

Policies used with the goal of maintaining stable prices and producing economic growth include:

A) both fiscal policy and monetary policy.

B) monetary policy only.

C) fiscal policy only.

Question #2 of 90

Question ID: 434245

Arguments against being concerned about the size of a fiscal deficit include:

A) the crowding-out effect.

B) higher future taxes.

C) Ricardian equivalence.

Question #3 of 90

Question ID: 413849

The demand for money curve represents the relationship between the quantity of money demanded and:

A) the quantity of money supplied.

B) short-term interest rates.

C) the price level.

Question #4 of 90

Question ID: 413902

Which one of the following Federal Reserve monetary policies, when pursued in line with the U.S. government's fiscal policies, would help increase aggregate demand during a period of high unemployment?

A) The sale of bonds by the Fed.

B) A decrease in the discount rate.

C) An increase in the reserve requirements for financial institutions.

Question #5 of 90

Question ID: 413839

On January 5, the U.S. Federal Reserve (the Fed) bought $10,000,000 of U.S. Treasury securities in the open market. At the time, the reserve requirement was 25%, and all banks had zero excess reserves. What is the potential impact of the Fed's purchase on the U.S. money supply?

A) $40,000,000 increase.

B) $25,000,000 decrease.

C) $10,000,000 increase.

Question #6 of 90

Question ID: 413838

The amount of money a commercial bank has available to lend is known as:

A) fractional reserves.

B) required reserves.

C) excess reserves.

Question #7 of 90

Question ID: 413865

When the Federal Reserve sells government securities on the open market, bank reserves are:

A) increased, which increases the amount of money banks are able to lend, causing a decrease in the federal funds rate.

B) decreased, which reduces the amount of money banks are able to lend, causing an increase in the federal funds rate.

C) decreased, which reduces the amount of money banks are able to lend, causing a decrease in the federal funds rate.

Question #8 of 90

Question ID: 413901

Which of the following fiscal and monetary policy scenarios is *most likely* to increase the size of the public sector relative to the private sector?

A) Expansionary fiscal policy and contractionary monetary policy.

B) Expansionary monetary policy and contractionary fiscal policy.

C) Contractionary fiscal and monetary policy.

Question #9 of 90

Question ID: 413836

When comparing a barter economy with an economy that uses money as a medium of exchange we would expect increased efficiencies due to a reduction in which of the following?

A) Transaction costs.

B) Nominal interest rates.

C) The need to specialize.

Question #10 of 90

Question ID: 413856

If a bank needs to borrow funds from the Federal Reserve to fund a temporary shortage in reserves, it would borrow funds at the:

A) discount rate.

B) prime rate.

C) federal funds rate.

Question #11 of 90

Question ID: 413877

To determine whether monetary policy is expansionary or contractionary, an analyst should compare the central bank's policy rate to the:

A) neutral interest rate.

B) target inflation rate.

C) trend rate of real growth.

Question #12 of 90

Question ID: 413886

Assuming the federal government maintains a balanced budget, the *most likely* effects of a tax increase on government expenditures and real GDP are:

	Government Expenditures	Real GDP
A)	Increase	Increase
B)	Increase	Decrease
C)	Decrease	Decrease

Question #13 of 90

Question ID: 434243

Which of the following conditions is difficult for monetary policy to address because a central bank cannot reduce its nominal policy rate below zero?

A) Deflation.

B) Stagflation.

C) Inflation.

Question #14 of 90

Question ID: 413880

Which of the following statements regarding the monetary policy transmission mechanism is *most* accurate?

A) Central banks can control short-term interest rates directly, but long-term interest rates are beyond their control.

B) Central banks can control long-term interest rates directly because decisions by consumers and businesses are based on these rates.

C) Central banks can control short-term interest rates by increasing the money supply to increase interest rates or by decreasing the money supply to decrease interest rates.

Question #15 of 90

Question ID: 413887

Robert Necco and Nelson Packard are economists at Economic Research Associates. ERA asks Necco and Packard for their opinions about the effects of fiscal policy on real GDP for an economy currently experiencing a recession. Necco states that real GDP is likely to increase if both government spending and taxes are increased by the same amount. Packard states that if both government spending and taxes are increased by the same amount, there is no expected net effect on real GDP.

Are the statements made by Necco and Packard CORRECT?

	Necco	Packard
A)	Incorrect	Incorrect
B)	Correct	Incorrect
C)	Incorrect	Correct

Question #16 of 90

Question ID: 413893

The time it takes for policy makers to enact a fiscal policy action is *best* described as:

A) legislative lag.

B) action lag.

C) implementation lag.

Question #17 of 90

Question ID: 485767

The government is reducing its spending to balance the budget, while the central bank is lowering its official policy rate. What will *most likely* be the combined effect on the economy?

A) The private sector as a percentage of GDP will increase.

B) The public and private sectors as a percentage of GDP will neither decrease nor increase.

C) The public sector as a percentage of GDP will increase.

Question #18 of 90

Question ID: 413872

Silvano Jimenez, an analyst at Banco del Rey, is reviewing recent actions taken by the U.S. Federal Reserve (the Fed) in setting monetary policy. Recently, the Fed decided to increase the money supply, which has resulted in a decrease in real interest rates. At a staff meeting, Jimenez brings this matter to the attention of his colleagues and makes the following statements:

Statement 1: Although the money supply increase has led to a decrease in real interest rates, we should begin to see U.S. investors decrease their investments abroad and the U.S. dollar will appreciate in the foreign exchange market.

Statement 2: The Fed's increase in the money supply will increase the amount of imports into the U.S.

Are Statement 1 and Statement 2 as made by Jimenez CORRECT?

	Statement 1	Statement 2
A)	Correct	Incorrect
B)	Incorrect	Incorrect
C)	Incorrect	Correct

Question #19 of 90

Question ID: 413848

Which of the following statements regarding money demand and supply is *least* accurate?

A) As the Fed reduces the money supply, short-term interest rates decrease.

B) The supply curve for money is vertical.

C) The supply of money is determined by the monetary authority and is not affected by changes in interest rates.

Question #20 of 90

Question ID: 413851

Which of the following statements about the demand and supply of money is *most* accurate? People who are:

A) holding money when interest rates are lower will try to increase their money balances and, as a result, the supply of money increases.

B) buying bonds to reduce their money balances will increase the demand for bonds with an associated increase in interest rates.

C) holding money when interest rates are higher will try to reduce their money balances and, as a result, the demand for money decreases.

Question #21 of 90

Question ID: 413890

Arguments for being concerned about the size of a fiscal deficit *least likely* include:

A) the crowding-out effect.

B) Ricardian equivalence.

C) a reduction in long-term economic growth.

Question #22 of 90

Question ID: 413844

If households are holding larger real money balances than they desire, which of the following is *least likely*?

A) The interest rate is higher than its equilibrium rate in the market for real money balances.

B) The opportunity cost of holding money balances will decrease.

C) The central bank must sell securities to absorb the excess money supply and establish equilibrium.

Question #23 of 90

Question ID: 498750

Which of the following is currently the most-used target for central banks?

A) Interest rate targeting.

B) Money supply targeting.

C) Inflation targeting.

Question #24 of 90

Question ID: 413857

A country is experiencing a core inflation rate of 7% during a recessionary period of real GDP growth. If the central bank has a single mandate to achieve price stability and uses inflation targeting with an acceptable range of zero to 4%, its monetary policy response is *most likely* to decrease:

A) short-term interest rates.

B) the foreign exchange value of the country's currency.

C) GDP growth in the short run.

Question #25 of 90

Question ID: 413862

If a monetary policy is focused on combating inflation, which open market actions by the Federal Reserve will *most* effectively accomplish this?

A) Sell Treasury securities, causing aggregate demand to decrease.

B) Sell Treasury securities, causing aggregate demand to increase.

C) Purchase Treasury securities, causing aggregate demand to decrease.

Question #26 of 90

Question ID: 434237

Promoting economic growth and price stability are the goals of:

A) fiscal policy, but not monetary policy.

B) monetary policy, but not fiscal policy.

C) both fiscal and monetary policy.

Question #27 of 90

Question ID: 498749

An individual has just purchased a home by taking on a 30-year fixed rate mortgage. She would benefit *most* from this transaction if future inflation rates are:

A) lower than anticipated.

B) exactly as anticipated.

C) higher than anticipated.

Question #28 of 90

Question ID: 413885

When an economy dips into a recession, automatic stabilizers will tend to alter government spending and taxation so as to:

A) enlarge the budget deficit (or reduce the surplus).

B) reduce the budget deficit (or increase the surplus).

C) reduce interest rates, thus stimulating aggregate demand.

Question #29 of 90

Question ID: 413829

Policies that can be used as tools for redistribution of wealth and income include:

A) monetary policy only.

B) both fiscal policy and monetary policy.

C) fiscal policy only.

Question #30 of 90

Question ID: 434242

Central banks that are able to define how inflation is computed and determine its desired level are *best* described as having:

A) transparency.
B) operational independence.
C) target independence.

Question #31 of 90

Question ID: 413858

Which of the following is *least likely* to be a function of the central bank?

A) Control money supply.
B) Issue currency.
C) Tax collection.

Question #32 of 90

Question ID: 485766

Xanadu attempts to decrease its inflation rate by implementing contractionary monetary policy. Which of the following is *most likely* to be the long-run effect on Xanadu's trade balance as a result of the monetary policy change?

A) Improve.
B) Remain the same.
C) Worsen.

Question #33 of 90

Question ID: 413859

Central banks are *most likely* to pursue a target inflation rate:

A) between 0 and 3%.
B) equal to 0%.
C) above 3%.

Question #34 of 90

Question ID: 472413

Which of the following is the *most likely* result of a central bank's shift to an expansionary monetary policy?

A) Domestic currency appreciates.
B) Exports increase.
C) Interest rates increase.

Question #35 of 90

Question ID: 413889

An argument against being concerned with the size of a fiscal deficit is that a deficit can:

A) lead to higher future taxes that will increase government revenues.

B) cause government borrowing to crowd out private borrowing.

C) aid in increasing GDP and employment if the economy is operating at less than potential GDP.

Question #36 of 90

Question ID: 434239

The Fisher effect describes a nominal interest rate as the:

A) actual inflation rate less the real interest rate.

B) expected inflation rate less the real interest rate.

C) expected inflation rate plus the real interest rate.

Question #37 of 90

Question ID: 413860

Frequent changes in advertised prices are one of the costs of:

A) expected inflation only.

B) unexpected inflation only.

C) both expected and unexpected inflation.

Question #38 of 90

Question ID: 413841

On January 3, Logan Industries deposited $1,000,000 in cash at Federal Savings Bank. No excess reserves were present at the time Logan made the deposit and the required reserve ratio is 10%. What is the maximum amount by which Federal Savings Bank can increase its lending?

A) $100,000.

B) $10,000,000.

C) $900,000.

Question #39 of 90

Question ID: 413832

Attempting to influence economic growth and inflation by changing tax rates and government spending is *best* described as:

A) government policy.

B) monetary policy.

C) fiscal policy.

Question #40 of 90

Question ID: 413891

The crowding-out model implies that a:

A) budget deficit will stimulate aggregate demand and trigger a multiplier effect which will lead to inflation.

B) budget surplus will retard aggregate demand and trigger an economic downturn.

C) budget deficit will increase the real interest rate and thereby retard private investment.

Question #41 of 90

Question ID: 413899

A government that is implementing a contractionary fiscal policy is *most likely* to:

A) decrease income tax rates.

B) increase spending on public works.

C) decrease transfer payments to households.

Question #42 of 90

Question ID: 434244

Fiscal policy includes a government's:

A) spending and tax policies only.

B) spending, tax, and monetary policies.

C) tax policies only.

Question #43 of 90

Question ID: 413896

Which of the following statements *best* explains the importance of the timing of changes in discretionary fiscal policy? Changes in discretionary fiscal policy must be timed properly if they are going to:

A) enable the government to control the money supply.

B) exert a stabilizing influence on an economy.

C) help the government achieve a balanced budget.

Question #44 of 90

Question ID: 413835

Money functions as a store of value because:

A) money received for work or goods can be saved to purchase goods or services in the future.

B) prices of goods and services are expressed in units of money.

C) money is accepted as the form of payment for goods.

Question #45 of 90

Question ID: 413854

The Fisher effect holds that a nominal rate of interest equals a real rate:

A) plus actual inflation.

B) minus expected inflation.

C) plus expected inflation.

Question #46 of 90

Question ID: 413900

The government budget deficit of Country M is increasing. At the same time, the government budget surplus of Country N is decreasing. Are the fiscal policies of these countries expansionary or contractionary?

A) Both are expansionary.

B) One is expansionary and one is contractionary.

C) Both are contractionary.

Question #47 of 90

Question ID: 413894

The time it takes for policy makers to determine that the economy requires a fiscal policy action is *best* described as:

A) impact lag.

B) recognition lag.

C) action lag.

Question #48 of 90

Question ID: 434241

If a central bank's targeted inflation rate is above the current rate, the central bank is *most likely* to:

A) increase the overnight lending rate.

B) increase the reserve requirement.

C) buy government securities.

Question #49 of 90

Question ID: 413874

If a central bank implements an exchange rate targeting policy successfully, the country's inflation rate is *most likely* to be:

A) greater than that of the target currency.
B) the same as that of the target currency.
C) less than that of the target currency.

Question #50 of 90

Question ID: 413845

Which of the following statements about the relationship between interest rates and the demand for and supply of money is *most* accurate? Interest rates affect:

A) the demand for money only.
B) both the demand for and supply of money.
C) the supply of money only.

Question #51 of 90

Question ID: 413879

The *most likely* reason for deflation to persist despite expansionary monetary policy is:

A) inelastic demand for money.
B) a liquidity trap.
C) bond market vigilantes.

Question #52 of 90

Question ID: 413833

A distinction between fiscal policy and monetary policy is that fiscal policy:

A) is aimed at promoting economic growth, while monetary policy is aimed at promoting price stability.
B) is typically expansionary, while monetary policy is typically contractionary.
C) concerns taxes and government spending, while monetary policy concerns the money supply.

Question #53 of 90

Question ID: 413869

What are the three essential qualities an effective central bank should possess?

A) Understandability, relevance, and reliability.

B) Independence, credibility, and transparency.

C) Transparency, comprehensiveness, and consistency.

Question #54 of 90

Question ID: 413892

The time it takes for a fiscal policy action to affect the economy is *best* described as:

A) impact lag.

B) economic lag.

C) fiscal lag.

Question #55 of 90

Question ID: 413868

A central bank has operational independence if it can independently determine:

A) the policy rate.

B) the horizon over which to achieve its inflation target.

C) how inflation is calculated.

Question #56 of 90

Question ID: 413876

An analyst has determined the projected trend rate of real GDP growth is 2.5% and the central bank's inflation target is 2.5%. If the central bank policy rate is 5.0%, monetary policy is *most likely*:

A) neutral.

B) contractionary.

C) expansionary.

Question #57 of 90

Question ID: 413846

The supply of money is primarily determined by:

A) the monetary authorities.

B) interest rates.

C) inflation.

Question #58 of 90

Question ID: 413866

If the Federal Reserve wishes to lower market interest rates without changing the discount rate, it can:

A) increase bank reserve requirements.

B) raise the yield on Treasury securities.

C) buy Treasury securities.

Question #59 of 90

Question ID: 413840

When additional or excess reserves are injected into the U.S. banking system, the money supply can potentially increase by an amount equal to the additional excess reserves multiplied by which of the following?

A) Reciprocal of the required reserve ratio.

B) Reciprocal of one minus the required reserve ratio.

C) Required reserve ratio.

Question #60 of 90

Question ID: 413881

Discretionary fiscal policy refers to:

A) increasing aggregate demand through lower interest rates.

B) built-in devices that counteract the business cycle phase.

C) active decisions regarding spending and taxing to affect economic growth.

Question #61 of 90

Question ID: 413883

Which of the following statements *best* explains how automatic stabilizers work? Even without a change in fiscal policy, automatic stabilizers tend to promote:

A) a budget surplus during a recession and a budget deficit during an inflationary expansion.

B) a budget deficit during a recession but do not promote a budget surplus during an inflationary expansion.

C) a budget deficit during a recession and a budget surplus during an inflationary expansion.

Question #62 of 90

Question ID: 413855

The primary objective of a central bank is to:

A) control inflation.

B) achieve full employment.

C) stabilize exchange rates.

Question #63 of 90

Question ID: 413882

Unemployment compensation is an example of:

A) a discretionary fiscal policy stabilizer.

B) an automatic fiscal policy stabilizer.

C) an automatic monetary policy stabilizer.

Question #64 of 90

Question ID: 413852

Which of the following is determined by the equilibrium between the demand for money and the supply of money?

A) Money supply.

B) Inflation rate.

C) Interest rate.

Question #65 of 90

Question ID: 434236

When the central bank reduces the quantity of money and credit in an economy, its monetary policy is *best* described as:

A) expansionary.

B) contractionary.

C) accommodative.

Question #66 of 90

Question ID: 472412

Contractionary monetary policy is *least likely* to decrease consumption spending by decreasing:

A) expectations for economic growth.

B) securities prices.

C) the foreign exchange value of the currency.

Question #67 of 90

Question ID: 413863

Which of the following statements regarding U.S. Federal Reserve open market operations is *least* accurate?

A) When the Fed sells Treasury securities, excess reserves decrease.

B) If the Fed wants to stimulate the economy, it will sell Treasury securities to banks.

C) When the Fed buys Treasury securities, short-term interest rates will generally decrease.

Question #68 of 90

Question ID: 413843

Which of the following relationships in regard to the quantity theory of money is *least* accurate?

A) Money × Velocity = Money Supply × Velocity.

B) Nominal GDP = Price × Money Supply.

C) Nominal GDP = Money Supply × Velocity = Price × Real Output.

Question #69 of 90

Question ID: 434238

The three reasons for holding money are most accurately described as:

A) transaction demand, precautionary demand, and speculative demand.

B) narrow money demand, precautionary demand, and speculative demand.

C) broad money demand, narrow money demand, and transaction demand.

Question #70 of 90

Question ID: 413895

Which of the following statements about achieving proper timing in fiscal policy is *least* accurate?

A) Improvements in quantitative methods have made the occurrence of recessions or expansions quite predictable.

B) Policy errors are inevitable due to unpredictable events.

C) There is usually a time lag between when a change in policy is needed and when the need is recognized by policy makers.

Question #71 of 90

Question ID: 413871

The open market sale of Treasury securities by the Federal Reserve is *least likely* to result in:

A) increased longer-term interest rates.

B) increased exports of U.S. goods.

C) a decreased rate of inflation.

Question #72 of 90

Question ID: 413864

Assume the U.S. economy is undergoing a recession. In its efforts to stimulate the economy by trying to influence short-term interest rates the Fed is *most likely* to take which two actions?

A) Sell Treasury securities and increase bank reserve requirements.

B) Buy Treasury securities and decrease bank reserve requirements.

C) Sell Treasury securities and decrease bank reserve requirements.

Question #73 of 90

Question ID: 413873

If the U.S. Federal Reserve decides to decrease the money supply, which of the following is *most likely* to occur in the short run?

A) A decrease in the unemployment rate.

B) An increase in the real rate of interest.

C) An increase in the velocity of money similar to decrease in the money supply.

Question #74 of 90

Question ID: 413837

Which of the following is the *most* accurate definition of the velocity of money? The velocity of money is the:

A) money supply of a country divided by its price level.

B) GDP of a country divided by its price level.

C) GDP of a country divided by its money supply.

Question #75 of 90

Question ID: 413878

An economy's long-term trend rate of real GDP growth is 3% and the central bank's target inflation rate is 2%. If the policy rate is 6%, monetary policy is:

A) contractionary.

B) neutral.

C) expansionary.

Question #76 of 90

Question ID: 413850

If the money interest rate is measured on the y-axis and the quantity of money is measured on the x-axis, the money supply curve is:

A) downward sloping to the lower right.

B) upward sloping to the upper right.

C) vertical.

Question #77 of 90

Question ID: 413831

Monetary policy refers to actions that influence economic activity by increasing or decreasing:

A) government purchases of goods and services.

B) the supply of money and credit.

C) tax rates on income and consumption.

Question #78 of 90

Question ID: 413842

Banks choose to hold a higher percentage of deposits as reserves because they believe general business conditions in the economy are subject to greater uncertainty. If all else is held constant, what is the *most likely* impact of this action?

A) There will be no effect on the money supply.

B) The money supply will decrease.

C) The money supply will increase during a period of inflation, but will decrease if the economy goes into a recession.

Question #79 of 90

Question ID: 413853

According to the Fisher effect, which of the following interest rates includes a premium for the expected rate of inflation?

A) Both yields on short-term government debt and yields on long-term corporate debt.

B) Neither yields on short-term government debt nor yields on long-term corporate debt.

C) Yields on long-term corporate debt, but not yields on short-term government debt.

Question #80 of 90

Question ID: 696228

The term "automatic stabilizers" refers to:

A) changes in taxes and expenditure programs legislators automatically enact in response to changes the level of economic activity in order to smooth economic cycles.

B) increases in transfer payments and decreases in tax revenues that result from an economic contraction without new legislation.

C) government expenditures and tax receipts that are required to balance over the course of the business cycle, although they may be out of balance in any single year.

Question #81 of 90

Question ID: 413875

A central bank follows an inflation targeting monetary policy. If the permissible band is plus-or-minus 2% around the target inflation rate, the central bank is *most likely* to choose a target inflation rate of:

A) 3%.

B) 0%.

C) 1%.

Question #82 of 90

Question ID: 413870

If a country's economy is growing at an unsustainably rapid rate and the central bank decreases its target overnight interest rate, the country's:

A) expected rate of inflation is likely to decline.

B) inflation rate is likely to increase.

C) long-term rate of economic growth will increase.

Question #83 of 90

Question ID: 413861

Compared to the costs of inflation that is unexpected, costs of inflation that iscorrectly anticipated are *most likely* to be:

A) less severe.

B) more severe.

C) equally severe.

Question #84 of 90

Question ID: 434240

Central banks pursuing expansionary policies may:

A) decrease the policy rate and make open market sales of securities.

B) increase the policy rate and make open market purchases of securities.

C) decrease the policy rate and make open market purchases of securities.

Question #85 of 90

Question ID: 413847

Which of the following statements about the demand for and supply of money is *least* accurate?

A) As gross domestic product rises, the demand for money balances also rises.

B) As inflation rises, the demand for money by households and businesses also rises.

C) As the interest rate rises, the supply of money also rises.

Question #86 of 90

Question ID: 413834

Money serves as a unit of account because:

A) money received for work or goods can be saved to purchase goods or services in the future.

B) money is accepted as the form of payment for goods.

C) prices of goods and services are expressed in units of money.

Question #87 of 90

Question ID: 413888

Assuming the economy currently is experiencing high inflation, an example of appropriate discretionary fiscal policy is:

A) reduce the money supply.

B) increase the federal funds target rate.

C) reduce government expenditures on major government construction projects.

Question #88 of 90

Question ID: 413867

Which of the following policy tools is the *least likely* to be available to the U.S. Federal Reserve Board?

A) Requiring the banking system to tighten or loosen its credit policies.

B) Setting the discount rate at which banks can borrow from the Federal Reserve.

C) Buying and selling Treasury securities in the open market.

Question #89 of 90

Question ID: 413897

The country of Zurkistan is experiencing both high interest rates and high inflation. The government passes laws that reduce government spending and increase taxes. It takes many months before interest rates fall and inflation is reduced. This is an example of:

A) recognition lag in discretionary fiscal policy.

B) action lag and automatic stabilizers.

C) impact lag in discretionary fiscal policy.

Question #90 of 90

Question ID: 413898