Test Bank for Money Banking and the Financial System 3rd Hubbard

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Money, Banking, and the Financial System, 3e **(Hubbard/O'Brien)**
Chapter 2 Money and the Payments System

2.1 Do We Need Money?

1) An important reason why economies at an early stage of development tend to operate inefficiently is
A) they tend to be dominated by the agricultural sector, where productivity is usually low.
B) they tend to have authoritarian governments that stifle innovation.
C) they tend to be plagued by superstitious beliefs that stifle innovation.
D) the high transactions costs associated with barter.
Answer: D
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

2) By "specialization" economists mean a situation where
A) individuals produce the goods or services for which they have relatively the best ability.
B) goods are traded directly for goods and money is not used.
C) individuals who produce goods do not also produce services and individuals who produce services do not also produce goods.
D) individuals are assigned to occupations on the basis of tests that gauge their relative abilities.
Answer: A
Diff: 1 Page Ref: 27
Topic: specialization
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

3) The most important economic benefit from specialization is that it
A) makes it possible for an economy to begin using money.
B) leads to an increase in the standard of living in an economy.
C) makes barter possible.
D) eliminates the need for financial markets.
Answer: B
Diff: 2 Page Ref: 27
Topic: specialization
Objective: Analyze the inefficiencies of a barter system
*: Recurring
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4) When an economy relies on specialization
A) the economy will generally produce only one product.
B) the economy will usually be heavily agricultural.
C) each individual in the economy produces the goods or services for which he or she has relatively the best ability.
D) each individual will be assigned by the government to produce that good or service the government believes the economy should specialize in.
Answer: C
Diff: 2 Page Ref: 27
Topic: specialization
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

5) Fundamentally, to reap the benefits of specialization, an economy must
A) be heavily industrial.
B) be heavily agricultural.
C) have an extensive system of higher education.
D) develop ways for individuals to trade goods with one another.
Answer: D
Diff: 2 Page Ref: 27
Topic: specialization
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

6) Barter is
A) another name for money.
B) an exchange of goods and services directly for goods and services.
C) the basis for economic specialization.
D) the main system of exchange in the United States today.
Answer: B
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
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7) Under a system of barter
A) each individual trades output directly with another.
B) only agricultural goods may be traded.
C) goods may be traded for money, but money may not be traded for goods.
D) currency is accepted for purchases, but personal checks are not.
Answer: A
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

8) Which of the following is an example of a barter transaction?
A) An individual pays her electric bill with a check.
B) An individual pays her electric bill with currency.
C) An individual provides three light bulbs to her neighbor in exchange for two gallons of milk.
D) An individual deposits three twenty-dollar bills in her checking account.
Answer: C
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

9) In a barter system individuals
A) find it impossible to specialize.
B) must be entirely self-sufficient.
C) find it difficult to specialize, but may be able to do so.
D) will almost invariably specialize.
Answer: C
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

10) A system of barter has substantial transactions costs because
A) taxes under such a system are generally a large fraction of the value of output.
B) traders must spend considerable time searching for trading partners.
C) the uncertainties of trade result in high legal fees being incurred to draw up binding contracts.
D) the uncertainties of trade result in high insurance premiums.
Answer: B
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
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11) Under a barter system
A) each good has many prices.
B) each good has a single price.
C) no prices for goods exist.
D) prices for goods are very stable.
Answer: A
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

12) How many prices would there be in a barter economy with 100 goods?
A) 100
B) 1,000
C) 4,950
D) 10,000
Answer: C
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

13) The problem of a double coincidence of wants refers to
A) the insatiability of wants in a free market economy.
B) poorly-managed companies producing what consumers want only by coincidence.
C) the necessity in a barter system of each trading partner wanting what the other has to trade.
D) the likelihood that needs will not be the same as wants.
Answer: C
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
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14) Andy can't make a deal with Danny. Andy has an Alex Rodriguez baseball card and would like to trade it to Danny for Danny's Albert Pujols card, but Danny doesn't want an Alex Rodriguez card. Andy's problem illustrates the drawback to a barter system known as
A) the specialization problem.
B) the double coincidence of wants problem.
C) the many prices problem.
D) the transactions problem.
Answer: B
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

15) Which of the following is NOT a significant cost that a barter system imposes on an economy?
A) Many prices must be maintained for each good.
B) Only agricultural goods may be traded.
C) Specialization of labor is hindered.
D) The costs arising from the problem of finding two people who each want what the other produces.
Answer: B
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

16) Which of the following is the most efficient means of trade?
A) barter
B) money
C) government rationing
D) the combination of barter with some government rationing
Answer: B
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
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17) In Moscow in 1989, what were taxi drivers using as a medium of exchange?
A) Russian rubles
B) Marlboro cigarettes
C) gold coins
D) caviar
Answer: B
Diff: 1 Page Ref: 27
Topic: barter
Special Feature: Making the Connection: What's Money? Ask a Taxi Driver in Moscow!
Objective: Analyze the inefficiencies of a barter system
AACSB: Reflective Thinking

18) Money eliminates the need for
A) any government role in the economy.
B) specialization.
C) people to have a double coincidence of wants.
D) the market system.
Answer: C
Diff: 1 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

19) Using a good as a medium of exchange confers the benefit that
A) the need to quote so many prices in trade is reduced.
B) the need for a double coincidence of wants is greatly increased.
C) the need for specialization is reduced.
D) transactions costs are increased, but they now may be paid in money terms.
Answer: A
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

20) Commodity money can best be described as
A) money used to purchase agricultural products.
B) a good used as money that also has value independent of its use as money.
C) standardized goods like gold that trade in a financial market.
D) the form of money used in a barter system.
Answer: B
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
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21) Which of the following is NOT a problem with barter?
A) Each good has multiple prices.
B) high transactions costs
C) the commodity money having value for other uses besides money
D) lack of standardization of products exchanged
Answer: C
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

22) The introduction of money to an economy results in
A) higher incomes.
B) higher productivity.
C) increased specialization.
D) all of the above.
Answer: D
Diff: 2 Page Ref: 27
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

23) Money can BEST be described as
A) anything that is generally accepted as payment for goods and services or in the settlement of debts.
B) paper that can be used to purchase goods and services.
C) commodities that have intrinsic value.
D) any form of wealth possessed by consumers.
Answer: A
Diff: 1 Page Ref: 25
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Reflective Thinking

24) How does the existence of money affect economic growth?
Answer: It reduces transactions costs and other efficiencies of barter. People can specialize, becoming far more productive than if they tried to produce all goods and services they consume themselves.
Diff: 2 Page Ref: 27
Topic: barter
Objective: Analyze the inefficiencies of a barter system
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25) What are four inefficiencies of a barter system?
Answer: Under a barter system, there are several inefficiencies. First, there must be a double coincidence of wants, resulting in high transaction costs. Second, there will be many prices for each good; one for each good for which it can be traded. Third, there is a lack of standardization in terms of the goods to be exchanged. Fourth, it will be difficult to accumulate wealth.
Diff: 2 Page Ref: 26
Topic: barter
Objective: Analyze the inefficiencies of a barter system
*: Recurring
AACSB: Analytical Thinking

2.2 The Key Functions of Money

1) Money is a medium of exchange in that
A) money is generally accepted for buying and selling goods and services.
B) currency may be exchanged for gold at any national bank.
C) other assets may be better or worse in facilitating exchange than money.
D) it must maintain most of its value over time.
Answer: A
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

2) Money as a medium of exchange refers only to
A) currency.
B) gold coins.
C) anything that is generally accepted as payment for goods and services.
D) checks at commercial banks.
Answer: C
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
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3) When economists refer to the role of money as a unit of account, they mean that
A) most accounting systems reflect that goods are purchased with currency.
B) most accounting systems reflect that goods are purchased with checks.
C) money gives traders a way of measuring value in the economy.
D) money makes it possible for specialization to take place.
Answer: C
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

4) When economists refer to the role of money as a store of value, they mean that
A) money never loses its value, unlike other assets.
B) money allows value to be stored easily.
C) the value of money falls only when the quantity of money in circulation falls.
D) the value of money falls only when the quantity of money in circulation rises.
Answer: B
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

5) An asset is
A) the same thing as a liability.
B) a thing of value that can be owned.
C) money, as opposed to stock or bonds.
D) anything that never declines in value.
Answer: B
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

6) The attribute that distinguishes money from other assets is that only money
A) retains its value during times of inflation.
B) is counted in determining the size of an individual's wealth.
C) serves as a medium of exchange.
D) may be used as collateral for a bank loan.
Answer: C
Diff: 1 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
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7) Wealth is
A) the sum of the value of assets.
B) equal to income.
C) a flow variable.
D) the sum of the value of assets minus the sum of the value of liabilities.
Answer: D
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

8) The difference between money and income is that whereas income is an individual's
A) flow of earnings over a period of time, money is an individual's stock of currency and currency substitutes.
B) stock of all assets, money is an individual's stock of currency and currency substitutes.
C) flow of earnings over a period of time, money is an individual's stock of all assets.
D) stock of currency and currency substitutes, money is an individual's stock of all assets.
Answer: A
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

9) In comparing money to shares of Apple stock, we can say that
A) money is a store of value, but shares of Apple stock are not.
B) shares of Apple stock are a store of value, but money is not.
C) both money and shares of Apple stock are stores of value.
D) neither money nor shares of Apple stock are stores of value.
Answer: C
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
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10) Why do individuals hold money when it does NOT provide the services that, say, a house does?
A) Money is the most liquid asset.
B) Money is the only form in which wealth may be held.
C) Money increases in value faster than other assets.
D) Money is useful in avoiding taxes on certain transactions.
Answer: A
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

11) Other assets are inferior to money in the sense that
A) they increase in value more slowly than does money.
B) they have a lower overall return than money.
C) they are more vulnerable to losing their real value as inflation increases.
D) they generate transactions costs when they are exchanged for money.
Answer: D
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

12) When economists refer to the role of money as a standard of deferred payment, they mean that
A) payments by checks are usually deferred until the checks clear the bank.
B) money earns interest while loan payments are deferred.
C) money provides a standard for payments that will occur in the future.
D) money today is worth less than money tomorrow.
Answer: C
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
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13) If prices increase rapidly
A) money's usefulness as a store of value is diminished.
B) money increases in value.
C) deflation is likely.
D) prices will decline to their normal level.
Answer: A
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

14) Suppose $100 buys less in the year 2017 than in 2000. Then we can say that
A) money's store of value has decreased.
B) money's store of value has increased.
C) the economy must have been growing rapidly between 2000 and 2017.
D) the economy must have been growing slowly between 2000 and 2017.
Answer: A
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

15) Which of the following is NOT an important criterion for whether a good will be usable as a medium of exchange?
A) The good must be of standardized quality.
B) The good must be valuable relative to its weight.
C) The good must have value even if it were not being used as money.
D) The good must be durable so that value is not lost through product spoilage.
Answer: C
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
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16) Which criterion for suitability as a medium of exchange do Federal Reserve Notes meet?
A) They are of standardized quality.
B) They are durable.
C) They are acceptable to most traders.
D) Federal Reserve Notes meet all of the criteria for suitability as a medium of exchange.
Answer: D
Diff: 1 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

17) What determines the acceptability of dollar bills as a medium of exchange?
A) our society's willingness to use green paper notes issued by the Federal Reserve as money
B) the willingness of the Federal Reserve to redeem dollar bills for gold
C) the willingness of the U.S. Treasury to redeem dollar bills for gold
D) the public's fear that failing to accept dollar bills will trigger a hyperinflation
Answer: A
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

18) In what sense do self-fulfilling expectations determine the acceptability of a medium of exchange?
A) People like to do what the government expects them to do.
B) People value something as money only if they believe others will accept it from them as payment.
C) People expect that money will never lose its value.
D) People expect that eventually every country will use the same medium of exchange.
Answer: B
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
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19) Fiat money
A) is money that would have no value if it were not usable as money.
B) is illegal in most advanced, industrial countries.
C) is usually some type of precious metal.
D) will generally be accepted in trade for less than its face value.
Answer: A
Diff: 1 Page Ref: 29
Topic: fiat money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

20) If money is declared to be legal tender, it must be
A) minted from a precious metal.
B) acceptable to citizens of foreign countries.
C) possible to exchange it for an equivalent amount of precious metal.
D) accepted to settle private transactions and it must be accepted for the payment of taxes.
Answer: D
Diff: 1 Page Ref: 29
Topic: fiat money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

21) By designating Federal Reserve currency as legal tender, the federal government
A) has ensured that Federal Reserve currency will serve as money.
B) has guaranteed that Federal Reserve currency may be exchanged for an equivalent amount of gold or silver.
C) has mandated that Federal Reserve currency be accepted for payment of debts.
D) has mandated that Federal Reserve currency be accepted by citizens of foreign countries in exchange for their countries' currencies.
Answer: C
Diff: 1 Page Ref: 29
Topic: fiat money
Objective: List and describe the four key functions of money
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22) What is the most important factor for Federal Reserve currency to be accepted as money?
A) its acceptance by businesses and households in the United States in exchange for goods and services
B) its designation as legal tender by the federal government
C) the willingness of the federal government to accept it in exchange for an equivalent amount of gold or silver coins
D) the willingness of foreign businesses and banks to accept it in exchange for goods and services
Answer: A
Diff: 2 Page Ref: 29
Topic: fiat money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

23) Which function of money eliminates the need for multiple prices for each good as in a barter system?
A) store of value
B) standard of deferred payment
C) unit of account
D) valuable relative to its weight
Answer: C
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

24) Which function of money allows for specialization to take place?
A) medium of exchange
B) unit of account
C) store of value
D) standard of deferred payment
Answer: A
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
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25) Which function of money enhances the ability of households to accumulate wealth?
A) medium of exchange
B) store of value
C) valuable relative to its weight
D) does not become worn out too quickly
Answer: B
Diff: 1 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

26) Money that has no value apart from its use as money
A) is known as commodity money.
B) is known as fiat money.
C) will result in a return to a barter system.
D) will result in rapid inflation.
Answer: B
Diff: 1 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

27) A person's earnings over a period of time is known as
A) money.
B) income.
C) wealth.
D) all of the above.
Answer: B
Diff: 1 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
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28) As of late 2016, approximately what portion of U.S. currency is held outside of the United States?
A) 1/10
B) 1/3
C) 1/2
D) 2/3
Answer: D
Diff: 1 Page Ref: 30-32
Topic: monetary aggregates
Special Feature: Making the Connection: Say Goodbye to the Benjamins?
Objective: Explain how the U.S. money supply is measured
AACSB: Reflective Thinking

29) Since the year 2000, total currency in circulation
A) has fallen by 20 percent.
B) has remained essentially the same.
C) has more than tripled.
D) has increased tenfold.
Answer: C
Diff: 1 Page Ref: 30-32
Topic: monetary aggregates
Special Feature: Making the Connection: Say Goodbye to the Benjamins?
Objective: Explain how the U.S. money supply is measured
AACSB: Reflective Thinking

30) More than three-quarters of the value of all U.S. currency consists of
A) $1 bills.
B) $20 bills.
C) $50 bills.
D) $100 bills.
Answer: D
Diff: 1 Page Ref: 30-32
Topic: monetary aggregates
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31) If fiat money has no value apart from its use as money, how can it be used as a medium of exchange?
Answer: The most important reason paper currency circulates as a medium of exchange is the confidence of consumers and firms that if they accept paper currency they will be able to pass it along when they need to buy goods and services. Also, the federal government has designated it to be legal tender, meaning the government accepts it in payment of taxes and requires it to be accepted in payment of debts.
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

32) Economic studies have shown that countries that have high inflation rates have lower rates of economic growth than do countries with low inflation rates. Explain what underlies this relationship between inflation and economic growth.
Answer: In terms of the issues discussed in this chapter, inflation reduces the usefulness of currency as a store of value and as a standard of deferred payment. In extreme cases, high rates of inflation have led to a shift to a barter system or to the use of foreign currency as a medium of exchange. These effects would tend to reduce the efficiency of the economy and the rate of economic growth.
Diff: 3 Page Ref: 28-29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Analytical Thinking

33) In what way are other assets less liquid than money?
Answer: You incur transactions costs when you exchange other assets for money.
Diff: 2 Page Ref: 28
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

34) What is the difference between money, income, and wealth?
Answer: Income is equal to a person's earnings over a period of time. Wealth is the sum of a person's assets minus the sum of a person's liabilities. Money is a medium of exchange and one component of a person's wealth.
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
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35) What are the five characteristics that make an asset suitable to be used as a medium of exchange?
Answer: It must be acceptable to most people; standardized in terms of quality; durable so that it doesn't become too worn out to be usable; valuable relative to its weight; divisible since prices of goods and services vary.
Diff: 2 Page Ref: 29
Topic: functions of money
Objective: List and describe the four key functions of money
*: Recurring
AACSB: Reflective Thinking

2.3 The Payments System

1) The payments system is
A) the mechanism for conducting economic transactions.
B) another name for the system of foreign exchange rates.
C) the phrase used to describe how transactions are carried out in an economy that does not use money.
D) the way in which economic transactions are carried out in a government-controlled economy, such as the former Soviet Union.
Answer: A
Diff: 1 Page Ref: 32
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

2) Which of the following is an example of a commodity money?
A) gold coins
B) dollar bills
C) British pound notes
D) Japanese yen notes
Answer: A
Diff: 1 Page Ref: 32
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

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3) All of the following are problems associated with commodity money EXCEPT
A) it is a cumbersome form of payments system.
B) commodities tend to have little value in and of themselves.
C) its value is dependent on its purity.
D) costs are incurred in certifying the purity and weight of commodity money.
Answer: B
Diff: 2 Page Ref: 32
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

4) Which of the following is an example of fiat money?
A) a cowry shell used as money on a South Pacific island
B) a gold coin used as money in nineteenth century England
C) a Federal Reserve Note used as money in the twenty-first century United States
D) a pound of salt used as money in medieval France
Answer: C
Diff: 1 Page Ref: 32-33
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

5) Checks are
A) not acceptable for settling transactions in most industrialized countries.
B) less important than currency as a means of settling transactions.
C) promises to pay, on demand, money deposited with a financial institution.
D) promises to pay, on demand, coins minted from precious metals.
Answer: C
Diff: 1 Page Ref: 33
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

6) Which of the following is NOT a step involved in using checks?
A) The recipient must present the check to the bank.
B) The bank must present the check to the checkwriter's bank.
C) The funds must be transferred from the checkwriter's bank to the recipient's bank.
D) The funds must be transferred from the recipient's bank to the checkwriter's bank.
Answer: D
Diff: 1 Page Ref: 33
Topic: payments system
Objective: Explain the role of the payments system in the economy
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7) The use of checks in transactions
A) entails lower information costs than the use of currency.
B) entails fewer steps than settling transactions with currency.
C) avoids the cost of transporting currency back and forth.
D) entails fewer steps and lower information costs than settling transactions with currency.
Answer: C
Diff: 2 Page Ref: 33
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

8) Automatic teller machines and debit cards are examples of
A) electronic funds transfer systems.
B) commodity monies.
C) legal tender in the United States.
D) modern barter systems.
Answer: A
Diff: 1 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

9) All of the following are examples of electronic funds EXCEPT
A) credit cards.
B) debit cards.
C) ACH transactions.
D) e-money.
Answer: A
Diff: 1 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
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10) All of the following are characteristics of debit cards EXCEPT
A) payments are deferred until a later date.
B) they can be used like checks.
C) they eliminate the problem of trust since the bank's computer authorizes the transaction.
D) when used at a store, the user's bank instantly credits the store's account with the amount and deducts it from the user's account.
Answer: A
Diff: 1 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

11) Which of the following statements about ACH transactions is FALSE?
A) They reduce the likelihood of missed payments.
B) They reduce transactions costs associated with check processing.
C) They reduce the costs that lenders incur in notifying customers of missed payments.
D) They typically involve digital cash.
Answer: D
Diff: 2 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

12) Which of the following is NOT on the Fed's list of the five most desirable outcomes for a payments system?
A) inflation-proof
B) security
C) efficiency
D) speed
Answer: A
Diff: 1 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
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13) Which of the following is a form of e-money?
A) gold
B) PayPal
C) an American Express card
D) traveler's checks
Answer: B
Diff: 1 Page Ref: 34
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

14) Bitcoin is a form of
A) commodity money.
B) legal tender.
C) e-money.
D) all of the above.
Answer: C
Diff: 1 Page Ref: 35
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

15) All of the following statements regarding bitcoin transactions are true EXCEPT
A) no permanent record of bitcoin transactions exist.
B) bitcoin transactions are now more prevalent than cash transactions.
C) retailers pay a lower processing cost for bitcoin transactions than for credit card transactions.
D) bitcoin transactions are final and unlike credit card transactions, cannot be disputed by the buyer.
Answer: B
Diff: 2 Page Ref: 35
Topic: payments system
Objective: Explain the role of the payments system in the economy
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16) According to a Federal Reserve study, electronic payments now make up _____ of all noncash payments.
A) 15 percent
B) just under half
C) more than two-thirds
D) just under 90 percent
Answer: C
Diff: 1 Page Ref: 36
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Reflective Thinking

17) In Sweden, cash accounts for _____ of transactions.
A) only about 2 percent
B) about 10 percent
C) approximately 40 percent
D) just under 90 percent
Answer: A
Diff: 1 Page Ref: 36-37
Topic: payments system
Special Feature: Making the Connection: Will Sweden Become the First Cashless Society?
Objective: Explain the role of the payments system in the economy
AACSB: Reflective Thinking

18) All of the following are true in Sweden EXCEPT
A) many branches of Sweden's banks do not accept cash deposits.
B) some stores have stopped accepting cash payments.
C) many churches encourage parishioners to make donations using a mobile banking app.
D) the government no longer issues paper currency.
Answer: D
Diff: 1 Page Ref: 36-37
Topic: payments system
Special Feature: Making the Connection: Will Sweden Become the First Cashless Society?
Objective: Explain the role of the payments system in the economy
AACSB: Reflective Thinking

19) According to the Fed, what are the five most desirable outcomes for a payments system?
Answer: Speed, Security, Efficiency, Smooth international transactions, and Effective collaboration among participants in the system
Diff: 2 Page Ref: 33-34
Topic: payments system
Objective: Explain the role of the payments system in the economy
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20) Why does the payments system continue to change over time?
Answer: New forms of payments are introduced that increase the efficiency of the payments system by reducing transactions costs.
Diff: 2 Page Ref: 32-34
Topic: payments system
Objective: Explain the role of the payments system in the economy
*: Recurring
AACSB: Analytical Thinking

2.4 Measuring the Money Supply

1) As of May 2016, the amount of money as measured by M2 was about
A) $880 billion.
B) $3.2 trillion.
C) $12.7 trillion.
D) $16 trillion.
Answer: C
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

2) The M2 aggregate
A) includes M1 plus short-term investment accounts.
B) includes M1 plus large-denomination time deposits.
C) equals currency plus checking account deposits at commercial banks.
D) is the best definition of money purely as a medium of exchange.
Answer: A
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

3) Which of the following is NOT included in M2?
A) currency
B) savings bonds
C) money market deposit accounts
D) overnight repurchase agreements
Answer: B
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
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4) Which of the following statements is TRUE about M2?
A) Its total value is smaller than that of M1.
B) Apart from those assets also included in M1, it includes no assets that offer check-writing features.
C) Its total value is about four times as large as M1.
D) It includes large-denomination time deposits.
Answer: C
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

5) Which of the following is included in M1, but not in M2?
A) currency
B) checking account deposits
C) travelers checks
D) Everything in M1 is in M2.
Answer: D
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

6) Money market deposit accounts are included in
A) only M1.
B) only M2.
C) M1 and M2.
D) neither M1 nor M2.
Answer: B
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
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7) Which of the following makes up the largest share of M2?
A) M1
B) savings deposits
C) small time deposits
D) money market mutual fund shares
Answer: B
Diff: 2 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

8) The Fed's current position towards the existing monetary aggregates is
A) it is convinced that M1 is the best measure of the money supply.
B) it is convinced that M2 is the best measure of the money supply.
C) it is an issue of ongoing research.
D) it is reverting to considering currency alone as the best measure of the money supply.
Answer: C
Diff: 2 Page Ref: 39
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

9) In May 2016, what was the total value of U.S. currency in circulation?
A) $2.4 billion
B) $1,375 billion
C) $1,866 billion
D) $16 trillion
Answer: B
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

10) A monetary aggregate is a measure of
A) the inflation rate.
B) the total economic activity of the country.
C) money broader than currency.
D) definitive money.
Answer: C
Diff: 1 Page Ref: 37
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
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11) The narrowest money measure is
A) currency plus non-interest bearing checking accounts.
B) currency plus all checking accounts.
C) currency plus all deposits at financial institutions.
D) definitive money.
Answer: B
Diff: 2 Page Ref: 37
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

12) Which of the following is the largest measure of money in the United States?
A) Federal Reserve notes
B) definitive money
C) M1
D) M2
Answer: D
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

13) Which of the following is NOT included in M1?
A) currency
B) savings account deposits
C) checking account deposits
D) traveler's checks
Answer: B
Diff: 1 Page Ref: 37
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
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14) Which of the following is the largest component of M1?
A) traveler's checks
B) savings deposits
C) checking deposits
D) currency
Answer: C
Diff: 1 Page Ref: 38
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

15) Which of the following describes the behavior of M1 in recent decades?
A) It soared during the recessions of 1990-91, 2001, and 2007-2009.
B) It tended to grow more rapidly than M2.
C) It was more stable than M2.
D) It has not declined since the 1970s.
Answer: A
Diff: 1 Page Ref: 39
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Reflective Thinking

16) Why has M2 grown more quickly than M1 in recent decades?
A) Currency in circulation has declined.
B) People own more shares of stock than in the past.
C) The amount of funds in CDs and money market mutual funds shares has grown faster than currency or checking deposits.
D) Most people use debit cards instead of checking accounts.
Answer: C
Diff: 2 Page Ref: 39
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
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17) What criteria should be used in deciding the best definition of the money supply?
Answer: The answer depends on the purpose of the measurement. Economists are primarily interested in the relation between monetary aggregates and other economic variables, such as output, the price level, and interest rates. In this respect, a monetary aggregate is most useful when it is most closely related to these economic variables. Until the 1980s, M1 was the most widely accepted measure of the money supply. In the 1980s and 1990s, M2 has been most widely accepted.
Diff: 2 Page Ref: 39
Topic: monetary aggregates
Objective: Explain how the U.S. money supply is measured
*: Recurring
AACSB: Analytical Thinking

2.5 The Quantity Theory of Money: A First Look at the Link Between Money and Prices

1) Suppose the GDP implicit price deflator was 112.7 in 2015 and 116.0 in 2016. Therefore, the inflation rate in 2016 would be
A) 2.8%.
B) 2.9%.
C) 3.3%.
D) 16%.
Answer: B
Diff: 2 Page Ref: 42
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Analytical Thinking

2) A hyperinflation occurs when
A) inflation persists for more than two years.
B) inflation persists for more than five years.
C) the inflation rate exceeds 50% per year.
D) the inflation rate exceeds 50% per month.
Answer: D
Diff: 1 Page Ref: 43
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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3) When prices rise, the purchasing power of money
A) rises.
B) falls.
C) is unaffected.
D) may rise, fall, or be unaffected depending upon circumstances.
Answer: B
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

4) The purchasing power of money
A) rises when prices fall.
B) rises when prices rise.
C) is set by the Fed in January of each year.
D) is constant.
Answer: A
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

5) The velocity of money can best be described as
A) how quickly prices are increasing.
B) how quickly output is increasing.
C) the number of times each dollar in the money supply is used to buy goods and services included in GDP.
D) the growth rate of the money supply.
Answer: C
Diff: 1 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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6) According to the equation of exchange, the money supply times the velocity of money equals the
A) price level.
B) growth rate of the money supply.
C) real GDP.
D) nominal GDP.
Answer: D
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

7) According to the quantity theory of money, the growth rate of which of the following is zero?
A) money supply
B) velocity
C) real GDP
D) price level
Answer: B
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

8) Suppose nominal GDP is $14 trillion and the money supply is $2 trillion. What is the velocity of money?
A) 0.143
B) 7
C) 12
D) 28
Answer: B
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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9) According to the quantity theory of money, if the long-run economic growth rate is 2.5%, by how much should the Fed increase the money supply if it wants inflation to be 2%?
A) 0.5%
B) 1.25%
C) 4.5%
D) 5%
Answer: C
Diff: 3 Page Ref: 41
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Analytical Thinking

10) According to the equation of exchange, how can national income grow even though the amount of money does NOT?
A) Price level increases.
B) Real GDP decreases.
C) Velocity increases.
D) Velocity decreases.
Answer: C
Diff: 2 Page Ref: 40
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

11) Hyperinflations are usually caused by large budget deficits financed by
A) selling bonds to private investors.
B) selling bonds to the central bank.
C) raising taxes.
D) borrowing from commercial banks.
Answer: B
Diff: 3 Page Ref: 44
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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12) Which country experienced hyperinflation of almost 15 billion percent in 2008?
A) Argentina
B) Canada
C) Iceland
D) Zimbabwe
Answer: D
Diff: 1 Page Ref: 24-25
Topic: equation of exchange and quantity theory
Special Feature: Chapter Opener: The Federal Reserve: Good for Main Street or Wall Street-or Both?
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
AACSB: Reflective Thinking

13) Research has shown that nations with highly independent central banks tend to have low
A) inflation.
B) interest rates.
C) economic growth.
D) unemployment.
Answer: A
Diff: 3 Page Ref: 46
Topic: equation of exchange and quantity theory
Special Feature: Key Issue and Question
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
AACSB: Reflective Thinking

14) All of the following took place during the German hyperinflation in the 1920s EXCEPT
A) banks reduced lending.
B) some banks only made loans to customers who agreed to repay in terms of foreign currencies or commodities.
C) Deutsche Bank had to lay off many workers due to lack of business.
D) households and firms increased their demand for loans.
Answer: C
Diff: 2 Page Ref: 44-45
Topic: equation of exchange and quantity theory
Special Feature: Making the Connection: Deutsche Bank During the German Hyperinflation
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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15) Evidence indicates that there's a strong relationship between money and inflation in
A) both the short and long run.
B) neither the short nor the long run.
C) short run, but not the long run.
D) long run, but not the short run.
Answer: D
Diff: 2 Page Ref: 42
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

16) In quantity theory terms, during a hyperinflation
A) money supply increases rapidly, but velocity does not.
B) velocity increases rapidly, but money supply does not.
C) both the money supply and velocity increase rapidly.
D) neither the money supply nor velocity increase rapidly.
Answer: C
Diff: 2 Page Ref: 46
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Reflective Thinking

17) According to the equation of exchange, if nominal GDP increases then
A) the quantity of money must also increase.
B) the velocity of money must also increase.
C) both the quantity of money and the velocity of money must also increase.
D) either the quantity of money and/or the velocity of money must also increase.
Answer: D
Diff: 2 Page Ref: 41-42
Topic: equation of exchange and quantity theory
Special Feature: Solved Problem: Relationship Between Money and Income
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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18) According to the equation of exchange, if the quantity of money decreases and the velocity of money remains constant, then
A) the level of real GDP must decrease.
B) the level of nominal GDP must decrease.
C) the price level must decrease.
D) the level of inflation must increase.
Answer: B
Diff: 2 Page Ref: 41-42
Topic: equation of exchange and quantity theory
Special Feature: Solved Problem: Relationship Between Money and Income
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
AACSB: Reflective Thinking

19) The American Civil War lasted from the spring of 1861 to the spring of 1865. During the war the Confederate government issued substantial amounts of fiat paper currency. What do you think happened to the price level (measured in Confederate dollars) in the Confederate states during the final months of the war?
Answer: During the final months of the war, the imminent demise of the Confederate government greatly reduced the willingness of people to hold Confederate currency. The usefulness of Confederate currency as a store of value and as a standard of deferred payment declined sharply. Those attempting to buy goods and services with the currency had to offer increasing amounts of it in order to find anyone willing to accept it. Or, put another way, the price level rose dramatically, measured in Confederate dollars.
Diff: 2 Page Ref: 44
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Analytical Thinking

20) Make use of the quantity theory of money to solve the following problem. If the Fed has an inflation target of 2% and the velocity of money is constant, by how much should it increase the money supply each year if economic growth is expected to average 3%?
Answer: Since the percent change in the money supply equals the percent change in real GDP plus inflation, the money supply should grow by 2% + 3% = 5%.
Diff: 2 Page Ref: 41
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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21) Make use of the quantity equation to answer the following problem. If the Fed increases the money supply by 4%, velocity increases by 1%, and economic growth is 3%, by how much will the price level increase?
Answer: Since the percent change in the money supply plus the percent change in velocity equals the percent change in real GDP plus the percent change in the price level, the price level will increase by 2% (4% + 1% - 3%).
Diff: 2 Page Ref: 41
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Analytical Thinking

22) Make use of the quantity equation to answer the following problem. If the Fed increases the money supply by 6%, economic growth is 2%, and inflation is 2%, what is happening to the velocity of money? Be specific.
Answer: Since the percent change in the money supply plus the percent change in velocity equals the percent change in real GDP plus the percent change in the price level, velocity is declining by 2%.
Diff: 2 Page Ref: 41
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
*: Recurring
AACSB: Analytical Thinking

23) What is normally the ultimate cause of hyperinflation?
Answer: The ultimate cause of hyperinflation is usually governments spending more than they collect in taxes, which results in government budget deficits. Governments that can't sell bonds to private investors will often sell them to their central banks. In paying for the bonds, the central bank increases the country's money supply. Excessive increases in the money supply result in hyperinflation.
Diff: 2 Page Ref: 44
Topic: equation of exchange and quantity theory
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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24) What does research suggest as to the relationship between the independence of the central bank and inflation? What is the rationale for this relationship?
Answer: Research indicates that the more independent a central bank is from the rest of the government, the lower the country's inflation rate will be. The reason is that an independent central bank is better able to resist political pressures to increase the money supply.
Diff: 2 Page Ref: 46-47
Topic: equation of exchange and quantity theory
Special Feature: Key Issue and Question
Objective: Use the quantity theory of money to analyze the relationship between money and prices in the long run
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