MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

1) The Fed uses three policy tools to manipulate the money supply: _____, which affect reserves and the monetary base; changes in _____, which affect reserves and the monetary base by influencing the quantity of discount loans; and changes in _____, which affect the money multiplier.
   A) open market operations; the discount rate; reserve requirements
   B) the discount rate; open market operations; margin requirements
   C) open market operations; the discount rate; margin requirements
   D) the discount rate; open market operations; reserve requirements

2) The interest rate charged on overnight loans of reserves between banks is the
   A) prime rate.
   B) rediscount rate.
   C) discount rate.
   D) Treasury bill rate.
   E) federal funds rate.

3) The quantity of reserves demanded equals
   A) total reserves minus borrowed reserves.
   B) required reserves plus discount loans.
   C) total reserves minus excess reserves.
   D) excess reserves plus discount loans.
   E) required reserves plus excess reserves.

4) The opportunity cost of holding excess reserves is
   A) the discount rate.
   B) the prime rate.
   C) the federal funds rate.
   D) the mortgage rate.
   E) the Treasury bill rate.

5) In the market for reserves, when the federal funds interest rate is below the discount rate, the supply curve of reserves is
   A) negatively sloped.
   B) horizontal.
   C) vertical.
   D) positively sloped.
   E) backward bending.

6) In the market for reserves, an open market purchase shifts the supply curve to the
   A) right, lowering the federal funds interest rate.
   B) left, lowering the federal funds interest rate.
   C) left, raising the federal funds interest rate.
   D) right, raising the federal funds interest rate.

7) In the market for reserves, an open market _____ shifts the supply curve to the _____, lowering the federal funds interest rate.
   A) purchase; left
   B) sale; left
   C) purchase; right
   D) sale; right

8) In the market for reserves, an open market sale shifts the supply curve to the _____ and causes the federal funds interest rate to _____.

A) right; fall B) left; fall C) right; rise D) left; rise

9) The vertical section of the supply curve of reserves falls when

A) the discount rate increases.
B) the federal funds rate falls.
C) reserve requirements are increases.
D) the discount rate decreases.
E) the federal funds rate rises.

10) In the market for reserves, an increase in the reserve requirement shifts the demand curve to the

A) right and causes the federal funds interest rate to fall.
B) left and causes the federal funds interest rate to fall.
C) right and causes the federal funds interest rate to rise.
D) left and causes the federal funds interest rate to rise.

11) Open market purchases raise the _____ thereby raising the _____.

A) monetary base; money supply B) money multiplier; money supply
C) money multiplier; monetary base D) monetary base; money multiplier

12) Open market sales shrink _____ thereby lowering _____.

A) the money multiplier; the money supply
B) reserves and the monetary base; the money supply
C) the money base; the money multiplier
D) the money multiplier; reserves and the monetary base

13) The two types of open market operations are

A) offensive and defensive.
B) dynamic and defensive.
C) positive and negative.
D) active and passive.
E) dynamic and reactionary.

14) Open market operations as a monetary policy tool have the advantages that

A) they occur at the initiative of the Fed. B) they are easily reversed if mistakes are made.
C) they are flexible and precise. D) all of the above.

15) The Fed's lender–of–last–resort function

A) has proven to be ineffective.
B) cannot prevent runs by large depositors.
C) creates a moral hazard problem.
D) is no longer necessary due to FDIC insurance.
E) all of the above.

16) The most important advantage of discount policy is that the Fed can use it to

A) precisely control the monetary base.
B) punish banks that have deficient reserves.
C) perform its role as lender of last resort.
D) control the money supply.

17) Disadvantages of discount policy include

A) the confusion concerning the Fed's intentions about future monetary policy because of the uncertainty about what a change in the discount rate is intended to signal.
B) its relative imprecision, when compared to open market operations, over control of the money supply.
C) large fluctuations in the volume of discount loans caused by infrequent adjustments in the discount rate to market interest rates.
D) all of the above.
E) only A and B of the above.

18) An increase in reserve requirements reduces the money supply since it causes

A) the money multiplier to fall.
B) reserves and the monetary base to fall.
C) reserves to fall.
D) both A and B of the above.

19) The main advantage of using reserve requirements to control the money supply and interest rates is

A) that raising them can reduce liquidity problems for banks with low excess reserves.
B) that they affect all banks equally and have a powerful effect on the money supply.
C) that they eliminate the need for the Fed to use dynamic open market operations.
D) none of the above.

20) If the Fed wants to drain reserves from the banking system, it will

A) purchase government securities.
B) sell government securities.
C) raise reserve requirements.
D) lower the discount rate.

Answer Key
Testname: CHAPTER 17 PQ.TST

1) A
2) E
3) E
4) C
5) C
6) A
7) C
8) D
9) D
10) C
11) A
12) B
13) B
14) D
15) C
16) C
17) D
18) A
19) B
20) B