Chapter 5
The Behavior of Interest Rates

Multiple Choice

1) If wealth increases, the demand for stocks _____ and that of long-term bonds _____.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: A
   Question Status: Previous Edition

2) If wealth decreases, the demand for stocks _____ and that of long-term bonds _____.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: C
   Question Status: Previous Edition

3) If wealth decreases, the demand for common stocks _____ and that of long-term bonds _____.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: C
   Question Status: Previous Edition

4) A decrease in wealth
   (a) increases the demand for stocks.
   (b) increases the demand for bonds.
   (c) has no effect on bond demand.
   (d) increases the demand for housing.
   (e) reduces the demand for housing.
   Answer: E
   Question Status: New
5) If the expect return on LM stock increases from 3 to 6 percent, and the return on OP stock increases from 6 to 12 percent, the expected return of holding LM stock ________ relative to OP stock and the demand for LM stock _________.
(a) rises; rises
(b) rises; falls
(c) falls; falls
(d) falls; rises
(e) remains unchanged; remains unchanged
Answer: C
Question Status: New

6) If the expected return on ABC stock rises from 5 to 10 percent and the expected return on CBS stock is unchanged, then the expected return of holding CBS stock _____ relative to ABC stock and the demand for CBS stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: D
Question Status: Previous Edition

7) If the expected return on ABC stock falls from 10 to 5 percent and the expected return on CBS stock is unchanged, then the expected return of holding CBS stock _____ relative to ABC stock and the demand for CBS stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: A
Question Status: Revised

8) If the expected return on ABC stock is unchanged and the expected return on CBS stock falls from 10 to 5 percent, then the expected return of holding CBS stock _____ relative to ABC stock and the demand for ABC stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: C
Question Status: Revised
9) If the expected return on NBC stock rises from 5 to 10 percent and the expected return on CBS stock rises from 12 to 18 percent, then the expected return of holding CBS stock _____ relative to NBC stock and the demand for CBS stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: A
Question Status: Previous Edition

10) If the expected return on CBS stock rises from 5 to 10 percent and the expected return on NBC stock rises from 12 to 18 percent, then the expected return of holding CBS stock _____ relative to NBC stock and the demand for CBS stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: D
Question Status: Previous Edition

11) If the expected return on U.S. Treasury bonds falls from 10 to 5 percent and the expected return on GE stock rises from 7 to 8 percent, then the expected return of holding GE stock _____ relative to U.S. Treasury bonds and the demand for GE stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: A
Question Status: Previous Edition

12) If the expected return on U.S. Treasury bonds rises from 5 to 10 percent and the expected return on GE stock rises from 7 to 8 percent, then the expected return of holding GE stock _____ relative to U.S. Treasury bonds and the demand for GE stock _____.
(a) rises; rises
(b) rises; falls
(c) falls; rises
(d) falls; falls
Answer: D
Question Status: Previous Edition
13) If housing prices are suddenly expected to shoot up, then, other things equal, the demand for houses will _____ and that of Treasury bills will _____.
   (a) increase; increase
   (b) increase; decrease
   (c) decrease; decrease
   (d) decrease; increase
   Answer: B
   Question Status: Previous Edition

14) If interest rates on Treasury bonds are suddenly expected to shoot up, then, other things equal, the demand for houses will _____ and that of Treasury bonds will _____.
   (a) increase; increase
   (b) increase; decrease
   (c) decrease; decrease
   (d) decrease; increase
   Answer: B
   Question Status: Previous Edition

15) If interest rates on Treasury bonds are suddenly expected to drop, then, other things equal, the demand for houses will _____ and that of Treasury bonds will _____.
   (a) increase; increase
   (b) increase; decrease
   (c) decrease; decrease
   (d) decrease; increase
   Answer: D
   Question Status: Previous Edition

16) If stock prices are expected to drop dramatically, then, other things equal, the demand for stocks will _____ and that of Treasury bills will _____.
   (a) increase; increase
   (b) increase; decrease
   (c) decrease; decrease
   (d) decrease; increase
   Answer: D
   Question Status: Previous Edition

17) When people begin to expect a large stock market decline, the demand curve for bonds shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: B
   Question Status: Previous Edition
18) When people begin to expect a run up in large stock market, the demand curve for bonds shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: D
   Question Status: Previous Edition

19) If the expected return on RST stock falls from 8 to 5 percent and the expected return on XYZ stock rises from 3 to 4 percent, then the expected return of holding XYZ stock ______ relative to RST stock and demand for XYZ stock ______.
   (a) rises; rises
   (b) rises; falls
   (c) falls; rises
   (d) falls; falls
   Answer: A
   Question Status: Previous Edition

20) If the expected return on RST stock declines from 12 to 9 percent and the expected return on XYZ stock declines from 8 to 7 percent, then the expected return of holding RST stock ______ relative to XYZ stock and demand for XYZ stock _____.
   (a) rises; rises
   (b) rises; falls
   (c) falls; rises
   (d) falls; falls
   Answer: C
   Question Status: Previous Edition

21) If the expected return on U.S. Treasury bonds falls from 8 to 7 percent and the expected return on corporate bonds falls from 10 to 8 percent, then the expected return of corporate bonds ______ relative to U.S. Treasury bonds and the demand for corporate bonds _____.
   (a) rises; rises
   (b) rises; falls
   (c) falls; rises
   (d) falls; falls
   Answer: D
   Question Status: Previous Edition

22) For a holding period of one year the expected return on a consol is _____ the higher is the price of the consol today, and _____ the higher is the price of the consol next year.
   (a) higher; higher
   (b) higher; lower
   (c) lower; higher
   (d) lower; lower
   Answer: C
   Question Status: Previous Edition
23) Holding the expected return on bonds constant, an increase in the expected return on common stocks would _____ the demand for bonds, shifting the demand curve to the _____.
   (a) decrease; left
   (b) decrease; right
   (c) increase; left
   (d) increase; right
   Answer: A
   Question Status: Previous Edition

24) Holding the expected return on bonds constant, a decrease in the expected return on stocks would _____ the demand for bonds, shifting the demand curve to the _____.
   (a) decrease; left
   (b) decrease; right
   (c) increase; left
   (d) increase; right
   Answer: D
   Question Status: Previous Edition

25) As the price of a bond falls and the expected return _____, bonds become _____ attractive to investors.
   (a) falls; less
   (b) falls; more
   (c) rises; less
   (d) rises; more
   Answer: D
   Question Status: Previous Edition

26) As the price of a bond _____ and the expected return _____, bonds become more attractive to investors and the quantity demanded rises.
   (a) falls; rises
   (b) falls; falls
   (c) rises; rises
   (d) rises; falls
   Answer: A
   Question Status: Previous Edition

27) If interest rates are expected to rise in the future, the demand for long-term bonds _____ and the demand curve shifts to the _____.
   (a) rises; right
   (b) rises; left
   (c) falls; right
   (d) falls; left
   Answer: D
   Question Status: Previous Edition
28) If interest rates are expected to fall in the future, the demand for long-term bonds today _____ and the demand curve shifts to the _____.
   (a) rises; right
   (b) rises; left
   (c) falls; right
   (d) falls; left
   Answer: A
   Question Status: Previous Edition

29) Higher expected interest rates in the future ____ the demand for long-term bonds today and shift the demand curve to the _____.
   (a) increase; left
   (b) increase; right
   (c) decrease; left
   (d) decrease; right
   Answer: C
   Question Status: Previous Edition

30) Lower expected interest rates in the future ____ the demand for long-term bonds today and shift the demand curve to the _____.
   (a) increase; left
   (b) increase; right
   (c) decrease; left
   (d) decrease; right
   Answer: B
   Question Status: Previous Edition

31) The reduction of brokerage commissions for trading common stocks that occurred in 1975 caused the demand for bonds to _____ and the demand curve to shift to the _____.
   (a) fall; right
   (b) fall, left
   (c) rise; right
   (d) rise; left
   Answer: B
   Question Status: Previous Edition

32) If fluctuations in interest rates become smaller, then, other things equal, the demand for stocks _____ and the demand for long-term bonds ______.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: D
   Question Status: Previous Edition
33) If fluctuations in interest rates become larger, then, other things equal, the demand for stocks _____ and the demand for long-term bonds _____.
   (a) increases; increases 
   (b) increases; decreases 
   (c) decreases; decreases 
   (d) decreases; increases 
   Answer: B
   Question Status: Previous Edition

34) If the price of gold becomes more volatile, then, other things equal, the demand for stocks will _____ and the demand for antiques will _____.
   (a) increase; increase 
   (b) increase; decrease 
   (c) decrease; decrease 
   (d) decrease; increase 
   Answer: A
   Question Status: Previous Edition

35) If the price of gold becomes less volatile, then, other things equal, the demand for stocks will _____ and the demand for antiques will _____.
   (a) increase; increase 
   (b) increase; decrease 
   (c) decrease; decrease 
   (d) decrease; increase 
   Answer: C
   Question Status: Previous Edition

36) If fluctuations in interest rates become greater, then, other things equal, the demand for common stocks _____ and that of long-term bonds _____.
   (a) increases; increases 
   (b) increases; decreases 
   (c) decreases; decreases 
   (d) decreases; increases 
   Answer: B
   Question Status: Previous Edition

37) If interest rates become more stable, then, other things equal, the demand for common stocks _____ and that of long-term bonds _____.
   (a) increases; increases 
   (b) increases; decreases 
   (c) decreases; decreases 
   (d) decreases; increases 
   Answer: D
   Question Status: Previous Edition
38) If the price of real estate becomes less volatile, then, other things equal, the demand for stocks will _____ and that of antiques will _____.
(a) increase; increase
(b) increase; decrease
(c) decrease; decrease
(d) decrease; increase
Answer: C
Question Status: Previous Edition

39) When stock prices become less volatile, the demand curve for bonds shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; falls
(c) left; falls
(d) left; rises
Answer: D
Question Status: Previous Edition

40) When stock prices become _____ volatile, the demand curve for bonds shifts to the _____ and the interest rate _____.
(a) more; right; rises
(b) more; left; falls
(c) less; left; falls
(d) less; left; rises
(e) less; right; falls
Answer: D
Question Status: Previous Edition

41) When stock prices become more volatile, the demand curve for bonds shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; falls
(c) left; falls
(d) left; rises
Answer: B
Question Status: Previous Edition

42) When stock prices become _____ volatile, the demand curve for bonds shifts to the _____ and the interest rate _____.
(a) more; right; rises
(b) more; left; falls
(c) less; left; falls
(d) less; left; rises
(e) more; right; falls
Answer: E
Question Status: Previous Edition
43) All else the same, an increase in the volatility of the stock market causes the demand for bonds to _____ and the demand curve to shift to the _____.
(a) fall; right
(b) fall; left
(c) rise; right
(d) rise; left
Answer: C
Question Status: Previous Edition

44) All else the same, a decrease in the volatility of the stock market causes the demand for bonds to _____ and the demand curve to shift to the _____.
(a) fall; right
(b) fall; left
(c) rise; right
(d) rise; left
Answer: B
Question Status: Previous Edition

45) When bond interest rates become more volatile, the demand for bonds _____ and the interest rate _____.
(a) increases; rises
(b) increases; falls
(c) decreases; falls
(d) decreases; rises
Answer: D
Question Status: Previous Edition

46) When bond interest rates become less volatile, the demand for bonds _____ and the interest rate _____.
(a) increases; rises
(b) increases; falls
(c) decreases; falls
(d) decreases; rises
Answer: B
Question Status: Previous Edition

47) An increase in the riskiness of bonds relative to alternative assets causes the demand for bonds to _____ and the demand curve to shift to the _____.
(a) rise; right
(b) rise; left
(c) fall; right
(d) fall; left
Answer: D
Question Status: Previous Edition
48) An increase in the riskiness of alternative assets relative to bonds causes the demand for bonds to _______ and the demand curve to shift to the _____.
   (a) rise; right
   (b) rise; left
   (c) fall; right
   (d) fall; left
   Answer: A
   Question Status: Previous Edition

49) When rare coin prices become volatile, the _________ curve for bonds shifts to the ________.
   (a) demand; right
   (b) demand; left
   (c) supply; right
   (d) supply; left
   (e) supply and demand; left
   Answer: A
   Question Status: Study Guide

50) When bonds become more widely traded, and as a consequence the market becomes more liquid, the demand curve for bonds shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: B
   Question Status: Previous Edition

51) When bonds become less widely traded, and as a consequence the market becomes less liquid, the demand curve for bonds shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: D
   Question Status: Previous Edition

52) An increase in the liquidity of bonds results in a _____ in demand for bonds and the demand curve shifts to the _____.
   (a) rise; right
   (b) rise; left
   (c) fall; right
   (d) fall; left
   Answer: A
   Question Status: Previous Edition
53) Increased liquidity of alternative assets _____ the demand for bonds and shifts the demand curve to the _____.
   (a) lowers; right
   (b) lowers; left
   (c) raises; right
   (d) raises; left
   Answer: B

54) An increase in the expected rate of inflation will _____ the expected return on bonds relative to the that on _____ assets.
   (a) reduce; financial
   (b) reduce; real
   (c) raise; financial
   (d) raise; real
   Answer: B

55) An increase in the expected rate of inflation will _____ the expected return on bonds relative to the that on _____ assets, and shift the _____ curve to the left.
   (a) reduce; financial; demand
   (b) reduce; real; demand
   (c) raise; financial; supply
   (d) raise; real; supply
   Answer: B

56) A decrease in the expected rate of inflation will _____ the expected return on bonds relative to the that on _____ assets.
   (a) reduce; financial
   (b) reduce; real
   (c) raise; financial
   (d) raise; real
   Answer: D

57) A decrease in the expected rate of inflation will _____ the expected return on bonds relative to the that on _____ assets, and shift the _____ curve to the left.
   (a) reduce; financial; demand
   (b) reduce; real; demand
   (c) raise; financial; supply
   (d) raise; real; supply
   (e) raise; real; demand
   Answer: E
58) An increase in the expected rate of inflation causes the demand for bonds to _____ and the demand curve to shift to the _____.
(a) fall; right
(b) fall; left
(c) rise; right
(d) rise; left
Answer: B
Question Status: Previous Edition

59) A decrease in the expected rate of inflation causes the demand for bonds to _____ and the demand curve to shift to the _____.
(a) fall; right
(b) fall; left
(c) rise; right
(d) rise; left
Answer: C
Question Status: Previous Edition

60) The demand curve for bonds has the usual downward slope, indicating that at _____ prices of the bond, everything else equal, the _____ is higher.
(a) higher; demand
(b) higher; quantity demanded
(c) lower; demand
(d) lower; quantity demanded
Answer: D
Question Status: Previous Edition

61) Factors that increase the demand for bonds include
(a) an increase in the inflation rate.
(b) an increase in the liquidity of common stocks.
(c) a decrease in the volatility of stock prices.
(d) all of the above.
(e) none of the above.
Answer: E
Question Status: Previous Edition

62) Factors that increase the demand for bonds include
(a) an increase in the inflation rate.
(b) an decrease in the liquidity of common stocks.
(c) a decrease in the volatility of stock prices.
(d) all of the above.
Answer: B
Question Status: Previous Edition
63) Factors that increase the demand for bonds include
(a) a decrease in the inflation rate.
(b) an increase in the liquidity of stocks.
(c) a decrease in the volatility of stock prices.
(d) all of the above.
(e) none of the above.
Answer: A  
Question Status: Previous Edition

64) Factors that increase the demand for bonds include
(a) a decrease in the inflation rate.
(b) an increase in the volatility of stock prices.
(c) an increase in the liquidity of stocks.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: E  
Question Status: Previous Edition

65) Factors that increase the demand for bonds include
(a) an increase in the volatility of stock prices.
(b) a decrease in the expected returns on stocks.
(c) a decrease in the inflation rate.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: D  
Question Status: Previous Edition

66) Factors that increase the demand for bonds include
(a) an increase in the volatility of stock prices.
(b) an increase in the expected returns on stocks.
(c) an increase in the inflation rate.
(d) only (b) and (c) of the above.
Answer: A  
Question Status: Previous Edition

67) Factors that decrease the demand for bonds include
(a) an increase in the volatility of stock prices.
(b) a decrease in the expected returns on stocks.
(c) a decrease in the inflation rate.
(d) all of the above.
(e) none of the above.
Answer: E  
Question Status: Previous Edition
68) Factors that decrease the demand for bonds include
   (a) an increase in the volatility of stock prices.
   (b) an increase in the expected returns on stocks.
   (c) a decrease in the inflation rate.
   (d) all of the above.
   Answer: B

69) Factors that decrease the demand for bonds include
   (a) an increase in the volatility of stock prices.
   (b) a decrease in the expected returns on stocks.
   (c) a decrease in the inflation rate.
   (d) a decrease in the riskiness of stocks.
   Answer: D

70) Factors that decrease the demand for bonds include
   (a) an increase in the inflation rate.
   (b) an increase in the liquidity of stocks.
   (c) a decrease in the volatility of stock prices.
   (d) all of the above.
   (e) none of the above.
   Answer: D

71) Factors that decrease the demand for bonds include
   (a) an increase in the liquidity of stocks.
   (b) a decrease in the volatility of stock prices.
   (c) a decrease in the inflation rate.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: E

72) Factors that decrease the demand for bonds include
   (a) a decrease in the inflation rate.
   (b) an increase in the volatility of stock prices.
   (c) an increase in the liquidity of stocks.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: C
73) Factors that decrease the demand for bonds include
   (a) a decrease in the inflation rate.
   (b) an increase in the volatility of stock prices.
   (c) an increase in the federal government budget deficit.
   (d) an increase in the liquidity of stocks.
   Answer: D
   Question Status: Previous Edition

74) The demand for Jackson Pollack paintings rises (holding everything else equal) when:
   (a) stocks become easier to sell.
   (b) people expect a boom in real estate prices.
   (c) Treasury securities become riskier.
   (d) people suddenly expect gold prices to rise.
   Answer: C
   Question Status: Previous Edition

75) The demand for Charles M. Russell paintings declines (holding everything else equal) when:
   (a) stocks become easier to sell.
   (b) people expect a boom in real estate prices.
   (c) Treasury securities become riskier.
   (d) all of the above occur.
   (e) both (a) and (b) of the above occur.
   Answer: E
   Question Status: Previous Edition

76) The demand for Charles M. Russell paintings declines (holding everything else equal) when:
   (a) stocks become easier to sell.
   (b) people expect a boom in real estate prices.
   (c) people suddenly expect gold prices to rise.
   (d) all of the above occur.
   (e) both (a) and (b) of the above occur.
   Answer: D
   Question Status: Previous Edition

77) The demand for silver bullion decreases, other things equal, when
   (a) the gold market is suddenly expected to boom.
   (b) the market for silver bullion becomes more liquid.
   (c) wealth grows rapidly.
   (d) any of the above occurs.
   Answer: A
   Question Status: Previous Edition
78) The demand for silver bullion increases, other things equal, when
   (a) the gold market is suddenly expected to boom.
   (b) the market for silver bullion becomes more liquid.
   (c) wealth grows rapidly.
   (d) any of the above occurs.
   (e) either (b) or (c) of the above occurs.
   Answer: E
   Question Status: Previous Edition

79) You would be more willing to purchase U.S. Treasury bonds, other things equal, if
   (a) you inherit $1 million from your Uncle Harry.
   (b) you expect interest rates to fall.
   (c) gold becomes more liquid.
   (d) any of the above occurs.
   (e) either (a) or (b) of the above occurs.
   Answer: E
   Question Status: Previous Edition

80) You would be more willing to purchase U.S. Treasury bonds, other things equal, if
   (a) you inherit $1 million from your Uncle Harry.
   (b) you expect interest rates to rise.
   (c) gold becomes more liquid.
   (d) any of the above occurs.
   (e) either (b) or (c) of the above occurs.
   Answer: A
   Question Status: Previous Edition

81) You would be less willing to purchase U.S. Treasury bonds, other things equal, if
   (a) you inherit $1 million from your Uncle Harry.
   (b) you expect interest rates to fall.
   (c) gold becomes more liquid.
   (d) any of the above occurs.
   Answer: C
   Question Status: Previous Edition

82) You would be less willing to purchase U.S. Treasury bonds, other things equal, if
   (a) brokerage fees for trading stocks decline.
   (b) you expect interest rates to rise.
   (c) gold becomes more liquid.
   (d) any of the above occurs.
   (e) either (b) or (c) of the above occurs.
   Answer: D
   Question Status: Previous Edition
83) You would be more willing to buy AT&T bonds (holding everything else constant) if
(a) the brokerage commissions on bond sales become cheaper.
(b) interest rates are expected to rise.
(c) you had suffered big losses in the stock market.
(d) you expected jewelry to appreciate sharply in value.
(e) none of the above.
Answer: A

Question Status: Previous Edition

84) You would be less willing to buy AT&T bonds (holding everything else constant) if
(a) the brokerage commissions on bond sales rise.
(b) interest rates are expected to rise.
(c) you expected jewelry to appreciate sharply in value.
(d) any of the above occurs.
(e) either (a) or (c) of the above occurs.
Answer: D

Question Status: Previous Edition

85) Holding everything else constant,
(a) if asset A’s risk rises relative to that of alternative assets, the demand for asset A will fall.
(b) the more liquid asset A, relative to alternative assets, the greater will be the demand for asset A.
(c) the lower the expected return to asset A relative to alternative assets, the greater will be the demand for asset A.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: E

Question Status: Previous Edition

86) Holding everything else constant,
(a) if stock ABC’s risk rises relative to that of alternative assets, the demand for stock ABC will fall.
(b) the less liquid is stock ABC, relative to alternative assets, the greater will be the demand for stock ABC.
(c) the lower the expected return to stock ABC relative to alternative assets, the greater will be the demand for stock ABC.
(d) only (a) and (b) of the above.
Answer: A

Question Status: Previous Edition
87) Holding everything else constant,
(a) if the risk of XYZ stock rises relative to that of alternative assets, the demand for XYZ stock will fall.
(b) the more liquid is stock XYZ, relative to alternative assets, the greater will be the demand for stock XYZ.
(c) the higher the expected return to stock XYZ relative to alternative assets, the greater will be the demand for stock XYZ.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: D
Question Status: Previous Edition

88) Holding everything else constant,
(a) if asset A’s risk rises relative to that of alternative assets, the demand will increase for asset A.
(b) the more liquid is asset A, relative to alternative assets, the greater will be the demand for asset A.
(c) the lower the expected return to asset A relative to alternative assets, the greater will be the demand for asset A.
(d) only (a) and (b) of the above.
Answer: B
Question Status: Previous Edition

89) The demand for gold bullion increases, other things equal, when
(a) the market for silver bullion becomes more liquid.
(b) interest rates are expected to rise.
(c) interest rates are expected to fall.
(d) either (a) or (b) of the above occurs.
Answer: B
Question Status: Previous Edition

90) You would be less willing to purchase U.S. Treasury bonds, other things equal, if
(a) you expect interest rates to fall.
(b) gold becomes more liquid.
(c) you expect bond prices to rise.
(d) either (a) or (b) of the above occurs.
Answer: B
Question Status: Previous Edition

91) You would be less willing to purchase U.S. Treasury bonds, other things equal, if
(a) you expect interest rates to rise.
(b) gold becomes more liquid.
(c) you expect bond prices to rise.
(d) either (a) or (b) of the above occurs.
Answer: D
Question Status: Previous Edition
92) You would be less willing to purchase U.S. Treasury bonds, other things equal, if
   (a) you expect interest rates to rise.
   (b) gold becomes more liquid.
   (c) you inherit $1 million from your Uncle Harry.
   (d) any of the above occurs.
   (e) either (a) or (b) of the above occurs.
   Answer: E

93) The theory of asset demand provides a framework for deciding what factors cause the demand curve for bonds shift. These factors include changes in the
   (a) wealth of investors.
   (b) liquidity of bonds relative to alternative assets.
   (c) expected returns on bonds relative to alternative assets.
   (d) risk of bonds relative to alternative assets.
   (e) all of the above.
   Answer: E

94) In a recession when income and wealth are falling, the demand for bonds _____ and the demand curve shifts to the _____.
   (a) falls; right
   (b) falls; left
   (c) rises; right
   (d) rises; left
   Answer: B

95) During business cycle expansions when income and wealth are rising, the demand for bonds _____ and the demand curve shifts to the _____.
   (a) falls; right
   (b) falls; left
   (c) rises; right
   (d) rises; left
   Answer: C

96) In an expanding economy with growing wealth, the demand for bonds _____ and the demand curve for bonds shifts to the _____.
   (a) rises; right
   (b) rises; left
   (c) falls; right
   (d) falls; left
   Answer: A
97) In a contracting economy with declining wealth, the demand for bonds _____ and the demand curve for bonds shifts to the _____.
(a) rises; right
(b) rises; left
(c) falls; right
(d) falls; left
Answer: D
Question Status: Previous Edition

98) In an expanding economy with growing wealth, the demand for bonds _____ and the demand curve for bonds shifts to the _____.
(a) rises; right
(b) rises; left
(c) falls; right
(d) falls; left
Answer: A
Question Status: Previous Edition

99) In a contracting economy with declining wealth, the demand for bonds _____ and the demand curve for bonds shifts to the _____.
(a) rises; right
(b) rises; left
(c) falls; right
(d) falls; left
Answer: D
Question Status: Previous Edition

100) The supply curve for bonds has the usual upward slope, indicating that as the price _____, ceteris paribus, the _____ increases.
(a) falls; supply
(b) falls; quantity supplied
(c) rises; supply
(d) rises; quantity supplied
Answer: D
Question Status: Previous Edition

101) Factors that can cause the supply curve for bonds to shift to the right include
(a) an expansion in overall economic activity.
(b) an increase in expected inflation.
(c) an increase in government deficits.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: D
Question Status: Previous Edition
102) Factors that can cause the supply curve for bonds to shift to the right include
   (a) an expansion in overall economic activity.
   (b) an increase in expected inflation.
   (c) a decrease in government deficits.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: E
   Question Status: Previous Edition

103) Factors that can cause the supply curve for bonds to shift to the right include
   (a) an expansion in overall economic activity.
   (b) a decrease in expected inflation.
   (c) a decrease in government deficits.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: A
   Question Status: Previous Edition

104) Factors that can cause the supply curve for bonds to shift to the left include
   (a) a decrease in expected inflation.
   (b) a decrease in government deficits.
   (c) an expansion in overall economic activity.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: E
   Question Status: Previous Edition

105) Factors that can cause the supply curve for bonds to shift to the left include
   (a) an expansion in overall economic activity.
   (b) a decrease in expected inflation.
   (c) an increase in government deficits.
   (d) only (a) and (c) of the above.
   Answer: B
   Question Status: Previous Edition

106) Factors that can cause the supply curve for bonds to shift to the left include
   (a) an expansion in overall economic activity.
   (b) an increase in expected inflation.
   (c) a decrease in government deficits.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: C
   Question Status: Previous Edition
107) During an economic expansion, the supply of bonds _____ and the supply curve shifts to the _____.
   (a) increases; left
   (b) increases; right
   (c) decreases; left
   (d) decreases; right
   Answer: B
   Question Status: Previous Edition

108) During a recession, the supply of bonds _____ and the supply curve shifts to the _____.
   (a) increases; left
   (b) increases; right
   (c) decreases; left
   (d) decreases; right
   Answer: C
   Question Status: Previous Edition

109) An increase in expected inflation causes the supply of bonds to _____ and the supply curve to shift to the _____.
   (a) increase; left
   (b) increase; right
   (c) decrease; left
   (d) decrease; right
   Answer: B
   Question Status: Previous Edition

110) Higher government deficits _____ the supply of bonds and shift the supply curve to the _____.
   (a) increase; left
   (b) increase; right
   (c) decrease; left
   (d) decrease; right
   Answer: B
   Question Status: Previous Edition

111) When the inflation rate is expected to increase, the expected return on bonds relative to real assets falls for any given interest rate; the demand for bonds _____ and the demand curve shifts to the _____.
   (a) rises; right
   (b) rises; left
   (c) falls; right
   (d) falls; left
   Answer: D
   Question Status: Previous Edition
112) When the inflation rate is expected to increase, the real cost of borrowing declines at any given interest rate; the supply of bonds _____ increases and the supply curve shifts to the _____.
(a) increases; left
(b) increases; right
(c) decreases; left
(d) decreases; right
Answer: B
Question Status: Previous Edition

113) When the inflation rate is expected to increase, the expected return on bonds relative to real assets falls for any given interest rate; the _____ for bonds falls and the _____ curve shifts to the left.
(a) demand; demand
(b) demand; supply
(c) supply; demand
(d) supply; supply
Answer: A
Question Status: Previous Edition

114) When the inflation rate is expected to increase, the real cost of borrowing declines at any given interest rate; the _____ of bonds increases and the _____ curve shifts to the right.
(a) demand; demand
(b) demand; supply
(c) supply; demand
(d) supply; supply
Answer: D
Question Status: Previous Edition

115) An increase in the expected rate of inflation causes the demand curve for bonds to _____ and the supply curve of bonds to _____.
(a) fall; fall
(b) fall; rise
(c) rise; fall
(d) rise; rise
Answer: B
Question Status: Previous Edition

116) A decrease in the expected rate of inflation causes the demand curve for bonds to _____ and the supply curve of bonds to _____.
(a) fall; fall
(b) fall; rise
(c) rise; fall
(d) rise; rise
Answer: C
Question Status: Previous Edition
117) When the inflation rate is expected to increase, the _____ for bonds falls, while the _____ curve shifts to the right.
(a) demand; demand
(b) demand; supply
(c) supply; demand
(d) supply; supply
Answer: B
Question Status: Previous Edition

118) When the inflation rate is expected to increase, the _____ of bonds increases while the _____ curve shifts to the left.
(a) demand; demand
(b) demand; supply
(c) supply; demand
(d) supply; supply
Answer: C
Question Status: Previous Edition

119) A decrease in expected inflation shifts the demand for bonds to the ________, the supply of bonds to the ________, and the interest rate ________.
(a) right; right; rises
(b) right; left; rises
(c) right; left; falls
(d) left; left; falls
(e) left; right; rises
Answer: C
Question Status: Study Guide

120) When the inflation rate is expected to rise, interest rates will ____; this result has been termed the _____.
(a) fall; Keynes effect
(b) fall; Fisher effect
(c) rise; Pigou effect
(d) rise; Fisher effect
(e) rise; Keynes effect
Answer: D
Question Status: Previous Edition

121) Expectations of inflation have a major impact on bond prices and interest rates through the
(a) Keynes effect.
(b) Gibson effect.
(c) Pigou effect.
(d) Fisher effect.
Answer: D
Question Status: Previous Edition
122) The economist Irving Fisher, after whom the Fisher effect is named, explained why interest rates _____ as the expected rate of inflation _____.
   (a) rise; increases
   (b) rise; stabilizes
   (c) rise; decreases
   (d) fall; increases
   (e) fall; stabilizes
   Answer: A
   Question Status: Previous Edition

123) During a business cycle expansion, the supply of bonds shifts to the _____ as businesses perceive more profitable investment opportunities, while the demand for bonds shifts to the _____ as a result of the increase in wealth generated by the economic expansion.
   (a) right; left
   (b) right; right
   (c) left; left
   (d) left; right
   Answer: B
   Question Status: Previous Edition

124) During a business cycle contraction, the supply of bonds shifts to the _____ as businesses perceive fewer profitable investment opportunities, while the demand for bonds shifts to the _____ as a result of the decrease in wealth.
   (a) right; left
   (b) right; right
   (c) left; left
   (d) left; right
   Answer: C
   Question Status: Previous Edition

125) When the price of a bond is above the equilibrium price, there is an excess _____ for (of) bonds and price will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   Answer: C
   Question Status: Previous Edition

126) When the price of a bond is below the equilibrium price, there is an excess _____ for (of) bonds and price will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   Answer: A
   Question Status: Previous Edition
127) When the price of a bond is _____ the equilibrium price, there is an excess supply of bonds and price will _____.
   (a) above; rise
   (b) above; fall
   (c) below; fall
   (d) below; rise
   Answer: B
   Question Status: Previous Edition

128) When the price of a bond is _____ the equilibrium price, there is an excess demand of bonds and price will _____.
   (a) above; rise
   (b) above; fall
   (c) below; fall
   (d) below; rise
   Answer: D
   Question Status: Previous Edition

129) When the price of a bond is _____ the equilibrium price, there is an excess _____ for (of) bonds and price will _____.
   (a) below; demand; rise
   (b) below; demand; fall
   (c) below; supply; fall
   (d) above; supply; rise
   Answer: A
   Question Status: Previous Edition

130) When the interest rate on a bond is above the equilibrium interest rate, in the bond market there is excess _____ and the interest rate will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   Answer: B
   Question Status: Previous Edition

131) When the interest rate on a bond is below the equilibrium interest rate, in the bond market there is excess _____ and the interest rate will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   Answer: D
   Question Status: Previous Edition
132) When the interest rate on a bond is ______ the equilibrium interest rate, in the bond market there is excess _____ and the interest rate will _____.
   (a) above; demand; rise
   (b) above; demand; fall
   (c) below; supply; fall
   (d) above; supply; rise
   Answer: B
   Question Status: Previous Edition

133) When the interest rate on a bond is _____ the equilibrium interest rate, in the bond market there is excess _____ and the interest rate will _____.
   (a) below; demand; rise
   (b) below; demand; fall
   (c) below; supply; fall
   (d) above; supply; rise
   (e) below; supply; rise
   Answer: E
   Question Status: Previous Edition

134) A situation in which the quantity of bonds supplied exceeds the quantity of bonds demanded is called a condition of excess supply; because people want to sell _____ bonds than others want to buy, the price of bonds will ______.
   (a) fewer; fall
   (b) fewer; rise
   (c) more; fall
   (d) more; rise
   Answer: C
   Question Status: Previous Edition

135) If the price of bonds is set _____ the equilibrium price, the quantity of bonds demanded exceeds the quantity of bonds supplied, a condition called excess _____.
   (a) above; demand
   (b) above; supply
   (c) below; demand
   (d) below; supply
   Answer: C
   Question Status: Previous Edition

136) If the price of bonds is _____ the equilibrium price, the quantity of bonds supplied exceeds the quantity of bonds demanded, a condition called excess _____.
   (a) above; demand
   (b) above; supply
   (c) below; demand
   (d) below; supply
   Answer: B
   Question Status: Previous Edition
137) When the interest rate changes,
   (a) the demand curve for bonds shifts to the right.
   (b) the demand curve for bonds shifts to the left.
   (c) the supply curve for bonds shifts to the right.
   (d) the supply curve for bonds shifts to the left.
   (e) none of the above occurs.
   Answer: E
   Question Status: Previous Edition

138) When the interest rate changes,
   (a) the demand curve for bonds shifts to the right.
   (b) the demand curve for bonds shifts to the left.
   (c) the supply curve for bonds shifts to the right.
   (d) it is because either the demand or the supply curve has shifted.
   Answer: D
   Question Status: Previous Edition

139) When the interest rate rises, either the demand for bonds ______ or the supply of bonds ______.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: D
   Question Status: Previous Edition

140) When the interest rate falls, either the demand for bonds ______ or the supply of bonds ______.
   (a) increases; increases
   (b) increases; decreases
   (c) decreases; decreases
   (d) decreases; increases
   Answer: B
   Question Status: Previous Edition

141) A decrease in the brokerage commissions in the housing market from 6 to 5% of the sales price will shift the ________ curve for bonds to the ________.
   (a) demand; right
   (b) demand; left
   (c) supply; right
   (d) supply; left
   (e) does not affect the demand or supply of bonds
   Answer: B
   Question Status: Study Guide
142) When people revise upward their expectations of future interest rates, the _____ curve for bonds shifts to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: B
   Question Status: Previous Edition

143) When people expect interest rates to rise in the future, the _____ curve for bonds shifts to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: B
   Question Status: Previous Edition

144) When people expect interest rates to fall in the future, the _____ curve for bonds shifts to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: A
   Question Status: Previous Edition

145) If people expect real estate prices to increase significantly, the _____ curve for bonds will shift to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: B
   Question Status: Previous Edition

146) If people expect real estate prices to decrease significantly, the _____ curve for bonds will shift to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: A
   Question Status: Previous Edition
147) When stock prices become more volatile, the ______ curve for bonds shifts to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: A
   Question Status: Previous Edition

148) When stock prices become less volatile, the ______ curve for bonds shifts to the _____.
   (a) demand; right
   (b) demand; left
   (c) supply; left
   (d) supply; right
   Answer: B
   Question Status: Previous Edition

149) When prices in the art market become more uncertain,
   (a) the demand curve for bonds shifts to the left and the interest rate rises.
   (b) the demand curve for bonds shifts to the left and the interest rate falls.
   (c) the demand curve for bonds shifts to the right and the interest rate rises.
   (d) the supply curve for bonds shifts to the right and the interest rate falls.
   (e) none of the above occurs.
   Answer: E
   Question Status: Previous Edition

150) When prices in the art market become more uncertain,
   (a) the demand curve for bonds shifts to the left and the interest rate rises.
   (b) the demand curve for bonds shifts to the left and the interest rate falls.
   (c) the demand curve for bonds shifts to the right and the interest rate falls.
   (d) the supply curve for bonds shifts to the right and the interest rate falls.
   Answer: C
   Question Status: Previous Edition

151) When prices in the art market become less uncertain,
   (a) the demand curve for bonds shifts to the left and the interest rate falls.
   (b) the demand curve for bonds shifts to the right and the interest rate rises.
   (c) the supply curve for bonds shifts to the right and the interest rate falls.
   (d) none of the above occurs.
   Answer: D
   Question Status: Previous Edition
152) When prices in the art market become less uncertain,
   (a) the demand curve for bonds shifts to the left and the interest rate rises.
   (b) the demand curve for bonds shifts to the left and the interest rate falls.
   (c) the demand curve for bonds shifts to the right and the interest rate falls.
   (d) the supply curve for bonds shifts to the right and the interest rate falls.
   Answer: A
   Question Status: Previous Edition

153) When prices in the stock market become more uncertain, the demand curve for bonds shifts to the
     _____ and the interest rate _____.
     (a) right; rises
     (b) right; falls
     (c) left; falls
     (d) left; rises
     Answer: B
     Question Status: Previous Edition

154) When prices in the stock market become less uncertain, the demand curve for bonds shifts to the
     _____ and the interest rate _____.
     (a) right; rises
     (b) right; falls
     (c) left; falls
     (d) left; rises
     Answer: D
     Question Status: Previous Edition

155) When the federal government’s budget deficit increases, the _____ curve for bonds shifts to the
     _____.
     (a) demand; right
     (b) demand; left
     (c) supply; left
     (d) supply; right
     Answer: D
     Question Status: Previous Edition

156) When the federal government’s budget deficit decreases, the _____ curve for bonds shifts to the
     _____.
     (a) demand; right
     (b) demand; left
     (c) supply; left
     (d) supply; right
     Answer: C
     Question Status: Previous Edition
157) When the expected inflation rate increases, the demand for bonds _____, the supply of bonds _____, and the interest rate ______.
(a) increases; increases; rises
(b) decreases; decreases; falls
(c) increases; decreases; falls
(d) decreases; increases; rises
Answer: D
Question Status: Previous Edition

158) When the expected inflation rate decreases, the demand for bonds _____, the supply of bonds _____, and the interest rate ______.
(a) increases; increases; rises
(b) decreases; decreases; falls
(c) increases; decreases; falls
(d) decreases; increases; rises
Answer: C
Question Status: Previous Edition

159) When a recession occurs, normally the demand for bonds _____ and the supply of bonds _____.
(a) increases; increases
(b) increases; decreases
(c) decreases; decreases
(d) decreases; increases
Answer: C
Question Status: Previous Edition

160) When an economy grows out of a recession, normally the demand for bonds _____ and the supply of bonds _____.
(a) increases; increases
(b) increases; decreases
(c) decreases; decreases
(d) decreases; increases
Answer: A
Question Status: Previous Edition

161) When the economy slips into a recession, normally the demand for bonds _____, the supply of bonds _____, and the interest rate _____.
(a) increases; increases; rises
(b) decreases; decreases; falls
(c) increases; decreases; falls
(d) decreases; increases; rises
Answer: B
Question Status: Previous Edition
162) When the economy enters into a boom, normally the demand for bonds _____, the supply of bonds _____, and the interest rate _____.
   (a) increases; increases; rises
   (b) decreases; decreases; falls
   (c) increases; decreases; rises
   (d) decreases; increases; rises
   Answer: A
   Question Status: Previous Edition

163) In a recession, bond demand shifts to the _______, bond supply shifts to the _______, and the interest rate _____.
   (a) right; right; rises
   (b) right; left; falls
   (c) left; left; falls
   (d) left; right; rises
   (e) left; right; falls
   Answer: C
   Question Status: Study Guide

164) In the 1990s Japan had the lowest interest rates in the world due to a combination of
   (a) inflation and recession.
   (b) deflation and expansion.
   (c) inflation and expansion.
   (d) deflation and recession.
   (e) disinflation and expansion.
   Answer: D
   Question Status: New

165) Deflation causes the demand for bonds to ________, the supply of bonds to _______, and interest rates to_______.
   (a) increase; increase; increase
   (b) increase; decrease; decrease
   (c) decrease; increase; increase
   (d) decrease; decrease; increase
   (e) decrease; decrease; decrease
   Answer: B
   Question Status: New

166) Deflation causes the demand for bonds to ________, the supply of bonds to _______, and bond prices to_______.
   (a) increase; increase; increase
   (b) increase; decrease; increase
   (c) decrease; increase; increase
   (d) decrease; decrease; increase
   (e) decrease; decrease; decrease
   Answer: B
   Question Status: New
167) Deflation causes the _____ bonds to increase, the _____ bonds to decrease, and _____ to decrease.
   (a) supply of; demand for; bond prices
   (b) supply of; demand for; interest rates
   (c) demand for; supply of; bond prices
   (d) demand for; supply of; interest rates
   (e) demand for; supply of; exchange rates
   Answer: D
   Question Status: New

168) Deflation causes the _____ bonds to increase, the _____ bonds to decrease, and _____ to increase.
   (a) supply of; demand for; bond prices
   (b) supply of; demand for; interest rates
   (c) demand for; supply of; bond prices
   (d) demand for; supply of; interest rates
   (e) demand for; supply of; exchange rates
   Answer: C
   Question Status: New

169) A low savings rate causes the _________ bonds to fall, and ______ to increase.
   (a) demand for; interest rates
   (b) supply of; interest rates
   (c) demand for; bond prices
   (d) supply of; bond prices
   (e) supply of; exchange rates
   Answer: A
   Question Status: New

170) A low savings rate causes the _________ bonds to fall, and ______ to decrease.
   (a) demand for; interest rates
   (b) supply of; interest rates
   (c) demand for; bond prices
   (d) supply of; bond prices
   (e) supply of; exchange rates
   Answer: C
   Question Status: New

171) A low savings rate will ______ interest rates, and ______ investment in capital goods
   (a) decrease; decrease
   (b) increase; decrease
   (c) decrease; increase
   (d) increase; increase
   (e) decrease; not affect
   Answer: B
   Question Status: New
Figure 5-1

172) In Figure 5-1, the most likely cause of the increase in the equilibrium interest rate from $i_1$ to $i_2$ is
   (a) an increase in the price of bonds.
   (b) a decline in the price of bonds.
   (c) an increase in the expected inflation rate.
   (d) a decrease in the expected inflation rate.
   Answer: C
   Question Status: Previous Edition

173) In Figure 5-1, the most likely cause of the increase in the equilibrium interest rate from $i_1$ to $i_2$ is
   (a) an increase in the expected inflation rate.
   (b) a decrease in the expected inflation rate.
   (c) a sharp decline in the growth rate of the money supply.
   (d) a combination of both (a) and (c) above.
   Answer: A
   Question Status: Previous Edition

174) In Figure 5-1, the most likely cause of the increase in the equilibrium interest rate from $i_1$ to $i_2$ is
   (a) an expected decrease in the government budget deficit.
   (b) an expected increase in the government budget deficit.
   (c) a sharp decline in the growth rate of the money supply.
   (d) a combination of both (a) and (c) of the above.
   Answer: B
   Question Status: Previous Edition

175) In Figure 5-1, an increase in the expected inflation rate causes the
   (a) interest rate to increase from $i_1$ to $i_2$.
   (b) interest rate to decrease from $i_2$ to $i_1$.
   (c) demand curve for bonds to shift to the left.
   (d) both (a) and (c) of the above.
   (e) both (b) and (c) of the above.
   Answer: D
   Question Status: Previous Edition
176) In Figure 5-1, an increase in the expected inflation rate causes the
(a) interest rate to increase from $i_1$ to $i_2$.
(b) interest rate to decrease from $i_2$ to $i_1$.
(c) demand curve for bonds to shift to the right.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.
Answer: A
Question Status: Previous Edition

177) In Figure 5-1, one factor that would not have caused the supply of bonds to increase (shift to the right) is
(a) an increase in government budget deficits.
(b) an increase in expected inflation.
(c) a recession.
(d) a business cycle expansion.
Answer: C
Question Status: Previous Edition

178) In Figure 5-1, one factor that would not have caused the supply of bonds to increase (shift to the right) is
(a) a decrease in government budget deficits.
(b) an increase in expected inflation.
(c) expectations of more profitable investment opportunities.
(d) a business cycle expansion.
Answer: A
Question Status: Previous Edition

179) In Figure 5-1, one factor that would not have caused the demand for bonds to decrease (shift to the left) is
(a) an increase in the expected return on bonds relative to other assets.
(b) a decrease in the expected return on bonds relative to other assets.
(c) a decrease in wealth.
(d) an increase in the riskiness of bonds relative to other assets.
Answer: A
Question Status: Previous Edition

180) In Figure 5-1, one factor that would not have caused the demand for bonds to decrease (shift to the left) is
(a) a decrease in the expected return on bonds relative to other assets.
(b) an increase in wealth.
(c) a decrease in wealth.
(d) an increase in the riskiness of bonds relative to other assets.
Answer: B
Question Status: Previous Edition
181) In Figure 5-1, factors that would not have caused the demand for bonds to decrease (shift to the left) include:
   (a) an increase in the expected return on bonds relative to other assets.
   (b) a reduction in the riskiness of bonds relative to other assets.
   (c) a decrease in wealth.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: E
   Question Status: Previous Edition

182) In Figure 5-1, factors that could cause the supply of bonds to increase (shift to the right) include:
   (a) an increase in government budget deficits.
   (b) an increase in expected inflation.
   (c) expectations of more profitable investment opportunities.
   (d) all of the above.
   (e) only (b) and (c) of the above.
   Answer: D
   Question Status: Previous Edition

183) In Figure 5-1, factors that could cause the supply of bonds to shift to the right include:
   (a) a decrease in government budget deficits.
   (b) a decrease in expected inflation.
   (c) a recession.
   (d) a business cycle expansion.
   Answer: D
   Question Status: Previous Edition

184) In Figure 5-1, factors that could cause the supply of bonds to increase (shift to the right) include:
   (a) an increase in government budget deficits.
   (b) a decrease in expected inflation.
   (c) expectations of more profitable investment opportunities.
   (d) all of the above.
   (e) only (a) and (c) of the above.
   Answer: E
   Question Status: Previous Edition

185) In Figure 5-1, factors that could cause the supply of bonds to shift to the right include:
   (a) a decrease in government budget deficits.
   (b) an increase in expected inflation.
   (c) a recession.
   (d) expectations of fewer profitable investment opportunities.
   Answer: B
   Question Status: Previous Edition
186) In Figure 5-1, one factor that would not have caused the demand for bonds to shift to the left is
(a) a reduction in the riskiness of bonds relative to other assets.
(b) an increase in the expected return on bonds relative to other assets.
(c) a decrease in the expected rate of inflation.
(d) expectations of higher interest rates in the future.
Answer: C
Question Status: Previous Edition

187) In Figure 5-1, one factor that would not have caused the demand for bonds to shift to the left is
(a) an increase in the riskiness of bonds relative to other assets.
(b) a decrease in the expected return on bonds relative to other assets.
(c) an increase in the expected rate of inflation.
(d) expectations of lower interest rates in the future.
Answer: D
Question Status: Previous Edition

188) In Figure 5-1, factors that could cause the demand for bonds to decrease (shift to the left) include:
(a) an increase in the expected return on bonds relative to other assets.
(b) a decrease in the expected return on bonds relative to other assets.
(c) an increase in wealth.
(d) a reduction in the riskiness of bonds relative to other assets.
Answer: B
Question Status: Previous Edition

189) In Figure 5-1, factors that could cause the demand for bonds to decrease (shift to the left) include:
(a) an increase in the riskiness of bonds relative to other assets.
(b) a decrease in the expected return on bonds relative to other assets.
(c) an increase in wealth.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: E
Question Status: Previous Edition

190) In Figure 5-1, factors that could cause the demand for bonds to decrease (shift to the left) include:
(a) an increase in the riskiness of bonds relative to other assets.
(b) an increase in the expected rate of inflation.
(c) expectations of higher interest rates in the future.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: D
Question Status: Previous Edition
191) In Figure 5-1, factors that could cause the demand for bonds to decrease (shift to the left) include:
   (a) a decrease in the riskiness of bonds relative to other assets.
   (b) a decrease in the expected rate of inflation.
   (c) expectations of higher interest rates in the future.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: C
   Question Status: Previous Edition

192) In Figure 5-1, factors that could cause the demand for bonds to shift to the left include:
   (a) expectations of lower interest rates in the future.
   (b) an increase in the expected return on bonds relative to other assets.
   (c) a decrease in wealth.
   (d) a reduction in the riskiness of bonds relative to other assets.
   Answer: C
   Question Status: Previous Edition

193) In Figure 5-1, the price of bonds would fall from P₁ to P₂ and the interest rate would rise from i₁ to i₂ if
   (a) inflation is expected to increase in the future.
   (b) interest rates are expected to fall in the future.
   (c) the expected return on bonds relative to other assets is expected to increase in the future.
   (d) the riskiness of bonds falls relative to other assets.
   Answer: A
   Question Status: Previous Edition

194) In Figure 5-1, shifts of both supply and demand would increase the price of bonds from P₂ to P₁ and the interest rate would fall from i₂ to i₁ if
   (a) interest rates are expected to fall in the future.
   (b) the expected return on bonds relative to other assets is expected to increase in the future.
   (c) inflation is expected to decline in the future.
   (d) the riskiness of bonds falls relative to other assets.
   Answer: C
   Question Status: Previous Edition

195) In Figure 5-1, the increase in the interest rate from i₁ to i₂ due to an increase in the expected inflation rate is called the
   (a) Fisher effect.
   (b) liquidity effect.
   (c) income effect.
   (d) Keynes effect.
   Answer: A
   Question Status: Previous Edition
In Figure 5-2, one possible explanation for the increase in the interest rate from $i_1$ to $i_2$ is

(a) an increase in the expected inflation rate.
(b) a decrease in the expected inflation rate.
(c) an increase in economic growth.
(d) a decrease in economic growth.

Answer: C  
Question Status: Previous Edition

In Figure 5-2, one factor that would not have caused the supply of bonds to shift to the right is

(a) an increase in government budget deficits.
(b) an increase in expected inflation.
(c) a recession.
(d) a business cycle expansion.

Answer: C  
Question Status: Previous Edition

In Figure 5-2, one factor that would not have caused the demand for bonds to increase (shift to the right) is

(a) an increase in the expected return on bonds relative to other assets.
(b) a decrease in the expected return on bonds relative to other assets.
(c) an increase in wealth.
(d) a reduction in the riskiness of bonds relative to other assets.

Answer: B  
Question Status: Previous Edition

In Figure 5-2, one factor that would not have caused the supply of bonds to shift to the right is

(a) an increase in government budget deficits.
(b) an increase in expected inflation.
(c) an increase in expected profitable investment opportunities.
(d) a business cycle contraction.

Answer: D  
Question Status: Previous Edition
200) In Figure 5-2, one factor that would not have caused the supply of bonds to increase is
   (a) an increase in government budget deficits.
   (b) a decrease in expected inflation.
   (c) expectations of more profitable investment opportunities.
   (d) a business cycle expansion.
   Answer: B
   Question Status: Previous Edition

201) In Figure 5-2, factors that could cause the supply of bonds to increase (shift to the right) include:
   (a) a decrease in government budget deficits.
   (b) a decrease in expected inflation.
   (c) expectations of more profitable investment opportunities.
   (d) all of the above.
   (e) only (b) and (c) of the above.
   Answer: C
   Question Status: Previous Edition

202) In Figure 5-2, one factor that would not have caused the demand for bonds to increase (shift to the right) is
   (a) a decrease in the expected return on bonds relative to other assets.
   (b) a reduction in the riskiness of bonds relative to other assets.
   (c) a decrease in the expected rate of inflation.
   (d) expectations of lower interest rates in the future.
   Answer: A
   Question Status: Previous Edition

203) In Figure 5-2, one factor that would not have caused the demand for bonds to shift to the right is
   (a) a reduction in the riskiness of bonds relative to other assets.
   (b) an increase in the expected return on bonds relative to other assets.
   (c) a decrease in the expected rate of inflation.
   (d) expectations of higher interest rates in the future.
   Answer: D
   Question Status: Previous Edition

204) In Figure 5-2, factors that could cause the demand for bonds to increase include:
   (a) an increase in the expected return on bonds relative to other assets.
   (b) a decrease in the expected return on bonds relative to other assets.
   (c) a reduction in the riskiness of bonds relative to other assets.
   (d) both (a) and (b) of the above.
   (e) both (a) and (c) of the above.
   Answer: E
   Question Status: Previous Edition
205) In Figure 5-2, factors that could cause the demand for bonds to increase include:
   (a) an increase in the riskiness of bonds relative to other assets.
   (b) a decrease in the expected return on bonds relative to other assets.
   (c) an increase in wealth.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: C
   Question Status: Previous Edition

206) In Figure 5-2, factors that could cause the demand for bonds to shift to the right include:
   (a) an increase in the riskiness of bonds relative to other assets.
   (b) an increase in the expected rate of inflation.
   (c) expectations of lower interest rates in the future.
   (d) all of the above.
   Answer: C
   Question Status: Previous Edition

207) In Figure 5-2, factors that could cause the demand for bonds to shift to the right include:
   (a) a decrease in the riskiness of bonds relative to other assets.
   (b) a decrease in the expected rate of inflation.
   (c) expectations of higher interest rates in the future.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: E
   Question Status: Previous Edition

208) In Figure 5-2, factors that could cause the demand for bonds to shift to the right include:
   (a) expectations of lower interest rates in the future.
   (b) an increase in the expected return on bonds relative to other assets.
   (c) a reduction in the riskiness of bonds relative to other assets.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: D
   Question Status: Previous Edition

209) When comparing the Loanable Funds and Liquidity Preference Frameworks of interest rate determination, which of the following are true?
   (a) The loanable funds framework is easier to use when analyzing the effects from changes in expected inflation.
   (b) The liquidity preference framework provides a simpler analysis of the effects from changes in income, the price level, and the supply of money.
   (c) In most instances, the two approaches to interest rate determination yield the same predictions.
   (d) All of the above are true.
   (e) Only (a) and (b) of the above are true.
   Answer: D
   Question Status: Previous Edition
210) When comparing the Loanable Funds and Liquidity Preference Frameworks of interest rate determination, which of the following are true?
(a) The liquidity preference framework is easier to use when analyzing the effects from changes in expected inflation.
(b) The loanable funds framework provides a simpler analysis of the effects from changes in income, the price level, and the supply of money.
(c) In most instances, the two approaches to interest rate determination yield the same predictions.
(d) All of the above are true.
(e) Only (a) and (b) of the above are true.
Answer: C
Question Status: Previous Edition

211) In his Liquidity Preference Framework, Keynes assumed that money has a zero rate of return; thus,
(a) when interest rates rise, the expected return on money falls relative to the expected return on bonds, causing the demand for money to fall.
(b) when interest rates rise, the expected return on money falls relative to the expected return on bonds, causing the demand for money to rise.
(c) when interest rates fall, the expected return on money falls relative to the expected return on bonds, causing the demand for money to fall.
(d) when interest rates fall, the expected return on money falls relative to the expected return on bonds, causing the demand for money to rise.
Answer: A
Question Status: Previous Edition

212) The loanable funds framework is easier to use when analyzing the effects of changes in _____, while the liquidity preference framework provides a simpler analysis of the effects from changes in income, the price level, and the supply of _____.
(a) expected inflation; bonds
(b) expected inflation; money
(c) government budget deficits; bonds
(d) government budget deficits; money
Answer: B
Question Status: Previous Edition

213) In Keynes’s liquidity preference framework, individuals are assumed to hold their wealth in two forms:
(a) real assets and financial assets.
(b) stocks and bonds.
(c) money and bonds.
(d) money and gold.
Answer: C
Question Status: Previous Edition
214) In Keynes’s liquidity preference framework, as the expected return on bonds increases (holding everything else unchanged), the expected return on money _____, causing the demand for _____ to fall.
(a) falls; bonds
(b) falls; money
(c) rises; bonds
(d) rises; money
Answer: B
Question Status: Previous Edition

215) In Keynes’s liquidity preference framework,
(a) the demand for bonds must equal the supply of money.
(b) the demand for money must equal the supply of bonds.
(c) an excess supply of bonds implies an excess supply of money.
(d) all of the above.
(e) none of the above.
Answer: E
Question Status: Previous Edition

216) In Keynes’s liquidity preference framework,
(a) the demand for bonds must equal the supply of money.
(b) the demand for money must equal the supply of bonds.
(c) an excess demand of bonds implies an excess demand for money.
(d) an excess supply of bonds implies an excess demand for money.
Answer: D
Question Status: Previous Edition

217) If there is excess demand for money, there is
(a) excess demand for bonds.
(b) equilibrium in the bond market.
(c) excess supply of bonds.
(d) too much money.
(e) too few bonds.
Answer: C
Question Status: New

218) An excess demand for bonds implies
(a) excess demand for money.
(b) equilibrium in the money market.
(c) a shortage of currency.
(d) a surplus of bonds.
(e) excess supply of money.
Answer: E
Question Status: New
219) The opportunity cost of holding money is
   (a) the level of income.
   (b) the price level.
   (c) the interest rate.
   (d) all of the above.
   (e) only (a) and (b) of the above.
   Answer: C
   Question Status: New

220) An increase in the interest rate
   (a) increases the demand for money.
   (b) increases the quantity of money demanded.
   (c) decreases the demand for money.
   (d) decreases the quantity of money demanded.
   (e) has no effect on the quantity of money demanded.
   Answer: D
   Question Status: New

221) A decrease in the interest rate
   (a) increases the demand for money.
   (b) increases the quantity of money demanded.
   (c) decreases the demand for money.
   (d) decreases the quantity of money demanded.
   (e) has no effect on the quantity of money demanded.
   Answer: B
   Question Status: New

222) If there is an excess supply of money
   (a) individuals sell bonds, causing the interest rate to rise.
   (b) individuals sell bonds, causing the interest rate to fall.
   (c) individuals buy bonds, causing interest rates to fall.
   (d) individuals buy bonds, causing interest rates to rise.
   (e) individuals buy bonds, causing bond prices to fall.
   Answer: C
   Question Status: New

223) If there is an excess demand for money
   (a) individuals sell bonds, causing the interest rate to rise.
   (b) individuals sell bonds, causing the interest rate to fall.
   (c) individuals buy bonds, causing interest rates to fall.
   (d) individuals buy bonds, causing interest rates to rise.
   (e) individuals buy bonds, causing bond prices to fall.
   Answer: A
   Question Status: New
224) A higher level of income causes the demand for money to _____ and the demand curve for money to shift to the _____.
(a) decrease; right
(b) decrease; left
(c) increase; right
(d) increase; left
Answer: C
Question Status: Previous Edition

225) A lower level of income causes the demand for money to _____ and the demand curve for money to shift to the _____.
(a) decrease; right
(b) decrease; left
(c) increase; right
(d) increase; left
Answer: B
Question Status: Previous Edition

226) A higher level of income causes the demand for money to _____ and the interest rate to _____.
(a) decrease; decrease
(b) decrease; increase
(c) increase; decrease
(d) increase; increase
Answer: D
Question Status: Previous Edition

227) A lower level of income causes the demand for money to _____ and the interest rate to _____.
(a) decrease; decrease
(b) decrease; increase
(c) increase; decrease
(d) increase; increase
Answer: A
Question Status: Previous Edition

228) When real income falls, the demand curve for money shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; fall
(c) left; falls
(d) left; rises
Answer: C
Question Status: Previous Edition
229) When real income increases, the demand curve for money shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; fall
(c) left; falls
(d) left; rises
Answer: A
Question Status: Previous Edition

230) When real income _____, the demand curve for money shifts to the _____ and the interest rate _____.
(a) falls; left; falls
(b) falls; right; falls
(c) falls; left; rises
(d) rises; left; rises
(e) rises; right; falls
Answer: A
Question Status: Previous Edition

231) When real income _____, the demand curve for money shifts to the _____ and the interest rate _____.
(a) falls; right; rises
(b) falls; right; falls
(c) falls; left; rises
(d) rises; left; rises
(e) rises; right; rises
Answer: E
Question Status: Previous Edition

232) In the Keynesian liquidity preference framework, a higher level of income causes the demand for money to _____ and the demand curve to shift to the _____.
(a) increase; left
(b) increase; right
(c) decrease; left
(d) decrease; right
Answer: B
Question Status: Previous Edition

233) In the Keynesian liquidity preference framework, a lower level of income causes the demand for money to _____ and the demand curve to shift to the _____.
(a) increase; left
(b) increase; right
(c) decrease; left
(d) decrease; right
Answer: C
Question Status: Previous Edition
234) In the Keynesian liquidity preference framework, when income is _____ during a business cycle expansion, interest rates will _____.
   (a) rising; rise  
   (b) rising; fall  
   (c) falling; rise  
   (d) falling; fall  
   Answer: A  
   Question Status: Previous Edition

235) In the Keynesian liquidity preference model, a business cycle ________ causes income to _______ and interest rates to _______.
   (a) expansion; decrease; decrease  
   (b) expansion; increase; decrease  
   (c) contraction; increase; increase  
   (d) contraction; decrease; decrease  
   (e) contraction; decrease; increase  
   Answer: D  
   Question Status: Study Guide

236) In the Keynesian liquidity preference framework, a rise in the price level causes the demand for money to _____ and the demand curve to shift to the _____.
   (a) increase; left  
   (b) increase; right  
   (c) decrease; left  
   (d) decrease; right  
   Answer: B  
   Question Status: Previous Edition

237) In the Keynesian liquidity preference framework, a decline in the price level causes the demand for money to _____ and the demand curve to shift to the _____.
   (a) increase; left  
   (b) increase; right  
   (c) decrease; left  
   (d) decrease; right  
   Answer: C  
   Question Status: Previous Edition

238) When the price level _____, the demand curve for money shifts to the _____ and the interest rate _____.
   (a) falls; left; falls  
   (b) falls; right; falls  
   (c) falls; left; rises  
   (d) rises; right; rises  
   (e) rises; right; falls  
   Answer: D  
   Question Status: Previous Edition
239) When the price level _____, the demand curve for money shifts to the _____ and the interest rate _____.
   (a) falls; left; rises
   (b) falls; right; falls
   (c) falls; left; falls
   (d) rises; right; rises
   (e) rises; right; falls
   Answer: C
   Question Status: Previous Edition

240) When the price level rises, the demand curve for money shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: A
   Question Status: Previous Edition

241) When the price level falls, the demand curve for money shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: C
   Question Status: Previous Edition

242) A rise in the price level causes the demand for money to _____ and the interest rate to _____.
   (a) decrease; decrease
   (b) decrease; increase
   (c) increase; decrease
   (d) increase; increase
   Answer: D
   Question Status: Previous Edition

243) A decline in the price level causes the demand for money to _____ and the interest rate to _____.
   (a) decrease; decrease
   (b) decrease; increase
   (c) increase; decrease
   (d) increase; increase
   Answer: A
   Question Status: Previous Edition
244) A rise in the price level causes the demand for money to ____ and the demand curve to shift to the ____.
   (a) decrease; right
   (b) decrease; left
   (c) increase; right
   (d) increase; left
   Answer: C
   Question Status: Previous Edition

245) A decline in the price level causes the demand for money to ____ and the demand curve to shift to the ____.
   (a) decrease; right
   (b) decrease; left
   (c) increase; right
   (d) increase; left
   Answer: B
   Question Status: Previous Edition

246) A decline in the expected inflation rate causes the demand for money to ____ and the demand curve to shift to the ____.
   (a) decrease; right
   (b) decrease; left
   (c) increase; right
   (d) increase; left
   Answer: B
   Question Status: Previous Edition

247) In the liquidity preference framework, a one-time increase in the money supply results in a price level effect. The maximum impact of the price level effect on interest rates occurs
   (a) at the moment the price level hits its peak (stops rising) because both the price level and expected inflation effects are at work.
   (b) immediately after the price level begins to rise, because both the price level and expected inflation effects are at work.
   (c) at the moment the expected inflation rate hits its peak.
   (d) at the moment the inflation rate hits it peak.
   (e) at the moment inflation begins to increase.
   Answer: A
   Question Status: Study Guide
248) In the liquidity preference framework, a one-time increase in the money supply has different price level and expected inflation effects. The difference is

(a) the increase in the interest rate caused by the rise in the price level remains once the price level has stopped rising, but the increase in the interest rate caused by expected inflation will be reversed once the price level stops rising.

(b) the increase in the interest rate caused by the rise in the expected inflation rate remains once the price level has stopped rising, but the increase in the interest rate caused by the rise in the price level will be reversed once the price level stops rising.

(c) once the price level stops rising, the interest rate declines because of the price level effect, but the expected inflation effect remains after the price level has stopped rising.

(d) once the price level stops rising, the interest rate continues to increase because of the expected inflation effect.

(e) there is no difference, as both effects cause the interest rate to rise.

Answer: A

Question Status: Study Guide

249) Interest rates increased continuously during the 1970s. The most likely explanation is

(a) banking failures that reduced the money supply.

(b) a rise in the level of income.

(c) the repeated bouts of recession and expansion.

(d) increasing expected rates of inflation.

(e) an increase in the price level.

Answer: D

Question Status: Study Guide

250) Holding everything else equal, an increase in the money supply causes

(a) interest rates to decline initially.

(b) interest rates to increase initially.

(c) bond prices to decline initially.

(d) both (a) and (c) of the above.

(e) both (b) and (c) of the above.

Answer: A

Question Status: Previous Edition

251) Holding everything else equal, an increase in the money supply causes

(a) interest rates to decline initially.

(b) interest rates to increase initially.

(c) bond prices to increase initially.

(d) both (a) and (c) of the above.

(e) both (b) and (c) of the above.

Answer: D

Question Status: Previous Edition
252) Holding everything else equal, a decrease in the money supply causes
(a) interest rates to decline initially.
(b) interest rates to increase initially.
(c) bond prices to increase initially.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.
Answer: B
Question Status: Previous Edition

253) Holding everything else equal, a decrease in the money supply causes
(a) interest rates to decline initially.
(b) interest rates to increase initially.
(c) bond prices to decrease initially.
(d) both (b) and (c) of the above.
Answer: D
Question Status: Previous Edition

254) When the Fed decreases the money stock, the money supply curve shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; falls
(c) left; falls
(d) left; rises
Answer: D
Question Status: Previous Edition

255) When the Fed increases the money stock, the money supply curve shifts to the _____ and the interest rate _____.
(a) right; rises
(b) right; falls
(c) left; falls
(d) left; rises
Answer: B
Question Status: Previous Edition

256) When the Fed _____ the money stock, the money supply curve shifts to the _____ and the interest rate _____
(a) decreases; right; rises
(b) increases; right; rises
(c) decreases; left; falls
(d) increases; left; rises
(e) decreases; left; rises
Answer: E
Question Status: Previous Edition
257) When the Fed increases the money stock, the money supply curve shifts to the _____ and the interest rate _____.
   (a) right; rises
   (b) right; falls
   (c) left; falls
   (d) left; rises
   Answer: B
   Question Status: Previous Edition

258) When the Fed _____ the money stock, the money supply curve shifts to the _____ and the interest rate _____.
   (a) decreases; right; rises
   (b) increases; right; falls
   (c) decreases; left; falls
   (d) increases; left; rises
   (e) decreases; right; falls
   Answer: B
   Question Status: Previous Edition

259) When the price level falls, the ________ curve for nominal money ________, and interest rates ________.
   (a) demand; decreases; falls
   (b) demand; increases; rises
   (c) supply; increases; rises
   (d) supply; decreases; falls
   (e) supply; increases; falls
   Answer: A
   Question Status: Study Guide

260) When the interest rate is above the equilibrium interest rate, there is an excess _____ for (of) money and the interest rate will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   Answer: C
   Question Status: Previous Edition

261) In the market for money, an interest rate below equilibrium results in an excess _____ for (of) money and the interest rate will _____.
   (a) demand; rise
   (b) demand; fall
   (c) supply; fall
   (d) supply; rise
   (e) cannot be determined
   Answer: A
   Question Status: Study Guide
262) A(n) ______ in the money supply creates excess ______ of (for) money, causing interest rates to ______.
   (a) increase; demand; rise
   (b) increase; supply; fall
   (c) increase; supply; rise
   (d) decrease; supply; fall
   (e) decrease; demand; fall
   Answer: B
   Question Status: New

263) A(n) ______ in the money supply creates excess ______ of (for) money, causing interest rates to ______.
   (a) increase; demand; rise
   (b) increase; demand; fall
   (c) increase; supply; rise
   (d) decrease; supply; fall
   (e) decrease; demand; rise
   Answer: E
   Question Status: New

264) A(n) ______ in the money supply creates excess demand for ______, causing interest rates to ______.
   (a) increase; money; rise
   (b) increase; bonds; fall
   (c) decrease; bonds; rise
   (d) decrease; bonds; fall
   (e) decrease; money; fall
   Answer: B
   Question Status: New
In Figure 5-3, one factor not responsible for the decline in the demand for money is
(a) a decline in the price level.
(b) a decline in income.
(c) an increase in income.
(d) a decline in the expected inflation rate.
Answer: C

In Figure 5-3, one factor not responsible for the decline in the interest rate is
(a) a decline in the price level.
(b) a decline in income.
(c) an increase in income.
(d) a decline in the expected inflation rate.
Answer: C

In Figure 5-3, one factor not responsible for the decline in the interest rate is
(a) a decline the price level.
(b) an increase in the money supply.
(c) a decline in income.
(d) a decline in the expected inflation rate.
Answer: B

In Figure 5-3, the increase in the interest rate from $i_2$ to $i_1$ can be explained by
(a) a decrease in money growth.
(b) a decline in the expected price level.
(c) an increase in income.
(d) all of the above.
(e) only (a) and (b) of the above.
Answer: C
269) In Figure 5-3, the increase in the interest rate from $i_2$ to $i_1$ can be explained by
(a) a decrease in money growth.
(b) an increase in the expected price level.
(c) an increase in income.
(d) both (a) and (c) of the above.
(e) both (b) and (c) of the above.
Answer: E
Question Status: Previous Edition

270) In Figure 5-3, the decrease in the interest rate from $i_1$ to $i_2$ can be explained by
(a) a decrease in income.
(b) an increase in the expected price level.
(c) a decrease in money growth.
(d) only (a) and (b) of the above.
Answer: A
Question Status: Previous Edition

271) In Figure 5-3, the decline in the interest rate from $i_1$ to $i_2$ can be explained by
(a) a decrease in income.
(b) a decrease in the expected price level.
(c) an increase in money growth.
(d) both (a) and (b) of the above.
(e) both (a) and (c) of the above.
Answer: D
Question Status: Previous Edition

272) In Figure 5-4, the factor responsible for the decline in the interest rate is
(a) a decline the price level.
(b) a decline in income.
(c) an increase in the money supply.
(d) a decline in the expected inflation rate.
Answer: C
Question Status: Previous Edition
273) In Figure 5-4, the decrease in the interest rate from \( i_1 \) to \( i_2 \) can be explained by
   (a) a decrease in money growth.
   (b) an increase in money growth.
   (c) a decline in the expected price level.
   (d) only (a) and (b) of the above.
   Answer: B
   Question Status: Previous Edition

274) In Figure 5-4, the increase in the interest rate from \( i_2 \) to \( i_1 \) can be explained by
   (a) a decrease in money growth.
   (b) an increase in the expected price level.
   (c) an increase in income.
   (d) both (a) and (c) of the above.
   (e) both (b) and (c) of the above.
   Answer: A
   Question Status: Previous Edition

275) When the growth rate of the money supply increases, interest rates end up being permanently higher if
   (a) the liquidity effect is larger than the other effects.
   (b) there is fast adjustment of expected inflation.
   (c) there is slow adjustment of expected inflation.
   (d) the expected inflation effect is larger than the liquidity effect.
   Answer: D
   Question Status: Previous Edition

276) When the growth rate of the money supply increases, interest rates end up being permanently lower if
   (a) the liquidity effect is larger than the other effects.
   (b) there is fast adjustment of expected inflation.
   (c) there is slow adjustment of expected inflation.
   (d) the expected inflation effect is larger than the liquidity effect.
   Answer: A
   Question Status: Previous Edition

277) When the growth rate of the money supply decreases, interest rates end up being permanently lower if
   (a) the liquidity effect is larger than the other effects.
   (b) there is fast adjustment of expected inflation.
   (c) there is slow adjustment of expected inflation.
   (d) the expected inflation effect is larger than the liquidity effect.
   Answer: D
   Question Status: Previous Edition
278) When the growth rate of the money supply decreases, interest rates end up being permanently higher if
(a) the liquidity effect is larger than the other effects.
(b) there is fast adjustment of expected inflation.
(c) there is slow adjustment of expected inflation.
(d) the expected inflation effect is larger than the liquidity effect.
Answer: A
Question Status: Previous Edition

279) When the growth rate of the money supply is decreased, interest rates will fall immediately if the
liquidity effect is _____ than the other money supply effects and there is _____ adjustment of expected inflation.
(a) larger; fast
(b) larger; slow
(c) smaller; slow
(d) smaller; fast
Answer: D
Question Status: Previous Edition

280) When the growth rate of the money supply is increased, interest rates will fall immediately if the
liquidity effect is _____ than the other money supply effects and there is _____ adjustment of expected inflation.
(a) larger; fast
(b) larger; slow
(c) smaller; slow
(d) smaller; fast
Answer: B
Question Status: Previous Edition

281) When the growth rate of the money supply is decreased, interest rates will rise immediately if the
liquidity effect is _____ than the other money supply effects and there is _____ adjustment of expected inflation.
(a) larger; fast
(b) larger; slow
(c) smaller; slow
(d) smaller; fast
Answer: B
Question Status: Previous Edition

282) When the growth rate of the money supply is increased, interest rates will rise immediately if the
liquidity effect is _____ than the other money supply effects and there is _____ adjustment of expected inflation.
(a) larger; fast
(b) larger; slow
(c) smaller; slow
(d) smaller; fast
Answer: D
Question Status: Previous Edition
283) If the Fed wants to permanently lower interest rates, then it should lower the rate of money growth if
   (a) there is fast adjustment of expected inflation.
   (b) there is slow adjustment of expected inflation.
   (c) the liquidity effect is smaller than the expected inflation effect.
   (d) the liquidity effect is larger than the other effects.
   Answer: C
   Question Status: Previous Edition

284) If the Fed wants to permanently lower interest rates, then it should raise the rate of money growth if
   (a) there is fast adjustment of expected inflation.
   (b) there is slow adjustment of expected inflation.
   (c) the liquidity effect is smaller than the expected inflation effect.
   (d) the liquidity effect is larger than the other effects.
   Answer: D
   Question Status: Previous Edition

285) Which of the following effects of a change in the money supply is most likely to affect the interest
   rate differently than the others?
   (a) The expected inflation effect
   (b) The income effect
   (c) The liquidity effect
   (d) The price level effect
   Answer: C
   Question Status: Previous Edition

286) Milton Friedman contends that it is entirely possible that when the money supply rises, interest rates
   may _____ if the _____ effect is more than offset by changes in income, the price level, and
   expected inflation.
   (a) fall; liquidity
   (b) fall; risk
   (c) rise; liquidity
   (d) rise; risk
   Answer: C
   Question Status: Previous Edition

287) It is entirely possible that when the money supply rises, interest rates may _____ if the _____ effect
   is more than offset by changes in income, the price level, and expected inflation.
   (a) fall; liquidity
   (b) fall; risk
   (c) rise; liquidity
   (d) rise; risk
   Answer: C
   Question Status: Previous Edition
288) Of the four effects on interest rates from an increase in the money supply, the one that works in the opposite direction of the other three is the
(a) liquidity effect.
(b) income effect.
(c) price level effect.
(d) expected inflation effect.
Answer: A
Question Status: Previous Edition

289) Of the four effects on interest rates from an increase in the money supply, the initial effect is, generally, the
(a) income effect.
(b) liquidity effect.
(c) price level effect.
(d) expected inflation effect.
Answer: B
Question Status: Previous Edition

290) If the liquidity effect is larger than the other effects, an increase in money growth will
(a) lower interest rates.
(b) raise interest rates.
(c) cause interest rates to rise initially but then fall below the initial level.
(d) cause interest rates to fall initially but then rise above the initial level.
Answer: A
Question Status: Previous Edition

291) If the liquidity effect is smaller than the other effects, and the adjustment to expected inflation is slow, then the
(a) interest rate will fall.
(b) interest rate will rise.
(c) interest rate will initially fall but eventually climb above the initial level in response to an increase in money growth.
(d) interest rate will initially rise but eventually fall below the initial level in response to an increase in money growth.
Answer: C
Question Status: Previous Edition

292) If the liquidity effect is smaller than the other effects, and the adjustment to expected inflation is immediate, then the
(a) interest rate will fall.
(b) interest rate will rise.
(c) interest rate will fall immediately below the initial level when the money supply grows.
(d) interest rate will rise immediately above the initial level when the money supply grows.
Answer: D
Question Status: Previous Edition
Figure 5-5

293) Figure 5-5 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the
(a) liquidity effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(b) liquidity effect is larger than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(c) liquidity effect is larger than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
(d) liquidity effect is smaller than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.

Answer: A
Question Status: Previous Edition

294) Figure 5-5 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the
(a) Fisher effect is dominated by the liquidity effect and interest rates adjust slowly to changes in expected inflation.
(b) liquidity effect is dominated by the Fisher effect and interest rates adjust slowly to changes in expected inflation.
(c) liquidity effect is dominated by the Fisher effect and interest rates adjust quickly to changes in expected inflation.
(d) Fisher effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.

Answer: C
Question Status: Previous Edition
Figure 5-6

295) Figure 5-6 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the

(a) liquidity effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(b) liquidity effect is larger than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(c) liquidity effect is larger than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
(d) liquidity effect is smaller than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.

Answer: C
Question Status: Previous Edition

296) Figure 5-6 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the

(a) Fisher effect is dominated by the liquidity effect and interest rates adjust slowly to changes in expected inflation.
(b) liquidity effect is dominated by the Fisher effect and interest rates adjust slowly to changes in expected inflation.
(c) liquidity effect is dominated by the Fisher effect and interest rates adjust quickly to changes in expected inflation.
(d) Fisher effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.

Answer: A
Question Status: Previous Edition
297) Figure 5-7 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the
(a) liquidity effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(b) liquidity effect is larger than the expected inflation effect and interest rates adjust quickly to changes in expected inflation.
(c) liquidity effect is larger than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
(d) liquidity effect is smaller than the expected inflation effect and interest rates adjust slowly to changes in expected inflation.
Answer: D
Question Status: Previous Edition

298) Figure 5-7 illustrates the effect of an increased rate of money supply growth. From the figure, one can conclude that the
(a) Fisher effect is dominated by the liquidity effect and interest rates adjust slowly to changes in expected inflation
(b) liquidity effect is dominated by the Fisher effect and interest rates adjust slowly to changes in expected inflation
(c) liquidity effect is dominated by the Fisher effect and interest rates adjust quickly to changes in expected inflation
(d) Fisher effect is smaller than the expected inflation effect and interest rates adjust quickly to changes in expected inflation
Answer: B
Question Status: Previous Edition
Questions for Web Appendix on Asset Pricing

299) The riskiness of an asset is measured by
   (a) the magnitude of its return.
   (b) the absolute value of any change in the asset’s price.
   (c) the standard deviation of its return.
   (d) all of the above.
   (e) risk is impossible to measure.
   Answer: C
   Question Status: New

300) The riskiness of an asset that is unique to the particular asset is
   (a) systematic risk.
   (b) portfolio risk.
   (c) investment risk.
   (d) interest-rate risk.
   (e) nonsystematic risk.
   Answer: E
   Question Status: New

Questions for Web Appendix on Gold

301) An increase in expected inflation will _____ the ____ for gold, _____ its price.
   (a) increase; demand; increasing
   (b) decrease; demand; decreasing
   (c) increase; supply; increasing
   (d) increase; supply; decreasing
   (e) decrease; supply; increasing
   Answer: A
   Question Status: New

302) A return to the gold standard, that is, using gold for money will _____ the ____ for gold, _____ its price.
   (a) increase; demand; increasing
   (b) decrease; demand; decreasing
   (c) increase; supply; increasing
   (d) increase; supply; decreasing
   (e) decrease; supply; increasing
   Answer: A
   Question Status: New
303) Discovery of new gold in Alaska will _____ the ____ for gold, _____ its price.
   (a) increase; demand; increasing
   (b) decrease; demand; decreasing
   (c) increase; supply; increasing
   (d) increase; supply; decreasing
   (e) decrease; supply; increasing
   Answer: D
   Question Status: New

## Essay Questions

1) Demonstrate graphically and explain the effect in the bond market of a decrease in the federal deficit. What is the effect on the interest rate and bond prices? How might capital spending be affected by the deficit?

Answer: A graph of the supply and demand for bonds should show the reduced deficit shifting the supply of bonds to the left. A correct graph will show a rise in bond prices and a fall in interest rates, and this should be explained. Lower interest rates stimulate capital spending, as explained in the discussion of the savings rate.

2) Demonstrate graphically the effect of an increase in the personal savings rate. Show and explain the effect of increased savings on bond prices and interest rates. How would this change affect capital spending?

Answer: A graph of bond supply and demand should show an increase in bond demand. The increase in bond prices and the fall in the interest rates should be clearly shown and explained. The increase in saving lowers interest rates, thus increasing capital spending.
3) During President Reagan’s administration, his supporters argued that higher real interest rates were the result of policies increasing the profitability of investment. Reagan’s critics argued that the high interest rates were the result of high budget deficits. Demonstrate graphically and explain how increased profitability of investments and increased deficits affect bond prices and interest rates. Based on your graphs, is there merit to either viewpoint?

**Answer:** As increased deficits and increased profitability of investment both increase the supply of bonds, one graph showing this shift and the resulting fall in prices and increase in interest rates is appropriate. As the graphical analysis cannot distinguish between the alternatives, answers will indicate that both views have merit.

![Graph showing bond supply and demand](image)

4) In the liquidity preference framework, demonstrate graphically the effect of a decrease in the money supply. Indicate on the graph the excess demand or excess supply of money. Explain the process of adjustment that results in a change in the equilibrium interest rate, and the direction of the change in rates.

**Answer:** The graph should show the money supply curve shifting to the left. At the original rate, excess supply is the difference between the demand curve and new supply curve at the original equilibrium interest rate. To adjust, individuals sell bonds, driving bond prices down and interest rates up until the new equilibrium rate is attained.

![Graph showing money supply and demand](image)

5) Economists recognize that interest rates are typically procyclical, meaning that interest rates increase during economic expansions and decline during recessions. Real income and generally inflation rise and fall with the economy. Using the liquidity preference model of interest rates, give three reasons why interest rates are procyclical.

**Answer:** The answer should explain that the income, price-level, and expected inflation effects would all increase interest rates during an expansion and decrease them in a recession.