Faculty of Commerce, Benha University

Economics of Money & Banking

Level 2

Course Code:

Economics E216

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Tutorial 6

1. The quantity theory of money is a theory of
   A. how the money supply is determined.
   B. how interest rates are determined.
   C. how the nominal value of aggregate income is determined.
   D. all of the above.

2. The average number of times that a dollar is spent in buying the total amount of final goods and services produced during a given time period is known as
   A. gross national product.
   B. the spending multiplier.
   C. the money multiplier.
   D. velocity.

3. If the money supply is 500 and nominal income is 3,000, the velocity of money is
   A. 60.
   B. 6.
   C. 1/6.
   D. undefined.

4. If the money supply is 600 and nominal income is 3,000, the velocity of money is
   A. 5.
   B. 50.
   C. 1/5.
   D. undefined.

5. In Irving Fisher's quantity theory of money, velocity changes slowly over time because
   (A) institutional and technological features of an economy that effect velocity change slowly.
   (B) interest rates change very slowly over time.
   (C) the economy grows slowly over time.
   (D) inflation does not affect velocity.

6. The view that velocity is constant in the short run transforms the equation of exchange into the quantity theory of money. According to the quantity theory of money, when the money supply doubles
   (A) velocity falls by 50 percent.
   (B) velocity doubles.
   (C) nominal incomes falls by 50 percent.
   (D) nominal income doubles.

7. Fisher's quantity theory of money suggests that the demand for money is purely a function of _____,
   and _____ have no effect on the demand for money.
   (A) expectations; prices
   (B) expectations; interest rates
   (c) income; prices
   (D) income; interest rates

8. Velocity, over the business cycle, tends to
   (A) rise during economic contractions.
   (B) fall during economic expansion.
   (C) stay constant.
   (D) fall during economic contractions.

9. Until The Keynesian theory of money demand emphasizes the importance of
   (A) a constant velocity.
   (B) irrational behavior on the part of some economic agents.
   (c) interest rates on the demand for money.
   (D) all of the above.

10. the Great Depression, economists did not recognize that velocity
   (A) increases during severe economic contractions.
   (B) declines during severe economic contractions.
   (c) declines during rapid economic expansions, since money growth fails to keep pace.
   (D) fails to decline during economic contractions.

11. Keynes's hypothesized that the transactions component of money demand was primarily determined
by the level of

(A) interest rates.
(B) velocity
(c) income.
(D) stock market prices.

12. Keynes argued that the precautionary component of the demand for money was primarily determined by the level of people's _____, which he believed were proportional to _____.
(a) incomes; wealth
(b) incomes; age
(c) transactions; income
(d) transactions; age

13. Because Keynes's assumed that the expected return on money was zero, he argued that
(a) people would never hold money.
(b) people would never hold money as a store of wealth.
(c) people would hold money as a store of wealth when the expected return on bonds was negative.
(d) people would hold money as a store of wealth only when forced to by government policy.

14. The Keynesian theory of money demand predicts that people will increase their money holdings if they believe that
(a) interest rates are about to fall.
(b) bond prices are about to rise.
(c) expected inflation is about to fall.
(d) bond prices are about to fall.

15. Keynes's theory of the demand for money implies
(a) that velocity is not constant but fluctuates with movements in interest rates.
(b) that velocity is not constant but fluctuates with movements in the price level.
(c) that velocity is not constant but fluctuates with movements in the time of year.
(d) that velocity is a constant.

16. Keynes's liquidity preference theory indicates that the demand for money
(a) is purely a function of income, and interest rates have no effect on the demand for money.
(b) is purely a function of interest rates, and income has no effect on the demand for money.

(c) is both a function of income and interest rates.
(d) is both a function of government spending and income.

17. Keynes's theory of the demand for money (the liquidity preference function) is consistent with
(a) countercyclical movements in velocity.
(b) a constant velocity.
(c) procyclical movements in velocity.
(d) a relatively stable velocity.

18. The Keynesian demand for real balances can be expressed as
(a) $M_d = f(i,Y)$.
(b) $M_d/P = f(i)$.
(c) PY/M.
(d) $M_d/P = f(i,Y)$.

19. The Baumol-Tobin analysis suggests that
(a) velocity is relatively constant.
(b) the transactions component of the demand for money is negatively related to the level of interest
rates.
(c) the speculative motive is nonexistent.
(d) both (a) and (b) of the above are true.
(e) both (b) and (c) of the above are true.

20. According to Friedman's modern quantity theory approach, the return to money includes
(a) the services provided by banks on checkable deposits.
(b) the interest payments on money balances.
(c) both of the above.
(d) none of the above.

21. Friedman's assumption that money and goods are substitutes indicates that
(a) changes in the money supply have only indirect effects on aggregate spending.
(b) changes in the money supply may have a direct effect on aggregate spending.
(c) interest rates have no effect on money demand, implying the velocity is constant.
(d) both (b) and (c) of the above are true.

22. Although Milton Friedman does not hold that velocity is a constant, he does conclude that
    (a) the money supply is the primary determinant of nominal income.
    (b) changes in velocity will be highly predictable.
    (c) changes in velocity are not predictable.
    (d) both (a) and (b) of the above are correct.

23. In Friedman's modern quantity theory, velocity depends upon
    (a) interest rates.
    (b) the ratio of actual to permanent income.
    (c) the ratio of interest rates to actual income.
    (d) the ratio of prices to interest rates.
    (e) the ratio of money to prices.

24. In Friedman's modern quantity theory, velocity is procyclical because
    (a) money demand depends on permanent income, which is more stable than actual income.
    (b) money demand depends on actual income, which is more stable than permanent income.
    (c) velocity depends upon interest rates, which are stable over the business cycle.
    (d) velocity depends upon interest rates, which move procyclically.
    (e) velocity depends upon the money supply, which is controlled by the Federal Reserve System.

25. In the liquidity trap
    (a) a small change in interest rates produces a small change in the quantity of money demanded.
    (b) a small change in interest rates produces no change in the quantity of money demanded.
    (c) money demand is not affected by interest rates.
    (d) a small change in interest rates produces a very large change in the quantity of money demanded.