Business in Action 9th edition Bovee Test Bank

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***Business in Action, 9e* (Bovee/Thill)**
Chapter 2 Economics, Money, and Banking

1) _____ is/are the study of how a society uses scarce resources to produce and distribute goods.
A) Opportunity costs
B) Economics
C) Capitalism
D) Entrepreneurship
E) Socialism
Answer: B
Explanation: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

2) Microeconomics includes the study of _____.
A) the costs of production as a means of stimulating the economy
B) the application of economic and financial data and statistics
C) the overall working of an economy in the society including its monetary and fiscal policies
D) policies that raise capital and labor output by increasing the incentive to produce
E) economic behavior among consumers and businesses
Answer: E
Explanation: The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

3) Which of the following refers to people and their individual talents and capabilities?
A) Natural resources
B) Knowledge
C) Capital investments
D) Human resources
E) Entrepreneurship
Answer: D
Explanation: Human resources are people and their individual talents and capacities.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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4) The money, equipment, and buildings that a business needs in order to produce goods and services are called _____.
A) natural resources
B) human resources
C) capital
D) knowledge
E) entrepreneurship
Answer: C
Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

5) _____ is/are led by innovation, initiative, and the willingness to take the risks in creating and operating businesses.
A) Opportunity costs
B) Socialization
C) Macroeconomics
D) Deregulation
E) Entrepreneurship
Answer: E
Explanation: Entrepreneurship is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

6) Which of the following creates competition for finite resources, thereby forcing trade-offs by participants in the economy?
A) Redundancy
B) Scarcity
C) Opportunity costs
D) Free market systems
E) Planned systems
Answer: B
Explanation: Scarcity doesn't mean a shortage of a particular resource; rather, it means that the resource has a finite supply. Scarcity has two powerful effects: It creates competition for resources, and it forces trade-offs on the part of every participant in the economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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7) The value given up when a different opportunity was pursued is referred to as _____.
A) opportunity cost
B) factors of production
C) scarcity value
D) finite supply
E) affordability
Answer: A
Explanation: Opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

8) Which factor of production represents the collective intelligence of an organization?
A) Natural resources
B) Human resources
C) Capital
D) Entrepreneurship
E) Knowledge
Answer: E
Explanation: Each society must decide how to use its economic resources, or factors of production. Knowledge is the collective intelligence of an organization.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

9) In the global marketplace, which of the following is often a type of key asset needed to successfully utilize an advantage?
A) Capital
B) Supplies
C) Intellectual
D) Production location
E) Workforce
Answer: C
Explanation: Traditionally, a business or a country was considered to have an advantage if its location offered plentiful supplies of natural resources, human resources, capital, and entrepreneurs. In today's global marketplace, however, intellectual assets are often the key.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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10) What can companies use to protect themselves in long-term purchasing contracts?
A) Producer price index
B) Gross domestic product rates
C) Inflation rate clauses
D) Price-escalation clauses
E) Consumer price index
Answer: D
Explanation: In addition to monitoring economic activity, PPIs have a number of managerial uses, from helping companies place an accurate value on inventories to protecting buyers and sellers with price-escalation clauses in long-term purchasing contracts.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

11) What is gross domestic product?
A) Products a country is famous for producing
B) An up and down swing in the economy.
C) A measure of a country's economic health.
D) All products produced and used within a country
E) An indication of an economy that is growing and consumers are spending more money.
Answer: C
Explanation: The broadest measure of an economy's health is the gross domestic product (GDP). Gross domestic product measures a country's output—its production, distribution, and use of goods and services—by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year).
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

12) The _____ measures the rate of inflation by comparing changes in the prices of a representative basket of goods and services such as clothing, food, housing, and utilities.
A) gross domestic product (GDP)
B) producer price index (PPI)
C) inflationary stability index (ISI)
D) consumer price index (CPI)
E) economic stimulus index (ESI)
Answer: D
Explanation: The consumer price index (CPI) measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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13) The _____ measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need.
A) gross domestic product (GDP)
B) producer price index (PPI)
C) inflationary stability index (ISI)
D) consumer price index (CPI)
E) economic stimulus index (ESI)
Answer: B
Explanation: The producer price index (PPI) measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need. Like the CPI, the PPI is often referred to as a single index, but it is actually a family of more than 600 industry-specific indexes.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

14) Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.
Answer: TRUE
Explanation: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

15) Capital includes land and minerals that a business needs in order to produce goods and services.
Answer: FALSE
Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

16) Scarcity creates competition for resources, and forces trade-offs on the part of every participant in the economy.
Answer: TRUE
Explanation: Scarcity has two powerful effects: It creates competition for resources, and it forces trade-offs on the part of every participant in the economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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17) Deciding how much money to spend on new manufacturing equipment versus launching a new advertising campaign is described as opportunity cost.
Answer: FALSE
Explanation: Opportunity cost refers to the value of the most appealing alternative from all those that weren't chosen. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

18) Compare and contrast microeconomics and macroeconomics.
Answer: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services. Economics is divided into a small-scale perspective and a large-scale perspective. The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics. The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics. While microeconomics looks at the small picture and macroeconomics looks at the big picture, understanding the economy at either scale requires an understanding of how the small and large forces interact. For instance, a number of macro forces and policies determine whether homeowners can afford to install solar energy systems. In turn, the aggregate behavior of all those homeowners at the micro level affects the vitality and direction of the overall economy.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

19) Explain the different factors of production.
Answer: *Natural resources* are things that are useful in their natural state, such as land, forests, minerals, and water. *Human resources* are people and their individual talents and capacities. *Capital* includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services. *Entrepreneurship* is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses. *Knowledge* is the collective intelligence of an organization.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

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20) Compare and contrast between trade-offs and opportunity costs.
Answer: Due to universal scarcity of resources, consumers, companies, and governments are constantly forced to make trade-offs, meaning they have to give up something to get something else. You have to decide how to spend the 24 hours you have every day, and every choice involves a trade-off—the more time you spend on one activity means less time for every other activity you could possibly pursue. Businesses must make similar trade-offs, such as deciding how much money to spend on advertising a new product versus how much to spend on the materials used to make it, or deciding how many employees to have in sales versus customer support. Opportunity cost refers to the value of the most appealing alternative from all those you didn't choose. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, explain why scarcity is central to economic decision making, and identify the major ways of measuring economic activity.

21) In a _____, companies can decide what to produce, how to produce, whom to sell to, and at what price to sell.
A) planned system
B) regulated economy
C) socialist economy
D) free-market system
E) communist economy
Answer: D
Explanation: In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed—or to fail—by their own efforts.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

22) The _____ economic system allows individuals to own and operate the majority of businesses with limited economic intervention by the government.
A) mixed
B) planned
C) capitalist
D) free-market
E) communist
Answer: A
Explanation: The practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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23) Which of the following is characteristic of a country with a planned economic system?
A) The economy relies chiefly on market forces to allocate goods and resources and to determine prices.
B) The economic system combines private and state enterprises with limited intervention from the government.
C) The economy subscribes to capitalistic competition, where private parties own and operate the majority of businesses.
D) The economic system is primarily capitalistic, but there is some degree of government ownership of the means of production.
E) The economy is largely controlled by the government and freedom of choice is limited in order to accomplish government goals.
Answer: E
Explanation: In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

24) The economic system that allows individuals the least degree of economic freedom is _____.
A) free-market
B) planned
C) capitalism
D) authoritarianism
E) mixed capitalism
Answer: B
Explanation: In a planned system, also called a command system or a command-and-control system, government controls the allocation of resources, including decisions regarding which products are produced and in what quantities. Planned economies are often equated with socialism, which in its most developed theoretical form involves collective ownership of the means of production.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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25) _____ occurs when a government takes control of a company or industry, which may result in a change in the entire economy.
A) Privatization
B) Deregulation
C) Nationalization
D) Free-market systems
E) Monopolistic competition
Answer: C
Explanation: The line between socialism and capitalism isn't always easy to define, and it doesn't always stay in the same place, either. Governments can change the structure of the economy by nationalizing—taking ownership of—selected companies or in extreme cases even entire industries.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

26) Which of the following is one of the ways the government helps to stabilize or stimulate the national economy?
A) Changes in supply
B) Changing monetary policy
C) Adjusting equilibrium pricing
D) Eliminating monopolies
E) Instituting an oligopoly
Answer: B
Explanation: Governments have two sets of tools they can use to stabilize and stimulate the national economy: monetary policy and fiscal policy.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

27) Which of the following involves changing the government's revenues or expenditures to change the growth rate of the economy?
A) Monetary policy
B) Antitrust regulation
C) Deregulation
D) Fiscal policy
E) Regulation
Answer: D
Explanation: Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation. On the revenue side, governments can adjust the revenue they bring in by changing tax rates and various fees collected from individuals and businesses.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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28) Governments established _____ in an effort to ensure all competitors have an equal chance of succeeding.
A) fiscal policies
B) trusts
C) free-market economies
D) antitrust legislation
E) deregulation legislation
Answer: D
Explanation: Antitrust laws limit what businesses can and cannot do, to ensure that all competitors have an equal chance of succeeding.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

29) Which of the following actions of the government indicates the privatization of an industry?
A) Allowing private businesses to operate in an industry that was previously operated by the government
B) Discouraging private business to operate in an industry that is critical for the growth of the economy
C) Acquiring the market leader to gain control of the industry and its resources
D) Imposing taxes on scarce raw materials to discourage unfair pricing by its suppliers
E) Imposing regulations on multinational businesses to protect local businesses
Answer: A
Explanation: Governments can change the structure of the economy by nationalizing—assuming ownership of—selected companies or, in extreme cases, even entire industries. They can also move in the opposite direction, privatizing services once performed by the government by allowing private businesses to perform them instead.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

30) Which of the following best describes deregulation?
A) Putting rules in place to govern economic activity
B) Having fewer rules and relying on the market to prevent excesses
C) Encouraging all stakeholders to put pressure on organizations to save money
D) Adjusting the amount of "spendable" money in the economy at any given time
E) Increasing the revenues to stimulate spending and limiting inflation
Answer: B
Explanation: Much of the debate about the government's role can be framed as a question of regulation versus deregulation–having more rules in place to govern economic activity or versus having fewer rules in place and relying more on the market to prevent excesses and correct itself over time.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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31) _____ laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.
A) Fiscal
B) Discrimination
C) Antitrust
D) Stabilization
E) Equilibrium
Answer: C
Explanation: Antitrust laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

32) Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
Answer: TRUE
Explanation: Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

33) In practice, no economy is truly a free-market economy.
Answer: TRUE
Explanation: Free market economy is a situation in which so many buyers and sellers exist that no single buyer or seller can individually influence market prices. In practice, no economy is truly a free-market economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

34) Fiscal policy involves the government limiting the nation's "spendable" money in the economy at any given time.
Answer: FALSE
Explanation: Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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35) Global economists use the terms capitalism and private enterprise to describe centrally planned economic systems.
Answer: FALSE
Explanation: The terms capitalism and private enterprise are often used to describe free-market systems.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

36) Compare and contrast between free-market systems and planned systems.
Answer: In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed—or to fail—by their own efforts. Capitalism and private enterprise are the terms most often used to describe the free-market system, one in which private parties (individuals, partnerships, or corporations) own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive. The planned system that allows individuals the least degree of economic freedom is communism.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

37) Is there such a thing as a "free" economy? Explain and support your views.
Answer: In practice, no economy is truly "free."
Local, state, national, and even international governments, such as the European Community, intervene in the economy to accomplish goals that leaders deem socially or economically desirable. This practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls. Price controls can involve maximum allowable prices (such as limiting rent increases) and minimum allowable prices (such as supplementing the prices of agricultural goods to ensure producers a minimum level of income or establishing minimum wage levels).
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

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38) Discuss how antitrust legislation fosters competition in the marketplace.
Answer: Based on the belief that fair competition benefits the economy and society in general, governments intervene in markets to preserve competition and ensure that no single enterprise becomes too powerful. For instance, if a company has a monopoly, it can potentially harm customers by raising prices or stifling innovation and harm potential competitors by denying access to markets. Numerous laws and regulations have been established to help prevent individual companies or groups of companies from taking control of markets or acting in other ways that restrain competition or harm consumers. Antitrust laws limit what businesses can and cannot do, to ensure that all competitors have an equal chance of succeeding. Some of the earliest government moves in this arena produced such landmark pieces of legislation as the Sherman Antitrust Act, the Clayton Antitrust Act, and the Federal Trade Commission Act, which generally sought to rein in the power of a few huge companies that had financial and management control of a significant number of other companies in the same industry. Usually referred to as trusts (hence the label antitrust legislation), these huge companies controlled enough of the supply and distribution in their respective industries. Governments remain active in antitrust activities to this day, with tech giants such as Google, Facebook, Amazon, and Microsoft getting hit with antitrust lawsuits and penalties that sometimes run into the billions of dollars.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

39) Explain why socialism and capitalism are not mutually exclusive and provide an example.
Answer: While free-market capitalism remains the foundation of the U.S. economy, some important elements of the U.S. economy are socialized and have been for many years. Public schools, the postal service, much of the transportation infrastructure, various local and regional utilities, and several major health care programs all fit the economic definition of socialism. Socialism and capitalism are competing philosophies, but they are not mutually exclusive, and each approach has strengths and weaknesses, which is why most modern economies combine aspects of both.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Define economic system, and explain the government's role in a free-market economy.

40) Which of the following refers to the amount of a good or service that customers will buy at a given time at various prices?
A) Demand
B) Utility
C) Equilibrium
D) Necessity
E) Want
Answer: A
Explanation: Demand refers to the amount of a good or service that customers will buy at a given time.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

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41) _____ refers to the quantities of a good or service that producers will provide on a particular date at various prices.
A) Necessity
B) Supply
C) Demand
D) Utility
E) Want
Answer: B
Explanation: Supply refers to the quantities of a good or service that producers will provide on a particular date at various prices.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

42) A(n) _____ shows the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.
A) supply curve
B) inflation rate
C) demand curve
D) deflation rate
E) competitive balance
Answer: C
Explanation: A demand curve is a graph showing the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

43) Demand curves typically slope downward. This implies that a(n) _____.
A) decrease in price will increase the quantity demanded
B) decrease in price will decrease the quantity demanded
C) increase in price will increase the quantity demanded
D) decrease in price will have no effect on quantity demanded
E) increase in price will have no effect on quantity demanded
Answer: A
Explanation: Demand curves typically slope downward, implying that as price drops, more people are willing to buy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

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44) The _____ depicts the relationship between prices and quantities that sellers will offer for sale, regardless of demand.
A) fiscal cycle
B) supply curve
C) equilibrium point
D) business cycle
E) competitive analysis
Answer: B
Explanation: The depiction of the relationship between prices and quantities that sellers will offer for sale is called a supply curve.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

45) Movement along the supply curve typically slopes upward because _____.
A) the amount of government regulation in an industry rises with increase in demand
B) the quantity that the sellers are willing to supply rises with decrease in demand
C) the amount of government regulation in an industry rises with an increase in price
D) the quantity that the sellers are willing to supply rises with increase in government regulation
E) the quantity that the sellers are willing to supply rises with an increase in price
Answer: E
Explanation: Movement along the supply curve typically slopes upward: as prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

46) The point at which the demand and supply curves intersect—the point at which the quantity demanded and supplied are balanced is called the _____.
A) equilibrium point
B) aggregation point
C) marginal point
D) break-even point
E) distribution point
Answer: A
Explanation: The point at which the demand and supply curves intersect—the point at which the quantity demanded and supplied are equal—is the equilibrium point.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

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47) Demand refers to the quantities of a good or service that producers will provide on a particular date at various prices.
Answer: FALSE
Explanation: Demand refers to buyers' willingness and ability to purchase products at various price points.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

48) The demand curve will shift to the left if the price of substitute products increases.
Answer: FALSE
Explanation: The demand curve will shift to the right if the price of substitute products increases.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

49) Movement along the supply curve typically slopes upward.
Answer: TRUE
Explanation: Movement along the supply curve typically slopes upward: As prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

50) The supply curve of a firm will shift to the right if technology increases the firm's production costs.
Answer: FALSE
Explanation: The supply curve of a firm will shift to the left if technology increases the firm's production costs.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

51) The equilibrium point is the point at which quantity of a good or service equals the quantity demanded.
Answer: TRUE
Explanation: The point at which quantity of a good or service equals the quantity demanded is known as the equilibrium point.
Difficulty: 1: Easy
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

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52) "As the supply and demand curves are dynamic, so is the equilibrium point." Explain this statement with an example.
Answer: As variables affecting supply and demand change, so will the equilibrium price. For example, increased concerns about airline safety could encourage some travelers to choose alternatives such as automobile travel or web conferencing, thus reducing the demand for air travel at every price and moving the equilibrium point as well. Suppliers might respond to such a reduction in demand by either cutting the number of flights offered or lowering ticket prices in order to restore the equilibrium level.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

53) The term _____ is used to characterize the fluctuations in an economy's rate of growth over a period of several years.
A) microeconomics
B) competitive pressures
C) cyclical machinations
D) business cycles
E) economic repercussions
Answer: D
Explanation: Business cycles are fluctuations in the rate of growth that an economy experiences over a period of several years.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

54) _____ occurs when no single firm is large enough to influence prices and distort the workings of the free-market system.
A) Pure monopoly
B) Inflation
C) Pure competition
D) Deflation
E) Recession
Answer: C
Explanation: Pure competition is a situation in which no single firm is large enough to influence prices and distort the workings of the free-market system.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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55) When the number of competitors in a market is small, and competitors influence each other through production and pricing decisions, a situation known as _____ is created.
A) monopoly
B) duopoly
C) oligopoly
D) monopolistic competition
E) pure competition
Answer: C
Explanation: When the number of competitors in a market is quite small, a situation known as oligopoly is created. Customers have some choice, unlike in a monopoly, but not as many choices as in monopolistic competition.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

56) Which of the following is a characteristic feature of economic contraction?
A) Decreased unemployment rates
B) Decreased consumer spending
C) Increased income
D) Increased employment
E) Increased demand
Answer: B
Explanation: During an economic contraction, spending declines, employment drops, and the economy as a whole slows down.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

57) The term _____ indicates two consecutive quarters of decline in the country's gross domestic product.
A) deflation
B) stagnation
C) depression
D) stagflation
E) recession
Answer: E
Explanation: If the period of downward swing is severe, the nation may enter into a recession. There are no official definitions of what constitutes a recession, but a common benchmark is a decline in GDP for two consecutive quarters.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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58) A deep and prolonged recession is known as _____.
A) an economic contraction
B) stagnation
C) deflation
D) demand immobilization
E) a depression
Answer: E
Explanation: A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

59) When a downward swing or recession is over, the economy enters into a period of _____.
A) recovery
B) depression
C) contraction
D) stagnation
E) repercussion
Answer: A
Explanation: When a downward swing or recession is over, the economy enters into a period of recovery.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

60) _____ unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new job.
A) Structural
B) Intrinsic
C) Frictional
D) Cyclical
E) Seasonal
Answer: C
Explanation: Frictional unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new one.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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61) When demand for goods and services drops, businesses reduce production, resulting in economic contraction. The unemployment resulting because of this phenomenon is known as _____ unemployment.
A) intrinsic
B) cyclical
C) structural
D) seasonal
E) frictional
Answer: B
Explanation: When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. This leads to cyclical unemployment.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

62) Which of the following reflects the percentage of the labor force currently without work?
A) Economic contraction
B) Economic fluctuation
C) Deflation
D) Monopolistic competition
E) Unemployment rate
Answer: E
Explanation: The unemployment rate indicates the percentage of the labor force currently without employment. The labor force consists of people ages 16 and older who are either working or looking for jobs.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

63) Why is inflation a concern for businesses and consumers?
A) Inflation affects the amount of goods and services you can buy for a given amount of money.
B) Inflation affects the amount of government intervention in small businesses.
C) Inflation affects the potential sustained fall in average prices.
D) Inflation affects the ability for sustained economic contraction.
E) Inflation affects the amount of goods and services a firm can produce in a production cycle.
Answer: A
Explanation: Inflation is a steady rise in the average prices of goods and services throughout the economy. Inflation is a major concern for consumers, businesses, and government leaders because of its effect on purchasing power or the amount of a good or service you can buy for a given amount of money.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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64) The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.
Answer: TRUE
Explanation: The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

65) A deep and prolonged recession can be considered a depression.
Answer: TRUE
Explanation: A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

66) Frictional unemployment is caused by economic fluctuations.
Answer: FALSE
Explanation: Frictional unemployment refers to the natural flow of workers into and out of jobs, such as when a person leaves one job without first lining up a new job.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

67) Deflation is an economic condition in which prices fall steadily throughout the economy.
Answer: TRUE
Explanation: Deflation is an economic condition in which prices fall steadily throughout the economy.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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68) Cyclical unemployment is caused by a mismatch between workers' skills and current employer needs.
Answer: FALSE
Explanation: Cyclical unemployment refers to seasonal unemployment caused by economic fluctuations. When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

69) How does capitalism promote monopolistic competition in the market?
Answer: Most of the competition in advanced free-market economies is monopolistic competition, in which a number of sellers offer products that can be distinguished from competing products in at least some small way. The risk/reward nature of capitalism promotes constant innovation in pursuit of competitive advantage, rewarding companies that do the best job of satisfying customers.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

70) Differentiate between structural and cyclical unemployment.
Answer: Structural unemployment occurs due to a mismatch between the skills of workers and the needs of employers. Workers can't find jobs that match their qualifications, and employers can't find employees with the skills their job openings require. Structural unemployment is an ongoing concern because changes in the external environments of business make some skills obsolete and create demand for new skills.
Cyclical unemployment is caused by economic fluctuations. When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. Then, an increasing number of people who want to work can't find jobs. During catastrophic depressions, cyclical unemployment can run as high as 20 or 25 percent.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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71) Define and discuss the term *business cycles*.
Answer: The economy is always in a state of change, expanding or contracting in response to the combined effects of factors such as technological breakthroughs, changes in investment patterns, shifts in consumer attitudes, world events, and basic economic forces. *Business cycles* represent the fluctuations in the rate of growth that an economy experiences over a period of several years. These cycles include *economic expansion*, when the economy is growing and consumers are spending more money, which stimulates higher employment and wages, which then stimulate more consumer purchases. The cycles include *economic contraction*, when spending declines, employment drops, and the economy as a whole slows down. Even though experts call these up-and-down swings business cycles, this term is somewhat misleading, because real economies do not expand and contract in regular and predictable "cycles." More accurately, the behavior of an economy can be characterized as e*conomic fluctuations*.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

72) Money serves as a _____ when it is used as a way of accumulating wealth until it is needed.
A) unit of accounting
B) means of payment
C) temporary store of value
D) medium of exchange
E) standard of deferred payment
Answer: C
Explanation: Money serves as a temporary store of value when used as a way of accumulating wealth until it is needed.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

73) Money serves as a(n) _____ to simplify transactions because a buyer can trade it for a good or service.
A) unit of accounting
B) indication of value
C) debt obligation
D) measure of liquidity
E) medium of exchange
Answer: E
Explanation: Money is anything generally accepted as a means of paying for goods and services. Money performs four financial functions. First, it serves as a medium of exchange, a tool for simplifying transactions between buyers and sellers.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

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74) In addition to trust, which of the following is the basis for the practical value of money?
A) Liquidity
B) Exchange rate
C) Medium of exchange
D) Unit of accounting
E) Store of value
Answer: A
Explanation: The practical value of money stems from two key properties: liquidity and trust. Money is the most liquid asset because it can be exchanged easily and more or less instantly for something else of value.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

75) In the money supply, what represents the cash held by the public and money deposited in checking accounts?
A) Liquidity
B) M1
C) Store of value
D) Time deposits
E) M2
Answer: B
Explanation: The money supply can be measured in several ways. Economists focus on two aggregates known as M1 and M2. M1 consists of cash held by the public and money deposited in a variety of checking accounts. In simple terms, M1 is money that is spendable now, and M2 adds money that could be spendable fairly soon.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

76) Which of the following best describes cryptocurrency?
A) Digital tokens issued to workers in a gig economy
B) Digital tokens that rely on cryptography for security
C) Any currency tied to a physical asset such as gold
D) A currency that is liquid and can be easily exchanged for tangible products
E) A measure of value that is consistent with every transaction
Answer: B
Explanation: Today, a new wave of alternative money is happening in the form of cryptocurrencies, digital tokens that rely on cryptography for security.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

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77) Money is anything generally accepted as a means of paying for goods and services.
Answer: TRUE
Explanation: Money is anything generally accepted as a means of paying for goods and services. It serves as a medium of exchange, a unit of accounting, a store of value, and a standard of deferred value.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

78) As an aggregate measure of the money supply, M1 consists of cash held by the public, as well as money in a variety of checking accounts.
Answer: TRUE
Explanation: In order to measure the money supply, economists focus on two aggregates known as M1 and M2. M1 consists of cash held by the public and money in a variety of checking accounts. M2 consists of money held in interest-paying accounts that may restrict the owner's right to withdraw funds on short notice.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

79) What are the four essential functions of money?
Answer: Money is anything generally accepted as a means of paying for goods and services. Every country has its own system of money, or currency, except for those that opt to share a currency such as the euro. Money performs four essential functions. First, it serves as a medium of exchange, a tool for simplifying transactions between buyers and sellers. Second, it serves as a unit of accounting (a measure of value, in other words) so that buyers and sellers don't have to negotiate the relative worth of dissimilar items with every transaction. Third, money serves as a temporary store of value-a way of accumulating wealth until it is needed. Fourth, money serves as a standard of deferred payment, meaning it can be used to represent debt obligations.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.5: List the four financial functions of money, and define two key measures of the money supply.

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80) The _____ is a fundamental driver of economic behavior because it influences short-term and long-term interest rates, foreign exchange rates, and inflation.
A) retail banking manifesto
B) amortization ratio
C) global prime rate
D) federal funds rate
E) prime mortgage market
Answer: D
Explanation: The federal funds rate is a fundamental driver of economic behavior because it influences short-term and long-term interest rates, foreign exchange rates, and inflation.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

81) Which of the following can be done by the Federal Reserve to inject money into the economy and decrease the federal funds rate?
A) The Federal Reserve reducing the discount window for banks
B) The Federal Reserve imposing selective credit controls
C) The Federal Reserve buying Treasury bonds
D) The Federal Reserve increasing short-term loans available to banks
E) The Federal Reserve increasing the reserve requirement on deposits
Answer: C
Explanation: When the Federal Reserve buys Treasuries, this action injects money into the economy, thereby increasing the money supply, which tends to then decrease the federal funds rate. The opposite effect happens when the Federal Reserve sells Treasuries: Selling pulls money out of the economy, decreasing the money supply and increasing the federal funds rate.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

82) Which of the following federal actions has the goal of reducing the money supply in markets?
A) The Federal Reserve liberalizes credit control actions on loans.
B) The Federal Reserve buys treasury bills from the market.
C) The Federal Reserve raises the discount rate.
D) The Federal Reserve reduces the reserve requirement.
E) The Federal Reserve promotes new loans to small businesses.
Answer: C
Explanation: The discount rate is the interest rate that member banks pay when they borrow funds from the Federal Reserve. Raising the discount rate discourages loans and therefore, tightens the money supply.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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83) _____ rate is the rate a bank charges its best loan customers.
A) Federal funds
B) Discount
C) Prime
D) Paper
E) Overnight
Answer: C
Explanation: Prime rate is the rate a bank charges its best loan customers. Many other interest rates are also based on the prime rate.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

84) The _____ is the federal agency responsible for protecting money in customer accounts and managing the transition of assets whenever a bank fails.
A) Federal National Loan Corporation
B) Federal Deposit Insurance Corporation
C) Federal Home Loan Association
D) Federal Mortgage Corporation
E) Federal National Mortgage Association
Answer: B
Explanation: After thousands of banks failed in the United States during the Great Depression, the government established the Federal Deposit Insurance Corporation (FDIC). It is the federal agency responsible for protecting money in customer accounts and managing the transition of assets whenever a bank fails.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

85) _____ is the government-sponsored enterprise responsible for guaranteeing and funding home mortgages for low and moderate income buyers.
A) The secondary mortgage market
B) The Federal discount window
C) Fannie Mae
D) The NYSE
E) The Federal Deposit Insurance Corporation
Answer: C
Explanation: Fannie Mae and Freddie Mac are two quasi-public companies that operate under the close supervision of the federal government with a mandate to support home ownership for low- and moderate-income buyers by making mortgage funding more readily available.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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86) _____ refers to sums of money (equal to a certain percentage of their deposits) that banks are legally required to keep on hand.
A) Securities
B) Mortgages
C) Reserves
D) Savings
E) Collateral
Answer: C
Explanation: All depository institutions (those that accept deposits from customers), including commercial banks, savings and loan associations, and credit unions, are required to hold a portion of those deposits in reserve).
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

87) Which of the following offers investing and advisory services to organizational customers, including governments?
A) Merchant bank
B) Credit union
C) Thrift bank
D) Private bank
E) Investment bank
Answer: E
Explanation: Investment banks offer a variety of services related to initial public stock offerings, mergers and acquisitions, and other investment matters.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

88) _____ offer financial services to businesses, particularly in the area of international finance.
A) Investment banks
B) Retail banks
C) Private banks
D) Credit unions
E) Merchant banks
Answer: E
Explanation: Merchant banks offer financial services to businesses, particularly in the area of international finance. Merchant banking is sometimes more narrowly defined as managing private equity investments, making it more akin to investment banking.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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89) Banking institutions that offer deposit accounts and focus on offering home mortgage loans are known as _____.
A) merchant banks
B) retail banks
C) thrift banks
D) private banks
E) credit unions
Answer: C
Explanation: Thrift banks, also called thrifts, or savings and loan associations, offer deposit accounts and focus on offering home mortgage loans.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

90) _____ are not-for-profit, member-owned cooperatives that offer deposit accounts and lending services to consumers and small businesses.
A) Loan associations
B) Retail banks
C) Credit unions
D) Thrift banks
E) Merchant banks
Answer: C
Explanation: Credit unions are not-for-profit, member-owned cooperatives that offer deposit accounts and lending services to consumers and small businesses.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

91) The federal funds rate is also known as the *overnight rate*.
Answer: TRUE
Explanation: The federal funds rate (aka, overnight rate) is the rate that member banks charge each other to borrow money overnight from the funds they keep in the Federal Reserve accounts.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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92) The discount rate is the interest rate that member banks charge each other to borrow money overnight from the funds they keep in the Federal Reserve accounts.
Answer: FALSE
Explanation: Discount rate is the rate that member banks pay when they borrow funds from the Federal Reserve.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

93) If the Federal Reserve sells Treasuries in open-market operations, the country's money supply increases.
Answer: FALSE
Explanation: If the Federal Reserve sells Treasuries in open-market operations, the country's money supply decreases.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

94) If the Federal Reserve buys Treasuries on the open market, the country's money supply increases.
Answer: TRUE
Explanation: If the Federal Reserve buys Treasuries on the open market, the country's money supply increases.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

95) The prime rate is the interest rate that a bank charges its most creditworthy customers.
Answer: TRUE
Explanation: The prime rate is the interest rate that a bank charges its most creditworthy customers.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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96) What is the relationship between the Federal Reserve's *reserve requirement* and the money supply?
Answer: All *depository institutions* (those that accept deposits from customers) are required to hold a portion of those deposits in *reserve*. The institutions may keep the reserve as cash in their own vaults or in an account at a regional Federal Reserve bank. By changing the reserve percentage, the Federal Reserve allows these institutions to lend out more or less of their deposited amounts, thereby affecting the size of the money supply. In contrast to the frequency of open-market operations, however, the Federal Reserve does not change the reserve ratio frequently because doing so is costly to implement and a small change can have a drastic effect.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

97) Identify and discuss the Federal Reserve's major responsibilities.
Answer: The work of the Federal Reserve can be divided into three broad categories: (1) serving as a bank for the federal government and many commercial banks, (2) supervising and regulating many financial institutions, and (3) managing the nation's money supply by designing and implementing monetary policy. As the "bank for banks," the Federal Reserve provides many of the services that a commercial bank provides to businesses and consumers. It also operates two electronic systems for transferring money between banks: one for large amounts of cash and the smaller automated clearing house (ACH) system for routine payments made by check.
The Federal Reserve monitors the operation of state banks that are members of the Federal Reserve system, all bank holding companies (companies than own multiple banks), and the U.S. operations of foreign banks. The Federal Reserve's key objectives are making sure that banks are financially sound and that customers' accounts are safe. Moreover, it has the authority to take formal or informal action against banks that are out of compliance with Federal Reserve guidelines. Two other important aspects of the Federal Reserve's regulatory mandate are approving bank mergers and acquisitions and implementing finance-related consumer protection laws. Monetary policy is decided by the Federal Open Market Committee (FOMC), which includes the Federal Reserve's board of governors, the president of the New York City Fed, and 4 of the other 11 regional presidents. The three primary goals of maximum employment, stable prices, and moderate inflation are sometimes in conflict, so the FOMC faces a constant balancing act as it tries to optimize the overall results.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.6: Explain the role of the Federal Reserve System, list the major types of banking institutions, and summarize banking's role in the economy.

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98) Which of the following describes the wide range of innovations that have the potential to improve financial services or cause radical disruption of them?
A) Neobanking
B) Freddie Mac
C) Fintech
D) Crowdfunding
E) Peer-to-peer lending
Answer: C
Explanation: The term fintech is used as a label for a wide range of innovations that have the potential to improve financial services–and in some instances, radically disrupt them. At least 10,000 companies are active in fintech, so advances are taking place in just about every corner of banking, investing, and insurance.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.7: Define fintech, and discuss five ways that financial institutions are innovating with digital technology.

99) _____ use(s) cloud technology to provide services through mobile and digital channels, thereby reducing the cost of banking services.
A) Neobanks
B) Freddie Mac
C) Fintech
D) FDIC
E) Peer-to-peer lending
Answer: A
Explanation: Mobile and cloud technologies have also helped to create a new category of banks, often referred to as neobanks, which provide services entirely through mobile and digital channels. Without large staffs and physical branches to maintain, these companies have much lower cost structures and therefore can offer banking services at lower costs.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.7: Define fintech, and discuss five ways that financial institutions are innovating with digital technology.

100) Discuss how fintech innovations work to improve investor returns in portfolio management.
Answer: A final group of fintech innovations apply cognitive automation and other tools to help investors make better financial decisions without paying for the services of a financial adviser. These so-called robo advisers assemble investment portfolios based on each client's risk tolerance, resources, and objectives. These systems aim to improve investors' returns by removing emotionally driven decision making and automating tasks that are time-consuming to do manually, such as rebalancing portfolios over time and tax-loss harvesting (selling an investment that has declined in value to use the loss as a tax write-off and then buying back into the market).
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.7: Define fintech, and discuss five ways that financial institutions are innovating with digital technology.

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