

Homework 9 – KEY

Average: 77.33 + Opt GI bonus

Due on 31/10/2023, by 23:00

This assignment is optional but STRONGLY RECOMMENDED. If you do not submit the answers till the deadline, the score of your final exam will substitute for the score for this assignment. Submit only the correct letter for each task on eLearn under 'Quizzes' within 'COR2100-Economics and Society G7-8-26-49'. Note that the actual text of questions and answers is not supposed to appear on the eLearn quiz. You have unlimited attempts. The system is programmed to credit your last attempt. Be informed that if you submit an attempt and afterwards you re-open the quiz, you must submit your answers AGAIN. Otherwise, the system will grade the unfinished attempt with 0 (because it is the last one) and there is NOTHING I can do to fix this after the fact. Late homework or homework submitted outside eLearn cannot be accepted as this would violate SMU official policy for fairness and transparency in grading. This assignment is protected by Grade Insurance™: If the assignment's average turns out to be below 75, an equal amount of bonus points will be given to every work, for the average to become 75. Direct any homework questions to your TA.

1. Which of the following is a function of money?
 - A. A means of creating wealth. *[Money represents wealth, it does not create it]*
 - 72%B. **A common reference point to compare different values.** *[True. Money is a unit of account]*
 - 24%C. Both A and B.
 - D. None of the above.

2. Which of the following features of money does bitcoin fail to serve?
 - A. Portability. *[You have access to your account as long as you take your phone with you]*
 - B. Durability. *[Digital assets do not wear out]*
 - 89%C. **Objective carrier of value.** *[Its value is not objective. You may take a sleep and wake up a billionaire or penniless]*
 - D. Divisibility. *[You can use any fraction of a bitcoin]*

3. Which of the following is NOT a function of the Central Bank?
 - A. It checks commercial banks' activity.
 - 90%B. **It profits by providing loans to commercial banks.** *[CB is a non-profit institution]*
 - C. It adjusts the interest rate to stimulate the economy.
 - D. It adjusts the interest rate to control inflation.

4. In periods of high inflation, which of the following population groups is most likely to be negatively affected?
 - A. Homeowners with fixed-rate mortgages. *[Their real loan installments will become lower]*
 - B. Firms operating in oligopolistic markets. *[Oligopolies have the ability to increase their prices, since they possess market power]*
 - C. Firms with fixed long-term contracts with their suppliers. *[The real cost of paying off their suppliers will drop]*
 - 91%D. **Individuals with large savings in cash.** *[Their real wealth will decline]*

5. What is the role of money when you give \$5 to a kid, and she puts the money in her piggy bank?
 - A. Unit of account.
 - B. Security service. *[Not a role of money]*
 - C. Medium of exchange.
 - 98%D. **Store of value.** *[She will use the value in the future]*

- 6.* What is the role of money when you buy stock of your favorite company?
- 44%A. **Medium of exchange.** *[Money is exchanged for a security]*
 - B. Store of value. *[You do not keep the money]*
 - 45%C. Both A and B.
 - D. None of the above.
7. Which of the following is likely to create a tendency for the interest rate to increase?
- A. When people decide to spend more. *[When people spend more, cash for loans becomes scarcer and the price of cash (r) will tend to increase]*
 - B. When people decide to save less. *[When people save less, cash for loans becomes scarcer and the price of cash (r) will tend to increase]*
 - 17%C. When GDP increases. *[When GDP increases, more cash for loans is needed and the price of cash (r) will tend to increase]*
 - 54%D. **All of the above.**
 - 15%E. None of the above.
8. Suppose that the Central Bank increases the money supply and observes that the price level decreases. Which of the following is likely to have happened?
- 26%A. Real GDP has increased by less than the percentage change in M_s .
 - 63%B. **Real GDP has increased by more than the percentage change in M_s .**
 - C. Real GDP has increased equally to the percentage change in M_s .
 - D. Real GDP has not increased.
[Because inflation = growth of M_s - growth of Real GDP and inflation here is negative, it follows that growth of M_s < growth of Real GDP]
9. Why inflation is bad?
- 31%A. Because money loses value. *[Not necessarily bad]*
 - B. Because nominal prices of goods change. *[Not necessarily bad]*
 - 63%C. **Because the increase in wages lags behind the increase in prices.**
 - D. Because wages increase by less than the prices. *[Not necessarily true]*
10. Which of the following is LESS likely to be the reason for Open Market Sale by the CB?
- A. To increase the interest rate. *[OMS will decrease money supply, causing the rate to increase]*
 - 10%B. To reduce demanded credit. *[Increased interest rates make borrowing more expensive and reduce the quantity of loans]*
 - 72%C. **To raise prices.** *[Decrease in money supply will put a downward pressure in prices]*
 - 14%D. To stabilize the financial system. *[Could be the reason if there is pressure for the interest rate to fall]*
- 11.√ Which of the following best describes the Phillips relationship?
- 92%A. **Inflation and unemployment change in opposite directions in the S-R.**
 - B. Inflation and unemployment change in the same direction in the S-R.
 - C. Inflation and unemployment change in the same direction in the L-R.
 - D. Inflation and unemployment change in opposite directions in the L-R.
 - E. Inflation and unemployment are not correlated.
[According to the Phillips relationship, there is a short-run trade-off between inflation and unemployment: when unemployment is low, inflation tends to be high, and vice versa]

12. ✓ Which of the following is most likely to prevent commercial banks from lending money, under the scarce-reserves regime?
- A. Low interest rates. *[It does not affect banks' ability to give loans]*
 - B. A high inflation rate. *[It does not affect banks' ability to give loans]*
 - 90% C. **Limited deposits.** *[Banks will not have enough reserves to meet the demand for loans, which could prevent them from lending money]*
 - D. Increased money supply. *[It means that commercial banks have access to more money, which allows them to lend more]*
13. ✓ Which of the following do we mean by “ample reserves regime”?
- A. The Central Bank decides to whom commercial banks will lend their ample reserves.
 - B. The Central Bank decides how much deposits commercial banks accept.
 - C. The public can deposit unlimited funds into commercial banks.
 - 97% D. **The Central Bank can lend to commercial banks as much reserves as they need.**
[In this regime, the Central Bank will provide commercial banks access to as many reserves as they need to meet their demand for loans]
14. ✓ What prevents commercial banks from loaning an infinite amount of money to the economy when reserves are ample?
- A. The CB must approve their loans.
 - B. Credit risk.
 - C. The demand for loans.
 - D. Both A and B.
 - E. Both A and C.
 - 76% F. **Both B and C.**
 - G. All of the above.
 - H. None of the above.
[A finite quantity of loans is demanded for each interest rate as given by the money demand and bankers face a risk of having to pay the reserves from their pockets if a debtor defaults]
15. ✓ Economists have calculated that an initial deposit of \$400 to a commercial bank resulted in a total of \$10,000 money creation. What is the reserve ratio?
- A. Around 2%.
 - 98% B. **Around 4%.**
 - C. Around 6%.
 - D. Around 8%.
 - E. Around 10%.
- [Total money creation is $\text{deposit} \cdot \frac{1}{RR}$ or $10,000 = 400 \cdot \frac{1}{RR}$ or $RR = \frac{400}{10,000} = 4\%$]*
16. ○ Which of the following could require an increase in money supply in order to prevent the real interest rate from changing?
- 16% A. An increase in GDP. *[Money demand for transactions would increase and cause r to increase unless M_S increases too]*
 - 15% B. An increase in the price level. *[Money demand for transactions would increase and cause r to increase unless M_S increases too]*
 - C. An increase in the price of bonds. *[Money demand for speculation would increase and cause r to increase unless M_S increases too]*
 - 63% D. **All of the above.**

17. A Singaporean billionaire buys a large amount of newly issued bonds by the Singaporean government. How does this affect Singapore's money market?

22%A. Money demand increases.

29%B. Money supply increases.

C. Both A and B.

43%D. **None of the above.**

[The transaction affects neither demand for money, nor money supply. Just money changed hands from the billionaire to the government]

18. Which of the following should you expect when the interest rate increases?

22%A. Speculators will sell bonds.

77%B. **Speculators will buy bonds.**

C. Speculators will neither buy nor sell bonds.

[An increase in the interest rate means that the price of bonds decreases, thus speculators will want to buy more of them]

19. Which of the following is most likely to increase M0 money ceteris paribus?

A. An increase in unemployment. *[Not related to the quantity of money]*

B. A decrease in government spending. *[Through government spending, the same money is transferred from the taxpayers to the government and then back to the economy]*

30%C. The increase in money demand. *[This money demand should not affect the money supply ceteris paribus]*

67%D. **The fear of a banking collapse domino.** *[This will lead to people holding more cash, thus increasing M0]*

20. Which of the following best describes the term "inflation tax"?

A. A tax on the income of individuals paid to the government in order to curb high inflation.

B. A sales tax firms pay for charging higher prices in periods of high inflation.

C. The cost that firms face from updating their prices in periods of high inflation.

94%D. **The transfer of purchasing power from individuals to the government due to inflation caused by increase in money supply.** *[As discussed in class]*