

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

- 1) The quantity theory of money is a theory of how \_\_\_\_\_  
A) the nominal value of aggregate income is determined.  
B) the money supply is determined.  
C) the real value of aggregate income is determined.  
D) interest rates are determined.
- 2) If the money supply is \$500 and nominal income is \$4,000, the velocity of money is \_\_\_\_\_  
A) 1/20.                      B) 1/8.                      C) 8.                      D) 20.
- 3) If the money supply is \$2 trillion and velocity is 5, then nominal GDP is \_\_\_\_\_  
A) \$1 trillion.                      B) \$2 trillion.                      C) \$5 trillion.                      D) \$10 trillion.
- 4) The equation of exchange is \_\_\_\_\_  
A)  $M + V = P + Y$ .                      B)  $M \times V = P \times Y$ .                      C)  $M + Y = V + P$ .                      D)  $M \times P = V \times Y$ .
- 5) For the classical economists, the quantity theory of money provided an explanation of movements in the price level. Movements in the price level result \_\_\_\_\_  
A) primarily from changes in the quantity of money.  
B) only partially from changes in the quantity of money.  
C) solely from changes in the quantity of money.  
D) from changes in factors other than the quantity of money.
- 6) The empirical evidence regarding the velocity of money indicates that velocity tends to be \_\_\_\_\_; that is, velocity \_\_\_\_\_ when economic activity contracts. \_\_\_\_\_  
A) procyclical; increases                      B) procyclical; declines  
C) countercyclical; declines                      D) countercyclical; increases
- 7) Until the Great Depression, economists did not recognize that velocity \_\_\_\_\_  
A) declines during rapid economic expansions, since money growth fails to keep pace.  
B) fails to decline during economic contractions.  
C) declines during severe economic contractions.  
D) increases during severe economic contractions.

- 8) The Keynesian theory of money demand predicts that people will increase their money holdings if they believe that \_\_\_\_\_ 8) \_\_\_\_\_
- A) interest rates are about to fall.                      B) bond prices are about to rise.  
C) bond prices are about to fall.                      D) expected inflation is about to fall.
- 9) The demand for money as a cushion against unexpected contingencies is called the \_\_\_\_\_ 9) \_\_\_\_\_
- A) speculative motive.                      B) precautionary motive.  
C) insurance motive.                      D) transactions motive.
- 10) Keynes argued that when interest rates were high relative to some normal value, people would expect bond prices to \_\_\_\_\_, so the quantity of money demanded would \_\_\_\_\_. 10) \_\_\_\_\_
- A) decrease; increase                      B) increase; decrease  
C) increase; increase                      D) decrease; decrease
- 11) In the Baumol-Tobin analysis of transactions demand, scale economies imply that an increase in real income increases the quantity of money demanded \_\_\_\_\_, while an increase in the price level increases the quantity of money demanded \_\_\_\_\_. 11) \_\_\_\_\_
- A) more than proportionately; proportionately  
B) proportionately; less than proportionately  
C) less than proportionately; proportionately  
D) proportionately; more than proportionately
- 12) In a liquidity trap, monetary policy has \_\_\_\_\_ effect on aggregate spending because a change in the money supply has \_\_\_\_\_ effect on interest rates. 12) \_\_\_\_\_
- A) a large; a large                      B) no; a large                      C) no; no                      D) no; a small
- 13) According to Milton Friedman, the demand for money is insensitive to interest rates because \_\_\_\_\_ 13) \_\_\_\_\_
- A) competition among banks keeps the opportunity cost of holding money relatively constant.  
B) people base their investment decisions on expected profits, not interest rates.  
C) transactions are not subject to scale economies as wealth increases.  
D) the demand for money is insensitive to changes in the opportunity cost of holding money.
- 14) In the liquidity trap, the money demand curve \_\_\_\_\_ 14) \_\_\_\_\_
- A) is vertical.                      B) is horizontal.  
C) is positively sloped.                      D) is negatively sloped.
- 15) A central question in monetary theory is whether or to what extent the quantity of money demanded is affected by changes in \_\_\_\_\_ 15) \_\_\_\_\_
- A) the price level.                      B) interest rates.                      C) inflation.                      D) income.



## Answer Key

Testname: CH19\_PRACTICE

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