ECON UN3265: Money and Banking

Summer 2026 — Practice Quiz

Chapter 5 — Practice Quiz

How to use this quiz. These multiple-choice questions are based on the Chapter 5 practice problems on the behaviour of interest rates. Work through them after the reading; the answer key is on the last page.

Questions

1. Hermann is deciding whether to buy shares of Volkswagen stock. Which change would most directly make him less willing to buy the stock?

- **A)** A decrease in his household wealth after his spouse loses her job.
- **B)** The German bond market becomes less liquid.
- **C)** He expects the price of gold to fall.
- **D)** The German bond market becomes more volatile.

2. Alessandria is deciding whether to buy a new car. Which situation would most likely make her less willing to buy the car today?

- **A)** She receives a large inheritance.
- **B)** The stock market becomes more volatile.
- **C)** She expects car prices to fall soon.
- **D)** She expects an alternative stock investment to lose value.

3. You are considering gold as an asset. Which situation would most likely increase your willingness to buy gold?

- **A)** Political risks are expected to decrease.
- **B)** Gold prices become more volatile.
- **C)** A period of hyperinflation is expected.
- **D)** The expected return on alternative assets rises sharply.

4. Parameswary is considering buying long-term corporate bonds. Which situation would most likely reduce her willingness to hold those bonds?

- **A)** Trading in those bonds increases.
- **B)** She expects a bear market in stocks.
- **C)** Brokerage commissions on stocks fall.
- **D)** Brokerage commissions on bonds fall.

5. If a boom in the stock market substantially increases household wealth, what is the most likely effect on the demand for Rembrandt paintings as collectible assets?

- **A)** Demand decreases because paintings become less liquid.
- **B)** Demand increases because wealth rises.
- **C)** Demand is unchanged because paintings are not financial assets.
- **D)** Demand decreases because expected returns on all assets must fall.

6. Mario prefers a 10-year bond with higher expected return and higher risk, while Luigi prefers a 5-year bond with lower expected return and lower risk. What can be concluded about their relative risk aversion?

- **A)** Mario is definitely more risk-averse than Luigi.
- **B)** Mario is definitely less risk-averse than Luigi.
- **C)** They must have the same risk aversion.

D) The information is insufficient because the risk-return tradeoff depends on preferences.

7. A government imposes a strict limit on the number of daily transactions in bonds. What happens in the bond market?

A) Bond liquidity rises, bond demand rises, and interest rates fall.
B) Bond liquidity falls, bond demand falls, and interest rates rise.
C) Bond liquidity falls, bond supply rises, and interest rates fall.
D) Only bond supply changes; demand is unaffected.

8. If people suddenly expect future real estate prices to rise, what is the likely effect on bond interest rates?

A) Interest rates fall because bonds become more attractive.
B) Interest rates rise because alternative assets now offer higher expected returns.
C) Interest rates remain unchanged because real estate is not part of the bond market.
D) Interest rates fall because bond supply decreases automatically.

9. During a crisis, government budget deficits rise sharply, but interest rates remain low. Which explanation makes this outcome most plausible?

A) Budget deficits can never affect bond markets.
B) An outward shift in bond supply may have been offset by strong bond demand or expansionary monetary policy.
C) A larger deficit necessarily lowers bond demand by the same amount.
D) Interest rates are unrelated to bond prices.

10. A prime minister credibly announces a strong anti-inflation program. If the public believes the announcement, what should happen to interest rates?

A) They should rise because expected inflation rises.
B) They should fall because expected inflation falls.
C) They should not change because expected inflation is irrelevant.
D) They should rise because bond prices rise.

11. If people in France permanently increase their savings rate, what is the predicted effect on the French bond market?

A) Bond demand rises, bond prices rise, and domestic interest rates fall.
B) Bond demand falls, bond prices fall, and domestic interest rates rise.
C) Bond supply rises, bond prices fall, and domestic interest rates rise.
D) Bond supply falls, bond prices fall, and domestic interest rates rise.

12. Why might fiscal policymakers worry about potentially inflationary conditions?

A) Fiscal expansion can increase aggregate demand and expected inflation, putting upward pressure on interest rates.
B) Fiscal policy has no effect on aggregate demand.
C) Inflation only depends on brokerage commissions.
D) Higher government spending always lowers expected inflation.

13. A new central bank chair is expected to advocate slower money growth than the current chair. Which set of effects is most accurate?

A) Only the liquidity effect matters, so interest rates must fall immediately and permanently.
B) Slower money growth can raise rates in the short run through a liquidity effect but lower them later through income, price-level, and expected-inflation effects.
C) Slower money growth always raises expected inflation.
D) Money growth affects output but not interest rates.

14. A financial adviser presents three portfolios. Stocks and bonds each have an expected return of 9%, while commodities have an expected return of 9.5%. Which investment maximizes expected return?

A) Stocks
B) Bonds
C) Commodities
D) Stocks and bonds tie for the highest expected return

15. For one-year discount bonds with face value \$1,000, demand is P = -0.6Q + 1140 and supply is P = Q + 700. What are the equilibrium price, quantity, and interest rate?

A) P = \$975, Q = 275, i ≈ 2.56%
B) P = \$945, Q = 325, i ≈ 5.82%
C) P = \$1,000, Q = 275, i = 0%
D) P = \$700, Q = 440, i ≈ 42.86%

16. Using the same market, suppose the central bank sells 80 bonds and bond demand is unchanged. What is the new equilibrium interest rate?

A) About 2.56%
B) About 3.00%
C) About 5.82%
D) About 9.50%

Answer Key

1. A 2. C 3. C 4. C 5. B 6. D 7. B 8. B 9. B 10. B 11. A 12. A 13. B 14. C 15. A 16. C