ECON UN3265: Money and Banking

Summer 2026 — Practice Quiz

Chapters 13 — Practice Quiz

How to use this quiz. These multiple-choice questions are based on Chapter 13 practice questions on central banks. The answer key is on the last page.

Questions

1. Should central banks be privately or publicly owned?

- **A)** They should always be purely private because monetary policy has no public consequences.
- **B)** They are usually public or quasi-public institutions because monetary policy affects the whole economy; what matters most is public accountability combined with independence from short-run political pressure.
- **C)** They should always be owned by commercial banks so that bank profits are maximized.
- **D)** Ownership is irrelevant because central banks do not make policy decisions.

2. Why was the Federal Reserve System set up with twelve regional Federal Reserve Banks rather than one central bank, as in other countries?

- **A)** Because the United States wanted each regional bank to issue a different national currency.
- **B)** Because Americans were historically suspicious of concentrated financial power, and a regional structure balanced national coordination with regional representation.
- **C)** Because monetary policy was intended to be set only by state governors.
- **D)** Because Congress wanted the Fed to avoid contact with commercial banks.

3. In what ways can national central banks influence the conduct of monetary policy in the European System of Central Banks?

- **A)** They cannot influence policy because they are completely outside the Eurosystem.
- **B)** They influence policy through their governors' participation in ECB decision-making, implementation of policy operations, and provision of national information and analysis.
- **C)** They independently choose separate interest rates for their own countries after every ECB meeting.
- **D)** They influence policy only by issuing fiscal budgets for national governments.

4. Why have some countries rejected the single currency despite being full members of the European Union?

- **A)** Because joining the euro requires giving up national monetary policy and exchange-rate flexibility, and some countries prefer to keep monetary sovereignty or avoid the risks of a common currency.
- **B)** Because EU membership legally prohibits countries from ever adopting the euro.
- **C)** Because the euro can be used only by countries outside Europe.
- **D)** Because adopting the euro eliminates all trade with other EU members.

5. How do the structure and independence of the European System of Central Banks compare with those of the Federal Reserve System?

- **A)** Both are designed to be independent, but the ECB/ESCB gives national central banks a formal role in a supranational system, while the Fed combines a Board of Governors with regional Reserve Banks within one country.
- **B)** The ECB is controlled by the U.S. Congress, while the Fed is controlled by euro-area governments.
- **C)** Neither system has regional representation or legal independence.
- **D)** The Fed and the ECB are identical in membership, mandate, and political structure.

6. What are the main difficulties encountered by newly established central banks in transition economies?

A) They usually have no need to build credibility because inflation expectations are always anchored.
B) They may face weak institutions, political pressure, limited technical expertise, underdeveloped financial markets, and the need to establish credibility for low inflation.
C) They are unable to issue currency or supervise banks under any circumstances.
D) Their only difficulty is choosing the color of banknotes.

7. What are the expected consequences of Brexit for the Bank of England?

A) Brexit likely increased the Bank of England's need to respond to uncertainty, exchange-rate movements, financial-market stress, and possible changes in trade and growth conditions.
B) Brexit transferred all Bank of England monetary policy decisions to the ECB.
C) Brexit eliminated the Bank of England's role in financial stability.
D) Brexit made monetary policy unnecessary because the pound disappeared.

8. How does the structure and policy of the People's Bank of China differ from traditional central banking systems, and what consequences can this have for other economies?

A) The PBoC is fully independent from the government and never intervenes in credit or exchange-rate markets, so it has no effect abroad.
B) The PBoC operates in a system with stronger state direction, capital controls, managed exchange-rate policy, and a close link to government objectives; its policies can affect global liquidity, exchange rates, trade balances, and capital flows.
C) The PBoC conducts policy only for the euro area.
D) The PBoC is a private clearinghouse with no monetary policy role.

9. A central bank decides by how much an interest rate should be changed to restore equilibrium. What tools does it use to take such decisions?

A) It relies only on the current unemployment rate and ignores all other information.
B) It uses economic data, forecasts, policy rules or reaction functions, models of inflation and output, and judgment about financial conditions and expectations.
C) It changes interest rates randomly because no information is useful.
D) It uses only commercial bank profits as its target variable.

10. Why might a more transparent communication strategy be detrimental to a central bank's objectives?

A) Transparency always makes monetary policy ineffective and therefore should never be used.
B) Excessive or poorly framed transparency can confuse markets, reduce useful flexibility, cause overreaction to conditional forecasts, or make it harder to adjust policy when circumstances change.
C) Transparency is detrimental only because the public cannot observe interest rates.
D) There is no possible cost to transparency under any circumstances.

11. Why might eliminating the central bank's independence lead to a more pronounced political business cycle?

A) Politicians may pressure the central bank to stimulate the economy before elections, creating short-run booms followed by higher inflation or later tightening.
B) Central bank dependence eliminates all incentives for politicians to influence policy.
C) Political business cycles occur only in economies without money.
D) Removing independence forces the central bank to focus only on long-run price stability.

12. 'The independence of the central bank has meant that it takes the long view and not the short view.' Is this statement true, false, or uncertain?

A) True in general: independence helps central banks resist short-run political pressures and focus on long-run goals such as price stability, although accountability still matters.

B) False, because independence forces central banks to maximize short-run election outcomes.

C) Uncertain because independent central banks are legally prohibited from considering inflation.

D) False, because only legislatures can affect inflation expectations.

Answer Key

1. B 2. B 3. B 4. A 5. A 6. B 7. A 8. B 9. B 10. B 11. A 12. A