UNIVERSITY OF ESSEX DEPARTMENT OF ECONOMICS

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EC248-2-SP: MONETARY INNOVATIONS AND CENTRAL BANKS

Class 3 (1 February 2006): Problem Set - Questions

Essay Questions

1) List three economic magnitudes affected by the money stock and state how money affects each of them. (Mishkin, Chapter 1)

2) Shortly after his election, President George W. Bush proposed legislation that resulted in a cut in income taxes. Explain how this tax cut affected the federal budget deficit. What are the possible economic consequences of this change in the budget deficit? (Mishkin, Chapter 1)

3) Explain the concepts of asymmetric information, adverse selection, and moral hazard. When do adverse selection and moral hazard become relevant to the lending process? How has the financial system developed to deal with these problems? (Mishkin, Chapter 2)

4) Why does the government regulate the financial system? How does regulation reduce the problems of adverse selection and moral hazard? What regulations are or have been used to protect the public from panics? (Mishkin, Chapter 2)

5) Explain the functions of money and the problems of barter that each overcomes. (Mishkin, Chapter 3)

6) The payments system has evolved from commodity money to fiat money to checks to electronic money. Discuss one advantage and one disadvantage of each form of money. (Mishkin, Chapter 3)

Multiple Choice / Simple Computation Questions

7) If your nominal income in 1996 was $50,000, and prices doubled between 1996 and 2002, to have the same real income, your nominal income in 2002 must be (Mishkin, Appendix to Chapter 1)
(a) $50,000.
(b) $75,000.
(c) $90,000.
(d) $100,000.
(e) $200,000.

8) If nominal GDP in 2001 is $9 trillion, and 2001 real GDP in 1996 prices is $6 trillion, the GDP deflator price index is (Mishkin, Appendix to Chapter 1)
(a) 67.

(b) 100.
(c) 150.
(d) 200.
(e) cannot be determined.

9) If real GDP grows from $10 trillion in 2002 to $10.5 trillion in 2003, the growth rate for real GDP is (Mishkin, Appendix to Chapter 1)

(a) 5%.
(b) 10%.
(c) 50%.
(d) 0.5%.
(e) cannot be determined.

10) If the CPI in 2004 is 200, and in 2005 the CPI is 180, the rate of inflation from 2004 to 2005 is (Mishkin, Appendix to Chapter 1)

(a) 20%.
(b) 10%.
(c) 0%.
(d) –10%.
(e) –20%.