ECONOMICS 353 **L. Tesfatsion/Fall 07**

EXERCISE 11: 8 Questions (8 Points Total) **DUE: Tues, Dec 4, 2007, 2:10pm**

****IMPORTANT REMINDER: LATE ASSIGNMENTS WILL NOT BE ACCEPTED – NO EXCEPTIONS****

EXERCISE INSTRUCTIONS:

- (1) Please **fill in your name and student ID number** on Side 1 of your bubble sheet and write **353 Exercise 11** in the top margin of Side 1.
- (2) Use a number 2 pencil to **mark your answers on Side 1 of the bubble sheet to all eiqht questions Q1 through Q8, below**, which are in multiple choice format. There is no Web Exercise question for Exercise 11.
- (3) Each question Q1 through Q8 is worth 1 point.

Q1. According to Mishkin Chapter 8, during 1970-2000 ____ was a more important source of EXTERNAL FUNDS for U.S. corporations than _____.

A. revenues from stock and bond issues; loans from financial intermediaries

B. loans from foreign financial intermediaries; loans from domestic financial intermediaries

C. loans from financial intermediaries; revenues from stock and bond issues

D. loans from government agencies; loans from financial intermediaries

Q2. Some of the key reasons why banks and other financial intermediaries are able to reduce or eliminate information problems and transaction costs include:

A. banks can spread their loan costs over large pools of depositors (lenders).

B. bank loans are typically made in private, which gives bankers a greater incentive to engage in costly information gathering.

C. banks can include collateral requirements in loan contracts, which can act as a signal regarding the type of borrower (high or low risk).

D. all of the above.

Q3. Corporate BONDholders are generally LESS likely to be concerned about moral hazard problems than corporate SHAREholders because

A. corporate bondholders have priority over stockholders in case of bankruptcy.

B. corporate bonds include restrictive covenants that condition payments on corporate profit performance.

C. corporate bond payments are not conditioned on corporate profit performance (except in extreme circumstances such as bankruptcy).

D. both A and B.

E. both A and C.

Q4. PRINCIPAL-AGENT PROBLEMS are said to occur in financial markets when

A. ownership of assets is separated from the control of these assets.

B. people who do not pay for information take advantage of the information that other people have paid for by observing their behavior.

C. high-risk borrowers are successfully able to pass themselves off as low-risk borrowers when applying for loans.

D. the cost per dollar loaned declines as the size of the loan increases.

Q5. The SARBANES-OXLEY ACT OF 2002, introduced in the wake of ____, increased supervisory oversight by _____.

A. the dot.com bubble burst; giving Congress the authority to review independent audits of initial public offerings (IPOs).

B. the demise of the Arthur Andersen company due to the Enron crisis; establishing the Public Company Accounting Oversight Board to supervise accounting firms and ensure independent audits.

C. the U.S. savings and loan crisis; creating a new Department of Conflict Resolution within the Federal Deposit Insurance Corporation (FDIC).

D. the U.S. twin deficit problem; directing the General Accounting Office to provide yearly detailed reports on U.S. fiscal expenditures.

Q6. The ECONOMIC GROWTH of a country refers to _____.

A. changes in its balance of payments.

B. changes in the infrastructure, organization, and governance of its economy.

C. changes in its money supply.

D. changes in the size of its economy, often measured by changes in GDP.

Q7. According to Mishkin Chapter 8, most U.S. FINANCIAL CRISES have begun with one or more of the following "trigger events":

A. a rise in interest rates.

B. a decline in the stock market.

C. a deterioration in banks' balance sheets.

D. an increase in uncertainty resulting, for example, from a failure of a prominent financial or nonfinancial institution.

E. all of the above

Q8. According to Mishkin Chapter 8, a key way in which U.S. financial crises have DIFFERED from financial crises in emerging economies such as Mexico is that

A. U.S. regulators have not permitted insolvent financial institutions to stay in operation.

B. foreign exchange crises (e.g., speculative currency attacks) have not played a dominant role in U.S. financial crises.

C. U.S. financial crises tend to be of far shorter duration.

D. U.S. financial crises have not resulted in substantial bank failures.