

ANSWER OUTLINE

ECONOMICS 353

L. Tesfatsion/Fall 05

EXERCISE 11: 8 Questions (8 Points Total)

DUE: Tues, Nov 29, 2005, 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 EIGHT questions Q1 through Q8, below, which are all in multiple choice format.
- (3) There is no Web browse question for Exercise 11.
- (4) Each question Q1 through Q8 is worth 1 point. All eight questions relate to the required materials for Mishkin Chapter 8: Part B.

Q1 (1 point). The ECONOMIC DEVELOPMENT of a country refers to a change in _____ that permits a higher standard of living for its people.

- A. its government fiscal (tax and expenditure) policy
- B. its balance of payments
- C. the growth rate of its GDP
- D D. the infrastructure, organization, and governance of its economy

Q2 (1 Point). The economic growth and development of a country are IMPEDED when the flow of funds from savers to borrowers is disrupted, which can result from

- A. inadequate or inappropriate government regulation.
- B. absence of standard accounting practices.
- C. a weak legal system.
- D D. all of the above.
- E. only A and B.

Q3 (1 Point). Key factors that can TRIGGER financial crises include

- A. a sudden increase in corporate net worth that leads to debt deflation.
- B. a sudden decline in stock market prices.
- C. a sudden increase in interest rates that worsens adverse selection
- D. all of the above.
- E E. only B and C.

Q4 (1 Point). A key way in which financial crises in the U.S. (and other relatively well developed countries) have DIFFERED from financial crises in developing (or emerging market) economies is that

- A. U.S. financial crises have typically not involved bank panics.
- B B. U.S. financial crises have typically not involved a foreign exchange crisis.
- C. U.S. financial crises have tended to be of far shorter duration.
- D. U.S. financial crises have not resulted in substantial bank failures.

Q5 (1 Point). An important factor that TRIGGERED the 1994-1995 Mexican financial crisis was

- A A. a decline in the net worth of Mexican banks and a contraction in their lending activity.
- B. the failure of the World Bank to provide support for economic development.
- C. the failure of Mexico to ratify the Free Trade Area of the Americas (FTAA).
- D. the OPEC oil price shocks.
- E. the Chiapas uprising.

**SEE THE FOLLOWING PAGE FOR
Q6, Q7, and Q8**

Q6 (1 Point). A key factor that WORSENEED AND PROLONGED the U.S. Great Depression was _____, which resulted in _____ .

- A. a sharp increase in inflation; a sharp decrease in the real money supply.
- B. a sharp increase in real government spending; a sharp drop in real GDP.
- C. a sharp drop in the aggregate price level; severe debt deflation.
- D. a sharp contraction in the real money supply; a sharp drop in interest rates.

Q7 (1 Point). By definition, a key DISTINCTION between an INSOLVENT firm and a BANKRUPT firm is

- A. an insolvent firm can no longer meet its legal obligations to its financial creditors.
- B. an insolvent firm necessarily has a negative net worth.
- C. an insolvent firm is necessarily suffering from debt deflation.
- D. an insolvent firm is required to undergo reorganization under the “Chapter 11” bankruptcy law.

Q8 (1 Point). ADVOCATES of the international rescue package provided to Mexico following its financial crisis in 1994-1995 say that Mexico’s subsequent recovery proves the importance of helping countries whose financial institutions _____, but CRITICS of the rescue package fear it worsened _____.

- A. are insolvent but still functioning; balance of payment problems.
- B. are experiencing debt deflation; inflation.
- C. need liquidity assistance but are not insolvent; moral hazard problems.
- D. are experiencing temporary reserve shortages; purchasing power parity problems.