

# Revision Lecture

## FIN 204 Lecture 14.3.

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## 1 Examples of Exam Problems

# Importance of Financial Markets

Financial markets and institutions

- A) involve the movement of huge flows of money.
- B) affect the profits of businesses.
- C) affect the types of goods and services produced in an economy.
- D) do each of the above.
- E) do only (a) and (b) of the above.

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Answer: D

# Understanding Interest rates

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# Money and Inflation: Empirical Evidence

One likely explanation for the relatively high rates of inflation experienced in many Latin American countries is the

- A) relatively slow growth in the money supply in these countries.
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Answer: B



# Stock Market Effects on the Overall Economy

A rising stock market index due to higher share prices

A) increases people's wealth and as a result may increase their willingness to spend.

B) increases the amount of funds that business firms can raise by selling newly-issued stock.

C) decreases the amount of funds that business firms can raise by selling newly-issued stock.

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Answer: D

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- C) deposits.
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Answer: C

# Understating Interest Rates

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- A) 12 percent
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# Understating Interest Rates

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Answer: C

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Problem: What might be the main reason for this?



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Problem: How cutting interest rates by the FED affects the US Dollar?  
Why?

## Exchange Rates (2)

On March 6, 2008 The Economist wrote: “In what looked like a co-ordinated effort, some European finance ministers expressed their concern at the relentless climb of the euro against the dollar (it has also risen against other currencies, including the pound and the yen). The European Central Bank has come under fire from some quarters for the euro’s ascent, which is blamed for hampering the prospects for growth and weakening Europe’s exports.”



## Exchange Rates (2)

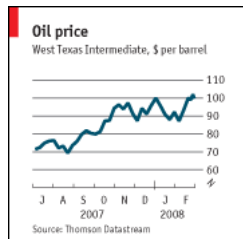
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Problem: What is the appropriate action to be taken by the ECB in this situation? (Hint: think the answer through the interest rates channel)

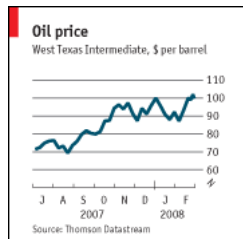
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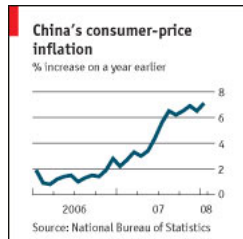


Problem: It seems that investors see oil and other goods as a good investment opportunity.

- 1 Why?
- 2 What is an appropriate measure to be taken by the central bank in this situation?
- 3 Justify your answer

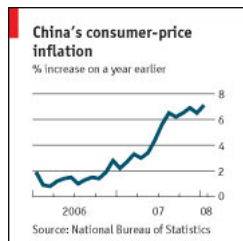
# Monetary Policy Response to Inflation

On Feb. 21, 2008 The Economist wrote:  
“Inflation increased in both America and China.  
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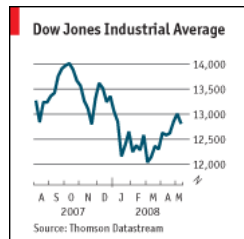
Problem:

- 1 What is the appropriate monetary policy response to inflation in case of an overheating economy like China?
- 2 What is an appropriate measure to be taken by the FED in this situation?



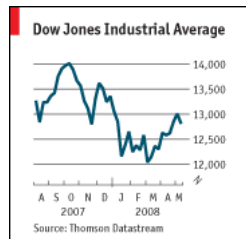
# Stock Market Crises

On May 8, 2008 The Economist wrote: “The Dow Jones Industrial Average closed above the 13,000 mark on May 1st for the first time since early January. The index has risen by roughly 8% since mid-March. With investors seemingly betting that the worst of the credit crisis is over, other stockmarkets in America and Europe were buoyant as well.”



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Problem:

- 1 If you invested 1000 USD in the beginning of March, and sold your assets in the beginning of May, how much did you have in the beginning of May?