





D (from banks short of reserves)

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Federal Funds





$S_0$  (from banks  
with excess  
reserves)































**R**















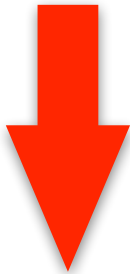
The effect of a **purchase** of bonds by the Fed on the  
Federal Funds Market

Feedbuys Bonds:

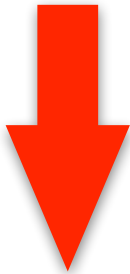
Reserves



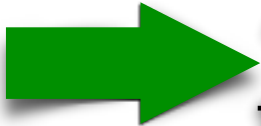
A purchase of bonds by the  
Fed floods the banking system  
with additional reserves



There will be **more** banks  
with excess Reserves



The **Supply** of funds in this  
market **increase**



A rightward shift in  
the Supply of funds



$\text{ffr}_e = 3\%$



$Q^s = Q^d$

Assume the  
market starts at  
equilibrium



$S_1$  (from banks  
with excess  
reserves)

A thin green line originates from the bottom-left corner of the image and extends diagonally upwards and to the right, ending just below the text  $S_1$ .

$\text{ffr}_1 = 2\%$

$Q^s = Q^d$

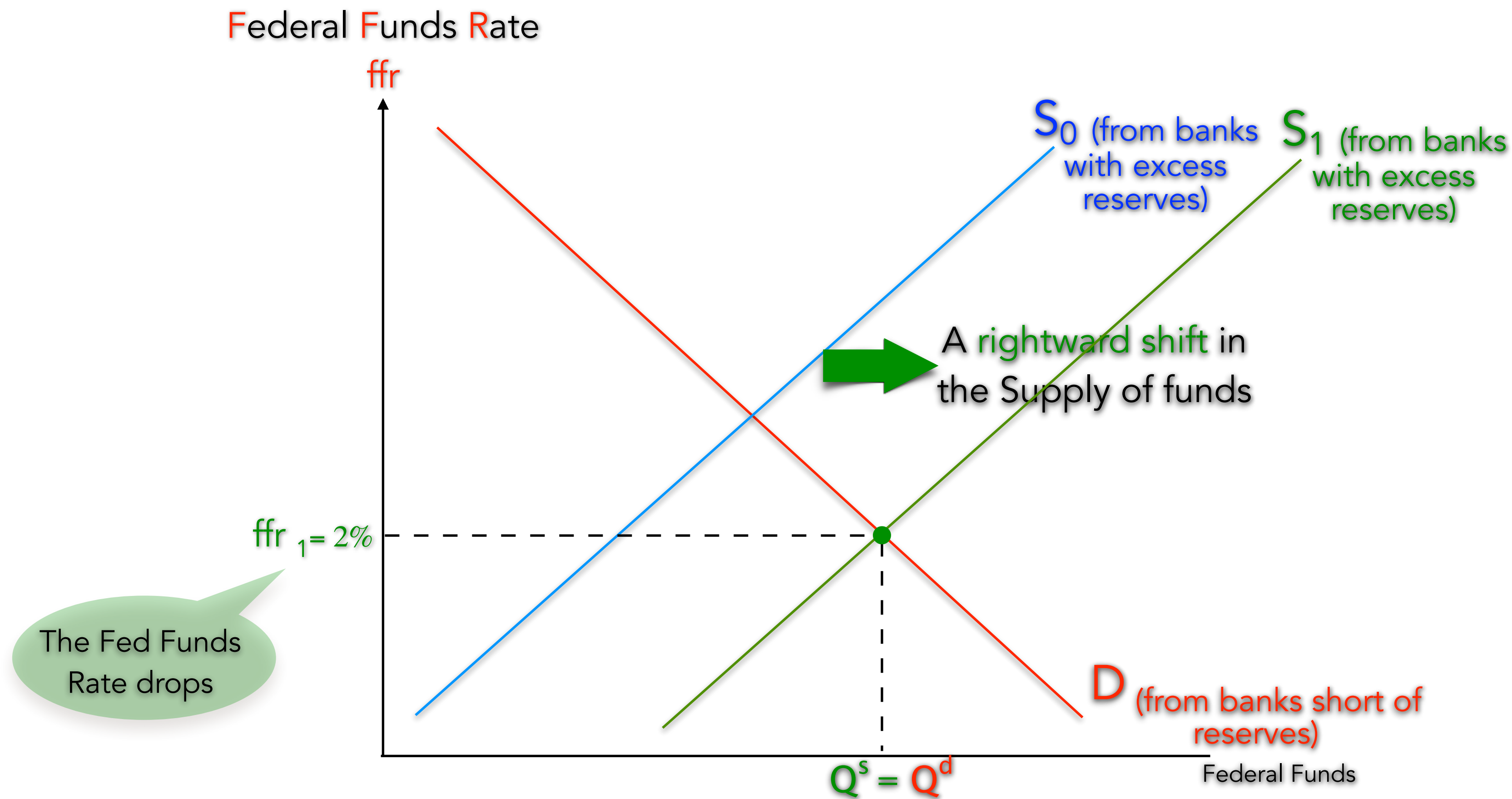


The Fed Funds  
Rate drops

Federal Funds Rate

ffr

# The effect of a **purchase** of bonds by the Fed on the Federal Funds Market



Fed **buys** Bonds: **Reserves** 

A **purchase** of bonds by the Fed **floods** the banking system with additional reserves



There will be **more** banks with excess Reserves



The **Supply** of funds in this market **increase**