























2

S

2



e



b







S

b

Y







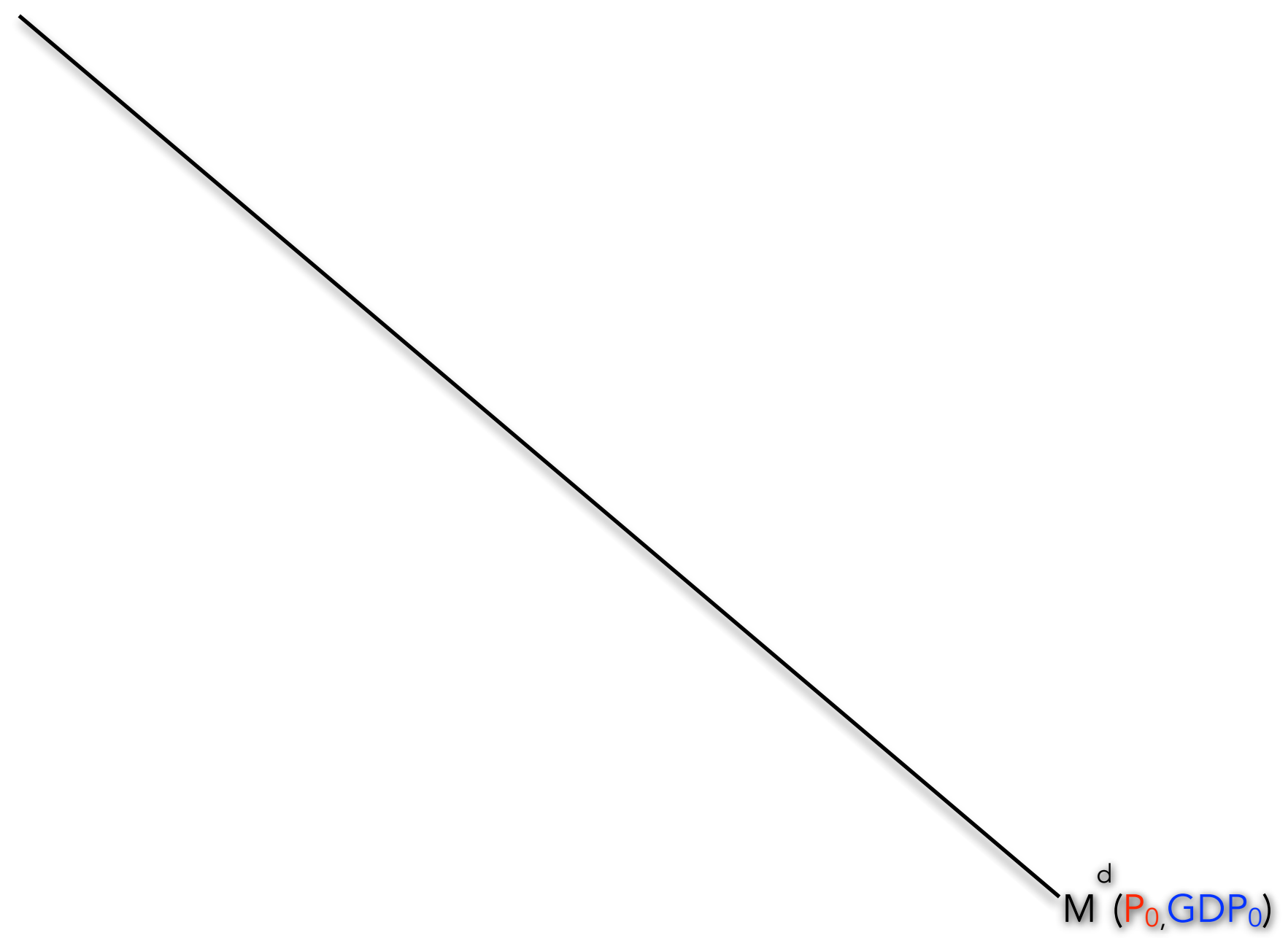






i





M_0^s



$M_0^s = 900b$

$i_0 = 6\%$



$i_1 = 3\%$



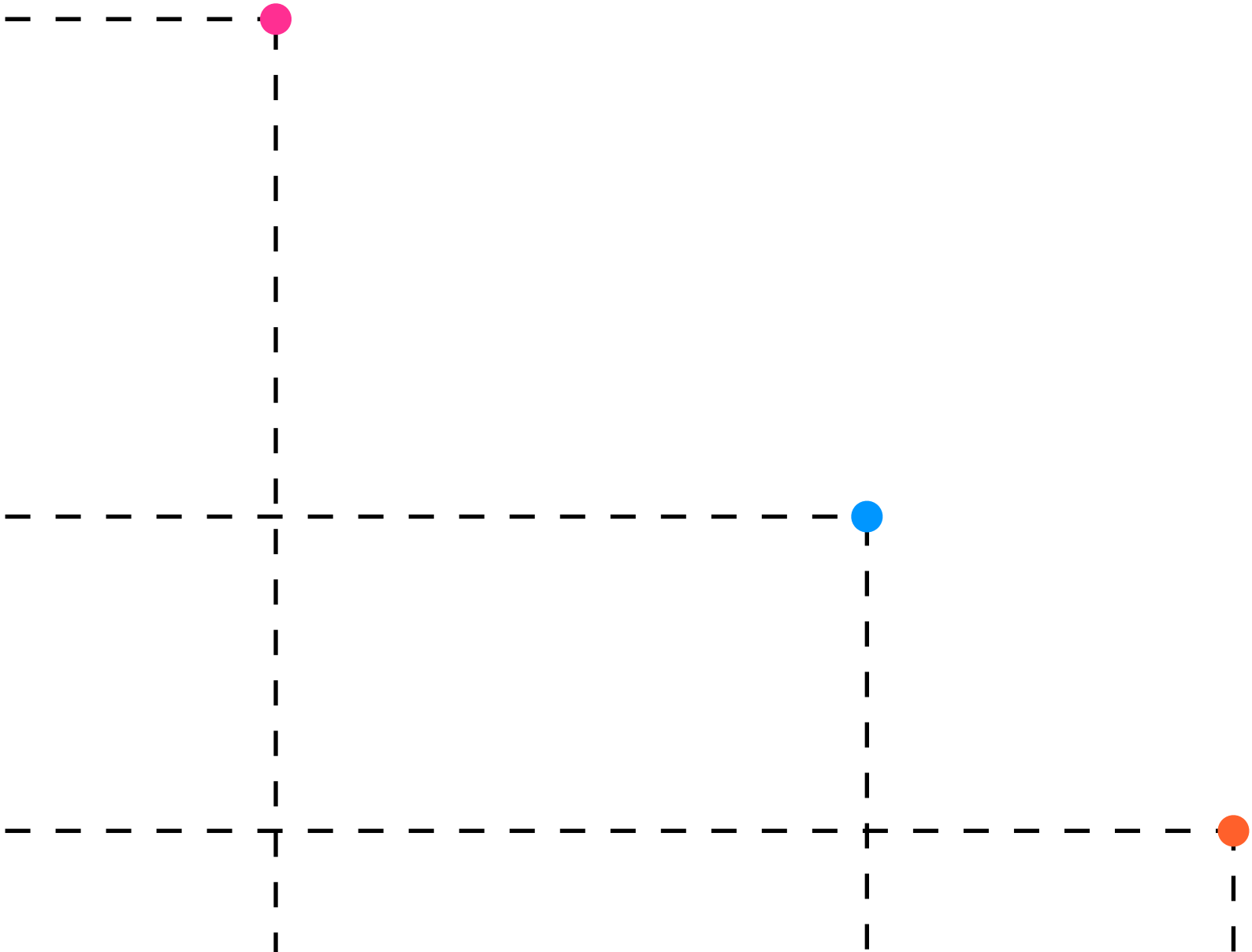
$i_2 = 1\%$



$M^d = 300b$

$M^d = 900b$

$M^d = 1,200b$





Assume the Money Market
starts at equilibrium at 3%

Feedseis Bonds:

M^s shifts left



Reserves



Loans



Deposits



M^S

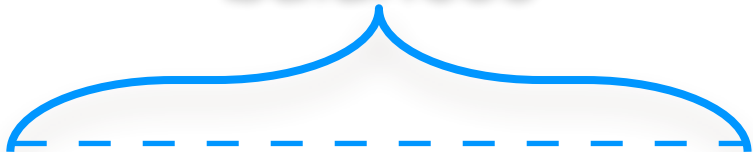


M_1^S



$M^S = 300b$

Short of liquid
balances



When there are shortages of liquid
balances, money is scarce and
there is pressure for the interest
rate to rise




The interest rate will rise to




a new equilibrium at 6%



New
equilibrium



The Fed disappears
reserves making money
scarce at 3%



When the Fed sells
bonds: Quantitative
Tightening (QT)

The effect of a sale of bonds by the Fed

The effect of a **sale** of bonds by the Fed

When the Fed sells bonds: Quantitative Tightening (QT)

→ The interest rate will **rise** to a new equilibrium at **6%**

