



D (from banks short of reserves)

Federal Funds





S_0 (from banks
with excess
reserves)

























R













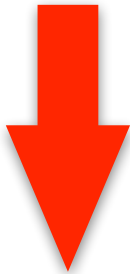
The effect of a **purchase** of bonds by the Fed on the
Federal Funds Market

Feedbuys Bonds:

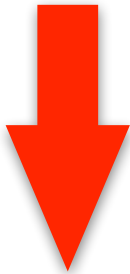
Reserves



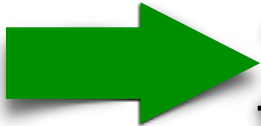
A purchase of bonds by the
Fed floods the banking system
with additional reserves



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)



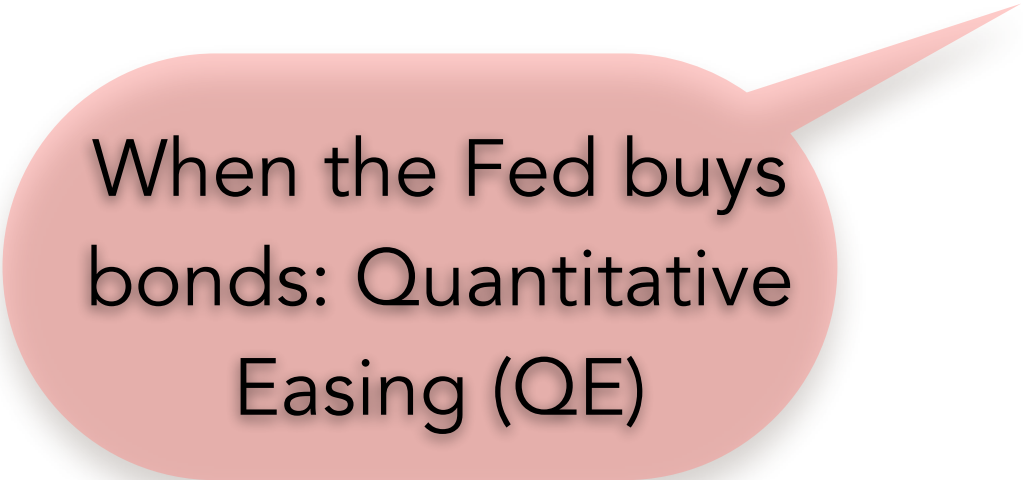
$\text{ffr}_1 = 2\%$



$Q^s = Q^d$



The Fed Funds
Rate drops



When the Fed buys
bonds: Quantitative
Easing (QE)

Federal Funds Rate

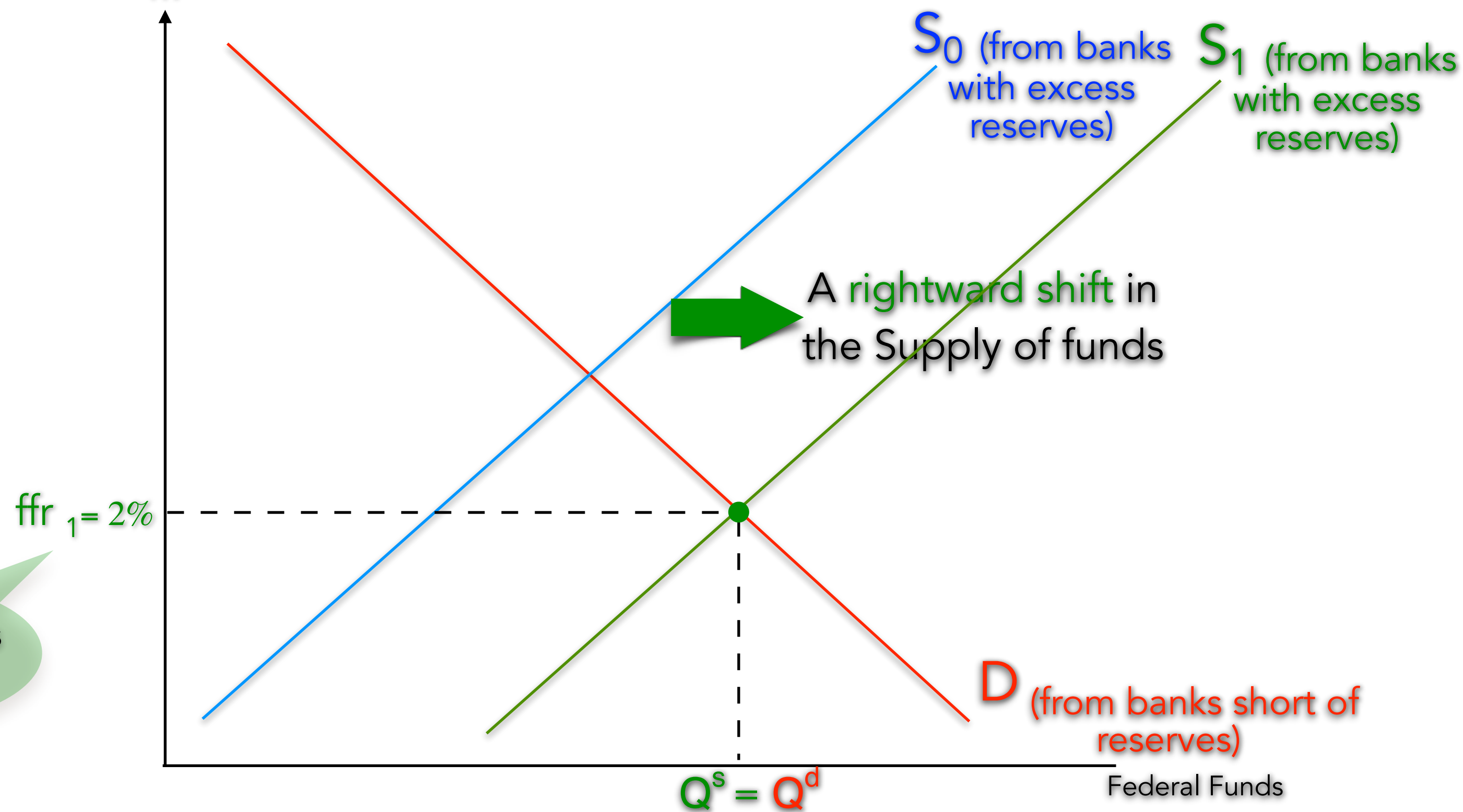
ffr

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

When the Fed buys bonds: Quantitative Easing (QE)

Federal Funds Rate

ffr



The Fed Funds Rate drops

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**