



D_0 (from banks short of reserves)

Federal Funds





S_0 (from banks
with excess
reserves)

























R





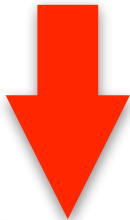








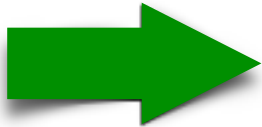
The effect of an increase in **Prices** on the Federal Funds Rate



The public deposits a larger
portion of their income in
checking accounts



Deposits increase



A rightward shift in
the Demand of
funds

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



$Q^s = Q^d$

Assume the
market starts at
equilibrium





D_1 (from banks short of reserves)

$\text{ffr}_1 = 4\%$

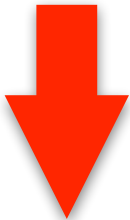


$Q^s = Q^d$



The Fed Funds
Rate increase

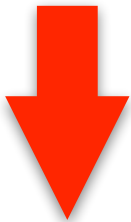
When **prices** increase, the public needs **more** liquid balances to pay for more expensive transactions



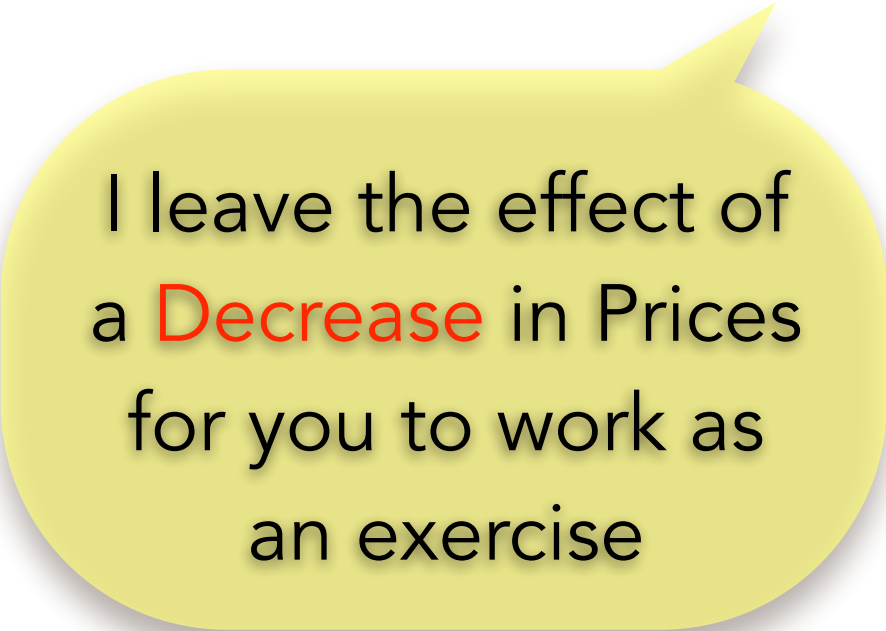
Required Reserves
increase

Demand for funds

increase



More banks will end the
day short of reserves



I leave the effect of
a **Decrease** in Prices
for you to work as
an exercise

Federal Funds Rate

ffr

The effect of an increase in Prices on the Federal Funds Rate

When **prices** increase, the public needs **more** liquid balances to pay for more expensive transactions



The public **deposits** a **larger** portion of their income in checking accounts



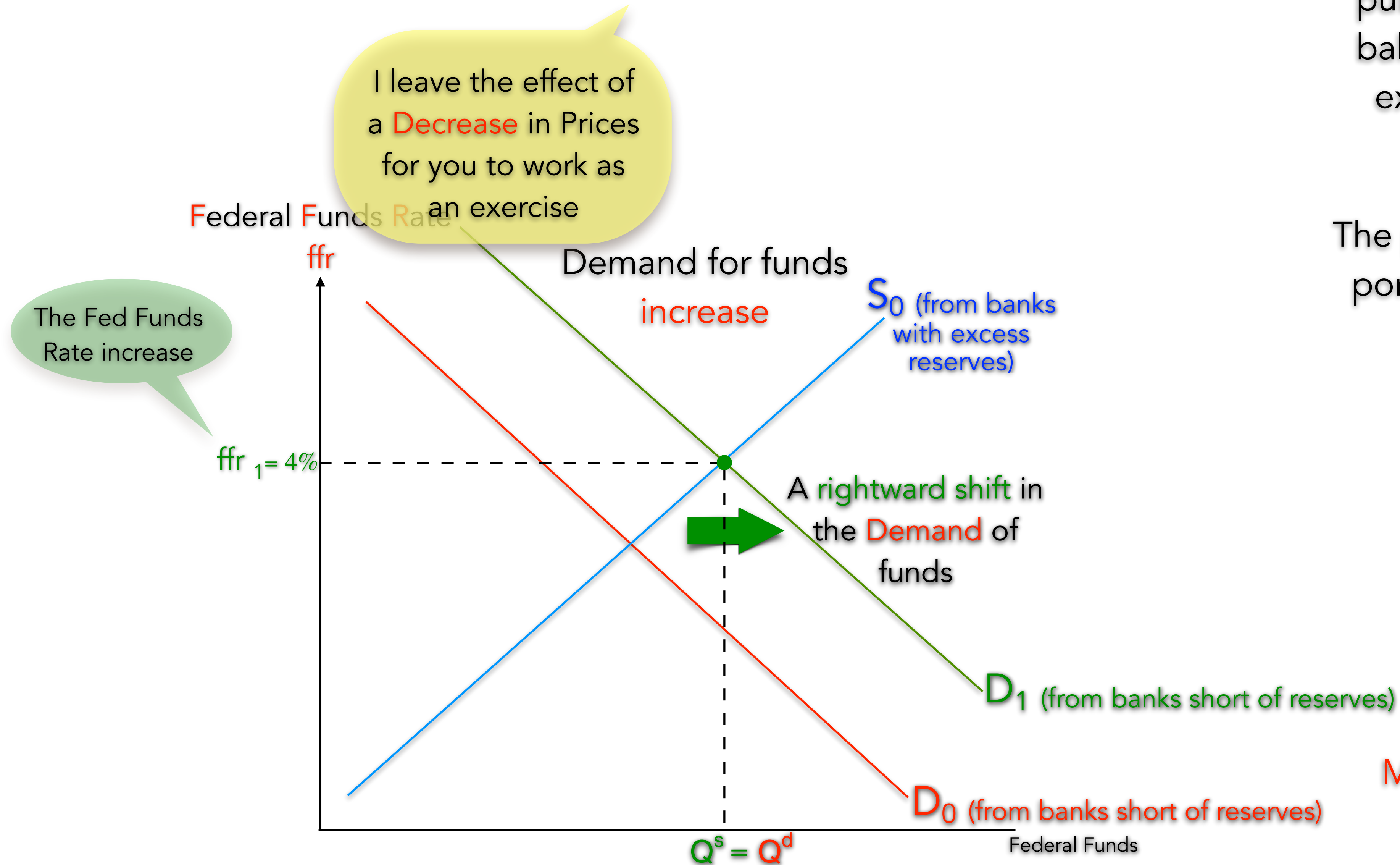
Deposits increase



Required Reserves increase



More banks will end the day **short** of reserves



The effect of a decrease in GDP on the Federal Funds Rate

