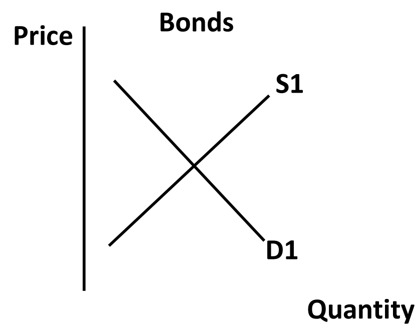
Homework #4

Economics 101 – Macroeconomics

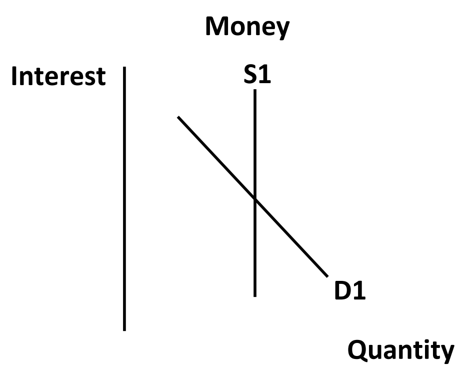
Professor Schenk

Due: August 9, 2010

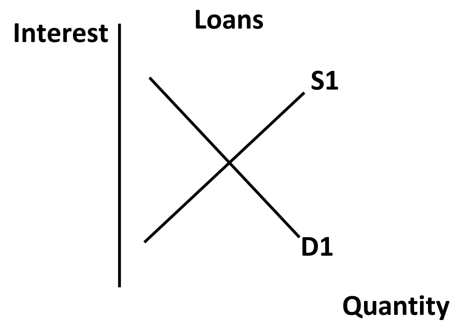
1. On November 6th, 2002, the FOMC released a statement: “The Federal Open Market Committee decided today to lower its target for the federal funds rate by 50 basis points to 1 1/4 percent.” Using the series of graphs below, follow the progress and actions of the FOMC.
   a. What happens in the bond market? Chart the answer and write a brief explanation.



   b. What happens to the supply of money? Chart the answer and write a brief explanation.

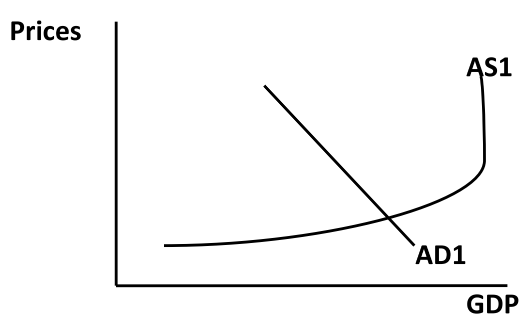


c. What happens to the loan market? Chart your answer and write a brief explanation.



d. How will the loan market affect the overall economy? Write an explanation in words.

e. What happens in the aggregate economy (use the interpretation in part d)? Chart your answer.



2. Suppose a customer deposits $1,500 in a bank. Suppose the reserve ratio is 10 percent. How much will that deposit create in demand for deposits in the economy?

    a. Now suppose the reserve ratio is decreased to 8 percent. How much will that deposit create in demand for deposits in the economy?

    b. Did lowering the reserve ratio contract or expand the supply of money in the economy?

3. A bank issues a loan where the lender promises to pay the bank $5,000 each year and a 5% interest rate. What is the value of that loan?

You're done!