ECO 301: Money and Banking
Week 12 Homework: Macroeconomic Dynamics and Monetary Policy

1. Suppose the economy is at the long-run equilibrium when the Federal Reserve conducts an open market sale of bonds. Describe and illustrate the impact on the equilibrium interest rate in the bond market, and the short-run macroeconomic impacts on real GDP, price level, employment, and unemployment (remember to use sticky-wages for the short-run effect).

2. Suppose there is an improvement in bond rating agencies methods and reliability. Describe and illustrate the impact on the equilibrium interest rate in the bond market, and the short-run macroeconomic impacts on real GDP, price level, employment, and unemployment (remember to use sticky-wages for the short-run effect).

3. Suppose an economy is originally at the long run equilibrium when a drop in businesses' economic outlook leads to a decrease in investment spending.

   (a) Describe and illustrate the impact on the equilibrium interest rate in the bond market, and the short-run macroeconomic impacts on real GDP, price level, employment, and unemployment (remember to use sticky-wages for the short-run effect).

   (b) Suggest an open market operation monetary policy that can remedy the effect of the recessionary shock that you illustrated in part (a). Describe and illustrate the impact of your policy on the equilibrium interest rate and quantity of reserves in the market for reserves, the equilibrium interest rate and quantity of borrowing in the market for bonds, real GDP, price level, employment, and unemployment? Start your bond market and aggregate goods and service market in the situation from the previous answer (i.e. redraw the answer from the previous problem and then show the impact of your policy on these markets).

4. Suppose the economy is originally at the long run equilibrium when an increase in global energy costs cause a widespread increase in the costs of production.

   (a) Describe and illustrate the short-run macroeconomic impacts on real GDP, price level, employment, and unemployment (remember to use sticky-wages for the short-run effect).

   (b) Trick question. Describe a monetary policy that can reduce inflation, increase real GDP, and increase employment. Explain why it's a trick question.