ECO 301: Money and Banking
Week 7 Homework: Supply and Demand for Bonds and Loanable Funds

1. Suppose businesses have an optimistic outlook and expect an increase in sales and profits over the next several years. Describe and illustrate the impact on the market for bonds. What is the equilibrium impact on the price of bonds, the interest rate on bonds, and the equilibrium quantity of borrowing? Illustrate using both the market for bonds and the market for loanable funds.

2. Suppose consumers expect a decrease in interest rates starting in about six weeks and continuing for two years. Describe and illustrate the equilibrium impact on the price of two-year bonds, and the interest rate on two-year bonds, and the equilibrium quantity of borrowing. Describe how the gap between 30-day and two-year interest rates would be affected.

3. Suppose an improvement in machine learning technology allows for more reliable ratings of bonds, allowing for businesses and consumers to trade larger quantity and greater variety of bonds with more confidence. What is the equilibrium impact on the price of bonds, the interest rate on bonds, and the equilibrium quantity of borrowing? Illustrate using both the market for bonds and the market for loanable funds.

4. Suppose the Fed makes an open market purchase of bonds. Describe and illustrate the impact on the market for bonds. What is the equilibrium impact on the price of bonds, the interest rate on bonds, and the quantity of trading?

5. Suppose people expect government deficits to continue to grow, leading to growing national debt. If this becomes true, describe and illustrate the impact on the market for bonds. What is the equilibrium impact on the price of bonds, the interest rate on bonds, and the quantity of trading?

6. Suppose people expect government deficits to continue to grow, leading to growing national debt, and so they expect the change in bond prices and interest rates that you illustrated in #7. What impact does this *expectation for future bond prices* have on the market for bonds today? What is the equilibrium impact on the price of bonds, the interest rate on bonds, and the quantity of trading?