

Mac 5 - Limited and Ample Reserves

Link to Powerpoint

From 2025 Set 2 Q2 (with addition)

2. Assume the economy of Jenland is in short-run equilibrium at a real output level above full-employment real output.
 - A. The banking system in Jenland has ample reserves. Identify a specific monetary policy action that the central bank of Jenland would implement to return the economy to full employment in the short run.
 - B. Draw a correctly labeled graph of the reserve market for Jenland, and show the effect of the central bank's action identified in part A on the policy rate.
 - C. Based on the change in the interest rate shown on your graph in part B, will each of the following increase, decrease, or remain the same in Jenland in the short run?
 - i. The price of previously issued bonds
 - ii. The price level. Explain.

D (added) NOW assume Jenland has Limited Reserves

i. What open market operation would the Central Bank employ to return to full employment output?

ii. Draw the impact of the action employed in d)i. In a Money Market Graph on the Nominal Interest Rate

From 2025 Set 1 Q2

2. The economies of Country L and Country A are currently in short-run equilibrium at output levels below full employment. Both countries intend to use monetary policy to close their output gaps. Country L has a banking system with limited reserves, and Country A has a banking system with ample reserves.
- A. What open-market operation would Country L implement to move the economy toward full employment in the short run?
 - B. What specific monetary policy action would Country A implement to move the economy toward full employment in the short run?
 - C. Draw a correctly labeled graph of the reserve market in Country A, and show the effect of the monetary policy action identified in part B on the policy rate.
 - D. Assume instead that no policy actions are taken in Country A and that the economy remains in short-run equilibrium at an output level below full employment. Will short-run aggregate supply in Country A increase, decrease, or remain the same as the economy self-adjusts in the long run? Explain.