q2 macro 2016

2A

ANSWER PAGE FOR QUESTION 2

2. a. First superior Bank can loan out \$0 new dollars because the bank keeps no excess reserves so it has no more money to loan out.

b. The bank can now loan out \$90 because it must keep \$10 / \$100 in required reserves.

c. i. $\frac{1}{10} \cdot 100 = 10$

$100 - 10 = 90 \left(\frac{1}{\frac{1}{10}}\right) = \boxed{\$900}$

ii. $\$100 \left(\frac{1}{\frac{1}{10}}\right) = \boxed{\$1000}$

d. The maximum change in the money supply is \$900 because $\frac{1}{10} \cdot 100 = 10$, $100 - 10 = 90$, $90 \cdot \left(\frac{1}{\frac{1}{10}}\right) = \$900$.

e. If people decide to hold on to their money longer or hold money in their homes rather than putting it in the banks then the multiplier effect of the deposit / loan will be smaller than the maximum change stated in part d.

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