Chapter 8: Conduct of Monetary Policy

- **Objectives** – By the end of this chapter, you should be able to:
  - Show the effect of a given monetary policy transaction (open market purchases or sales, discount loans, etc.) on the balance sheets of the Federal Reserve system, the banking system, and the nonbank public.
  - Derive the demand and supply of reserves with respect to the Federal Funds Rate and the level of Nonborrowed reserves, and explain the factors that shift each curve, including changes in open market operations, discount lending, and reserve requirements.
  - Differentiate between the types of discount loans made by the Fed, as well as between defensive and dynamic open market operations.
  - Explain the Fed's role as a "Lender of Last Resort", including the benefits and costs of such a policy with respect to bank failures and moral hazard.
  - Compare and contrast the monetary policy tools of the European Central bank with that of the Federal Reserve System.
  - Explain the role of time inconsistency in a central bank's actions, and the role of a nominal anchor in the limitation of this potential problem.
  - Discuss the potential goals of a central bank with respect to economic policy, and the effect that hierarchical or dual mandates may have on these goals.
  - Describe the methods by which monetary or inflation targeting may be implemented by a central bank, and the positive and negative aspects of each type of policy. Be able to cite specific countries as case studies portraying the relative success of each type of targeting policy, and cite specific examples to support your case.
  - Show the limitations inherent in choosing a policy instrument both graphically and in words, especially with respect to fluctuations in the demand for reserves.

- **Assigned Reading** - Mishkin and Eakins, pp. 169-177 and 179-202

- **Optional / Recommended Reading** - For those who would like more information about how trading on the open market by the New York Fed is conducted on a daily basis, read pages 178-179 of your text.

- **Optional Practice Problems**
  - Mishkin and Eakins, pp. 205-207:
    - Questions: #6, 9, 13, 17
    - Quantitative Problems: #2, 4, 6, 7
    - Web Exercises: #1
Chapter 9: Money Markets

- **Objectives** – By the end of this chapter, you should be able to:
  
  o Define the types of securities traded in money markets, and explain the similarities and differences between holding a money market security and holding currency.
  
  o Explain the necessity of money markets, both historically and in terms of the current economic climate.
  
  o Calculate the annualized discount and investment rate for treasury bills when given information about prices, face value, and time to maturity. Similarly, if you are given either the discount or investment rate and two of the other three variables, you should be able to find the missing third variable.
  
  o Outline the bidding procedure for treasury bill auctions, including the difference between competitive and non-competitive bids. If you are given a set of bid amounts and prices, you should be able to identify the winning bidders and the final auction price.
  
  o For each of the following money market securities, be able to explain the process by which these securities are bought and sold, the usual levels of risk and interest rates associated with holding them, their average time until maturity, and the types of investors and borrowers that usually engage in the market:
     - Treasury Bills
     - Federal Funds
     - Repurchase Agreements
     - Negotiable Certificates of Deposit
     - Banker’s Acceptances
     - Eurodollars
  
  o Compare and contrast all of the money market instruments listed above with respect to typical observed interest rates, liquidity, valuation, and the role of government regulation (if any) in the relative popularity of each.
  
  o Explain the role of banker’s acceptances in the facilitation of international trade.

- **Assigned Reading** - Mishkin and Eakins, pp. 211-234

- **Optional Practice Problems**
  
  o Mishkin and Eakins, pp. 235-236:
    
    - Questions: #4, 5, 9, 13, 14
    - Quantitative Problems: #3,4,8,9,11,12
    - Web Exercises: #1 (This one would be especially useful if you’d like to see how rates have changed as a result of the recent financial crisis).