

Assignment Two
Due: January 29, 2004

1. In this question, you will gather data on money growth, inflation, and the interest rate and comment on the relationship among these data series. You need not print the data. Instead, submit graphs to support your answers.
 - a. Visit Fred II at the web site of the Federal Reserve Bank of St. Louis. While there, download data for the three month treasury bill yield on secondary markets, the CPI for all urban consumers, and M2. Choose not-seasonally-adjusted series for M2 and the CPI. The data should be monthly. Note that the data are available for different periods and you will have to align them in your spread sheet.
 - b. For January 1960 through the end of the data record, create series for the rate of money growth and the inflation rate from the data you input. Define the rate of money growth to be $DM_t = \ln(M_t) - \ln(M_{t-12})$ and define the inflation rate similarly. This formula defines growth rates with year-to-year changes.
 - c. For January, 1960 until the end of the record, graph money growth, inflation and the T Bill rate. Use the scatter graph option and choose dates as the data for the x-axis. Make sure the scale of the x axis begins in 1960 or your graph will be needless compressed. Print the graph and submit it with your assignment.
 - d. Do the data support Friedman's view that "Inflation is always and everywhere a monetary phenomenon"?
 - e. Create an estimate of the real rate of interest between January, 1960 and December, 2002. Creating this estimate will require some thought. Remember that the real rate of interest is defined as the "opportunity cost measured in terms of goods" for borrowing money over a period of time. Using the three month treasury bill implies that we have a three month horizon in mind? Take care to create your real rate with the correct inflation series.
 - i. Explain in detail how you compute the real rate of interest.
 - ii. Do the data support the existence of a Fisher effect?
 - iii. Would you conclude based on the data that the real interest rate in the US was constant between 1960 and 2002?
2. Mankiw, Question 3, p. 110.
3. Mankiw, Question 9, p. 110
4. Mankiw, Question 1, p. 154.