ECO 156, Fall 2026, Required Assignment #4

Applications to Bond Markets and Monetary Policy

This assignment is due on Friday, December 4 at 5 PM. This is the last day of classes, plan accordingly.

Instructions Answer each of the following questions. Most questions can be effectively answered in a few concise sentences. Submit your assignment via this Google form. You will need to be logged into your Bates account to access the link.

Part I: A Credit Card Interest Cap

1. Some U.S. politicians have proposed capping credit card interest at a 10% annual rate. Describe some details about this proposal (*e.g.* who has proposed it) and provide a source.

2. How do recent credit card interest rates compare to this 10% proposal? Provide data, ideally in a graph, and provide a source.

3. Using the basic model of supply and demand from the first part of the class, model the market for credit card debt. In this setting 1) households supply debt by borrowing, 2) credit card companies demand debt by lending and 3) the price of credit card debt is inversely related to the interest rate. How does this cap (which acts like a price ceiling/floor) affect the amount of borrowing?

4. Based on your result from #3, how would this policy affect households' consumption choices? Discuss any macroeconomic implications (inflation and the output gap) of this policy.

Part II: Term Premiums

This article from the San Francisco Fed provides some additional background on term premiums.

5. Why are term premiums usually, but not always positive?

6. Find some recent estimates of U.S. 10-year term premiums. Present your results, provide a source, and describe if they have risen or fallen in recent decades.
7. Has U.S. inflation become more or less stable in recent decades.

8. Why might your answer from #7 explain your answer to #6? Earn a bonus point for connecting your answer to monetary policy.

Part III: Past Movements in Long-term Yields

9. Over the past year, the 10-year U.S. Treasury yield has risen significantly. Provide a plausible reason why?

10. What happened to the 10-year Treasury yield during the covid-19 pandemic? Why do you think it reached such extreme levels?

11. What happened to mortgage rates during the covid-19 pandemic? Why were they different from the 10-year Treasury yield?

12. In 2025, Moody's downgraded U.S. sovereign debt. Why did they do this and why might it matter?

Notes.
1.**AI use** You may use AI to search for sources. All answers should be crafted in your own words. You should not use AI to solve any math problems. Hand drawn graphs are recommended. If you use AI to create graphs, this should be indicated and the graphs should be customized to the details of the question.