Monetary Policy: Key

1. Liquidity is closely related to being a means of exchange. A liquid asset is more easily converted to cash which makes it easier to use to buy goods and services. More liquid assets are this more likely to be counted as money.

2.

$$i = \frac{1000}{800} - 1 = 25\% \tag{1}$$

3.

$$i = \frac{1000}{700} - 1 = 42\% \tag{2}$$

Notice that a lower bond price implies a higher yield.

4. Lower asset prices reduce aggregate demand which then results in lower inflation and lower output. The Fed should attempt to replace this lost demand by lowering interest rates. If done exactly correctly and on time (easier said than done), it can return AD to its original position.

5. This is just the reverse of #4. Expansionary fiscal policy creates inflation. The Fed should seek to offset its effect by raisin interest rates.

6. The AS shifts to the left leading to higher inflation and lower output. The optimal policy for the Fed is not obvious because both sides of its mandate are at odds with each other.

7. Lowering interest rates helps increase output but at the cost of even higher inflation. Raising interest rates reduces inflation but at the cost of even lower output. The Fed faces a complex tradeoff.

8. False. In most models, it only impacts aggregate demand.

9. This refers to a Central Bank's policy of buying long-term debt even after short-term interest rates are close to zero. by doing so, the Fed hopes to further lower long-term interest rates.

10. False. The Federal Reserve Act requires the Fed to seek price stability. The Fed has interpreted this to be 2% inflation..

11. Bitcoin does not do well at meeting the criteria for money. It is difficult to use to buy goods and services making it a poor means of exchange. Its volatility also makes it a questionable store of value.