

Practice Problems: Money Market and Monetary Regimes

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Open Market Operations

1. Suppose the central bank would like to increase the nominal money supply. Explain the open market operation it must conduct.
2. Suppose the central bank would like to decrease the nominal money supply. Explain the open market operation it must conduct.

Monetary/Exchange Rate Regimes

3. We discussed three exchange rate/monetary regimes. Name and explain each.
4. Consider a fixed exchange rate regime.
 - a. Does the central bank actively increase or decrease the money supply?
 - b. Explain how an increase in the money supply occurs if market conditions change so that an increase in the nominal money supply is required. What happened to international reserves?
 - c. Explain how a decrease in the money supply occurs if market conditions change so that a decrease in the nominal money supply is required. What happened to international reserves?
5. Imagine a country that has a fixed exchange rate regime. It is running a current account deficit and suffers a sudden stop. It tries to offset the sudden stop by spending down international reserves. Discuss the problems it will face doing this and the implications for its exchange rate regime.