

2. The Federal Reserve can influence the supply of money.
- (a) Assume that the Federal Reserve targets a lower federal funds rate.
 - (i) What open market operation can the Federal Reserve use to achieve the lower target?
 - (ii) Given your answer to part (a)(i), what will happen to the price of government bonds?
 - (b) Using a correctly labeled graph of the money market, show the effect of the open market operation from part (a)(i) on the nominal interest rate.
 - (c) Assume that the Federal Reserve buys government bonds from commercial banks. Based only on this transaction, will the level of required reserves in the commercial banks increase, decrease, or remain the same?
 - (d) Another monetary policy action involves changing the discount rate. Define the discount rate.
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