

# 4.6 Monetary Policy

Name: \_\_\_\_\_ Class: \_\_\_\_\_ Date: \_\_\_\_\_

Total: 9 marks

## Objective

Build the skills to answer exam questions on **monetary policy**.

**You must be able to:**

- define **monetary policy** 货币政策 as the central bank's control of the money supply and interest rates
- distinguish **expansionary** (easy) from **contractionary** (tight) monetary policy
- describe the tools: **open-market operations** 公开市场操作, the reserve requirement, and the discount rate
- trace how a change in interest rates affects investment, AD, and output

## 1 Worked examples

Study these first. Each one shows the method for a question type used later.

### ■ Monetary policy

The central bank's control of the **money supply** and **interest rates** to steer the economy.

### ■ Expansionary vs contractionary

- **Expansionary** —buy bonds, cut the reserve ratio or discount rate → rates **down** → AD **up** (fights recession).
- **Contractionary** —the reverse (fights inflation).

### ■ The tools and transmission

**Open-market operations**, the **reserve requirement**, and the **discount rate**.  
Lower rates → more investment → higher AD → higher output.

## 2 Practice

2.1 Define monetary policy.

[1]

**2.2** Name the three tools of monetary policy. [2]

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**2.3** State the monetary policy used to fight a recession. [1]

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### 3 Exam-style questions

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**3.1** To conduct expansionary monetary policy, a central bank [1]

- **A** sells bonds
- **B** buys bonds
- **C** raises the reserve ratio
- **D** raises taxes

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**3.2** When the central bank buys bonds, interest rates [1]

- **A** rise
- **B** fall
- **C** stay the same
- **D** become negative

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**3.3** A central bank wants to reduce high inflation.

(a) Name the type of monetary policy it should use. [1]

(b) State one tool and how it would be used. [2]

### 4 Go further

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- work through the **4.6 Monetary Policy** lesson on the **Learn** page;
- read the **Financial Sector** section of the AP Macroeconomics handout on the **Know**

page.

## Solutions

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**2.1** the central bank's control of the money supply and interest rates to influence the economy.

**2.2** open-market operations, the reserve requirement, the discount rate.

**2.3** expansionary (easy) monetary policy.

**3.1 B.**

**3.2 B.**

**3.3** (a) contractionary (tight) monetary policy. (b) e.g. sell bonds on the open market (or raise the reserve ratio / discount rate) to reduce the money supply.