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WORKSHEET 12

SCHOOL: BA SANGAM COLLEGE **YEAR: 12** **Name:___________**

SUBJECT: ECONOMICS

Strand	3. Macroeconomics
Sub Strand	3.1 Money and Banking
Content Learning Outcome	3.1.1 Study the domestic market for money

LESSON NOTES – MONEY AND BANKING

MONEY DEMAND - is the desired holding of financial assets in the form of money that is cash or bank deposits rather than investment. The demand curve for money is downward sloping because when interest rate increases, the demand for money falls.

Money demand exists for three motives:

1. **Transaction Demand** is a desire to hold money to buy things with i.e. for means of exchange.
2. **Precautionary Demand** is the demand that arises due to people holding money for emergency purpose or for unforeseen circumstances.
3. **Assets (Speculatory Demand)** is when people may hold money to buy shares now and sell later at a higher price so that they can get capital gain if they find the share price is increasing.

Factors Affecting Money Demand

1.The General price Level- If the general price level rises, pushing up the price, people would demand more money than before to buy things. Therefore MD (money demand) shifts right. And general price level is falling; people will demand less money than before, therefore MD shifts left.

2. Real Income - That is, if real income increases, people will demand more money to use therefore MD will shift to the right and if real income decreases, people would demand less money to spend. Money demand shift to the left.

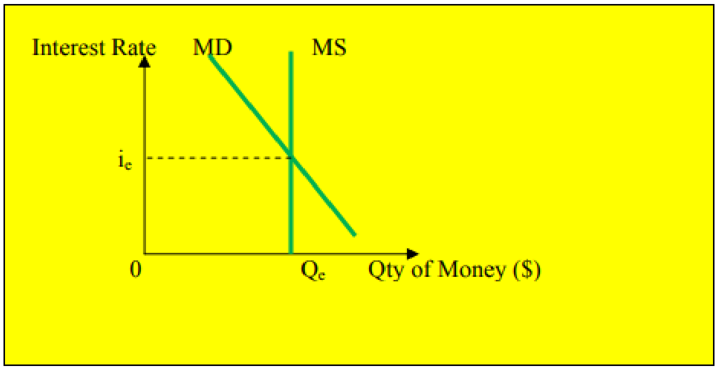
MONEY SUPPLY - Money Supply is vertical. It remains constant irrespective of the changes in the level of interest rate. The money supply is set and maintained by Reserve Bank.

Factors Affecting Money Supply

• Open Market Operation (OMO) - when Reserve bank purchases govt bonds from banks or the public it to leads increase monetary base thus increases money supply.
• Reserve Ratio - Increase in reserve ratio leads to decrease in the loanable fund which leads to decrease in MS while decrease in Required Reserve (RR) leads to increase in advances (loanable funds) which leads to increase in MS.

• Interest rate – increases in interest rate leads to decrease in investment, resulting in a decrease in AD thus decrease in MS and vice versa.

Money Market Equilibrium



It is achieved where MD intersects with MS. The basic interest rate for the economy is determined by money market equilibrium.

Note: The overall demand for money demand set by consumers and business while the MS is set and controlled by the Reserve Bank

ACTIVITY

1. There is an asset demand for money because money is a
A. Store of value. B. Medium of exchange. C. Unit of account. D. Standard of deferred payment.

2. During periods of rising general price level and rising interest rates, the demand for real cash is expected to
A. Fall. B. Rise C. Fluctuate. D. Be constant.

3. Keeping money aside in case of a bargain, is an example of ______________ demand for money.
A. Asset B. Transaction C. Speculatory D. Precautionary

4. An increase in reserve ratio will result in
A. Increase money supply B. rise in interest rate C. fall in interest rate D. Increase in money demand
(4 marks)

5. Discuss the shape of money demand curve.
____
____ **(1 mark)**

6. Discuss the shape of money supply curve.
____
____**(1 mark)**

7. Which institution in Fiji controls the money supply? _________________________ **(1 mark)**

8. State the whether the money supply will **decrease or increase** in the case of:
- Rise in interest rate _________________
- Bank keeps more money as reserves _________________
- Bank increases the quantity of loan ________________. **(3 marks)**

THE END