

## The Last One!

Do not write your name on the assignment. Write your name only on the back of this sheet of paper and staple your answers on the front of this sheet of paper. Failure to follow these directions will cost you 1 point on the assignment.

- 1) (10 points each) For each event, explain how that event affects M1 and M2.
  - A) You take \$1000 from your savings account and put it into your checking account.
  - B) You use your credit card to purchase a \$15 compact disk by the Mighty Mighty Bosstones. (It is well worth the money.)
  - C) You take \$50 out of your checking account via an ATM.
- 2) (20 points) How does the liquidity of the items in M1 compare to the liquidity of the items in M2 that are not in M1? How has the emergence of ATMs affected the liquidity of M2?
- 3) (25 points) What is adverse selection in the banking industry? What do banks do to avoid it? Explain how that action that you describe prevents the problem of adverse selection from occurring.
- 4) (25 points) Why do we care how big the money supply is? Given your answer, should we be more concerned with M1 or M2? Why?