

Place your name on the back of this sheet of paper and nowhere else. Staple your answers face up on the front of this sheet of paper. Failure to follow these directions will cost you 1 point. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to type it will cost you 10 points. If you use double-sided printing or print on the back of scrap paper, I will give you one additional point.

1) (10 points) Explain $M^d/P = L(Y, r + \pi^e)$.

2) (10 points each) For each of the following events, tell me what happens to M1 and M2. Explain your logic.

- A) You take \$400 from a money market deposit account and put it in your checking account.
- B) You pay for a \$500 textbook with a credit card.
- C) You deposit \$300 cash in a savings account.
- D) You take a car loan for \$5000.
- E) You pay for a \$2 drink at a bar with a check.

3) (10 points) Which items have a higher interest rate, the items in M1 or the items in M2 which are not in M1? What is the economic reason they give the higher return?

4) (10 points) What happened to the demand for money in M1 when it became possible to go online and move money from a savings account to a checking account online? Explain your logic.

5) (10 points) Explain the difference between *unit of account* and *medium of exchange*.

6) (10 points) Why does the time to maturity make a difference to the demand for an asset?