

Place your name on the back of this sheet of paper and nowhere else. Staple your answers 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) (15 points) Explain  $M^d = P * L(Y, r + \pi^e)$ . Since “L” is just a symbol for a function, you do not explain L, but I would like you to tell me why they chose “L” instead of the normal “F”.

2) (10 points each) For each event, determine what happens to M1 and M2. Explain your logic.

A) You transfer \$100 from your savings account to your checking account.

B) You withdraw \$50 cash from your savings account.

C) You pay the automobile repair shop \$300 with a check.

D) You pay \$300 for a textbook using a credit card.

E) You borrow \$12,000 from a bank.

3) (15 points each) For each of the following events, explain how it would affect the demand for that asset. Explain why the demand changes as described.

A) The housing market crashed in 2008. Housing used to be thought of as a safe investment.

B) The advent of internet banking on M2.

4) (5 points) Does M1 or M2 do a better job of being a medium of exchange? Explain your logic.