ECON 317 - Money, Banking, and Financial Institutions

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Monetary Policy

Exercise 1

Using the text on the functioning of monetary policy available on Moodle, answer the following questions:

(a) What is the objective of the Bank of Canada?

(b) Through which channels can the Bank of Canada maintain inflation at the desired level? Briefly explain how each channel works.

(c) What is the main challenge in implementing monetary policy?

Exercise 2

(a) Explain how the Bank of Canada reduces the supply of reserves.

(b) Using a graph, explain the effect of a reduction in the supply of reserves on the overnight target rate.

(c) What is the effect of a reduction in reserves on prices? Explain.

Exercise 3

(a) Explain the relationship highlighted by the Phillips Curve.

(b) Why does the Phillips Curve not hold over time?

(c) What are the implications for monetary policy?

Exercise 4

Read the text: http://www.cepii.fr/blog/bi/post.asp?IDcommunique=190

(a) Explain why central bank independence impacts inflation.

(b) Why might it be tempting to remove monetary policy from the responsibilities of governments?

(c) Why does the author argue that the claim that the monetary sphere is disconnected from the real sphere is unjustified?

(d) Explain the tension between an independent central bank and a democratic society.