



College of Business Administration
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Aggregate Economic Conditions & Analysis
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Monetary Growth Rate and Inflation

Assume that for each percentage point increase in the nominal interest rate, people want to hold 100 goods fewer real cash balances. During period 2 people (correctly) become aware that the growth rate of money supply will increase from 5 percent to 10 percent per year.

a) Fill in the market clearing values in the table below.

Time Period	Real Interest Rate, r	Expected Inflation,	Nominal Interest Rate, R	Nominal Money Supply, M	Price Level, P	Real Money Supply, M/P
0	3%	5%	8%	\$5714.29	\$2.86/good	2000 goods
1	3%	5%	8%	\$6000.00	\$3.00/good	2000 goods
2	3%	10%		\$6300.00		
3	3%	10%		\$6930.00		
4	3%	10%		\$7623.00		

Solution:

Time Period	Real Interest Rate, r	Expected Inflation,	Nominal Interest Rate, R	Nominal Money Supply, M	Price Level, P	Real Money Supply, M/P
0	3%	5%	8%	\$5714.29	\$2.86/good	2000 goods
1	3%	5%	8%	\$6000.00	\$3.00/good	2000 goods
2	3%	10%	13%	\$6300.00	\$4.20/good	1500 goods
3	3%	10%	13%	\$6930.00	\$4.62/good	1500 goods
4	3%	10%	13%	\$7623.00	\$5.08/good	1500 goods