1) Suppose that the Federal Reserve would like to contract the monetary base by $200M. The reserve requirement is currently 8% and the cash/deposits ratio is 90%.

   a) What transaction would be required to lower the monetary base by $200M?

       The fed would have to conduct an open market sale of treasuries.

   b) Assuming that banks hold no excess reserves, calculate the money multiplier.

       \[ mm = 1 + \frac{C}{D} = 1 + \frac{R}{D} = 1.90 + 0.98 = 2 \]

   c) What impact would a $200M reduction in the monetary base have on the M1 money supply?

       A $200M reduction in the monetary base would lower M1 by $$400M

   d) How would this transaction affect the price level?

       Prices will fall..