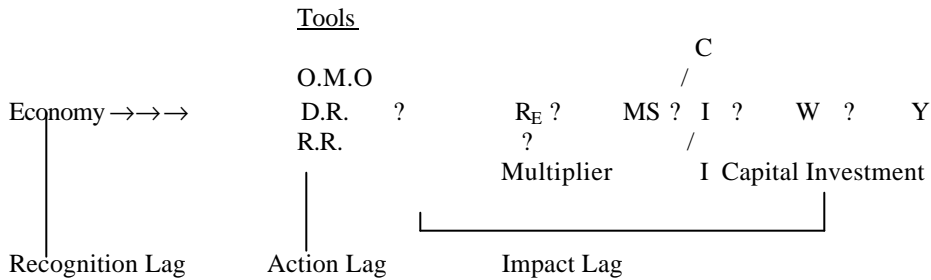


Chapter 20

The Instruments of Central Banking

Federal Reserve Tools

Transmission Mechanism



- * - Quantitative tools
 - Reserve Requirement
 - LRA vs CRA
 - Payment System
 - Simple multiplier
 - Deposit Expansion

Discount Rate

- Lags market rates
- Not permanent source of funds
- Used for
 - Adjustment Credit
 - Seasonal Credit
 - Extended Credit

- Open Market Operation

- Temporary purchase-repurchase agreements
 - Temporary sale - matched sale-purchase—reverse repos
 - Temporary purchase-repurchase agreement
 - Outright Sales/Purchases
- Purchase/ Sale of Sec.
 - New York DESK
 - OMO Conducted through "DESK"
 - Receives a reserve position of banking system as of the night before
 - Key indicator of whether the quantity of reserves is high or low relative to demand is the Fed Fund rates—if many banks have excess reserves—Fed Fund rate will fall since no one is buying
 - Call to Treasury to see if it is likely to move the balances from the tax and loan accounts at commercial banks and if what is likely to happen to Treasury balances at the Fed
 - 11:15 Conference call to board of governors and one of the Fed's bank's presidents to confirm trades for the day
 - account manager directs the Fed's traders to buy or sell securities outright or temporarily

Temporarily

Repurchase agreements

Reverse Repos (matched –sale-purchase agreement)

- Target growth rates implications
- * - Qualitative Tools
 - Purpose
 - Reg. Q
 - Margin Requirements
 - Moral Suasion
 - Min. Down Payments (during war times)
 - Credit Control Program of 1980

Dynamic versus Defensive Open Market Operations

Dynamic is policy driven --implemented to increase or decrease the level of reserves

Defensive is implemented to offset the impact of other conditions

Repurchase agreements

Reverse Repos—Matched sale-purchase agreements

1980 DIDMCA Purpose:

1. Deregulate some aspects of banking
2. Enhance the Fed=s ability to control the money supply

DIDMCA brought all depository institutions that had transaction accounts or nonpersonal time deposits under the reserve requirements set by the Fed.