

Answer on Question #56774, Economics | Macroeconomics

Question:

suppose Mr.Y deposits AED 100.000 into a one-year certificate of deposit at 5% interest.the central bank sets the reserve ratio for the banks at 10%.

- a.illustrate how the banks create money with the hep of given information.(show first 5 steps)
- b.calculate the total money creation in the economy with the help of formula.

Answer:

- a) Typically, money creation is a process of increasing money supply in a country or a monetary region like in Eurozone. Alternatively, central banks may pump in more money to their economies through lending money to financial institution or purchasing financial assets which detractors refer to expansionary monetary policy, money printing. Commercial banks also play a part in creating money by asking for mandatory deposits from the public. Attaining the sizeable threshold reverse as dictated by the central bank, enables the central bank to monitor and regulate money supply in the economy, and the product of the process and base money through fractional reserve banking.
- b) To get the total money creation we'll have to compute it this way

$$=100,000/0.1$$

$$=AED 1,000,000$$

As shown by the multiplier effect.