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Definitions and Concepts for AQA Economics A-level

Paper 2: Macroeconomics

Topic 4 – Financial Markets and Monetary Policy

Bank of England: Central bank in the UK economy, which is in control of monetary policy.

Bond: Debt; represents money that must be paid back over a period of time.

Broad money: Money held in banks and building societies but that is not immediately accessible.

Central bank: Controls the banking system and manages the government's monetary policies.

Contractionary monetary policy: Monetary policy implemented to decrease aggregate demand.

Default: The failure or inability to meet the legal minimum requirements of a loan.

Dividend: Portion of firms' profits paid to shareholders.

Equation of exchange: The stock of money in an economy multiplied by the velocity of circulation equals the price level multiplied by real output (MV=PQ).

Expansionary monetary policy: Monetary policy implemented to increase aggregate demand.

Financial sector: Firms that provide financial services.

Hot money: Highly volatile money derived from investors storing money in different institutions, looking for the highest rate of return.

Interest: Money paid to a lender by a borrower.

Monetary Policy Committee (MPC): Nine economists who meet monthly to set the Bank Rate as well as other monetary instruments.

Monetary policy: Use of interest rates and other monetary instruments to achieve macroeconomic objectives.

Money supply: Stock of money in the economy, comprised of cash and bank deposits.

Narrow money: Physical money and more liquid assets.

Quantitative easing (QE): By buying assets (generally government bonds) using newly created electronic money.

Rate of interest: The reward for saving and the cost of borrowing.

Repo rate: Rate at which the central bank can lend money to commercial banks.

Reserve currency: Foreign currency held in a country's official reserves due to its value as a medium of exchange.

Reverse repo rate: Rate at which the central bank can borrow money from commercial banks.

Shadow banking system: Unregulated firms that provide credit.

Share: Equity; represents entitlement to a portion of a firm's profits via dividends.

Systemic risk: When issues within one firm in the financial sector could bring about the collapse of the sector and/or the economy.

Transmission mechanism of monetary policy: The process by which alterations to the base rate affect determinants of aggregate demand.