

4.7 The Loanable Funds Market

Name: _____ Class: _____ Date: _____

Total: 9 marks**KEY WORDS** loanable funds market 可贷资金市场 • equilibrium real interest rate 实际利率 • nominal interest rate

Objective

Build the skills to answer exam questions on **the loanable funds market**.

You must be able to:

- describe the **loanable funds market** 可贷资金市场, where saving is supplied and borrowing demanded
- determine the **equilibrium real interest rate** 实际利率
- analyse how government borrowing, saving, or investment demand shift the market

1 Worked examples

Study these first. Each one shows the method for a question type used later.

■ The loanable funds market

Savers supply loanable funds; **borrowers** (firms investing and the government) demand them.

■ Equilibrium

The **real interest rate** where the quantity of funds saved equals the quantity borrowed.

■ Shifts

- More **government borrowing** → demand shifts right → real rate **up** (crowding out).
- More **saving** → supply shifts right → real rate **down**.

2 Practice

2.1 State who supplies and who demands loanable funds. [2]

2.2 State what is determined in the loanable funds market. [1]

2.3 State the effect of increased government borrowing on the real interest rate. [1]

3 Exam-style questions

3.1 In the loanable funds market, the “price” is the [1]

- **A** nominal interest rate
 - **B** real interest rate
 - **C** exchange rate
 - **D** price level
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3.2 An increase in saving shifts the supply of loanable funds [1]

- **A** to the left
 - **B** to the right
 - **C** not at all
 - **D** vertically
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3.3 The government runs a large budget deficit and borrows heavily.

(a) State the effect on the demand for loanable funds. [1]

(b) State the effect on the real interest rate. [1]

(c) Name the effect this has on private investment.

[1]

Solutions

2.1 savers supply funds; borrowers (firms and government) demand them.

2.2 the equilibrium real interest rate.

2.3 it rises.

3.1 B.

3.2 B.

3.3 (a) it increases (shifts right). (b) it rises. (c) crowding out of private investment.