Economics 732: Monetary Economics II  
Spring 2002  
Cornell University  

Problem Set # 5

Sunspots and Money Taxes

\[ l = 1, \quad n = 3 \]
\[ \omega = (\omega_1, \omega_2, \omega_3) = (3, 2, 1) \]
\[ \tau = (\tau_1, \tau_2, \tau_3) = (4, -4, 0) \]

1. Draw the tax-adjusted Edgeworth box that relates extrinsic uncertainty to intrinsic uncertainty.

2. Consider 3 cases:
   
   (i) perfect securities markets
   (ii) no securities markets
   (iii) restricted participation on securities markets

   (a) How do these compare in volatility of prices?
   (b) How do these compare in volatility of quantities?
   (c) What do you conclude?