Econ 1115: Principles of Macroeconomics

Lecture 17: Money and Banks

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Outline

double coincidence of
wants

1. Money
   - Fractional reserve system
2. Reserve Banking

- What is money?

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- What if we did not have money?

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  1. Requires the double coincidence of wants
  2. If not, results in a series of exchanges
  3. Waste of time searching, and transaction costs

Functions of money

Functions of money

- Medium of exchange — intermediary good

Functions of money

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- Medium of exchange
- Unit of account

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- Medium of exchange
- Unit of account
- Store of value

Types of money

- Commodity money:

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- What are cryptocurrencies and virtual money then?

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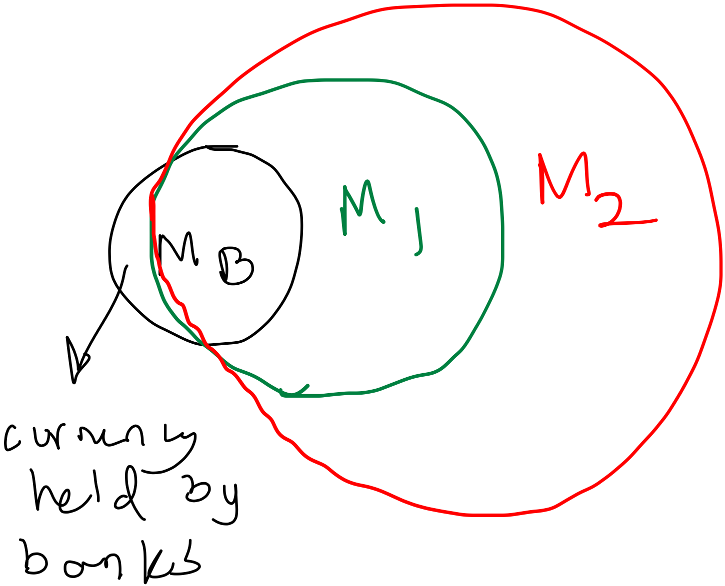
  excludes banks

- M1 = currency in circulation + checkable deposits (demand deposits + traveler's checks etc.)



MB
M1
M2
currency held by banks

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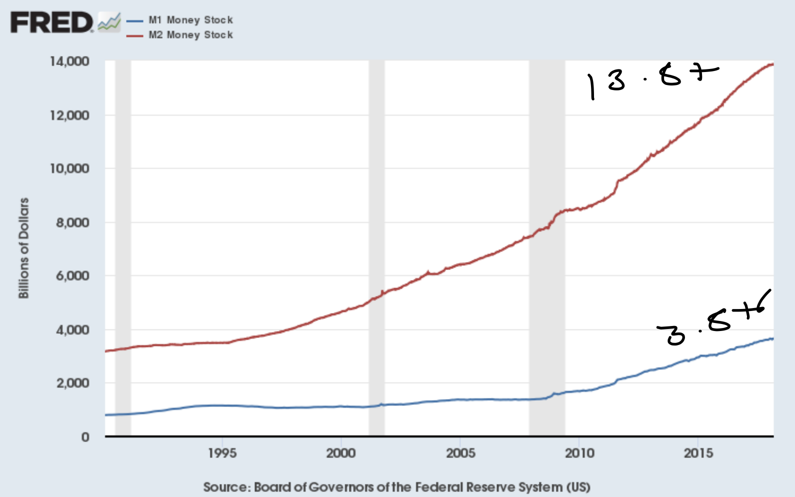
- Monetary Base = currency in circulation + currency held by banks
- M1 = currency in circulation + checkable deposits (demand deposits + traveler's checks etc.)
- M2 = M1 + savings deposits, small time deposits, money market accounts


FRED
M1 Money Stock
M2 Money Stock
14,000
12,000
10,000
8,000
6,000
4,000
2,000
0
Billions of Dollars
1995
2000
2005
2010
2015
13.6T
3.6T
Source: Board of Governors of the Federal Reserve System (US)

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We will discuss the Fed and its role in more details tomorrow.

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rr = 10%

3% (small banks)

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- 100% reserve

M_1 = Currency + c/d

– \$500 + \$50

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- Money Multiplier $= \frac{1}{\textit{Reserve Ratio}}$
- Calculate money multiplier if RR = 5% or 0.05