Money Pre-Test

1. Where does money come from?
2. What does the Federal Reserve do?
3. Is the Federal Reserve owned by the government?
4. What percentage do banks have to hold onto for reserve funds?
5. What is interest?
6. Is U.S. money paper or cloth?
7. List 5 questions you have always had about money, banking, or the stock market.
Section 1 – Money
Money is anything that serves as a medium of exchange, a unit of account, and a store of value.
Three Uses of Money

Money as Medium of Exchange

– A medium of exchange is anything that is used to determine value during the exchange of goods and services.
Money as a Unit of Account

– A unit of account is a means for comparing the values of goods and services.
Money as a Store of Value

– A store of value is something that keeps its value if it is stored rather than used.
The Six Characteristics of Money

• A currency must meet the following characteristics:
1. Durability

- Objects used as money must withstand physical wear and tear.
2. Portability

- People need to be able to take money with them as they go about their business.
3. Divisibility

• To be useful, money must be easily divided into smaller denominations, or units of value.
4. Uniformity

- Any two units of money must be uniform, that is, the same, in terms of what they will buy.
5. Limited Supply

• Money must be available only in limited quantities.
6. Acceptability

- Everyone must be able to exchange the money for goods and services.
The Sources of Money’s Value

1. Commodity money consists of objects that have value in themselves.
2. Representative money has value because the holder can exchange it for something else of value.
3. Fiat money, also called “legal tender,” has value because the government decreed that it is an acceptable means to pay debts.
Section 2 – The History of American Banking
Alexander Hamilton was in favor of a national bank which could issue a single currency, handle federal funds, and monitor other banks.
Thomas Jefferson - Anti Federalist

- Thomas Jefferson opposed the creation of a national bank, and instead favored banks created and monitored by individual states.
Shifts in the Banking System

First Bank of the United States (1791)

- held tax revenues, collected taxes, issued representative money, and monitored state-chartered banks.
Burr–Hamilton duel
Chaos in American Banking

– first Bank charter expired in 1811.
– Different, state-chartered banks began issuing different currencies.
– The Second Bank’s charter was not renewed in 1832.

– Andrew Jackson vetoed the charter.

– another period dominated by state-chartered banks took hold.
• State-chartered banks tripled
Problems

1. Bank Runs and Panics
2. Wildcat Banks
3. Fraud
4. Different Currencies
Currency in North and South

- The Union issued the first paper currency.
- “Greenbacks”
Banking Stabilization in the Late 1800s

- The National Banking Acts of 1863 and 1864 said Federal government could:
  1. charter banks
  2. require banks to hold adequate reserves of silver and gold
  3. issue a single national currency
1900-gold standard

1. It set a definite value on the dollar.
2. The government could only issue currency if it had gold in its treasury to back its notes.
Banking in the Twentieth Century

- The Federal Reserve Act of 1913 created the Federal Reserve System, which served as the nation’s first true central bank.

- The Banking Act of 1933 created the Federal Deposit Insurance Corporation (FDIC). Today, the FDIC insures customers deposits up to $250,000. The nation was also taken off of the gold standard.
Section 3 – Banking Today
Measuring the Money Supply

• **Money supply** - all the money available in the United States economy.
• M1 – money that is easily accessible to pay for goods and services.
• Liquidity – directly converted to cash. EX: currency, checking accounts, and travelers checks.
• M2 – all of M1 plus Savings and money market mutual funds.
Functions of Financial Institutions

1. Storing Money
   - compounded interest

EX: Savings, checking, money market accounts, and CD’s.
2. Credit Cards
3. Loans
4. Mortgages
Types of Financial Institutions

Commercial Banks
– offer checking services, accept deposits, and make loans.
Savings and Loan Associations

– Savings and Loan Associations were originally chartered to lend money for home-building in the mid-1800s.
Savings Banks

– Savings banks traditionally took smaller deposits and transactions than commercial banks wished to handle.
Credit Unions

– Credit unions are cooperative lending associations for particular groups, usually employees of a specific firm or government agency.
Finance Companies

–Finance companies make installment loans to consumers.
Electronic Banking

- **Automated Teller Machines (ATMs)**
- Customers can use ATMs to deposit money, withdraw cash, and obtain account information.
• **Debit Cards**
• **Debit cards** are used to withdraw money directly from a checking account.
• **Automatic Clearing Houses (ACH)**

• An ACH transfers funds automatically from customers' accounts to creditors' accounts.
• **Home Banking**

• Many banks let customers use a computer to check account balances and make transfers or payments.
• **Stored Value Cards**

• Stored value cards are embedded with magnetic strips or computer chips with account balance information. Ex: Prepaid phone card
Additional Information....
M0

- **M0**: currency (notes and coins) in circulation and in bank vaults, plus reserves which commercial banks hold in their accounts with the central bank (minimum reserves and excess reserves).
- M0 is usually called the monetary base - the base from which other forms of money (like checking deposits, listed below) are created - and is traditionally the most liquid measure of the money supply.
M1

- **M1**: currency in circulation + checkable deposits (checking deposits, officially called demand deposits, and other deposits that work like checking deposits) + traveler's checks. M1 represents the assets that strictly conform to the definition of money: assets that can be used to pay for a good or service or to repay debt. Although checks linked to checking deposits are gradually becoming less popular, debit cards linked to these deposits are becoming more popular. Like checks, debit cards, as a means to complete a transaction through their links to checkable deposits, can also be considered as a form of money.
• **M2**: M1 + savings deposits, time deposits less than $100,000 and money market deposit accounts for individuals. M2 represents money and "close substitutes" for money. M2 is a key economic indicator used to forecast inflation.
M3

- **M3**: M2 + large time deposits, institutional money-market funds, short-term repurchase agreements, along with other larger liquid assets. M3 is no longer measured by the US central bank.
How Banks Make a Profit

- The **largest source of income for banks is the interest they receive from customers who have taken loans.**
- **Interest** is the **price paid for the use of borrowed money.**
### Electronic Banking

**Automated Teller Machines (ATMs)**
Customers can use ATMs to deposit money, withdraw cash, and obtain account information.

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