

# Topics in Banking, Central Banking, and Finance

Lecture 4

Econ 4905, Fall 2016

# Absence of Money Illusion:

- Let  $P^m$  be an equilibrium price of money associated with the fiscal policy  $\tau$ . If instead the fiscal policy is  $\lambda\tau$  where the scalar lambda is  $0 < \lambda \leq 1$ , then  $P^m / \lambda$  is *an* equilibrium price of money.

## The Quantity Theory of Money:

- Let  $P^m$  be **the** equilibrium price of money associated with the fiscal policy  $\tau$ . Then,  $P^m / \lambda$  is **the** equilibrium price of money associated with  $\lambda\tau$ .
- Our models are consistent with AMI, but they are not consistent with QTM.

# Banking History

- The gold-smith
- Usury
- Florence and Northern Italy
- Genoa
- Venice
- Bruges
- Hanse
- Bank of England
- First Bank of the United States
- Alexander Hamilton and Thomas Jefferson
- Revolutionary War Debt
- French and Cayugas
- Cayugas and the Revolution

# Four English Groups in America

- Puritans. New England from East Anglia.
- Quakers. Delaware Valley from Wales and the mid-lands
- Southern Gentry. *nth* sons and distressed sons of the aristocracy.
- Back country. From the borders.

Also

- New Amsterdam
- New Netherlands

# Banking History

- Andrew Jackson and the collapse of the central bank
- Antipathy to cities and finance by planters and backwoodsmen.
  - Main Street versus Wall Street
- English Civil War, the American Revolution, the American Civil War

# The Federal Reserve

- **Board** of Governors
- Regional Banks
- Historical primacy of the NY Fed
- Open Market Committee

- Fiscal policy and the Deficit (Surplus)
- Debt
- Monetary Policy: The composition of the public debt
- Interest-bearing
- Non-interest-bearing
- QE
- Commercial banking, depository institutions
- Shadow banking

# Banking Instruments:

- Demand deposits
- Time deposits
- Secured loans
  - Mortgages
- Unsecured loans
  - Personal
  - Business
- Line of Credit
- Commercial Paper
- Financial intermediation
- Dis-intermediation
- Bank runs



# Finance

- Miracle of compound interest
  - Rule of 70
- Corporate equity (common stocks)
- Corporate bonds (debt)
- Preferred stocks (debt)
- Leverage (or gearing)
  - $\text{Debt} \div (\text{equity} + \text{debt})$
- Limited liability
- Corporate income tax
  - Double taxation of common stocks
  - Interest deductible
  - Dividends not deductible

# Readings

- 4 papers on banking and bank runs from reading
- Diamond-Dybvig classic
- Ennis-Keister survey
- Peck-Shell
  - Combining “sunspots” with risk of panic-based runs
- Shell-Zhang
  - Bank runs, mechanism design, and game theory