

高等学校经济类双语教学推荐教材

PEARSON



*economics
classics*

Economics

经济学经典教材·金融系列

Classics

货币、银行

和金融体系

Money, Banking,

and the Financial System

R·格伦·哈伯德 (R. Glenn Hubbard)

著

安东尼·P·奥布赖恩 (Anthony Patrick O'Brien)

中国人民大学出版社

PEARSON



INTERNATIONAL BANKING

International Banking

INTERNATIONAL BANKING

INTERNATIONAL BANKING

INTERNATIONAL BANKING

高等学校经济类双语教学推荐教材



ECONOMICS
CLASSICS

经济学经典教材·金融系列

ECONOMICS CLASSICS

货币、银行 和金融体系

Money, Banking, and the Financial System

R·格伦·哈伯德 (R. Glenn Hubbard)

著

安东尼·P·奥布赖恩 (Anthony Patrick O'Brien)

中国人民大学出版社

· 北京 ·

图书在版编目(CIP)数据

货币、银行和金融体系：英文/（ ）哈伯德，（ ）奥布赖恩著. —北京：
中国人民大学出版社，2013.6

经济学经典教材·金融系列

ISBN 978-7-300-17410-5

I. ①货… II. ①哈… ②奥… III. ①货币银行学-高等学校-教材-英文 ②金融体系-高等学校-教材-英文 IV. ①F820 ②F830.2

中国版本图书馆CIP数据核字(2013)第116312号

高等学校经济类双语教学推荐教材

经济学经典教材·金融系列

货币、银行和金融体系

R·格伦·哈伯德 著

安东尼·P·奥布赖恩

Huobi, Yinhang he Jinrong Tixi

出版发行 中国人民大学出版社

社 址 北京中关村大街31号

邮政编码 100080

电 话 010-62511242 (总编室)

010-62511398 (质管部)

010-82501766 (邮购部)

010-62514148 (门市部)

010-62515195 (发行公司)

010-62515275 (盗版举报)

网 址 <http://www.crup.com.cn>

<http://www.ttrnet.com> (人大教研网)

经 销 新华书店

印 刷 三河市汇鑫印务有限公司

规 格 215mm×275mm 16开本

版 次 2013年8月第1版

印 张 36.25 插页 1

印 次 2013年8月第1次印刷

字 数 1 390 000

定 价 69.00元

版权所有

侵权必究

印装差错

负责调换

出版说明

入世十年，我国已完全融入到经济全球化的浪潮中。党的十六大确立了“引进来，走出去”的发展战略，使得“国际化”复合型人才的需求不断增加。这就对我国一般本科院校多年来所采取的单一语言（母语）教学提出严峻挑战，经济类专业双语教学改革迫在眉睫。

为配合高校经济类专业双语教学改革，中国人民大学出版社携手培生、麦格劳-希尔、圣智等众多国际知名出版公司，倾情打造了该套“经济类双语系列教材”，本套教材包括：经济管理类专业开设的核心课程、经济学专业开设的主干课程以及财政金融专业和国际贸易专业的主要课程。所选教材均为国外最优秀的本科层次经济类教材。

我们在组织、引进和出版该系列教材的过程中，严把质量关。聘请国内著名经济学家、学者以及一线授课教师审核国外原版教材，广泛听取意见，努力做到把国外真正高水平的适合国内实际教学需求的优秀教材引进来，供国内广大师生参考、研究和学习。

本系列教材主要有以下特点：

第一，教材体系设计完整。本系列教材全部为国外知名出版公司的优秀教材，涵盖了经济类专业的所有主要课程。

第二，英文原版教材特色。本系列教材依据国内实际教学需要以及广泛适应性，部分对原版教材进行了全文影印，部分在保持原版教材体系结构和内容特色的基础上进行了适当删减。

第三，内容紧扣学科前沿。本系列教材在原著选择上紧扣国外教学前沿，基本上都是国外最流行教材的最新版本。

第四，篇幅合理、价格适中。本系列教材一方面在内容和篇幅上很好地适应了国内双语教学的实际需要，另一方面，低定价策略又避免了国外原版图书高额的购买费用。

第五，提供强大的教学支持。依托国外知名出版公司的资源，本系列教材为教师提供丰富的配套教辅资源，如教师手册、PPT课堂演示文稿、试题库等，并配有内容丰富的网络资源，使教学更为便利。

本系列教材既适合高等院校经济类专业的本科教学使用，也适合从事经济类工作和研究的广大从业者的阅读和学习。我们在选书、改编过程中虽然全面听取了专家、学者和教师的意见，努力做到满足广大读者的需求，但由于各教材的作者所处的政治、经济和文化背景不同，书中内容仍可能有不妥之处，我们真诚希望广大读者提出宝贵意见和建议，以便我们在以后的版本中不断改进和完善。

中国人民大学出版社

Preface

Do You Think This Might Be Important?

It's customary for authors to begin textbooks by trying to convince readers that their subject is important, even exciting. Following the events of the financial crisis and recession of 2007–2009, we doubt anyone needs convincing that the study of money, banking, and financial markets is important. And exciting . . . maybe it's a little too exciting. Nothing comparable to the upheaval of 2007–2009 had happened in the financial system since the Great Depression of the 1930s. The financial crisis changed virtually every aspect of how money is borrowed and lent, how banks and other financial firms operate, and how policymakers regulate the financial system. There seems little doubt that the effects of the crisis will linger for a very long time, just as did the effects of the Great Depression.

Our Approach

In this book, we provide extensive analysis of the financial events of the past few years. We believe these events are sufficiently important to be incorporated into the body of the text rather than just added as boxed-off features. In particular, we stress the lesson policymakers recently learned the hard way: What happens in the ever-expanding part of the financial system that does not involve commercial banks is of vital importance to the entire economy.

We realize, however, that the details of the financial crisis and recession will eventually pass into history. What we strive to do in this text is not to add to the laundry list of facts that students must memorize. Instead, we present students with the underlying economic explanations of why the financial system is organized as it is and how the financial system is connected to the broader economy. We are gratified by the success of our principles of economics textbook, and we have employed a similar approach in this textbook: We provide students with a framework that allows them to apply the theory that they learn in the classroom to the practice of the real world. By learning this framework, students will understand not just the 2007–2009 financial crisis and other past events but also developments in the financial system during the years to come. To achieve this goal, we have built four advantages into this text:

1. A framework for understanding, evaluating, and predicting
2. A modern approach
3. Integration of international topics
4. A focus on the Federal Reserve

Framework of the Text: Understand, Evaluate, Predict

The framework underlying all discussions in this text has three levels. First, students learn to *understand* economic analysis. “Understanding” refers to students developing the economic intuition they need to organize concepts and facts. Second, students learn to *evaluate* current developments and the financial news. Here, we challenge students to use financial data and economic analysis to think critically about how to interpret current events. Finally, students learn to use economic analysis to *predict* likely changes in the economy and the financial system. Having just come through a period in which Federal Reserve officials, members of Congress, heads of Wall Street firms, and nearly everyone else failed to predict a huge financial crisis, the idea that we can prepare students to predict the future of the financial system may seem overly ambitious—to say the least. We admit, of course, that some important events are difficult to anticipate. But knowledge of the economic analysis we present in this book does make it possible to predict many aspects of how the financial system will evolve. For example, in Chapter 12, “Financial Crises and Financial Regulation,” we discuss the ongoing cycle of financial crisis, regulatory response, financial innovation, and further regulatory response. The latest episode in this cycle was the passage in July

2010 of the Dodd-Frank *Wall Street Reform and Consumer Protection Act*. With our approach, students learn not just the new regulations contained in Dodd-Frank but, more importantly, the key lesson that over time innovations by financial firms are likely to supersede many of the provisions of Dodd-Frank. In other words, students will learn that the financial system is not static—it evolves over time in ways that can be understood using economic analysis.

A Modern Approach

Textbooks are funny things. Most contain a mixture of the current and the modern alongside the traditional. Material that is helpful to students is often presented along with material that is not so helpful or that is—frankly—counterproductive. We believe the ideal is to produce a textbook that is modern and incorporates the best of recent research on monetary policy and the financial system without chasing every fad in economics or finance. In writing this book, we have looked at the topics in the money and banking course with fresh eyes. We have pruned discussion of material that is less relevant to the modern financial system or no longer considered by most economists to be theoretically sound. We have also tried to be as direct as possible in informing students of what is and is not important in the financial system and policymaking as they exist today. For example, rather than include the traditional long discussion of the role of reserve requirements as a monetary policy tool, we provide a brief overview and note that the Federal Reserve has not changed reserve requirements since 1992. Similarly, it has been several decades since the Fed paid serious attention to targets for M1 and M2. Therefore, in Chapter 18, “Monetary Theory II: The *IS–MP* Model,” we replace the *IS–LM* model—which assumes that the central bank targets the money stock, rather than an interest rate—with the *IS–MP* model, first suggested by David Romer more than 15 years ago. We believe that our modern approach improves the ability of students to make the connection between the text material and the economic and financial world they read about. (For those who do wish to cover the *IS–LM* model, we provide an appendix on that model after Chapter 18.)

By cutting out-of-date material, we have achieved two important goals: (1) We provide a much briefer and more readable text, and (2) we have made room for discussion of essential topics, such as the “shadow banking system” of investment banks, hedge funds, and mutual funds, as well as the origins and consequences of financial crises. See Chapter 11, “Investment Banks, Mutual Funds, Hedge Funds, and the Shadow Banking System,” and Chapter 12, “Financial Crises and Financial Regulation.” Other texts either omit these topics or cover them only briefly.

We have both taught money and banking to undergraduate and graduate students for many years. We believe that the modern, real-world approach in our text will engage students in ways that no other text can.

Integration of International Topics

When the crisis in subprime mortgages began, Federal Reserve Chairman Ben Bernanke famously observed that it was unlikely to cause much damage to the U.S. housing market, much less the wider economy. (We discuss Bernanke’s argument in Chapter 12, “Financial Crises and Financial Regulation,” where we note that he was hardly alone in making such statements.) As it turned out, of course, the subprime crisis devastated not only the U.S. housing market but the U.S. financial system, the U.S. economy, and the economies of most of the developed world. That a problem in one part of one sector of one economy could cause a worldwide crisis is an indication that a textbook on money and banking must take seriously the linkages between the U.S. and other economies. Our text consists of only 18 chapters and is one of the briefest texts on the market. We achieved this brevity by carefully pruning many out-of-date and esoteric topics to focus on the essentials, which includes a careful exploration of international topics. We devote two full chapters to international topics: Chapter 8, “The Market for Foreign Exchange,”

and Chapter 16, “The International Financial System and Monetary Policy.” In these chapters, we discuss such issues as the European sovereign debt crisis of 2010 and the increased coordination of monetary policy actions among central banks. We realize, however, that, particularly in this course, what is essential to one instructor is optional to another. So, we have written the text in a way that allows instructors to skip one or both of the international chapters.

A Focus on the Federal Reserve

We can hardly claim to be unusual in focusing on the Federal Reserve in a money and banking textbook . . . but we do! Of course, all money and banking texts discuss the Fed, but generally not until near the end of the book—and the semester. Based on speaking to instructors in focus groups and on our own teaching experience, we believe that this approach is a serious mistake. We have found that students often have trouble integrating the material in the money and banking course. To them, the course often seems a jumble of unrelated topics. Particularly in light of recent events, the role of the Fed can serve as a unifying theme for the course. Accordingly, we provide an introduction and overview of the Fed in Chapter 1, “Introducing Money and the Financial System,” and in each subsequent chapter, we expand on the Fed’s role in the financial system. So, by the time students read Chapter 13, “The Federal Reserve and Central Banking,” where we discuss the details of the Fed’s operation, students already have a good idea of the Fed’s importance and its role in the system.

目 录

前 言	i
第 1 章 货币和金融体系简介	1
1.1 金融体系的核心组成部分	2
1.2 2007—2009 年的金融危机	14
1.3 源于金融危机的核心议题和问题	16
第 2 章 货币和支付体系	24
2.1 我们需要货币吗?	25
2.2 货币的核心功能	27
2.3 支付体系	29
2.4 度量货币供给	32
2.5 货币数量论:货币与价格之间联系的首次审视	35
第 3 章 利率和收益率	49
3.1 利率、现值和终值	50
3.2 债务工具及其价格	56
3.3 债券价格与到期收益率	60
3.4 债券价格与债券收益率之间的反向关系	63
3.5 利率和收益率	69
3.6 名义利率对实际利率	70
第 4 章 利率的决定	82
4.1 如何构建一个投资组合	83
4.2 市场利率与债券的需求和供给	88
4.3 债券市场模型和利率的变动	96
4.4 可贷资金模型和国际资本市场	101
第 5 章 利率的风险结构和期限结构	116
5.1 利率的风险结构	117
5.2 利率的期限结构	127
第 6 章 股票市场、信息和金融市场效率	148
6.1 股票和股票市场	149
6.2 股票价格是如何决定的	154
6.3 理性预期和有效市场	159
6.4 金融市场的实际效率	165
6.5 行为金融学	168
第 7 章 衍生品和衍生品市场	179
7.1 衍生品、对冲和投机	180
7.2 远期合约	181
7.3 期货合约	182
7.4 期权	189

7.5	互换	197
第 8 章	外汇市场	211
8.1	汇率和贸易	212
8.2	外汇市场	215
8.3	长期汇率	219
8.4	汇率短期波动的供需模型	222
第 9 章	交易成本、不对称信息和金融体系的结构	238
9.1	匹配储蓄者和借款人的障碍	239
9.2	逆向选择和道德风险问题	241
9.3	关于美国金融体系结构的结论	252
第 10 章	银行经济学	264
10.1	商业银行业务基础:银行资产负债表	265
10.2	商业银行的基本业务	273
10.3	管理银行风险	276
10.4	美国商业银行业的趋势	280
第 11 章	投资银行、共同基金、对冲基金和影子银行体系	297
11.1	投资银行业务	298
11.2	投资机构:共同基金、对冲基金和金融公司	308
11.3	契约性储蓄机构:养老基金和保险公司	312
11.4	系统风险和影子银行体系	317
第 12 章	金融危机和金融监管	328
12.1	金融危机的根源	329
12.2	大萧条时期的金融危机	336
12.3	2007—2009 年的金融危机	340
12.4	金融危机与金融监管	343
第 13 章	联邦储备和中央银行业务	362
13.1	联邦储备体系的结构	363
13.2	联储如何运作	372
13.3	美国之外的中央银行独立性	377
第 14 章	联储的资产负债表和货币供给过程	387
14.1	联储的资产负债表和基础货币	388
14.2	简单存款乘数	395
14.3	银行、非银行公众和货币乘数	399
	附录:M2 的货币供给过程	416

第 15 章 货币政策	417
15.1 货币政策的目标	418
15.2 货币政策工具和联邦基金利率	421
15.3 联储的货币政策工具详述	426
15.4 货币指标制和货币政策	432
第 16 章 国际金融体系与货币政策	453
16.1 外汇市场干预和基础货币	454
16.2 外汇市场干预和汇率	456
16.3 国际收支	460
16.4 汇率制度和国际金融体系	462
第 17 章 货币理论 I: 总需求和总供给模型	484
17.1 总需求曲线	486
17.2 总供给曲线	489
17.3 总需求和总供给模型中的均衡	494
17.4 货币政策的作用	499
第 18 章 货币理论 II: IS-MP 模型	513
18.1 IS 曲线	514
18.2 MP 曲线和菲利普斯曲线	523
18.3 IS-MP 模型中的均衡	529
18.4 利率是货币政策的一切吗?	537
附录: IS-LM 模型	547
术语表	G-1

Contents

Preface.....	i
Chapter 1 Introducing Money and the Financial System.....	1
CAN THE FED RESTORE THE FLOW OF MONEY?	1
1.1 Key Components of the Financial System.....	2
1.2 The Financial Crisis of 2007–2009	14
1.3 Key Issues and Questions from the Financial Crisis	16
An Inside Look at Policy: Fed Ready to Help Economy, But Options Are Limited	19
Chapter 2 Money and the Payments System.....	24
THE FEDERAL RESERVE FIGHTS TO PRESERVE ITS INDEPENDENCE	24
Key Issue and Question	24
2.1 Do We Need Money?	25
2.2 The Key Functions of Money	27
2.3 The Payments System	29
2.4 Measuring the Money Supply.....	32
2.5 The Quantity Theory of Money: A First Look at the Link Between Money and Prices	35
Answering the Key Question	41
An Inside Look at Policy: Its Independence Was Threatened, but New Law Grants the Fed New Powers	42
Chapter 3 Interest Rates and Rates of Return.....	49
BANKS IN TROUBLE	49
Key Issue and Question	49
3.1 The Interest Rate, Present Value, and Future Value.....	50
3.2 Debt Instruments and Their Prices.....	56
3.3 Bond Prices and Yield to Maturity.....	60
3.4 The Inverse Relationship Between Bond Prices and Bond Yields.....	63
3.5 Interest Rates and Rates of Return	69
3.6 Nominal Interest Rates Versus Real Interest Rates	70
Answering the Key Question	73
An Inside Look at Policy: Higher Interest Rates Increase Coupons, Decrease Capital Gains	74
Chapter 4 Determining Interest Rates.....	82
IF INFLATION INCREASES, ARE BONDS A GOOD INVESTMENT?	82
Key Issue and Question	82
4.1 How to Build an Investment Portfolio	83
4.2 Market Interest Rates and the Demand and Supply for Bonds	88

4.3 The Bond Market Model and Changes in Interest Rates 96
4.4 The Loanable Funds Model and the International Capital Market 101
Answering the Key Question 108
An Inside Look at Policy: Investors Forecast Lower Bond Prices, Higher Interest Rates 109

Chapter 5 The Risk Structure and Term Structure of Interest Rates 116

WHY INVEST IN TREASURY BILLS IF THEIR INTEREST RATES ARE SO LOW? 116
Key Issue and Question 116
5.1 The Risk Structure of Interest Rates 117
5.2 The Term Structure of Interest Rates 127
Answering the Key Question 138
An Inside Look at Policy: Executives from Moody’s, Standard and Poor’s Describe Pressure to Grant High Ratings 140

Chapter 6 The Stock Market, Information, and Financial Market Efficiency 148

WHY ARE STOCK PRICES SO VOLATILE? 148
Key Issue and Question 148
6.1 Stocks and the Stock Market 149
6.2 How Stock Prices Are Determined 154
6.3 Rational Expectations and Efficient Markets 159
6.4 Actual Efficiency in Financial Markets 165
6.5 Behavioral Finance 168
Answering the Key Question 170
An Inside Look: Prices Rally but Individual Investors Still Avoid Stocks 171

Chapter 7 Derivatives and Derivative Markets 179

HOW DANGEROUS ARE FINANCIAL DERIVATIVES? 179
Key Issue and Question 179
7.1 Derivatives, Hedging, and Speculating 180
7.2 Forward Contracts 181
7.3 Futures Contracts 182
7.4 Options 189
7.5 Swaps 197
Answering the Key Question 201
An Inside Look at Policy: Traders Uncertain About Impact of New Derivatives Rules 202

Chapter 8 The Market for Foreign Exchange 211

WHY WOULD THE U.S. FEDERAL RESERVE LEND DOLLARS TO FOREIGN CENTRAL BANKS? 211

Key Issue and Question	211
8.1 Exchange Rates and Trade	212
8.2 Foreign-Exchange Markets	215
8.3 Exchange Rates in the Long Run	219
8.4 A Demand and Supply Model of Short-Run Movements in Exchange Rates	222
Answering the Key Question	230
An Inside Look at Policy: Investors Buy Dollars and Sell Euros as Europe Faces a Debt Crisis	231

Chapter 9 Transactions Costs, Asymmetric Information, and the Structure of the Financial System 238

BUYER BEWARE IN FINANCIAL MARKETS!	238
Key Issue and Question	238
9.1 Obstacles to Matching Savers and Borrowers	239
9.2 The Problems of Adverse Selection and Moral Hazard	241
9.3 Conclusions About the Structure of the U.S. Financial System	252
Answering the Key Question	256
An Inside Look at Policy: Ratings Downgrades Happen Too Late for Investors in Mortgage-Backed Securities	257

Chapter 10 The Economics of Banking 264

WHAT HAPPENS WHEN LOCAL BANKS STOP LOANING MONEY?	264
Key Issue and Question	264
10.1 The Basics of Commercial Banking: The Bank Balance Sheet	265
10.2 The Basic Operations of a Commercial Bank	273
10.3 Managing Bank Risk	276
10.4 Trends in the U.S. Commercial Banking Industry	280
Answering the Key Question	289
An Inside Look at Policy: Interest-Rate Hikes Threaten Bank Profits	290

Chapter 11 Investment Banks, Mutual Funds, Hedge Funds, and the Shadow Banking System 297

WHEN IS A BANK NOT A BANK? WHEN IT'S A SHADOW BANK!	297
Key Issue and Question	297
11.1 Investment Banking	298
11.2 Investment Institutions: Mutual Funds, Hedge Funds, and Finance Companies	308
11.3 Contractual Savings Institutions: Pension Funds and Insurance Companies	312
11.4 Systemic Risk and the Shadow Banking System	317
Answering the Key Question	319

An Inside Look at Policy: Did a Shadow Bank Panic Cause the Financial Crisis of 2007–2009?	320
--	-----

Chapter 12 Financial Crises and Financial Regulation 328

A CLOUDY CRYSTAL BALL ON THE FINANCIAL CRISIS.....	328
Key Issue and Question	328
12.1 The Origins of Financial Crises	329
12.2 The Financial Crisis of the Great Depression.....	336
12.3 The Financial Crisis of 2007–2009	340
12.4 Financial Crises and Financial Regulation	343
Answering the Key Question	352
An Inside Look at Policy: Congress Struggles to Reform Financial Markets, Prevent Future Crisis.....	353

Chapter 13 The Federal Reserve and Central Banking 362

IS THE FED THE GIANT OF THE FINANCIAL SYSTEM?.....	362
Key Issue and Question	362
13.1 The Structure of the Federal Reserve System.....	363
13.2 How the Fed Operates	372
13.3 Central Bank Independence Outside the United States.....	377
Answering the Key Question	380
An Inside Look at Policy: U.S. Senate Questions Three Nominees to Fed's Board of Governors.....	381

Chapter 14 The Federal Reserve's Balance Sheet and the Money Supply Process 387

GEORGE SOROS, "GOLD BUG"	387
Key Issue and Question	387
14.1 The Federal Reserve's Balance Sheet and the Monetary Base	388
14.2 The Simple Deposit Multiplier.....	395
14.3 Banks, the Nonbank Public, and the Money Multiplier	399
Answering the Key Question	408
An Inside Look at Policy: Fed's Balance Sheet Needs Balancing Act	409
Appendix: The Money Supply Process for M2.....	416

Chapter 15 Monetary Policy 417

BERNANKE'S DILEMMA.....	417
Key Issue and Question.....	417
15.1 The Goals of Monetary Policy.....	418
15.2 Monetary Policy Tools and the Federal Funds Rate.....	421
15.3 More on the Fed's Monetary Policy Tools	426

15.4 Monetary Targeting and Monetary Policy	432
Answering the Key Question	444
An Inside Look at Policy: The Fed May Buy More Bonds to Boost Sluggish Economy	445

Chapter 16 The International Financial System and Monetary Policy 453

CAN THE EURO SURVIVE?	453
Key Issue and Question	453
16.1 Foreign Exchange Intervention and the Monetary Base	454
16.2 Foreign Exchange Interventions and the Exchange Rate	456
16.3 The Balance of Payments	460
16.4 Exchange Rate Regimes and the International Financial System	462
Answering the Key Question	476
An Inside Look at Policy: Are the Euro's Benefits Worth the Costs?	477

Chapter 17 Monetary Theory I: The Aggregate Demand and Aggregate Supply Model 484

IS THE UNITED STATES FACING A "NEW NORMAL" OF HIGHER UNEMPLOYMENT?	484
Key Issue and Question	484
17.1 The Aggregate Demand Curve	486
17.2 The Aggregate Supply Curve	489
17.3 Equilibrium in the Aggregate Demand and Aggregate Supply Model	494
17.4 The Effects of Monetary Policy	499
Answering the Key Question	505
An Inside Look at Policy: Unemployment Stays High Despite Low Interest Rates, Fiscal Stimulus	506

Chapter 18 Monetary Theory II: The *IS–MP* Model 513

THE FED FORECASTS THE ECONOMY	513
Key Issue and Question	513
18.1 The <i>IS</i> Curve	514
18.2 The <i>MP</i> Curve and the Phillips Curve	523
18.3 Equilibrium in the <i>IS–MP</i> Model	529
18.4 Are Interest Rates All That Matter for Monetary Policy?	537
Answering the Key Question	539
An Inside Look at Policy: Slow Growth Despite Low Interest Rates Has Fed Searching for New Options	540
Appendix: The <i>IS–LM</i> Model	547
Glossary	G-1

Introducing Money and the Financial System

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- 1.1** Identify the key components of the financial system (pages 2–14)
- 1.2** Provide an overview of the financial crisis of 2007–2009 (pages 14–16)
- 1.3** Explain the key issues and questions the financial crisis raises (pages 16–18)

CAN THE FED RESTORE THE FLOW OF MONEY?

Large areas of southern Arizona and California's central valley have rich soils but receive very little rain. Without an elaborate irrigation system of reservoirs and canals, water would not flow to these areas, and farmers could not raise their vast crops of lettuce, asparagus, cotton, and more. The financial system is like an irrigation system, although it is money, not water, that flows through the financial system. During the economic crisis that began in 2007, the financial system was disrupted as it hadn't been since the 1930s, and large sections of the U.S. economy were cut off from the flow of funds they needed to thrive. Just as cutting off the irrigation water in California's San Joaquin Valley would halt the production of crops, the financial crisis resulted in a devastating decline in production of goods and services throughout the economy.

Like engineers trying to repair a damaged irrigation canal to restore the flow of water, officials of the U.S. Treasury Department and the Federal Reserve (the Fed) took strong actions during the financial crisis to restore the flow of money through banks and financial markets to the firms and households that depend on it. Although some of these policies were controversial, most economists believe that some government intervention was necessary to pull the economy out of a deep recession.

How deep was the recession of 2007–2009? More than 8 million jobs were lost, and the unemployment rate rose above 10% for the first time in almost three decades. Many college students graduating during the recession had difficulty finding jobs, and even those who did often had to accept less desirable positions at lower salaries than they had expected. And this was not just a temporary setback for these graduates. Studies show that workers entering the labor force during a recession typically receive salaries that are 10% less than the salaries they would have earned had they entered the labor force during an economic expansion. Even worse news: Their salaries may remain lower for a decade or more.

The financial crisis contributed to the bankruptcy of General Motors and Chrysler, two pillars of industrial America, as well as to the disappearance of decades-old Wall Street investment houses such as Lehman Brothers and Bear Stearns. Stock prices plunged, and many older workers saw their savings shrink and had to put their retirement dreams on hold.

AN INSIDE LOOK AT POLICY on page 19 reviews three options Federal Reserve Chairman Ben Bernanke considered to further support the economy in late 2010.