

Lecture 4

Lecture 4 will use the following transparencies, plus Figure 1 and Table 1-2 of Chapter 3 of the textbook

Functions of Money

- Medium of Exchange
- Unit of Account (important for quoting prices, writing contracts)
- Store of Value
- Standard of Deferred Payment

The Value of Money

- Value of money (in terms of goods): inverse of the price level
- Real return on money between one period to the next: ratio of next period price level to the current price level (= the *inflation rate*)

Features of Money

Whatever serves as money should be

- Easy to carry
- Hard to counterfeit
- Durable
- Divisible
- Be stable in value

The Evolution of Money

- Commodity Money System (typically precious metals)
 - 1 dollar is a fixed amount of gold
 - if paper dollar exist, they can be converted into gold
- Fiat Money System
 - 1 dollar is a piece of paper issued by the government
 - it is a claim to nothing at all
 - it is a legal tender

Non-Cash Payments

- Checks
- Direct debit transactions
- Debit cards
- Wire transfers (Fedwire, CHIPS) among banks
- Automatic clearinghouses (ACH)
- e-money (stored-value cards; e-cash/checks)

Measuring Money

- Money definitions frequently change with financial innovation
 - Narrow and broad money supply series do not move together closely
 - Short run money data are inaccurate in short run (bank reporting deadlines; seasonal adjustment)
- > money supply data hard to interpret in the short run when policy decision must be made)
- > most central banks have given up formulating targets for the money supply