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CATALOG NO. 50939

Bank Assets (Dec. '56, FRB)

1956, all commercial banks

Loans \$876	36	"Commercial," incl. (largely secured by r.e. prothly)
	4	"Agri." " " "
	4	For buyg or carryg securities
	22	R.e.
	18	Other loans to individuals { largely secured by r.e. no doubt
	3	Other loans { (Consumer credit, 11.8 prothly)

Investments 73	51	U.S. (of which 40 is bonds)
	11	U.S. guaranteed
	13	State & local
	4	other

160

Argument: All bank assets besides U.S. are largely backed by r.e. collateral. Banks' willingness to lend to pvt. borrowers is due to hi l.v. When these drop, pvt loans drop, deflation ensues. U.S. decides not to borrow more, so d.d. drop. Anti-g deflation, non-bank bondholders hanging on to bonds, so banks have no borrowers. Aggreg conceal, too, some risky banks, which fail.

Bank Assets, etc., p. 2

No run, panic, due to insurance etc. But that was not vital anyway, merely spectacular. Other aspects continue as before.

F.R. data don't tell you much about character of loans, probly. "Commercial & industrial", e.g., may be land based.

All lenders.	1939	1945	1950	1953	1955	1956
Consumer Credit	7.2	5.7	21.4	31.2	38.6	40.2
Installment	4.5	2.5	14.7	23.0		30.8
Other	2.7	3.2	6.7	8.2		9.4

All lenders,						
Mortgage Loans		35.5	73	101	130	141
Funds		21.0	52			109
Individuals		13.7	20			29

Corp. Bonds
outstanding

Commercial banks

Assets	Liabilities
Loans \$896	D.d. 121
U.S. Sec. 51	Time 51
Other Sec. 16	Cap. 16
Cash 42	<hr/> 188
<hr/> 204	Interbank dep. 15
	<hr/> 203

$42 - 15 = 27$, cash, net, of which 19.4 were member reserves, probly rest are non-members reserves in large part.

Member banks

Assets	Liabilities
Loans 76.6	D.d. 103
US Sec. 46.6	Time dep. 41
Other Sec. 13.2	Cap. 14
Cash } 22 minus interbank	<hr/> 158
<hr/> 158.4	

Nov. 1956 Condition of all F.R. banks

Gold stock 21.9
F.R. Notes 27.1
F.R. dep. 20.2

Treas. Currency 5.1
Breakdown, p. 1327
"Currency in circ." 31.4

Member reserves 19.4
Required 18.7

F.R. Assets:
U.S. Secs 24.2
Loans .6
Float 1.5
Gold cert. ~~20.4~~
21.2

Gold
Notes & dep = 44.9

Member res. req.

Min 13 10 7
Max 26 20 14
current 20 18 12

Annual rate of turnover of d.d., ~~51~~
155. See p. 1326 M

Money. Hope saw exhibit.

Is M worth just gold in it? Or gold can redeem it for.

a. Coins, seigneurage (Kick wrong, says no more)

b. Paper, extreme of seign.

But backed by gold.

But more paper than gold — still govt guarantees.

Or no gold at all, since '33. "Will pay bearer on demand \$5"

c. Or use anything. Cigs, sheepskin, wampum, etc. Tax warrants.

M not valuable bcs reps gold, & people want gold. But bcs

M a great convenience, need something to serve as M.

Gold is vble largely bcs is a convenient M. But ~~any~~ grain

many things can be made convenient M, — then are

"good as gold"

Fns of M.

Medium of exch.

Is a med. bcs is a store of value. (Just as is convenient to store up grain to meet unpredictable demands, smooth out discrepancies of prod. & consmptn, so with M, grvlyzed pp. Avoid barter, double coincidence of wants)

Being medium, is also more. — of present & also deferred

Any store of value cd conceivably serve as M. But some more convenient.

Gold: advantages.
Stable (why?), portable, ^{Hi value in small bulk} durable, ^{no chemical touches it.} divisible, cognizable. But very soft.

Paper. (& minor coin)

1. More portable.
2. " durable - can destroy old, print new. But can burn etc.
3. " divisible - no cost, just make change
4. " cognizable (except counterfeitg. But that less problem than fake gold)
5. Less stable. Some say is advantage - doesn't fluctuate wildly, but in control of govt, while gold, insofar as does fluctuate, is beyond govt control - gold rush, new techm, Russ. dumpg.
_____ & govt can ΔM if need more
Other hand, can't always trust govt. Those who put faith in gold are those who think govt can't be trusted to manip. currency. - too much ΔM .

6. No real cost to ~~gold~~ paper. Immense cost of producing gold. Scarcity. ~~Gold~~ Paper, govt just says is legal tender & it is. good as gold

Again, some say is advantage. Keeps from depreciatg.
Q dets value. Gold, know Q won't Δ much.

Advantages of bank deposits over paper. (checking, not sav.)

More portable - e.g. send check by mail

" durable

" divisible

Less subject to theft & loss

Check is receipt

Get some int. on, sometimes.

Less safe. Banks bust. But insured up to \$10,000

Variable. Not disadv. to individ., for as dep. vary, changes value of all M, incl. gold.

But to society. E.g. '30-33. RE loans, cumulation

→ Most imp M now

Advantages of gold:

1. Avoid inflation - limit. Q. (cd. also by lim. paper)

2. Internat. War chest. & Internat. M. + ~~the only~~

~~not only~~ Not only int. M: £ used to be, now \$ (wk'g for the Yankee \$)
£ still is: we have not seized our opp. 40% still in £.
Bcs convertible to gold, in part.

Int. M - if not the only int. medium, is prime int. measure.

~~nsam~~ 3. When govt breaks down, gold good. E.g. Eur., smuggling. Paper & bank dep.s based on faith.

What is g.s.? Are we on it? (gold coin, gold bullion, gold exch.)

Devaluation, mean anything?

Credit.

K & H love to classify. Don't sit down & memorize types - just use head.

Credit instruments — I.O.U.s, formalized. Often "negotiable": - i.e. payable to bearer, not just original lender.

"Commercial paper" — shrt tm. I.O.U.s — 90 days - 1 yr, owed by reputable borrower, ~~person~~ or endorsed by bank.

Banks esp. inv. in shrt tm comm. paper, bcs they must remain liquid, & shrt tm is nearly M — just 90 days from being M. & often passes as M itself.

9, Mon || ch. 15 optional

Review Price Index. $\frac{P_0}{P_0} + \frac{\Delta P}{P_0} = \frac{P_1}{P_0}$

Put on board accts of banks & F.R.

Position of gold - amplifier

Main tool: open mkt.

Potential expansion

	FR			Membr.
	a	L		
gold	22	88	→	60 300

& then cut res. req.

Minor fns of F.R.

Socialized banking. So why pay bankers?

Next: bus cycles. Then monetary policy & fiscal policy vs. them. Join sam. in favor of fiscal, emph. p.w., etc.

✓ **24D. MONETARY POLICY, 1955-56.** Hearings before the subcommittee on economic stabilization of the Joint Economic Committee, Congress of the United States (84th Cong., 2d sess.), pursuant to section 5 (a) of Public Law 304 (79th Cong.), December 10 and 11, 1956. 1957. 162 p. il.

Catalog No. Y 4.Ec 7:M 74/9

45¢

with the knowledge and skills to conduct large reeding operations in time of national emergencies created either by natural disaster or enemy attack. 1957. 190 p. il.

Catalog No. FCD 1.6/8:12-1

55¢

11D. DEALER GUIDE FOR FHA TITLE I LOANS. This publication describes in detail the proper methods for dealers and contractors throughout the country in handling FHA

$P_0 Q_0$ $P_1 Q_1$

147-49

N7

250

156

325

 $X \equiv \text{price index}$

$$X_1 = \frac{P_1}{P_0}$$

$$\frac{P_1 Q_1}{X_1} = \frac{P_1 Q_1}{\frac{P_1}{P_0}} = P_0 Q_1$$

Is dividing by X same as subtracting $\frac{\Delta P}{P_0}$ % of $P_1 Q_1$?

$$P_1 Q_1 - \left(\frac{P_1 - P_0}{P_0} \right) P_1 Q_1 = P_1 Q_1 - \frac{P_1^2 Q_1}{P_0} + P_1 Q_1$$

Evidently No.

Bes wd be taking % on wrong base. Suppose N_1 rose 20% & prices rose 20%. Now if we reduce Y_1 by 20% of Y_1 , takes it down to less than Y_0 .

Shd reduce it by 20% of Y_0 ?

$$P_1 Q_1 - \frac{P_1 - P_0}{P_0} P_0 Q_0 = P_1 Q_1 - \frac{P_1}{P_0} P_0 Q_0 + P_0 Q_0 = P_1 Q_1 - P_1 Q_0 + P_0 Q_0$$

Ass $Q_1 = Q_0$, this brings us back to $P_0 Q_0$.

But if ΔQ , n.g. ^{close, but not completely accurate} Bes then when subtract $\frac{\Delta P}{P_0} P_0 Q_0$ from $P_1 Q_1$, you are only adjusting for the higher P of Q_0 , & not acct'g for the P of ΔQ

Prices & money
What is infl-n? 2 defs.

Have assumed const. P . Now consider changes

How much? Indices $\frac{\Delta P_0 Q}{\Delta P} = \Delta Q$ i.e. ; $\frac{[P_0 + \Delta P] Q_1}{P_0 + \Delta P}$

Wt'g

CPI & UAW; parity; Dow-Jones ave.

~~Make any diff.~~ Make any diff. if all p change simul?

M holders, bonds, pensions, annuities, insurance, lenders.

Hurt banks?

Stepladder inc.s

Fixed inc.

P.U.

Hist. of P

Infl. in war, defl. postwar. Infl. bcs govt can't collect taxes, sources dry up.

Cause of ΔP , Δ spendg, ΔM . Is good. Infl. w/o full empl. bad.

Money. Sam. shows no connection, poorly org. chap. $MV = PT$. or
 $\Delta M \rightarrow \Delta Y$ & ΔC & ~~and~~ Δmpc , hence ΔY

Kinds of M .

Remember, explain what d.d. is before showing how banks ΔM .

Deposit Creation. Order of exposition. *Write on board.*

1. Depositors inject ~~cash~~ ^{currency}. D.d. is means of payment, warehouse receipt for ~~cash~~, ^{currency} goes out of existence.

2. Banker lends out currency. Depositors write checks, but just to each other, so currency never needed. M. is created.

(Fraud? Hoax? Once thought so. 1st goldsmiths probly thought they were gett'g away w. something. Can be hoax today.

But basically honest. ~~Bank~~ More honest than ins. co., which c'dn't meet all claims, is gambling w. stat. Banker can meet all, in time. Is just gambling w. time. Assets long term; liabilities demand.

3. Banker lends by creating new deposit. Cash never called for. Expand

3 1/2. Dep. write ^{deposits, currency} checks to ea. other. (in practice is a little of each 2 & 3)
4. Depositors write checks to other banks, but deposit checks on others. Clearing, evens out.

5. Net loss of deposits - bank liquidates some loans, carries on. Other banks build up deposits, expand loans.

6. System as whole. Like one big bank, all deposits stay in it. Start w. 100% reserves. Expand indef. Bank swaps IOUs w. borrowers. Banks' IOU goes to depositor

$$\begin{array}{r}
 12 \overline{) 366.66} \\
 \underline{4,400.} \\
 36 \\
 \underline{80} \\
 72 \\
 \underline{8}
 \end{array}$$

$$\begin{array}{r}
 75 \\
 16 \\
 \hline
 59
 \end{array}$$

who is then real lender.

What is "behind" bank d.d.? I.O.U.s of borrowers, in return for which d.d. were orig. created. Or currency, d-o. (but no specific backg for any deposit) Or original cap. & surplus of owners, & assets bought w. bonds (or do banks issue bonds?)

Real lenders are dep.s. Why pay int. to bank?

are you lendg when hold currency? To whom?

Bank is agency for liquidatg debt. M. is liquid debt.
Used to print bank notes

D.d. is I.O.U., passes for M. Behind it is mainly other I.O.U.

6. Instability, potential

Unstable system. Ok in good times, but in a crisis breaks down. Bcs I.O.U.s to banks, ~~are pay~~ standg behind M, are to be paid in — Money! Completely circular system, when viewed as whole.

Any one bank, to be sure, can liquidate, get M from others. Just as any one bank, expandg, seems only to lend out dep.s M, not create M. But system as whole creates a means of payment, that has to be accepted for its own sake, can't be turned into currency quickly

Ok as long as debts good. They turn bad, liquidity press, more turn bad, liquidity panic, all collapses.

7. Control of System

Such unstable system needs control

a. Public control — i. by withdrawing M. Xmas. Need for reserves.
 ii. By inv. opp - willingness to pay int.

b. Govt control

1. Res. req. The reserve bank keeps for own needs may not be enough for social needs, meet runs. So ~~the~~ res. req. Curb temptation to sail too close. (Must keep work's reserves on top of req. res.)

2. Amt of res. Then F.R., in conj. w. public decisions
 Draw 2 ^{T-acc'ts} together.

F.R. assets det. Notes & Dep.

A. Gold

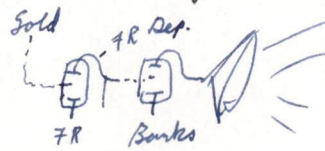
B. { ^{lend to banks} Rediscount

C. { ^{lend to govt} Open Mkt. }

Not "cash". FR has res. req. too, 25%.
 Radio amplifier system.

3. Selective ~~Direct~~ Controls

Instalment
 Stock mngns



c. Inv. opp.

To prt. bus.

To govt. bonds.

Treas. control — build up deposits at fed., draw down member reserves. Now, reducing deposits to stimulate, lower i. Can do only so much this way. Frustrated.

FR, ~~Western~~ System.

12 FR banks (57 for us)

Banker's banks. Like city banks used to be. Only Fed is in no danger of going dry in panic - make system safe. Lend to members in emergencies, & com. & dep. almost w/o limit.

Bd of Govns. Martin. 7 members, Pres US appts, 14 yr tms. - long, hence often fights
Great power - no strict ratio to gold. 25% } Treas. - e.g. Snyder vs
Hi i.a. McCabe
min, but now at nearer 50%.

Major Fns:

- Powers:
- a. Detmn FR M. By chng'g redisc. rate; & open mkt lendg.
 - b. " member res. req. Between 3, 7, 10, 13, to twice that.
 - c. Direct controls - mgn req., stocks.
instalment credit down payment req.

Both are just directly forbidd'g 2 specific kinds of loans.

Minor fns - pretty imp.

- ✓ 1. Members keep res.s as dep. w Fed - so no fudg'g.
2. Supervise banks - examine, for soundness.
3. Clear'g. - cancell'g checks vs each other. Interv^{district} regional.
- ✓ 4. Fiscal agent for govt. - i.e. govt keeps its M + here, thus favor'g no prvt bank.
- ✓ 5. Makes elastic supply of FR notes, to meet demand.

7, (cont)

Position of gold

Radio amplifier, 3 stage. Like Judo - control large wt. w. small.

Gold is 'cash' to Fed. 25% res. req.

Does gold really control? 2 schools of thought.

Used to - int. g.s. Now, control amplification, thru open mkt. Like volume control on radio. This gives national control of M. Is used as instrument of nat. policy. '30s, sterilized golden avalanche. '40s, expanded w/o Agold.

(Paradox: strong "g.s." men often vs. "internationalists" - but g.s. is int-l control of M supply)

~~Change over~~

a		L	
Now,	Gold 22	Reps	21
		Notes	26
			<hr/> 47

Actual res., $\frac{22}{47} = 46 + 90$

Res req. 25%

Potential expansion, $n \& d = \frac{1}{4} \times 22 = \$88b$, of which dep. = $\frac{21}{47} \times 88 = \$39b$
 say dep = \$40b. On these reserves, banks cd hv d.d. = $5 \times 40 = \$200b$
 (at 20%. Mention loose control)

Now, d.d. = c. ~~\$80~~^{\$90}b. Room for great expansion.

& if get to 25%, simple act of cong. lowers. M-make's machine all set any time to go.

Socialize banks? When country goes socialist, banks first. Vital speeches, Apr. (?) 1955

FDIC collects a surplus, stands ready to help those that fail. Fund might run out — fact of being insured may encourage lax banking.

1. But behind that is "boundless emergency monetary powers" of gov't. Since '35, can monetize all kinds of bank assets.

2. Besides, most assets are ^{Fed.} gov't sec.

3. So gov't regulates banks' investments

provides basic check clearing services, interdistrict.

4. Sat., 9.

Stands ready to ~~take~~ monetize their assets in emergency.

Is their main customer & income source

5. ——— Protects them from comp'n (FDIC saturation policy)

6. ——— Insures their loans

7. ——— " " deposits.

8. ——— Tries to regulate total M — banks' indep. merely hinders.

So what is a pvt banker good for? To ration credit.

~~To him that hath.~~

But then gov't comes along & says banks are mis-allocating credit, sets up special agencies to lend to those whom bankers pass by. For all credit rationing amounts to is following rules examiners lay down. To him that hath...

One good feature: pvt lenders collect their debts — loans aren't just giveaways.

& they do clear checks, US just supplies interdistrict service

~~c. Selective controls~~

~~Stock margins (read Gubraith)~~

~~Comm. credit~~

Use as preview for cycles.

~~Insert spiel on why not socialize banks?~~

3. Evolution of bank assets — 3d thing affecting AM, most imp. tnt.

a. Comm. loans Cycle. We begin story w. comm. loan thy. But go back to wildcats, find opposite. -- c.l. thy. a reaction to previous land booms

Preview:
b. Fm. banks
in mtggs.

Farm boom & bust, preview of things to come. 1920 boom load up on inventories, but only a brief problem to liquidate — comm. & loan thy ok. Mortgages N.E. — fm banks bust, '20s.

c. Decline of
comm. loan

City banks. Mergers, self-financing. Decline of comm. & loan. Turned to long-term: land boom.

d. Growth of
n.e. &
stock loans

'26, preview --- reserves rush in & out of Fla., as collateral falls.

Shaky banks look for way out. Stocks. Mgn loans, call loans, hi i.r., good collateral, etc

e. Collapse

Gubraith on '29. Fisher, Bogart, Hoover

$\frac{1}{2}$ deposits destroyed.
Why didn't F.R. save?

Fri, 10/8/11, p. 3

Reform legislat: FDIC, Banking Acts
 ... money no spec.

f. Excess reserves

Sam's unfair criticism of ΔM . It was only FR who ΔM .
So? What happened to d.d.? Check Bernis hist. stat.

Late '30s, sell govt bonds to banks.

g. U.S. govt,
new customer.

War " " " " , & to FR.

h. ^{u.s.} Debt mgmt
& banks

Postwar, farce of support; bond mkt 'to help bond holders'.
(except banks, did help them)

1951 compact, Δ i. r. The, "replace infl." - then -Δ i. r.?

Further infl. w/o Δ Nat. debt. ... monetize it. Banks don't fear inflation

Thus banks can ΔM . Now, what det. how much they create?

- available reserves (effect of cash withdrawals?)
- Res. Reg.
- Inv. opp.

✓ Hi risk of banking.

When an area was booming, then ceases to, a, some assets go sour
b, Depositors pull out. Combination ruins. Thus put
banking & traditional Am. land booms incompatible.

Legal res. for FR Member Banks, 1951:

24	20	14	d.d.
6	6	6	b.d.

How make banks safe? Som. dubious about res. reg. - needless waste in good times, no help in crisis.

Successive steps:

- Bank reg. (1907 panic ensued)
- FR system (1929 ensued)
- FDIC

(Govt loan guarantees, too.)

Will it work? No doubt, until govt breaks faith. How? Infl.
Of course, FDIC is not a govt guarantee of bank dep.s.

Refute Bern's idea of small banking? Tote up % assets of a few large ones.

Lecture on changing composition of bank assets. Commercial loan theory
Am't of reserves; & of deposits.

10 min. quiz:

~~Give~~ 9 give ^{Wts 8} ~~with~~ ΔP , 4 comm. They construct P index. over

Bach ch 6 on price levels.

Talks of importance of defining infl., but fails to define it.

Give 3 defs:

ask qns

ΔP (only occur after "full empl."? - no, demand)

ΔM (suppressed infl. S & D, rpt) (Note this brings prosperity. (of ΔP rising autonomously))

Δ spend'g.

P infl. How measure? P index.

a Weight's - show technique. Bach, p. 89

b. What do w. index? Divide by it. $\frac{\$1}{2.0} = 50\%$

When "inflation", you "deflate" the \$.

~~maximally, $M = PQ$~~
"Deflating."
in genl, true value of \$ is what it will buy.

c. anomalies in weight's.

Change's volumes of purchases

New goods

Obsolete goods

When p rises, inelast. demand, higher % is spent on item, weight rises

Lower p may indicate less demand, for food, hence no Δ welfare. Or lower cost of supply.

" " together w. ΔQ is good. If ΔQ , means little.

Solution? Beware intertemporal & interregional c'sens. E.g. lower cost of liv'g in south. Cf to Calif. "Parity" - continuous conflict over

components & wt's, ~~so~~ so "rigid" P supports not rigid. CP & UAW wage.

Output is PQ . If want Q alone, divide by P . Or if want changes in Q alone, divide by changes in P

Impact of ΔP .

Bach's g'ml'g's some dubious, due to other causes, pp 93-8.

~~Gainers~~ Losers:

Bach p. 98 { Creditors (except less delinquency)
M holders
Fixed inc.

Stepladder inc.: T.T.C.

P.U.? Greater vol. offsets loss.

	1950	1956	W+	Relative	W x R
a	3.26	3.26	.10	1.00	.10
b	.01	.02	.70	2.00	1.40
c	53.00	31.00	.05	.58	.029
d	9.28	6.50	.15	.70	.105
			<u>1.00</u>		<u>1.634</u>

$$\begin{array}{r}
 .58 \\
 \times .05 \\
 \hline
 53 \overline{) 31.0} \\
 \underline{318} \\
 265 \\
 \underline{265} \\
 450 \\
 \underline{427}
 \end{array}$$

$$\begin{array}{r}
 .7 \\
 928 \overline{) 650.0} \\
 \underline{6496} \\
 40
 \end{array}$$

$$\begin{array}{r}
 .58 \\
 .05 \\
 \hline
 .0290
 \end{array}$$

~~Def.~~ Gainers:

Debtors (recall big ones. Bach p. 98. Note middlemen $\frac{1}{2}$ - " $\frac{1}{2}$ gainers")

Current producers - bcs others get less of pie. Stimulates output

Holders of real assets - same reason. Stimulates inv-t.

Buyers of fixed p. services. Employers. Users of p.u.

Everyone? Not from ΔP , but ΔMV that caused it.

Beyond this can't say. Firms? Not now.

Labor? Other factors pushed up wages. in war

Mon. Risk

Said entrep. takes risk. See what it is.

1. Some risks predictable, by actuarial ~~risk~~ tables. ~~By insurance~~, laws of probability. Insure vs them. Convert the risk into an annual cost. Probability of loss is less than ins. cost — otherwise ins. co. edn't pay expenses. Just as at Reno, probability of loss > gain, so pay expenses. (Now why will man insure home etc, pay ins. co. expenses, to avoid gambling; then go to Reno, pay costs, for pleasure of gambling?)
2. Other kinds of risk can't predict. Notably price risk. Also, entering any new field, no past experience, don't know what costs will turn out to be. Nor, of course, demand. So far as I know, is no one who insures vs that directly.

Ways of avoiding it.

- a. Hedging (bund p.s for ag.)
- (b. Find inst.; inv. trust; diversify -- giant corps) ^{conc.} Tax policy (Lender's & borrower's risk. Min. risk by lend'g to rich corp. Bank's - turning solid assets to liquid.) Other hands, some prefer risk.

a. Hedging.

Best ~~never~~ job of hedg'g I ever heard, Robinson-Turpin...

✓ Not usually that good a deal. Just arrange to avoid gambling. Bet vs self.

Why avoid it? After all, might win as well as lose. Answer is, to specialize. Spec'g successfully is an intricate art, & if you're going to mnge a ~~plant~~ ^{warehouse} successfully, better cut it out.

I found that out a few yrs ago — decided a

ec-st shd hv some experience spec'g, so took it up. Vacant lot, various stocks. Well, when you have life savings rid'g on some spec, pretty hard to conc. on anything else . . .

Finally cut it out. Ok for later yrs, but not for when try'g to write, or anyth'g creative.

Not everyone wants to avoid gambli'g, so not everyone hedges.

Hedg'g: not near so complic to understand as you'd think from rd'g K&H. But never saw good expl. yet.

✓ Main idea just this: you ~~carry~~ are in a bus. where yr main fn. is to create time utilities - carry over, store goods from hrst time, when cheap, to winter, when dearer. Want to specialize, conc. on work of storage, not stay up nites worry'g about ~~the~~ const. fluctuations of mkt.

✓ When buy, also sell - sell future. ^(promise to deliver. known as s-g short)
That means of course someone else promises to buy
Sell future for more than cost you today, to cover your costs of storage, int, etc.

✓ Very simple. Guaranteed future P. ^{When} But one complication, makes it hard to understand. Fn of storage not just to hold over grain from 1 fixed time to ~~the~~ another. Rather, to be

(Must be standardized - why?)

ready to meet unpredictable changes in demand. Don't know when you'll be called on to deliver.

So our elevator man, who is hedged, has a guaranteed mkt in Dec., if he wants to wait that long, or has to.

But he also has another gimmick. He doesn't have to deliver the exact grain in his warehouse in Dec. He can sell that earlier, if gets a good chance. Normally he does so.

That leaves him with no wheat, but an obligation to deliver in Dec. at the guaranteed fwd. price. - his shortsale contract.

(That sht sale contract will acquire either a + or - value, depending on whether grain ~~went up or down~~ down or up.) If went down, acquires + value - thus offsetting loss he took on grain. ~~If went up, loss~~ Then he sells it, cancelling loss.

Other hand, if grain rose, he makes extra profit ~~on~~ on selling it, but his shtsale contract acquires neg. value

Can't sell that neg. value. Might pay someone to take it.

More often, just keeps it & takes his loss on delivery date - offsetting his spec. gain.

One final complication: to avoid spec'g during interval

from sell'g grain to deliver'g on his hedge, he buys long, for
delivery on hedge^{delivery} date.

Proposed "fwd p. for agr." ~~the~~ Will know what that is when see it, issue in
politics.

Innumerable possible complications & combinations — just gives
idea. what hedg'g about.

To what lengths. people go to avoid risk. -- some people, i.e., —
other people court it. For hedg'g doesn't ^{elim.} ~~decrease~~ risk —
just shifts it from those who don't want it to those who do.

~~When buy~~

In bus. where carry big inv., p risk, want to avoid.

So when buy, also sell - sell future - promise to deliver at specific future date, at prearranged price. ^{sell short.} Means someone promises to buy. So you're safe - guaranteed future p. - will be high enough to cover yr costs.

Simple? Yes, unless you sell early. Then left hanging, with promise to deliver, risky. So buy long, to offset, ok. (Which wd do if relation of spot & future p was such as to make it profitable - spot went up, or future down)

Many possible combos.

—
Great distrust of commodity mkt, suspicion.

Due to misunderstanding - what we misunderstand we fear; what fear, hate.

So now Congress investigating coffee futures mkt.

Not bcs they don't understand it. Spec. in futures mkt is favorite indoor sport w. Congress. (why? inside info)

~~the~~ Favored scapegoat, time-honored.

Coffee hi bcs Brazilians hv. bn restricting output for yrs - tax on coffee bushes. But we can't put finger on that, sounds too much like what we do ourselves. So pick on futures.

Maybe some day grow up.

? How important is hedg^g in ec? (not very. Requires standard comm, so you can guarantee to deliver a certain grade. Organized futures mkt - Chi. bd. of trade) (most raw materials - -

So most imp. thing to remember re hedg^g is it ~~the~~ shows to what ^{some} lengths people will go to avoid risk; & how those who want risk & those who don't may come to terms, so each gets what he wants, & is mutual benefit. (ownership utility)

(& of course if you ever go in for spec. on commodity mkt^s, as so many of our congressmen seem to, you'll need to know about hedg^g.)

Take p risks on only raw comm.s? No, on every asset. Esp. fixed assets.

Further ways to minimize risk. (After hedg'g)

1. Never borrow. to buy assets. Borrower takes biggest risks. - must meet payments.
2. Insure - pool risks. But limited.
- ~~3. Lend to someone or corp. w. assets to mortgage.~~
3. Diversify
 - a. Individ. can't do it much, unless very rich. - Hearst. Besides, lose efficiency, spread all over map.
 - b. Incl inst.s.

Chase

i. Bank. - ask how.

(Introduce ΔM -- does bank just lend the M you put in?

ii. Others? Ins. co. Bldg & loan

iii. Corp. - is a fin. inst. Invest in op. corp. with finger in many pies.

Or an inv. trust, ^{what is?} hold'g many corps.

Or a h.c. - define?

Investors preferred them, hence can form them & sell stock for more than sum of values of stock of constituent co.s. - whole = > sum of its parts

4. So far hv just been speak'g of 1 kind of risk -- "productive"

risk. Is also "lender's" risk - that borrower may prove a deadbeat, & welsh out on you. Minimize 2d by

lend'g to rich, ^{rich corps -- how lend to corp?} Or mix'g your assets w. rich & powerful men, buy'g stock in ^{rich} ~~rich~~ corps.

5. Lend to people or corps so famous that you can get someone else to take the loan off your hands easily. -- negotiable sec. Again, that means big corps.

You may think some small local enterprise is just as good a risk as SP. In fact, if you've ever been frightened by SP, esp. anything fragile, you may think the local enterprise better.

But SP sec. negotiable - listed on NY SE, ~~etc~~, worldwide rep. & millions of acres of land as ~~etc~~ collateral - can always sell.

So lend to SP.

→
~~The~~ So if understand this little problem of risk, are in a fair way to understand final structure of ec.; reasons why final power so uneven, so conc.; & hence why productive assets, esp. nat. resources, are becoming so conc.

Tax policy & risk - can deduct losses only if have other inc, encourages bizness.

Cap. gains tax. ^{loophole} - encourages small to sell to big, take inc. as cap. gain

Fincl inst.s:

Banks; ~~Mer~~ Comm. - check'g accts, AM; Savings. (Most think of all as sav.s)

Inv. banks - keep eye on, for are nerve centers of ec. control. Wall St, J.P. Morgan.

Underwriting - buy corp stock, peddle it to final holders. Fincl middlemen.

Also imp. as engineers of big mergers, architects of money - K & H.
don't tell you that, but just ~~what~~ 3 fns: invest'g, underwrite, sale.
129, Black eyes. - Krenner & Toll. No subst. for final buyer being

wary.

Inv. Trusts. Spread risk

Corp. -- many a giant h.c. is ~~an~~ an inv. trust.

If a bank lends, in cash,
does that create ~~cash~~ money?

The cash was previously idle in
the bank. - an interbank
obligation.

From one view, when someone
puts currency in bank, gets a
deposit, that destroys the
currency: the bank immediately
turns it in to FR, its deposits
move up.

So that destroys
nothing - unless you say interbank
deposits are not cash, or money
which say.

Over

So here is valid terminology:

If put M in comm. bank, the M goes out of circ. - is in effect destroyed, as far as being part of M supply goes.

In return, create a deposit which is Money. Net effect zero: transfer from 1 kind of M to another.

Then When bank lends, "creates" M . -
Whether lends cash, or creates d.d.

FR system controls
amt of reserves. Reserves
are FR deposits held by banks.

Public demand controls how
much cash is outstanding - outside
banks. That is not reserves.

Till money is not reserves.

And if public puts cash in
banks, bank sends excess to
Fed, it becomes a deposit.

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Is credit rationing
consistent with equingrl
principle.

How banks reduce dep. obligations?

1. Borrower pays in dd of bank
- ~~2. " " " " " " another bank~~
2. Depositor demands cash.
 - a. Borrower may.
 - b. " writes check to someone who keeps acct in another bank, your bank must pay other
 - c. Recipient of check cashes it.
3. Bank "liquidates." - goes out of business. (Russ. expression)
Ordinarily banks don't like to lose depts, try to attract, expand.

~~skip~~

4. Why can't bank Δ cash w/o limit by Δ g deposits? Because can't Δ own ^{depositors} ~~deposits~~ by creat'g d.d. - they all flow out, long run. Must attract dep-ns other ways - good service.
- Or, if it can, then must have income to service them, so can't sell all TOLs for cash.

Any limit?

Yes, can't go on writing IOUs forever, someone will cash them.

Bank goes on so long as those who get the IOUs keep them in the bank -- borrower writes check to another one who keeps funds in same bank, etc.

& as long as community needs IOUs as M, will.

But some who get IOUs will cash. Or move to another bank. Banker must have cash for them.

Other hand, he will get cash from new depositors

For system as whole, - regard'g it as one big bank -
What limits expansion is amt of ~~cash~~ currency - govt currency.
Public keeps a certain amt out of banks.

As ~~if~~ banks expand dep.s, more & more currency flows out to public, (as ΔP & need more cash) & have more deposits than want. (& may ΔP , Δ need for cash)

~~Now in if~~

Too, banks finda selves w lower & lower ^{currency} ~~cash~~ reserves.

Why need reserves? Bank in tenuous position:
legally & morally obliged to pay currency on demand to all depositors at once. But com't. - has to have assets out earning, to make bank's pay. So every commercial

(over)

cd. you have a bank w 100% res? No inq? H: charges.

bank unable to meet oblig.s.

But experience shown can get by w certain reserves for contingencies — 5, 10%. Get below that, trouble —

maybe 1 day, suspend payments, lose confidence, you're thru.

Mon.

K & H said trouble w banks, tried to make too much profit, what mean? Too small reserves.

What if bank folds, just those reserves available to pay?

— i.e. are bank's dd. "backed" by anything besides 5% res of currency
Bank loans, + cap., + double liab. to '37, & insurance since.

skip,

Fri.

So banks limit dd to some multiple of ~~cash~~ currency reserves.

Pvt. caution reinforced by law, U.S. (but law unnec. Eng, Switz, no legal res.)

Now this need for res.s explains how govt can control, as const. requires. By regulat'g cash, res. req., puts upper limit on how far banks can ΔM .

Limits to govt's control

Distrib. of currency. Some may hoard — sinkholes.

Mon. ✓

Or dishoard. Unpredictably. Large multiple effects.

Loss of confidence, ^{system works on trust, confidence.} snowballing, bank panics, — ΔM .

Govt. controls max, not min. Can't force ΔM by Δ g reserves. '30s, excess reserves, no bank expansion.

New pts, Fri.

1. all ΔM from bank expansion comes from new loans.

If put M in, destroys the M

" take " out, creates " "

Mon. 2. Nat. bank system

Interbank dep.s counted as reserves. Pyramided toward a top
few. Thus, if 5% "reserves" held, meant only $1\frac{1}{2}\%$ real
res.s in bank system.

Mon. 3. Banks need to hold & attract depositors.
Hate to see M leave town, esp.

4. Interbank clearing.

Works on trust, confidence.

Central bank.

"cash" Reserves of comm. banks aren't ^{alone} cash, but ^{also} deposits at center.

C.B., by controlling amt of its dep.s, thus controls max of all dep.s.

In practice, too, c.b. ~~dep~~ can Δ dep.s & notes up to 90% of gold.

Basic c.b. reserves are gold. FR must have 25% res. for gold &

deposits. So new \$1 gold comes in, can Δ FR by what?

\$4: - \$1 to pay for gold, & \$3. more, can lend to comm. banks, or to

govt. & thus put in circ.

→ Role of gold, internat. Multiply effects, control mechanism.

120, 30,000 comm. banks

150 15,000

9,000 state. 5,000 Nat.

Evolution. Landmarks. 1863

1914.

Before '63, state banks. Issued notes - states cdn't, but states cd charter banks that cd, borrow of them, pay bills w notes, never redeem.

Not always so wild as K&H make out. ^{much self-reg & state reg.} But can wild in big land booms. But banks still do. - will again?

Nat. Bank'g.

Taxed state bank notes out of existence. Double liability (dropped in

'33). Min. cap. req. No n.e. loans. Reserves req.

Man. Weakness of Pre FR banking: country banks kept reserves as deposits w big city banks. Big city banks didn't keep adequate reserves for crises — ok for other times.

1 step further: How govt controls amt of letture.

"Currency" - what mean?

Green stuff. - letture.

also d.d. of c.b. - FR.

Green stuff is just bank note of FR. dd of FR much same, but don't see it. Both same - arise from loans of FR, (it lends to govt & banks), 25% gold res.

C.B., by controll'g amt of its notes & dep's, controls all d.d.

How?

What controls notes & deposits of c.b.? - said gold, but only part of story. We're narrowing this down now, getting to focus of control.

Common in ec. - e.g. cruise timberland, wonder why one hold'g of 1,000s of acres & millions of bd-ft is treated diff. from another, probly won't find answer out in woods. Some little office, 25th floor Chase Nat. Bank bldg NY, wizened, hunchback accountant writing figures in bank ledger, ~~determines~~ ^{decides} flow of credit that ~~the~~ determines practises on 1,000s of acres. That's what ec. is, goes back to foci of control, & power. -- intricate

Mon.

What K & H mean, banks tried make too much profit?

(Too small reserves. Expanded to hilt in pd. of public confidence
Had to suspend payments when changed. Esp. central city banks.

Hence ^{name} FR — to hold reserves of banks, be able to deliver
in emergency. Not strained to limit of res.s all time, able
to expand in pinch.

When FR?

Any bank panic thereafter?

Why didn't FR save?

(Power limited to helping liquidate assets. Assuming
banks are fundamentally solvent. long run.

But weren't. Bad loans.

How come about? Decline of comm. loan. Time
FR conceived, most bank loans "comm" — shd tm, to
businesses, self-liquidating.

'20s, mergers, giant corps took over much bus.,
& were self-financed, internally. No outlet for bank
loans.

So banks went into r.e. — booming that time.

Took mortgage collat. Not self-liquid. & long tm.

Not fit asset to back d.d. — but public unaware, all caught up
in madness of times, thought nothing so liquid as r.e. & stocks.

also loaned to people to buy stocks. - took stock as collateral.

Stocks &c. crashed. ^{Loans went sour.} Cumulatively, as foreclosers thru on mkt to collect.

Bank liabilities > assets - long run. Public found out, runs, etc.

FR not ready to meet that.

What wd. happen today if banks bust?

(FDIC)

How does FR ΔM ?

1. Buying gold.

(Basically by Δ loans & inv.

Dist. redisc. & open mkt op. ns. Open mkt is lend'g to govt; redisc., to banks.

(also, by $-\Delta$ req. res.) Rarely, lends direct - not good, public agency.

That is major fn.

✓ of minor fns., remember 2:

1. Members keep res.s there - no fudg'g

2. Elastic currency - original purpose of FR bank, evolved.

Mon.

Govt debt & M

What's "deficit finance".

Effect of govt borrow'g on M supply. Is borrow'g infl?

How might it be?

Distinguish "pump-priming" from "monetizing debt"

Show assets & liabilities of banks.

Do reserves limit? Govt just sells to FR, too.

Does gold res. limit FR? Used to be 40 & 3590, came up
vs limit toward '45, Congress lowered to 25%.

What else might do? Devalue further.

139 - 46, curr. & d'd, \$356 - \$1106. Infl.

During war, managed to raise c. 4190 by taxes,	
3590 .. borrow'g exist'g M	
	(sav. bonds)
2390 .. M creation.	

Now is that end of problem? Is debt creation in
danger of caus'g infl. only when debt Δ 's?

Continual problem of debt mgmt - refund'g. Always
com'g due.

No assurance that hold'g public will buy new ones.

Hi bond $p = \text{low}$ i.e.

explain in class.

Bond ~~pay~~ matures in 10 yrs.
also pays int. along the way.

Present value of future value
is $\frac{1}{(1+i)^n}$. If Δi , present value
falls.

When sell bonds, are selling
promise to pay in future. If
i.e. h_i , must sell for low price
today.

Seems miracle to me, w danger of infl, Treas. can
still convince people to buy. Stung once

~~146-51, FR~~

So if not, must sell to banks - monetize. Banks don't fear
infl - M on both sides bal. sheet.

Some hist.

146-51, FR the captive of Treas.

Treas wants:

Min. int. Sell to h. bidder - low i.r.

Protect war holders.

Hence has FR support mkt. Buy bonds, thus supporting
directly, & what else?

Gov's want:

Stop infl.

No favor to bondholders if infl.

146-51, FR did what treas. wanted. Then compact.

Then Eis.

(5) Best exposition.

1. Banker sets up shop, gets deposits, of cash. But doesn't keep 100% cash behind them, lends some out. (at first he can lend all out, bcs has cash reserve of original capital) At 1st can lend out cap, if wish. But object^{is} to attract depositors, so can lend out their money, make a profit on it — incl. middlemen, using original pile of M to attract more M , like corp. selling bonds. Use that original cap. ^{too,} to get good location, nice bldg. attract depositors. (used to attract them by pay'g int. — but now outlawed, thus advantaging big old banks w good locations)

So from viewpoint of banker, he just lends out his depositors

the money

(Except in old bank note days. They weren't same as d.d. For d.d. goes to another bank, which demands cash. Bank note stays in people's pockets. So bank notes can be wider than d.d. expansion)

2. Thus he creates deposits, as good as M ; & also returns the M to circulation, or 80% of it. Thus he takes \$20 from circ. to create \$100 of deposits.

~~Needn't follow thru multiple expansion as inf. series~~

Don't take multiple expansion inf. series too literally — shows you what can happen. Actually, is rare that reserves shows you that if M moves into one bank, gradually will spread out among several, & banking system as a whole can expand to c. 5 times (or more).

(Actually, inv. opps are a more critical variable)

What good does that do borrower? Bank's IOU negotiable. —

pays it out for goods. Have exchanged IOUs, but of different quality —
different risk, ^{negotiability.} hence one called borrower, other lender. And one pays int. to other.

Now who has loaned to whom? Borrower spends M,
gets goods. Who really lends?

Then why pay int. to bank?

(Bank provides service to holder of dd that is = of int. —
an implicit int., called "liquidity".

Hard work to create it — clearing checks main
cost, putting up original nucleus of cap., bldg, ~~and~~ ^{may}
creat'g mystic aura of prestige & respectability, insur'g vs
robberies, xfer'g guard'g funds, etc etc.

But banks overdo it, service charges — when start charg'g
you for privilege of lend'g M to others, too far.

B & B mak'g M. But will finally sell out, cap gains, I'll use
M orders.

By way, what mean "buy paper" — Reg-Grand?

Deposit exp.

Despite K&H, int.

1. Comm-bks ^{savings} ~~middle class~~ banks. ??

Diff. way to attract funds: int.-t, vs liquidity.

Which kind creates M?

apply = mgmt.

2. How ΔM ?

~~Am't~~ What's "a deposit". Am't bank owes you

How get?

a. Put M in.

b. Borrow

c. Receive check from depositor

ΔM when borrow - from comm. Not sav. (maybe under 1 roof)

3. Used to print & give bank notes

Hypothetical.

4. Suppose comm. needs M. Get prominent citizens.

2 exchange I.O.U.s - will redeem in goods. Negotiable

5. Real. People don't just write I.O.U.s for community service.

But arise natch, when want to borrow.

Borrower writes his I.O.U., gives to lender. Lender gives M. Or, if lender is comm. bank, gives what? Bank's

I.O.U. - d.d.

(OVER)

Gold. Originally valuable for own sake, hence good M.

But soon, greatest demand was for monetary use. Bes it had 5 qualities, gained universal acceptability — exchanges for goods readily.

~~Money not v~~

But paper can have that too. If ~~made~~ properly reg. by responsible govt, that actively ferrets out competitors. — counterfeiters. — Mn. 880.

Thus gains stability, etc — & thus acceptability & that's ~~what~~ gold has.
 _{all} legal tender helps

~~For gold not value~~

✓ Money not valuable bes has gold behind it. Gold ^{itself} is only valuable bes a convenient money, & widely acceptable as such.  Anything else w. qualities mak'g it acceptable is good as gold.

✓ So paper M. Since '33 non-convertible. Still good as ever. Why? ...

✓ 3d M is d.d. Put yr M in bank. Hereafter pay by check, get paid so. 90%

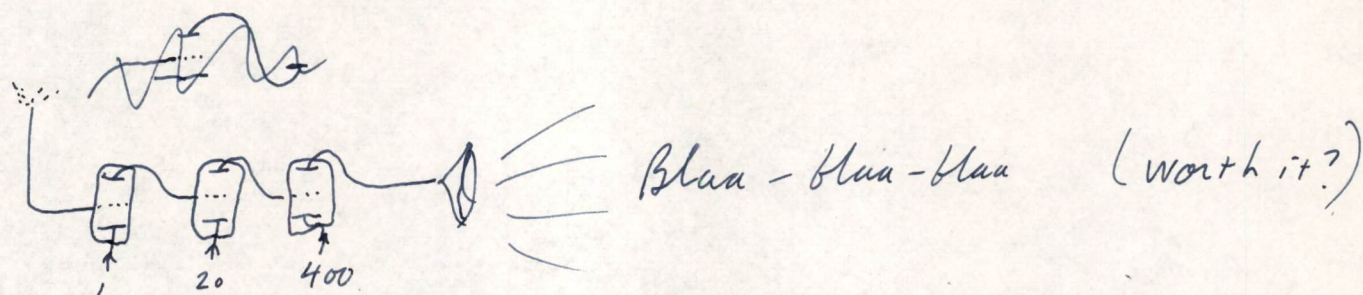
More convenient.
~~Some think~~ ~~MM.~~

D.d. replace paper? No, are in addition. You put M

machinations of high finance.

Or think of it like Judo — use a small weight w
consummate skill, control a large one.

Or radio receiver. Take weak signal, ^{amplify,} let it control
whole apparatus:



Controlling focus, — matter of controversy. Natch, you & I
aren't only people who realize what control can exert
there. The citadel always changj hands — issue in every
election, tho not one most voters understand. But those who
contribute to campaigns do.

~~Japan~~ Used to be gold, pretty strictly. ^{35%}~~40%~~ res. req. for FR ^{depos}~~notes~~.
^{40%}~~45%~~ notes. Idea was to let gold flows determine M — internat. control, free
mkt. But control passed — ^{wanted nat. control of M.} convenience of Treas. in financj. ^{so} ^{more.}

one day in c. '45 casually dropped to 25%, that was that.

Cd. do it again. So in effect, now, control in hands of Treas. &

Govins of FRB. I.e., no longer signal coming in on antenna,
but can change ^{amplification} ~~volume~~ at will! — signal got too strong, threatened to blast us
out of room.

Now, have \$226 gold.

216 dep.s
266 notes (NOT available as reserves)

Discretion of FR governs - of course in conjunction w govt
adm. policy - determines how far go.

Printing presses ready, any time want to flood country w \$M,
no legal obstacle.

Now, FR creates M by

1. Buying gold. Biggest source. No revenue, true, but can
op. at loss, is supposed to, to
be sound.
 2. Lending M to govt
 3. " " " banks
 4. Rarely, lending direct.
- (~~5.~~ Gov't deposits funds there? No - that destroys M)

Cd \$M much more, at Govt's discretion. Lending. & by lowering res. req.
Blow roof off P. Now 226 gold, cd have \$88b n&d, instead of
47 as now. & on that base, c. ~~\$400b~~²⁰⁰ dd, instead of c. 80b as
now. Also cd. devalue again, lower res. req., etc.

Goes back to golden avalanche of '30s. - In policy, brought in
gold, sterilized in effect.

$$\begin{array}{r} .48 \\ 47 \overline{) 22.0} \\ \underline{188} \\ 320 \\ \end{array}$$

$$\begin{array}{r} 26 \overline{) 21} = \\ 47 \overline{) 21.0} \\ \underline{188} \\ 220 \\ \underline{188} \\ \end{array}$$

$$\begin{array}{r} 88 \\ .44 \\ \underline{352} \\ 352 \\ \underline{38.72} \end{array}$$

Are non-members subject to
FR instalment & stock margin
requirements? Yes. Even non banks
are, says AG Hart. $\therefore$ I infer all
banks are, too.

How ΔM ?

First, what is M ?

Gold? Used to be, used to pass by weight. Or in full-bodied coins. No more.

(Gold was convenient bcs

Recognizable - aqua regia, Mon in white suit

Portable - hi value in small compass

Divisible

Durable

Stable in value

These qualities made it a good M - still do.)

Gold coins had these advantages even more. ^{except stability.} Also made profit for sovereign: seigniorage.

ΔM by debasing coins.

Next step, dispense w metal,

Paper M

All seigniorage

Easy to ΔM .

All advantages of gold, except stability

Proved acceptable, hence good as gold -
that's all gold has

in bank, doesn't stay.

One bank.

a. Suppose ~~the~~ ^{def.} stays there (either by being inactive; or by checks going to others in this bank; or by other deposits coming in as this goes out)

Then need keep no M behind it. Lend all out again.

~~In fact if~~

b. Then what has happened? ΔM --- by swap I.O.U.s
Used to be bank notes.

Bank cd. just lend, w/o new deposits, if a, All depts came back to it. Or, b, other banks expanding simul.

in bank, doesn't stay there.

One bank

Cash 20	dd 100
you 80	

~~So banks operate~~

Bank cd even op. w/o any cash. If mny bank, no calls for M.

Exch. 9.0. U.S., one circulates as M.

System as whole, put in \$100 cash, all stays, allows \$400 more d.d.

Even govt M is now mainly only like bank dep. - bank note.

As to govt M, most is FR bank note. Before understand that, must understand ~~what~~ ~~how~~ how banks work.

Circulating I.O.U., ~~liquidated~~ ^{assets} made liquid.

1. a & I of whole bnk's system. ΔM by a. Receiving M
b. Lending
2. a & I of one bank. Receive dep's, lend out 80%.

Assets	Liab.

(bank notes, paper representation of d.d.)

✓ Legal reserves - (Unrec. in prop.; insufficient in adversity)
Are banks safe? Ins. co.s are even less safe in that potential liabilities exceed assets. But death rates are surer than psychology. Also, banks have power to create M - easy to lend, great temptation. Esp. in boom, when others are too.
Making banks safe

Bank reg - keep assets liquid; also, limit entry w. hi. cap. reg. paradox, money vs risk.

FDIC.

FRS.

Panic of 1907.

Fr's original: provide cash in hurry, for other assets.

'29 / France, why?

History of bank assets.

Fri, 10 & 11

1. Deposit expansion
2. F.R. controls
3. Evolution of bank assets - leads into bus. cycle.

1. See other sheets

2. F.R. controls

- a. Res. req.
- ✓ b. Limit of res.
- c. Direct, selective

a. Reg.

Vary from 7-10-13 to 14-20-26. F.R.B. discretion. Why diff. for diff. banks?

- ✓ b. Limit of res. s. F.R. deposits (no fudging to lesser degree, notes)
F.R. a unique bank: can expand, but need never pay cash: its notes & depts are cash.
1913, 2 theories, 2 controls

1. G.S.

Gold inflow, treas. sells such as it got to FRB, sold.
Internat. system. Tied us to world ec.

2. Comm. loan

Fed. rediscounts shrt tm. comm. paper for members. ~~imposed~~
To expand dep.s, lower rediscount rate. But keep only shrt. tm. comm-l loans behind M.

'20s et seq, evolved 3d method of expand'g reserves: F.R. buys govt bonds ~~directly~~ in "open mkt".

Other 2 remained. '30s, Δ gold. '40s, Δ govt bonds.

The pyramid of credit. (radio amplifiers)

Gold, \$226' ¹⁹⁵³ $\rightarrow$ { Notes, (234)
Dep. (16) $\rightarrow$ } 73
(Other, 50, not M)

Control used to be in the gold; now in open mkt; expand'g dep.s: cushion.

5. Banks do create M. Swap T.O.U. (Govt M is just T.O.U.)
Asset behind it is customer's T.O.U.

They don't just lend what is deposited — they create the dep., & it comes back to them, or to some bank.

D.D. not "near-money"

✓ All the individual banker does, or seems to, is lend out his depositor's money ... c. 80% of it. He loses most of this M — to other banks, which then have excess reserves & expand. But individ. banker never appears to be creating Money — he just invests what is intrusted to him, & keeps a cash reserve.

It might appear all he can thus do is somewhat less than double the M supply. But the 80% of M he loses goes to someone else's bank, etc.

Thus I have been wrong in part to say Sav & Loan Ass., etc., who pay on demand, can at most less than double M. They can do just what comm. banks do.

X Finally, 3d kind of M. Good old priv. enterprise, broke gov't
mppy. Bankers created most convenient means of payment —
checks. d.d. ^{define: bank's oblig.} 90%. Have all conveniences of gold, but moreso.

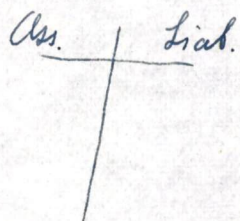
X & gov't has taken over bank's practice, so even lettuce is
now mostly bank notes.

But wait, you say, everybody knows those d.d. are
only good bcs they represent real M.

True — they aren't legal tender. But people accept
them, & deposit them to their accts, & no cash changes hands,
so they serve as M.

But can banks ΔM ? Suppose you put M in bank,
get d.d. $\Delta d.d.$, but $-\Delta M$. But now bank lends
the M out -- d.d. remains. ΔM .

✓ Or, suppose bank lends, & just creates d.d.



Keep some % assets in liquid form, thus stay safe.
Exchange I.O.U.s. Liquefy debt.