Assignment

MCQs

1. Correct option is c) Mutual savings banks
2. Correct option is b) provides with checking accounts and loans
3. Correct option is d) interest earned on their loans
4. Correct option is c) liabilities
5. Correct option is c) $9400

Questions

1. a) The main functions of a bank are accepting deposits, granting loans and transfer of funds. These services resemble the activities carried out by the families and individuals in the ancient civilizations.

b) The development of paper credit money in the seventeenth century by goldsmith bankers is incorporated into modern banking. Also some goldsmiths dealt in home and foreign coins. Then civil war interrupted the normal goldsmith business, so they managed to facilitate deposits of silver and gold safely and kept record of the deposits from depositors also. Goldsmiths also lent out the gold and silver to borrowers and created profits. To make up for the high demand of borrowing, they paid interests to the depositors and introduced fix deposits.

2. In the United States, there are the following three thrift institutions:

a) Commercial banks: these are the banks that make profits for their shareholders by acquiring deposits and then using them in different profit generating ventures.

b) Savings banks: these banks specialize I lending loans to individuals and families particularly for construction of houses and other buildings. Originally these banks only offered savings accounts and later dealt in DD and enable people and businesses to borrow money and also mortgages.

c) Credit Unions: Credit unions are groups shaped by individuals with a "**common bond**." By common we mean they work for the common organization, or share the common religious institution, or societal strata or being base in the same locality. They gather the money to form the deposits. Anyone can’t become a member of a credit union but those who share the common bond of the credit union. Credit unions are not for profit organizations but they enable savings and make the availability of money for the members at minimal costs. Credit unions aren’t bound to pay taxes and may get subsidized as in availability of space etc.

3. If a bank had to keep all of its deposits I the reserves, then the bank won’t be able to lend out any loans and will not make profits. In this way, the banks will not be able to affect the money supply in the economy. The money will not circulate and will not be able to earn more money.

4. a) A banks loan creates money as the bank lends out loan, it doesn’t hand over the loan amount to the borrower, rather it credits his/her account with the amount of the loan. Now the borrower has to pay back the principal amount and the additional interest on the loan. In this way, more money is created by lending out loans.

b) The extent to which bank can create money is limited by these two b/c firstly, a bank cannot lend money that it doesn’t have. A bank needs to have the amount of money that it wants to lend out as deposits. Secondly, the reserve ration requires the bank to reserve a certain amount of money with the central bank. This is the amount of money that the bank can’t invest or lend out. So inability of the bank to invest and lend out hinders it from creating more money through interest earnings.

c) The amount to which the deposits can be expanded can be found out by the following formula.

ADD= AER/ r,

Where AER is the excess reserves I the banking system and “r” denotes the require reserves ratio. So the money that banks lend out circulates through the economy and creates more money.