**Syllabus CEU SPP & ECOBUS**

**Money, Banking, Central Banking, Monetary Policy**

**Instructor:** Lajos Bokros, professor of economics and public policy

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**contact hours**: any time of mutual convenience, agreed in advance

**credits**: 2 (4ECTS)

**Term**: Winter, 2018-2019

**Course level**: MA/MSc

**Prerequisites**: basic knowledge of macroeconomics and finance, some familiarity with the basic concepts of financial accounting

**Course description**: having understood the nature and functions of money in the market economy, (where „money” is an adjective and „moneyness” is a noun) we analyze the *money creation process* in the modern market economy. Debunking the myth of fiat money (by mentioning cryptocurrencies) students will appreciate the significance of money as a societal phenomenon based on *trust and confidence* in the state. Emphasizing the need for *liquidity* we arrive at the analysis of banks. Distinction will be made among commercial, investment and development banks by looking at their balance sheets and their role in transforming private savings into investment. Highlighting the ever present *maturity mismatch and currency transformation*, the inherent fragility and vulnerability of the banking system will be explained by showing the contradictions among *liquidity, solvency and profitability*.

Central banking will be brought into this increasingly complex picture by highlighting the *lender-of-last-resort* function. We analyze the role of high-powered money (reserve money, central bank money) vs. deposit money created by the commercial banks. Monetary policy objectives will be explained in detail. By regulating the price & quantity of reserve money, the *regulation of the supply* of central bank money will be key in understanding the societal and economic role of central banks as monetary authorities with a state-sanctioned monopoly to provide liquidity to commercial banks. Relative *independence* or functional autonomy of central banks will be explained both from legal and political point of view as well as the transparency and public accountability of these institutions required by democratic societies.

The course will explain the monetary sources of *inflation* and the *objectives and* *constraints of monetary policy* to reduce it. Likewise, we will analyze the recent phenomenon of deflation and the limited effectiveness of unconvential monetary policy (QE) to overcome it.

Students will understand the distinction between monetary and *prudential regulation and supervision* and grasp the importance of state intervention in the money and financial markets by the various regulatory and supervisory authorities. We will analyze the most important methods of both monetary and prudential regulation and supervision together with the early warning systems embedded with and employed by the respective institutions.

We put special emphasis on macro and micro aspects of *banking crises, insolvency procedures* affecting, first and foremost, commercial banks. Restructuring, recapitalization, bankruptcy and liquidation will be analyzed in detail. The role of the regulatory bodies as well as the treasury should be clearly understood. The huge fiscal implications of state-led restricturing and recapitalization will be highlighted, too.

Last but not least we analyze what is considered to be a *systemically important bank*, with all its implications to global finance.

**Learning outcomes**: students will understand money and finance and will be in a position to explain its complexities in simple terminology. The role of crucial financial institutions in the economy and society will also be made comprehensible and explainable by the detailed analysis of the various types of financial institutions. Students will appreciate the role, possible impact and limitations of public policy in monetary and financial affairs; they will understand why we need different types of regulation and supervision in a well-functioning market economy. It will be clear why the state is not an antidote but an indispensable prerequisite for the free market, especially in its role as preventing and mitigating the impact of banking and financial crises. Students will be equipped with the most important analytical tools of dissecting the complex regulatory and supervisory problems emerging in various economic and political situations and their use in practical governance.

**Compulsory reading**:

1. Gregory Mankiw: Principles of Macroeconomics, MIT, 1991
2. Olivier Blanchard: Macroeconomics. Chapter 4. Financial Markets. MIT, Prentice Hall, Cambridge, various editions
3. Robert H. Marshall and Rodney B. Swanson: The Monetary Process: Essentials of Money and Banking. Houghton Miffin Co. Boston, 1974
4. Douglas Vickers: Money, Banking and the Macroeconomy. Prentice Hall, New Jersey, 1985
5. David Goacher: The Monetary and Financial System. Chapter 1. Money and Inflation. The Chartered Institute of Bankers, 1990
6. Milton Friedman: The Optimum Quantity of Money. Chicago, 1969
7. Friedrich A. Hayek: Denationalisation of Money. London, 1976.

**Recommended reading**:

1. Acharya-Cooley-Richardson-Walter (eds): Regulating Wall Street. The Dodd-Frank Act and the New Architecture of Global Finance. Part Two. John Wiley & Sons, Inc. 2011
2. Martin Wolf: Fixing Global Finance. The Johns Hopkins University Press, Baltimore, 2008
3. George Selgin (ed): Money Free and Unfree. CATO Institute, Washington, DC, 2017
4. Ludwig von Mises: The Theory of Money and Credit. Liberty Classics, Indianapolis, 1980

**Assessment**:

final exam paper: 80%

active participation in class: 20%