A Course in Monetary Theory

1. Sept 25: No meeting

2. Oct 2: 1. Sketch of Course
       2. Discussion of reading

I. Introduction
   A. Restriction of monetary analysis to an Enterprise Economy

       b. Remarks on Analytical Institutions

II. Elementary Keynesian and Classical System

  1. Nature of Keynesian model
  2. Determined nature of Classical

   Aspects: demand dominance

   5. Labor market dominance
I. The Classical Dichotomy and the Neutrality of Money
   A. Interpretation of Monetary and Value Theory
   B. The Neutrality and Non-Neutrality of Money
II. The Demand for Money and the Velocity of Circulation
   A. Development in Liquidity Preference
   B. Adjustment of Liquidity Preference
   C. The Distinguishing Characteristics of Money
   D. Empirical Research on the Demand for Money
III. The supply of money, monetary control, and monetary dynamics
   A. The supply of money
   B. Monetary control and instrument
   C. Monetary dynamics

IV. Monetary policy
   A. Objectives and instrumental role
   B. The effectiveness of monetary policy
   C. The adequacy of the policy

V. Conclusion and remarks
Introductory Remarks:

A. Monetary Theory

1. **Prerequisite**
   - At least 1 year of undergraduate economic theory

2. Knowledge of monetary and financial institutions, their behavior, and how they affect the economy. We should have to explain what is meant by "monetary policy" in a comprehensive way.

3. 200 A is the course in monetary theory.  

4. 225 B is a course in monetary institutions and policy.  

5. The applications may be somewhat different this year.  

6. It will not be strange that I cannot seem to make remarks about economic policy and the ones of economic theory are so along.

7. I will diverge from the outline where something of interest occurs to me.

8. Patience is not in print apparently.  

9. Expect you have bought:
   - Galley & Shaw
   - The State of Monetary Economy
8. If a large number of empirical literature on immortality phenomena will emphasize on this in 2012 and supere.

9. Really begin with the General Theory as a starting point in this course. May want to look at a handbook such as Adler to refresh your memory on to be various "models" - especially the Keynesian vs the Classical models and how they interact between them models.
I. Introduction.

There is always a step so that he might
for the purpose of analysis if wishes
will.

The problem of monetary theory is how does the fact that an enterprise economy uses money affect its behavior. A number of facts in this statement of the problem require further examination. The dimensions affected by economic behavior and the context of the term money have to be made precise. In addition the statement of the problem restricts our attention to the behavior of an enterprise economy and his restriction does in fact set the framework for our analysis.
A. Restriction of Monetary Analysis to an Enterprise Economy

The distinguishing attributes of an enterprise economy are not that decisions are decentralized and that market determined variables are parameters for individual decisions. As the hence-honor analysis of socialism has shown, an economy without the private ownership of produced means of production can be bound upon decentralized decisions. In fact, the individual decision unit considers naturally in its order to have basic decisions upon the same profit or utility maximization rules that presumably guide decisions in an enterprise economy.

It is also possible for an enterprise economy to operate without decision.
We now know that the existence of a public, that is, a market determined variables in decision by variables that reflect conscious guidance of the economy, is consistent with the existence of an enterprise economy. Modern planning is evidence for the birth of this economy.

The basic factor distinguishing, for instance, an enterprise from a reproducing and socialist tenure is the private ownership of productive wealth. Because households allocate their income among consumption and saving, and because income can be allocated to change wealth and consumption, wealth can be allocated to change wealth and consumption. In some, the private ownership of wealth implies that he acts at which wealth changes must be consistent with his preference of the community units that make up the community.
Any attempt at a precise statement of the rate of accumulation and decrease of household wealth requires that the parameters determining his relationship can be verified. Income distribution is an obvious determinant of how much would be saved at varying income, interest rate, and income distribution is sensitive to fiscal policy parameters. The uncertainty in accumulation rates with preferences of individual units therefore does not preclude planning, but it does does not allow him conditions under which he plan must conform. Switching an enterprise economy has been more difficult and subtle than has finding a through-going industrial economy.
There are two reasons for emphasizing the overall consistency of planning with an enterprise economy. One is that money is very much a "policy" oriented part of economics.

Monetary policy also, at least up to now, may affect business upon which decisions are based. Hence, monetary policy actions are undertaken for their effect upon the overall economic situation. These actions do have other effects, and the nature of these other effects is often almost always overlooked in the analysis of monetary policy. The planning effect, but it is in measures, not purposes.

Monetary policy has allocational and distributive influence as a planning instrument. An open question is that we may in fact be ignorant of their nature because of the mystery of monetary phenomena.
Another reason for emphasizing the
consistency of planning with an
enterprise economy is that how much money and
monetary changes depends upon the presence and
rules by which money affects decisions. New
finances and rules are dependent upon how
financial institutions had existed and their
behaviors. Financial institutions and rules are
close to a great extent determined
by laws and often are guided by regulating
agencies. Thus, the mechanics of planning
and guiding in an enterprise economy
include the definition of the behavioral
rules for monetary variables.
B. Wealth and the Ownership of Wealth.

First fact is that the production process uses "physical capital" that is there exists stocky items which will yield valuable services in the future. The term capital covers a multitude of items: durable goods that yield streams of services over time; one that "inventory's" arts production processes, consumer goods inventories, items produced discontinuously and the valuable skills of humans.

Both man and human capital have present values which reflects their value in the past and a discount rate. Some of them and present values appear as private marketable wealth, other productive capacity appear as private wealth which cannot be allocated from it owner and still other sources of income producing capacity appear as "socially owned wealth".
The fundamental production concept is the existence of stocks that generate flows. The stocks are capable of generating flows over an extensive time period. The flows are inputs to the production process, but for the flows to take place, it is necessary for the capital, in wealth, that is in the starting to exist. The stock-flow interrelations is a fancy field. How would overall economic policy to be stock we are considering no non-human wealth - the general name for the flow we are considering to incomes.

Monetary theory is basically concerned with stock-flow interrelations. As such, what is subsumed under the headings capital and investment theory is essential to monetary theory.
In a sophisticated and advanced enterprise economy, the ownership of productive and service productive capacity by households can be direct or indirect, and direct ownerships can enjoy various protections due to legal forms. The direct ownerships of private, non-farm productive capacity by a household takes the form in an older modern economy of owning shares in debt in corporations and other business enterprises or owning real property - land in housing. In a private enterprise agricultural society, a major form of private wealth is farm land ownership, but for many practical purposes we can interpret this into the private ownership of farm enterprises.
In addition to the direct ownership of private wealth, households can directly own debts of public authorities. At any date, private transferable wealth is equal to the sum of the market values of private productive wealth and government debts.

Indirect ownership of wealth exists when institutions exist which while emitting their own liabilities acquire as their assets liabilities of those units. Indirect ownership also implies layering: the sum value of assets outstanding is greater than the value of private wealth and public debt.
A more sophisticated and advanced enterprise economy not only in the market value of a large amount of wealth invested in households but there is a partial function of financial instrument and practices which leads to the indirect ownership of real wealth by households.

A wealth owner no longer needs own a farm or a factory or he himself to initiate but own his farm or his factory. He now can own deposits or equity in pension funds and life insurance reserves.

A modern sophisticated enterprise economy not only exhibits the decentralization of ownership by means of corporate farm but also the layering of financial relations by means of financial intermediaries. A problem
Monetary theory is to determine how it all fits together to form financial layers. The economy affects certain behaviors.
A representation of an enterprise economy is the complete set of interrelated balance sheets. To each unit - household, government, business firm - a balance sheet is attached. The balance sheet's main body states the marketable assets and liabilities of the unit. For simplicity's sake we assume that all "human firms" are organized as partnerships - so that households do not own productive capacity.

The existence of consumer capital obviously modifies this above.

The financial structure of an economy in the set of balance sheets, the interrelationships among balance sheets which reflects hierarchy - and the various special rights and privileges of liabilities/assets. The financial rights and privileges I call leverage. Protection and in a complex society he financial set of instruments as standing allows a line of financing.
We will first take up the
set of books and bringing. We will have taken
the outstanding risk and the contingent liabilities
that underlies many of the balance sheets in
an enterprise, earning and contingent liabilities of
government.

As stated earlier to each unit
we associate a balance sheet. In the main
body of the balance sheet we state its assets
marketable, and its liabilities. For a
firm, its assets consist of its human capital
and other fixed capital. However,
and its liabilities of short-term debt. Two assets?

For every dollar
In a closed economy,

formatted the document 12/6/11, to this note

1st 1st
As stated earlier to each unit we associate a balance sheet. In the main body of the balance sheet, the units are recorded in the asset and liability columns. An asset is the unit's ownership interest in its assets and its revenues. The liability of the unit is its assets and its liabilities. Thus units: its assets are "tangible" or "financial". In a closed economy, the set of both assets closed in the sense that the liabilities of one unit are the financial assets of another.

**Consolidation of Balance Sheets:**

Two or more balance sheets are consolidated when the assets and liabilities are added as if they were one unit, and any items that appear both as an asset and liability are cancelled.

If only households and firms exist, then a consolidated set households and firms
Balance sheet will yield

1) No financial assets only tangible assets
2) No liabilities aside from Net Worth.

Hence, in a closed economy consisting only of households and firms, household net asset will be equal to the value of their tangible assets, i.e., net human wealth.

If a government exists, it will balance sheet consists of only liabilities - pure dead weight debt.

Then, the consolidated assets of consolidated private sector (households and firms) will consist of tangible assets plus the government debt; the net worth of the households will have to equal to the value of tangible assets + debt.
A financial asset represents a claim to
payments which can be considered as being
financed by the contributions to production of
the tangible assets of the unit
emitting the financial asset. The characteristics
of the production process and the attributes of
household preferences systems may lead to widely
differing supplies and demands for particular
financial assets at particular contractula
conditions. This "disequilibrium" situation
leads to possibilities of arbitrage.
The data should be made precise by citing specific examples and studies. Firms may have assets which will produce a stream of earnings over a long period of time. The financial commitment may be willing to make and to make payments over a long period of time. In addition, firms may have short-lived assets to finance the acquisition of these assets. They will be more likely to enter into short-term financial commitments whenever possible. In this case, they would be willing to enter into short-term contracts unless in some dimension, long-term contracts were more expensive than short-term contracts.
The "cost flow" associated with a production process can be illustrated by a modified form of the standard cost curve. Let us assume a production process with fixed quantities of capital and labor. One example are owned by the firm, and other...
assuming a wage-capital ratio of \( \frac{w}{K} \).

constant returns to scale:

\[
\frac{K}{w} = \text{constant}
\]

The variable cost curve along the constant capital expansion path would look like this.
The difference between the TVC and TVC + TVK is the "cost flow" applicable to the "work in process" labor and capital against fixed capital charges. This flow is "work in process" labor.
Shyevering, Money as a product of layering in money and money.

2) Part-time hired labor:
- Distributing independent
- Workers' union
- Steer protection

3) Contingent liabilities
- Of a bank

Investment Demand on himself as part and
adaptor process

Transmission Mechanism:

4. Money + Capital Markets:

Money MKT INSTRUMENTS: Wholesale MKT
- Irreducible C.P.'s
  1. Bank liab., like Prime Rate
  2. Non-bank financial intermediaries

Banks as
struct as men
The fact that money is of particular relevance for the present economic with complex financial structures leads us quite naturally to the conclusion that its proportions of monetary dishonesty may in fact be conditioned proportions in which their truth depends upon the nature of the monetary and financial institution and not upon any inherent properties of a decentralized economic economy. Query: Has the significance of money in determining systemic behavior changed with the introduction of financial derivatives?

Significance also implies a new value of a parameter in a selection model. New variables become "statistically" significant.

It is not too different what if we decide instead of limited to a number of variables in a model? An somewhat different
We have been talking of the relevance of money in determining system behavior for some time without specifying what the dimensions of system behavior are. The traditional dimensions of system behavior are four:

A. Allocation of resources among uses

B. Distribution of income

C. Stability: (1) in terms of the relations between a desired or target level and an actual level, or between an actual level and potential maximum

D. Growth: (1) rate of change of potential income plus the rate of change of welfare generating attitude which is not related to marketable output or income and (2) increase in the dimensions of welfare which are not included in the conventional rate of change of some national constant definition of income.
Discuss the dimensions of system behavior:

1. Allocation of Resources: How is the allocation of resources affected by the nature and how behavior, the money supply?

This system is usually examined in terms of the determination of the demand side of the normal division of current output between I and C, i.e., the division of output between I and C and affected by the existence and use of money. This becomes the key economic policy instrument. Consequently, policies primarily determine a net effect on total full employment income between I and C. Note that if you accept the view that this percentage of money invested determines the rate of growth, then the allocation of resources and government efforts include:

[Handwritten notes continue]
There is another more subtle way in which monetary phenomena may not stay money and must affect the allocation of resources: historically, the effect of interest rate variations upon choice of investment opportunities, considered two investment—\( u \) current and \( v \) future—leads future income—which can be total short and long rates higher than two corporates as

\[
\text{Example: Short } 10 \% \quad \text{Long } 5 \%
\]

initial private short rate \(20\%\) long rate \(50\%\)

Both short and long present value \(100\%\) an investor is indifferent between the two if current and \(5\%\) investment is \(100\%\)

Assume short rises to \(29\%\) long to \(65\%\)

Short with \(15\%\) long with \(35\%\) same firms but perfect hedge if Re on \(20\%\) in long earns \(15\%\) rise short (FED)

Fall to \(21\%\) Short with \(10\%\), long with \(25\%

Another \(40\%\) to choose \(short\)

\[\text{must bring short to } 80\% \text{ to yield } 12.5\%\]
Crismus 2

Anns: 14 last 1
14 last 2

Some err of production

$103.14 for more
long $15 in respectability

Mills intended note $39. next
5% long.

1-2 could come both with $15 in market

Crismus on a went note to $90, next, 69% long.

Short life came with $99 long helped must worth $86 3/4.

That note would have to be under $50, maybe $56 2/3.

Following interest notes:

2% that
49% long

Price $103.14 for more $101

5% in respectability $123.

for pay if for that things
Innovation and incentives even though high may still have become opportunities costs. Monetary policy can affect interest rate level as well as interest rate structure; it can affect the choice between short and long investment.

Footnote: Note discussion made on "
Distribution of Income

What have we done so far? It seems to be evident that a complex financial system allows small amounts of dispersed wealth to serve as a vehicle for financial intermediation and coordination among financial instruments, even in a lower rate structure. The market for financial assets tends to undermine the relative return to the long-term owners of wealth.

\[ Y = T + C \]

Keynesian framework: Wave's wave, not fixed value.
\[ Y = P = I \rightarrow \]
\[ P \text{ is determined by } W \]

Kaldor Theory
C. Stability

Monetary theory & Cycle

mechanism & correlation

price level

Quantity Theory


D. Income

Provision & Expenditures
Analytical Institutions in the present monetary theory:

always must question what effect

the actual institutions have upon behavior.