

Money multiplier essay sample

[Economics](#), [Money](#)



The expansion of a country's money supply that results from banks being able to lend. The size of the multiplier effect depends on the percentage of deposits that banks are required to hold as reserves. In other words, it is money used to create more money and is calculated by dividing total bank deposits by the reserve requirement.

Investopedia explains ' Multiplier Effect'

The multiplier effect depends on the set reserve requirement. So, to calculate the impact of the multiplier effect on the money supply, we start with the amount banks initially take in through deposits and divide this by the reserve ratio. If, for example, the reserve requirement is 20%, for every \$100 a customer deposits into a bank, \$20 must be kept in reserve.

However, the remaining \$80 can be loaned out to other bank customers. This \$80 is then deposited by these customers into another bank, which in turn must also keep 20%, or \$16, in reserve but can lend out the remaining \$64. This cycle continues – as more people deposit money and more banks continue lending it – until finally the \$100 initially deposited creates a total of \$500 ($\$100 / 0.2$) in deposits. This creation of deposits is the multiplier effect.

The higher the reserve requirement, the tighter the money supply, which results in a lower multiplier effect for every dollar deposited. The lower the reserve requirement, the larger the money supply, which means more money is being created for every dollar deposited.

Read more: <http://www.investopedia.com/terms/m/multipliereffect.asp#ixzz1r8dNt1dC>

<https://assignbuster.com/money-multiplier-essay-sample/>

Term high-powered money Definition: Also termed the monetary base, the total of currency held by the nonbank public, vault cash held by banks, and Federal Reserve deposits of the banks. This contains the monetary components over which the Federal Reserve System has relatively complete control and is often used as a guide for the Fed's money control ability and monetary policy. « Hierarchy of needs | historical cost »

Permalink: <http://glossary.econgruru.com/economic-term/high-powered+money> Narrow money:

One measure of the money supply that includes all coins, currency held by the public, traveler's checks, checking account balances, NOW accounts, automatic transfer service accounts, and balances in credit unions. Also called M1

Read more: http://www.investorwords.com/5673/narrow_money.html#ixzz1r8otwV8c

In economics, broad money is a measure of the money supply that includes more than just physical money such as currency and coins (also termed narrow money). It generally includes demand deposits at commercial banks, and any monies held in easily accessible accounts.

Components of broad money are still very liquid, and non-cash components can usually be converted into cash very easily. The most commonly used measure of broad money is M2, which includes currency and coins, and deposits in checking accounts, savings accounts and small time deposits, overnight repos at commercial banks, and non-institutional money market accounts.

This is the main measure of the money supply, and is the economic indicator usually used to assess the amount of liquidity in the economy, as it is relatively easy to track.[1] However broad money can have different definitions depending on the situation of usage, usually it is constructed as required to be the most useful indicator in the situation. More generally, broad money is just a term for the least liquid money definition being considered and less a fixed definition across all situations.[2] As such broad money may have different implications in the United States than it does in Australia and even from academic paper to paper. The term broad money will usually be more exactly defined before a discussion, when it is not sufficient to assume a wider definition of money.