



# MONEY AND BANKING SYSTEM

- We want
- We think about
- We use

!! MONEY !!

- Money

- is universal instrument accepted as payment for goods and services to provide payments and express value of other goods

- Functions of money

- Medium of exchange
- Standard of value (money are used to evaluate goods and services)
- Store of value (money are gathered and saved for future consumption or turning into capital)



# Way of Exchange

- **Natural exchange** (barter) – two individuals possessing the commodity the other want
  - Inefficient trading (low or no transferability and divisibility)
  - Imagine you have tomatoes and want fridge: then you have to find somebody who has fridge (and do not need it) and wants tomatoes (need for double coincidence)
  - If you find such person, then you have to agree how many tomatoes are equal to the fridge
- To overcome this problem -> we need money
- **Weighing** of gold and silver
- **Coining** from gold and silver
- Coining from other metals
- **Banknotes**



# Types of Money

## ■ Coins, banknotes

- cash money
- nowadays emitted solely by central national bank
- they serve in regarded country as a legal currency and everybody is obliged to accept them

## ■ Deposit money

- are stored in banks and other financial institutions
- checkable deposits** – can be withdrawn immediately
- time deposits** – with necessity to give a notice to bank before paying out



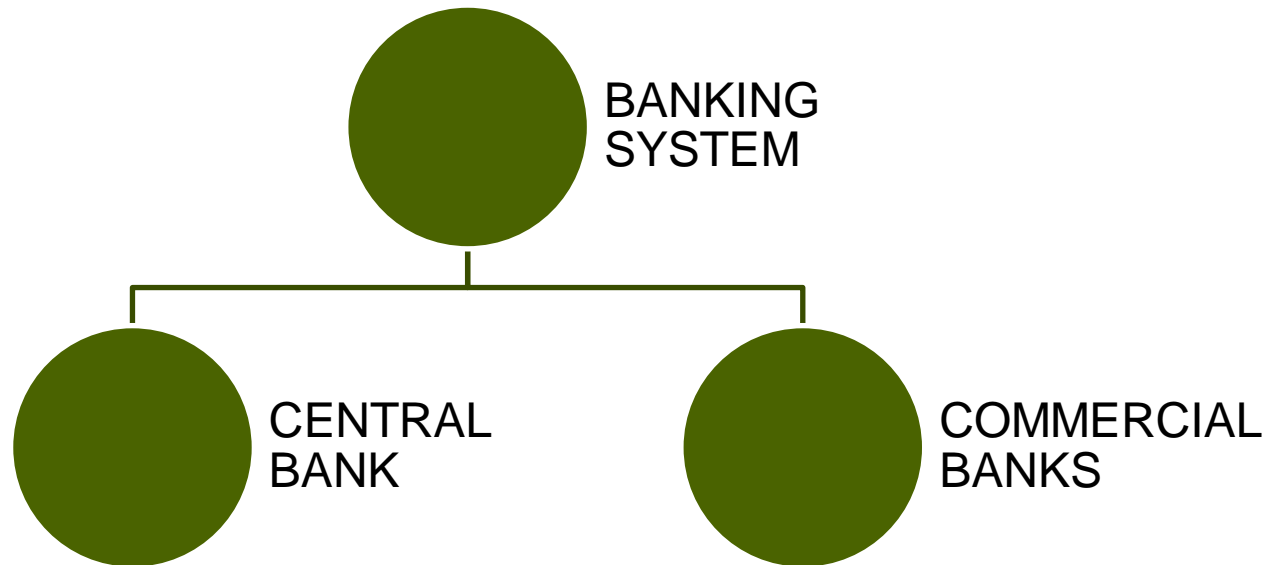
# Financial Market

- = a mechanism which allows people to trade money for securities or commodities such as gold or other precious metals.
- 2 segments:
  - **money market**
    - facilitates trading financial instruments with high liquidity and very short maturities (eurodollar deposits, state loans)
    -
  - **capital market**
    - facilitates the buying and selling of financial instruments (equity securities and debt securities) [*majetkové a dluhové cenné papíry*]
- In CZ, supervision of financial market performs Czech National Bank (CNB)

# Banking System

## ■ Bank

- is a business entity that provides banking services for profit. Traditional banking services include **receiving deposits** of money, **lending money** and processing transactions. Some banks (called Banks of Issue) issue banknotes as legal tender.





# Central Bank

- responsible for the **monetary policy** of its country or of its group of member states (e.g. EU)
- responsible to maintain the **stability of the national currency** and money supply
- controls subsidized loan **interest rates**
- actc as a "bailout" lender of last resort to the banking sector during times of financial crisis
- It may also have **supervisory powers** to ensure that banks and other financial institutions do not behave recklessly or fraudulently
- usually headed by a Governor, President in the case of the European Central Bank.



# Commercial bank

- it raises funds by **collecting deposits** from businesses and consumers via checkable deposits, savings deposits, and time (or term) deposits
- it **makes loans** to businesses and consumers. It also buys corporate bonds and government bonds
- its primary liabilities are deposits and primary assets are loans and bonds
- is usually private institution run to gain profit
- activity is strongly affected by government and central bank in order to secure stability of the banking system (stating conditions of bank foundations, compulsory insurance of deposits etc.)





# Czech National Bank

- Established under the Constitution of the Czech Republic and carries out its activities in compliance with Act No. 6/1993 Coll., on the Czech National Bank
- Supreme governing body of the CNB is the **Bank Board**, consisting of the CNB Governor, two Vice-Governors and four Chief Executive Directors. All Bank Board members are appointed by the President of the Czech Republic for a term of six years.
- **Primary objectives:**
  - Price stability (creating low-interest environment in the economy)
  - Creation of conditions for sustainable economic growth
- CNB is **independent** institution
- Without prejudice to its primary objective, the CNB also supports the general economic policies of the Government



# Financial Market Supervision of CNB

- CNB is responsible for **supervision of the financial market** in the Czech Republic
- CNB **lays down rules** safeguarding the stability of the:
  - banking sector,
  - capital market,
  - insurance industry,
  - pension scheme industry.
- It systematically regulates, examines, assesses and, where appropriate, issues penalties for non-compliance with these rules.



# Examples of CNB actions

- Revocation of the banking license
  - 30.4.2003 – Union Banka, reason: bank does not maintain its solvency in the Czech currency and in foreign currencies
  
- Revocation of permission to operate
  - 24.10.2016 – ERB Bank, reason: dysfunctional management and control systems of bank and purchase bonds in conflict with the law
  
- Managing exchange rate CZK/EUR near the level of 27 CZK / EUR in order to meet the inflation target (2%)
  - Exchange rates on next lecture



# Some historical information about CZ banking system

- Deposit insurance
  - Limit 100,000 EUR (= cca 2,750,000 CZK)
  - Coverage:
    - Banks, building savings banks
    - In CZK and in foreign currencies
    - E.g.: current account, savings account, term deposits
  
- Bank failures
  - 22 banks between 1994 - 2003



# The European Central Bank

- Established 1998
- The ECB is the **central bank for** Europe's single currency, the **euro**.
- The primary objective of the ESCB:
  - is maintaining the **price stability**
  - And: "without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Community with a view to contributing to the achievement of the objectives of the Community as laid down in Article 2."  
(Treaty article 105.1)
  - The objectives of the Union (Article 2 of the Treaty on European Union) are a **high level of employment** and **sustainable and non-inflationary growth**.
- Politically independent institution
- Policy of transparency: bank provides the general public and the markets with all relevant information on its strategy, assessments and policy decisions as well as its procedures in an open, clear and timely manner

# Financial Market

- Changes in equilibrium on financial market

Price level rises



Need of subjects to hold money rises as well

Increased demand for money



Banks will provide more expensive money

Increase of interest rate



# Financial Market

- Central bank stimulates aggregate demand by lowering interest rate (cheap money policy). Central bank allows money supply growth.





# CNB discount rate

- the interest rate at which commercial banks can borrow money from the central bank
- allows to control the supply of money on the market provided by commercial banks
- is the lower limit of short-term interest rates on the money market
  
- Increasing discount rate -> reduces inflation
- reduction of discount rate -> expansive increase of money





- Thank U 4 your attention