

- duration analysis, p. 239
- equity multiplier (EM), p. 232
- excess reserves, p. 222
- gap analysis, p. 239
- interest-rate risk, p. 226
- liability management, p. 226
- liquidity management, p. 226
- loan commitment, p. 237
- loan sale, p. 241
- money center banks, p. 230
- off-balance-sheet activities, p. 241
- required reserve ratio, p. 222
- required reserves, p. 222
- reserve requirements, p. 222
- reserves, p. 222
- return on assets (ROA), p. 232
- return on equity (ROE), p. 232
- secondary reserves, p. 222
- T-account, p. 223
- vault cash, p. 222

QUESTIONS AND PROBLEMS

Questions marked with an asterisk are answered at the end of the book in an appendix, “Answers to Selected Questions and Problems.” Questions marked with a blue circle indicate the question is available in MyEconLab at www.myeconlab.com/mishkin.

- 1 Why might a bank be willing to borrow funds from other banks at a higher rate than it can borrow from the Fed?
- * 2 Rank the following bank assets from most to least liquid:
 - a. Commercial loans
 - b. Securities
 - c. Reserves
 - d. Physical capital
- 3 Using the T-accounts of the First National Bank and the Second National Bank, describe what happens when Jane Brown writes a \$50 check on her account at the First National Bank to pay her friend Joe Green, who in turn deposits the check in his account at the Second National Bank.
- * 4. What happens to reserves at the First National Bank if one person withdraws \$1,000 of cash and another person deposits \$500 of cash? Use T-accounts to explain your answer.
- 5 The bank you own has the following balance sheet:

Assets		Liabilities	
Reserves	\$ 75 million	Deposits	\$500 million
Loans	\$525 million	Bank capital	\$100 million

If the bank suffers a deposit outflow of \$50 million with a required reserve ratio on deposits of 10%, what actions must you take to keep your bank from failing?

- * 6 If a deposit outflow of \$50 million occurs, which balance sheet would a bank rather have initially, the balance sheet in Problem 5 or the following balance sheet? Why?

Assets		Liabilities	
Reserves	\$100 million	Deposits	\$500 million
Loans	\$500 million	Bank capital	\$100 million

- 7 Why has the development of overnight loan markets made it more likely that banks will hold fewer excess reserves?
- * 8 If the bank you own has no excess reserves and a sound customer comes in asking for a loan, should you automatically turn the customer down, explaining that you don't have any excess reserves to lend out? Why or why not? What options are available for you to provide the funds your customer needs?
- 9 If a bank finds that its ROE is too low because it has too much bank capital, what can it do to raise its ROE?
- * 10 If a bank is falling short of meeting its capital requirements by \$1 million, what three things can it do to rectify the situation?
- 11. Why is being nosy a desirable trait for a banker?
- * 12 A bank almost always insists that the firms it lends to keep compensating balances at the bank. Why?
- 13. “Because diversification is a desirable strategy for avoiding risk, it never makes sense for a bank to specialize in making specific types of loans.” Is this statement true, false, or uncertain? Explain your answer.

QUESTIONS AND PROBLEMS

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- 1 Why was the United States one of the last of the major industrialized countries to have a central bank?
- * 2 Which regulatory agency has the primary responsibility for supervising the following categories of commercial banks?
 - a. National banks
 - b. Bank holding companies
 - c. Non-Federal Reserve state banks
 - d. Federal Reserve member state banks
3. “The commercial banking industry in Canada is less competitive than the commercial banking industry in the United States because in Canada only a few large banks dominate the industry, while in the United States there are around 7,500 commercial banks.” Is this statement true, false, or uncertain? Explain your answer.
- * 4. Why did new technology make it harder to enforce limitations on bank branching?
- 5 Why has there been such a dramatic increase in bank holding companies?
- * 6. Why is there a higher percentage of banks with less than \$25 million of assets among commercial banks than among savings and loans and mutual savings banks?
- 7 Unlike commercial banks, savings and loans, and mutual savings banks, credit unions did not have restrictions on locating branches in other states. Why, then, are credit unions typically smaller than the other depository institutions?
- * 8 What incentives have regulatory agencies created to encourage international banking? Why have they done this?
 9. How could the approval of international banking facilities (IBFs) by the Fed in 1981 have reduced employment in the banking industry in Europe?
- * 10. If the bank at which you keep your checking account is owned by Saudi Arabians, should you worry that your deposits are less safe than if the bank were owned by Americans?
- 11 If reserve requirements were eliminated in the future, as some economists advocate, what effects would this have on the size of money market mutual funds?
- * 12. Why have banks been losing cost advantages in acquiring funds in recent years?
13. “If inflation had not risen in the 1960s and 1970s, the banking industry might be healthier today.” Is this statement true, false, or uncertain? Explain your answer.
- * 14. Why have banks been losing income advantages on their assets in recent years?
15. “The invention of the computer is the major factor behind the decline of the banking industry.” Is this statement true, false, or uncertain? Explain your answer.

WEB EXERCISES

1. Go to www2.fdic.gov/SDI/SQB. Select “Historical Statistics on Banking,” then “Commercial Bank Reports.” Finally, choose “Number of Institutions, Branches, and Total Offices.” Looking at the trend in bank branches, does the public appear to have more or less access to banking facilities? How many banks were there in 1934 and how many are there now? Does the graph indicate that the trend toward consolidation is continuing?
2. Despite the regulations that protect banks from failure, some do fail. Go to www2.fdic.gov/hsob/. Select the tab labeled “Bank and Thrift Failures.” How many bank failures occurred in the United States during the most recent complete calendar year? What were the total assets held by the banks that failed? How many banks failed in 1937?

11. How can the S&L crisis be blamed on the principal-agent problem?
- *12. Do you think that eliminating or limiting the amount of deposit insurance would be a good idea? Explain your answer.
13. Do you think that removing the impediments to a nationwide banking system will be beneficial to the economy? Explain your answer.
- *14. How could higher deposit insurance premiums for banks with riskier assets benefit the economy?
15. How has the too-big-too-fail policy been limited in the FDICIA legislation? How might limiting the too-big-too-fail policy help reduce the risk of a future banking crisis?

WEB EXERCISES

- Go to www.fdic.gov/regulations/laws/important/index.html. This site reports on the most significant pieces of legislation affecting banks since the 1800s. Summarize the most recently enacted bank regulation listed on this site.
- The Office of the Comptroller of the Currency is responsible for many of the regulations affecting bank operations. Go to www.occ.treas.gov/. Click on “Legal and Regulatory” and then on “Law and Regulations.” Now click on the 12 CFR Parts 1 to 199. What does Part 1 cover? How many parts are there in 12 CFR? Open Part 18. What topic does it cover? Summarize its purpose.

WEB REFERENCES

www.ny.frb.org/banking/supervision/regulate.html

View bank regulation information.

www.federalreserve.gov/Regulations/default.htm

Access regulatory publications of the Federal Reserve Board.

www.fdic.gov/regulations/laws/important/index.html

Describes the most important laws that have affected the banking industry in the United States.

www.fdic.gov/bank/historical/bank/index.html

Search for data on bank failures in any year.



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To see how it works, turn to page 19 and then go to www.myeconlab.com/mishkin

1. When banks were faced with the housing crisis, liquidity issues, and other problems, what parts of the bank balance sheet were impacted and how did this lead to failure or near failure?

2. What are the costs and benefits of a too-big-to-fail policy and do you believe that this is the policy that the Federal government is taking now? What is your opinion about it?

Question 1

Describe the process of performing an internal audit. What are the goals of an internal audit?

Question 2

What is the resource-based view? Describe this approach to competitive advantage and explain its general reasoning.

Question 3

Compare and contrast U.S. firms with European firms. Why do the management styles, workplace norms, and other factors of work life differ in Europe from the U.S.?

Question 4

Explain the importance of financial ratio analysis in the context of assessing internal strengths and weaknesses.

Question 5

Explanation of what the IFE Matix is used for and specifically how might it be used in strategy formulation