



Chapter

24

Money and Banking

Why It Matters

Our market economy is based on the idea of voluntary exchange—we exchange money for the goods and services we need. You live in a world where this exchange usually involves money. It is the primary medium of exchange for goods and services.

BIG Ideas

Section 1: What Is Money?

The basis of the market economy is **voluntary exchange**. In the American economy, the exchange usually involves money in return for a **good or service**. People are willing to accept money in exchange for goods, and financial institutions give people both a safe place to deposit their money or take out loans.

Section 2: The Federal Reserve System

Political and economic institutions evolve to help individuals and groups accomplish their goals. The central bank of the United States is the Federal Reserve System. It controls the money supply, serves as the government's bank, and watches over the banking industry.

Section 3: How Banks Operate

Political and economic institutions evolve to help individuals and groups accomplish their goals. Banks offer important financial services to millions of people.

◀ Sorting \$100 bills at the U.S. Department of the Treasury

FOLDABLES™ Study Organizer

Evaluating Information Study Foldable Make the following Foldable to help you evaluate the workings of the Federal Reserve.

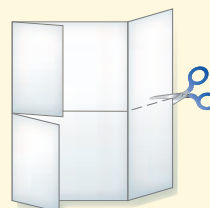
Step 1 Mark the midpoint of the side edge of a sheet of paper. Then fold in the outside edges to meet at the midpoint.



Step 2 Fold in half from side to side.

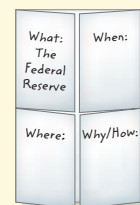


Step 3 Open and cut the inside fold lines to form four tabs. Label the tabs *what*, *when*, *where* and *why*.



Reading and Writing

As you read the chapter, note information about the Federal Reserve under the appropriate tab.





Section
1

Guide to Reading

Big Idea

The basis of the market economy is voluntary exchange. In the American economy, the exchange usually involves money in return for a good or service.

Content Vocabulary

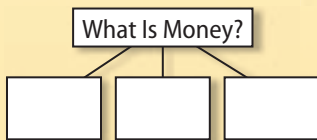
- coin (p. 657)
- currency (p. 657)
- commercial bank (p. 658)
- savings and loan association (S&L) (p. 658)
- credit union (p. 658)

Academic Vocabulary

- obvious (p. 657)
- medium (p. 657)

Reading Strategy

Describing As you read the section, complete a graphic organizer like the one below that illustrates three functions of money.



What Is Money?

Real World Economics No flaws allowed here. This Treasury Department expert examines new sheets of \$100 bills as they shoot off the presses. The money is actually made at the Bureau of Engraving and Printing. The first \$100 bills, issued in 1862, were called “legal tenders.” Benjamin Franklin became the face on the \$100 bill in 1914. Today this bill, which may stay in circulation for up to five years, is the largest denomination in use.

▼ U.S. Treasury worker inspects newly printed \$100 bills



NORTH CAROLINA STANDARDS
Civics and Economics

- 8.08** Evaluate the investment decisions made by individuals, businesses, and the government.
- 8.09** Describe the role of money in trading, borrowing, and investing.



Money

Main Idea People are willing to accept money in exchange for goods.

Economics & You How much money do you have in your pocket or purse? Read to find out why this money has value to you and everyone else.

Money is more interesting than you might think. It serves different functions, comes in several different forms, and has value for reasons that are not immediately **obvious**, or clear.

Functions and Types of Money

Money has three functions. First, it serves as a **medium**, or form, of exchange—we can trade money for goods and services. Without money, people would have to barter—exchange goods and services for other goods and services. Second, money serves as a store of value. We can hold our wealth in the form of money until we are ready to use it. Third, money serves as a measure of value. Money is like a measuring stick that can be used to assign value to a good or service. When somebody says that something costs \$10, we know exactly what that means.

Types of Money How would you define money? According to economists, money is anything that people are willing to accept in exchange for goods. At various times in history, salt, animal hides, gems, and tobacco have been used as mediums of exchange.

The most familiar types of money today are coins and currency. **Coins** are metallic forms of money such as pennies and nickels. **Currency** includes both coins and paper money. There are other forms of money as well.

Civics ONLINE

Student Web Activity Visit glencoe.com and complete the Chapter 24 Web Activity.

What Gives Money Value?

Why do we value and accept money? The simple reason is that we are absolutely sure that someone else will accept its value as well. Without this confidence in money, we would not accept it from someone else for payment in the first place.

Money by itself generally has no other value. A \$10 bill costs only a few cents to make and has no alternative use. Coins contain only small amounts of precious metal. The same is true of checking and savings accounts—they have value only because we accept that they have value.

Reading Check Explaining Why does money have value?

Bartering People have used different goods for buying or trading. Kyle MacDonald from Montreal, Quebec, spent a year trading items on the Internet through Craigslist. He started trading with a red paper clip and ended up trading for a home. **Identifying What two types of money are most commonly used today?**





The Financial System

Main Idea Financial institutions give people a safe place to deposit their money or take out loans.

Economics & You Do you have a savings account? Read to find out what happens to your money when you make a deposit.

Do you know what happens when people and businesses with money to save take it to financial institutions? These institutions do not simply put the money in a safe and leave it there. Instead, they put the money to work by lending it to other people or businesses that need funds. They use the money to make more money. The financial institution covers its costs—and makes a profit—from the interest, or fees, it charges for those loans.

Financial Institutions

Commercial banks are financial institutions that offer full banking services to individuals and businesses. They are probably the most important part of our financial system because of their large areas of influence. Most people have their checking and savings accounts in commercial banks.

Savings and loan associations (S&L) are financial institutions that traditionally loaned money to people buying homes. They also take deposits and issue savings accounts in return. Today, S&Ls perform many of the activities that commercial banks do.

Credit unions work on a not-for-profit basis. They are open only to members of the group that sponsors them, usually businesses, labor unions, and government institutions. Generally, credit unions offer better rates on savings and loans than do other financial institutions.

Features of U.S. Currency



Analyzing Charts

- Predicting** What security features of this bill would be most difficult to duplicate for a counterfeiter?
- Explaining** Why is counterfeit money in the monetary system a problem for the economy?



Each of these types of banking institutions performs a similar function. They all act to bring together savers and borrowers. They give people a safe place to deposit their money when they want to save it and a source for borrowing when they need a loan. You will learn more about this system in Section 3.

Safeguarding Our Financial System

The financial system of the United States is one of the safest in the world. This safety results from two factors—regulation and insurance.

Banking is one of the most regulated industries in the country primarily because of the banking disaster of the 1920s. Most financial institutions have to report to one or more regulatory agencies. They are required to follow rules and accounting practices that minimize unnecessary risk.

The FDIC When financial institutions fail, federal deposit insurance protects consumers’ deposits. The most important insurance agency is the Federal Deposit Insurance Corporation (FDIC), a national corporation that insures individual accounts in financial institutions for up to \$100,000. The collapse of the banking system during the Great Depression of the 1930s wiped out people’s entire savings. Now if a bank fails, depositors do not lose their savings.

Consumer Confidence Because accounts in financial institutions have some type of government insurance, consumers feel safer wherever they deposit their money. As a result, they continue to make deposits—and those deposits give financial institutions the funds they need to make loans that help fuel economic growth.

 **Reading Check Explaining** How do financial institutions make a profit?

Section Review 1

Vocabulary

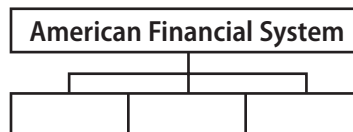
- Write** a paragraph about the U.S. financial system that uses each of these terms: *coin, currency, commercial bank, savings and loan association (S&L), credit union*.

Main Ideas

- Name** two forms of money in addition to currency and coin.
- Describing** What is the purpose of the FDIC?

Critical Thinking

- Explaining** What advantage do credit unions offer their customers? Why?
- BIG Ideas** In a graphic organizer like the one below, describe the types of institutions in the American financial system.



CITIZENSHIP Activity

- Comparing** Obtain brochures from several banks, credit unions, and savings and loans. Compare their services and fees. If you had \$1,000 to deposit, which institution would you choose? Explain your choice.
- Descriptive Writing** Write a paragraph describing which financial institution services you expect to use over the next five years.



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Section
2

The Federal Reserve System

Guide to Reading

Big Idea

Political and economic institutions evolve to help individuals and groups accomplish their goals.

Content Vocabulary

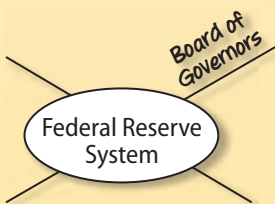
- central bank (p. 661)
- Federal Open Market Committee (FOMC) (p. 661)
- monetary policy (p. 664)
- discount rate (p. 664)
- reserve (p. 665)
- open market operations (p. 665)

Academic Vocabulary

- manipulate (p. 661)
- contract (p. 664)

Reading Strategy

Classifying As you read this section, complete a graphic organizer like the one below by listing the components that make up the Federal Reserve System.



Real World Economics The Federal Reserve System, usually known as the Fed, is the United States bank from which all other banks borrow. Its board is run by chairperson Ben Bernanke, shown here with the president of the European Central Bank at an international monetary conference. Previously a professor and economic analyst, Bernanke replaced Alan Greenspan, long-time chairperson of the Fed. The Fed enters your life every day as the agency that controls interest rates on loans and controls the money supply, affecting inflation in America.

▼ **Ben Bernanke, right, has been the Fed chairperson since February 2006**





Structure and Organization

Main Idea The central bank of the United States is the Federal Reserve System.

Economics & You Do you remember hearing about “the Fed” raising interest rates? Read to find out what this important body does.

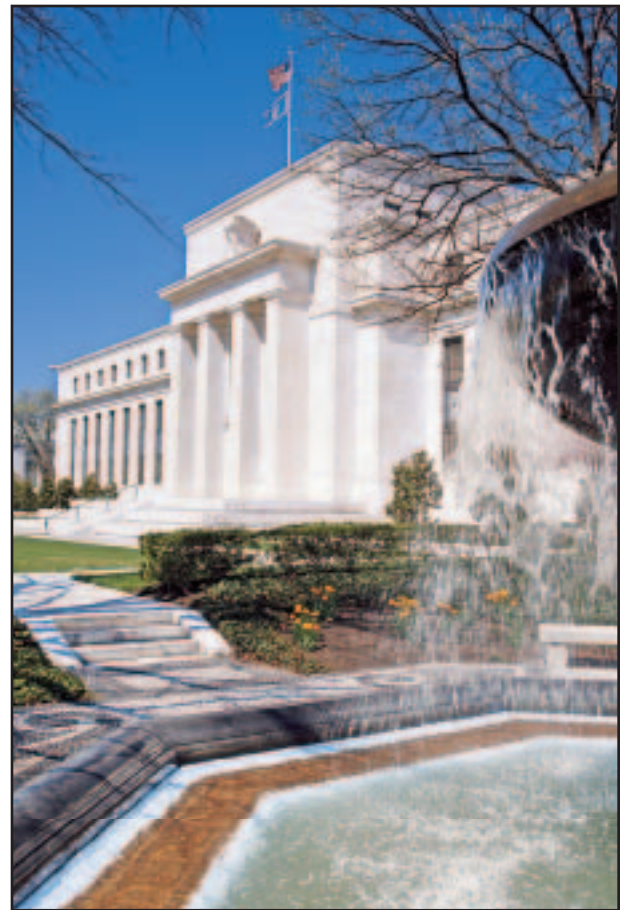
The **central bank** of the United States is the Federal Reserve System, known as the Fed. When people or corporations need money, they borrow from banks. When banks need money, they borrow from the Fed. The Federal Reserve System is a banker’s bank.

The United States is divided into 12 Federal Reserve districts. Each district has one main Federal Reserve Bank, along with branch banks. Thousands of banks in the United States are members of the Federal Reserve System. Member banks are owners of the Fed because they buy stock in the Fed and earn dividends from it.

Board of Governors

The Fed was established in 1913. At that time the largest banks were required to buy stock in the Fed. To prevent these banks from having too great an influence over the Fed, the law also required that the president appoint and the Senate ratify the seven members who make up the Board of Governors. The president selects one of the board members to chair the Board of Governors for a four-year term.

The Board of Governors controls and coordinates the Fed’s activities. It sets general policies for the Federal Reserve and its member banks to follow. Board members and the chairperson are independent of both the president and the Congress. This allows the Board of Governors to make economic decisions independent of political pressure.



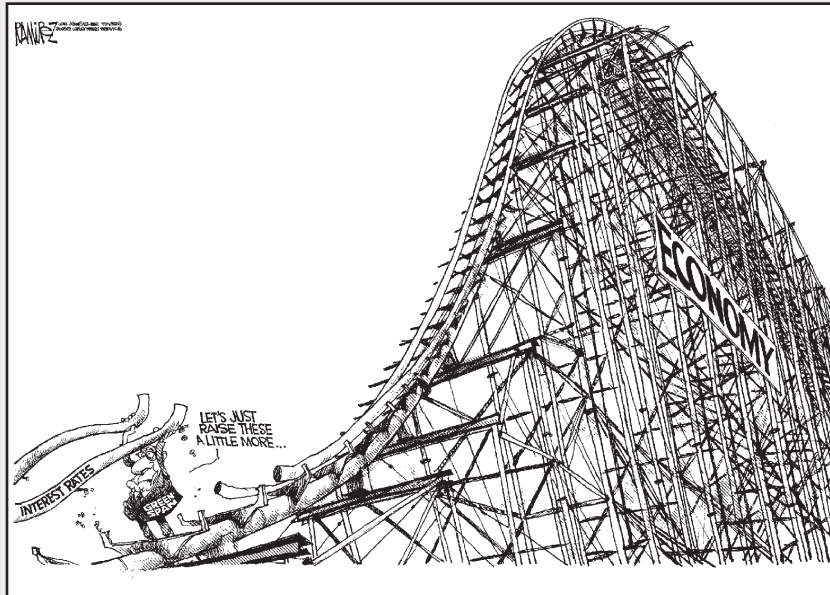
The Fed The headquarters of the Federal Reserve System is in Washington, D.C. The Board of Governors sets the Fed’s policies. **Explaining Why is it important that the Board remain independent of the legislative and executive branches?**

Advisory Councils

The Fed has several advisory councils. One council reports on the general condition of the economy in each district. Another reports on financial institutions. A third reports on issues related to consumer loans. Officials of the district banks serve on these councils.

The FOMC A major policy-making group within the Fed is the **Federal Open Market Committee (FOMC)**. The FOMC makes the decisions that affect the economy as a whole by **manipulating**, or controlling, the money supply. The FOMC has 12 members.

Reading Check Explaining How is the Fed’s Board of Governors chosen?



Michael Ramirez/Copley News Service

In this cartoon, Michael Ramirez makes a comment on the U.S. economy and on the former chairperson of the Federal Reserve, Alan Greenspan.

1. What action is Greenspan taking?
2. What symbol does the cartoonist use to represent the economy?
3. Why do you think the cartoonist chose this symbol?
4. Do you think the artist approves of Greenspan's action? Explain.

Every year, more than half of all Americans do volunteer work. role in it. One of the responsibilities of citizens is to help make their of volunteer groups small. Perhaps...

Functions of the Fed

Main Idea The Fed controls the money supply, serves as the government's bank, and watches over the banking industry.

Economics & You Can money ever be "cheap" or "expensive"? Read to find out how the Fed can raise or lower the "price" of money.

The Fed has two main regulatory functions: it deals with banking regulation and consumer credit.

The Fed as Regulator

The Fed oversees and regulates large commercial banks. If two national banks wish to merge, the Fed will decide whether the action will lessen competition. If so, the Fed could block the merger. It also regulates connections between American and foreign

banking and oversees the international business of banks that operate in this country.

The Fed also enforces many laws that deal with consumer borrowing. For example, lenders must spell out the details of a loan before a consumer borrows money. The Fed specifies what information lenders must provide.

Acting as the Government's Bank

The Fed also acts as the government's bank. First, it holds the government's money. Government revenues are deposited in the Fed. When the government buys goods, it draws on these accounts. Second, the Fed sells U.S. government bonds and Treasury bills, which the government utilizes to borrow money. Third, the Fed manages the nation's currency, including paper money and coins. This money is produced by government agencies, but the Fed controls its circulation. When coins and currency become damaged, banks send them to the Fed for replacement.



How Monetary Policy Works

One of the Fed's major tasks is to conduct monetary policy. **Monetary policy** is the controlling of the supply of money and the cost of borrowing money—credit—according to the needs of the economy. The Fed can increase or decrease the supply of money.

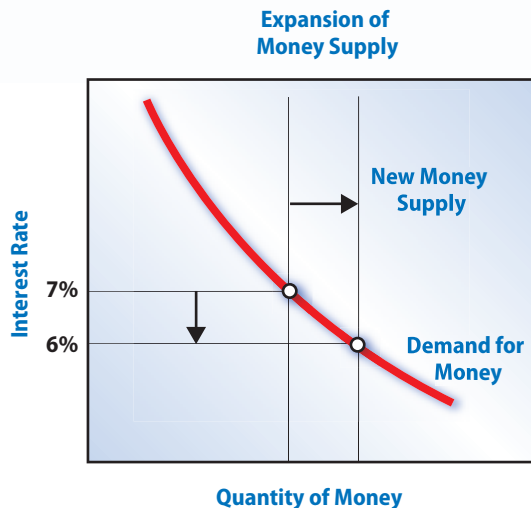
Changing the Supply of Money The supply and demand diagrams on this page help explain monetary policy. Because the amount of money is fixed at any given time, the money supply is shown as a vertical line. In the diagrams, the point where supply of money and demand for money meet sets the interest rate—the rate that people and businesses must pay to borrow money. The Fed can change the interest rate by changing the money supply. So, if the Fed wants a *lower* interest rate, it must expand the money sup-

ply by moving the supply curve to the right. This is shown in diagram A. If the Fed wants to *raise* the interest rate, it has to **contract**, or reduce, the money supply by shifting the supply curve to the left (see diagram B).

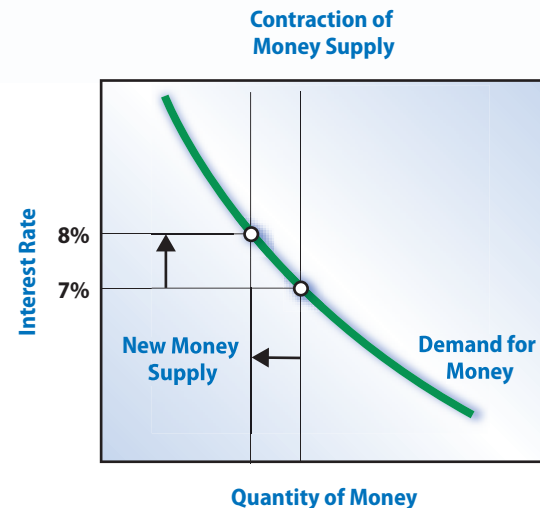
Monetary Policy Tools Several tools help the Fed manipulate the money supply. First, the Fed can raise or lower the **discount rate**. The discount rate is the rate the Fed charges member banks for loans. If the Fed wants to stimulate the economy, it lowers the discount rate. Low discount rates encourage banks to borrow money from the Fed to make loans to their customers. If the Fed wants to slow down the economy's rate of growth, it raises the discount rate to discourage borrowing. This contracts the money supply and raises interest rates. High discount rates mean banks will borrow less money from the Fed.

Monetary Policy and Interest Rates

(A) Effects of Buying Bonds



(B) Effects of Selling Bonds



Analyzing Graphs

1. **Describing** What happens to interest rates when the money supply contracts?
2. **Inferring** Why does the price of credit fall when the money supply increases?



Second, the Fed may raise or lower the **reserve** requirement for member banks. Member banks must keep a certain percentage of their money in Federal Reserve Banks as a reserve against their deposits. This money is called the reserve. If the Fed raises the reserve requirement, banks must leave more money with the Fed, and they have less money to lend. When the Fed lowers the reserve requirement, member banks have more money to lend.

Finally, the Fed can change the money supply through **open market operations**. These are the purchase or sale of U.S. government bonds and Treasury bills. Buying bonds from investors puts more cash in investors' hands, increasing the money supply. This shifts the supply curve of money to the right, which lowers interest rates. Consumers and businesses then borrow more money, which increases consumer demand and business production. As a result, the economy grows. If the Fed decides that interest rates are too low, the Fed can sell bonds.

When people buy those bonds, money comes out of the economy. This shifts the supply curve to the left, and raises interest rates.

Why Is Monetary Policy Effective?

Monetary policy can be implemented quickly and Fed officials can also easily fine-tune its policy. They can watch the results of selling bonds or raising the discount rate. If the desired result has not occurred, they can act again, selling more or fewer bonds or raising or lowering the discount rate.

Interest Rates and Business Interest rates influence business investment and consumer spending. The Fed can affect these activities by manipulating interest rates. For example, if the Fed wants to encourage business investment, it can lower interest rates. Raising rates will have the opposite effect.

 **Reading Check** **Describing** How does the Fed protect consumer borrowers?

Section Review 2

Vocabulary

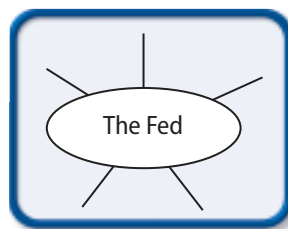
- Create** a fill-in-the-blank quiz for a partner using these words: *central bank, Federal Open Market Committee (FOMC), monetary policy, discount rate, reserve, open market operations.*

Main Ideas

- Describing** In what way are member banks the owners of the Fed?
- Explaining** In what ways does the Fed act as the government's bank?

Critical Thinking

- Concluding** What would Fed officials likely do if prices rise too quickly?
- BIG Ideas** On a diagram like the one below, list five of the functions of the Federal Reserve System.



CITIZENSHIP Activity

- Comparing** Contact three banks in your community. Find out what interest rate they are charging on loans for a three-year loan on a new car. Compare this to the current Fed discount rate. Which is higher or lower?
- Expository Writing** Write a short newspaper article that explains how the Fed can use its powers to encourage or discourage business activity.



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Section
3

How Banks Operate

Guide to Reading

Big Idea

Political and economic institutions evolve to help individuals and groups accomplish their goals.

Content Vocabulary

- checking account (p. 667)
- savings account (p. 667)
- certificate of deposit (CD) (p. 667)

Academic Vocabulary

- initial (p. 667)
- principal (p. 667)
- behalf (p. 668)

Reading Strategy

Classifying On a graphic organizer like the one below, identify three types of bank deposits.



Real World Economics Imagine what might happen if all your money were held in a bank that went bankrupt. This is what happened during the Great Depression in 1929. When the stock market crashed, stock prices fell nearly 25 percent in two days. As banks tried to collect the money investors had borrowed and invested in the stock market, many people lost everything that they owned. Banks went bankrupt, too.

▼ Wall Street speculator tries to sell his car to make up for losses



NORTH CAROLINA STANDARDS
Civics and Economics

- 8.08** Evaluate the investment decisions made by individuals, businesses, and the government.
- 8.09** Describe the role of money in trading, borrowing, and investing.



Banking Services

Main Idea Banks offer important financial services to millions of people.

Economics & You Do you know the difference between a savings and a checking account? Read to find out how these accounts differ.

Banks are started by investors. They pool financial investments, money, property, and other funds to provide banking services to people in their communities. If 10 investors each put up \$10,000, the new bank would have \$100,000 in funds.

A bank that relied on only the funds raised by its **initial**, or first, investors would not grow. It would have a limited amount of money available for loans. Banks need to attract depositors to survive.

What Banks Do

To earn money, banks accept deposits to create different types of accounts and then use these deposited funds to make loans.

Accepting Deposits Banks hope to attract customers who make deposits. They offer **checking accounts**, which allow customers to write checks or to use check or debit cards. Checks can be used to pay bills or to transfer money from one person to another. These accounts, however, usually pay no or only a low rate of interest. People do not keep money in checking accounts for very long. They deposit the money and then use the funds to meet their regular expenses.

Sometimes people have some money that they can leave untouched for longer periods of time. With **savings accounts**, banks pay interest to customers based on how much money they have deposited. Because the bank pays interest, the money grows larger the longer it is left in a savings account.

Banks also offer **certificates of deposit (CDs)** to customers. CDs require a saver to



Banking Transactions A New York City bank in the early 1930s handles the day-to-day transactions of its customers. **Explaining** What are the advantages of a checking account?

deposit his or her funds for a certain period of time. CDs offer higher interest rates than checking accounts or savings accounts. The longer the maturity—the period of time—the higher the interest rate that the bank pays. Depositors cannot withdraw their money any sooner unless they pay a substantial penalty. Thus they lose control of their money for some time.

Making Loans One of the **principal**, or main, activities of banks is to lend money to businesses and consumers. Loans can actually increase the supply of money.

Suppose that Maria deposits \$1,000 in the bank. The bank can use some of that money to make loans to other customers. Those people then deposit the money they have borrowed, and that money, too, can be loaned to new customers. In that way, the amount of money in circulation continues to accumulate.

Reading Check Explaining Where do banks get the money they loan to customers?



Andres Mendoza

Andres Mendoza, 16, of George, in the state of Washington, is all business when it comes to . . . well, business. So he signed up for a weeklong camp called Washington Business Week (WBW), which was hosted by Gonzaga University in Spokane.



QUESTION: You're originally from Oaxaca, Mexico?

ANSWER: My family moved to the United States four years ago. We didn't speak English, but luckily we learn really fast; it wasn't as difficult as it seemed.

Q: What's up with WBW?

A: WBW shows what's involved in working for a business—or running your own.

Q: What did you do there?

A: We formed mock companies. I was named Chief Executive Officer—or CEO—of my company. Everyone had to develop ideas for new products—ours was a microwave that not only warmed but also *froze* the food.

Before going to WBW, I really had no idea what went into running a business. I thought everything was about making money. But at WBW, you learn there's so much more to it—like behaving ethically.

For more info on Washington Business Week go to www.wbw.org.



Making a Difference

CITIZENSHIP

Analyzing Do you think there is a market for Mendoza's product? Explain.

Changes in Banking

Main Idea Throughout American history, banking has become safer and more efficient.

Economics & You Look closely at a dollar bill. Who issued it? Read to find out why this was not always the case in the United States.

The banking system of the United States has changed through the years. Often, crises led to key developments that helped strengthen American banks and safeguard the rights of citizens.

Early Banking

In the early days of our nation, leaders found that the country needed a central bank to bring order to the nation's finances. The Bank of the United States, chartered in 1791, collected fees and made payments on behalf of, or on the part of, the federal government. In 1816, the Second Bank of the United States was chartered for 20 years. The Bank, however, aroused much opposition, and when its charter lapsed, it was allowed to go out of business.

After that, the only banks in the nation were those chartered by the states. Because the federal government did not print paper currency until the Civil War, most of the money supply was paper currency that privately owned, state-chartered banks issued.

The end of the Bank of the United States removed a vital check on the activities of state-chartered banks. Freed from the Bank's regulations, private banks expanded the volume of bank notes, leading to an increased money supply and inflation.

The National Banking Act In 1863, Congress passed the National Banking Act. Federally chartered private banks issued national banknotes, or national currency, which were uniform in appearance and backed by U.S. government bonds.



The Federal Reserve The National Banking Act corrected some of the weaknesses of the pre-Civil War banking system. Bank crises, however, did not disappear. The Panic of 1907 resulted in the passage of the Federal Reserve Act of 1913, which you read about earlier in this chapter.

The Great Depression The Great Depression of the 1930s dealt a severe blow to the banking industry. When Franklin D. Roosevelt became president, he closed all banks. Each bank was allowed to reopen only after it proved it was financially sound. Congress established the Federal Deposit Insurance Corporation (FDIC), which insured funds of individual depositors.

Recent Developments

Several more recent developments have also changed the face of American banking. Among these were the savings and loan crisis and congressional legislation.

The Savings and Loan Crisis In the late 1970s Congress began to ease regulation of banking activities. Savings and Loans (S&Ls) were allowed to make higher-risk loans and investments. When these investments went bad, hundreds of S&Ls failed in the late 1980s and early 1990s. Because the federal government insured the savings of most depositors, the cost of bailing out these institutions cost taxpayers an estimated \$200 billion. As a result, the FDIC intervened and took over regulation of the S&L industry.

The Gramm-Leach-Bliley Act The Gramm-Leach-Bliley Act, passed in 1999, permits bank holding companies greater freedom to engage in a full range of financial services, including banking, insurance, and securities. The act also requires all financial institutions to establish safeguards to protect their customers' personal financial information.

 **Reading Check Identifying** Which banks issued paper currency before the Civil War?

Section Review 3

Vocabulary

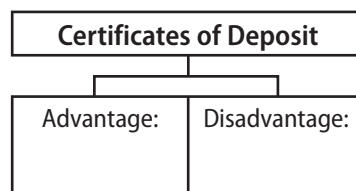
- Write** a paragraph about the activities of a bank using each of these terms: *checking account*, *savings account*, *certificate of deposit (CD)*.

Main Ideas

- Describing** How do bank loans increase the supply of money?
- Explaining** What effect did the National Banking Act of 1863 have on banking in the United States?

Critical Thinking

- Predicting** What do you think would happen if everyone who had money deposited at a bank wanted to withdraw it at the same time?
- BIG Ideas** Using a diagram like the one below for certificates of deposit, compare the advantages and disadvantages of putting money into CDs.



CITIZENSHIP Activity

- Comparing** Obtain brochures from at least three banks that explain the banks' services to customers. How are the services alike? How are they different?
- Creative Writing** Use what you learned in this section to write a TV or radio commercial for a bank, stressing its services.



Study Central™ To review this section, go to glencoe.com.

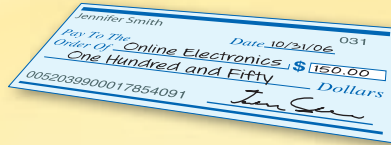


Financial Literacy

Life of a Check

A check is a written order directing your bank to transfer money from your account to the account of whomever receives your check. Millions of checks are moved around the country, sorted, tabulated, and credited or debited to the accounts of financial institutions. This is known as check clearing.

1. Jennifer has a checking account with Home Bank of Detroit, Michigan. She buys a CD player for \$150 from Online Electronics.



2. Online Electronics deposits the check in its account with City Bank of Toledo. City Bank credits Online Electronics' account + \$150.



3. City Bank of Toledo sends the check electronically to the Federal Reserve Bank of Chicago to be cleared.



4. FRB of Chicago credits City Bank of Toledo (Online Electronics' financial institution) + \$150.



6. Home Bank then pays FRB of Chicago \$150 and it reduces (debts) Jennifer's account by \$150. She receives a summary statement.



5. After processing, FRB of Chicago sends the check to Home Bank (Jennifer's financial institution).



The circular flow chart illustrates the steps a check takes as it goes from a purchase through the Federal Reserve System, and back to your bank.

Analyzing Economics

1. **Explaining** What does the statement "my check cleared" mean?
2. **Explaining** You receive \$50 and deposit it into your bank. What is one way to make sure this transaction was completed?

Visual Summary

What is money?

- anything that people are willing to accept in exchange for goods
- a measure of value
- part of the broad financial system
- a medium of exchange
- a store of value



U.S. Treasury worker

What is the Federal Reserve?



The Federal Reserve

- serves as the nation's central bank
- regulates commercial banks
- wields a great deal of power in our economy
- affects business through its decisions
- controls monetary policy

A bank ATM customer



What do banks do?

- provide services to consumers, such as savings and checking accounts and CDs
- make a profit by lending deposited money to consumers



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North Carolina End-of-Course Test Civics and Economics Practice

TEST TAKING TIP

Try not to go back and change your answers unless you are very sure they are wrong. Usually your first thought is your best thought.

Reviewing Vocabulary

Directions: Choose the word(s) that best completes the sentence.

- _____ includes both coins and paper money.
 - Bank notes
 - Currency
 - Checking accounts
 - Federal Reserve notes
- An institution owned and operated by its members that provides low-interest loans to its members is called a _____.
 - credit union
 - commercial bank
 - state bank
 - board of governors
- The interest rate that the Federal Reserve charges on loans to its member banks is the _____.
 - dividend
 - money supply
 - discount rate
 - medium of exchange
- An account in which deposited money can be withdrawn at any time by writing an order is called a _____.
 - savings account
 - checking account
 - discount rate
 - certificate of deposit

Reviewing Main Ideas

Directions: Choose the best answer for each question.

Section 1 (pp. 656–659)

- How do banks and other financial institutions that lend money make a profit?
 - by charging interest
 - by borrowing money
 - by printing currency
 - through promissory notes
- What is the main purpose of the Federal Deposit Insurance Corporation?
 - buy and sell for investors
 - approve changes in the interest rate
 - insure checking and savings deposits
 - make decisions that affect the economy as a whole

Section 2 (pp. 660–665)

- The central bank of the United States is the _____.
 - Board of Governors
 - Federal Reserve System
 - Federal Open Market Committee
 - Federal Deposit Insurance Corporation
- The Fed requires banks to keep a ____, or a percentage of their money.

<ol style="list-style-type: none"> reserve 	<ol style="list-style-type: none"> interest rate
<ol style="list-style-type: none"> discount rate 	<ol style="list-style-type: none"> growth rate

Section 3 (pp. 666–669)

- In what kind of account do savers have the most control over their money?
 - savings accounts
 - certificates of deposit
 - open market operation
 - legal tender

10. A deposit account that requires savers to deposit their money for a certain period of time is a _____.
- A savings account
 - B certificate of deposit
 - C open market operation
 - D legal tender

Critical Thinking

Directions: Base your answers to questions 11 and 12 on the chart below and your knowledge of Chapter 24.

Functions of Money
Medium of exchange
Store of value
Measure of value

11. If you read in the newspaper that the Federal Reserve had just lowered the discount rate, what might you conclude about the economy?
- A The nation is in a financial crisis.
 - B The economy is operating at full capacity.
 - C The Fed wants to discourage bank loans.
 - D The economy is sluggish and needs to be stimulated.
12. Money serves as a measure of value. What does this mean?
- A Your money is safe in a savings account.
 - B Money is a value medium everyone understands.
 - C Money owed must be paid.
 - D CDs are a good investment.
13. To say that money is a medium of exchange means that _____.
- A money is durable
 - B an item for sale is marked with a price
 - C money can be deposited in a bank
 - D a seller will accept it in exchange for a good or service

Document-Based Questions

Directions: Analyze the document and answer the short-answer questions that follow.

Ben S. Bernanke was sworn in on February 1, 2006, as chairman of the Board of Governors of the Federal Reserve System. This passage is from a speech given by Bernanke in November 2006.

Inflation, which picked up earlier this year, has been somewhat better behaved of late. Overall inflation was pushed up this spring by a surge in energy prices, but the recent declines in energy prices have largely reversed those effects. Price inflation for consumer goods and services excluding energy and food, the so-called core inflation rate, has also moderated a bit in the past few months. But the level of the core inflation rate remains uncomfortably high.

—Ben S. Bernanke

14. How does Bernanke characterize the rate of inflation—in positive terms, negative terms, or both? Explain.
15. Is Bernanke calling for any specific action or policy to combat inflation? Based on your reading, what could cause the Fed to take action?

Informational Writing

16. When the Federal Reserve was started, it was to serve the function of a “lender of last resorts.” Do you think banks need the Federal Reserve to act as a lender of last resorts more often during good economic times or bad economic times? Explain.

STOP



For additional test practice, use Self-Check Quizzes—Chapter 24 on glencoe.com.

Need Extra Help?

If you missed question...	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Go to page...	657	658	664	667	658	659	661	665	667	667	664	657	657	660	660	660