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TEORI
EKONOMI MONETER

An Overview of Money

- **Money**

Any asset that is widely accepted for purpuses of exchange, i.e. as payment for goods and services

  - Money is not income, and money is not wealth
  - Money is:
    - A Means of Payment, or Medium of Exchange
    - A Store of Value
    - A Unit of Account

What is Money?

- ***Barter*** is the direct exchange of goods and services for other goods and services.
- A barter system requires a ***double coincidence of wants*** for trade to take place. Money eliminates this problem.

As a ***medium of exchange***, or ***means of payment***,

money is generally accepted by buyers and sellers as payment for goods and services.

What is Money?

As ***a store of value***,
money serves as an asset that can be used to transport purchasing power from one time period to another.

What is Money?

As a ***unit of account***, money is a standard that provides a consistent way of quoting prices.

What is Money?

- Money is easily portable, and easily exchanged for goods at all times.
- The ***liquidity property of money*** makes money a good medium of exchange as well as a store of value.

Characteristics of MONEY

Acceptability -- people must be willing to accept it as a means of payment and in settlement of a debt

Durability -- must last a reasonable length of time before deteriorating

Divisibility -- to function as money an asset must be capable of division into smaller units to accommodate transactions of differing value

Characteristics of MONEY

- **Portability / Convenience -- ** to function as money an asset must be portable and easy to use, it must be light, small to carry around and easy to transfer ownership
- **Uniformity** -- money of the same value must be of uniform quality
- **Stability of Value** -- in order to fulfil its various functions (especially as a store of wealth and as a means of evaluating future payment), it must retain its value
- **Hard for Individuals to Produce Themselves** -- it must be hard to forge

Categories of Money

- Kartal
  - Materials:
    - Logam
    - Kertas
  - Issued by:
    - Negara
    - Bank Sentral
- Giral
  - Primary deposit
  - Derivative deposit
  - Loan deposit

FORMS of MONEY

- **Commodity Money** – **money that takes the form of a commodity with intrinsic value**. Something that performs the function of money and also has alternative, non-monetary uses, e.g., gold, silver, cigarettes. For hundreds of years gold could be used directly to buy things, but it also had other uses ranging from jewelry to dental fillings.
- **Fiat Money/token money** -- **money without intrinsic value that is used as money because of government decree**.

  Something that serves as money but has no other important uses, e.g., Coins, currency and checkable deposits (current account)

Definition of Money Supply (M1, M2 and M3)

- Definition of Money Supply:

the quantity of money available in the economy

- Definition of Monetary Policy:

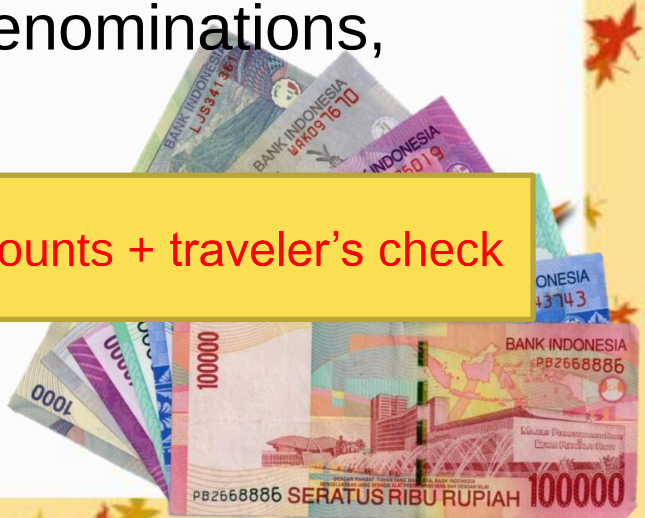
the setting of the money supply by policymakers in the central bank

Definition of Money Supply (M1, M2 and M3)

M1 – the narrowest definition of money supply, consists of currency outside banks plus checking accounts plus traveler's checks

- Currency held outside banks – includes coins and paper money in the hands of public
- Checking accounts – balances can be withdrawn by using check
- Traveler's check – issued in specific denominations, these are treated as cash

M1 = currency held outside banks + checking accounts + traveler's check



Definition of Money Supply (M1, M2 and M3)

M2 – A broader definition of money supply, it includes all of the components of M1 plus time deposits and savings deposits

* Time deposits (fixed deposits) – interest-earning deposits with a specified maturity, which are subject to penalty for early withdrawal
* Savings deposits – interest-earning deposits with
  no specific maturity
* M2 = M1 + time deposits + saving deposits

Definition of Money Supply (M1, M2 and M3)

M3 = **M2** + deposits with **non-bank financial institution** (e.g., deposits of finance companies and post office saving)

Credit Card ???

- is not a form of money; when a person uses a credit card, he or she is simply deferring payment for the item
- serves as a temporary medium of exchange but not a store of value

Banking

Badan usaha yang menghimpun dana dari masyarakat dalam bentuk simpanan dan menyalurkan kepada masyarakat dalam rangka meningkatkan taraf hidup rakyat banyak.
(UU perbankan No. 7/1992)

Structure of Banking System

Central bank :

- an institution designed to oversee the banking system and regulate the quantity of money in the economy

Financial institution :

- privately owned institutions that serve the general public
- intermediaries that stand between savers from whom they accept deposits ;
- and investors to whom they make loans

Banking

Types of Bank:

1. Central Bank (Bank Sentral)
2. Commercial Bank (Bank Umum)
3. Saving Bank (Bank Tabungan)
4. Development Bank (Bank Pembangunan)
5. Rural Bank (Bank Desa)

Strategic Objectives of Bank Indonesia

- Maintain monetary stability
- Maintain the financial sustainability of the Bank of Indonesia
- Strengthen the effectiveness of monetary management
- Create a sound and effective banking system and financial system stability
- Maintain the security and effectiveness of the payment system
- Increase the effectiveness of Good Governance implementation
- Strengthen the organization and build highly competent human resources with the support of a knowledge-based work culture
- Integrate the Bank of Indonesia's transformation in line with Bank Indonesia's destination statement of 2008

Credit Creation

- To explore a process on how banks create money.
- To understand this process, you need to be familiar with some basic principles of accounting.
  - Assets are things a firm owns that are worth something. Most important among a bank's assets are its loans.
  - A firm's liabilities are its debts-what it owes. A bank's most important liabilities are its deposits.
  - Deposits in banks are considered as liability in banks' balance sheet
  - As deposits are held in banks, the behaviour of banks can influence the quantity of deposits in the economy, and therefore, the money supply

Money Creation
Fractional-Reserve Banking

- Definition of fractional reserve banking:
  - **a banking system in which banks hold only a fraction of deposits as reserves**
- Definition of Reserve Ratio:
  - **the fraction of deposits that banks hold as reserves**
- Bank reserves consist of cash in the bank plus its deposits at central bank (BI)
- The required reserve ratio is the ratio of reserves to deposit that banks are required, by law, to hold

A bank's required reserve = deposits x required reserve ratio

Therefore, actual reserves - required reserves = excess reserves

Monetary Policy

- Definition of Monetary Policy**:**
  - **the setting of the money supply by policymakers in the central bank**.
- The mechanics of monetary policy include all the measures which influence
  - the supply of money
  - the price of money (the rate of interest)

Monetary Policy

2 types of monetary policy

- contractionary, restrictive or tight monetary policy
- expansionary or cheap monetary policy

Aims of monetary policy

- to maintain stability of domestic prices
- fluctuating prices will cause disturbances in economy
- to achieve higher rates of economic growth
- to eliminate fluctuations in productions and employment
- if demand is too low, workers will be retrenched; unemployment will occur
- to achieve full employment of resources

Tools of Monetary Control

- **Quantitative tools** - includes the required reserve ratio, the discount rate and open market operations where the central bank can estimate what amount of money supply will be affected.
    1. ***Open-Market Operation (OMO)***
    2. ***Reverse Requirement***
    3. ***Discount Rate***
    4. ***Funding***
    5. ***Special Deposits***

Tools of Monetary Control

Qualitative tools

- Selective Credit Control
- Moral suasion
- Special directives
- Interest rate policy
- Mortgage control

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