

Solution Manual for Economics of Money Banking and Financial Markets 10th Edition by Mishkin ISBN 0132770245 9780132770248

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PART ONE

Introduction

Organization of the Instructor's Manual

To help instructors cope with the increased demands for good teaching in recent years, *The Economics of Money, Banking, and Financial Markets*, Tenth Edition, includes the most comprehensive package of supplementary materials of any money, banking, and financial markets textbook. As part of these supplemental materials, I have designed the Instructor's Manual to help save you time in preparing class materials, such as class outlines, solutions to homework problems, lecture notes, and overhead transparencies.

This Instructor's Manual is divided into four parts. Part One discusses how to use the Instructor's Manual and the other textbook ancillaries to make your teaching of the money and banking course both more effective and less time-consuming. Part Two contains an overview of all the textbook chapters along with teaching tips that I have found effective. Part Three contains the answers to the end-of-chapter problems for use by the instructor to prepare solution sets for the problems he or she assigns to the students as problem sets. Part Four contains transparency masters of chapter outlines, which can be used either to make overhead transparencies for use in class or to make handouts for the students.

To obtain any of the available ancillaries, adopters of the text just need to get in touch with their Pearson sales representative, or alternatively they can visit the Instructor's Resource Center at www.pearsonhighered.com/irc.

Alternative Course Outlines

There are many different ways to teach a course on money, banking, and financial markets. For this reason, the material in *The Economics of Money, Banking, and Financial Markets*, Tenth Edition, has been arranged with flexibility in mind, so that many teaching styles can be accommodated. The following sections suggest sample outlines for four main approaches to teaching money, banking, and financial markets, showing how the text can be adapted to each approach, as well as to quarter and semester teaching schedules. Note, however, that many variations on these outlines are possible.

Chapter No. Chapter Title

1. Why Study Money, Banking, and Financial Markets?
2. An Overview of the Financial System
3. What Is Money?
4. Understanding Interest Rates
5. The Behavior of Interest Rates
10. Banking and the Management of Financial Institutions
11. Economic Analysis of Financial Regulation
12. Banking Industry: Structure and Competition
13. Central Banks and the Federal Reserve System
15. Tools of Monetary Policy
16. The Conduct of Monetary Policy: Strategy and Tactics
22. Aggregate Demand and Supply Analysis
23. Monetary Policy Theory

For a one-semester course, cover any six of the following optional chapters:

Chapter No. Chapter Title

6. The Risk and Term Structure of Interest Rates
7. The Stock Market, the Theory of Rational Expectations, and the Efficient Market Hypothesis
8. An Economic Analysis of Financial Structure
9. Financial Crises
14. The Money Supply Process
17. The Foreign Exchange Market
18. The International Financial System
19. Quantity Theory, Inflation, and the Demand for Money
20. The *IS* Curve
21. The Monetary Policy and Aggregate Demand Curves
24. The Role of Expectations in Monetary Policy
25. Transmission Mechanisms of Monetary Policy

Chapter No. Chapter Title

1. Why Study Money, Banking, and Financial Markets?
2. An Overview of the Financial System
3. What Is Money?
4. Understanding Interest Rates
5. The Behavior of Interest Rates
10. Banking and the Management of Financial Institutions
11. Economic Analysis of Financial Regulation
12. Banking Industry: Structure and Competition
13. Central Banks and the Federal Reserve System
15. Tools of Monetary Policy
16. The Conduct of Monetary Policy: Strategy and Tactics
17. The Foreign Exchange Market
18. The International Financial System
22. Aggregate Demand and Supply Analysis
23. Monetary Policy Theory

For a one-semester course, cover any four of the following optional chapters:

Chapter No. Chapter Title

6. The Risk and Term Structure of Interest Rates
7. The Stock Market, the Theory of Rational Expectations, and the Efficient Market Hypothesis
8. An Economic Analysis of Financial Structure
9. Financial Crises
14. The Money Supply Process
19. Quantity Theory, Inflation, and the Demand for Money
20. The *IS* Curve
21. The Monetary Policy and Aggregate Demand Curves
24. The Role of Expectations in Monetary Policy

25. Transmission Mechanisms of Monetary Policy

A one-quarter course would probably not include any other chapters unless some of the chapters on central banking and the conduct of monetary policy (Chapters 13, 15, and 16) were deleted.

Chapter No. Chapter Title

1. Why Study Money, Banking, and Financial Markets?
2. An Overview of the Financial System
3. What Is Money?
4. Understanding Interest Rates
5. The Behavior of Interest Rates
6. The Risk and Term Structure of Interest Rates
7. The Stock Market, the Theory of Rational Expectations, and the Efficient Market Hypothesis
8. An Economic Analysis of Financial Structure
9. Financial Crises
10. Banking and the Management of Financial Institutions
11. Economic Analysis of Financial Regulation
12. Banking Industry: Structure and Competition

For a one-semester course, cover any seven of the following optional chapters:

Chapter No. Chapter Title

13. Central Banks and the Federal Reserve System
14. The Money Supply Process
15. Tools of Monetary Policy
16. The Conduct of Monetary Policy: Strategy and Tactics
17. The Foreign Exchange Market
18. The International Financial System
19. Quantity Theory, Inflation, and the Demand for Money
20. The *IS* Curve
21. The Monetary Policy and Aggregate Demand Curves
22. Aggregate Demand and Supply Analysis
23. Monetary Policy Theory
24. The Role of Expectations in Monetary Policy
25. Transmission Mechanisms of Monetary Policy

A one-quarter course would probably only include one or two of the optional chapters.

Chapter No. Chapter Title

1. Why Study Money, Banking, and Financial Markets?
2. An Overview of the Financial System
3. What Is Money?
4. Understanding Interest Rates
5. The Behavior of Interest Rates
13. Central Banks and the Federal Reserve System
14. The Money Supply Process
15. Tools of Monetary Policy
16. The Conduct of Monetary Policy: Strategy and Tactics
22. Aggregate Demand and Supply Analysis
23. Monetary Policy Theory
24. The Role of Expectations in Monetary Policy
25. Transmission Mechanisms of Monetary Policy

For a one-semester course, cover any six of the following optional chapters:

Chapter No.	Chapter Title
6.	The Risk and Term Structure of Interest Rates
7.	The Stock Market, the Theory of Rational Expectations, and the Efficient Market Hypothesis
8.	An Economic Analysis of Financial Structure
9.	Financial Crises
10.	Banking and the Management of Financial Institutions
11.	Economic Analysis of Financial Regulation
12.	Banking Industry: Structure and Competition
17.	The Foreign Exchange Market
18.	The International Financial System
19.	Quantity Theory, Inflation, and the Demand for Money
20.	The <i>IS</i> Curve
21.	The Monetary Policy and Aggregate Demand Curves

A one-quarter course would probably only include three or four of the optional chapters.

Overviews of the Textbook Chapters and Teaching Tips

I have been teaching money and banking now for over thirty years. The overviews and teaching tips in Part Two of the Instructor's Manual are intended to share with you some of my experiences in the classroom with teaching the material in the textbook. The overview and teaching tips for each chapter provide a brief description of the contents of the chapter, discuss the novel features of the chapter, indicate what central points need to be transmitted to the student, suggest teaching tips that I have found useful in class, and provide guidance as to what material can easily be skipped in each chapter.

Answers to End-of-Chapter Problems

Part Three of the Instructor's Manual contains the answers to end-of-chapter problems. Some of these questions require students to look up current data, and in these cases no answers are given; however, for the rest of the questions, the answers are quite complete.

Many instructors will use the end-of-chapter questions for homework assignments, as I do. I have found it useful to hand out answers to the questions provided in Part Three to the students as solutions sets after they have completed their assignments; they find them to be an invaluable study aid. Making up these solution sets for reproduction should be quite easy, either by cutting and pasting from Part Three or downloading the files from the Instructor's Resource Center at www.pearsonhighered.com/irc.

PowerPoint Presentation

Also offered in the instructor's supplement package is a PowerPoint Presentation that contains lecture notes and all the textbook's figures and tables. These slides are comprehensive and outline all the major points covered in the text. The lecture notes have been class-tested successfully—they are the ones that I use in class—and they should help other instructors prepare their lectures as they have helped me.

Please note that unless you have access to PowerPoint version 4.0 or higher you will only be able to project the provided images using the viewer that is included; editing or adding material will not be possible unless you have the software program.

To obtain the PowerPoint files, adopters of the text just need to get in touch with their Pearson sales representative, or visit the Instructor's Resource Center at www.pearsonhighered.com/irc to download the available electronic files.

Readings for Money, Banking, and Financial Markets*

Reading 1

"Is U.S. Federal Debt Too Large?" Pedro Amaral, *Economic Commentary*, No. 2010–10, Federal Reserve Bank of Cleveland, August 24, 2010.

Reading 2

"Evaluating the Relative Strength of the U.S. Capital Markets." Stavros Peristiani, *Current Issues in Economics and Finance* 13(6), Federal Reserve Bank of New York, June 2007.

Reading 3

"The Fate of One-Dollar Coins in the U.S." Sébastien Lotz and Guillaume Rocheteau, *Economic Commentary*, Federal Reserve Bank of Cleveland, October 15, 2004.

Reading 4

"Are Consumers Cashing Out?" Paul W. Bauer and Daniel Littman, *Economic Commentary*, Federal Reserve Bank of Cleveland, October 1, 2007.

Reading 5

"Inflation Expectations: How the Market Speaks." Simon Kwan, *FRBSF Economic Letter* No. 2005–25, Federal Reserve Bank of San Francisco, October 3, 2005.

Reading 6

"Flight to Safety and U.S. Treasury Securities." Bryan Noeth and Rajdeep Sengupta, *Regional Economist*, Federal Reserve Bank of St. Louis, July 2010, 18–19.

Reading 7

"The Yield Curve as a Leading Indicator: Some Practical Issues." Arturo Estrella and Mary R. Trubin, *Current Issues in Economics and Finance* 12(5), Federal Reserve Bank of New York, July/August 2006.

Reading 8

"How Economic News Moves Markets." Leonardo Bartolini, Linda Goldberg, and Adam Sacarny, *Current Issues in Economics and Finance* 14(6), Federal Reserve Bank of New York, August 2008.

Reading 9

"The Price Is Right?" Renee Courtois, *Region Focus*, Federal Reserve Bank of Richmond, Fall 2009, 16–19, 34.

Reading 10

"For Better and For Worse: Three Lending Relationships." Mitchell Berlin, *Business Review*, Federal Reserve Bank of Philadelphia, November/December 1996, 3–12.

Reading 11

"How Will a Credit Crunch Affect Small Business Finance?" Gregory F. Udell, *FRBSF Economic Letter* No. 2009–09, Federal Reserve Bank of San Francisco, March 6, 2009.

Reading 12

“Compensation and Risk Incentives in Banking and Finance.” Jian Cai, Kent Cherny, Todd Milbourn, *Economic Commentary*, No. 2010–13, Federal Reserve Bank of Cleveland, September 14, 2010.

Reading 13

“Going Private.” Vanessa Sumo, *Region Focus*, Federal Reserve Bank of Richmond, Winter 2008, 12–17.

Reading 14

“Perils of Price Deflation: An Analysis of the Great Depression.” Charles T. Carlstrom and Timothy S. Fuerst, *Economic Commentary*, Federal Reserve Bank of Cleveland, February 15, 2001.

Reading 15

“Predicting Crises, Part I: Do Coming Crises Cast Their Shadows Before?” Bharat Trehan, *FRBSF Economic Letter*, No. 2009–29, Federal Reserve Bank of San Francisco, September 21, 2009.

Reading 16

“Reforming the Raters.” Renee Courtois, *Region Focus*, Federal Reserve Bank of Richmond, Spring 2009, 14–19.

Reading 17

“Mortgage-Backed Securities: How Important Is ‘Skin in the Game’?” Christopher M. James, *FRBSF Economic Letter*, No. 2010–37, Federal Reserve Bank of San Francisco, December 13, 2010.

Reading 18

“De-Leveraging and the Financial Accelerator: How Wall Street Can Shock Main Street.” Satyajit Chatterjee, *Business Review*, Federal Reserve Bank of Philadelphia, Second Quarter 2010, 1–8.

Reading 19

“Capital Cushions: The Basel Accords and Bank Risk.” Stephen Slivinski, *Region Focus*, Federal Reserve Bank of Richmond, Spring 2009, 6–9.

Reading 20

“Why Economists Still Worry About Bank Runs.” Doug Campbell, *Region Focus*, Federal Reserve Bank of Richmond, Fall 2005, 36–38.

Reading 21

“Addressing TBTF by Shrinking Financial Institutions: An Initial Assessment.” Gary H. Stern and Ron Feldman, *The Region*, Federal Reserve Bank of Minneapolis, June 2009, 8–13.

Reading 22

“The Costs and Benefits of Bank Supervisory Disclosure.” Edward Simpson Prescott and Stephen Slivinski, *Economic Brief* EB09–05, Federal Reserve Bank of Richmond, May 2009.

Reading 23

“If Fed Becomes Super Regulator, Politicians Would Be Its Kryptonite.” Sharon K. Blei, *The Regional Economist*, Federal Reserve Bank of St. Louis, January 2009, 14–15.

Reading 24

“Federal Preemption of State Bank Regulation: A Conference Panel Summary.” Erin Davis and Tara Rice, *Chicago Fed Letter* 230a, Federal Reserve Bank of Chicago, September 2006.

Reading 25

“Out from the Shadows: The Run on Shadow Banking and a Framework for Reform.” Renee Courtois Haltom, *Region Focus*, Federal Reserve Bank of Richmond, Third Quarter 2010, 22–25.

Reading 26

“U.S. Monetary Policy: An Introduction. Part 2: What Are the Goals of U.S. Monetary Policy?” *FRBSF Economic Letter* No. 2004–02, Federal Reserve Bank of San Francisco, January 23, 2004.

Reading 27

“How’s Business? The Role of the Beige Book in Fed Policymaking.” Renee Courtois, *Region Focus*, Federal Reserve Bank of Richmond, Summer 2009, 5–7.

Reading 28

“Explaining Bank Credit Crunches and Procyclicality.” Robert R. Bliss and George G. Kaufman, *Chicago Fed Letter* No. 179, Federal Reserve Bank of Chicago, July 2002.

Reading 29

“Why Are Banks Holding So Many Excess Reserves?” Todd Keister and James J. McAndrews, *Current Issues in Economics and Finance*, 15 (8), Federal Reserve Bank of New York, December 2009.

Reading 30

“Federal Reserve Liquidity Programs: An Update.” Niel Williardson and LuAnne Pederson, *The Region*, Federal Reserve Bank of Minneapolis, June 2010, 14–25.

Reading 31

“Quantitative Easing: Entrance and Exit Strategies.” Alan S. Blinder, *Review*, Federal Reserve Bank of St. Louis, November/December 2010, 465–79.

Reading 32

“Monetary Policy in a World with Interest on Reserves.” Charles T. Carlstrom and Timothy Fuerst, *Economic Commentary*, No. 2010–4, Federal Reserve Bank of Cleveland, June 10, 2010.

Reading 33

“Conducting Monetary Policy when Interest Rates Are Near Zero.” Charles T. Carlstrom and Andrea Pescatori, *Economic Commentary*, Federal Reserve Bank of Cleveland, October 2009.

Reading 34

“Disagreement about the Inflation Outlook.” Sylvain LeDuc, Glenn D. Rudebusch, and Justin Weidner, *FRBSF Economic Letter*, No. 2009–31, Federal Reserve Bank of San Francisco, October 5, 2009.

Reading 35

“Reflections on Monetary Policy: Flexibility, Transparency, and Inflation.” Michael H. Moskow, *Chicago Fed Letter* No. 230, Federal Reserve Bank of Chicago, September 2006.

Reading 36

“Publishing Central Bank Interest Rate Forecasts.” Glenn D. Rudebusch, *FRBSF Economic Letter* No. 2008–02, Federal Reserve Bank of San Francisco, January 25, 2008.

Reading 37

“U.S. Monetary Policy: An Introduction. Part 4: How Does the Fed Decide the Appropriate Setting for the Policy Instrument?” *FRBSF Economic Letter* No. 2004–04, Federal Reserve Bank of San Francisco, February 6, 2004.

Reading 38

“The Taylor Rule: A Guidepost for Monetary Policy?” Charles T. Carlstrom and Timothy S. Fuerst, *Economic Commentary*, Federal Reserve Bank of Cleveland, July 2003.

Reading 39

“Interest Rates, Carry Trades, and Exchange Rate Movements.” Michele Cavallo, *FRBSF Economic Letter* No. 2006–31, Federal Reserve Bank of San Francisco, November 17, 2006.

Reading 40

“An Anchor of Gold.” Stephen Slivinski, *Region Focus*, Federal Reserve Bank of Richmond, Second Quarter 2010, 5–7.

Reading 41

“Is the International Role of the Dollar Changing?” Linda S. Goldberg, *Current Issues in Economics and Finance*, 16 (1), Federal Reserve Bank of New York, January 2010.

Reading 42

“Dollarization Explained.” Stephen Slivinski, *Region Focus*, Federal Reserve Bank of Richmond, Fall 2008, 2–5.

Reading 43

“The Greek Crisis: Argentina Revisited?” Fernanda Nechio, *FRBSF Economic Letter*, No. 2010–33, Federal Reserve Bank of San Francisco, November 1, 2010.

Reading 44

“Raising Capital: The Role of Sovereign Wealth Funds.” Anna L. Paulson, *Chicago Fed Letter*, No. 258, Federal Reserve Bank of Chicago, January 2009.

Reading 45

“What We Do and Don’t Know about Discretionary Fiscal Policy.” Renee Courtois, *Economic Brief* EB09–04, Federal Reserve Bank of Richmond, April 2009.

Reading 46

“Can the Nation Stimulate Its Way to Prosperity?” Jason Saving, *Economic Letter* 5 (8), Federal Reserve Bank of Dallas, August 2010.

Reading 47

“The Great Moderation: Good Luck, Good Policy, or Less Oil Dependence?” Andrea Pescatori, *Economic Commentary*, Federal Reserve Bank of Cleveland, March 2008.

Reading 48

“U.S. Monetary Policy: An Introduction. Part 3: How Does Monetary Policy Affect the U.S. Economy?” *FRBSF Economic Letter* No. 2004–03, Federal Reserve Bank of San Francisco, January 30, 2004.

Reading 49

“Regulatory and Monetary Policies Meet ‘Too Big to Fail’.” Harvey Rosenblum, Jessica J. Renier, and Richard Alm, *Economic Letter* 5 (3), Federal Reserve Bank of Dallas, April 2010.

Reading 50

“Why Policymakers Might Care about Stock Market Bubbles.” Paul Gomme, *Economic Commentary*, Federal Reserve Bank of Cleveland, May 15, 2005.

Reading 51

“Rising Relative Prices or Inflation: Why Knowing the Difference Matters.” Owen F. Humpage, *Economic Commentary*, Federal Reserve Bank of Cleveland, June 2008.

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Reading 52

"Do Deficits Matter? And, If So, How?" Stephen Slivinski, *Region Focus*, Federal Reserve Bank of Richmond, Second Quarter 2010, 12–15.

Reading 53

"Getting Back on Track: Macroeconomic Policy Lessons from the Financial Crisis." John B. Taylor, *Review*, Federal Reserve Bank of St. Louis, May/June 2010, 165–76.

Reading 54

"Sticky Situation." Doug Campbell, *Region Focus*, Federal Reserve Bank of Richmond, Spring 2005, 20–23.

Reading 55

"Activist Monetary Policy For Good or Evil? The New Keynesians vs. the New Classicals." Tom Stark and Herb Taylor, *Business Review*, Federal Reserve Bank of Philadelphia, March/April 1991, 17–25.

Study Guide

The only way to learn effectively about money, banking, and financial markets is by continual, and active, application of the basic concepts developed in the textbook. To help the student in this endeavor, we provide the *Study Guide*.

The *Study Guide* contains the following elements for each chapter:

Chapter Review:

Each chapter begins with a summary of the chapter. The chapter review is divided into sections based on the section headings provided in the text.

Helpful Hints:

This section provides some additional suggestions and examples to help clarify the more difficult material.

Terms and Definitions:

Students match key terms from the text to their definitions. This section is particularly important because a working economic and financial vocabulary is necessary in order for the student to advance through the material.

Problems and Short-Answer Questions:

We provide a number of multi-step problems that require numerical, graphical, or written solutions. The problems are based on the larger issues developed in the chapter. Smaller issues are addressed with approximately ten short-answer questions.

Critical Thinking:

This section provides a single multi-step problem that is an application of one of the major issues developed in the chapter.

Self-Test:

The self-test section provides fifteen true/false and twenty multiple-choice questions to validate areas of successful learning and to highlight areas needing improvement.

Solutions:

Detailed solutions for all problems and questions are provided at the end of each chapter.
