How do real interest rates affect economic activity in the short run?

Changes in real interest rates affect the public's demand for goods and services mainly by altering borrowing costs, the availability of bank loans, the wealth of households, and foreign exchange rates.

How does monetary policy affect inflation?

In fact, a monetary policy that persistently attempts to keep short-term real rates low will lead eventually to higher inflation and higher nominal interest rates, with no permanent increases in the growth of output or decreases in unemployment.

Doesn't U.S. inflation depend on worldwide ca[illegible]y, not just U.S. capacity?

In this era of intense global competition, it might seem parochial to focus on U.S. capacity as a determinant of U.S. inflation, rather than on world capacity. For example, some argue that even if unemployment in the U.S. drops to very low levels, U.S. workers wouldn't be able to push for higher wages, because they're competing for jobs with workers abroad, who are willing to accept much lower wages.

How long does it take a policy action to affect the economy and inflation?

The lags in monetary policy are long and variable. The major effects of a change in policy on growth in the overall production of goods and services usually are felt within three months to two years. And the effects on inflation tend to involve even longer lags, perhaps one to three years, or more.

Why are the lags so hard to predict?

Since monetary policy is aimed at affecting people's demand, it's dealing with human responses, which are changeable and hard to predict.

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В 1781 г. образован центральный банк. Закрылся в 1811 г., затем период серьезных споров о роли и функ-

ционировании банков в стране. Во время Гражданской войны правительство начало выпуск не только монет, но и банкнот. В 1907 г. многие банки обанкротились.

EARLY BANKING HISTORY

The history of banking goes back thousands of years. The Babylonians performed many of the banking functions of today, taking deposits, engaging in foreign exchange, and issuing paper with the same functions as checks.

In the United States, however, there were no banks at first, and strict laws limited the number of coins that could be brought to the colonies. Thus, colonists were forced to barter, that is, to trade goods for goods.

The demand for money was so great that Massachusetts issued its own paper money in 1690. Land banks were established to lend money to farmers. Britain ended practices by 1741. In fact, a new bank was formed in Pennsylvania during the American Revolution to finance the war against England.

Alexander Hamilton persuaded Congress to form a central bank in 1781 over the objections of Thomas Jefferson and others. It closed in 1811, only to be replaced in 1816 because state-chartered banks couldn't support the War of 1812. Throughout this period, there was serious debate about the role and function of banking in this country. The battle between the Central Bank of the United States and state banks got really hot in the 1830s. The fight ended when the Central Bank was closed in 1836.

By the time of the Civil War, the banking system was a mess. During the war, coins were hoarded because they were worth more as gold and silver than as coins. The government began printing money that was money only because the government declared it so, not because the material it was made from had any value of its own.

Eventually, the government established federally charted and state-charted banks. In 1907 many banks failed. People got nervous about their money and went to the bank to withdraw their funds. Shortly thereafter, the cash ran out and some banks had to refuse money to depositors.