

Topic:

The Financial sector / Money and Banking

Additional Activities

- Class podcast on [financial sector](#)
- European [debt crises](#)
- [Banking crisis](#)

Important definition: Monetary policy refers to the actions taken by a Central Bank (ECB) to influence the money supply, interest rates, and availability of credit.

Characteristics of Money

- **Durable** – money needs to last a long time in circulation.
- **Divisible** – larger amounts can be broken down into smaller amounts to enable small purchases to be made.
- **Recognisable** – genuine currency should be instantly recognisable with many identifying characteristics.
- **Acceptable** – money is legal tender accepted for purchasing all goods and services.
- **Portable** – money can be easily transported and transferred from one person to another.
- **Scarce** – to ensure money maintains its value it must be relatively scarce / limited in supply.
- **Homogenous** – all denominations of money must be identical to each other

Evaluation of Electronic Money for Banks

Advantages	Disadvantages
• Reduced need for labour (lower costs, more profitable) • Greater efficiency (technology increases productivity)	• More security risks/hacking • Data protection issues • Technological issues

Evaluation of Electronic Money for Consumers

Advantages	Disadvantages
• Convenience - can pay bills anytime • Less expensive • Less crime - than having cash	• Difficulty of use - especially for the elderly • Security risks/hacking - increased fraud • Possible overspending / impulse buying

Evaluation for Cash

Advantages of Cash	Disadvantages of Cash
• Financial Inclusion: Helps older people, rural residents, and low-income households who rely on cash. • Supports Small Businesses: Small retailers and market traders may not afford card payment systems. • Backup During Digital Failures: Useful if card or mobile payments fail due to technical issues or cyberattacks. • Protects Privacy: Cash leaves no digital trail, keeping personal information private. • Emergency Preparedness: Ensures economic activity continues during disasters or power outages.	• Encourages Criminal Activity: Harder to trace, making money laundering and tax evasion easier. • High Maintenance Costs: ATMs and cash infrastructure are expensive to maintain. • Slows Move to Cashless Society: Digital payments are more convenient and efficient. • Declining Demand: Most people now use cards or mobile payments. • Environmental Impact: Producing and transporting cash adds to carbon emissions. • Security Risks: Handling cash increases the risk of theft for individuals and businesses.

Irish Financial Institutions

- **To do:**
 - What bank are you with?
 - How many students in each bank (Calculate % market share)
 - Calculate the HHI to figure out level of market concentration
 - What do the results mean?

2024 OL

- (c) The information below details new rules introduced by the Central Bank of Ireland as to how much can be borrowed by people buying a house for the first time.

2022	First-time home buyers may borrow up to 3.5 times their gross income.
2023	First-time home buyers may borrow up to 4 times their gross income.

- (i) Indicate with a tick (✓) below whether you think the new mortgage borrowing rules has a positive or negative effect on first-time home buyers in the Irish housing market. Explain your answer.

Positive: ☐ Negative: ☐

Explain:

Fintech company Revolut now has over two million users in Ireland and is set to enter the mortgage market by offering mortgage loans to Irish consumers.

Adapted from rte.ie

- (ii) Indicate one possible economic effect Revolut becoming a mortgage lender may have on people applying for a mortgage in Ireland.

Economic effect:

Types of Financial Institutions

Bank	Explanation
Commercial Banks	• Institutions which provide deposit / lending services to personal consumers / business. ◦ Services include, deposit taking, loans, night safes, credit/debit cards, mortgages, advice
Pillar Banks	• AIB is state owned (more than 99%) ◦ Combined with EBS in 2011 • Bank of Ireland is not under state control (gov sold 35% share holding to private investors) • Other commercial banks include KBC and Permanent TSB
Merchant Banks	• Also called wholesale banks, they deal with business sector and underwriting new issues of shares • Providing advice on mergers and take-overs • Providing financial advice for companies • Vide
International Financial Services Centre	• IFSC was established 1987 • Irish and foreign-owned financial organisations • International banking, asset financing, fund management, corporate treasury management, insurance. • Half world's top 50 banks located there • Half the world's top 20 insurance companies

How Banks Create Credit

- Commercial banks accept **cash deposits** from their customers e.g. say €100, for safekeeping.
- These banks know from experience that their customers will only demand back a small amount of these deposits in cash - say 10% because of their use of cheques as an acceptable method of payment.
- Can now use 90% to create credit;
- Use the money multiplier to calculate the overall impact of creation of credit.
 - [Video](#)

$$\text{Increase in credit} = \text{Increase in Cash Deposits} \times \frac{1}{\text{Banks Reserve Ratio}}$$

Numerical example: 4 marks

A person deposits €100 into a bank. The bank's reserve ratio is 10%.
So the bank can create credit as follows:

$$€100^* \times \frac{1}{10\%} = €1,000^* \quad [€100 = €100^*]$$

(1 mark per asterisked figure)

Question: If the same scenario was presented to you, but the Central Bank changed the reserve ratio to **8%**, what would the impact be?

Question 2: Calculate the money multiplier of the amount of credit a bank would credit if the lodgement was 1,000 and reserve ratio was **4%**.

Factors that Impact Banks ability to Create Credit

Bank	Explanation
Future Economic Expectations	- If banks are optimistic about the economy, they are more likely to lend. - If they expect a downturn or financial instability, they may lend less to reduce risk.
Interest Rates / Monetary Policy	Higher rates → borrowing costs rise → Banks may reduce lending. Lower rates → borrowing costs fall → banks may increase lending.
Reserve Ratios	- The reserve is the percentage of deposits banks must keep as cash or liquid assets. - Higher reserve → less money available for lending. - Lower reserve → more money available for lending.
Ability to Raise Capital Internationally	- Banks that can borrow easily from international markets can lend more - Poor global conditions make it harder to raise funds, reducing lending.
Availability of Creditworthy Customers	- Banks only lend to those deemed creditworthy. - If fewer customers are creditworthy, lending decreases.
Customer Cash Deposits	More deposits allow banks to create more credit and increase lending.

Question 15

The Government has published The Finance (Provision of Access to Cash Infrastructure) Bill 2024, which aims to ensure that sufficient and effective access to cash is available across the country.

Adapted from RTE News, (July, 2024)

- (a) (i) Do you agree or disagree with The Finance (Provision of Access to Cash Infrastructure) Bill 2024?
Indicate your choice below by ticking (✓) the relevant box and justify your choice.

Agree	☐	Disagree	☐
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Justify:

- (ii) Outline two factors that affect the amount of credit that Irish retail banks can create.

1.
2.

- (iii) According to the Irish Times, Allied Irish Bank (AIB) is investing €40 million upgrading almost two-thirds of its 170-branch network by the end of 2025.
Outline one economic reason, why, in your opinion, AIB is making this investment.

Economic reason:

Regulation of Banks

- Financial Banking Crash 2008 [video](#)
- [Video](#)

Advantages of Regulating Banks

Advantages	Explanation
To avoid reckless lending	- The Irish Central Bank has limited borrowing to 3.5 times income. - During the Celtic Tiger, borrowers were able to take out excessively large mortgage. - This resulted in large bad debts for banks. Anglo Irish and Irish Nationwide were dissolved.
To protect depositors	- Depositors want to know their savings are safe and can be withdrawn when they want them. - In 2007, large queues of people tried to withdraw deposits from Northern Rock banks, as they lost confidence. Video
To protect borrowers	- If banks fail to regulate banks, they may not operate within the recommended guidelines. - E.g Irish banks, such as KBC illegally moved mortgage holders off low interest tracker mortgages and on to more expensive variable rates. - This cost the borrowers thousands in higher interest payments. 41,000 were impacted by the scandal. By mid 2019, these customers had received 683 million in compensation, thanks to the Central Bank. Video

Exam Q: 2021

KBC Bank Ireland was fined €18.3 million by the Central Bank of Ireland for its role in the tracker mortgage scandal.

Adapted from The Irish Times

- (a) Based upon the above statement outline why it is important for **consumers** that Irish banks are properly regulated by the Central Bank of Ireland.

- (b) Other than the regulation of commercial banks, outline two other **duties** of the Central Bank of Ireland.

1.
2.

The Central Bank of Ireland

- **Oversees / regulates** the banking system to maintain financial stability and provides **protection for depositors and investors**.
- Responsible for the production and **distribution of euro notes and coins**.
- Manages the country's official **external reserves** to ensure financial security.
- Conducts **economic research** and offers policy advice.
- Acts as the **government's banker**, managing its accounts and transactions.
- Accountable to both the Dáil and Seanad for its activities.
- Functions as the **lender of last resort**, providing credit to financial institutions facing difficulties when other funding options are unavailable.

Exam Question

- (a) Explain **two** functions of the Central Bank of Ireland.

1.
2.

Nationalisation of Banks

- **Nationalisation** occurs when the government takes ownership of private enterprises, typically in sectors like banking or utilities, to protect the economy or provide essential services.
- In Ireland, nationalisation became a critical tool during the **2008 financial crisis**.

Evaluation of Nationalisation

Advantages	Disadvantages
• Stability to economy / investor confidence • Availability of credit • Employment / consumer protection	• Increased taxation • Opportunity costs • Shareholders penalised

The European Central Bank

- Established in 1998, based in Frankfurt and responsible for formulating and implementing monetary policy in the Eurozone. [Video](#)

Functions / objectives of ECB

Advantages	Explanation
Price Stability	• This means keeping inflation below but close to 2% over the medium term • Stable prices protect the purchasing power of money, and help create certainty for households and businesses
Implement Monetary Policy	• The ECB decides on interest rates and controls the money supply in the Eurozone. • By raising or lowering interest rates, the ECB can influence borrowing, spending, and investment, helping to control inflation or stimulate economic growth.
Foreign Exchange	• The ECB holds and manages the foreign currency reserves of the Eurozone. • These reserves can be used to influence exchange rates or ensure financial stability during periods of uncertainty.
Manage Official External Reserves	• The ECB holds and manages the foreign currency reserves of the Eurozone. • These reserves can be used to influence exchange rates or ensure financial stability during periods of uncertainty.
Supervision of Credit Institutions	• The ECB plays a role in supervising banks and credit institutions in member states. • This helps ensure the stability of the financial system and reduces the risk of bank failures that could harm the wider economy.
Printing of Euro Banknotes	• The ECB decides how many notes are needed to meet demand across the Eurozone.

Composition of the ECB

Executive Board	President, Vice-President + four other appointees Implements monetary policy Gives instructions to national Central Banks
General Council	Executive Board and governors of all EU member state's Central Banks One member = one vote
Governing Council	Executive Board and governors of Eurozone members' Central Banks Formulates monetary policy

Exam Question 2023

(b) One role of the European Central Bank (ECB) is to formulate monetary policy for the Eurozone.

(i) Explain the term monetary policy.

Interest Rates

- **Interest rates** are the price a borrower pays to **borrow money** and the returns that **savers receive** for saving.
- Irish consumers pay higher mortgage interest rates compared to other eurozone countries. In 2025, the average rate in Ireland is about **4%**, while the eurozone average is lower at 3.59%.
- Mortgage rip off [explained](#)

Factors that determine level of Interest Rates

Low interest rates	High interest rates
• The ECB lowers interest rates during a recession to encourage borrowing and boost spending. • More money enters the economy if the ECB uses Quantitative Easing (QE). • Lower rates make borrowing cheaper for households and businesses. • Saving becomes less attractive as interest earned on deposits decreases. • Mortgage repayments are reduced, helping households save money. • The government pays less to service the national debt. • Lower costs for businesses increase competitiveness. • Lower interest rates encourage firms to invest in growth and expansion.	• The ECB raises interest rates during periods of high economic growth to slow down the economy and reduce inflation. • Money supply decreases if the ECB uses Quantitative Tightening (QT) to reduce economic activity. • Credit cards have high interest rates (up to 20%), making them profitable for banks. • High rates discourage investment by increasing borrowing costs. • Mortgage payments become more expensive, reducing disposable income. • Higher interest rates encourage saving as returns on deposits increase. • Economic growth slows down, and businesses reduce investment. • Rising borrowing costs can lead to higher unemployment.

Newspaper article

Interest Rates in Ireland and the Eurozone: Good News, With a Catch

January 2026 – adapted from recent reporting

The **European Central Bank (ECB)** controls interest rates for countries that use the euro, including Ireland. Over the past year, the ECB **cut interest rates** because inflation started to fall and economic growth slowed (European Central Bank).

What Does This Mean for People?

Lower interest rates are good news for **borrowers**. People with **tracker or variable mortgages** now pay less each month, leaving them with more money to spend. Some people taking out new mortgages may also get slightly cheaper loans (Irish Times).

However, **savers lose out**. When interest rates fall, banks usually pay less interest on savings accounts. This means people earn less money on their savings (Central Bank of Ireland).

Why Could This Be a Problem for Ireland?

Ireland already has a **housing crisis**, with high house prices and not enough homes available. Lower interest rates make it cheaper to borrow money, which can increase demand for houses. This could push prices even higher, making it even harder for young people to afford a home in the future (Irish Times).

While lower interest rates help some people right now, they do not solve Ireland's bigger problems. For the housing crisis, what is really needed is **more homes**, not just cheaper loans.

Exam Question: Deferred Paper 2022

The chart below displays the benchmark interest rate in Ireland from 2008 to 2020.



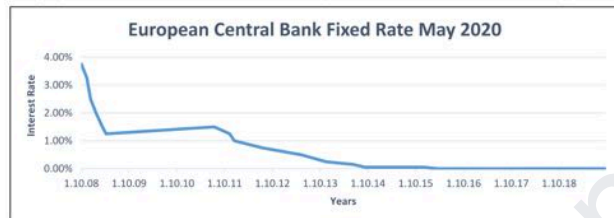
Adapted from the ECB
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(a) Outline **two** key trends in interest rates using data from the above chart.

(b) Explain how current interest rates may affect **borrowers** in Ireland.

Exam Question 2021

The graph below shows the fluctuation in the European Central Bank Fixed Rate as of May 2020.



Adapted from Statista

- (a) Explain the historical reason for this trend in the European Central Bank's interest rate.

- (ii) Calculate the **real rate of interest** if the nominal interest rate was 2.25% and the inflation rate was 5.5%. **Show your workings.**

Workings:

Answer:

- (iii) The number of people using the services offered by Neobanks/Challenger banks such as Revolut and N26 has grown rapidly in Ireland in recent years.

Adapted from RTÉ News

Outline two reasons why so many Irish people have adopted a digital-only bank account such as Revolut.

1.
2.

Impacts of restricting loans/mortgages

- (eg. Bigger deposit required)
- Could ease the trend of rising property prices
- Increased demand for rental properties
- Help stabilise the business cycle / reduce the boom-bust in the cycle
- Could hinder the recovery in the property market
- In January 2015, the Central Bank of Ireland (CBI) introduced restrictions on residential mortgage lending (bigger deposit requirement for mortgage loans and upper limits on borrowing based on income). Economic impacts of these restrictions on the Irish property market.

Why would mortgages accounts be in arrears

- Increased interest rates resulting in increased costs of borrowing
- Increased unemployment
- Economic recession: employees have lower incomes resulting from tax increases/reductions in pay.
- Reckless lending/ borrowing

How Banks can help mortgage arrear customers

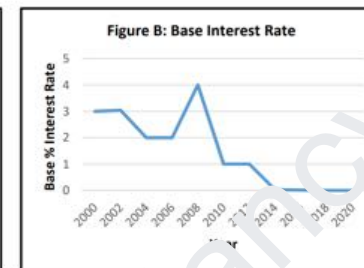
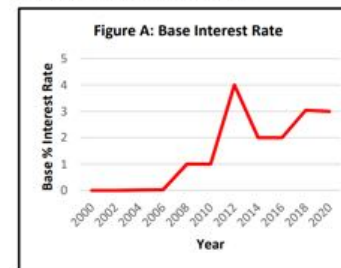
- Reschedule the loan contract
- No penalty payments such as extra interest charges for those in arrears
- Debt / equity swaps: Take partial ownership of the property in return for reduced repayments.
- Debt forgiveness
- Re-value properties at market value and base interest repayments on this value.

Benefits of providing finance under favourable terms (lower interest rates) for SME

- Create jobs / training opportunities
- Encourage entrepreneurship
- Flexible / Able to adapt to changes in market conditions
- Local development improvements
- Government finances improve
- Reduced reliance on FDI

SEC 2022

Only one of the charts below accurately displays the trend in the European Central Bank (ECB) interest rate from 2000 to 2020.



Adapted from ecb.europa.eu

- (a) (i) Identify which chart accurately displays the correct trend in the ECB rate from 2000 to 2020. Choose by means of a tick (✓) one of the boxes below.

Figure A:

Figure B:

- (ii) Justify your choice in (i) above:

Justify:

- (b) Other than setting the base % interest rate outline two other **roles** of the ECB.

1.
2.

Exam Question 2023

Eurozone interest rates increased four times in the last six months of 2022.

Adapted from [ecb.europa.eu](https://www.ecb.europa.eu)

(a) Justify why the European Central Bank (ECB) made this decision.

(b) Does being a member of the Eurozone affect Ireland's ability to implement monetary policy in Ireland? Yes: ☐ No: ☐

Explain your answer.

Explanation: