



**Class Notes for ECON 154-302L – Summer 2000**

**Financial Institutions  
in Canada and the United States**

**Volume I**



**by**

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# 1 Introduction

These two volumes describe historical and present structures of the financial institutions and markets in Canada and in the U.S. Both volumes are used as a one semester ‘Money & Banking’ course with emphasis on the financial institutions’ structures. The course answers the following questions: What is a financial institution? What are its activities? What is the financial market? Who participate in it? What are the instruments - Volume II - dealt in it? What are the government regulations imposed on the financial institutions? Is the present financial system efficient? What can you propose for a better system?

We will start with a ‘dramatis personae’ (i.e., the cast of players) – the financial institutions – which participate in it. For each financial institution we will study its structure, power, functions and its regulations. Then interest will shift to the instruments used in the financial markets and finally a clear distinction between the money and the capital market will be developed. Also, we will study the characteristics, history, powers and objectives of the central bank as a powerful financial institution. We investigate the law and order of financial institutions regulatory bodies as well as the acts pertaining to their function.

How huge the Canadian financial sector is? The Canadian financial sector employs more than 500,000 people with an annual payroll of more than \$22 billion. It exports nearly \$50 billion of services annually and represents 5 per cent of Canada's gross domestic product. The Canadian financial sector yields over \$9 billion annually in tax revenue to all levels of government.

Economy-wide level, the assets of financial institutions are a major source for investment and make the majority of the money supply. Services provided by financial institutions are to almost every individual in the economy.

We will compare all the following points across all financial institutions,

1. History and creation
2. Size and structure
3. Major activities and source of income
4. Federal agencies regulating the financial institution
5. Acts pertaining to the functions of the financial institution

To start, let’s ask a simple question. ‘Why do we need financial institutions?’ Imagine a world without financial institutions. In such a fictional world – often referred to as ‘Robinson Crusoe Economy’ – there exists a gap between borrowers and lenders (savers). To match both characters requires a huge cost. Such a matching cost is the cost of double coincidence of want. Again, even if such a cost is small – i.e., all individuals meet in one place called a market on one given day each week – there exist many risk factors that impinge on the loan contracts. It is very difficult for a lender to monitor the borrower actions and it is costly to undertake credit/risk analysis.