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Why Is The Growth In Commercial Bank Loans Important? And What's Going On Today?

When a bank grants you a loan they create money by crediting your account. This is bank money, not the full faith and credit money created by the Federal Government. As long as the bank is sound, or your account balance is below the current FDIC limit, bank money spends like real money. It's only when a bank fails that you realize you don't have actual US dollars in your account. In reality, you have a guaranteed access to US dollars that is only as good as the FDIC limit or the solvency of the bank.

The bank money created by the loan is destroyed when the loan is paid back. Hopefully the loan was productive and facilitated the creation of a real asset. This is wealth creation, for which bank money is just a tool. Consider the following example:

$100,000 mortgage loan

30 year term

4% interest rate (compounded monthly)

Over the life of this loan, the borrower will pay back to the bank the original $100,000 plus $71,869.50 in interest. The real asset left over, or "wealth created" is the house. Some homes will be worth many times the original investment, some will be destroyed by fire, and some will lose value. What about the interest? Where did it come from?

From 1980 to the financial crisis in 2008, we have collectively borrowed 3 times what we earned. Where does the money come from to pay the interest on these loans? It has to come from somewhere, and there are only two possibilities. One being increased issuance of real money by the federal government, or continued growth in bank loans (borrowing more money to pay the interest on previous loans). Both contribute, but the majority comes from private sector bank loan growth. The private sector is much larger than the government sector. When loan growth "turns down", the economy suffers.

Mosler economics helps us keep up with all types of bank loan growth metrics in the economy. How is the current drop in loan growth (see attached) anything other than a bad omen for the economy?

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Credit check, Fed comment

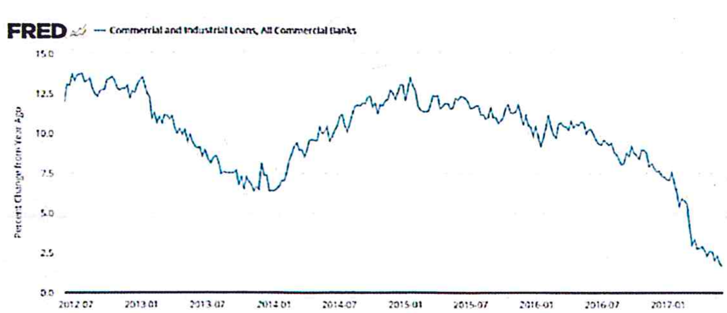
Posted by WARREN MOSLER on June 11, 2017 in Uncategorized

No Comments

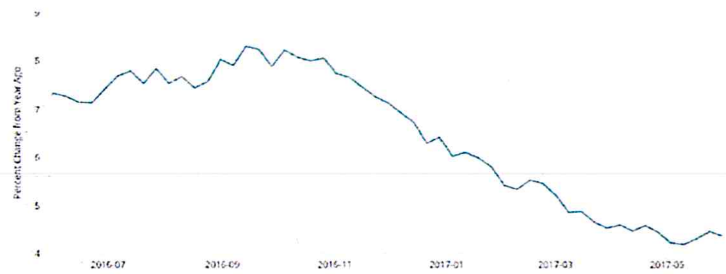
The collapse continues.

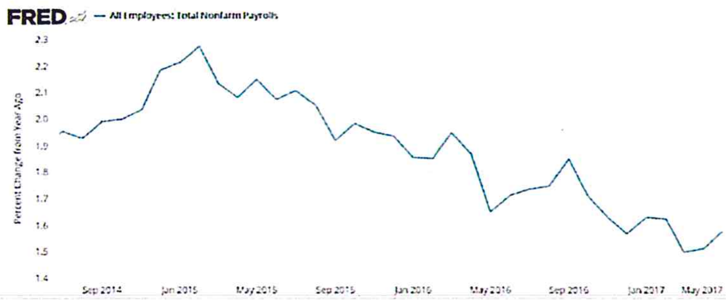
With total bank credit just over $12.5 trillion, it's about $500 billion less than it would have been had last year's loan growth continued.

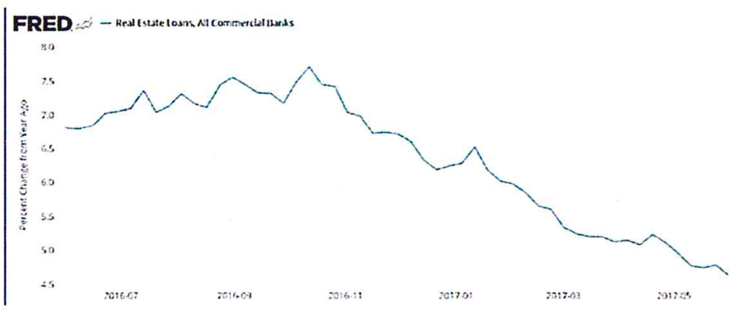
If this lower rate of loan growth continues, and isn't replaced by some other channel that facilitates agents spending more than their incomes, the implication is that GDP could be a full 2% less than last year, as a substantial portion of bank lending finances purchases of real goods and services:



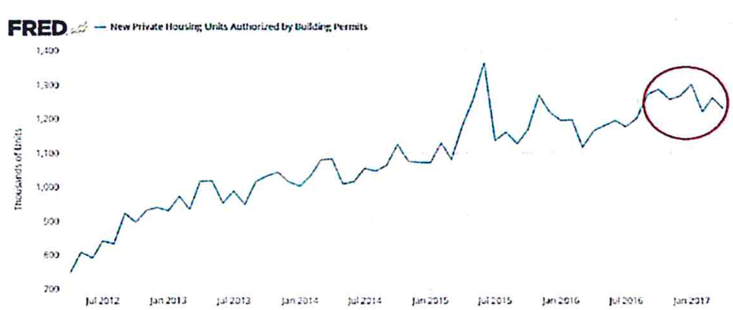
FRED — Bank Credit of All Commercial Banks

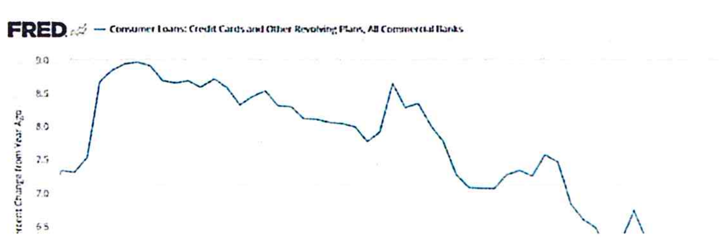


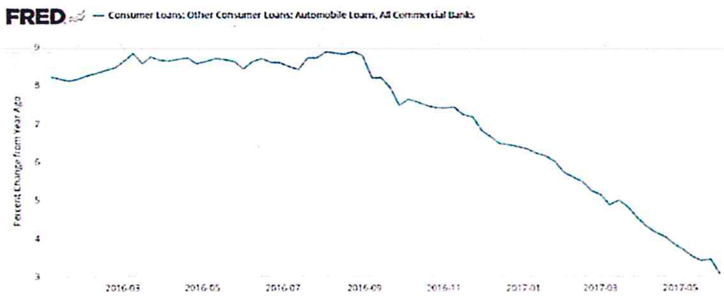

FRED — All Employees: Total Nonfarm Payrolls

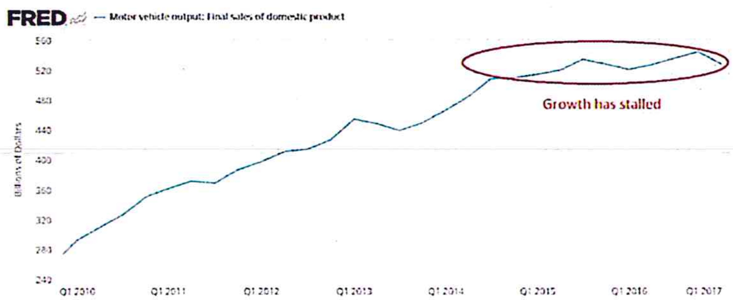

FRED — Real Estate Loans, All Commercial Banks


FRED — Existing Home Sales©
Growth has stalled


FRED — New Private Housing Units Authorized by Building Permits


FRED — Consumer Loans: Credit Cards and Other Revolving Plans, All Commercial Banks





Looks like another rate hike coming from the Fed next week.

Seems to me the Fed models (not mine) tell them rates work through the credit channels, the idea being a rate hike will slow down credit growth and thereby keep the economy from overheating, etc.

But with credit growth as it is per the above charts, seems they are already decelerating.

So what would be the point of a rate hike?

To make credit growth decelerate even faster?

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