Re: Non−Banks versus Banks

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From: William F Hummel (*wfhummel_at_comcast.net*)
Date: 07/22/04

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Date: Thu, 22 Jul 2004 19:36:22 GMT
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On Thu, 22 Jul 2004 10:25:51 −0700, Mike Coburn wrote:

>William F Hummel wrote:
>
>> Coburn would have us believe that when a bank receives a new deposit
>> of $1B, it can immediately lend $10B. In the above example, that
>> would leave the bank $8B short of what it needs to cover checks
>> written against the loan. Absurd on its face.
>
>So in the 10 seconds before the loan is granted the bank borrows
>the $8B and does the deal, or the bank does the deal and then 10
>seconds later borrows the $8B. I have never DEPENDED on this
>after loan borrowing to make my case though I think it quite
>realistic. I have said only that EVEN IF THE BANK ACTUALLY HAD
>TO BORROW to make the loan then the bank would, and does, in fact
>borrow so as to cover the loan.
>
>My major point has been made and not once rebutted by you that
>the FRACTIONAL RESERVE SYSTEM allows banks to routinely support
>loans with only a fraction of the money (10%) ON HAND.

Coburn, there is no ducking what you said. It's on the record, and here are a couple of statements showing what you actually said.

(1) "This notion that a bank must have the dough that it lends BEFORE it can lend is total horse manure. Due to the ability of the bank to borrow whatever it might need at a discount, banks can routinely loan what they do not have."

(2) "That $1B deposit just gave this bank the ability to create $10B in new loans so long as the real assets of the bank (paid in capital) will stand up to the 10 to 1 requirement on bank assets."

Both of the statements are nonsense, and show that your understanding of money and banking is third rate, at best.

In the first statement, your claim that a bank may lend BEFORE it has the dough is total horse manure (to borrow your own phrase). Only if it has sufficient reserves to cover the loan BEFORE it issues the loan would that be feasible.

Also banks can borrow at the discount window only at a penalty rate of at least one percentage point. The notion that banks borrow at the discount window in order to acquire funds to lend is silly. They can borrow funds cheaper in the money market.

In the second statement, you have confused the capital adequacy requirement with the reserve ratio requirement. The 10:1 ratio applies to the reserve requirement, in particular to the ratio of demand deposits to reserves. Reserves are not the same as a bank's capital.

Also the capital adequacy requirement refers to the minimum allowable ratio of the bank's capital (assets − liabilities) to its risk−weighted assets. That requirement is 8%.

As for your fast switch to the subject of FRACTIONAL RESERVE BANKING, there is nothing to refute. No one denies we have a fractional reserve banking system. The problem is you don't understand it.