

# **The problems of modern banking and their affects on society**

## **– Money, Debt and Interest**

Nils Fagerberg

The Global Economy

3 October 2011

# Examples of economic flows of today

- **19 billions SEK/ month**

Monthly average from total development aid, 1960-2009

Source: United Nations

- **240 billions SEK/month**

Monthly average from total debt servicing from developing countries, 2002-2006

Source: Eurodad

- **19000 billions SEK/month**

Monthly average from total bail out costs for saving banks, 2008-2009

Source: United Nations

# Some figures from the swedish economy

- The swedish economic growth during 2010 was the highest since 1964. Sweden is richer than ever!
- 492000 individuals and enterprises are caught in a debtrap (2010) Kronofogdemyndigheten
- 220000 families can not afford enough clothes and food to their children (2010) Socialstyrelsen
- 26 % of individuals between 15 and 24 years are unemployed (2011) Arbetsförmedlingen
- 229 spieces are extinct and further 857 spieces are endangered. Artdatabanken

# The missing link?

Every year we get a little bit richer

Economic growth has been positive for years throughout the world as long as we have used the measure.

The money system



Severe problems which we have difficulty to solve

- Environmental destruction
- Shortage of resources
- Unemployment
- Increasing income gaps
- Deteriorating welfare
- Social maladjustment

• The fundamental problem is how money is created and organised in the modern world!

• The established economic community do not want to open the black box!

# Nils Fagerberg

- M in Ecological Economics, Mälardalen University, 2007.
- B of Social Science, Mälardalen University, 2007.
- M Sc in Forestry, SLU, 1998.

- Consultant for continuous cover forestry
- Teacher in forestry at Linneaus university
- Consultant in ecological economy

- Lectures / talks about ecological economics / monetary systems
- Consultancy assignments
- Ekonomisk Reform
- Thesis about the monetary system

Ulvsåkra

[www.ekologiskekonomi.se](http://www.ekologiskekonomi.se)



Är den svenska valutan anpassad för en långsiktig hållbar utveckling - vilka brister finns och hur kan de åtgärdas?

**EkonomiskReform**  
[www.ekonomiskreform.se](http://www.ekonomiskreform.se)

[www.ekonomiskreform.se](http://www.ekonomiskreform.se)

# Ecological economics

- Based on an interest in adapting economic theory to the laws of nature
- Trying to specify the correct theory, model or system.

# Environmental economics

- Based on an interest to include environmental problems into conventional economic theory
- Trying to specify the correct marketprice of environmental problems

# What are the problems with the money system?

- An understanding of the problems starts with the fact that money is not a law of nature but a social construction!

These are the main problems:

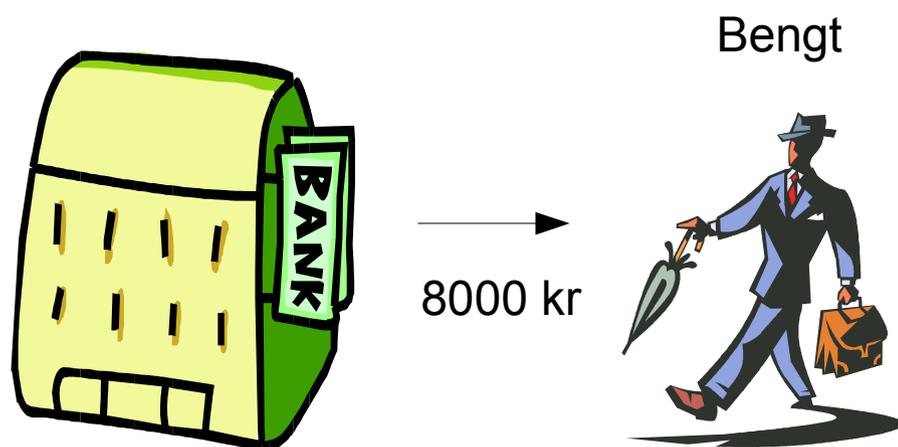
1. Money is created on condition that someone gets into debt.
2. Money is created (owned) by private companies, but its value is guaranteed by society (the state).
3. The income from moneycreation (interest) goes to the banks.

These problems leads to:

1. A constant scarcity of money
2. Some people have to get caught in the debttrap
3. A constant transfer of capital from borrowers to lenders (gap of private means)
4. The scarcity of money creates a demand for economic growth

# How do banks create money?

- The bank has 1000 kr in bills, nothing more.
- The bank gives 8000 kr as a loan to Bengt
- The bank creates 8000 kr out of thin air!

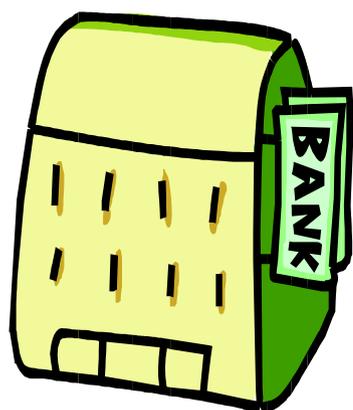


## How is this possible?

First, some things to notice:

- The bank is not creating real money (coins, bills), it is creating credit (digital money based on debt)
- The bank has to follow a reserve requirement. It can only lend when the requirement is fulfilled.
- The bank has an obligation to keep accounts (bookkeeping).

# The bookkeeping of the banks



→  
8000 kr



The balance sheet of the bank:

## 1. Before Bengt gets the loan

Assets:	
Cash:	1000
Lending:	0

Liabilities:	
Deposits:	0
Equity capital	1000

## 2. After Bengt has got the loan

Assets:	
Cash:	1000
Lending:	8000

Liabilities:	
Deposits:	8000
Equity capital	1000

- Bengt gets his money on a deposit account in the bank
- Bengts promise to repay the loan enters the lending account

# There is differences between money and money

- Real money

Coins, bills and central bank means (RIX-system). Money which are created by a central legal authority (the state). Most often without debt as precondition.

- Credit (money)

Moneyunits which are created through indebttness. Most often created by banks.

- A rough estimation on how the swedish moneystock has been created.

Source: Nils Fagerberg, 2005

	Government	Private
Debt as precondition	1%	92%
Debtfree	7%	0%

# The capital reserve requirement

- Reserve requirements (Basel II):

$$8\% < \frac{\text{(capital base) Equity capital}}{\text{(capital requirement) Rated assets}} \qquad 0,08 < \frac{1000 \text{ kr}}{12500 \text{ kr}}$$

- Equity capital does not have to be "real money" (central bank means) Debenture loans and postpositive debts are included.
- Rating (rating of risks depending on borrower)
- Credit is part of the banks equity capital (earned profits)

In other words, the reserve requirement puts very seldom any practical limit on the amount of money a bank is able to create!

# The reserve requirement

*"A bank can get away with an equity capital - real stock capital and earned profits - of 2800 kr for lending 1 miljon kr"*

Stefan Ingves, Governor of Sveriges Riksbank, 09-11-19

**Forget the reserve requirement, in the end, what limits the banks credit creation is the availability of credit worthy and willing borrowers!**

# The control of the key interest rate of the riksbank

- The key interest rate does not put a limit on the amount of credit which can be created.
- The key interest rate steers the price of new credit, therefore it indirectly steers the demand of new credit.

# What happens when Bengt pays off his loan?

The balance sheet of the bank:

## 1. Before Bengt gets the loan

Assets:	
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Liabilities:	
Deposits:	0
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## 2. After Bengt has got the loan

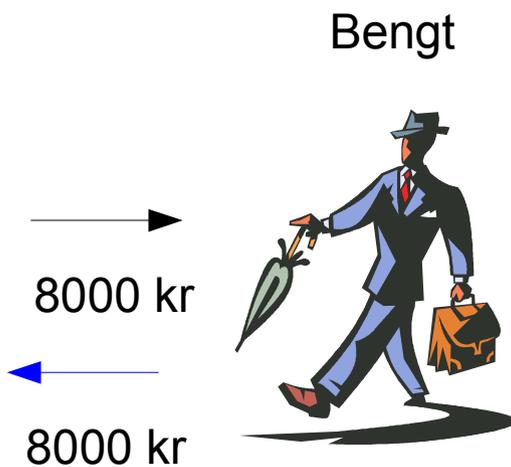
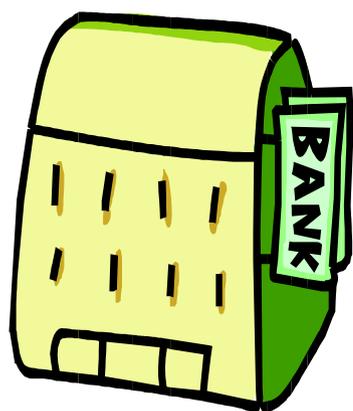
Assets:	
Cash:	1000
Lending:	8000

Liabilities:	
Deposits:	8000
Equity capital	1000

## 3. Bengt pays back his loan to the bank

Assets:	
Cash:	1000
Lending:	0

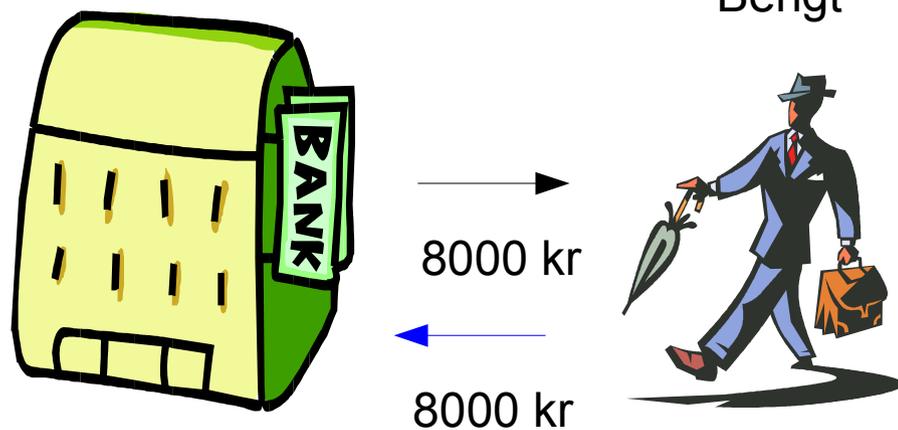
Liabilities:	
Deposits:	0
Equity capital	1000



- Credit disappears !

# But there is one more thing

## - the bank demands interest for its services



$$(8000 * 0,03) = 240 \text{ kr}$$

### 1. Before Bengt gets the loan

Assets:	
Cash:	1000
Lending:	0

Liabilities:	
Deposits:	0
Equity capital	1000

### 2. After Bengt has got the loan

Assets:	
Cash:	1000
Lending:	8000

Liabilities:	
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### 3. Bengt pays back his loan to the bank

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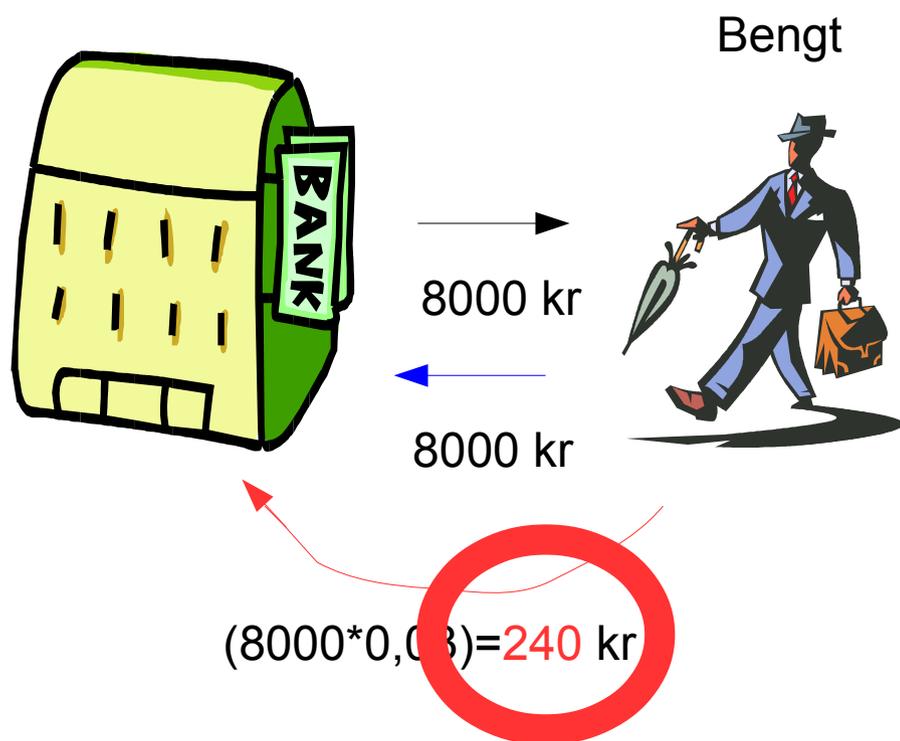
Liabilities:	
Deposits:	0
Equity capital	1000

### 4. Bengt pays interest

Assets:	
Cash:	1240
Lending:	0

Liabilities:	
Deposits:	0
Equity capital	1240

But there is one more thing  
- the bank demands interest for its services



In other words:

A) The principal disappears, but the interest remains and ends up in the bank's profit.

B) The bank creates credit which covers the cost of the principal but does not cover the cost of the interest.

A) The principal disappears, but the interest remains and ends up in the banks profit

- How much interest is payed to swedish banks per year?

- Total deposits in Sweden 2005 were 3 226 000 000 000 kr.
- 3% of total deposits is 96 780 000 000 kr

- Credit is part of the banks equity capital (earned profits)

$$0,08 < \frac{1000 \text{ kr}}{12500 \text{ kr}}$$

$$0,08 < \frac{1240 \text{ kr}}{15500 \text{ kr}}$$

Banks are basically able to create as much money (credit) as they want as long as there are enough trustfully borrowers around to serve the system!

B) The bank creates credit which covers the cost of the principal but does not cover the cost of the interest.

How do people solve the problem when they look for 96 000 000 000 kr which don't exist?

Features of the modern economy:

1. They borrow more money → Indebtness, debt crises, inflation
2. They work harder/expand their bussines/increase income → Economic growth, competition, overtime work, positive trade balance, consumption, new markets
3. Cut costs → Austerity packages, downsizing
4. They give up/bankruptcy → Social maladjustment, unemployment

# What are the problems with the money system?

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# Questions to consider

- Why shall private companies have the right to create official money when its value basically is guaranteed by society?
- Why shall private banks charge a fee for this creation, when risk is taken by society in the end?

# Conclusions

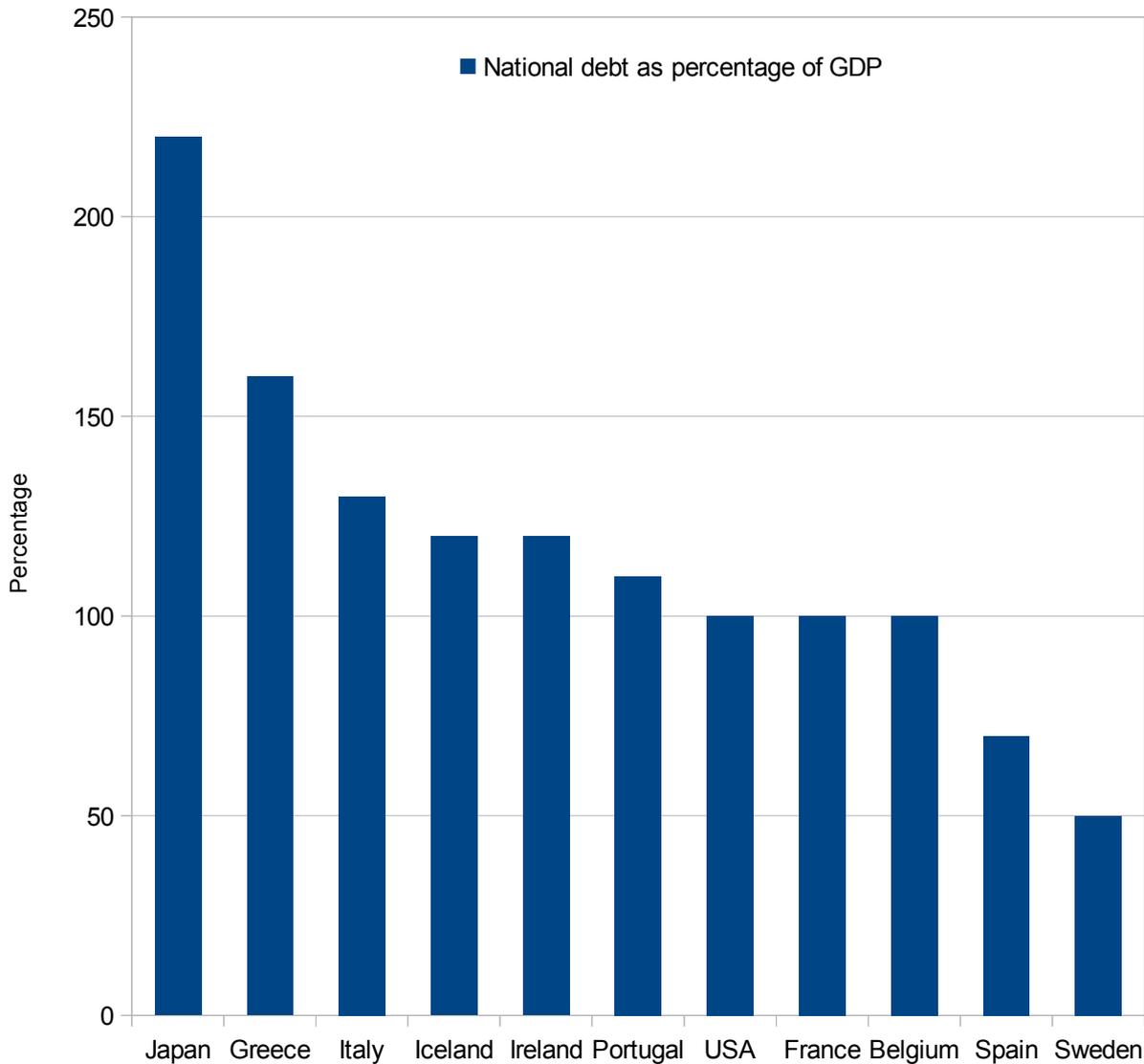
## - consequences for society

The construction of the moneysystem is directly destructive for development. It creates social maladjustment, economic instability and environmental destruction. In these three aspects, the moneysystem forces human development towards a tipping point of chaos.

Major negative impacts are:

- a constantly increasing scarcity of money
- demands on continuous economic growth
- debt trap for individuals, organisations and nations
- escalating income gaps

# The ongoing national debtcrisis



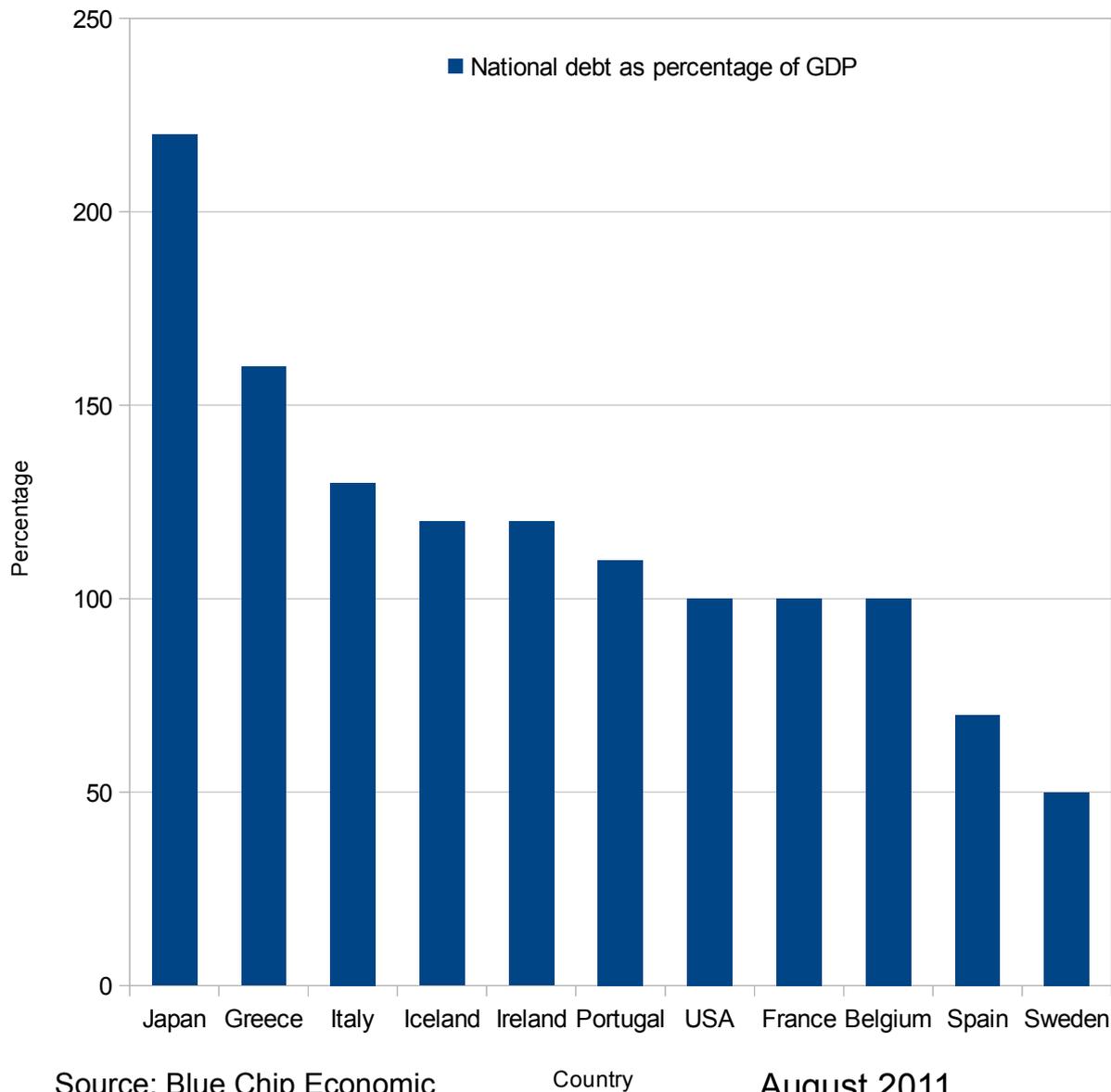
- When a state needs money they sell securities (bonds or promissory notes)

- A national debt consists almost entirely of outstanding bonds and promissory notes

- 90 % of the buyers are banks, insurance companies and non-financial companies.

Swedish market, 2005

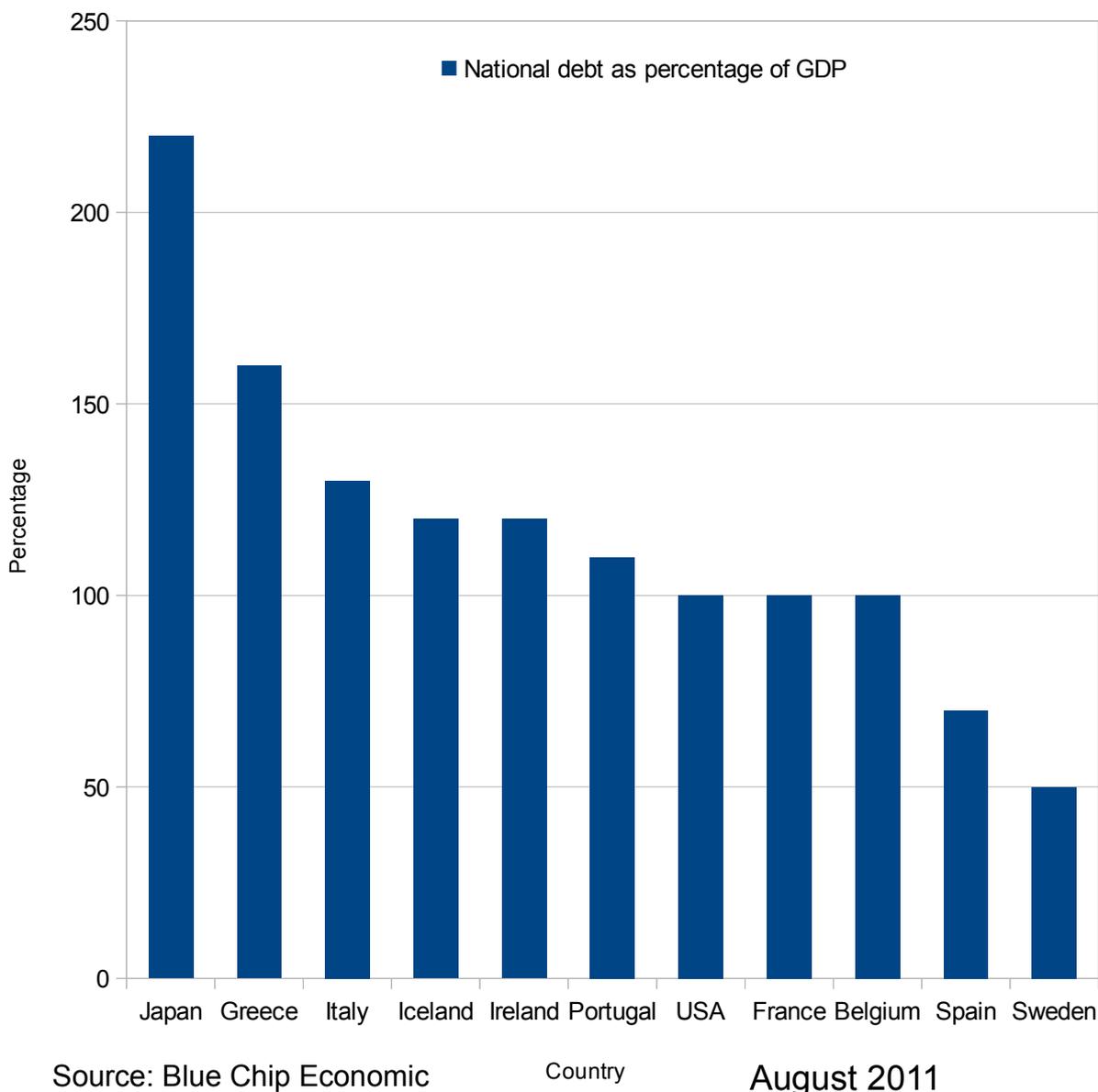
# The ongoing national debtcrisis



Results of this arrangement:

- Banks get interest on their capital requirement reserves.
- In a saturated credit market where noone wants to borrow, the state has to take on debt in order to free new money.
- National debt means taxpayers have to pay interest to banks.
- What happens when a country can not pay its interests any longer?

# The ongoing national debtcrisis



These are the two options:

1) The government stops paying interests on its outstanding debt.

- Owners of the securities pay the price.
- The crisis might well spread to other countries.

2) Government cuts spending in order to please the security market.

- All citizens in the country pay the price.
- The crisis is less likely to spread to other countries.

”They never told us that money is a system of power and that the more dependent we are on money as the mediator of human relationships, the more readily those who have the power to create money and to decide who gets it can abuse that power.”

David Korten, Economist and author, 2010

”The dominant monetary paradigm has been developed over a period of 300 years or more and it is the biggest powercenter that the world has ever known”

Thomas Greco, Monetary researcher and author, 2011

”Of all the many ways of organising banking, the worst is the one we have today”

Mervyn King, Gouvenor of the Bank of England, 2010

”In a time of universal deceit, telling the truth is a revolutionary act”

An example on how difficult it is to discuss this topic

# SVD OPINION

- NYHETER
  - NÄRINGSLIV **Brännpunkt**
  - UR
  - OPINION
  - SPORT
  - RESOR
  - MAT&VI
- 
- BRÄNNPUNKT
  - LEDARSIDAN
  - BLOGGAR
  - KRÖNIKOR/KOLUMNER
  - KORSELD

## Finansiella systemet är omätligt och sjukt



Rekommendera 635

Tweet 14

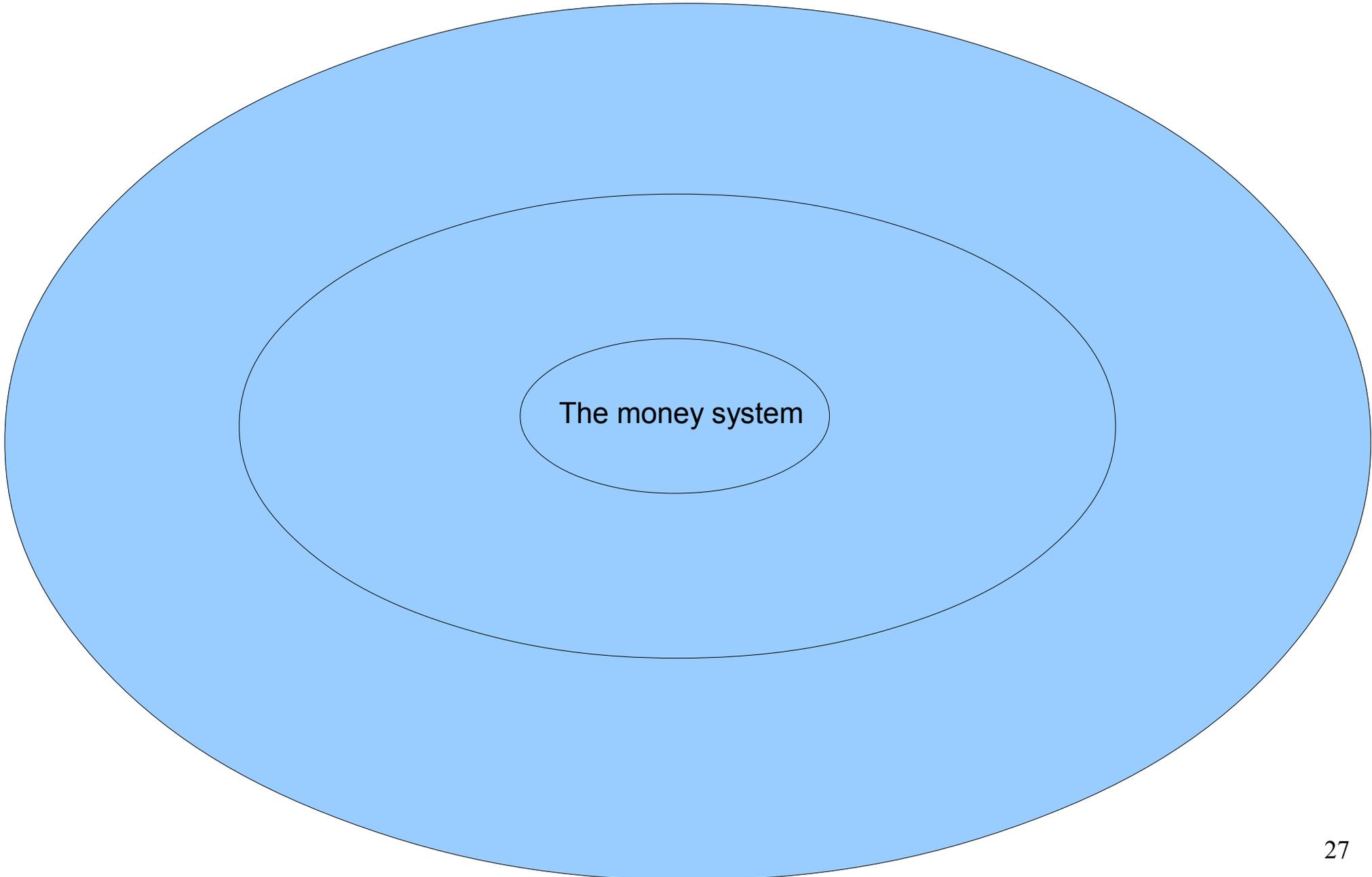
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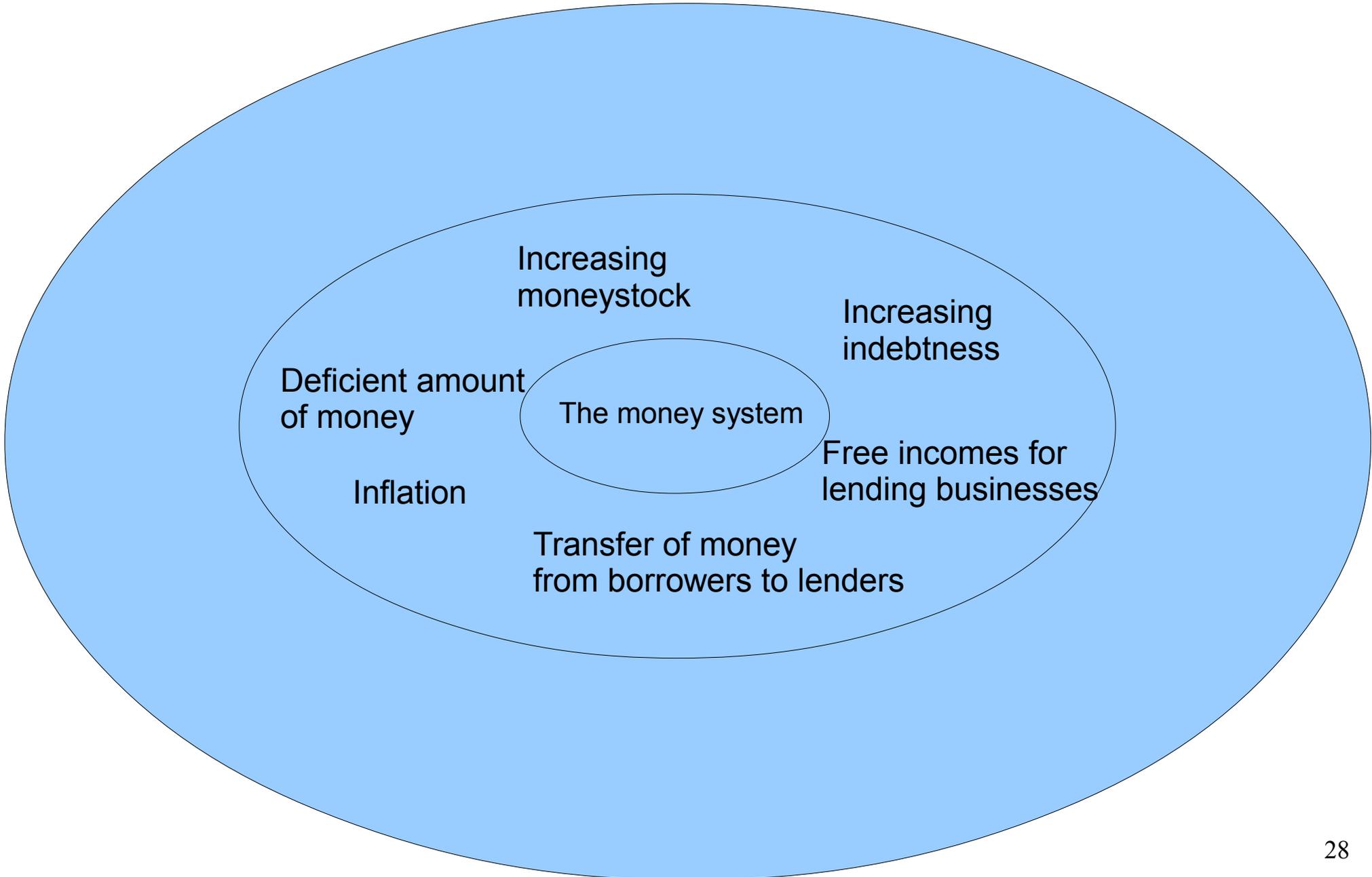
Läs mer



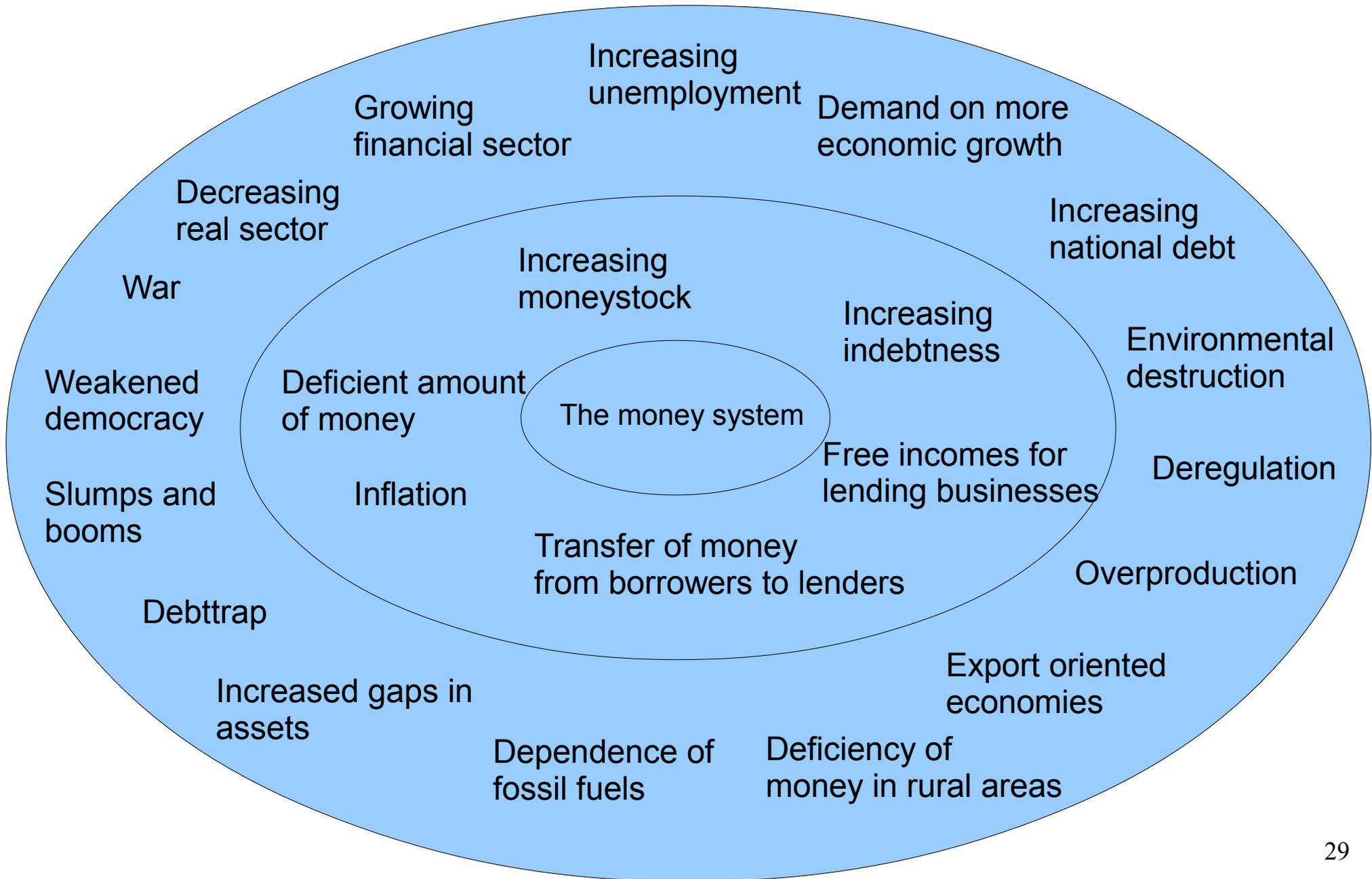
# What is the money system affecting?



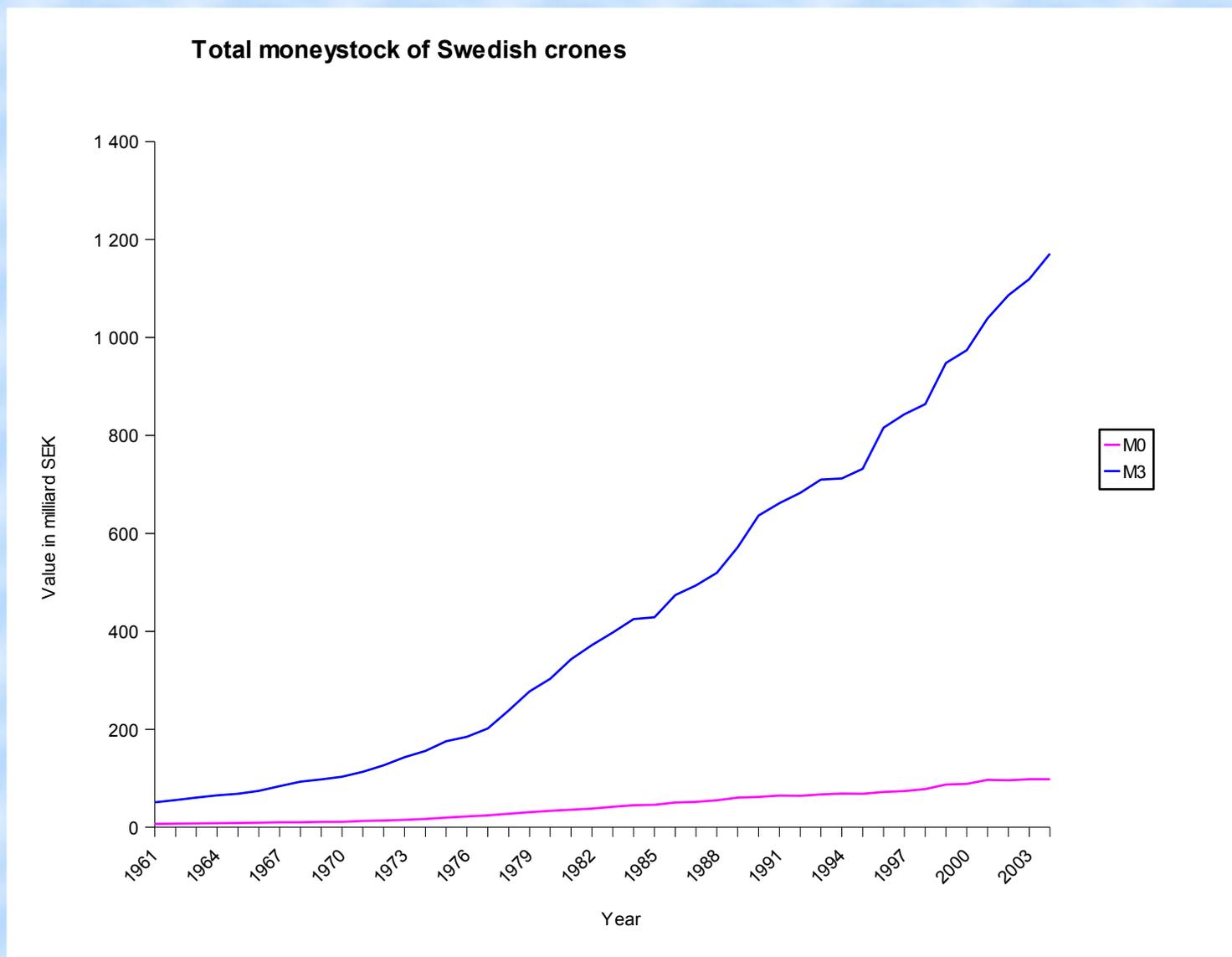
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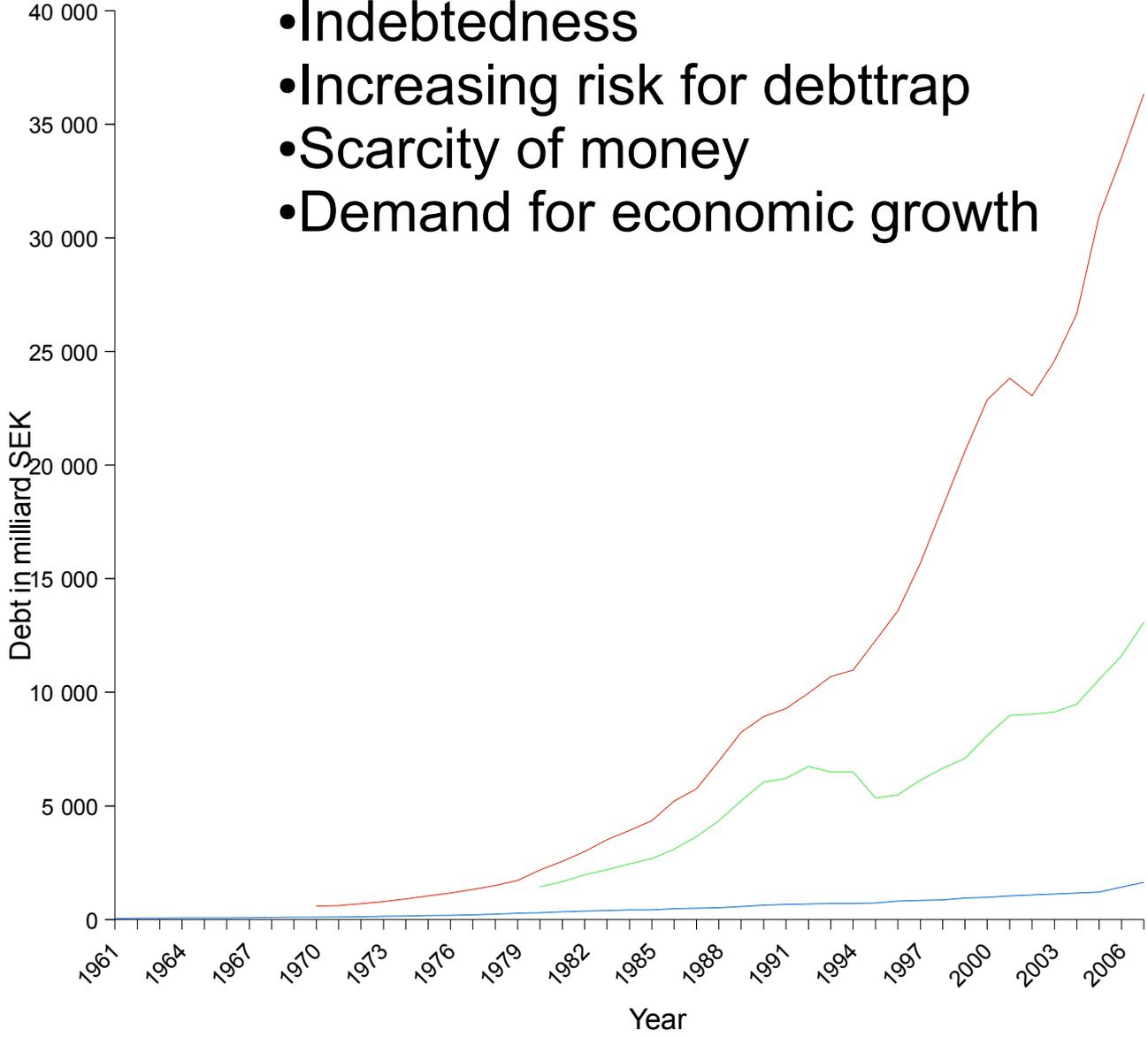


# Coins, bills and credit



# Total moneystock and total debt

- Indebtedness
- Increasing risk for debttrap
- Scarcity of money
- Demand for economic growth



**Total debt**

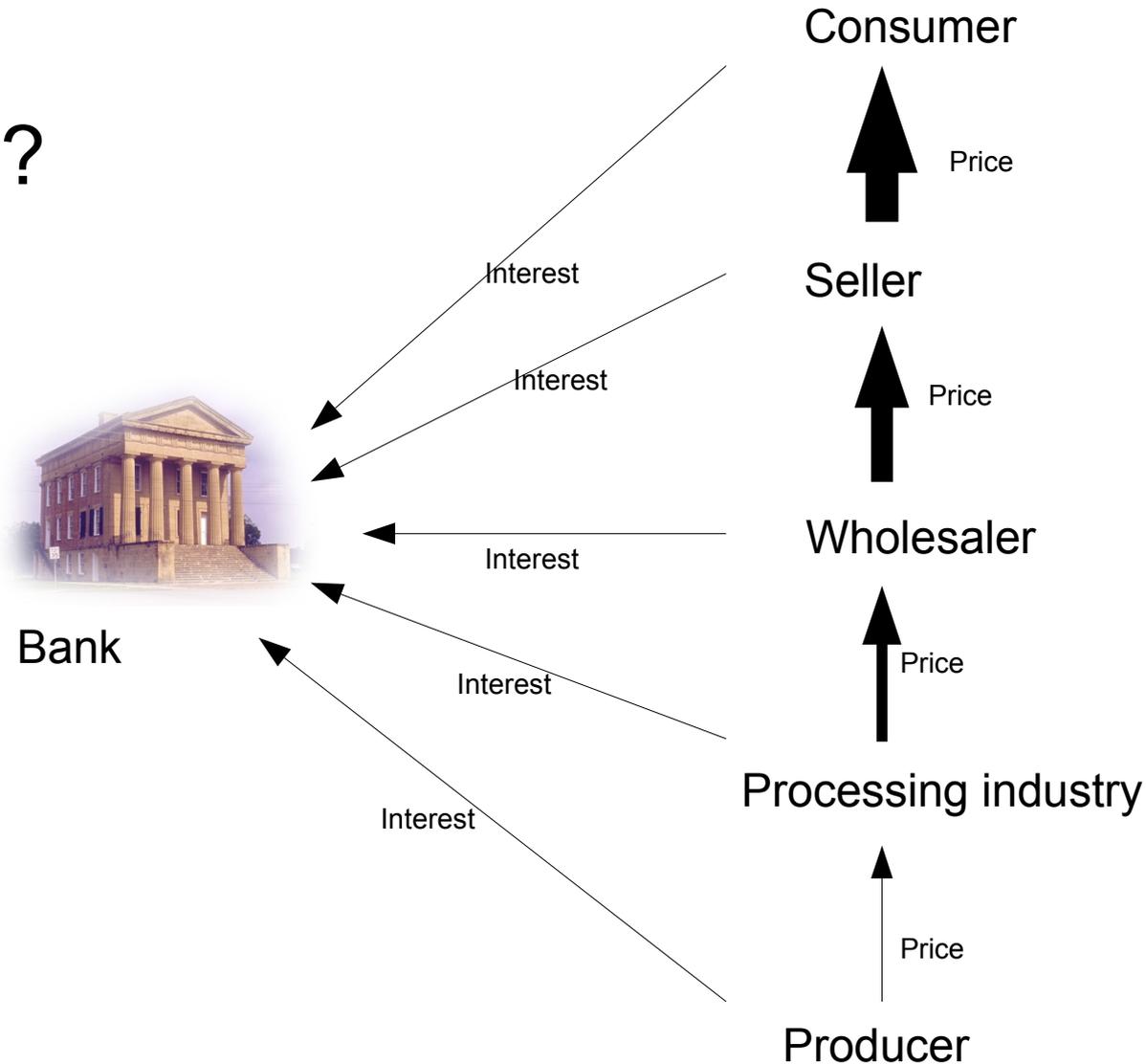
- Other debts
- Trade credits
- Insurance savings
- Fonds
- Other shares and holdings
- Stocks
- Leasing
- Financial derivatives
- Bonds

**Debt of loan**

- Loans of combines
- Loans
- Certificates

# Banks are "taxing" society through interest

Inflation?



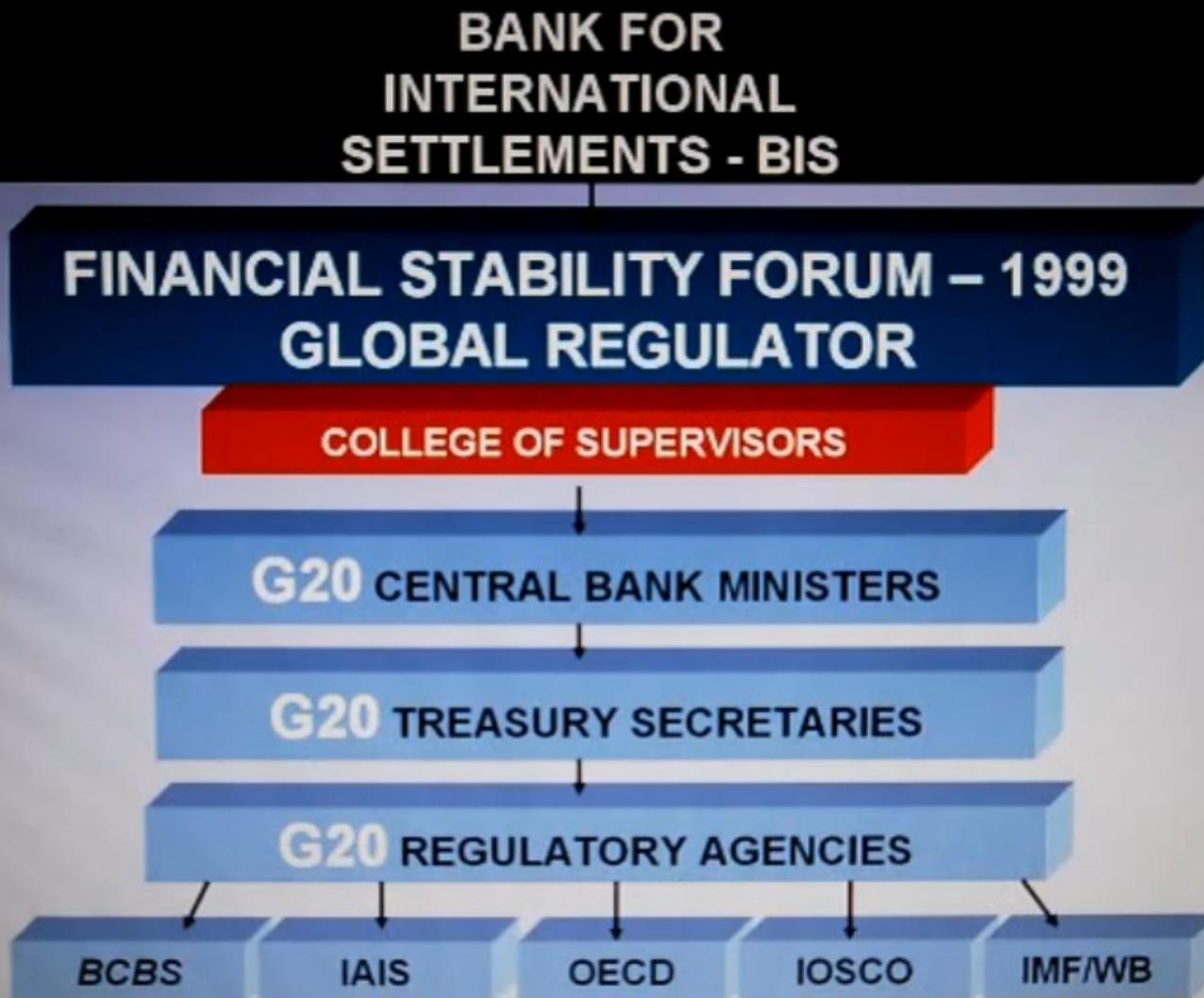
The money system



Economic growth



# Financial crisis leads to a transfer of power from democratic institutions to central banks



BCBS = Basel committee on Banking Supervision

IAIS = International Association of Insurance Supervisors

OECD = Organisation for economic co-operation and development

IOSCO = International Organization of Securities Commission

IMF = International Monetary Fund

WB = The World Bank

Source: Joan Veon

# What is the problem?

- Money is created on condition that someone gets into debt.

Money should be created without debt as a prerequisite.

- Money is created and owned by private enterprises although its value is guaranteed by the citizens.

Money should be owned by the people and created by an independent democratic authority.

- Benefits from money creation (interest) goes to private enterprises (banks).

Benefits from a national currency should go to the people.

# Two ways to work for a solution

- Change from above. The money system is reformed through decisions in democratic institutions.
- Change from underneath: Alternative local currencies/exchange systems are developed and are allowed to work along the national currency.

# Suggestion on change from above

1. Riksbanken uses its sovereign right to create the national money by directly deciding the amount of new money which shall be put into circulation.
2. Each time a new amount is released, it is given to the government to decide how it shall be put into circulation.
3. Private banks are forbidden to create credit.

# What would happened ?

- indebtedness would decrease step-by-step
- money would become more available
- real sector grows, financial sector shrinks
- more money to public sector/ welfare and infrastructure
- efficient control of the inflation/ minimal cycles
- possibility to leave the goal of economic growth
- less capital transfers through interest payments, decreasing income gaps

# Do you want to know more?

## Litterature (available also in swedish):

- The web of debt (Bankerna & skuldnätet) - Ellen Hodgeson Brown
- Interest and Inflation-Free Money (Pengar utan ränta och inflation) - Margrit Kennedy
- Agenda for a new economy (Agenda för en ny ekonomi) - David Korten

## Free films on internet:

- The crash course – scientific thorough description
- The moneyfix - easy introduction and overview
- The American dream - by The Provocateur Network (entertaining animated cartoon)

## Swedish sites:

- Ekonomisk reform – site for discussions on monetary reform