

"Banks invent money out of nothing whenever they lend"

By Bernard Hickey - Wednesday June 20, 2018
Interview with Mark Sainsbury



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Bernard Hickey - Economics commentator,
Newsroom Pro Editor, former Managing Editor
of Interest.co.nz

HICKEY

Essentially we're talking about parking capital. This is what the story really is all about.

It's about close to ten trillion dollars worth of money created in China in the last decade, close to four trillion printed by the European Central Bank and the United States Federal Reserve in the last decade, and in Japan a couple of trillion dollars.

Now that money has to fly around the world, we have open capital markets and New Zealand is a fantastic place for people to park that money.

That's one of the reasons you have seen this restriction (foreign home buyer ban) go in not just on farmland but on residential land because we know that money is going to come in here and pump up prices.

SAINSBURY

Hey Bernard, when you say like the European Central Bank they just print money?

HICKEY

Yep

SAINSBURY

What do you mean? They can just do this? Like sort of social credit?

HICKEY

Absolutely, I mean that's the story, what they call quantitative easing.

So if you're a central bank and you've already cut interest rates to zero and you want to increase economic activity, you have a spreadsheet then you just plug into the spreadsheet 2 trillion dollars and then you use that to buy government bonds off banks and pension funds.

SAINSBURY

But what's it backed by?

HICKEY

Nothing! That's the beauty of fractional reserve system we have for banking and central banking, and once we got rid of the gold standard that's how the world works.

Now, you know, you could argue when you do that it's going to create inflation, but it hasn't this time simply because the money has gone into assets as opposed to goods and services.

So you have had massive asset price inflation but it hasn't filtered into goods and services because we've had an enormous amount of production in a lot of factories around the world.

You know you can buy, you know, European Cars really cheaply now because there's so much surplus out there, and the advent of new technology means that a lot of things are a lot cheaper. Work is actually a lot cheaper because a lot more labourers are in the global markets.

SAINSBURY

Could we do that here? Could, you know, while Jacinda is off having a baby could Winston say to the finance minister "get the old printing press going and knock out another 2 trillion dollars for us"?

HICKEY

Well, I think you would have to remove the independence of the Reserve Bank before you could do that.

SAINSBURY

That's alright.

HICKEY

They would be pretty grumpy about that. I think you would have to see New Zealand cut interest rates to zero too and you would have to have no concerns about inflation.

You probably need unemployment to be high for them to move ahead with something like that.

I mean this is what Russel Norman suggested.

I mean there have been two quite radical suggestions by politicians in the last four or five years, one was Russel Norman's suggestion we could print money - he's gone.

The other one was Metiria Turei suggesting that house prices should drop.

SAINSBURY

I remember that, that was on the, it was with Guyon Espiner and Duncan Garner they had that nightly show, and I remember watching that and thinking that's going to go bad.

HICKEY

Yeah, I mean it seems outrageous and radical for a central bank to print money but actually its the way that our banking system works and once we're off the gold standard this is how the world works, and actually, at the moment, it is private banks that print money.

They invent money out of nothing whenever they lend.

The only thing stopping them from going completely berserk is central banks force them to keep some of their capital aside whenever they make a loan.

So that's the dirty little secret of international finance.

SAINSBURY

Wow !

HICKEY

That money is invented out of nowhere by private banks and central banks. In recent years central banks have been going at it hammer and tongs.

But that's great for asset prices. It certainly has pumped up New Zealand and global asset prices.

Stock markets are at record highs. Property prices at record highs.

Now, what should have happened I think is the money was printed and given to poor people through the benefit system to get that money out there, because at the moment most of that money's been parked in assets.

It's not actually been used to stimulate economic growth.