

Money out of Thin Air

By [The Mogambo Guru](#)

12/15/03 The exponential explosion of dollar-denominated credit...through the "miracle of fractional banking"...

Foreign central banks are shifting into overdrive on their holdings of U.S. debt last week, as evidenced by their balances at the Fed increasing by \$9 billion to a new record. Hahaha! Dorks!

Just to show those jerk foreigners that they haven't cornered the market in stupidity, U.S. banks also bought up a nice \$4 billion themselves!

But, and if you really want to see something scary, walk with me over to where the Treasury holds sway, and we will cling to each other in fear and whimper pitifully as we watch vile specters swirl around us, and we note that they issued another \$17 billion of debt in the same short week!

The whole scene reminds me of the end of the movie "Raiders of the Lost Ark," where our intrepid hero, Indiana Jones and his perky girlfriend are bound to a post, and the Nazis are opening the Lost Ark of the Covenant and all those angels are swirling around. At first the specters are beautiful and friendly, like what happens when you first start printing money and creating excess credit. Everything is wonderful and lovely! Then, right before our very eyes, the angels metamorphose into shrieking, devouring demons, and everyone is killed and the earth is swept bare, except our hero and his lovely sidekick.

Fractional Reserve Banking: \$5.8 Billion in One Week

But getting back into something more attuned to reality as it really exists, we note that the Fed increased raw, fungible credit by \$5.8 billion, too! In one week! And, I might add, to a new record, another new all-time new high, never before seen since the inception of the entire Federal Reserve System! A veritable avalanche of raw, naked credit, the original high-powered money if ever there were such a thing, the fabled Money Out Of Thin Air of story and song, money that can be multiplied by almost a hundred-fold, a thousand-fold, a million-fold, a zillion-fold, all through the miracle of fractional banking!

I say this even though people at the supermarket always look at me like I have lost my mind when I stand by the checkout counter and tell them about it, because taking a very, very rough estimate of the multiplier, I look at Required Reserves, \$41.64 billion, and divide that by Savings/other Deposits of \$4084.8 billion. And what happens when you do that?

Well, if you are like me, and you have my powerful skills with calculators, then you get some weird series of answers because you did something wrong with all those confusing buttons and then, in desperation, you finally ask someone who is just walking by to please use come over here and figure this damn thing out for me, then we get the surprising answer of 0.01.

This means that for every dollar of deposits, banks actually have only one cent of reserves in case people come looking for their money. Okay. Now, taking a look at Total Assets of the U.S. banking system, we find roughly \$4,381 billion. And when we compare that to the reserves of \$41 billion, it is, likewise, one puny cent of reserves against a dollar's worth of some of those loans going bad.

Fractional Reserve Banking: A Dime Vs. A Penny

That one cent in reserves, that one measly penny, is backing up both a growing contingency of souring loans going bad, AND people wanting their money! Whew!

And now, as part of your homework for today, I want you to go and get a textbook, any textbook, on economics, and look up the authors' example of fractional reserve banking. What is the standard amount of reserves that THEY use to illustrate the use of fractional reserves? Ten percent! They, meaning guys who write textbooks, would have an entire dime's worth of reserves for every dollar of deposits! And we have, in real life, a lousy penny! A penny!

And if you spend any time reading that section, you will note that nowhere in the text do the authors of those textbooks ever imply that reserves would get down to one lousy penny! Does that imply something to you?

And why is this possible, anyway? Because we have a fiat currency, and a guy named Greenspan who will stoop to anything, and another guy named Bernanke and his printing press, and if the banks ever need any money, for anything, they can just let those two know, and they and their Federal Reserve will just – presto! – print up some credit, and buy the holdings of the banks, which also went up last week, as I noted above somewhere. In short, they commit monetary fraud on a grand scale.

They will even print up actual currency! Which I add with that hysterical arching of my eyebrows and high-decibel voice, arms flailing about like my arms were on fire, although without the leaping up and down because the old knees aren't what they used to be, they did just that, last week! Again! They printed up \$4.4 billion in cash! Dollar bills! And they have printed up, in the last year, \$38 billion! Lovely stacks and stacks, pallet after pallet, of tens and twenties and fifties and hundreds! About \$138 for every man, woman and child in the whole country.

Fractional Reserve Banking: A Decade's Worth of \$4.5 Billion Weeks

\$4.5 billion in one week doesn't sound like that much, I admit, but it is for one lousy week, and can't you see where this is headed? Now imagine not just one week, but a month's worth of \$4.5 billion weeks, a year's worth of \$4.5 billion weeks, a decade's worth of \$4.5 billion weeks! It adds up!

And you think, and pardon me while I try and stifle this laughter, that the dollars that you are putting away today – tee hee! – into your retirement plan – giggle! – are going to maintain their – snort snort! – purchasing power when you – hahahaha! – retire? Pardon me, but hahahahahahaha! I can't help myself! Hahahaha!

Wiping the tears away from my eyes, my ribs really hurting from all that laughing, I note that the Federal Reserve and the Treasury are debasing your money right in front of your eyes, and yet you think – hahahahaha! – that when you retire, every one of those dollars you are depositing today will be every bit as valuable years and years from now? Hahahaha! And you admit that you are watching the Fed and the Treasury debasing your money right in front of your own eyes, week after week after week, and yet you STILL believe that a dollar today is the same as a dollar tomorrow? Hahahahaha! Stop! Stop! You're killing me! Hahahaha!

Now far be it from me, taking a long breath and trying to calm down and be serious for a minute because I am such a classy guy deep down, to suggest that there is any connection at all between the Fed creating money out of thin air to buy up government bonds, and thus effectively extinguishing the debt through that particular fraud, and the fact that the banks suddenly decided to acquire more government bonds. Must be a mere, umm, coincidence. (Hahahaha! Now I'm killing myself!)

So, in one stellar example, we have all had a good laugh, I have demonstrated the perils of a fiat currency, the danger of fractional banking, related it all to "Raiders" (which is a helluva good movie, a classic, really), and now I've predicted that we are all going to die, except for the PWOG, which is an acronym for People Who Own Gold, because you know what a sucker I am for acronyms, especially silly- sounding ones, because things are going to get really, really ugly one day real soon, and this may be the only bit of levity that we get out of it.

Regards,

The Mogambo Guru,
For the Daily Reckoning

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P.S. Doug Casey, editor of the newsletter International Speculator, thinks that "the precious metals are the only place to be. But I've said for years that, this cycle, gold isn't just going to go through the roof. It's going to the moon."

Man! As a guy who has a little gold, and my wife has some gold fillings in her teeth that I have had my eye on, and which I am including in my pathetic net-worth calculations, this kind of happy-talk about gold being in a record- setting bull market mania really appeals to me in the greedy, I'm going-to-be-so-rich-I can't-wait way. If you had listened to the Mogambo and bought some gold, too, then you would also be doing a little dance and singing "We're in the money! We're in the money!" Well, maybe not quite yet. But soon!