Where Do Banks Get Money to Lend Borrowers?aa

Reading Time: 7 minutes

The question of, “Where Does Money Come From?” is not at all new. To this day,there is still little understanding as to how money is created and used.

The simplest way to go about answering where banks get the money to lendborrowers is to start with the basics.

The most straightforward explanation available is that the money that is lent to borrowers, was taken in by the banks from savers.

From here on, the answer only gets more complex.

What is a Bank?

To get to the answer, you can start by understanding basic definitions, such asprecisely whata bank is. While it is important to note that there is more than onetype of bank, many bankstend to offer services in multiple areas.

As a whole, a bank is a financial institution, where the public deposits money intothe bank,and the bank creates a demand deposit for the public whilesimultaneously creating loans.

What is the Federal Reserve Bank?

Acting as the central bank of the United States is the Federal Reserve Bank. Thebanks’ responsibility lies in the policies that create or destroy billions of dollarsdaily.

Real money creation lies in how the banks of America loan the printed dollars tothe broader economy.

What is a Borrower?

The dictionary definition of a borrower is an organization or a person that takesout a loan from a bank intending to pay it back over time, with interest.

An organization borrows money for many reasons, including alleviating financialhardships, large purchases, or even supplementing an expensive event.Regardless of the reason for borrowing, an expense should always be justifiedbefore a loan is taken out by the borrower.

Banks are a Financial Intermediatory

While many traditional economic textbooks only go as far as considering banksto be financial intermediaries with regard to the concept of money creation, thisarticle won’t stop at that. A bank serves as the most common type of financialintermediatory.

A financial intermediatory is an institution that connects borrowers to savers. It acts as a middleman between individuals or other entities to facilitate the flow of funds, where one party (saver) has a surplus of funds; and the other party (borrower) has a deficit of funds.