# Let's Schmooze

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## Negative Interest Rates ~ Down the Rabbit Hole?

Are interest rates headed into that enigmatic rabbit hole? The Sweden central bank, following other central banks around the globe, recently announced that it would start charging negative interest rates on any deposits that it held, mostly by commercial banks serving the retail public.

What's going on here? Aren't interest rates supposed to be positive ~ that is, in the green? Why are commercial banks now being penalized for parking cash at the central banks?

It's an interesting story, and we'd better take a good look at it. If negative interest rates become a long-term trend, we'll all be reminded in short order that in the proverbial rabbit hole all sorts of bizarre things can be expected to happen. Let's start with a little background.

Globally and economically, capitalism reigns supreme. There is no other competitive economic model or system around. And, one of the foundational presumptions of capitalism is that it is a good thing to make money, or profits, on investments, and that continually making money and profits is to be expected.

That, in turn, is due to another foundational presumption in capitalism ~ that continuous growth is a good thing, and is also to be expected ~ and desired.

In capitalism, continual economic growth is what supports investors' expectations that placing their money, or capital, in various investment vehicles will yield positive results day after day, week after week, month after month, and year after year. Business models don't work if profits on invested capital are not expected. For more on the fundamentals of capitalism, refer to the chapter on *Capitalism* in our manuscript entitled *Expressions of Consciousness* at the Book tab at www.heirling.com.

Now, back to interest rates. Interest rates are simply a major way that profits are made on capital, such as money, or cash. There are four components of interest rates. One, interest rates on the use of capital provide a protection against the erosive effect of inflation on the capital in play. Two, interest rates constitute an acknowledgment of the risk inherent in making any investment ~ you might not get paid back. And three, capitalistic profiteering is built into the interest rate ~ charging whatever the market will bear on top of formal inflation and risk calculations. For more on these three interest rate components, refer to *Those Interest Rates* at the Article tab at www.heirling.com.

The fourth 4th component of interest rates is simply a reflection of the universal supply-and-demand premise. If there is a lot of whatever you have laying around for the asking, you probably won't get much for yours. On the other hand, if lendable money is in scarce supply, you will probably make out like a bandit when you lend yours out. We know that right now there is a lot of money just laying around for the asking. Think of all those easy credit offers hitting your mailbox every day. For more on the fourth 4th component, refer to *All That Money* at the Article tab at www.heirling.com.

So, ergo, aggregate interest rates are supposed to (1) address any concerns of inflation eroding the capital in play, (2) acknowledge the collection risk inherent in any capital investment, (3) grab any free profits that can be squeezed out of the freewheeling marketplaces, and (4) allow for the sheer amount of money lying around to be lent out, or invested ~ i.e. ~ the competition.

So, why are interest rates going negative? Why are even the central banks starting to charge commercial banks to deposit money, instead of paying them the usual interest on their deposits?

It's the fourth 4th component that's at play now ~ there are oceans of cash laying around ~ an obscene amount of money looking for a place to go. We touched on that in the last part of *Crony Capitalism* at the Article tab at www.heirling.com. Commercial bankers are sitting on trillions of dollars, and they're keeping them on deposit with the central banks.

Why? Why don't they lend those trillions out to businesses and individuals and make their interest profits the normal banking way ~ thru loans to the public?

The answer is simple. When commercial bankers look at global economies today, they see listless economic growth, perhaps even the negative growth characteristic of economies starting to shrink. They see, or anticipate, deflation, instead of the inflation that comes with meaningful economic growth. They also see what is usually associated with economic stagnation ~ low or nonexistent profits, and bloated asset prices all across the various economic arenas.

Commercial bankers don't want to lend their money out in a high-risk deflationary economy. They'd rather park their money in the central bank for a low, but risk-free return, until the economy rebounds.

And that's the catch-22. All those trillions of dollars that the commercial bankers have parked at the Federal Reserve aren't helping the economy rebound. That's why central bankers are coming up with the idea of paying negative rates on these deposits, i.e., charging the commercial bankers a fee to deposit their trillions with the Fed.

The Feds are trying to entice the commercial bankers into taking those trillions of dollars out of the central bank, and to start investing in our go-no-where economy by lending the money out to Main Street.

But the commercial bankers, with their concerns of undue investing risk in shrinking economies, are reluctant, and dragging their heels.

It's a game of chicken, waiting to see who blinks first ~ the Feds or the commercial bankers.

If the Feds blink first, our economy is stuck in the swamp of despair ~ and at the bottom of the looming rabbit hole.

If the commercials blink first, our economy might rebound and economic growth might reassert itself ~ and that rabbit hole just might fade away.

Whom do you have your money on?  Right now, the future of our economy rides on the question ~ "who blinks first?"

~ *'til we meet again* ~