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More on money vs. credit

All spending is on goods or services of various duration. Consumption is spending on short duration goods and services, it results in extermination of value. Investment is spending on longer, but all spending is for future consumption.

Consumption is equated to spending on final goods and services. But spending by households, while at the final stage of production (retail) is only final in terms of the market. As far as the totality of the economy that includes household or personal non-market well-being what is termed consumption may be more long-term than much of investment. Some measures of investment thus include spending on housing etc. But again, all spending is ultimately for consumption.

This is why it is imprecise to refer to consumption spending as necessary for a vibrant economy when that is predominantly extermination of value—certainly not an activity that contributes to growth or productivity.

Money lent is credit. Wealth is held in assets. Assets include money (liquid) and non-money. Individuals keep a balance of cash and bank checking or checkable deposits as a source of instant conversion to other assets or services. This balance is usually considered money.

Money demand is reduced when an individual reduces holdings of cash or bank deposits to acquire other assets. Spending money does not reduce its amount in the economy but is a reduction in its demand and tends to increase prices of the assets demanded in its place. Sometimes this is called an increase in velocity or turnover of money, but at all times someone holds the money so that the stock is unaffected.

If you decide that you can get along with less money it may be because you have decided to purchase financial assets that appear to be as liquid as money, or because you want an asset that gives you some physical return or service or an asset that gives you some return in money or interest.

Purchase of a newly issued financial asset that provides a return can be seen as an increase in credit.

Thus, purchases of financial assets are a form of lending.

Selling a financial asset or withdrawing money from an account that thereby increases total money balances of either cash or demand deposits reduces credit in the economy—the amount in cash and checking accounts remains unchanged, demand for money increased.

An increase in the money stock or money balances may cause credit to increase, or spending on goods to increase, or both, and may result in neither if money demand increases.

Inflation is usually deemed to be a general rise in prices – the result of increases in spending on goods and thus may accompany a fall in money demand, a rise in money supply or merely a reduction in credit.

During a hyperinflation, it is well understood that the demand for money falls against the demand for assets driving general prices higher, yet the demand for financial instruments can also fall. Hence, there can be a credit collapse, as confidence in financial holdings is lost. What is more, the transactions demand for money often rises, as each unit is worth less in transactions. This propels monetary authorities to print or create more units.

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