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More on money vs. credit

All spending is on goods or services of various durations. Consumption is spending on short-duration goods and services, which results in the extermination of value. Investment is spending on longer-term, 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 in consumer durables or more long-term and future-oriented than much of business investment. Some measures of investment thus include spending on housing, etc. But again, all spending is ultimately for consumption, and consumption spending overall is aimed at a shorter time horizon than investment.

This is why it is imprecise to refer to consumption spending as necessary for a vibrant economy when it 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-monetary assets. Individuals maintain a balance of cash and bank checking or checkable deposits as a source of immediate conversion into other assets or services. This balance is usually considered money.

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

One may decide to get along with less money and purchase financial assets that appear as liquid as money, or one may want an asset that provides a physical return or service, or an asset that yields a future return in money or interest.

The purchase of a newly issued financial asset that provides a return can be seen as an increase in credit and is a form of lending.

Selling a financial asset or withdrawing money from an account that thereby increases one’s money balances of either cash or demand deposits reduces credit in the economy–the aggregate of cash and checking accounts remains unchanged as demand for money increases.

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

An increase in the money supply is inflation of that supply. However, 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 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, a credit collapse can occur as confidence in financial holdings erodes. What is more, the transaction demand for money often rises, as each unit is worth less in transactions. This impels monetary authorities to print or create more units, but the printing or money creation is usually seen as

inadequate. After credit has collapsed and financial assets have been minimized, then further losses result mostly from currency depreciation and so if authorities make credible a halt in money production, prices can be stabilized.