



D = 250

$r = 10\%$

ARRR==25

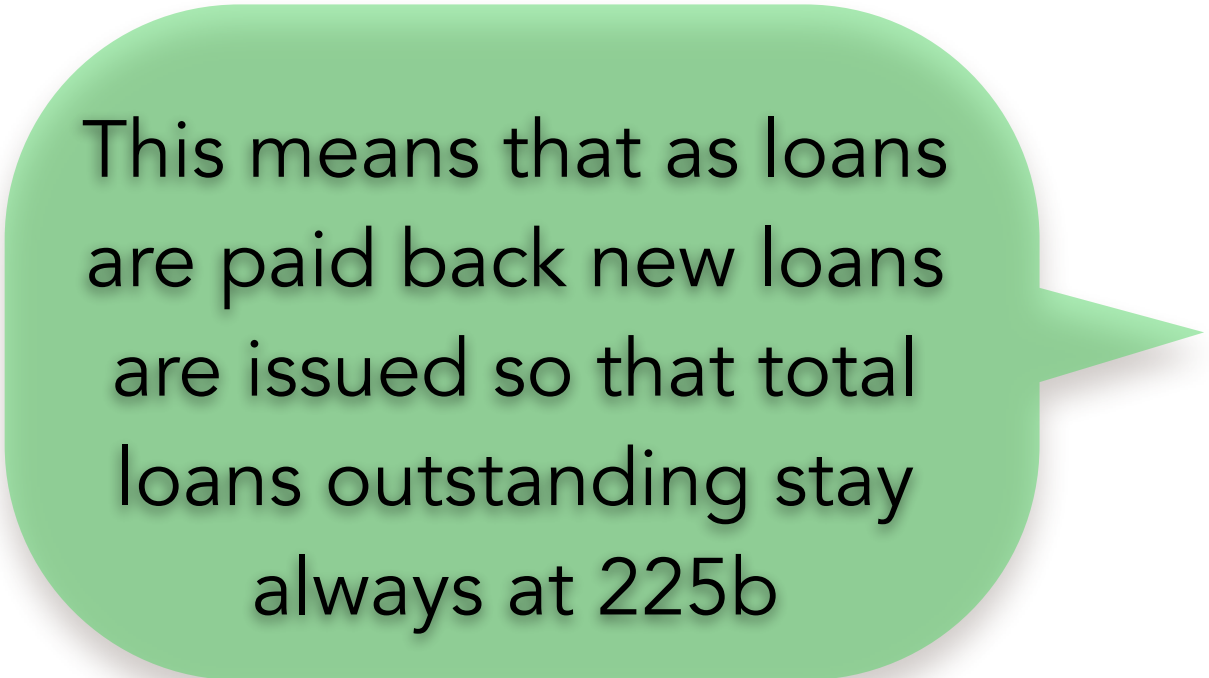
L

=

225

To understand what happens next, we must take a closer
look at the loan process

Bank A



This means that as loans
are paid back new loans
are issued so that total
loans outstanding stay
always at 225b



h

e

F



d



S

S

a



e





b



n



S

o







e

a

S

e

b





h







p



S





S

a

n

o

R

e

S

e







S

Bank A is **actually**
holding the exact
amount of reserves it
is **required** to hold

RR=24.4

-6

-6

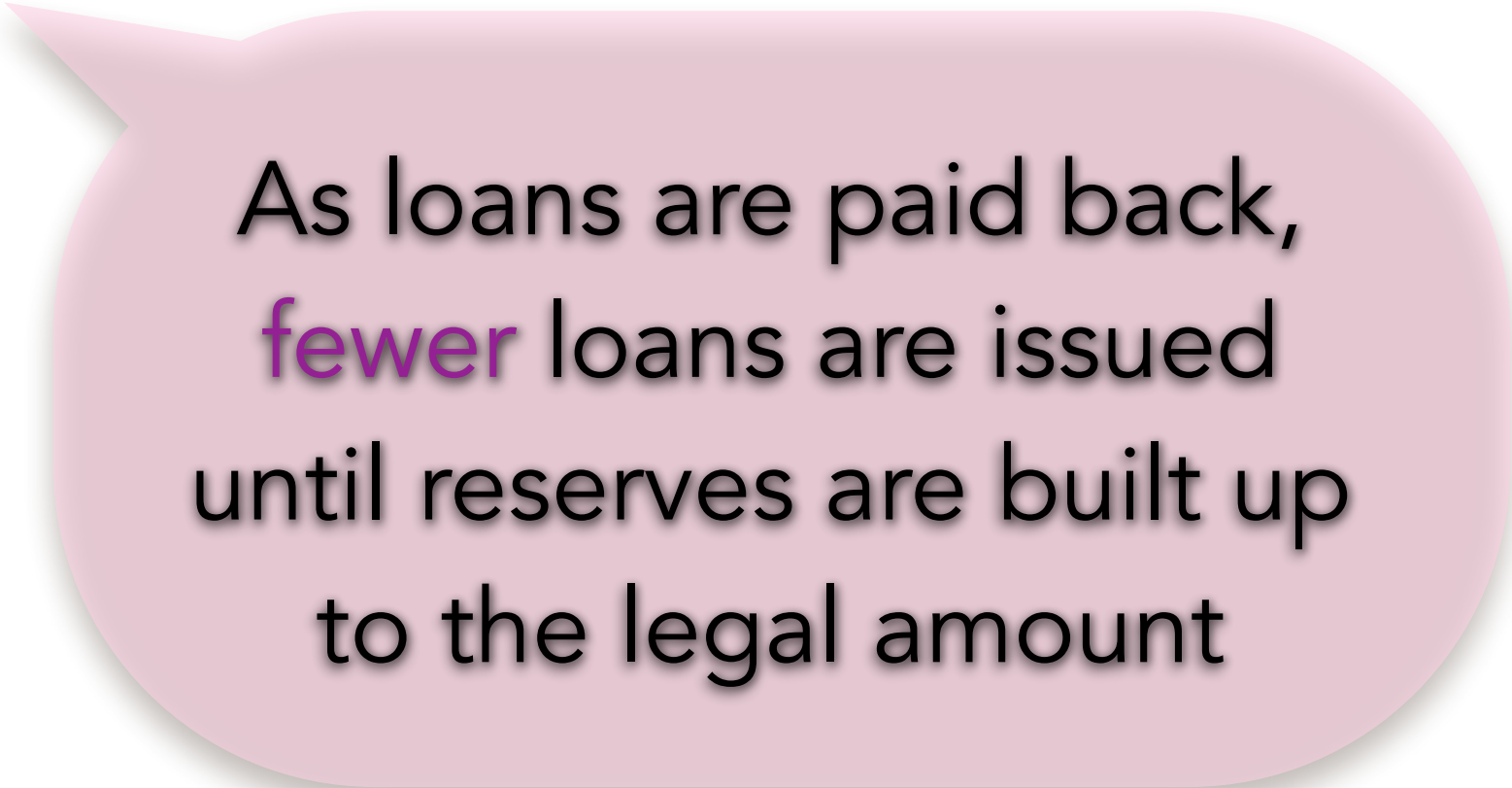
AR=19



The bank is
now short of
reserves

New D=244

Short = 5.4



As loans are paid back,
fewer loans are issued
until reserves are built up
to the legal amount

-5.4

New L = 219.6





A

S

a









b



n

d

S

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h

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9

g

e



S

a

d

e







a

S

e



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d

p



S





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h

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d

d

e







S

e

S



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V

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n

a



b

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S



This is the
drop for
Bank A

A **sale** of bonds by the Fed triggers a **decrease** in **deposits** because the public pays with checks drawn on their bank accounts

A sale of bonds by the Fed triggers a decrease in actual reserves because the Fed decreases reserves in all banks

The Fed's sale of bonds decrease both:

Deposits and Reserves

To understand what happens next, we must take a closer look at the loan process

Bank A is **actually** holding the exact amount of reserves it is **required** to hold

The bank is now short of reserves

Bank A $r=10\%$	
$AR=RR=25$	$D = 250$
-6	-6
$AR=19$	$New D=244$
$-RR=24.4$	
$Short = 5.4$	
$L = 225$	
-5.4	
$New L = 219.6$	

This is the drop for Bank A

As loans are paid back, **fewer** loans are issued until reserves are built up to the legal amount

A **sale** of bonds by the Fed triggers a **decrease** in **deposits** because the public pays with checks drawn on their bank accounts

A **sale** of bonds by the Fed triggers a **decrease** in **actual reserves** because the Fed decreases reserves in all banks

The Fed's sale of bonds **decrease** both: **Deposits** and **Reserves**

The same will happen **for all banks** in the banking system: all banks will **decrease Loans**