$D = 250$

$$r=10\%$$

AR=RR=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

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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

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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

This is the drop for Bank A

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	

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