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The role of fractional reserve banking and a privatised debt-based money supply

A major problem for housing affordability lies in the very structure of our privatised money supply. To ignore this major factor is to overlook the relationship between the growth in the debt-based money supply and price inflation especially as it applies to housing.

When money is created by private banks out of nothing for profit and enters the economy as interest-bearing debt, the result is ever growing debt and inflation. Virtually all of our money is debt. Banks only create the principal loan. No money is created to cover the interest due and so this must come from the existing pool of debt money. It is necessary to have a constant supply of new money so when banks restrict their lending the economy contracts. However, this necessary new money is of course more debt and all bearing interest.

This is a structural problem that will not be corrected unless action is taken to remove the power to create money from commercial banks. Public ownership of the money supply is essential if the quantity of money is to be managed in the national interest.

Money creation and housing speculation

It is not surprising that loans for housing have increased. Under the Basel Rules using a risk based assessment for lending, housing is safer for lenders as a mortgagee sale of a house is easier than to wind up a business.

Far too much money has gone into housing speculation which has pushed house prices up well beyond increases in wages. The increased proportion of household income spent on servicing a mortgage has meant that money that could have been spent in the real economy has been diverted to the financial economy.

Christchurch housing is an opportunity

The government could create new money that is debt-free and interest-free. This new money could be spent into the real economy for housing for Christchurch. Borrowers could pay charges to cover administration costs but not compounding interest. With resources and labour available at current prices this new debt-free money spent into the economy would not be inflationary.

Christchurch offers the perfect opportunity to begin a managed transition from a debt-based money supply. Money would be put directly into the real economy creating jobs rather than into the financial economy.

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