Commercial Bank Balance Sheet Rules

1. Both sides must balance. Assets = Liabilities
2. Required reserves are what you typically need to solve for first.

Hints: use the decimal form of the reserve requirement

ex: 20% reserve requirement becomes .2 in the formula

demand deposits are also called checkable deposits

1. Next find the excess reserves. Excess reserves can be used to loan more money and expand the money supply or to purchase securities from the Fed. Banks can make money off of both loans or securities but loans provide more profit while securities provide more liquidity.
2. If the demand deposits (checkable deposits) change on the Liabilities side of the balance sheet, there will always be a change on the Assets side. This is not the rule for the Assets side, if something like the Reserves change first, that money can be moved to Loans or Securities without the Liabilities side ever changing. The sheet will still balance, but all of the changes can remain on the Assets side.

ex: A bank purchases 200k in securities, the Reserves would go down by 200k and the Securities would go up by 200k. Both Reserves and Securities are on the Assets side of the balance sheet.

1. If you are asked to change the money supply (How much does the money supply expand or contract):
   1. If they ask for the initial change in the money supply don’t use the multiplier.
      1. If they ask for the total change in the money supply use the multiplier.
   2. The money supply only changes if a loan has been made. If they say someone takes $500 in cash and puts it in their checking account there is no change ($500 moves around in M1). If they get a loan for $500, the money supply goes up by $500 initially and multiplies if it leaves that bank.
2. Beware of created money vs existing money. If the monetary multiplier is 5, and a loan of $100 is made by a bank, the money supply changes by $500 ($100 \* 5).

Of that change of $500, 100 of it was already in the bank, $400 is “created” money. They like to ask how much money is created or new and will offer $500 as an answer. Be careful of that.

1. Actual Reserves are the total of all reserves on the Assets side. They can include both required and excess or each type of reserve may be listed separately and they would then add up to actual reserves.

**Formula Summary**