Funding the Future

Where does the money go?

https://www.taxresearch.org.uk/Blog/2023/06/14/where-does-the-money-go/

Published: January 12, 2026, 8:15 pm

I was asked this question recently by an academic (wh is not an economist):

Where is the best place to get an answer to this question:

Where does the extra money go when mortgage rates increase? Aside from the amount that goes to pay higher rates to savers?

The answer is I know of no such best place, so let me have a go.

There are simple answers here, and there are more complicated ones.

And then there are complex ones.

The simple answer

First (and this is common to all three answers), interest is paid by:

* Households, mainly on mortgages, but also on other debts;
* Companies, as most are funded by borrowing and not by share capital;
* Government of all sorts, from Westminster to parish councils;
* Banks, on deposits.
* Overseas borrowers, especially in developing countries if they borrow in sterling (which admittedly is not common, as most borrow in dollars).

That simplifies the list, a bit, but all economics requires modelling and that always simplifies things, a bit.

Second, the following collect interest:

* Households with savings;

* Companies with savings;

* The government (as some people owe it money, albeit a lot less than. it supposedly owes);

* Banks, as they are owed interest on the money they lend;

* The overseas sector that saves in the UK - which is a recurring feature of the UK economy now.

The same comment about simplification applies.

A simple model is, then, that borrowers are worse off and those with savings are better off when interest rates are increased. It could be said to be as simple as that.

Only it is not that simple, of course. That is because of the impact of the interest payments and the redistributional impact of this whole process.

Let's just look at the first order issues in this section. These relate to:

* The impact on the person paying.

* The impact on the recipients.

* The imbalances between the two.

The person paying is most likely on a reasonably fixed income (because most people are) or on a tight budget (because why else would they borrow?) or both (unless they are the government when the ability to create money means that these constraints do not apply, albeit that those making decisions think that they do). The consequence is that those paying interest will behave as if they are actually worse off or that they think they are, and in either case will try to reduce their spending on other items to make payment of the interest. The consequences of that reduction will be ignored for now. They are, then, worse off in material terms as payment for a non-material liability will have reduced their ability to meet material need. That is exactly what the Bank of England wanted by raising rates. They think this will reduce demand and so reduce the prices of goods and services in the market.

However, as a matter of fact, every interest payment has to be matched by an interest receipt. Double entry requires that, and is unavoidable. So, whilst a whole range of people and entities in society will be worse off, there will be others better off in the same amount.

There are, however, differences to note. Firstly, the number of people and entities paying interest in society is greater than the number receiving it. That is **because wealth is highly concentrated**:

Figure 2: The richest 1% of households had wealth of more than £3.6 million, least wealthy 10% had £15,400 or less

Household total wealth by percentiles, Great Britain, April 2018 to March 2020

It is not true that only those with lower wealth borrow, but there is an inevitable association because why borrow if you do not need to do so?

So, the interest is by and large received by organisations with wealth, whether they be individuals, their wealth managers (such as pension funds - and most pension wealth follows the above pattern) or banks.

In principle, all these people and organisations could now go out and spend as much in the economy as has been foregone by those who have made the additional interest payments. They don't do that, however, and for good reason. That is that, firstly, banks tend to keep an undue part of the interest paid to them as primary recipients of most interest payable in the UK. They do not increase the rate they pay to savers as fast as they increase the rate to borrowers. As a consequence, they overly increase their income and, even after paying bonuses to already wealthy bankers, maintain this position overall. So they unduly gain. And, secondly, the wealthy do not spend what they get because they already have enough to meet their needs. We know that, because that is why they are wealthy: they have more than they immediately require. They now have more. That is it.

So, the net result is that most are worse off; the wealthy are wealthier and banks have made undue profit on the way.

There are policy consequences. If raising rates made sense in the first place (and I very often question that) the consequent increase in the wealth of banks and of those already wealthy in society makes no sense at all. They need accumulate no more just because monetary policy says that the spending of those with lower disposable incomes needs to be crushed by increasing rates. It would make sense in that case that the social cost of raising rates be countered by additional taxes on wealth and undue bank profits. It would, however, seem that these never happen. The sense that the policy of crushing the well-being of some might simply be an exercise intended to increase the well-being of others is hard to avoid as a result. At the very least, the political signalling in all this is dire.

This, however, is the simple model.

The more complex model

Being aware of the length of this post, let me simply outline the other two models needed to appraise this policy.

The more complex model looks at the more immediate impact of reduced spending by households and others with increased interest liabilities both on their well-being and on the broader economy. So, the impact on their spending on wellbeing would be

appraised in straightforward terms i.e. how much either spending is foregone and what does this mean e.g. in terms of financial stress, the risk of default, organisation failure, hunger and so on. It could also note the impact on choices by the government if it thinks it is constrained by additional interest costs (which it is not). These are first-order impacts of the change. Many will be deeply significant. Deprivation and fear will be the consequence for many: it is impossible to ignore this, and the risks of resulting economic failure can be predicted e.g. in homelessness and business failure.

Yet more complex models

More complex modelling looks at the knock-on effects of:

* Reduced spending by many;
* Undue and imbalanced reward to others.

In effect, this looks at the multiplier effects of the changes. How much bigger is, for example, the impact on the economy than the prima facie reduction in spend by impacted households when multiplier effects are considered? Again, what is the multiplier effect on government spending? And is there an employment element? On the reward side, how will the imbalances play out if not corrected?

All these could, I suspect, be modelled in Minsky. All I can say is, give me a lot more time, although the direction of travel is obvious: the misery of most spreads with some being immune to the suffering.

Conclusion

So, to answer the question:

Where does the extra money go when mortgage rates increase? Aside from the amount that goes to pay higher rates to savers?

It's not simple is the honest answer, but for now, assume that banks gain unduly, the wealthy are immune from risk and inequality grows whilst real economic activity falls. And we call this policy.