The history of money and its role in the modern world

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Article
The history of money
and its role in the modern world
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“Money is the most universal and most efficient system of mutual trust ever devised.”

Yuval Hariri

Preface

The last 18 months have certainly been a testing time. The global pandemic has forced us to adjust our lives in ways we never imagined or thought possible. We have endured lockdowns as well as restrictions on family visits, social gatherings, exercise and holidays, not to mention the devastating health impact and tragic loss of life.

We have for the most part adapted, shifting our work (where possible) and shopping online, 'Zooming' our friends and family, and keeping the dream alive of our next vacation. When able to venture out, we have kept our obligatory 1.5 metres distance and shunned cold hard 'dirty' cash in favour of 'tap and go'.

Yet, money in many respects has become more important than ever.

At an individual level, the 'value' of money has undoubtedly increased, as many employees were stood down and struggled to pay their mortgage, rent, utilities and groceries. At a broader public level, the value of money has, however, been somewhat distorted after governments around the world collectively spent an unfathomable amount to protect their populations and rescue their economies. With debts racking up into the trillions of dollars, funded largely by central banks, and no hope of paying it off anytime soon, the mind boggles. It is difficult to put a value on protecting humanity.

We are now seeing the impact of all this 'money printing' in rising inflation, with a strong rebound in economic activity fuelling a surge in commodity, house and share prices. With the service sector effectively 'closed for business' at various stages during the pandemic, as we were unable to travel and dine out, there has been strong demand for manufactured goods, as we improved our homes, beefed up our technology and curiously, purchased more cars.

The strong demand, coupled with a temporary shut-down in manufacturing in 2020, has caused prices for some consumer goods to soar to decade highs. Used car and truck prices, for example, rose 45% in the US in the 12 months to June 2021, reflecting increased demand and supply constraints, such as the global semiconductor shortage.[1]

As vaccination rates increase and more economies reopen, we expect this recovery to gain momentum, particularly as employment grows, confidence returns and consumers draw down on their accumulated savings. Those who were able, chose to hold onto the generous government payments last year, sending savings rates to record high levels of over 30% in the US and 20% in Australia in 2020.[2]

1 Source: Federal Reserve Bank of St Louis.
2 Source: Federal Reserve Bank of St Louis; Reserve Bank of Australia.

These savings are now making their way back into the economy as consumers unleash pent-up demand. As this 'velocity of money' increases (i.e. how often money is spent in the economy), inflation usually follows.

Higher inflation should theoretically translate to higher bond yields. However, at the time of writing, after a brief spike to 1.7% p.a. in March 2021, yields on US 10-year Treasuries continue to hover below 1.3% p.a. - as the market seems to accept the premise that the rise in inflation will be 'transitory'. [3] There is always a danger in consensus thinking. We aren't in the business of forecasting economic variables, however, we believe there is a risk that price rises will be more long-lasting than what is currently priced in by the markets, which may see central banks increase official interest rates much earlier than expected.

Such extraordinary levels of money creation and signs of significant inflation (after a long absence) begs the question of the role and value of money in society. We place enormous trust in the value of money when we transact.

In our feature article, Investment Specialist Julian McCormack delves into the origins of money over many centuries - from 'barter' and debt, to metal-backed currencies, fiat currencies and the rise of the US dollar.

> **It's a fascinating look at history and makes one realise just how the form and function of money has shifted over time – often driven by political and economic motivations of governments. Central banks have also played a role, notably their various interest rate policies and bond-buying activities.**

Reflecting on the past provides a valuable perspective on current events. With inflation creeping up and extraordinarily large budget deficits that need to be funded at some point, we suspect that change is afoot.

A low interest rate environment has been the primary driver of asset markets in recent years, a change in that scenario could have significant implications for equities, particularly high growth stocks, which have been a major beneficiary of this trend.

Andrew Clifford,
Chief Executive Officer & Co-Chief Investment Officer,
Platinum Asset Management
August 2021

3 Source: FactSet Research Systems.


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In recent years, we have stretched the limits of any traditional understanding of money via radical policies, such as negative interest rates, quantitative easing and yield curve control. As the global financial crisis (GFC) saw the re-writing of the monetary policy rule book, so the COVID-19 crisis saw the abandonment of any pretence of 'fiscal rectitude' in every major economy.

The history of money and its role in the modern world

By Julian McCormack

In the rebound from the COVID-induced disruption, inflation and nominal growth have risen sharply and debate has raged about the transience of the inflationary surge.

As we explored in last year's annual report, the defining characteristic of populists is that they spend money.[1] Now, in order to grapple with the question of incipient inflation, we must grapple with defining money itself.

Money is a social institution whose rules are more like religious edicts than physical laws. There is nothing definite about money, save our understanding that it has value and our trust in that value's persistence. Money is in essence a story – and that story is changing.

In this article, we will briefly examine the history of money and demonstrate that its form and purpose have shifted over time. Our contention is that another shift is underway in the function and nature of money at present – with central banks now effectively providing infinite funding, which is being married to fiscal spending after 40 years of austerity – a shift we examine briefly toward the article's close.

THE BARTER MYTH

A typical history of money usually starts with a story of a world of barter transactions transformed into a world of money-based transactions.[2] This is almost certainly wrong. Credit is, by an enormous margin, more common than barter in every recorded traditional society.

> **It is vanishingly rare that any sociologist or anthropologist has recorded an instance of barter as a form of exchange – we repeat – *this has almost never been recorded.***

Vastly more common is the building of 'debt' and its expunging via social obligation. "I'll scratch your back if you scratch mine." Or "I'll give you these eggs, if at some time in the future you help me erect a barn".[3]

This may be confused for barter – but note the creation of obligations that persist through time, not the discrete, instantaneous exchanges of value described in economics text books as barter.

MONEY AS CONGEALED TRUST

All societies are based on trust to some degree. Historically, we developed money not to replace barter, but to replace trust. Once dealing with large-scale societies and members of different social groupings, a unit of exchange becomes necessary. Historically, this did not tend to emerge until large numbers of people moved through areas in which they were strangers – particularly as soldiers.

Having been rewarded with plunder, how might a soldier transport the value of their loot home? Coins help, particularly when the coins themselves are made from precious metals – especially metal recently liberated from its former owners.

> Throughout the history of Europe and Asia, in periods of relative peace, credit-based systems of commerce predominate; in periods of war and generalised violence, coin-based systems predominate.[4]

Precious metal coins evolved as money in order to substitute for prior exchanges of value based on trust and reciprocity.

"Money is the most universal and most efficient system of mutual trust ever devised… Money isn't a material reality – it is a psychological construct… But why does it succeed? People are willing to do such things when they trust the figments of their collective imagination. Trust is the raw material from which all types of money are minted."[5]

MONEY WAS RARELY A STATE-BACKED MONOPOLY UNTIL RECENTLY

For most of its history, money has comprised varied mediums of exchange with different issuers whose coins and notes were in mixed circulation across multiple jurisdictions. In antiquity, the value of coinage was based on the content of the metal it was composed of, meaning that a Persian coin, such as a Daric, was readily usable in ancient Greece, as the purity of the metal content was generally accepted.[6]

Ancient merchants issued certificates of deposit, which could be transferred to third parties in different states. These were specific and contractual, rather than general bearer receipts representing specific, repeated, face-values in coin or equivalent value.[7]

The first genuine 'paper money' was developed by the Chinese, and again, it was not originally a state monopoly system.[8] In 9th century China, 'exchange notes' were developed – these were negotiable certificates dubbed 'flying money'. These precursors of banknotes were widespread in China by the early 11th century.[9]

Later, in Europe, banknotes – literal IOUs claimable against an individual bank or depositor at a bank – were in common circulation alongside centrally issued notes and coins for centuries. In more modern times, the acceptance of Spanish silver coins was so widespread in the United States in its early years, that its more important forms were recognised as legal tender.

> The dollar sign '$' derives from the superimposition of a 'P' and an 'S', which was a symbol for peso. Spanish coins remained in circulation until the middle of the 19th century in the US.[10] There was no monopoly on the issue of currency within nation states until relatively recently.[11]

CENTRAL BANKS EMERGED SPECIFICALLY TO FINANCE GOVERNMENTS, ESPECIALLY THEIR WARS

The foundation of the central bank *par excellence*, the Bank of England, occurred in 1694, when the Bank was established to assist William III in funding his ongoing war with France. The Bank was private, with King William III and Queen Mary among its original stockholders, and was granted a royal charter enabling it to issue bank notes and act as a banker to the government.

This was necessary largely because of the strength of Parliament, which had responsibility for issuing supply bills since the 15th century and whose power had been increased by the Glorious Revolution of 1688-89, which installed William III and Queen Mary.

The foundation of one of the world's early[12] and preeminent central banks was necessary as a result of Parliament's intentional underfunding of a war.[13] The Bank of England was private and existed alongside other banks, each issuing their own currency in the form of bank notes.

THE GOLD STANDARD WAS AN ACCIDENT

It was only by mistake that multi-metallism and bimetallism slipped into gold-only backing for currency. Prior to the late 17th century, the Royal Mint was managed by the Company of Moneyers, whose members were notorious for "self-dealing, corruption and drunkenness".[14]

> **To deal with the situation, the British government took the extraordinary step of appointing Sir Isaac Newton to the post of Warden of the Mint in 1696, which he gladly accepted for its handsome salary.**

Despite his genius, Newton was in some financial hardship at the time.[15] Newton's initial responsibilities revolved around assaying and the prevention of counterfeiting, which was rife at the time. Eventually, he grappled with the problem of an outflow of silver and sought to set the price of gold and silver relative to each other in Britain.

In doing so, however, he set the price of silver relative to gold too cheaply versus other European powers, causing silver to flow offshore and over time, locking Britain into a de facto monometallic gold standard.

This occurred by draining the Bank of England's reserves of silver and leaving gold alone to dominate the reserves held in British banks.[16]

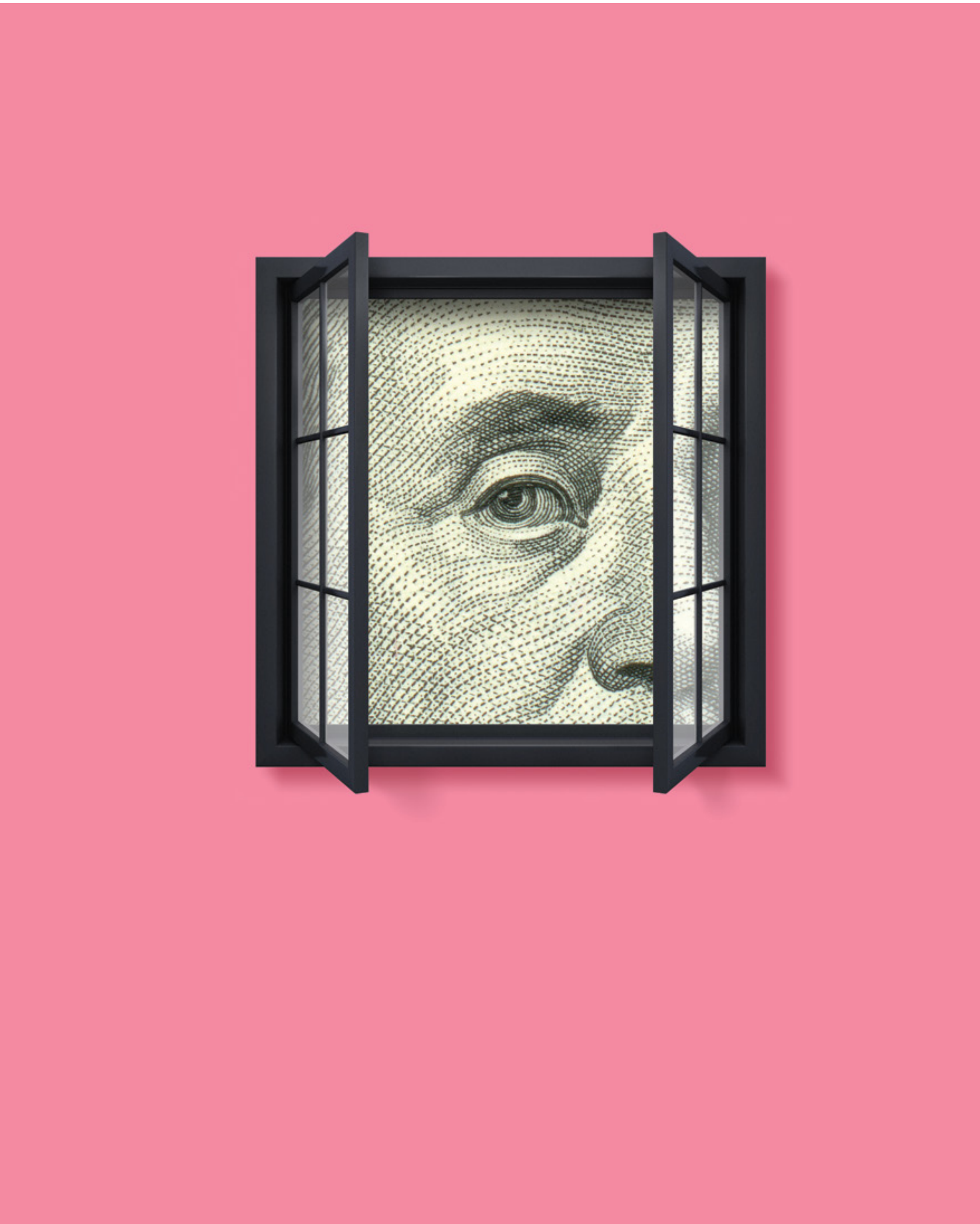
A similar dynamic occurred in the US. The country's first Treasury Secretary Alexander Hamilton, drawing inspiration from Newton's 1717 report on setting the ratio of gold and silver, set this ratio for the metals in the US at 15:1.

However, the market value of the metals relative to each other changed – discoveries of huge, silver-rich mines in Nevada helped to drive down the price of silver relative to gold, such that the ratio of the prices in the open market drifted out to 16:1 by the 1810s.

> **This effectively created an arbitrage opportunity – a holder of silver could sell silver for gold, take that gold to the Mint to exchange it back into silver, sell that silver for gold on the open market and make a profit.**

This resulted in gold being driven out of circulation – an example of *Gresham's Law* in operation – leaving gold as the dominant reserve metal.[17]

Simply put – the gold standard arose by mistake.



The gold standard never implied that currency was actually 'backed by gold' in any literal sense – no country ever had a currency fully backed by gold in the modern era, with the proliferation of trade acceptances, bank notes and other instruments ensuring that currency in circulation was always multiples of gold backing and that the rate of backing was not constant. As an example, in Britain, in 1913, currency in circulation was backed approximately one-part-in-seven by gold.[18]

> Gresham's Law: 'Good money' leaves circulation, leaving 'bad money' traded. Where people mistrust the value of a currency, they seek to hoard more trustworthy alternatives – leaving the 'bad money' in circulation; and where an arbitrage exists, the 'cheap' money will remain in circulation, with the 'dear' money forced out of circulation.[19]

THE HEADY BENEFITS OF GOLD

Adherence to at least a partial backing of currency by gold, assisted states in gaining access to London capital markets in the 18th and 19th centuries. Partial gold backing gave creditors some confidence of repayment, thus allowing credit to flow, paradoxically diminishing the backing of gold to currency!

How the gold was acquired was irrelevant: for example, Japan's industrialisation was catalysed by the seizure of gold from China following the 1894-95 Sino-Japanese War via massive reparations, which facilitated Japanese borrowing in London.[20]

For merchants and investors, trade credit and foreign direct investment were catalysed by use of the gold standard due to the tradability of merchants' acceptances and bank bills globally.

For merchants, there were huge financing advantages in being able to borrow against future cargoes or revenue streams. On the other hand, creditors were able to on-sell credit risk in the form of discounted merchants' acceptances.

Throughout the 19th and early 20th centuries this was easiest in London by a wide margin, given the immense depth of the market for acceptances there relative to any other financial centre.[21]

GOLD'S COLOSSAL COSTS

The gold standard had two colossal costs. It was deeply, cruelly regressive; and it was ferociously unstable.

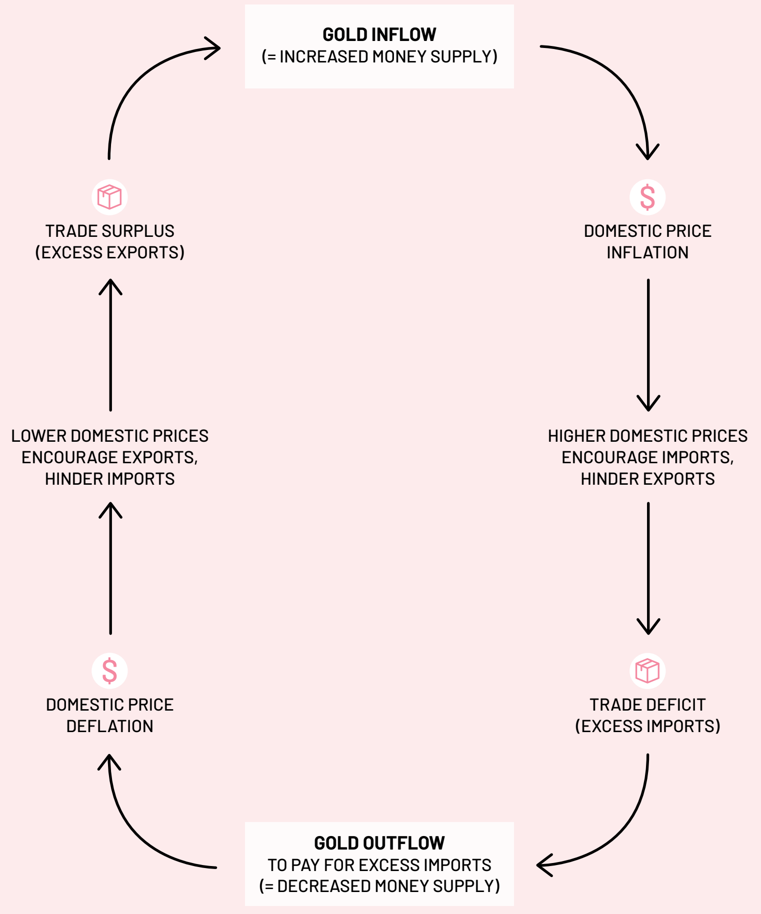
The functioning of the classical gold standard allowed for gold to function as a money supply equilibration tool, which tended toward a shrinking money supply and deflation in order to stem gold outflows caused by any rise in domestic prices, as shown in the diagram on the right.[22]

> **The effect of this cycle, with specie (gold) flowing out of economies in the presence of trade deficits, was to induce periodic bouts of deflation and deep recessions. One effect of these recessions, in the absence of social safety nets of the modern state, was to steeply reduce life expectancy during and in their aftermath. The gold standard was brutal in its impacts on everyday people.[23]**

The 19th century was racked by financial crises and a run on banks roughly once every 10 years somewhere in major financial centres globally.[24]

The reason is simple, and inherent to the gold standard itself. The banking system created money in the form of banknotes and merchants' acceptances. These were all exchangeable for gold, albeit usually at a discount. However, the system itself was always multiple times geared in terms of currency in circulation versus available gold supply.

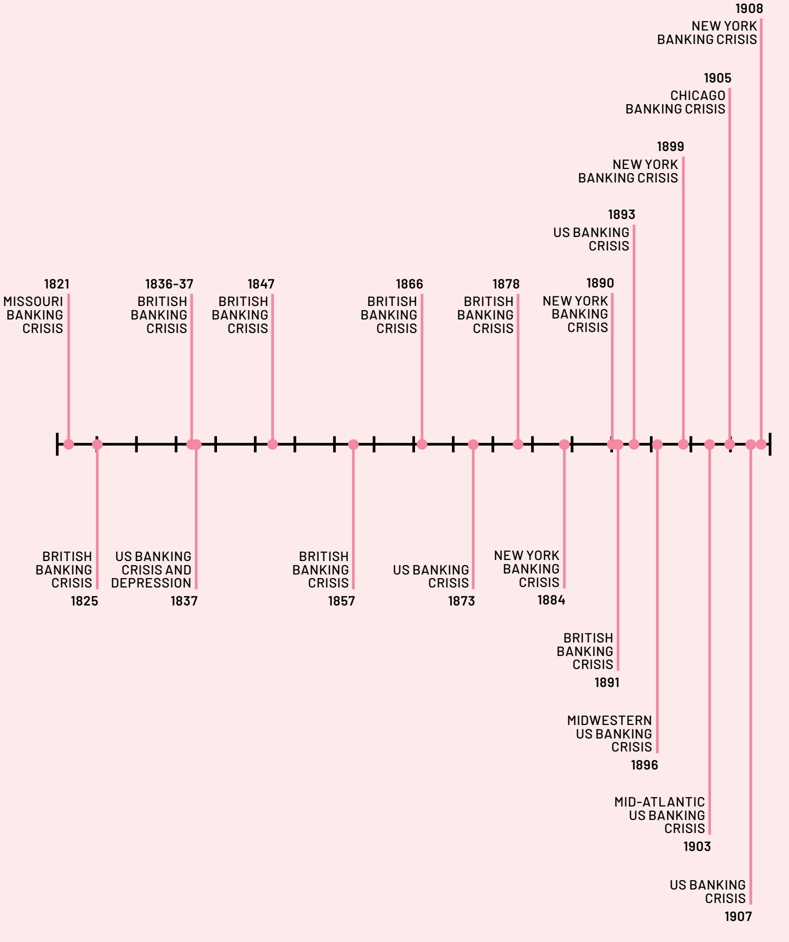
GOLD FUNCTIONED AS A MONEY SUPPLY EQUILIBRATION TOOL



At the first hint of instability or insolvency on the part of one or more banks, all participants had both the incentive to exchange currency for gold, and the legal right to do so.

The arbitrary assignment of a metal as the determinant of value for currency, and as a limit to its supply, did nothing to avert instability – indeed, it encouraged it.

US AND BRITISH BANKING CRISES UNDER THE GOLD STANDARD



Source: https://www.federalreservehistory.org/essays/banking-panics-of-the-gilded-age
https://www.researchgate.net/publication/299890635_British_Financial_Crises_in_the_Nineteenth_and_Twentieth_Centuries
https://www.stlouisfed.org/a-foregone-conclusion/chapter-one

THE BRETTON WOODS SYSTEM – EXORBITANT PRIVILEGE, NAKED POWER

In the final stages of World War II, with Allied victory relatively certain, one of the world's most influential living economists faced off against a US Treasury functionary to decide the fate of the non-communist world's monetary system.

John Maynard Keynes had been a leading economist for 30 years and *the* most exalted economist globally for over a decade. He set forth his ideas for a global balance of payments adjustment system using a new, international unit of exchange known as the Bancor, to be administered by an International Clearing Union. The system was elegant, flexible, fair and sought to avoid risks caused by extreme imbalances, both for deficit and surplus nations.

Squaring off against Keynes was a largely unknown economist, Harry Dexter White. He was no slouch himself, a PhD with degrees from Stanford and Harvard. He also happened to represent the nation that accounted for one-half of global industrial production at the time.[25] Readers can likely guess what happened.

> **Despite a clearly articulated explanation of a functional international balance of payments system delivered by such an esteemed economist, raw power won the day.**

In July 1944, at a holiday resort named Bretton Woods in New Hampshire, all key Allied powers agreed to install the US dollar as the dominant unit of exchange in all international transactions, and avoid any penalty or self-balancing mechanism for inveterate surplus-generating nations.

Why? Because the Americans were the preeminent creditor nation globally, and in White's words, they did not want to be repaid in "funny money".[26]

POST BRETTON WOODS – FROM CREDITOR TO DEBTOR AND ONTO FUNNY MONEY

The flaw in the Bretton Woods System, similar to those of the classical gold standard, is that it rested on the commitment of one country to provide two reserve assets: dollars, the supply of which is unlimited; and gold, the supply of which *is* limited. The problem was articulated as early as 1947 by Belgian born economist Robert Triffin – indeed the paradox became known as the 'Triffin Dilemma'.

> **This stated that should the US not provide enough dollars to fund a growing global economy, growth would be stifled and the system would grind into a deflationary rut; however, should the US provide ample dollar funding to promote global growth, then the backing of the dollar by gold would be thrown into question. The dollar would then become susceptible to the international equivalent of a bank run.**

American liabilities to foreigners first exceeded US gold reserves as early as 1960. Rapidly growing and efficient Germany and Japan found themselves posting large trade and current account surpluses and thus accumulating dollars throughout the 1950s and 1960s. Would these dollar reserves hold their value, when clearly gold backing for such large reserves was insufficient?

Speculation mounted against the dollar throughout the 1960s and institutional responses included the foundation of a Gold Pool to share the cost of meeting gold redemptions, the issuance of Special Drawing Rights by the International Monetary Fund (IMF) in an attempt to provide an alternative reserve asset (Bancor anyone?) and the use of exchange rate bands around the dollar known as the 'snake'. It was all too little too late.

In August 1971, after Britain requested a large redemption of dollars for gold in order to meet redemptions against the imperilled pound, US President Richard Nixon did the inevitable and suspended the convertibility of gold for dollars. It was never to be reinstated.[27]

Funny money indeed.

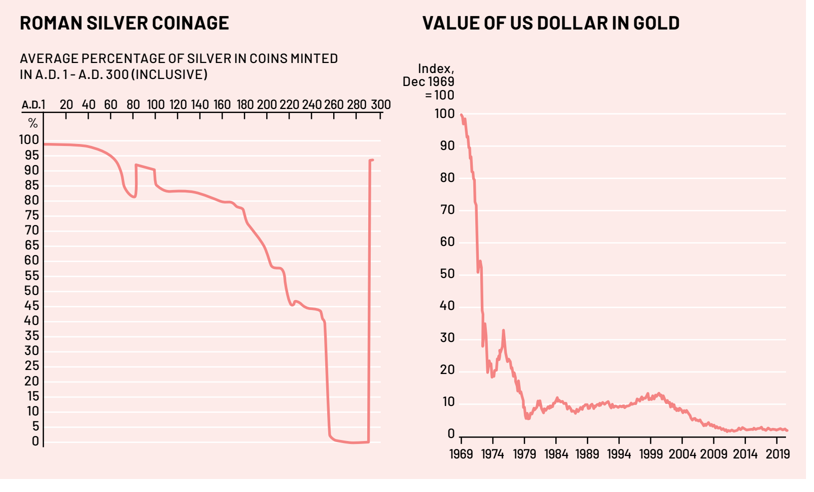
POST 1971: ADRIFT IN A FIAT OCEAN

Since 1971, global trade, investment and general economic activity have come to rest on floating currencies, unbacked by gold or any other 'hard asset' (i.e. fiat currencies). The US dollar has retained dominance of global transactions – it is used in approximately 85% of all foreign exchange transactions, with US exports only representing 13% of the global total and US foreign direct investment just 20%.[28]

> **The purchasing power of all currencies has utterly collapsed versus any form of hard asset – gold, commodities, real property and so forth.**

When charted beside the currency debasements of the late Roman Empire – the collapse in the buying power of the dollar since 1971 measured in gold looks similarly cataclysmic. In gold terms, the dollar has lost roughly 98% of its value in 50 years (see below).

However, the commercial world keeps turning. Economic agents continue to accept and use state-issued, unbacked fiat currency, the dominance of which is unchallenged, with alternatives, such as gold or crypto currencies, peripheral at best.[29]



Source: https://warwick.ac.uk/fac/arts/classics/staff/butcher/debasement_and_decline.pdf; Bloomberg.

A WORLD IN A DAZE: THE POST-GFC PERIOD TO 2020

The post-GFC period to 2020 was replete with breathless reporting about "unprecedented monetary policies" and some amount of fear about "Keynesian" excesses and "big government".[30] The trouble with that narrative was that it was untrue.

There was little unprecedented about the monetary response of policy officials globally – interest rate setting/manipulation, zero rates and bond buying were all features of the Depression-era monetary responses to the 1929 Wall Street Crash in many countries, notably in the US and Japan – albeit slower in most major economies and with highly unhelpful tariffs imposed globally.[31]

> Far from there being a wave of huge Keynesian policy responses, there was little fiscal support for major economies after 2010. Every major economy shrank their respective budget deficits from 2010 onward.

In Europe, Germany seized the opportunity of the crisis to discipline the spendthrift peripheral nations of the European Union (EU). In the US, the 2010 Tea Party revolution saw fiscal hawks become pivotal in the House, advocating for spending cuts and lower deficits. China's initial stimulus came in the form of bank-directed credit growth, which resulted in the deep financing reforms and industrial slowdown of 2013-16.

This contrasts with massive fiscal support unleashed in major economies in the 1930s by 'populists' in most major economies of the day.[32] Populists re-emerged toward the end of the 2010s and fiscal restraint began to erode, most notably in the form of the Trump tax cuts, which entrenched ~5% of gross domestic product (GDP) budget deficits as a permanent feature of US fiscal policy.[33]

There was also friction within Europe about the strictures of the EU's fiscal compact, which seeks to limit budget deficits to 3% of GDP and government debt to 60% of GDP.[34]

> We have written for several years about the emergence of populism and its largely overlooked core definition: populists spend money! Extraordinary shifts in public opinion about trade policy, socialism and nationalism have followed.[35]

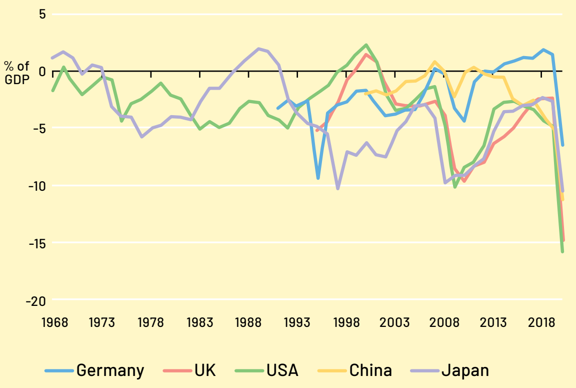
However, the *coup de grâce* of 40 years of austerity in fiscal policy may have come with the policy responses to the 2020 COVID-19 pandemic.

2020: THE *COUP DE GRÂCE* FOR AUSTERITY?

After 40 years of falling interest rates and declining/low inflation in the developed world, investors have been trained to believe that inflation is impossible. Central banks globally begged elected officials to spend money for a decade – and in general, they refused to do so in most large economies.[36] That was until 2020.

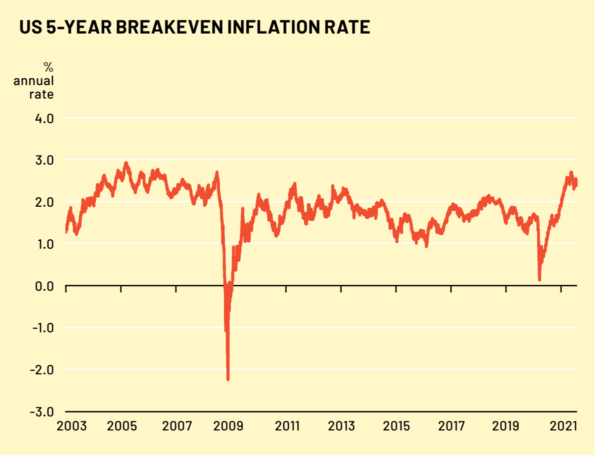
Just as the GFC saw the abandonment of monetary rectitude among central bankers, so the reaction to COVID-19 may have seen the abandonment of any pretence of fiscal discipline among elected officials in the developed world.

CENTRAL GOVERNMENT BUDGET BALANCES



Source: Bloomberg; OECD; Fitch. Annual data to 2020.

Correspondingly, inflation and inflation expectations rose dramatically.



Source: Federal Reserve Bank of St. Louis. Data as at 18 August 2021.

At present, debate rages about the permanence or transience of 2021's inflation surge. The breakeven rates for the US, currently project an inflation rate of 2.5% in five years' time, close to 20-year highs.

> **And we believe that inflation may well prove more durable than many foresee. However, more important is the insight that there is nothing remotely resembling a physical law that defines inflation.**

ON INFLATION

It is reasonably clear that no central bank, nor economic observer, has a robust, predictive model of inflation. One member of the Federal Reserve board is reported to have described inflation modelling in the early 2010s as "crap in, crap out".[37] US Federal Reserve (Fed) Chairs have shifted between a core and headline consumer price index (CPI) as their preferred measure of inflation.[38] Additionally, robust measures of inflation are rejected if they give problematic modelling results.[39] This is hardly a scientific approach.

It also seems reasonably clear that inflation is a multi-variate phenomenon, with causation stemming from diverse factors, such as wealth and income distribution, savings rates, money supply, and interest rates as well as institutional factors, such as the power of organised labour.

What seems absolutely clear is that Milton Friedman's aphorism that "inflation is always and everywhere a monetary phenomenon" is at best an oversimplification. See below for Paul Volcker's view:

> "...when we talk about credibility, I think far, far, too much emphasis is put on these monetary targets."[40]

Perhaps most powerfully – inflation may be what we expect it to be. This is the "rational expectations" school of inflation causation: no policy tool can be employed to fight (or encourage) inflation, unless it is expected to work by enough economic agents within a system.[41] It is worth remembering that in the late 1970s, it was accepted by virtually all serious economists that inflation was a persistent feature of the system.[42] This was on the cusp of the "Volcker Shock" and the taming of inflation for a generation.

Contrast this to the situation which presents itself now: there is close to universal consensus that inflation is transitory. Bond markets globally at the time of writing are strengthening, with yields falling and curves flattening, despite buoyant commodity prices, inflation expectations, business survey results and consumer expectations.

Moreover, just as Volcker was explicit about the need to tame inflation, today's central bankers appear resolute in their desire for increased inflation and perfectly comfortable with rates of inflation above target for periods of time.[43]

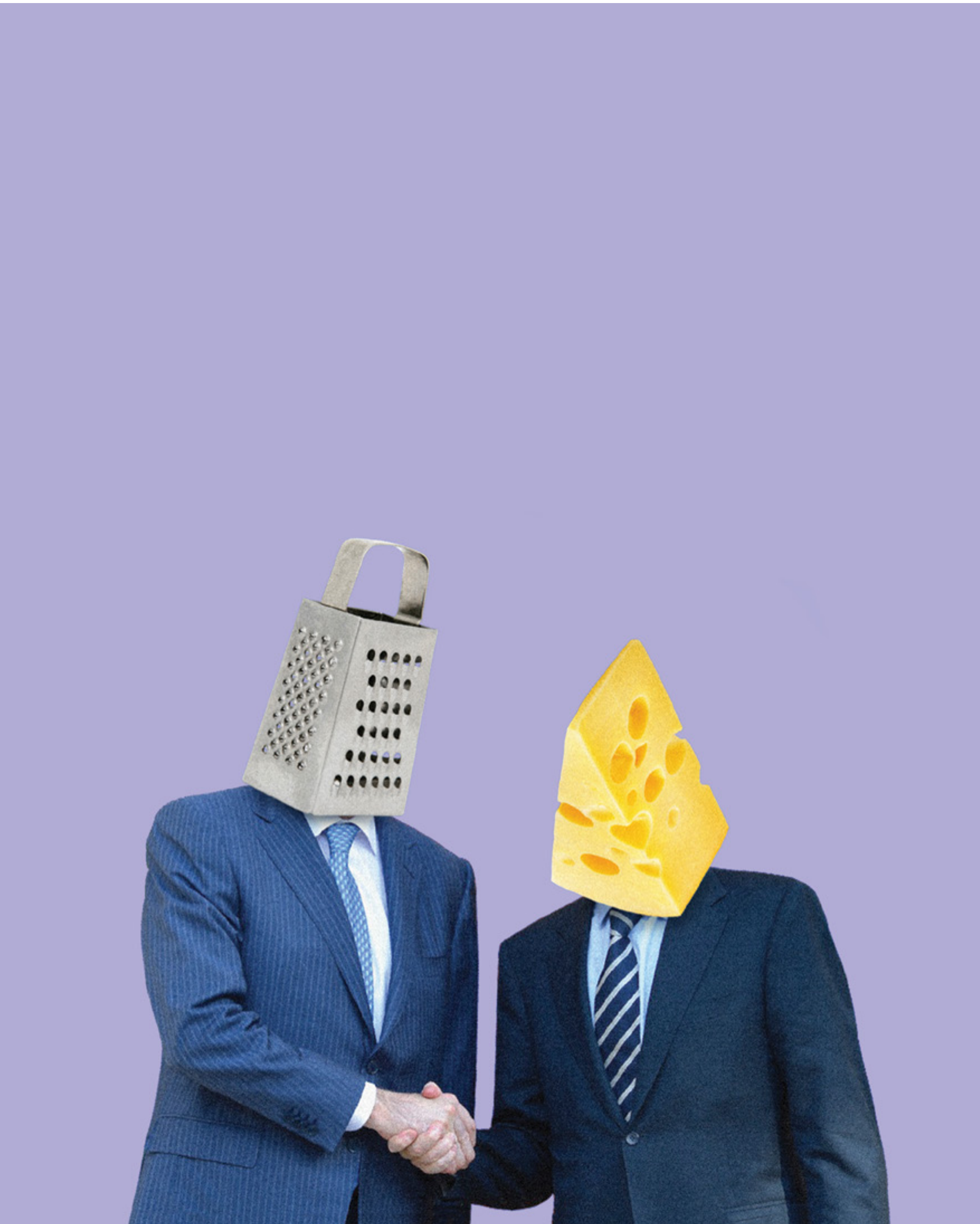
MODERN MONETARY THEORY

For well over a decade, a series of ideas have percolated around the fringes of mainstream economics, which appear to describe the functioning of monetary systems in the post-1971 fiat world well, those of Modern Monetary Theory (MMT). MMT provides a description of pure fiat monetary systems, which is sensible and robust, and corresponds well to massive debt accumulations seen by governments with deep capital markets and widely accepted currencies.

To summarise:

- There is little 'debt like' about government debt in its own currency – it can be extinguished instantly and is functionally an offset account to reserves in the banking system;
- Taxes are not solely collected in order to spend the money, as money can be created instantly via issuance of government bonds (remembering that these are just offset accounts to bank reserves) as well as in the banking system, where the vast majority of money creation occurs;
- Fiat currency maintains a value in part because citizens must pay tax in that currency;
- Taxes also have impacts on aggregate demand and by extension inflation and wealth distribution, and can be used to condition behaviour (e.g. 'sin' taxes);
- There is no inter-generational burden of government debt in a government's own currency – remember, it can be extinguished instantly;
- The consequence of excessive government bond issuance or direct money creation is currency weakness and inflation – NOT insolvency or penury.[44]

> **This framework provides a reasonable basis for understanding how Japan has accumulated colossal government debt, with no inflation, no currency collapse and reasonable economic outcomes.**



Real per capita GDP in Japan has grown comparably or even *faster* than that of the US since the peak of 'Japan mania' in 1989[45] and the country's ratio of employed persons to total population is *higher* than that of the US.[46] This has also been achieved with far lower income and wealth inequality than in the US.[47]

This would seem to be inconsistent with classical economics' notions of 'crowding out' or the existence of an inverse relationship between interest rates and inflation.

These are simply unobservable. An MMT explanation of the role of money and debt in fiat economies appears to offer a reasonable approximation of reality.

CONCLUSION

We would counsel against passive acceptance of consensus when thinking about a phenomenon as incredibly complex as inflation, especially in the face of monetary policy tools that allow for effectively limitless money creation, in combination with ambitious fiscal targets globally.

However, more profoundly, we would highlight the central point of this article – money is a fluid, social institution, and the governing structures around it – centrals banks, treasuries, monetary policy settings and tools – are all subject to profound change.

> **There is every chance that we are living through a period of such change, that decades of no change have shifted to weeks of decadal change.**

Fed buying of corporate bonds, unprecedented peace-time budget deficits, profound questioning of globalisation, massive transfer payments, unprecedented savings rates, and huge asset price surges, indicate there is ample evidence to suggest this.

POST SCRIPT: MONEY IS POLITICAL

In the last two centuries, Britain and the US, both creditor nations, embraced and expanded forms of a gold standard, but when their trade and current account positions slipped into deficit, they pushed for revaluations, and finally abandoned their respective versions of a gold standard altogether.

Britain lacked the economic and military power to retain reserve currency status without gold backing. The US remained the dominant military and industrial power globally after 1971 and its power increased in subsequent decades given the decline and fall of the Soviet Union and related communist states. And of course, the dollar retained reserve currency status.

The loudest voices clamouring for 'hard money' systems tend to be creditors, or those ideologically aligned with them. There is a distinct moral overtone to gold standard/hard money arguments.

Take for example Jim Rickard's view:

> "A gold standard is the ideal monetary system for those who create wealth through ingenuity, entrepreneurship, and hard work. Gold standards are disfavored by those who do not create wealth but instead seek to extract wealth from others through inflation, inside information, and market manipulation."[48]

How, precisely, the use of gold in monetary policy would avoid market manipulation and the use of inside information escapes your humble author. Any passing knowledge of the 1920s will suffice to dispel such a notion.[49]

There is also a tendency to millennialism and dark prophecy, such as Ronald Reagan's statement before the 1982 election that:

"No nation in history has ever survived fiat money, money that did not have precious metal backing."[50]

The glaring logical fallacies here are that vanishingly few nations in history have survived having any form of currency, or anything for that matter – all nations fall eventually – and that all nations in existence today *have* unbacked currencies.

The delicious irony is that economic policies under US President Reagan saw fiscal deficits, which increased the level of national debt from 22% to 38% of GDP.[51]

So much for prophecy.

> **The Cantillon Effect: Money may *not* be neutral. If money enters circulation at a specific point, say the banking system, then inflationary effects may have an outwardly radiating effect, allowing early holders of the 'new' money to benefit in terms of spending power.[52]**

To demonstrate – imagine that it is 1610, and a huge shipment of gold arrives in Spain from the New World, and that the influx of gold goes on to trigger inflation. Now, imagine that prior to docking, one of the sailors takes a tender and races to shore to spend his share of the gold. He gets the advantage of spending the gold, before the inflationary impact of the rest of the bullion on the economy is felt, thus enjoying a possibly significant benefit in terms of buying power versus other people in Spain affected later by the increase in money supply.

Now, imagine that a hedge fund manager is a close counterparty with a money centre bank, and that the Federal Reserve injects huge levels of funding into the banking system to shore it up in a period of volatility. The hedge fund manager may benefit from that liquidity before virtually anyone else in the economy given the rapidity with which they can draw on credit via their banking relationships, access to capital, and ability to deploy that capital rapidly.

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2 See for instance: *https://www.forbes.com/sites/peterpham/2017/11/20/what-is-money/#3c2a124816ea*

3 This set of ideas is taken from David Graeber's excellent work *"Debt: The First 5,000 Years"*, Melville House, Brooklyn, 2011. See especially pp22-28

4 Ibid, pp212-214

5 Yuval Hariri, "*Sapiens: A Brief History of Humankind*", Vintage Books, 2011, p131

6 See for example: *https://coinweek.com/ancient-coins/ancient-coins-wealth-persian-empire/*

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11 See for example: *https://www.economist.com/briefing/2017/04/27/the-history-of-central-banks*

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13 *https://www.parliament.uk/about/living-heritage/evolutionofparliament/parliamentaryauthority/revolution/overview/financialrevolution/*; *https://www.bankofengland.co.uk/about/history* ; *https://www.economist.com/briefing/2017/04/27/the-history-of-central-banks*

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15 Ibid. Also *https://www.royalmint.com/discover/uk-coins/sir-isaac-newton/*

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17 *https://oll.libertyfund.org/titles/laughlin-the-history-of-bimetallism-in-the-united-states-1898/simple#lf0073_label_056*; Milton Friedman, "*Bimetallism Revisited*", Journal of Economic Perspectives, Volume 4, Number 4, Fall 1990

18 Liaquat Ahamed, "*Lords of Finance: 1929, The Great Depression and the Bankers Who Broke the World*", Random House, 2009, p168

19 See for example: *https://www.economist.com/buttonwoods-notebook/2010/03/25/currency-controls-and-greshams-law*

20 Metzler, pp29-33

21 Eichengreen, pp15-18

22 From Metzler, p19

23 See for example: "*Long-Term Trends in Life Expectancy and the Consequences of Major Historical Disasters*", *https://www.demogr.mpg.de/books/drm/009/part1.pdf*, p6

24 Edward Chancellor, "*Devil Take the Hindmost: A History of Financial Speculation*", Plume, 2000, p121; *https://www.federalreservehistory.org/essays/banking-panics-of-the-gilded-age*

25 Eichengreen, p39

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31 Ray Dalio, "Principles for Navigating Big Debt Crises", Greenleaf, 2018; see also Chancellor, chapter 7; Richard J Smethurst, "*Takahashi Korekiyo, Japan's Keynes: From Foot Soldier to Finance Minister*", Harvard, 2007

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34 *https://www.europarl.europa.eu/factsheets/en/sheet/89/the-eu-framework-for-fiscal-policies*

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