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MONETARY REFORM: GOOD, BETTER, BEST

When I was a young person still in high school, the locker room of our gymnasium had the following message on a sign at the entrance: *Good, better, best; may we never rest until our 'good' is 'better' and our 'better' 'best'.*

As a student working on a master of liberal arts degree many decades ago, I chose as my final project to research and write on the history of monetary systems. Studying this history through the lens of my own experience working in the U.S. financial sector convinced me that the existing system of monetary creation, banking and credit issuance is a fundamental cause of economic, social and political instability. When combined with centuries of landed privilege, the inevitable consequence is the accelerating concentration of income and wealth the world's population is experiencing.

Throughout the last four hundred years (or, actually, the last four thousand years) bankers again and again have shown themselves willing to take inappropriate risks with both their own money as well as deposited money. When public confidence has eroded for any reason, depositors galloped to their bank to withdraw their money before it was too late. The bankers panicked and exercised call provisions on loans they made to people. The borrowers panicked and sold assets in order to raise money to repay the banks. The contraction of economic activity spread. Regions, then nations fell into depression or worse.

After one of the greatest of depressions hit the world in the 1930s, governments in many countries were pressured by their people, generally, and by various vested interests, particularly, to do something to mitigate the potential for this to happen ever again. Even so, there was a great reluctance to admit that the world's central banks (i) either had insufficient tools with which to respond to the global economic problems; or (ii) failed to effectively use the tools they possessed. One of the easiest reforms to introduce turned out to be deposit insurance. Banks would contribute to a fund to be used to guarantee depositors their money could be withdrawn even if the specific bank had insufficient assets to honor the demand. The viability of deposit insurance depended on a combination of appropriately assessed premiums based on regular analysis of bank financial statements, and an understood commitment by the central bank and/or government treasury to act as *lender of last resort*.

Absent what in relatively modern history served as honest monetary creation, namely the issuance of receipts for gold and silver coinage held on deposit, governments in almost all countries passed legislation establishing a government-supervised central bank. The central bank was authorized to print (and, more recently, to create in digital form) central bank notes in whatever quantity the banking authorities deem necessary to meet the aggregate public and private sector needs. These bank notes are the primary form of legal tender used to pay for services and pay taxes, supplemented by whatever non-precious metal coins are minted directly by the government.

What perplexes many reformers (myself included these days) is why a central bank should be in a position to create new money out of thin air, then use this new money to invest in/purchase government securities that yield interest. In this process, government incurs debt that must be serviced and, if not retired, refunded again and again. And, in order to service this debt, the income and assets of citizens is subjected to taxation. Given the escalating level of public debt carried by many governments, one has to wonder where the money will come from to both service debt and fund public goods and services.

An argument is being made by some proponents of *modern monetary theory* that those governments issuing sovereign currency could solve the debt problem by using this currency (rather than central bank notes) to purchase maturing securities from private holders. There is nothing preventing the central bank itself from doing the same thing. This solution meets the 'good' test. The path to 'better', I believe, is to gradually retire all central bank notes and replace them with debt-free currency issued by the government treasury which would then be spent into the economy either directly or by means of grants to lower levels of government and as a universal basic income allocation to each citizen. As Thomas Paine first suggested in his tract *Agrarian Justice*, an annual contribution could be made into a trust account for young persons, accessible when they reach the legal age of competency. However, getting to 'best' as a monetary structure would still require establishing a system of deposit banks.

It must be admitted that the mining of gold and silver in order to create coinage money is a practice that is both environmentally damaging and a waste of natural resources, labor and capital goods. This does not mean that a monetary system attached to a universally-available tangible good is by definition problematic. There are any number of goods that have all or most of the positive characteristics of coinage minted out of precious metals and none of the negatives. One such good (recommended some years ago by economics professor James Buchanan) is the construction brick. Construction bricks are easy to produce, they last almost forever without deteriorating, they have a stable demand in markets everywhere around the globe, they do not require expensive systems of storage and protection from theft, and the process of production is (by comparison to coinage) environmentally sustainable.

In conversation with a colleague, it was pointed out to me that the demand for construction bricks is declining in the face of less costly more efficient construction materials. So, perhaps, the analysis put forward by Professor Buchanan is now impractical. The issue remains whether monetary units are best denominated in something tangible, something that time has proven to maintain reasonably stable exchange value but without the limitations and problems associated with precious metals. The history I have briefly presented reveals that severing this relationship has proven to establish the conditions that – in conjunction with repeating cycles of boom and bust of land markets – shift all resources, financial resources included, away from productive economic activity in favor of speculation. On the other hand, perhaps what passes for money is less important than how the money supply is created and managed. Paper currency is these days used to a great extent in the underground economy in order to evade the police powers of the state. Most consumer transactions are processed using a debit or credit card. The balance of one party is increased, that of the second party decreased, and one or both parties are charged a processing fee by the card company.

Where does all this leave us? As I am writing this article, I have been sitting in on a series of lectures by someone who has spent the last two decades studying the problems I have described above and what he has learned from the debate over monetary issues between two economists -- Silvio Gesell and John Maynard Keynes. Gesell's position was essentially that money should act as a medium of exchange only and not a storehouse of value. Money should over time be designed to lose its exchange value, at, say, a rate of five per cent per annum. Holders of money would, therefore, has a significant financial incentive to actually invest their money in tangible capital goods and other types of income-producing property in order to prevent any loss in the value of owned assets; and, of course, to generate additional income.

No doubt the times and circumstances have dramatically changed since Henry George offered his own set of insights on what would constitute the most stable, efficient and just monetary structure. Perhaps his most astute observation was expressed in his final book, *The Science of Political Economy*: "The truth is that there is no universal money and never yet has been." So, the search continues.