The Money Muddle

By Oscar B. Johannsen

The volatility of the stock market with increases of 100 or more in the Dow Jones Industrial Average one day, only to be succeeded by 100 or more decreases a few days later, has led to concern that this behavior may presage a recession or even a depression.

On the other hand, despite the fact that such indices as the Consumer Price Index (CPI), now about 2%, are low, there is fear that prices of goods and services are actually rising significantly, bringing into question the validity of such indices as the CPI.

Most people believe that inflation consists of rising prices (price inflation). But inflation is a monetary phenomenon. Simply put, inflation means too much money chasing too few goods. That the article which the government calls money is flowing out into the marketplace at a rapid pace is obvious. It is growing at the rate of eight to nine percent annually. This is higher than what is termed an acceptable rate of growth.

Are we faced with a recession-depression or inflation? The Federal Reserve governors apparently believe inflation is the more likely scenario, and they should know, as they have been increasing the so-called money supply almost constantly, and only recently have pulled back with increases in the Federal funds rate. To do this, they must decrease the money supply. The problem is that the monetary authorities do not know any more than anyone else what the correct amount of money should be.

Dr. Milton Friedman, the eminent monetary expert, believes that the Federal Reserve is almost invariably wrong in its prognostications, so it should increase the money supply at a fixed rate, and not attempt to do the impossible.

The fundamental problem is that the government has made money its monopoly, which it administers by means of the Federal Reserve System. What it treats as money consists of the Federal Reserve paper currency which we all carry in our wallets. A paper dollar is actually a non-interest bearing debt of a Federal Reserve bank which is guaranteed by the government. It is just a promissory note. At one time it was a promise to pay a dollar's worth of gold. Technically, the definition of a dollar is that it is 1/42.22 of an ounce of gold, or, as it is usually put, the official "price" of gold is $42.22 an ounce. Thus, if you present to a Federal Reserve bank 42 paper dollars and 22 cents, it should give you an ounce of gold. But, of course, it will not. The government has simply ignored its guaranty and, instead, called the Federal Reserve currency legal tenure which can be used to pay debts, purchase goods, and pay taxes.

The sad fact is that unless there is a greater understanding by the public that money, in a sophisticated society such as ours, is gold, and not mere paper (promises which are never kept), the so-called money supply will keep on increasing, prices will keep on rising, and the pubic will blame the businessman, the grocer, the butcher, the tailor, everyone but the real culprit — the government.

It has been estimated that the purchasing power of the paper dollar since 1933 has fallen more than 90%. Thus, what used to cost 10 cents in 1933, today costs about $1.00. The 2¢ stamp in 1933 now costs 33¢, or over 15 times more; the 5¢ subway ride now costs $1.50, or 30 times more. Much more anecdotal evidence could be cited, but is unnecessary, as everyone is aware that prices of goods and services are constantly rising.

What is likely to occur? It could well be that some unforeseen disturbance in the economy might give rise to a fear that a depression will ensue, and people, particularly in the stock market, will begin panic selling, causing a big drop in stock prices. If the market will continue falling, the Federal Reserve will be in a quandary. On the one hand, its Chairman has been publicly concerned with what he calls the "exuberance" of the market. Thus, any correction should be welcomed, so one would think. But too big a drop would bring pressure on the Federal Reserve to do something. In 1929, it is claimed, the Federal Reserve did all the wrong things. It tightened money, and the government passed legislation raising tariffs to protect industry — all of which made matters worse.

It seems most likely since the American public has never been involved in an inflation of any scope as that in Germany in the early 1920's, that the Federal Reserve will be more concerned with a depression than an inflation, so it will increase the money supply in sufficient amounts to abort any depression. The gamblers in the stock market will be delighted, much of the public will approve, but those on fixed incomes will really pay the price. Not only will stock prices stop falling, and probably increase, but prices of all goods and services will rise. There will be too much money chasing too few goods, especially as business will cut back on production, so increases in goods will not keep pace with the increases in the amount of money in the marketplace.

The fundamental problem is caused by our system of land tenure, which gives spectacular gains to many lucky landowners but causes the economy to be unstable, resulting in booms and busts. The Federal Reserve tries the impossible, attempting to eliminate the booms and the busts with its monetary policies of one sort or another, but in the main, it only makes matters worse.

Until we have a just system of land tenure and a money based on a commodity such as gold, and not on paper promises which are never kept, we must reconcile ourselves to living in an economy which suffers from continual ups and downs which no one understands, and causes all kinds of problems, both monetary and personal.