THE ECOLOGY OF MONEY

by Richard Douthwaite

Introduction and Summary

Most people think that there's only one type of money because one type is all they've ever known. They know about foreign currencies but they see these, quite correctly, as essentially the same sort of money as they use in their own countries. They also know about cheques, credit and debit cards, credit notes, and several of the other forms that money can take but, correctly again, regard these simply as special purpose versions of notes and coins. Money is money, they think, regardless of the form it takes. Only the few who know a little monetary history, or are members of a Local Exchange Trading System (LETS), realise that this is not the case. There are, potentially at least, many different types of money and each type can affect the economy, human society and the natural environment in a different way.

Most economists think that there's only one type of money too. That is when they think about it at all. The profession, to quote two sociologists is: "curiously uninterested [in the topic], restricting itself to discussions of price, scarcity and resource allocation with no specific interest in money as such."[1]. David Hume, one of the founding fathers of economics, referred to money as "the oil which renders the motion of the wheels smooth and easy" [2] and this attitude persists to this day. Indeed, Paul Samuelson's well-known economics textbook defines economics as: "the study of how men and society choose, *with or without the use of money*, [my italics] to employ scarce productive resources" [3].

In other words, economists see money acting as a catalyst that eases and speeds up economic interactions that would have taken place anyway. Naturally, they are interested in the amount of money reaching circulation because that affects the pace at which the economy can run, consequently determining whether national income rises or falls. However, very few seem to have ever considered the possibility that the particular type of monetary catalyst in use might be affecting the outcome of the economic interaction. Or that if other forms of money were used the results might be quite different. The only economists even to glance in this direction are either Marxists or members of the Social Credit movement who, because of the nature of their beliefs, have cause to analyse and question the nature of money more closely than more typical members of their profession. The last big-name economists to concern themselves with different forms of money and their effects were Maynard Keynes,[4] Henry Simons and Irving Fisher in the 1930s, a period in which the money system was quite clearly dysfunctional.

This Briefing will show that history is littered with examples of monetary systems that operated on quite different lines to the one we know at present. If these systems had survived, they would have produced cultures most unlike today's unsustainable, unstable global monoculture. The Briefing will demonstrate that different money systems affect the world in different ways. Ecology is defined as: "the study of the set of relationships of a particular organism with its environment."[5] Consequently, anyone who is unfazed by regarding money as an organism can consider this book an ecology of money. Some of the more enlightened economists will probably be happy to do so. Professor Paul Ormerod, whose books have done much to alert the public to the problems within his profession, writes that: "conventional economics is mistaken when it views the economy and society as a machine whose behaviour, no matter how complicated, is ultimately predictable and controllable. On the contrary, human society is much more like a living organism - a living creature whose behaviour can only be understood by looking at the complex interactions of the individual parts."[6]

Certainly, if we wish to live more ecologically, it would make sense to adopt monetary systems that make it easier for us to do so. Note the plural here. It is not just a case of exchanging a monetary system that emerged as a result of a series of historical accidents for one with a conscious design. As each money system tends to lead to a particular set of consequences, we are likely to have to use three or four money systems simultaneously to produce the combination of characteristics that we want our society to possess.

Questions to ask

Young journalists are taught to ensure they answer six questions in every story they write - Who? What? When? Where? Why? and How? This Briefing asks these same questions of every type of money discussed: commercially-produced money; people-produced money, and government-produced money.

1. Who issued the money? Was it the state, a financial institution, or the users of the money themselves?

2. Why did they do so? Was it as a method of taxation, to make a profit for their shareholders, or simply to provide the users with a means of exchange?

3. Where was the money created? Was it in the area where it was going to be used? Or was it elsewhere, with the result that would-be users had to sell goods or services outside their area to collect enough of money to be able to trade among themselves?

4. What gives the money its value? Is it backed by gold (or another commodity), a promise of some sort, or nothing at all?

5. How was the money created? Was it by people going into debt to a central organisation? Or did the users simply agree to allow each other credit and generate it among themselves?

6. When was the money created? Was it done once, several times, or continuously as part of a system of creation and destruction that caters for people's trading needs?

We'll ask a seventh question too:

7. How well does (or did) it work? Economics textbooks state that money serves three main functions, so we need to assess a currency's performance in relation to them all. In other words, we should check how well each type of money serves:

A. A medium of payment or exchange. A good payment medium makes it easy for people to buy and sell to each other. This means that it must be generally acceptable and have a high value for its weight so that it is easy to transfer from buyer to seller. It must also be divisible, so it can be used for small transactions as well as large ones. And while there needs to be enough of it around (to enable everyone who wants to buy or sell to be able to do so easily), there must be some limit on its availability so people keep their confidence in it and its acceptability is maintained.

B. A store of value. A currency is a good store of value if someone receiving it is able to use it to purchase the same amount of goods and services regardless of when they spend it - next month, next year, or when they retire.

C. A unit of account. Is the monetary unit a good one in which to keep financial records and to quote prices? Normally, people keep their accounts and quote prices in the currency they use most frequently, but in times of uncertainty, or high inflation, they may use another currency instead. During the German hyperinflation in the early 1920s, for example, shopkeepers quoted their prices and kept their records in US dollars although their customers were paying in marks.

There are circumstances in which these three roles can come into conflict with each other. When prices are falling rapidly, for example, the 'store of value' property of money becomes extremely attractive and people begin to hoard whatever money comes their way in the knowledge that they will be able to buy more with it later on. This naturally interferes with the ability of the currency to act as an effective means of exchange. Shortages of money develop and normal trading becomes difficult. In the 1930s, businesspeople even had to invent special currencies - the Swiss Wirtschaftsring (see Box 3) is a notable example - so that they could settle accounts among themselves. If, on the other hand, prices are soaring rather than falling, money becomes a poor store of value and holders rush to spend it as soon as they can. This leads to prices rising more rapidly still. In view of these conflicts, it seems doubtful whether countries that limit themselves to the use of just one form of money can expect all three functions of money to be adequately satisfied.

Plan of action

The first three chapters of this Briefing explain how the characteristics of money are determined by the way it is created and then put into circulation. Chapter One (Commercially-Produced Money) explains that the commercial banks create almost all the money that we use and put it into circulation by allowing us to borrow it from them. It goes on to explore the consequences of this rather odd arrangement, among which are the present economic system's chronic instability and insatiable need for growth.

Chapter Two (People-Produced Money) deals with the amazing monies that people have created to use among themselves. These include American tobacco warehouse receipts, inscribed clay tablets representing quantities of Egyptian wheat, and carved stones in the South Pacific too heavy for anyone to carry. Strings of seashells and today's LETS fall into this category too. The important feature about all these currencies is that they are only created when the society involved has resources, usually of human labour, which it wants to put to better use.

Chapter Three (Government-Produced Money) shows how, down the centuries, this form of money has often caused serious inflation as it has been used as a system of tax collection. Henry VIII, for example, added large amounts of copper to the silver from which he made his coins so that he could make more of them. As a result, prices doubled and a rebellion broke out. Despite this ominous precedent, we discuss a current proposal that governments should create any additional money their countries need and spend it into circulation. If this system were introduced in Britain, it would allow tax cuts of around 16%.

Chapter Four (One Country: Four Currencies) attempts to weave all these threads together by devising a multi-level multi-currency system which would ease the world's transition to sustainability by improving the way which the economy allocates scarce resources between the present and future generations. It proposes an international unit-of-account currency whose value would be based on the right to emit greenhouse gases. This would be linked, through a currency exchange market, to national currencies that were only used for trading and were not expected to hold their value over long periods of time. Special currencies would be launched to fulfil the store-of-value function. Lastly, local currencies would have a strong role to play. as they would not only be used to overcome local shortages of national currency but also to raise funds for special purposes.

No consensus

The most important feature of this Briefing is its insistence on three things.

1. All monies should be created by, or on behalf of, their users and not by institutions wishing to profit from the activity.
2. Different types of currency have to be used concurrently if the three key functions of money are to be adequately performed.
3. The international unit-of-account currency, to which all other monies would be related, has to represent, and thus protect, a truly scarce resource. In other words, when we save money, we should also be saving something vitally important, like the integrity of the natural world.

This Briefing is not, therefore, a judiciously balanced, middle-of-the-road report on some emerging consensus in the currency-reform area. Such a document would be impossible to write as, apart from the widespread and long-standing agreement that governments rather than banks should put money into circulation, monetary reformers don't seem to agree about anything. Instead, this Briefing is an attempt to discover why the present economic system breaks down catastrophically if economic growth fails to occur. It also suggests how the monetary system could be reformed to remove this defect, which obviously stands in the way of our achieving a sustainable world.

I don't expect everyone to agree with the conclusions I've reached. One friend, whose opinions I value, wrote, "this looks like being an extremely stimulating and thought-provoking Briefing." I understood this to mean "You've gone too far," particularly as his letter went on "You may be running a risk if you publish firm proposals, as presented in this draft, [that you will] find quite soon that you want to change them significantly." In other words, I'd gone much too far and might want to retreat. I've decided, however, to accept the risk of this happening and not to water things down. However, all the ideas I discuss are under development and if they change as a result of a debate provoked by this Briefing, their publication will have been worthwhile.

No reader should feel that they need to understand every paragraph completely before moving on, though I hope that they will be able to do so. If, when they reach the end of the book, they accept the urgent need for a radical restructuring of the money-creation system and have some sort of feeling for the general direction the restructuring should take, that should be quite enough.

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