

Ideal Money and the Motivation of Savings and Thrift

Introduction

I have been talking, at meetings, about my ideas on the topic of Ideal Money for a few years now while the world, by coincidence, has passed through and into some financial/economic crises that have been quite interrelated to the systems or varieties of money that have been recently in use.

For example, most recently, the difficulties that derived from the national debt of Greece, which is currently defined in terms of euros whereas it had been, earlier, defined in terms of drachmas; these difficulties have led to extreme "bail out" actions and to global fears and reactions.

And earlier the "panic of 2008", which was quite severe and somehow very reminiscent of the American "panic of 1907", seemed to derive from causal factors in the USA which linked with the traditional array of efforts provided by federal support and/or subsidies for the building of single-family homes.

(So there, somehow, came into being a flood of "sub-prime

mortgages" which led to floods of "derivatives" which were, unjustifiably, advertised as being of high "investment grade"). (This economic crisis had a particularly dramatic impact in Iceland through an enterprise there called "Icesave".)

General Considerations and History

The special commodity or medium that we call money has a long and interesting history. And since we are so dependent on our use of it and so much controlled and motivated by the wish to have more of it or not to lose what we have we may become irrational in thinking about it and fail to be able to reason about it as if about a technology, such as radio, to be used more or less efficiently.

We present the argument that various interests and groups, notably including "Keynesian" economists, have sold to the public a "quasi-doctrine" which teaches, in effect, that "less is more" or that (in other words) "bad money is better than good money". Here we can remember the classic ancient economics saying called "Gresham's law" which was "The bad money drives out the good".

The saying of Gresham's is mostly of interest here because it illustrates the "old" or "classical" concept of "bad money" and this can be contrasted with more recent attitudes which have been very much influenced by the Keynesians and by the results of their influence on government policies since the 30's.

Digression on the Philosophy of Money

It seems to be relevant to the politics of state decisions that affect the character of currency systems promoted by states that there are typical popular attitudes in relation to money. Although money itself is merely an artifact of practical usefulness in human societies and/or civilizations, there are some traditional or popular views associating money with sin or immorality or unethical or unjust behavior. And such views can have the effect that an ideal of good money does not seem such a good cause as an ideal of a good public water supply. There is also, for example, the Islamic concept which has the effect of classing as "usury" any lending of money at interest.

(Here we can wonder about what sort of inflation rates might have been typical for any major varieties of money, such as Byzantine money, at the times actually contemporaneous with the Prophet Mohammed.)

In general, money has been associated in popular views with moral or ethical faults, like greed, avarice, selfishness, and lack of charity. But on the other hand, the existence of money often makes it easy to make valuable donations of philanthropic sorts and the parties receiving such contributions tend to find it most helpful when the donations are received as money!

But the New Testament story about "money changers" being driven from the Temple illustrates clearly the idea of putting the clearly mundane and possibly "unclean" utility of money at some distance from where that money would presumably continue to be received when used as a vehicle for donations.

Economics has been called "the dismal science" and it is certainly an area of studies where "the mundane" is appropriately studied.

And philosophically viewed, money exists only because humanity does not live under "Garden of Eden" conditions and there are specializations of labor functions. So we are always exchanging, mediated by money transfers, the differing fruits of our varied forms of labor.

Welfare Economics

A related topic, which we can't fully consider in a few paragraphs, is that of the efforts to be made by the national state and society in general for dealing with "social equity" and concerns for the general "economic welfare". Here the key viewpoint is methodological, as we see it. HOW should society and the state authorities seek to improve economic welfare generally and what should be done at times of abnormal economic difficulties or "depression"?

We can't go into it all, but we feel that actions which are clearly understandable as designed for the purpose of achieving a "social welfare" result are best. And in particular, programs of unemployment compensation seem to be comparatively well structured so that they can operate in proportion to the need.

And public works projects allow the wealthy to pay through taxes to provide jobs for workers and these can produce valuable works if the projects are well planned.

If the argument is given, like in a context of partisan political differentiations, that business and economic activity should be "stimulated" in order to reduce the unemployment statistics, then many special interests, within a national economy, may hope to benefit before the unemployed workers (who are stationed lower in the pyramidal structure of a national economy) receive enough benefits so that the statistics of unemployment become moderated.

Honesty is the Best Policy

When I spoke at an economics meeting in Tampa, Florida, in 2001, on the topic of "Ideal Money". I suggested the use of an "ICPI" index for the definition of the proper value for an "ideal" money. Here ICPI stood for "Industrial Consumption Price Index" (which would be a sort of index which could naturally be calculated from world market prices).

But I did not have any specific proposals, like prices for copper, or platinum, or electric energy to suggest for the index.

Now, after some years of thought and observations, I feel that the sort of authority or agency that would be able to establish any version of ideal money (money intrinsically not subject to inflation) would be necessarily comparable to classical "Sovereigns" or "Seigneurs" who have provided practical media for use in traders' exchanges. We can prepare to appropriately respect the functioning of such an agency (conceivably like the IMF or BIS or ECB) and concede to the effective agency some discretion about the specific form of a guiding index of prices.

But here is where I see the importance of honesty, as if like the honesty of a well-regarded classical European monarch or emperor. Sometimes the people in the USA have been told things like "inflation is not a problem" when statistics compiled by the Labor Department (following "classical" rules) indicate that there is, indeed, ongoing inflation.

If an appropriately honest government-like agency is to issue the actual currency, and to provide for the

central bank deposits denominated in terms of that currency, for a money system, then it can also, naturally, compute the indexes that would measure the presence or absence of inflation or deflation. My position is that the appropriate "target rate" for measured inflation is zero. In recent times, after the unsurprising breakdown of the IMF-sponsored system of fixed exchange rates, there have been globally varying patterns of inflation linked to the varying national or regional currencies. If the Canadian money unit is "targeted" for 2% inflation and if it gains in value compared with the unit of the USA then this suggests that the actual recent inflation rate for the currency of the USA is at least 2%.

My natural presumption is that the authorities responsible for national currencies, during this time period (since 1971), have effectively calculated their strategies on a basis of how respectable (from a classical viewpoint parallel to "Gresham's Law") they seek to appear to be, in comparison to other national paper fiat monies and in comparison to the US dollar.

Some History of Institutions Created to Promote Savings by Individual Savers

The first case of a "Postal Savings Bank" was established

in the UK in 1861 paying interest at 2.5 %. In the USA a comparable system was established in 1911 but was discontinued in 1966 (although "postal money orders" continue to be available). When visiting Shenzhen in China recently as a tourist, I was surprised to see a "Postal Savings Bank" in existence there. And I later learned that at this time the largest such national system is that in Japan.

The "Savings and Loan Associations", or the variously named institutions with analogous descriptive names, originated in the UK in the midst of the era of "strong money", when the British pound was on the "Newtonian" gold standard. Around 1770 the comparable savings institutions in the UK were those called "building societies".

Earlier in their modern history the "savings and loan associations" in the US had a separate insurance corporation established to protect their depositors which was the FSLIC and which was directly parallel to the FDIC corporation which insured deposit account balances in ordinary "commercial banks".

But when the great tide of inflation flowed in from Washington's definitive break (in 1971) with providing, for the IMF member states, a gold quota for the dollar, and with various cases of corruption in the S. & L. area that arose

derived from relaxation of earlier versions of strong regulatory standards, the result ultimately was that the FSLIC (which had borne the great weight of bailouts) was simply abolished and all of its remaining insureds were put under the umbrella of the FDIC (which had previously also insured the institutions called "savings banks" besides of its main function of insuring small or modest sized deposit accounts in retail commercial banks)).

Before being effectively terminated, the "S&L's" in the USA were perhaps comparable to "Icesave" and that comparison suggests also how their investments may have had weaknesses with regard to risk probabilities. So, under extreme variations in the general economic/financial climate, they were not able to survive (although their customers were generally comfortably protected by the FSLIC insurance program).

Conditions for the Attractiveness of Savings Accounts

An individual of the species "homo oeconomicus", blessed, we presume, with the facility of "rational expectations", can be imagined in the situation of needing to decide on whether to put money into a "savings account" or perhaps to follow

some other strategy with his money, over a period of time.

It is not widely advertised by American financial or banking institutions, but the rate of interest that they would pay on deposit or "money market" accounts might be lower than the rational expectation for the rate of inflation relevant for the national currency.

So should the "economic person" rationally decide to "save", using such a channel for the depositing of his money, or, perhaps, should that person decide to go early into a housing purchase for which he/she might need to borrow money, perhaps under the conditions applicable to "sub-prime" borrowers?

It is obviously not simply "thrifty", but under conditions of uncertainty about the continuing value of the national currency it could, indeed, be the more rational choice to go earlier into the house purchase rather than to wait to develop a stronger basis, by saving money over a time period, before reaching the time to make a "down payment" on a mortgage financed house purchase.

But under the conditions generally obtaining, for the US dollar and for the British pound, at the time period, say, of 1870 through 1910, there were modest interest rates available for savers (or savings account depositors of

whatever motivation) in Savings and Loan Associations or in other institutions offering comparable deposit accounts AND this in the context of the general absence of inflation (because of the dollar and the pound then both standing in a standardized fixed price relationship to the "troy ounce" of gold) .

But of course we can note that in those days, although depositors could earn a genuine increment of interest on their savings deposits there was generally no provision for an insurance coverage for the possibility, like recently with "Icesave", that the calculations of the institution might not be perfectly far-seeing. It was, perhaps, a time when one needed to know something, effectively, about both the moral character and the financial wisdom of one's banker.

It seems that there have been times, historically, when there would be "good bankers", like maybe a Rothschild, or a Morgan, or a Giannini, and recently or now, we seem, comparatively, to have been in the era of bank executives who win, as players, if their employer does not fail during their time as employees, and lose, as players, if the bank fails and is absorbed through something like the American FDIC, but then do not really LOSE BIG (with need to pay damages) by having simply the status of employees of a corporation. (In the USA

a bank that is not a corporation is very rare; an example of that is Brown Brothers Harriman and Company.)

Contracts and Justice

In Game Theory there is generally the concept of "pay-offs", if the game is not simply a game of win or lose (or win, lose, or draw). The game may be concerned with actions all to be taken like at the same time so that the utility measure for defining the payoffs could be taken to be any practical currency with good divisibility and measurability properties at the relevant instant of time.

But also there can be quite analogous game situations with the time for the game actions extending over, comparatively, a long period of time. In the USA there is frequently news about a basketball player (or another variety of professional athlete) who is signing on (typically assisted by an agent) to serve for a period of some years on the athletic team "owned" by some sports entrepreneur.

The interesting thing is that, as the time period for all the performances of the athletic services contract becomes more extended, the contract becomes more comparable to mortgage loan contracts in relation to how the quality of the currency unit of the terms of the contract will relate

to the demands expressed in the contract.

In the area of mortgages the phenomenon of the uncertainty about the amount of inflation to be expected has led to various adaptations, for example the frequent use of "ARM" mortgages where the interest rate collected varies with the current pattern of interest rates in some market.

So we can see that, for contracts relevant to the studies, in particular, of a school or department of "Business Administration", it is as if there is another player in the game of the contract signers and this player is the Sovereign who provides the medium of currency in terms of which the contract is to be expressed.

Well, my basic point is simply that as the currency of the Sovereign tends to have less stability and less reliability of its value than the circumstances affecting the formation of business-relevant contracts become quite perturbed.

It seems that inflation affecting currencies is GENERALLY or NORMALLY with some associated unpredictability, although it would be POSSIBLE, for example, for the Swedish krona to have a 1% "targeted" inflation rate in terms of comparison with the Swiss franc although this is NOT what we would rationally expect, because of various political and other considerations!

My recommendation to economists generally and to planners

who may influence the economic and business rules operating within or among states is to consider the value of economic and business conditions where it is possible to deal well with longer term contracts. Such contracts, for example, have notably been of use in the past with public works projects.

National Money and Provincial Money

If the money used in the central capital areas of a nation is also used in the provinces and if the provinces also have governments and local taxes then the quality of the money ordained by the Sovereign on the national level will affect the conditions for trade and investment, etc. in any province. For example we could think of the UK and of Scotland as the province. If, say, a Scot named Adam Smith has a temporary surplus of earned income over expenses then what can he do with this surplus that is both cautious and wise?

Mr. Smith must logically have some concern over the conjectural probabilities regarding the value of the currency he would use (which we can presume to have the same value per unit as that used in London).

In Switzerland the analogous provinces are the "cantons". And these cantons typically may have a cantonal bank which

is, in a sense, comparable to an office of a postal savings system. But each cantonal bank is under local control and administration.

A depositor in such a provincial bank MIGHT be able to save a little money with a modest level of efficiency, but ONLY if the characteristics of the money standard which is used to define his/her account are favorable.

Thus we can see how the cantons of Switzerland themselves, as economic entities, have an interest in the qualities of the exchange medium that is provided by the Sovereign (Confederation). And similarly in Edinburgh there is the possibility of locally founded concerns about the pound.

In relation to these considerations I suggest that, in general, if the money that must be used by a set of provinces of an aggregative state is of a comparatively higher level of quality than that this circumstance can favor decisions in the provinces in favor of more thrifty options or alternatives.

Contractual Reliability as a Pattern of Culture

There have often been attempts by various students of history or writers on Economics to link times and places of good economic progress to cultural circumstances that might be imagined to favor, somehow, the good fortune.

If this sort of thing were really well understood then it should be taught in schools of "Business Administration"! (I have the personal impression that such theories are NOT taught like that.)

We can see, however, that there is an option which can be taken or partially taken to improve the metrical reliability of contracts.

For example imagine two parties in Zimbabwe wishing to arrange for one of them to sell the rights to a patent to the other when the patent will be valid for 15 years into the future. On a cash basis the issue is simple, comparatively, and if it was that the Zimbabwe dollar was in use there then they could have used that for the cash transaction.

But the patent might be worth considerably more if the payment for it could be stretched out over the 15 years remaining of its validity. However, if a contract were to be written involving payment for the patent in installments

then the seller would logically wish to consider the prospects, over the period of 15 years into the future, of the value of the Zimbabwe dollar. But can this be scientifically or objectively calculated?

My point is simply that good reliability of the estimates of the future value of a currency, a "medium of exchange", is favorable for the formation of contracts of a business-related variety.

And the general pattern, within a State or a zone of legal customs and rules, becomes effectively a part of the business culture there and we can see that, other things being equal, a more favorable "business culture" should be expected, at least as long as we remain dependent on "private enterprise" and on entrepreneurs, if only on a partial scale, to enhance economic progress and the effective value of the products produced within the State or zone.

Investment Banking and the Quality of A Local Currency

It can be observed, for example, that the income acquired as wages through the labor of workers working, perhaps, in the "City of London", in the area of "investment banking" contributes a disproportionate part of the total income coming into

the UK as part of the "gross national product" of the UK. Some of these workers may be "quants" who are actually mathematicians working similarly to actuaries. Now the activities of all the banks and financial and related enterprises there in the City or in London naturally interact with the characteristics of the currency used. Of course the London office of J. P. Morgan Chase, for example, may do most of its transactions on other bases than in terms of pounds. But the comparative quality and stability of the pound will naturally affect the attitudes of all the participants in the financial businesses there.

We can observe also that the prominence, in areas of finance, of London, is not a recent development in time but that it goes back, in time, to when the Empire was still a successful and profitable enterprise and when the pound had become the Number One currency of the world (or at least the Number One currency for TRADING purposes in the later part of its good era).

Now at this time, in 2011, it seems to me that some other centers might desire to get into this sort of profitable employment of human labor. In particular the possibility of centers like Tokyo, Shanghai, Kuala Lumpur, Beirut, and Sao Paulo comes to mind.

And in each case the quality (in a sense like that of Gresham in Gresham's Law) of the locally employed currency will favor or disfavor the prospects for the growth of a local center for financial activities including "investment banking".