

Argentina and Paper Money

By Samuel L. Blumenfeld

What the people of Argentina are going through is possible in any country that uses paper “money” as the basis of its economic activity. Today’s paper money has no backing and therefore is only worth what the government or central bank says it is worth. We call that kind of paper money “Legal Tender.” In other words, the government invests its faith and credit in the value stated on the paper note. Money is supposed to be a medium of exchange and a storage of wealth and we accept paper money because the government backs its stated value. But such a system can only work if the people have trust and confidence in their government and their government behaves responsibly.

If we go back to the early days of economic activity, we find that barter was the earliest form of exchange. A person could exchange a cow for sausages. In other words, one gave value for value. The medium of exchange was awkward and cumbersome, and the two individuals involved had to make value judgments about what they were getting for their commodity.

But then it was found that gold would be accepted by many sellers in lieu of a perishable commodity as a medium of exchange, because of its scarcity and convenience. Gold also became an excellent storage for wealth. You could hold gold without its spoiling for as long as you wanted, and people would gladly exchange commodities for it.

But then, as civilization progressed, keeping gold became inconvenient. It could also be easily stolen. So people began putting their gold for safekeeping in banks, and the banks issued gold certificates or banknotes. The banknotes were worth their weight in gold. But then the banks used the gold deposits as security for high-interest loans, which they made by issuing banknotes. But when the loans were not repaid, and the owners of gold cashed in their banknotes, the bank became insolvent, and their notes were no longer honored.

This was the case in early America, where the Farmer’s Almanack up to 1863 actually listed “Worthless and Uncurrent Bank Notes in New England.” Thirteen banks in Boston alone were listed as having worthless bank notes.

None of today’s currencies have any backing at all except the faith and credit of the government behind it. In Argentina, the faith and credit of the government no longer exists. And so its citizens hold paper money that has already lost half its value by government devaluation. The Argentine peso cannot be said to be a storage of wealth. Only those individuals who were smart enough to buy gold or U.S. dollars will come out ahead of the game, because they didn’t trust their government to maintain the value of Argentine currency.

So what is money today? The money that becomes figures in a computer must still be earned the old fashioned way, by working for it, or earning it through prudent investment. That is, for most people. The expansion of government has made it possible to pay the needy in welfare checks and food stamps.

It is still possible to use gold as a storage of wealth. As long as paper money is susceptible to inflation, the dollar will continue to decrease in value. Thus, we have experienced exactly what the Argentines have experienced but over a much longer period of time.

Those people in Argentina who owned gold came out ahead of everyone else, because the price of gold is set on the world market in London, and it is now worth as much as holders of the Argentine peso have to pay for it. Also, those who owned valuable real estate did well.

Once you understand the vulnerabilities of paper money, you have to invest your money and store it in ways that will maintain and hopefully increase its value. Putting it in the bank at today's low interest will not increase its value. The stock market is still the best way to grow wealth. But you must buy stock in companies that you know will grow and prosper.

Real estate is one of the best ways to store wealth, particularly in areas of increasing value. It makes sense to take advantage of today's low mortgage rates to buy a house. Antiques and valuable works of art also make good investments.

As for gold, it is a commodity. Its price is subject to periodic fluctuations caused by political and economic crises. There is no way of knowing for sure what the price of gold will be tomorrow. In other words, those who bought gold when it was \$800 an ounce lost half its value as it declined to \$350. It all depends at what price you buy it and at what price you sell it. *One can also invest in gold stocks.*

In short, our greatest security is not in paper money but in the ability to create an income for ourselves. In order to do that we must be able to create and provide value for others. America is blessed with a huge number of individual entrepreneurs and inventors who keep making things better and better. The genius of capitalism is that it can take a cartoon character of a mouse and build it into a billion-dollar entertainment conglomerate. It can take a simple hamburger and turn it into a worldwide fast-food phenomenon. And it can take a simple carbonated drink and make it universally recognized as the symbol of a nation.

The Bible tells us that the love of money is the root of all evil. But money now is not a shiny pile of gold, but figures in a computer. Our goal should be to use the gifts God has given us to create value through our efforts, our intelligence, our genius. That is the only way to make our economic pursuits pleasing in ~~God's~~ eyes.

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So it is the behavior of government that determines the value of our currency. In the U.S. money is issued by the Federal Reserve Bank, a private institution that determines interest rates for the nation's banks. Gold is still a better storage of wealth than paper dollars, which are subject to inflation. Ancient Rome suffered from inflation when the emperor added other metals to the gold coins, thus decreasing the value of the coin. In America, where we used to have silver coins, we now have metallic coins that we use like paper money. You can buy a silver dollar from a coin dealer for much more than our present dollar.

As our modern capitalist economy grew, the need for investment cash grew with it. Thus, gold had become an impediment to economic development. By liberating paper from gold and calling it legal tender, man had invented the greatest fuel for economic development in history. But paper money, like nuclear power, has its risks and is totally dependent on responsible government for its value. Legal tender was invented to stimulate commercial enterprise. But politicians have used it to redistribute the wealth, throwing billions at such projects as the War on Poverty. And the only reason why the United States has not gone the way of Argentina is because we have a citizenry willing to pay the taxes to support such wasteful spending.

Wherever you have paper money without any gold or silver backing, you can get runaway inflation. Germany in the 1920s is an example of paper money becoming worthless overnight. In the United States we've had slow inflation that is almost unnoticeable. However, those of us old enough to remember when a hotdog cost 5 cents can see the effects of inflation in the same hotdog costing \$1.95 at the mall food court.

Of course, technological advance has cheapened lots of goods and services not because of any government monetary policy, but because technology has lowered the cost of production. For example, despite inflation, long distance calls today are much cheaper than they were in the 1930s. And the price of chickens, once considered a luxury, has significantly declined. Competition and technology account for this favorable development.

What keeps the American economy viable as opposed to Argentina is that in America we have a huge number of individual entrepreneurs and inventors who keep making things better and better. Unfortunately, nothing comes out of Argentina except beef and Tangos.