What Is Money?

By Samuel L. Blumenfeld

Money is an instrument of commerce, a measure of value, a means of exchange, and a storage for wealth. However, in Argentina not too long ago, that measure of value was abruptly changed by the government, which wiped out a considerable amount of wealth "strored" in that national currency, and raised the prices of everything. And so, money can be a treacherous thing.

It all depends on who or what is backing the money, for, as we all know, paper money has no instrinsic value. A thousand-dollar Confederate note has value only as antique paper, which some collectors want and are willing to pay for. The government that once backed that Confederate note no longer exists, and therefore its only value today is as an historical artifact.

Can what happened in Argentina happen in the United States? Not only can it happen, but it has already happened—in a much slower way. All you have to do is study the prices of commodities in the last century to know that a U.S. dollar bought much more fifty years ago than today. I collect old magazines, and the ads reveal much about the changing value of our money. For example, in 1901 you could get the finest suit or overcoat from Hart Schaffner & Marx for $45.00. The Waverly Electric Automobile cost $850. In 1917 you could get a Franklin Touring Car for $1,950. Its most expensive model was $3,100. In 1929, the most expensive Chrysler was priced at $1,595. Its cheapest model was $985.00.

The Depression was a period of deflation. Prices were low, but money and credit were difficult to come by. Today that comparable Chrysler would cost $45,000, but credit would be very easy to obtain. What accounts for this vast difference in the value of money? It has to do with the printing press. Paper money is created by simply printing it up. If too much is printed, you get inflation, that is, more money chasing fewer goods.

Have you ever noticed what happens when a department store has a huge sale? Here in Boston, the old Jordan Marsh used to have its annual warehouse sale. People would line up before dawn in order to be first to grab the item so many others wanted. You could buy the same item at your leisure and convenience at the usual price. But very low prices create great demand for fewer goods.

In the normal course of business, prices are set on the basis of what it costs to make the item, plus a margin of profit. No one would sell an item for exactly the same amount of money it cost to make it. There must be a profit in order to make all that effort in creating a product worth while. The profit is the reward for the effort.

That is why socialist criticism of profit is so ridiculous. Profit is what makes progress possible in a free society. Profit is how wealth is created. Without it you would have economic stagnation and subsistence living. Back in the days of the Communist USSR, the essentials were very cheap and very scarce. Thus, people stood in line for hours to buy a loaf of bread. That's what happens when the government runs the economy.

But, getting back to money, it is better understood if you know something about its evolution. Back in the earliest days of commerce, barter was the accepted method of exchange. If you owned a cow and wanted bricks, you would go to the producer of bricks and offer your cow in exchange. The brick maker had to have the means of using the cow before it died. Thus, such exchanges were cumbersome and limiting.

As commerce expanded, exchanges had to be made more convenient. So precious metals became the means of exchange. Gold, in particular, became the "money" of choice. It was easily portable, maintained its value, did not rot or spoil, and everybody wanted it. Thus gold coinage became the easiest way to handle this medium of exchange. As far as pricing was concerned, buyer and seller decided on the right amount of gold for the exchange. But the biggest problem with gold ~~is~~ that it could easily be stolen.
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Thus, the need for banks. They came into existence in order to make exchanges of commodities and gold more convenient. Merchants deposited their gold in the banks for safekeeping. They were given certificates or banknotes that could be converted into gold on demand. The banks acted as agents, or go-betweens, for buyer and seller. But instead of gold being shipped from one bank to another, buyer and seller did their business with the banknotes. Thus, accurate accounts had to be kept.

Eventually it became more convenient to exchange pieces of paper than the gold itself. The pieces of paper indicated who owed what to whom. But these pieces of paper had intrinsic value: the buyer's gold, which was stored in the bank. For handling all of these commercial transactions, the banks were paid fees.

The bankers then got the bright idea of making loans to merchants who needed "money" to carry out a transaction. And so they issued banknotes to the debtor. The merchant paid the bank back with interest. The bank's great concern was with defaulting loans, for the bank had borrowed the gold from its customer, and had to pay it back. And if it couldn't, the bank was in big trouble. And if it became insolvent, its 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. They were worthless because the bank no longer had the gold with which to redeem them.

Until we abandoned the gold standard, all bank notes were redeemable in the gold or silver on deposit. But today's government-issued money has nothing but the full faith and credit of the government behind it. It is called legal tender. By liberating paper from gold, man had invented the greatest fuel for economic development and expansion 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.

In Argentina, the full faith and credit of the government simply went down the drain. And so its paper money lost half its value overnight by government devaluation. Thus, the Argentine peso proved not to be a reliable storage of wealth.

And the same can be said for the American dollar which buys much less today than it did back in the 1930's, '40's, and 50's. Back in the 1930's when I was a child, I could buy a hotdog for five cents. Today, the same all-beef hotdog costs anywhere from $1.95 to $3.00. Of course, we all earn more money today for our labor, because even the cost of labor goes up with the cost of everything else.

The reason why the powers that be found it necessary to separate money from gold and silver, is because the metals placed a tremendous brake on the expansion of credit. Our present booming consumer economy, which is so dependent on easy consumer credit, is a direct result of that policy. The only way to satisfy the tremendous need for credit, was with paper money backed by the full faith and credit of the government. In other words, it is the taxpayer who backs our credit economy and its paper money.

Today, money consists mainly of figures in computers. Even in supermarkets, more and more customers are using plastic to make small purchases. Paper money, or legal tender, is not even being used. The credit card registers the amount owed the store, the data is then put into the account of the customer, who then receives his monthly statement with the transaction recorded. He then makes the necessary payment by check or computer and the bank changes the figures.

And because it is now so easy to acquire material possessions, we do not expect the things we buy to last very long. Technology keeps changing things. And so a ten-year-old TV set is thrown out. Garage sales have now become a seasonal tradition.

The convenience of plastic has expanded its use. To buy gas you insert a credit card in the pump, filler up, and get a receipt. Everyone now has a cell phone. Everyone has a computer and is now on the Internet. You can buy or sell just about anything to anyone anywhere in the world on Ebay.

Indeed, technology has cheapened lots of goods and services, despite inflation, and not because of any government monetary policy, but because technology has lowered the cost of production. For example, the cost of a long distance call today is much less than it was back in the 1930s. And the price of chickens, once considered a luxury, has significantly declined. Competition and technology account for this favorable trend. But what we gain in technology, the government takes away in higher taxes.