Part One

THE MONEY PROBLEM

Chapter 1

WHY WORRY ABOUT MONEY AND GOLD?

Everything that King Midas touched turned to gold, until ultimately he was a very poor man, because he had no useful possessions at all. The moral of this story is that money isn't everything in life. Indeed, money and gold bring wealth and power only in terms of what one can buy with them.

On the other hand, history tells us that money can be crucially important. Revolutions have seldom been caused by an excess of purchasing power, but men have frequently been stirred to violence when they are hungry and factories stand idle simply because no one seems to have enough money to buy what they are able to produce. Poverty in the midst of potential plenty always appears shocking and senseless.

These contrasts are the essence of the subject matter with which this book is concerned. Put in its simplest terms, we want to be sure that we have enough money around so that we can buy everything that has been produced, but never so much that we try to buy more than has been produced. The problem that will concern us most is the difficulty of keeping the number of dollars spent in line with the quantity of goods produced.

Despite the problems money causes, mankind invented it and sticks to it because it relieves us of the almost insurmountable difficulties of doing business through barter. For this reason, even the most primitive societies have tended to use some form of money, whether it be feathers or wampum or giant stones buried under the sea. As societies become more complex and people more specialized in the tasks they perform, money is even more necessary to enable one man to exchange his production for another's.

With the growing complexities of the marketplace and of the methods of production, we find that the character of money changes. It becomes more and more abstract, until it reaches the highly sophisticated form of our own money, which consists primarily of numbers on the ledgers of the banks that maintain our checking accounts. Although we still use some currency (worth, in reality, no more than the paper it is printed on) and some coins, most of the money we spend moves from buyer to seller through the writing of checks that order the banks to debit one account on their books and to credit another. Thus, most of our money has no real value and no tangible existence: we can't see it or feel it or smell it. This is one of the reasons why its quantity is so difficult to regulate.

Nevertheless, while we shall be most concerned with this abstract money that exists only on bank ledgers, we shall also see that gold continues to play a crucial role in our financial affairs. Sophisticated as we may be, our links to gold persist. Gold has shown amazing vitality through the ages as the paramount symbol of money and wealth. The Midas legend teaches us that gold may be nothing more than a useless (if beautiful) metal, but it has surely been the cause of an extraordinary amount of rapaciousness, plunder, and adventure in the history of man.

Why gold is "good as gold" is an intriguing question. Freud suggested that our fascination with gold is related to the erotic fantasies and interests of early childhood. Perhaps its very purity inspires men to violence. Anyone who has ever seen a pile of gold bricks or gold coins will always remember the sense of awe it inspires. In any case, its prosaic physical characteristics—high density and such strong resistance to oxygen that it never tarnishes—have increased its usefulness as money.

Whatever the reasons, men will go to great lengths to find gold and dig it up. After visiting the Klondike and the Yukon, Will Rogers commented: "There is a lot of difference between pioneering for gold and pioneering for spinach." Although North American gold mines are still producing, most of the free world's gold comes from South Africa, where the white man owns and profits from the gold but leaves to the black the business of digging it out of the dusty hell two miles below the surface of the earth.

Yet, with all the digging and prospecting and plunder, men have managed to scrape together a surprisingly small amount of this precious stuff. The entire accumulation of monetary gold over the centuries has brought the world's gold hoard today to just about 40,000 tons; American industry pours 40,000 tons of steel in less than one *hour*!

While nature essentially controls the quantity of gold in existence, it is men who assign it values in terms of dollars and pounds and rubles; it is also men who decide how much money a given amount of gold may "back." When we look at the alternations between inflation and deflation in our history, men seem to have done a poor job of regulating the supply of money.

We find repeated cases in which people seemed to have so little money that they were unable, or certainly reluctant, to buy everything that could be produced. As a result, prices fell, profits vanished, production shrank, and unemployment spread. Only when all prices and all wages had been pushed down so low that the formerly inadequate supply of money seemed sufficient to buy up all the goods and services offered for sale at bargain levels did the wheels finally begin to turn again and men go back to work.

We can also find frequent examples of the opposite situation—the inflationary spiral in which the quantity of money outruns the supply of goods. When people want to buy more than has been produced, prices rise. Then some people lose out through being outbid in the marketplace. Those who suffer most are usually the ones who least deserve to be the losers—the frugal, the conservative, the prudent, together with the poor and unorganized who are unable to battle for the higher incomes they need to stay even with the rising prices.

Thus, regulation of the supply of money is not just a matter that concerns financiers and bankers: it is intimately involved with our prosperity and with our social tranquillity. With all its technicalities, this is a subject with the broadest political and economic implications.

Our analysis of it now begins with the very crux of the process—the links that exist between the quantity of money and the levels of business activity and prices.