Credit and State Theories of Money: The Contributions of A. Mitchell Innes, Ed. L. Randall Wray. Cheltenham, UK and Northampton MA, USA: Edward Elgar Publishing Limited, 2004. 271 pp

The sub-title to this book is particularly important, since the book's main purpose is to provide a show-case for the two articles by Mitchell Innes, from the Banking Law Journal in 1913-1914, on the evolution and nature of money. These articles are extraordinary, because in them Innes attacks the Metallist/Mengerian theories head-on, just when the Gold Standard was riding high. It has been much easier to do so subsequently, after the adoption of fiat money has made the Chartalist/Credit role of money so much more obvious.

Mitchell Innes, an Englishman, joined the British Diplomatic Service, and was working in Washington, D.C., as a Councillor, when he wrote these articles, (hence their appearance in an US Journal). It is doubtful whether diplomacy was his forte. He was brilliant, original, assertive, given to exaggeration, widely read, rebellious, no team-player, self-confident, contemptuous of authority. He went on to link his early work on the social foundations of money, where one strand was the use of money as a compensation to the victim by wrong-doers, to a subsequent slashing attack on modern penal systems.

The West, he wrote, had substituted, in place of recompense to the victim, a system of forcing criminals to pay their duty to the State.

Mitchell Innes used his wide knowledge of history to demonstrate that creditor/debtor relationships had long pre-dated the development of coinage, and had given birth both to money, as a unit of account, accounting and (probably) writing, as a way of keeping score. Money preceded and facilitated free markets, not vice versa. Moreover, even when coinage was developed, it was almost always less than full-bodied, often mere tokens.

Considerable advances have since been made in our knowledge and understanding of economic relationships in earlier millennia, and two of the supporting Chapters, by Henry on `The Case of Egypt' and by Hudson on `The Archaeology of Money', are excellent in this vein. I particularly liked the idea that money was brought into being by growing specialisation, notably that between professionals, especially engineers (controlling water flow in Egypt, bridge building in Rome), and ordinary farmers. The professionals had, (and have), a monopoly of specialist knowledge, and used this to metamorphose into religious and dominating castes, who used their positions to exact taxation from the general public.

I remain somewhat more confused about mediaeval monetary history. Innes claims that the embodiment of

precious metals in the coinage of the times was of secondary importance, so the attempt by sovereigns to raise funds by debasement was the "unfounded accusation of historians," p. 23. While Ingham goes along with that initially, p. 177, in his Chapter on `The Emergence of Capitalist Credit Money', he subsequently (partly) recants by referring to the `Great Debasement' of Henry VIII of England, p. 205. [Ingham's Chapter also largely reproduces the best parts of his subsequent 2004 book on <u>The Nature of Money</u>, those covering the evolution of money and banking in the UK between 1600 and 1800]. Instead, Innes emphasizes the `crying down' of the nominal value of outstanding coins, which actually raises the ratio of bullion value to nominal value. We seem to have two diametrically opposite theories here.

Whichever is correct, it will not alter my prevailing judgment that the Chartalist/credit approach is historically valid, whilst the Metallist/Mengerian/Mainstream view of money arising as a means of reducing transaction costs is nothing but a pure myth, a fable. That said, the heterodox Chartalists (like me) do not help their cause by overstatement. Innes implies that <u>all</u> credit is money; `Money, then, is credit and nothing but credit', p. 42; `Credit and credit alone is money', p. 76; though, on one occasion, p. 52, he qualified this by the adjective `good credit'.

Instead, as Ingham and Wray note, <u>not</u> all credit is money, and a study of the criteria necessary to make bilaterial credits transferable to third parties, and usable by them in settling their own debts is crucial. It is here, with the developing hierarchy of credit relationships, that the credit and State (Chartalist) theories of money merge, (not fully appreciated by Innes).

Next, in an otherwise excellent Conclusion, Wray goes too far when he states that "the state can choose anything it likes to function as the `money thing'", p. 243. Assume that the State chooses something that anyone can reproduce, supply or counterfeit very easily, say earth-worms or dead flies. Then the supply of money would shoot up, hyperinflation would ensue, and the monetary system would become useless. Many of the early monetary units, e.g. tally sticks, coins purposefully broken in two parts, clay tablets within casings, had no intrinsic value, but their credit/debt value could be uniquely confirmed. One of the problems of electronic money is the perceived danger of hacking and fraud. I have always contended that the margin between the intrinsic (bullion) worth of coinage and its nominal value will be a function of the power of the State authority.

As a generality, and as evidenced by this book, Chartalists fail to pay sufficient attention to the need to control the supply of money; Innes gets very close to the `real bills' fallacy. Thus he writes, p. 48, "Once insure that banking shall be carried on by honest people under a proper understanding of the principles of credit and debt, and the note issue may be left to take care of itself." Again Innes is so keen to disassociate inflation from fluctuations in the availability of precious metals that he regards supply shocks to output, e.g. wars and plagues, as the main cause of inflation in the Middle Ages.

So I regard much Chartalist/Credit theorising as unsound on the importance of controlling the supply of money, so as to maintain price stability. That said, they <u>have</u> made a proper study of history and institutions, which most professional economists nowadays have not, and they are, I believe, correct in their interpretation of the early evolution and essential nature of money.

Does that matter? It can do. Both Ingham and I have attributed part of the incorrect analysis of European Monetary Union, and the current problems of relating (federal) monetary policies to (national) fiscal policies, to bad monetary theory. Perhaps just as important, it is symptomatic of a general approach that

tries to turn economic analysis into an `arithmetic problem', (see Wray, p. 233), dropping successively social relations, economic history and the politics of erstwhile `political economy' from the pure, mathematical but often jejune, core of economic analysis. We need to turn back that tide, and this book helps to do so.

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