MONEY, DEBT AND ECONOMIC ACTIVITY

by

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PREFACE

EVENTS SINCE 1914 have been fascinating (if also disconcerting) for students of money. We have witnessed astronomical inflations, and the world's longest and deepest depression. Money the world over has been virtually divorced from gold. Interest rates have ceased to play their age-old part in the market system. The established uniformities of "velocity of circulation" have broken down. Experiences of World War II have upset our traditional skepticism of price control; experiences since then have reminded us of the inadequacy of our forecasting methods.

The subject of "money and banking," with so much new experience to interpret, tends to lose coherence. Only a few years ago, money was the prize course in many economics departments—the surest to command spontaneous interest among students, and the one in which the teacher had the strongest sense of showing how useful economics could be. Today, the subject of money looks much more drab. Courses in the "fiscal policy" aspects of public finance, in business cycles, in international trade, and in "pure theory" now eclipse courses in money. They are so stimulating largely because so much of their subject matter has been appropriated from "money and banking" courses.

This incorporation of monetary topics is a sound development in the teaching of these other subjects. But it is not a reason for letting money and banking become merely a collection of loosely related fragments that other courses have not yet taken over. On the contrary, the course in money can best interpret the record and show how to fit the different parts of economics together. Ideally, we might rely for "synthesis" of the student's thought primarily on an advanced course in economic theory, stressing dynamic aspects. But in the present unsatisfactory state of dynamic theory, money is overwhelmingly the best focus for much of what the economist has to present.

Such novelty as I can fairly claim for this book lies in its stress on cross-connections—both between topics within the field of money, and between money and other fields. I should hesitate to claim novelty for the substance of the argument at any point (unless perhaps for the treatment of uncertainty in Part II). The pattern of cross-connections, too, will strike many students of money as familiar: it is along the lines of contemporary economics —one of those things that are "found and not made." The contribution I hope I have made is one of bringing useful ideas out from between the lines of the literature.

This is an institutionalist book. It starts out from institutions: accounting practices, debt, the banking structure. The key theoretical concept of "liquidity" is shown as something that grows out of these institutions. The importance of facts is stressed throughout. I have tried to convey a sense of the evolution of economic institutions—avoiding the pitfall of letting notions of evolution suppress the question *what* it is that changes. "Noneconomic" influences on prices and "noneconomic" restrictions on policy are frankly recognized. Above all, the book is institutionalist in its concern for getting an economics which can guide public policy.

At the same time, this is a theoretical book. Its core is in the theoretical chapters (Chapters VII and VIII) dealing with the payments approach and cash-balances approach. In Part I, the theory is largely between the lines, and not at a very high level of abstraction; but Part I is designed, nevertheless, to serve as introduction to the more explicitly theoretical material which follows. In the "applied economics" of Parts III, IV, and V, theoretical argument is used freely. In short, I operate on the principle that institutional and theoretical analysis are "completing" rather than "competing" goods.

In laying out the book, I have not intentionally passed over any monetary topic (however elementary) as something the reader was already supposed to know. On the other hand, I have not avoided any topic which I myself could handle, for fear of its being too difficult for students. It seems to me that practically everything about money is comprehensible to an intelligent reader who is willing to give the subject sustained attention and to face the fact that the views he may have picked up casually in high school or by listening to the radio may have to be screened and straightened out with an eye to possible bias. I have not tried to hide the existence of loose ends in monetary analysis. But I am confident that enough of the structure I present will withstand criticism to keep the reader from being left helpless in the face of the policy problems of our times.

To keep the book down to convenient size, I have been forced to drop some of the traditional "money and banking" material. I do not regard this necessity as a misfortune. Every subject must, sooner or later, pass through a phase of dropping excess baggage; such a phase is due in money and banking. But a check of the index and table of contents will show that I have found space for most of the traditional topics which are relevant to present-day policy problems. What is omitted is chiefly (1) detail on bimetallism and on banking history, and (2) detail on bank operations, legal instruments, functions of particular bank officers, and so forth. The first group of topics has lost current relevance. The second group is current enough, but its value is chiefly for students who need to know what it feels like to work in a bank because they aim to get banking jobs. Even this restricted group of students, in my opinion, can better spare this material than the materials it would displace. Such details can readily be learned on the job; the broader economics of money cannot.

This book is neither Keynesian, anti-Keynesian, nor on the fence. On the other hand, it is definitely not *pre*-Keynesian. It seems to me that the time has come to take Keynes matter-of-factly as one of the important sources of contemporary ideas. It would be absurd today to be for or against John Stuart Mill; and it is not the economics of Karl Marx that constrains people still to be for or against him. Why be for or against John Maynard Keynes? If we try to reject Keynes's ideas *in toto,* our thinking is impoverished, for he was the most fertile monetary thinker of the interwar years. If we feel obliged to follow a Keynesian "line," we are forced both to reject too much of the old economics and to block off too many promising new lines of inquiry.

The most direct intellectual influence on this book is probably that of J. R. Hicks. His "Suggestion for Simplifying the Theory of Money" (in *Economica,* February, 1935) gave direction to my monetary thinking. In particular, his proposal to develop the core of monetary theory out of banking theory, "regarding every individual in the community as being, on a small scale, a bank," is the clue from which I worked out the pattern of Parts I and II in this book. But my treatment of uncertainty diverges rather sharply from that of Dr. Hicks. This is the point at which, it seems to me, the literature is weakest—"classical" literature, Keynesian literature, and literature of compromise alike. Corrections for uncertainty factors lead to a convergence of the different points of view. It is my hope that in Part II I have brought this convergence to a stage where we can use both Keynesian and "classical" reasoning on our key problems, and not have to forget about one before we start using the other.

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Besides the obligations which the footnotes will make clear, I should record the influence of Professor Lloyd W. Mints and the late Professor Henry C. Simons, of the University of Chicago. At several crucial points (particularly Chapter X), I have been strongly influenced by Dr. Gardiner C. Means. Discussions with businessmen and economists during my two years with the Committee for Economic Development are reflected at many points; the estimates of cash stocks in the Appendix were also worked out during this period, and the chartbook material (particularly in Part III) developed out of wall charts designed for CED discussions. My colleague, Professor James W. Angell, was so friendly as to criticize early drafts of Parts II and IV, to their very great benefit. Professor Arthur D. Gayer, Professor G. L. Bach, and Mr. Charles Hoffman worked through the whole manuscript, catching up errors of substance, presentation, and arrangement. Miss Lillian Margot, of Prentice-Hall, contributed many shrewd insights in the editing process. I am indebted to Miss Joan Gordon for clearing up the illegible spots in my home-made typescript, and preventing it from disappearing in a quagmire of work papers.

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