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Book Review: *Money: The Unauthorized Biography*

By George Selgin

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The aftermath of the worst financial crisis since the Great Depression is an apt occasion for taking a fresh look at money, that most basic of all financial instruments, atop which all the rest teeter.

As his subtitle suggests, Felix Martin has attempted a warts-and-all unmasking, to which he brings formidable credentials—a doctorate in economics from Oxford, two stints at the World Bank, and his current position as macro-economist for the London-based investment manager, Thames River Capital. The author is further aided by his felicitous prose and eye for money's naughtier antics.

He's not short of tales to tell: about money's little prank of masquerading as stone wheels in the western Pacific, its domestication by Greek kings, its kidnapping by crafty private bankers, and finally, its post-2001 binge. But in his eagerness to reveal truths to which others have been blind, Martin ends up exposing not so much money's mysteries as his own incomprehension of its real nature. According to a reviewer in the Guardian, this book will leave readers both "surprisingly entertained" and "better informed." Entertained but misinformed is more like it.

The author first leads readers astray by assuming that money has always consisted of an elaborate system of IOUs rather than of physical stuff. But while simple societies may have tracked and settled debts in many different ways, among non-intimates, monetary IOUs have themselves always been promises to pay some particular stuff, whether tobacco, sea shells, metal discs, or engraved paper.

The distinction between monetary promises and the stuff promised is, admittedly, often unclear, as it was when Britain's pound sterling ceased to refer to any actual coin, and when modern central banks turned their paper promises to pay gold into what one former New York Fed vice president dubbed “IOU nothings.”

But the fact that a Federal Reserve note is no longer a promise to pay anything else doesn’t make the note an “arbitrary increment on an abstract value scale.” Sometimes a note is just a note, and high-toned talk about universally applicable value confuses the real nature of exchange of goods for money. When a luncheonette sells me a ham on rye for $4.99, that doesn’t mean the sandwich has a value of $4.99, universally or otherwise. It just means that to the luncheonette the sandwich is worth less than $4.99, and to me, more.

The author’s knowledge of what economists have had to say about money is more inadequate still. With the phrase “Adam Smith and his school,” he lumps together every thinker from John Locke and Bernard Mandeville to Friedrich Hayek, throwing in some later mathematical economists for good measure. He then attributes to this homogenized mass “a vision of society in which economic value had become the measure of all things,” together with a blindness to the “debt and financial instability” to which this crass vision leads.

If Martin’s knowledge of intellectual history is less than solid, his choice of economic good guys is downright scary. He has soft spots for the ancient Spartans, whom he says wisely chose to dispense with money and all of the “impersonal and inhumane relations its use entailed,” and for Russian revolutionary Vladimir Lenin and his crew, who tried to do the same.

Another of Martin’s heroes is Scottish economist John Law, whose monetary “system,” implemented in France in 1720, was, according to Martin, “ingenious, innovative, and centuries ahead of its time.” Nearly three centuries later, one is tempted to add: Law’s system collapsed, catastrophically, in 1721.

Martin’s jaundiced view of money leads, naturally enough, to his proposal for reform. Stopping shy of suggesting another stab at Sparta’s convivial solution, he instead endorses the old-hat idea of making commercial banks hold cash reserves equal to their readily transferable liabilities. To be free of the bath water of financial crises, we must, in other words, throw out the baby of old-fashioned banking.

A glance beyond the limited experience of a few countries ought to be enough to make anyone think twice about such a Draconian remedy. Canada, for instance, suffered neither bank failures nor bank bailouts during the recent crisis; indeed it has had an almost uninterrupted record of financial stability since the mid-19th century. Scotland long boasted a similar record, with no central bank to look to for bailouts and very little bank regulation of any kind, until English currency laws were thoughtlessly imposed upon it in 1845.

It happens that Adam Smith supplied an eloquent account of the workings and advantages of Scotland’s once-brilliant fractional-reserve banking system, as he witnessed it in its formative years. That story can be found in book two, chapter two of The Wealth of Nations, but so far as Martin is concerned, Smith’s account, along with many other valid economic insights about money, might as well be among its best-kept secrets.

George Selgin is director of the Cato Institute's Center for Monetary and Financial Alternatives.