Money and Currency

Author(s): JOSEPH A. SCHUMPETER

Source: *Social Research*, FALL 1991, Vol. 58, No. 3 (FALL 1991), pp. 499-543

Published by: The Johns Hopkins University Press

Stable URL: https://www.jstor.org/stable/40970658

Money and Currency*

BY JOSEPH A. SCHUMPETER

Introduction by Richard Swedberg

AFTER SCHUMPETER'S DEATH in 1950, a huge manuscript on the theory of money was found among his belongings.[1] It was soon identified by Schumpeter's wife, Elizabeth Boody Schumpeter, as a book originally entitled *Geld und Währung (Money and Currency)* which Schumpeter had been working on in the early 1930s while he was still teaching in Bonn. This issue of *Social Research* contains the first two chapters of this manuscript, as translated by the late Arthur W. Marget. The main reason for publishing these chapters is that they contain some very interesting ideas about the social nature of money and how economic theory is not sufficient, in and of itself, to account for all the relevant aspects of money.

Schumpeter's main purpose in writing *Money and Currency* was to develop a new theory of money, as he had created a novel theory of economic change in *The Theory of Economic Development* (1911). Schumpeter, however, was never able to complete the manuscript to his satisfaction, and he therefore did not want to publish it. In 1970, when a German edition appeared, it passed nearly unnoticed. It was commented upon only by a small number of economists, and in their opinion Schumpeter's monetary theory from the 1930s had little, if anything, to add to the economics literature. Practically no attention was paid to the first two chapters with their argument that money is part of "the total social process"; that money plays an extremely interesting *political* role in society; and that economic theory always must be complemented by economic sociology, economic history, and statistics. One of the purposes of publishing these two chapters today is to draw attention to exactly these aspects of Schumpeter's thought.[2]

[1] I am grateful to Professors James S. Earley and Michael Reclam, who helped me to locate the translated chapters of *Money and Currency*.

[2] Schumpeter's attempt to create a theory of money is primarily to be found in "Das Sozialprodukt und die Rechenpfennige" (1917; tr. 1956 by Arthur W. Marget); *The Theory of Economic Development* (1st ed., 1911; 2nd ed., 1926; tr. 1934); and *Business Cycles* (1939). A short time before his death, Schumpeter wrote to a colleague, who had

It is not exactly clear when Schumpeter decided to write a book on the theory of money. In all likelihood he made the decision in the mid-1920s, just after having been appointed professor of public finance at the University of Bonn.[3] The book was to be part of a series called *Enzyklopädie der Rechts- und Staatswissenschaft*, which was edited by Schumpeter's friend and colleague in Bonn, Arthur Spiethoff. It is clear that Schumpeter had very high hopes for his book on money, which represented the first major project in economic theory he had undertaken after his unhappy forays into politics and business during 1919–24.[4] And at the beginning everything went well for him in Bonn: he was enjoying being back in academia and his first chapters of the money book breathe confidence and joy.[5] In 1926, however, disaster struck: within a few months, Schumpeter's mother, wife, and newborn son died.[6] Schumpeter was devastated, and to temper his sorrow he tried to retreat into work. But this did not work—the trauma had made him lose the ease with which he used to write and concentrate. For hours Schumpeter would now sit with an empty paper in front of him,

expressed a desire to write about his monetary theory: "I have never treated the problems of money per se: my views of money have been presented only incidentally in works of mine primarily devoted to other topics" (Schumpeter to René Roux, Nov. 8, 1949, Harvard University Archives; this letter, as other letters in this brief article, are quoted by permission of the Harvard University Archives). For the secondary literature on Schumpeter's theory of money, see first of all Arthur W. Marget, *The Theory of Prices: A Re-Examination of the Central Problems of Monetary Theory*, 2 vols. (New York: Prentice-Hall, 1938–42); Michael Reclam, "J. A. Schumpeter's 'Credit' Theory of Money," unpublished Ph.D. dissertation, University of California at Riverside, 1984; and Bärbel Naderer, *Die Entwicklung der Geldtheorie Joseph A. Schumpeters* (Berlin: Duncker & Humblot, 1990). For further information, see the literature cited in Massimo M. Augello, *Joseph A. Schumpeter: A Reference Guide* (Berlin: Springer-Verlag, 1990), pp. 69–78.

[3] In 1925, according to Bernd Kulla, "Spiethoff, Schumpeter und *Das Wesen des Geldes*," *Kyklos* 42 (1989): 432; and in 1926–27, according to Robert Loring Allen, *Opening Doors: The Life and Work of Joseph A. Schumpeter* (New Brunswick: Transaction Publishers, 1991), 1:263.

[4] Schumpeter had worked as an academic in 1909–19. During 1919 he was finance minister for seven months, after which he went into business. See, e.g., Richard Swedberg, *Schumpeter: A Biography* (Princeton: Princeton University Press, 1991), chs. 3 and 4.

[5] This is confirmed by the state that the first few chapters of the original manuscript are in. While the later chapters have enormous amounts of additions appended to them, this is not the case with chapters 1 and 2.

[6] The wife referred to in this sentence was Schumpeter's second wife, Annie Reisinger. In 1937 Schumpeter remarried Elizabeth Boody Firuski.

unable to write.[7] During the next few years Schumpeter's peace of mind was also disturbed by the fact that he had to write and lecture for money in order to pay back the huge debt that he had incurred during his years as a businessman. Still, by the end of the 1920s Schumpeter had succeeded in producing a full manuscript on the theory of money. Spiethoff, who got to see the manuscript, was pleased and thought that the book could be published fairly soon.

But all was not as it should be with the book, and Schumpeter was very unhappy about it. In 1929–30 he made an enormous effort to revise the whole manuscript but failed. In September 1929 he wrote to Spiethoff, "I have made a desperate attempt to finish my book on money . . . but only to fall back into a state of exhaustion."[8] And in April 1930: "I work as crazy every day on my money book. . . ."[9] In 1930 something also happened that made things even worse: Keynes published his important *A Treatise on Money*. Various versions exist of Schumpeter's reaction to Keynes's work. According to a student, Schumpeter tore up his manuscript; while according to a colleague, he burned it. Neither is true, since the manuscript from 1930 was later found among Schumpeter's belongings. Still, it is clear that he now felt that he had to recast his own monetary theory in a radical manner. Wolfgang Stolper was later to note, "I recall in discussions with him after Keynes' Treatise on Money came out that Schumpeter complained that the treatise had made his manuscript completely out of date and that he had to rewrite it from scratch."[10]

And Schumpeter did try to rewrite his manuscript "from scratch" during the next few years. Even after he decided to move to Harvard in 1932, he worked very hard on the money book. But he was not successful, and in March 1933 he wrote to his friend Gottfried Haberler that "the depression exhaling from this manuscript has nearly spoiled my first year at Harvard."[11] Exactly when Schumpeter made the decision to stop working on the money book and instead concentrate on his next huge work, *Business Cycles*, we do not know. The last time that Schumpeter sounds affirmative about finishing the whole book is mid-1933.[12] As late as 1935, however, the book was still advertised in Germany as "forthcoming."

[7] Allen, *Opening Doors*, 1:263.
[8] Schumpeter to Spiethoff, Sept. 19, 1929, as cited in Kulla, "Spiethoff," p. 433.
[9] Schumpeter to Spiethoff, Apr. 2, 1930, as cited in Kulla, "Spiethoff," p. 433.
[10] Wolfgang Stolper to Imrie de Vegh, Jan. 4, 1955 (Harvard University Archives).
[11] Schumpeter to Gottfried Haberler, Mar. 20, 1933 (Harvard University Archives).
[12] Kulla, "Spiethoff," p. 434.

On and off for the rest of his life Schumpeter contemplated writing a book on money, and he often referred to his soon-to-be-published book on this topic. In 1946 he even signed a contract to produce a book entitled *Money* (as well as one entitled *Banking*) for the Harvard Economic Handbooks Series, edited by Seymour Edwin Harris.[13] Elizabeth Boody Schumpeter also tells us that during the late 1940s Schumpeter retrieved his 1930 manuscript from "the brown trunk, in which it was kept" in order to work on it.[14] And two months before his death, Schumpeter wrote to a friend that "within a year or two I hope to write a book on money. . . ."[15]

But the money book was never written, and after Schumpeter's death all that could be found was an enormously unwieldy manuscript with masses of appended material, often in Schumpeter's hard-to-decipher shorthand. Schumpeter's wife, who devoted several years to the task of arranging Schumpeter's papers, decided to try to have the money book put in order and translated into English. The person she chose for this task was Arthur W. Marget, a friend and colleague of Schumpeter's who had been at the economics department at Harvard in 1932–37 and who was very interested in Schumpeter's theory of money.[16] Some time after Schumpeter's death, Elizabeth wrote to a friend, "I have been very fortunate in solving one of my translations problems. Arthur Marget, who spent two weeks with me recently in Taconic [where the Schumpeters had a house], has taken away the manuscript of the unpublished book on money. He will have it typed and will then translate it. . . . For Marget it will be a labor of love, and I am sure that he will do it with great care."[17]

The same year Schumpeter died, Marget was appointed to an important position at the Federal Reserve in Washington, and this left him with little time to work on Schumpeter's manuscript. Still, during the next few years he succeeded in having a typed copy made of the manuscript as well as translating the first three chapters. But this is as far as he got, and by 1954 Marget realized that he would

[13] See Herold B. Hicks to Schumpeter, Feb. 6, 1946; and Schumpeter to José Verarga, Mar. 21, 1946 (both letters in the Harvard University Archives).

[14] Joseph A. Schumpeter, *History of Economic Analysis* (London: Allen & Unwin, 1954), p. 1194.

[15] Schumpeter to René Roux, Nov. 8, 1949 (Harvard University Archives).

[16] Marget was an expert in monetary theory, and his *Theory of Prices* (1938–42) contains many references to Schumpeter's work on money.

[17] Elizabeth Boody Schumpeter to Hans Staehle, August 3, 1950 (Harvard University Archives).

never be able to finish the task. He wrote in the fall of 1954 to one of the trustees of the Schumpeter estate that "I had hoped that I would find the time not only to go through the manuscript carefully, but actually to undertake a translation of it. . . . But, unhappily, it has turned out to be simply impossible for me to go further with it. I did have a German type-script made . . . and I managed to start the translation. It is quite clear now, however, that I shall not be able to take it up again."[18] The decision was now made by the trustees to entrust Wolfgang Stolper, an economist who had been Schumpeter's student in Bonn as well as at Harvard, with the task of turning the manuscript into a book and having it translated. Stolper, however, never completed the task—he could not penetrate Schumpeter's notes in shorthand and he always felt a certain resistance to the idea of publishing a work that Schumpeter had expressly refused to make public before it had been improved. "Somehow I feel it is not quite fair to publish a manuscript which Schumpeter did not wish to have published during his lifetime."[19] After a few years Stolper gave up and returned the manuscript to the Harvard Archives. An offer in 1958 by Erica Gerschenkron (the wife of Alexander Gerschenkron) to translate the book was turned down by the trustees—rather unwisely, one feels.

At this point it looked as if Schumpeter's manuscript from 1930 would never be published. In 1970, however, a German edition suddenly appeared. As it turned out, Marget had given the economist Fritz Karl Mann a copy of the typed version in the 1950s; and it was this version that was now published, under the title *Das Wesen des Geldes*.[20] And today, another twenty years down the road, the first two chapters of *Money and Currency* can finally be published—thanks to Marget's having translated them and to the generous editorial policy of *Social Research*.

[18] Arthur W. Marget to Lucy Talcott, Aug. 30, 1954 (Harvard University Archives).

[19] Wolfgang Stolper to Imrie de Vegh, Apr. 4, 1955 (Harvard University Archives).

[20] Mann chose to name the manuscript after the title of the key chapter in Schumpeter's manuscript. It should also be noted that there exists quite a bit more manuscript pages (not to speak of appended suggestions for changes) at the Harvard University Archives than what Mann published. See especially HUG(FP) 4.77, boxes 9–10.

Chapter 1: Introduction

§ 1. *Currency policy* means more than formulating, influencing,[1] or regulating a special branch of market technique. The interest—often passionate, always great—which is aroused by the practical questions of money and the value of money is, indeed, to be explained only by two facts: that in a people's monetary system is reflected everything that this people wills, does, suffers, *is*; and that, at the same time, a people's monetary system exerts a significant influence on its economic life and its fate generally.

The condition of a people's monetary system is a symptom of all its conditions. That the currency must, in principle, be affected (even though the effect may not be equally visible in every case) by a deficit in the state budget; by the nature and spirit of financial policy, even without a deficit; by every measure of trade or business policy which furthers or restricts economic activity—indeed, by *every* measure of economic and social policy; and, finally, by upswing or decline in economic life: this we recognize immediately, whatever the difficulties of correct diagnosis of a concrete situation; and we recognize it already at the threshold of our discussion.

But it follows from this that the state of the currency must also reflect all the elements (and the whole social and political development) which explain these deficits, this financial, economic, and social policy, this upswing and decline: such as victory and defeat in war, preparation for war, revolutions, successes and failures in foreign policy, domestic political groupings, the strength or weakness of governments. This is all the more true because all these things, in the *historical* course of events, will not necessarily have their first effects on

[1] In this connection, it is the *fact* of influencing and not the *intent* to influence that is decisive. A prince who debased the coinage did not necessarily intend to change the value of money. A profligate parliament usually does not consider at all the effect of its actions on the currency. But both carry on currency policy in the sense of the definition implied above. Cf. § 3.

currency policy only after they will have led to corresponding actions or to changes in the economic process. On the contrary, they can also have direct effects: as, for example, whenever a general loss of confidence changes people's attitude toward money before anything has happened to affect the rate of interest or foreign exchange rates directly. Thus *every* kind of policy can become currency policy, *every* kind of event can become an event of currency policy. And it follows, finally, that the ultimate data of this social and political development are also the most profound determinants of currency policy and monetary history: the geographic and political situation of a people; the objective and subjective possibilities of its economy; its social structure and political organization; its attitude toward economic matters and toward the future; its morals and energy—everything that is covered by the expressions "national spirit" and "national character." Nothing tells so clearly what stuff a people is made of as what it does in the field of currency policy.

To be sure, this side of the matter can also be overstressed, to the disadvantage of both practice and analysis. An understanding of these far-reaching relationships is in itself not sufficient to comprehend the nature of monetary developments and the effects which they exercise in their turn. Anyone, for example, who explains an inflation by national misfortunes (Germany), or, in other cases, by a powerfully driving national will that leads a people beyond the economic possibilities of the moment (Japan), has not explained this inflation as a monetary phenomenon. If he contents himself with a reference to overall social processes, of which inflation appears as one element, he will have leaped over the group of problems which are specifically the problems of currency policy. And a characteristic class of inadequacies—both in the field of currency policy and in the field of monetary analysis—whose nature and scope will become clear to us as we go on, is a consequence of the belief that comprehension of the complex of social causes underlying a monetary phenomenon is identical with comprehension of this phenomenon itself. The latter would be true only if the complex of social causes determined the monetary phenomenon unambiguously. But an unprejudiced person will perceive immediately that (to continue with our example) a political and social situation of a kind that makes inflationary currency policy practically understandable does not determine the actual appearance of an inflation with the same inevitability (and still less does it determine the extent of the inflation with the same unambiguity) as, say, an abundant crop determines the fall in price of agricultural products: anyone, for example, who says that the collapse of the German currency was due to the invasion of the Ruhr has thus far said *nothing* from the standpoint of currency policy.

No one objects when we say that the skin condition of an animal's body depends on the condition of all its organs, but, at the same time, that the condition of the skin is an essential element in the condition of all the other organs. Just as little objection should be raised to our present inverse proposition: namely, that currency policy and the existing state of the currency in principle always exert an important influence on what a people wills or does and on all elements of its social and economic condition. This proposition holds both in the sense that currency policy and the condition of the currency substantively affect all other policies and all other kinds of conditions, and in the sense that regard for currency policy and the condition of the currency help to determine behavior also in fields that seem quite remote, and help to explain conditions which seem to have nothing to do with the currency. To the generation that has lived through the World War and the postwar period, it is not necessary to explain that currency difficulties may become the central problem of financial policy and may dominate it; or that, in general, every social and economic policy may become dependent on the state of the currency and a concern therewith; or, likewise, that, at the same time, currency conditions decide the economic decline or economic success of individuals and bring about economic and social displacements whose quantitative over-all significance is far greater than that of the effects of all the revolutions that have occurred in the same historical period. We have seen the domestic and foreign policy of states with wrecked monetary systems during this period depend on the state of their currencies. And we have all experienced the disorganizing effect of a destruction of the currency on the national character, on morals, and on all the ramifications of cultural life. But just as the events of the war and postwar period have otherwise brought nothing new economically or sociologically, but have merely presented long-familiar phenomena on an enlarged scale, so all these things could be shown to have happened also, for example, during the Napoleonic period or during the social and intellectual tensions and explosions of the sixteenth century. (In the latter case this was particularly clear, because the price revolution, which frightened people and created an atmosphere of unrest in which traditions and customs lost their importance and the social organism pulsated feverishly, was due quite predominantly to monetary causes—the accident of imports of precious metals from America and internal currency depreciations.) *Qualitatively*, the same proposition holds also for tranquil periods. Direct observation of actual practice shows us how every weakness of the currency weakens the position of a people in domestic and foreign policy; how, through central bank policy as the connecting link, the impulse of every fluctuation in the condition of the national currency spreads itself over the whole economy and makes itself felt on all symptoms of economic health—the levels of employment, of wages and profits, export and import figures, and so on.

But this side of the matter can also be overstressed, to the disadvantage of both practice and analysis. Specifically, it is possible to overstress both the significance (and particularly the causal role) of currency relationships and the significance of what currency *policy* can do for the currency itself and for the economy. An obviously absurd attempt has been made, for example, to explain the decline of the old Roman empire by the cessation of imports of the precious metals. Of more practical importance is the almost mystic view, widely held by laymen, according to which the monetary system (which is not understood) is a source of mysterious influence on the weal and woe of peoples and is even the source of most social evils. A sharply defined type of monomaniac social reformer sees in the monetary system, in its reform or abolition, the social panacea: the existence of such individuals has always been one of the greatest sources of unpleasantness for the professional makers of monetary policy and students of money. But even when exaggeration of the power of currency policy or of the merit of specific monetary systems does not take pathological forms, it is frequent and disturbing enough.[2] One finds here, even in the case of people otherwise sensible and indeed of high standing, particularly in business life, a fanatical declaration of faith with respect to monetary policy which is amenable to no argument and whose roots are often difficult to ascertain: many a person who is otherwise unprejudiced and conciliatory, even on touchy questions, in this matter feels bound to regard anyone who differs with him as a rascal. For our purpose it was necessary only to warn against two opposite, but equally false, basic attitudes.

§ 2. *Currency* policy is *policy*. Therefore scientific analysis can, indeed, make comprehensible the establishment, the effects, and the tendencies of monetary systems and currency conditions—it can "explain the facts"—and therefore can indicate what kinds of *instruments* of monetary policy must be

[2] How very receptive the public is to such exaggeration is shown by no other example so well as by the powerful immediate effect of that speech of Bryan which contained the words, immortal in their way: "You shall not crucify mankind upon a cross of gold." It was one of his electioneering speeches in one of his campaigns for the presidency of the United States. He was not elected. But the audience was moved to its core. And yet the sentence quoted is devoid of any sound meaning.

used in order to attain *given aims*; but it cannot set "ultimate" aims for political action—i.e., it cannot set aims which are not themselves again subordinate to other given aims. Apart from the case in which the reason for a given setting of aims is an error concerning substantive relationships—in which case, of course, a scientific clarification of the relationship decides the fate of the aim—the tools of an empirical special subject such as economics enable us only to establish why certain aims are pursued by certain people under certain circumstances; they do not enable us to prove that these aims themselves are "right" or "wrong." These principles were formulated with classic pithiness already by Senior, and later by Sedgwick. The reader who is interested in this matter may be referred to the statements by v. Gottl, Sombart, and M. Weber at the Vienna meeting of the Verein für Sozialpolitik in 1909.

We wish to illustrate the principles by an example in our field. Up to around the middle of the 1890s, the American farmers were in favor of a silver currency; later they became supporters of the gold standard. These settings of goals of currency policy become comprehensible to us when we consider that the farmers up to the date indicated were predominantly a debtor class, whereas from that date on they acquired increased holdings of active bank accounts, and to some degree also other monetary investments. They were therefore interested at first in an alleviation of their debt burden; but then this motive disappeared and another—weaker, to be sure, but in the opposite direction—took its place. A silver currency was a suitable means for alleviating the debt burden because, under the circumstances then prevailing, a silver currency meant a falling value of money; the gold standard was then essentially a suitable means for maintaining intact the purchasing power of money-claims, because under the circumstances prevailing at the turn of the century the purchasing power of gold was relatively stable. Hence, these settings of goals in monetary policy, which we have recognized as dependent on the "ultimate" goals indicated above, and therefore as "means," we may characterize as "right" from the standpoint of these given "ultimate" goals (just as we might have characterized them as "wrong" if the silver currency had been devised as a means of lowering the rate of interest) without becoming unfaithful to the scientific standpoint, or confusing our own desires with our analysis, or, finally, without taking sides ourselves by offering value-judgments and engaging in politics. The "ultimate" goal itself we can formulate and understand. But from the scientific standpoint we cannot use it to plead a cause. To be sure, we can indicate to the man of action points of view which he is overlooking. Thus, in the case under discussion, the farmers could have been shown that a long-lasting fall in the value of money is likely to cause a deterioration in the terms of credit, or to raise also the prices of industrial products which the farmer must buy, or, finally, to provoke disturbances in the economic or social process: developments which might have robbed the farmers of part, of the whole, or even of more than the whole, of the advantage which they expected. If it had been a question, not of the farmers, but of a socially dominant class of great landed proprietors, we might have been able to adduce the further argument that the goal of economic advantage was being sought by them, at least in part, only in the interest of their social and political standing, and that a currency policy directed toward immediate gain would damage the political standing of this class: after all, even within the sphere of economic interests, a distinction must always be drawn between momentary advantage and the interest in *enduring* advantage, and, within a wider sphere of interests (all of them still very "practical" interests), a distinction must be drawn between the *economic* and the social interests of a group. No matter how far we press, in this way, in the direction of more and more comprehensive final aims, no matter how great our gains of territory within which scientific analysis could "set intermediate goals," in principle the final aim in each case must remain inaccessible to us.

If we abstract from the cognitive gulf between what "is" (or "is valid") and what "should be" (or "should be valid"), and ask ourselves the question in purely practical terms, the impossibility of a "scientific policy," in the proper sense of the term, derives first of all from the fact that social groups orient their desires with respect to currency policy (as with respect to all policy) toward their *interest*—broadly or narrowly conceived—and that a choice among various currency policies is possible only on the basis of an appraising partisanship. But this is not all. Even if no group wished to act in accordance with its own interest, and if each wished to act only in accordance with some conception of "the general welfare," we should not be much further ahead. For this "general welfare" looks different from each of the standpoints from which individuals and groups survey the social world and which are indicated to these individuals and groups by their surroundings and their cultural inheritance. No analysis, regardless of how conscientious it may be, can, for example, put the significance of preserving creditor claims in the same light for the socialist, who rejects in principle the continuing validity of these claims, and for the conservative, who regards such continuing validity as an essential element of the social order. The whole social world of each person—what one loves as radiant and good or what one hates as sinister and bad—forces itself into the judgment on such matters. No mere conflict of interests is ever as sharp as the conflict between people who neither wish to defend nor in fact defend the interests of particular groups, but whose outlook rests on different ideals with respect to the future of the nation or of society.

But this conclusion needs a qualification, which is, to be sure, not one of principle, but has all the more practical significance. A physician can make his prescriptions without having to add, each time, "*if* you wish to become well," because the criteria for the condition which we characterize as one of health apply to the great majority of people, and this majority has the desire to be "well," as defined by these criteria. In the same way, the economist could speak of right and wrong measures, and of good and bad currency conditions, without further explanation, if the goals set by people were *in fact* sufficiently similar to one another: the gulf of principle between the realm of analysis and that of volition would not disappear as a result of this, but its significance for the work of science and of practice would disappear if everybody wanted the same thing. In the area of ultimate goals—at the present time, therefore, especially in the area covered by the conflict between the socialist and the private enterprise ideals—such identity in the orientation of desires may be impossible. But in very many other areas this is not so. And we even see that under the disturbed surface of the political struggle the conflicts in the setting of aims are tending to become milder at important points, and that "questions of principle" are tending to fall into the background. Nowhere is this more the case today than in the field of currency policy. Here the disorders of the war and the postwar period, of which all are still aware, have resulted in desires in the field of monetary policy which, to be sure, are not the same for all people, but are very similar for such a majority that divergency of aims practically does not come into consideration: at the moment, hardly more than deviations from the ideal of the majority come into consideration in the case of the concept of health and "ultimate" hygienic aims. Hence, we may make use of the evaluating categories "wrong and right," or "good and bad," in our field with greater freedom than is otherwise permissible, although it must never be forgotten that such epithets, if they are to have scientific meaning, always imply *either* that we are given a group interest from whose standpoint we speak *or* that, in the circumstances of the case, a unanimity of aim for all, or at least for all essential groups, can be assumed.

§ 3. It is easy to formulate that "ultimate" ideal of currency policy which is in our day so widely accepted—even by people who would reap an immediate advantage from a currency policy oriented otherwise—that we may characterize it as the general ideal. For this purpose, we must be clear with respect to a trivial fact which should really require no comment: clearly, the only reason why currency policy and currency conditions have such great significance is that a part of economic welfare depends on them. But currency policy acquires relevance for economic welfare or for economic events in general only because, and insofar as, it influences the *prices of articles of consumption*—in the usual phrase, "the purchasing power of money" or "the value of money." If it did not do so, it would be a technical side-issue which would interest no one and would never have become one of the great national questions. An interest in currency policy and currency conditions is therefore an interest in the "value of money." Currently policy is therefore, in the last analysis, policy with respect to the value of money (von Mises). This simplifies our question with respect to the currency ideal of the present day. There can be, altogether, only three currency ideals to be considered: the ideals of a rising, a falling, and a constant purchasing power of money. We shall see, later on, that these concepts are by no means as simple as they seem to the layman, and we shall have much to say with respect to them. Here we are using them in their popular meaning, with which everyone is familiar, even though in an abundantly imprecise way.

1. The goal of a slowly rising value of money, because it corresponds immediately with the *interest of creditors*, which never was or is popular, is hardly argued for expressly. Rather what is argued for is the identical goal of cheaper prices—the concept of *relative* cheapness of the important consumption goods of the masses being often confused with the concept of a fall of (in principle) *all* prices, with which it has nothing to do. The phenomena of depression, which have usually accompanied general declines in prices, have made this goal entirely unpopular. But it is worth mentioning, even at this stage, that the goal cannot be rejected, say, on the only ground on which science can reject an ideal: namely, that its rational justification

involves errors of substance. Not only is nothing of the sort involved, but it can even be shown that the aversion which this goal encounters in part does imply errors: such as an exaggeration of the harm done to the productive process by a *slow and foreseeable* fall in prices. We need only consider the matter from the standpoint of another type of mentality—one, which, to be sure, is strange to us—in order to understand that a correspondingly high evaluation of the importance of the creditor interest—including that of the "fixed-income receiver"—can also make the premium on saving, which lies in a rising value of money, appear extremely plausible as an element in the "general welfare"; even more so the idea that the fruits of economic development "should" accrue to all classes in the form of an increasing purchasing power for the income-unit rather than in the form of an increase in the nominal amount of income. Moreover, we shall see that the capitalist economy, left to itself, has a tendency, in a certain degree, to realize this ideal: that, in other words, the capitalist economy would, in the absence of "other" disturbances, evidence a *long-run* fall in prices.

2. The goal of a slowly falling value of money is to be distinguished from the question whether in individual cases a fall in the value of money may not be an appropriate method for curing depression phenomena or other temporary evils. At the moment, what is under discussion is a falling value of money as a normal long-run phenomenon. This would acquire meaning only from a standpoint which would insist that no service "should" be linked with a claim on the economy that would be in principle perpetual, and therefore that a gradual dispossession of the current holders of claims expressed in money is desirable:[3] a point of view which is hostile to capital but is not socialistic. The goal in question is somewhat discredited by the fact that it has appeared in alliance with

[3] Under this heading would come "shrinking money" [*Schwundgeld*, analogous to "stamped scrip"], which has been proposed on various occasions.

utopias and quackeries of currency policy; but in substance it is no more absurd than the opposite goal. No less a person than Knut Wicksell has supported it. Moreover, it has found supporters as a method of furthering production and relieving the burdens of the currently most active elements of the economy, the entrepreneurs—a kernel of truth being thereby mingled, to be sure, with much substantive error. Our own generation is still so much impressed by the radical spoliation of creditors and the effects, which it has witnessed, of this way of "furthering production," that it has little taste for this ideal of currency policy.

3. The goal of "stable" or "constant" purchasing power dominates our time. In it the expressed wish of the policymaker and the businessman, or—even more significant—their feeling that such a wish is a matter so self-evident as to be no longer subject to discussion, coincides with the opinion of the best authorities of our subject. This wish and this opinion are not new. If one analyzes the actual behavior, with respect to currency policy, of the men and the institutions who established the practical tradition of the nineteenth century, one finds that the objective meaning behind this behavior was the goal of stable purchasing power, however it may have been formulated and however inadequate the methods applied may have been. The best directors of the central banks, the best supporters of bimetallism, as well as of the pure gold standard, have in fact sought nothing other than this. Even older is the recognition by students of money that at least *many* fluctuations in the value of money perform no function, in the sense that they scatter at random over the economy gains and losses which, unlike other gains and losses, have no definite role in the economic process—that they are technical shortcomings and nothing more: although on the question whether this is true for *all* variations in the value of money and, if not, for *which* variations it is true, very different views have prevailed and still prevail. With this recognition was joined the desire, for scientific as well as for practical purposes,

to establish comparability between sums of money in different places and at different times, and with it also the effort to measure numerically the fluctuations that were occurring in the value of money; so that even one who does not himself accept the ideal of stable prices, or does not accept it completely, must recognize that a large part of the best work was done under its banner. And this resulted in a whole series of proposals for the reform of currency policy—the reform proposals that are to be taken seriously were intended to serve almost exclusively the goal of stable prices—many of these proposals being attached to some of the best names in our science (Walras, Marshall, Irving Fisher, Keynes). The experiences of the war and the postwar period have only provided new wind for these sails, and have put the goal of a "stable value of money" on the agenda of practical discussion. Thereby a new horizon was opened up: currency policy for the first time came into the view of a larger circle as a *therapy of the economy*, as a method for giving shape to the industrial body by means of economic policy. For the time being, however, it is stability of the value of money as such which stands in the foreground—even in those cases in which nothing more is sought than a "sound" currency and secure rates of foreign exchange. We shall develop our argument chiefly from the standpoint of this goal, without, however, identifying ourselves with it.

Let us hold to the proposition that a "sound currency" nowadays means, in practice, a currency which is capable of preventing the value of money from fluctuating. In America the expression "sound money" forced its way into the arsenal of political weapons, first during the struggle over silver. Originally "sound money" meant, to be sure, a money consisting of gold, or reliably redeemable in gold, without much emphasis being put on the fluctuations in gold itself. But that this represented only a preliminary step toward further understanding, and was in fact a crude expression of the desire for a stable money, we see from the *moral* connotations which the expression acquired. The "sound money man" was the man who disapproved of fluctuations in the value of money and the speculative gains resulting therefrom because he regarded them as "unreal" from a moral and business standpoint, and who meant, by "sound" money, above all "*honest*" money: yet, in the light of what was said above, properly interpreted, this leads back to the ideal of stable money, even though the earlier generation was satisfied with an instrument for accomplishing this ideal—the gold standard—which was not adequate for the purpose.[4] Let us consider a further strand in these relationships which meanwhile has become atrophied. The gold standard was always part of the program of liberal parties of the strict faith:[5] first, as a consequence of the point of view indicated above; and also because it corresponded to the ethics of liberal economics (the *do ut des* of the market), even though, as we have said, it did not do so completely. But then there was added a connotation which has nowadays lost its political force. Gold money became sound money for liberalism also because it was a money which was beyond the reach of political manipulation (or was at least less accessible to such manipulation) and left domestic price formation and the foreign exchanges to the accidents of gold production and the mechanism of gold movements. Hence also one of the psychological sources of the aversion of the modern intellectual to gold as the standard metal, because it smacks of the autonomy of the private enterprise economy and offers difficulties to the propensity toward intervention of both socialists and neomercantilists.

The ideal of stable money does not necessarily mean, of

[4] But *because* that generation was satisfied with this instrument, and regarded the gold standard as guaranteeing stability, there evolved an association between "honest" money and gold money which has retained an ethical note even in our own day. This is, on the one hand, very important for currency policy, and, on the other hand, a good example of "associative thinking" in matters of policy.

[5] The Democratic party in America never belonged to this group.

course, that it was necessary to argue at *every* moment for the perpetuation of the value of money then prevailing. If, for example, what we have is a ruined currency, this ideal requires that an attempt should be made to go over to a "sound," and therefore stable, currency. At what exchange rate this is to be done; whether the stable currency unit is to be accepted at a value greater than, less than, or equal to that attaching, for the moment, to the ruined currency unit—this is a separate matter. Moreover, the setting of this goal in itself requires only that the purchasing power of the monetary unit should show no long-term changes. Again it is a separate question whether short-term fluctuations, especially in the case of cyclical or seasonal variation, are or are not to be condoned and even, under certain circumstances, to be brought about. Finally, again a warning that is even more necessary in the case of this currency ideal than in the case of the other two: without further analysis, not only its detailed articulation, but its very nature is indefinite and hazy. It would be a good preparatory exercise for the grader to clarify what he and others understand by this ideal, and in this way to reveal to himself what an abundance of problems requiring solution lies behind the concept.

Chapter 2: On the Sociology of Money

§ 1. Before we say something on the development and the present status of monetary studies, we wish, in this chapter, to touch on several topics in a field that could be called The Sociology of Money. These topics lie outside our real task [which is to contribute to the *economic* theory of money], but they have an effect on some of those problems which do lie within our field, and the present state of scientific discussion makes it desirable to go into the matter briefly. In so doing, we shall use all concepts in their everyday meaning, without defining all of them. And we shall use the opportunity to prepare the way for later argument.

Money, like any other economic institution, is one element in the total social process, and as such, it is subject-matter not only for economic theory, but also for sociology and, finally, for the historical, ethnological, and statistical "investigation of facts." This is not the place to expound in principle the relation of the latter to "theory." It should be sufficient to say that for us what "the investigation of facts" means is not only that it is the object of theoretical explanation and a means of verifying theoretical propositions, but also that there seems to exist between "theory" and "the investigation of facts" a continuous mutual interaction in the posing of problems, ways of interpretation, and the utilization of our perceptions, in accordance with the nature of every empirical discipline. In the light of our discussion in Chapter 1, the required factual material extends, indeed, far beyond—and almost without any apparent limit beyond—mere "monetary history" or monetary statistics.

We must, therefore, be aware that the science of money is represented only by the *combination* of the history, statistics, and ethnology of money and credit, on the one hand, and the theory of money, credit, and currency, on the other; and that these subjects are so inseparable that it is impossible to produce a satisfactory history of money independently of theory, or to develop a complete theory which would not be laboriously developed in the light of the facts (in principle, *all* the facts) currently available. But within the framework of our present task, the individual fact of currency history can appear only in the role of an example; for our task consists of indicating how monetary phenomena are to be envisioned and interpreted—although it is incidentally desirable that we should not fail to mention any of the "great" events of monetary history: that is, those events which, whether they are or are not instructive for our understanding,[1] were symptomatically or causally of

[1] I.e., whether or not they are "generally interesting." Of course, an historically

significance *for the actual course of events* as unique historical developments, as historical individuals.

We shall, moreover, develop the theory of money and credit transactions on the basis of a schema which is taken from the modern form of such transactions and is directed toward the modern problems raised by these transactions. And we shall do this not merely, indeed, for reasons of didactic expediency, but also because this procedure seems to us substantively more correct than would be a starting from as primitive a set of conditions as possible. The reader will see that (and the reasons why), in so doing, all other monetary conditions, hitherto observed or even regarded as possible only conceptually, will receive their due, by means of an appropriate adaptation of our scheme, or the dropping of many characteristics and the insertion of others: if the reader should not see this, it could be only the result of shortcomings in our exposition. Now, two questions of principle are raised by this procedure, which thus juxtaposes substantively problems which belong to different periods and incommensurable cultural environments, and in which the historically latest form of our object of investigation becomes its basic theoretical form, or at least becomes the closest "real" neighbor of the basic theoretical form.

The first of these questions is as follows: Is there *one* theory of Money for all historical epochs or "economic styles" (Spiethoff), or must a special theory be constructed for each? The very posing of this question implies rejection of one possible view: namely, the view that the cultural environment of each epoch is *so* unique that it becomes incomprehensible

significant development can be theoretically so simple that it offers us no theoretical interest; conversely, a development may provide unique insights into matters of principle even though it need hardly be noticed by the historian, either because of the smallness of its practical effects or the smallness of the country in which it occurs. Cf. Macaulay's Essay on Sir William Temple, and Max Weber in "Roscher und Knies und die Logischen Probleme der Historischen Nationalökonomie," *Gesammelte Aufsätze zur Wissenschaftslehre* (Tübingen, 1922).

from the standpoint of the cultural environment of every other epoch and inaccessible through the categories of these other epochs. This may be so; but no one who takes this position should at the same time assume, with the naive arrogance of the intellectual, that it will nevertheless be possible, precisely for him, to look strange cultures in the face with his time-bound eyes: on the contrary, he must give up not only activity in individual disciplines but also the very writing of history.

If a less extreme position is taken, one comes to a view to which social science in all fields (e.g., in the field of legal history and legal theory) owes so much: the view that we may not judge conditions and developments of cultures remote from us in time or space from the narrow viewpoint of the intellectual and material interests of our own culture, and may not project our own standards—even our logical standards—into strange cultures, as the sociologically untrained people of all times (not merely of the eighteenth century) are always inclined to do. But since this conception implies that strange cultures are nevertheless accessible, somehow and in some sense, to us, the attempt to provide analytical methods for opening them up to us can at the most be mistaken in an individual case, but cannot be meaningless in principle. Whether these methods are different each time, or are always the same, is merely a question of performance, which can be solved only by practical work and not by philosophizing.

Certainly money means something very different in the minds and the behavior of people of different cultures. It may be difficult or impossible to reduce its *cultural significance* to a common denominator for different periods. But this kind of interpretation of meaning is not what concerns monetary science. For the latter, what is involved is rather—if we must speak of "meaning" at all—*that* meaning which lies in the *function* of money in the economic process. For *this* meaning the *other* ("cultural significance") is relevant only insofar as it influences the actual behavior of people with respect to money;

and here it is again a question of performance (to be answered in the individual case) whether one succeeds in grasping those elements of a given cultural environment which are essential for the explanation of the events of monetary history. An example: if the object that performs the monetary function is at the same time a sacred object, and disposal of it is connected with religious prescriptions, the money transactions of the community in question will look different (not only from the standpoint of cultural history, but also from an economic standpoint) from what would otherwise be the case: for instance, the inclination to hold on to pieces of the object as long as possible will take on a scope that would be incomprehensible from the standpoint of "merely" economic considerations, but may be very important for the actual course of events. But this is the only relevance that this type of mentality or cultural environment has for this case. Important as further exploration of it may be otherwise, *from the standpoint of monetary theory* we have nothing to gain thereby. Our analytical apparatus operates with respect to such a case exactly as it does in others, and requires, for the handling of such a case, only the precaution of taking into account the actual effect upon people's behavior of the sacramental character of the money commodity along with the other concrete data which, after all, must always be "inserted" into theoretical reasoning. From facts of this kind, in themselves, therefore, there can arise no argument *for* "epoch-bound" theories and *against* "general" theories.

On the other hand, the form of monetary relationships might itself be so different from one epoch to another that it would be of no practical value to present separately a "general" theory which would be limited to meaningless generalities. At first glance, this really seems to be the case: what does a system of payments through the banks have in common with Homer's "accounting in terms of cattle"? Moreover, many ways of viewing the matter fit some individual historical situations so much better than they do others that one might be tempted to characterize them as "right" for the former and "wrong" for the latter.

Monetary doctrine might very well, therefore, take the form of a conceptual formulation of "types" of successive historical situations. This would give us a series of monetary theories corresponding to these various "styles." And this would give a very clear and graphic expression not only to the historical qualification of our subject-matter, but also to the practical problems of each epoch. It could not then come about so easily that, as sometimes happens, analyses of special circumstances are extended to other circumstances which do not have the same characteristics: as when, for example, in discussions of the transfer problem in present-day Germany the argument is such as to imply that international relationships are confined to commodity trade and automatic gold movements in the same degree as they would have been a hundred years ago, and overlooks the movements of short-term capital—to mention only one factor.

But if we were to proceed in this way, we would find that we should *in fact* have to repeat very many things each time and, in addition, that what would have to be repeated would be precisely the theoretical heart of the matter, the principle for understanding it, and the most important lever of analysis. We could not say, for example, that the commodity value of the money material was part of the essential nature of money in the Germany of the tenth century and was not part of it in the Germany of the twentieth century. On the contrary, it would appear that this criterion is either *always* or *never* part of the essential nature of money, even though it may be very true that if we had had information about no other conditions than those of the tenth century, we might never have hit upon the idea that there may be such a thing also as money "without commodity value."[2] It should be noticed, moreover, that this

[2] Completely without significance, moreover, are the views of the people who are themselves under consideration. The concept of income (not a very valuable concept)

has nothing to do with the question whether an independent value of the money material may not have been practically indispensable at that time. This question may call for an affirmative answer. For the people of that day, money of any other sort may have been incomprehensible and unusable in commerce (although it should not be asserted that this was in fact the case). But it does not follow from this that the theoretical interpretation of the money of that economic world would have to pass through the criterion of commodity value. Incidentally, attention may be directed to the great importance, also from the standpoint of currency policy, of the distinction between "practically unavoidable" and "theoretically essential." Currency policy today, for example, as we shall see, cannot easily in practice neglect the connection of every currency with gold. If the currency policy of a single country did so, doubtless a source of inadequacies would be opened up. But this does not mean that it is the very nature of money to consist *of* gold or to be tied *to* gold.[3] By refuting such a view, one could refute the practical standpoint indicated above only if the latter rested on nothing more than this theoretical conviction—and this is hardly the case.

§ 2. The second question is as follows: In view of the fact that the modern monetary and credit system is very complicated and the further fact that it has *evolved* out of primitive and historically prior conditions, must we not go back to the historical, ethnological, primeval "origins" of money, as the natural starting-point of our analysis? This may be called the question of the relation between historical priority and logical priority.

for example, is directly applicable to the economy of the early Middle Ages in Germany, although—according to Bücher—the people of the period did not themselves have the concept.

[3] For this view the name "metallism" has become common (Knapp). We see, then, that we have reasons for distinguishing *theoretical* metallism from those considerations of expediency in the matter of currency policy which we will call *practical* metallism. The two have nothing in common and can be argued for independently of each other.

Of course we must extend our factual material in place and time as far as we can. Anyone, however, who investigates the historical and prehistorical "beginnings" of money in the hope that the essence of the matter will thereby reveal itself in its purest and simplest form is in danger of going astray in three different respects.

First of all, it is customary, in the historical and sociological investigation of social institutions, to supplement the material of the beginnings of history with ethnological material, on the assumption that the conditions of primitive peoples of the present day are relics of our own past. This assumption can be made only under special rules of caution. The primitives, or culturally backward peoples, of the present day have behind them a past during which, continually thrust back into more and more inadequate surroundings, they have deteriorated and have acquired "primitive qualities" which were not characteristic of them previously.

Apart from this, however, it is a prejudice to believe that either what happens first historically or what is culturally more primitive is also necessarily the simpler logically and the less complicated. This is best seen from an example. Anyone who attempts to approach an understanding of the essential nature of the modern entrepreneur by tracing back the type historically very soon lands at a social condition in which the entrepreneur seems to be absent. But in fact it is not the essential function that is lacking: what is lacking is only its embodiment in a special type of economic subject. It becomes an element in a unified position of social leadership, which often unites also priestly, judiciary, and administrative functions. But in order to see through the substance of this matter, and to recognize the element of entrepreneurship in, say, the chieftain of a primitive horde, one must have become clear, on the basis of other considerations, as to what constitutes this element of entrepreneurship. And even so the most primitive conditions present not a simpler, but a more complex, body of factual material. Only as time went on did the entrepreneurial function take on sharper outlines. And we find that even as recently as a hundred years ago, this function was so regularly tied up with the capitalist function that the theory of those days almost unanimously lumped the two of them together; indeed, as is well known, it regarded the capitalist function as the essential one. In this case, therefore, the essence of the matter became crystallized only in the course of history, and it is precisely the most modern forms of manifestation that are here the purest logically and the simplest substantively.

To be sure, one may not assume, conversely, that it is always so. Rather, the logical and the historical "unfolding"[4] must always be kept separate in principle. And since it is also not self-evident a priori that the historical development must evidence all possible traits of the object studied, or must always evidence in complete purity all its essential or interesting traits, nothing justifies the expectation that an understanding of its essential principles will emerge as an inevitable by-product of an historical investigation.

As applied to our case: if a person holds the *theoretical* view that money, by its very nature, is a commodity which is also used as medium of exchange, and at the same time holds the view that, *from the standpoint of cultural history*, money "originally" represented such a commodity, he would thereby be stating that the "essential" form of money is also the oldest historically. Such a coincidence is sociologically interesting. But from the standpoint of practical analytical work it is, in and of itself, entirely *accidental*. There is just as little ground for basing the theoretical view in question on possible facts of cultural history as there is for basing a conjecture as to cultural history on that theoretical view: no theory of money can be refuted by demonstration of the falsity of any assertions of its

[4] This word is used here in a quite unphilosophic sense; above all, however, it is not used in an emanative sense. Moreover, a distinction must always be made between the history of actual developments and the views of particular periods concerning these developments; and one must also, in making this distinction, ask one's self whether the same word always means the same thing substantively.

author concerning the primitive history of money, and no theory can be proven to be correct by a demonstration of the correctness of such assertions by its author.[5] And which historical condition is to be considered as evidencing the "basic form" of money—if *any* is to be considered as such—is decided for each investigator on the basis of his theoretical understanding, not the other way around. The view which is here supported has already been indicated. From this point of view, it is precisely the primitive forms of money which are seen to be the complicated ones, the ones which veil the essence of the matter most completely—and it is precisely *those* transactions which use a commodity to perform the functions of money that represent, from a theoretical point of view, the greatest aberration of reality from the "essence of the matter."

Yet we must be on our guard against rejecting, solely on this ground, the argument of the writers who have fallen into the error that we have censured. It is, rather, a question of fact, in the individual case, as to just what is invalidated by this error. And we must also be on our guard against ascribing this error, just censured, to every writer whose exposition looks as if he were committing it. To do so would be to misunderstand what was a very common method of exposition in our subject especially in the past. Just as it would be excessively unintelligent to base objections to the epic form of exposition of social utopias (or even of the findings of social science) which used to be so favored and was so charming, on the ground that the things under discussion never happened "that way," so, in considering that form of exposition of findings in social science which developed from the epic form and has held its place among us for an unduly long time, we ought not interpret every assumption clothed in pseudo-historic forms as an assertion concerning conditions of cultural history.[6] Even

[5] The lumping of the genetic problem with the analytical problem is characteristic of all writing on money up to and including that of Menger.

[6] This applies also to such constructions as those illustrated by the idea of a *contrat*

when a writer *thinks* that he is advancing a proposition which is objectively tenable, the content of his proposition may still be useful when regarded as an assumption for the purpose of organizing a simple collection of facts and of distinguishing the different logical steps in the exposition.

§ 3. This conclusion does not, indeed, deprive the problem of the genetic origin of money of any of its significance for sociology, social psychology, and cultural history; but it does deprive it of a large part of its significance for monetary theory. The remarks that we nevertheless wish to make on this point will be inserted here. For the rest, reference is made to the literature, to which the best introduction, for the purposes of the economist, is still Menger, and, of more recent authors, especially Burns.[7]

First of all, we must determine what phenomena in the economic world of primitive peoples we wish to regard as historical sources for later systems of monetary transactions. In so doing, it will be expedient to start from those four functions of money which the monetary doctrine of the nineteenth century—especially the English—used to distinguish and put in the forefront of its exposition. All or some of them are what is meant by historians, ethnologists, or paleontologists when they speak of the origins of money. What are involved are the functions of money as medium of exchange, as measure of value, as standard of payments, and as store of value.

1. *Medium of Exchange.* Wherever there is exchange, we observe—not always, to be sure, but even in very primitive cases—that there is a taking and giving, in exchange, of goods which the receiver does not use or consume, but uses for further exchange. If we ask merely why this happens, there

social. Likewise, descriptions in terms of the "Crusoe economy" represented merely a not entirely flattering concession to the reader's ability to understand.

[7] Carl Menger, "Geld," in *Handwörterbuch der Staatswissenschaften*, 3d ed. (Jena, 1909), 4:565 ff.; Arthur Robert Burns, *Money and Monetary Policy in Early Times* (New York, 1927).

can be only one answer: because it is obviously so expedient[8] that, under the influence of encouraging experience over thousands of years, it makes its way wherever there are regular exchange transactions involving more than two commodities.

It should be noted that when we say that it is very time-consuming, inconvenient, and often impossible to find a trading partner who has precisely what one needs, and who needs precisely what one has, and that for this reason there will be introduced and maintained *indirect exchange*, in which one accepts what one does not need (or does not need in these quantities) but what one may expect to exchange for what one really wants—we in no way ascribe to primitive men a prior understanding of the expediency of the procedure, or any conscious rationality, or even a special act of decision: any more than we ascribe to a swarm of bees an understanding of the geometric properties of the cell of the honeycomb. Nor is there any question of an "invention" of money. But precisely for this reason, we have merely learned *that* this practice has established itself; we have not learned *how* it established itself. This is an entirely different question, a part of the great complex of questions which is connected precisely with the rise of all social institutions.

[8] It should be observed that the exchange mechanism could not, without "indirect" exchange, ever lead at all to the otherwise attainable maximum of utility for all participants. If, for example, we have three commodities—A, B, and C—which are exchanged only directly, so that on each occasion only two are exchanged against each other, there will arise three markets, on each of which will be established between the two commodities an exchange ratio which could be independent of the exchange ratios on the other two markets. Hence, it could happen that, if we let a, b, and c represent units of the commodities, on Market I, 3a might be given for, say, 2b; on Market II, 3a for 1c; and on Market III, 4b for 1c. But in that case, the possessor of 4b who wishes to have C will obviously do better if, instead of acquiring his 1c for 4b on the market of B for C, he would go first to Market I—where he gets for his 4b, in the first instance, 6a, which, to be sure, he does not want, but for which he can get 2c on Market II: this is the essence of arbitrage. If our man could not do this, he would experience not only the possible inconvenience mentioned above, but also a loss of utility. Walras was the first to call attention to this. The use of the word "arbitrage" in discussing a transaction within a primitive tribe illustrates that distinction between "functional meaning" and "cultural meaning" whose neglect has so often led to irrelevant objections.

We have already noted the source of unwarranted objections to the answering of our first question on the basis of understanding by *us*, the observers, of the necessities and feasibilities of the economic situation in a developing system of exchange: namely, that the only thing considered by these objectors is this second problem of the rise of social institutions. In the same way, the unwarranted invoking of the first way of putting the question arises from a failure to recognize the existence and the independent significance of the second way of putting it. An example of this from another field: If we ask *why* men came to tame and breed domestic animals, and why this practice has been maintained, the answer can of course be only that the products and services of domestic animals meant a decisive enrichment of the economic process. But this conclusion tells us nothing about *how* men came to have domestic animals. For it is not only not certain, but not even probable, that prior knowledge of these advantages led to the result, if for no other reason than because its full scope was realized only afterward, and could not have been foreseen. The original motive for taming animals may therefore have been different from that which was decisive for the maintenance and development of the custom. Only in the course of a functional change, which rested on experiences with animals already tamed, could the domestic animal have assumed its later economic role. And inasmuch as the whole thinking of primitive men is ritually colored, it is natural to assume that the original motive had its roots in religious conceptions, and that religious commandments and prohibitions were the channels for that close acquaintance with certain types of animals which was the necessary condition for the discovery and exploitation of their aptitudes. Nevertheless, within the framework of a separate posing of the question, the fact of these aptitudes remains a permissible and necessary explanation which does not take the place of reference to ritual elements, etc.

In the case of money, we understand, further, that the use of particularly *marketable* or *salable* commodities—that is, commodities which everyone is more or less able to use or willing to have—became established in indirect exchange, and that such commodities were gradually recognized as media of exchange without express agreement or legislative compulsion—indeed, without any regard for the general interest. We observe also that sometimes those commodities appear which, under the economic conditions involved, are particularly desired, such as skins—also scalps—ivory, coral, slaves, domestic animals, salt, mats, textiles, tea, tobacco, amber, cocoa beans, bananas, glass beads, dye-stuffs, grain, rice, pieces of metal,[9] or even simple tools such as knives, hatchets, etc. In all this, it is of entirely secondary importance to decide what circumstances helped to bring a particular commodity to its preferential position as medium of exchange: the circumstance, e.g., that it was a current product of the country or a preferred article of import and not producible within the country, or, contrariwise, a staple article of export. In all these instances, which are not limited either to particular areas or particular races, the medium of exchange owes its function to an economic commodity-significance of its own, which is itself unmistakably independent of the medium-of-exchange function. A doubt in this connection is possible only in the case of articles of adornment.[10] For, whereas other types of use or consumption

[9] Bronze pieces from around 4000 years ago onward. The most important instances come from Egypt, China, and Babylon. Later lead, gold, silver, iron and other metals appear—gold earlier than silver, iron chiefly in Greece.

[10] Especially in the case of objects which carry a note of social psychology, and in the case of cultural objects or those which represent, say, social distinction. It should again be emphasized that, in itself, this is a matter of complete indifference for the question of the economic "Why"—in contrast to the "How" of cultural history. It is, indeed, not asserted that the medium-of-exchange function developed precisely in connection with "commodities" that were nonreligious, or served for the satisfaction of "material" needs. A ritual character would explain valuation, and, to that extent, the commodity character of these objects quite as well as would their fitness, say, to serve as food. In still another sense is the "exchange-mediation theory" of the genesis of money independent of, and compatible with, a religious element: specifically, it is possible to hold the view that money serves essentially to facilitate exchange and *therefore* came

provide their explanation immediately, in the case of an object of adornment there is the further question why it is considered to be an object of adornment. And here it might happen that the article performs the medium-of-exchange function, and only thereby acquires a *distinguished position*, and especially also a *distinguishing significance*. A significance for use which in its turn has a prior basis in a commodity's function as medium of exchange would of course not be suited to explain the latter function itself.[11] Such an instance may possibly be represented by the use of shells, especially cowrie shells, which are found among paleolithic remains and in the form of coins which imitate the shape of shells, and continue to live for an extraordinarily long time as linguistic relics. Among modern primitive peoples the ornamental significance is sometimes completely absent—as in the complicated system of shell-money of the Rossel Islands[12]—although, again, this does not prove that it was always absent in these instances.

Despite this limitation—it is a very important one, but it is also the only important one—the supporting evidence for this conception of the genesis of money is so oppressively abundant that we must understand its vitality, especially if we bear in mind that the differences and the controversies as between the individual variants of this conception do not affect its basic idea. In addition, there are at least important cases of exchange-mediation in which one might be tempted to deny the commodity significance of the *exchange-mediator* and to speak of a "token money," but which in fact clearly point backward to earlier commodity meanings. Thus, according to

into being, and *at the same time* that its use corresponds to divine precepts—as one may read in St. Thomas.

[11] Cf. a similar instance of circular reasoning, of which the marginal utility theorists *seem* to be guilty: Money has use-value because it has exchange-value, and has exchange-value because it has—precisely the *former*—use-value.

[12] Cf. W. E. Armstrong, "Rossel Island Money: A Unique Monetary System," *Economic Journal* 34 (1924): 423 ff. On China, see Chi Zang Waung, "The Ancient Coins and Currency of China," *Economic Journal* 23 (1913): 524 ff.

Max Weber, Russia had fur money—small pieces of fur without use value. But the thought that this fur-money *without* use-value goes back to fur-money *with* use-value is too obvious to prove more than that there can be such a thing as money *made of material without value in itself*: a point which is not relevant here and which we knew anyway. (Similarly, in the light of what has just been said, no basic significance is to be attributed to the classification by Weber [*Wirtschaftsgeschichte*, p. 211]: Ornament Money—Use Money—Clothing Money—Token Money.) What is apt to make the strongest impression, however, is the fate of the most important ethnological example which monetary doctrine has thus far been able to adduce of a pure token-money without any commodity significance. The natives of the Portuguese colony of Angola used in their domestic transactions a value-token which European observers used to call the "macute," and which seemed to have no commodity-significance. Writers on money in the eighteenth century, including Montesquieu and Steuart, put very great emphasis on this, and Mill, also, regarded the macute as an authentic case of a conventional unit of a pure money of account. But it seems now to be established[13] that the macute was originally a piece of clothing—thus representing a typical case of commodity money, which was only gradually reduced to an otherwise useless scrap of cotton cloth or matting which was in turn finally included under the Portuguese coinage authority, at first simply by a stamping of the cloth and later by the replacement of this cloth by a coin—so that the historical connection with a commodity money is given here also. And in *this* connection, this is all that is necessary.[14]

[13] Cf. A. Sommer, "Die Makute, ein Irrtum der Geldlehre," *Jahrbücher für Nationalökonomie und Statistik* 131 (1929/II). The author overestimates, to be sure, the significance of the erroneous factual assertion for the theoretical argument of the writers in question.

[14] The theoretical problem as to whether such a connection is logically necessary is, to be sure, not advanced thereby.

As matters stand, therefore, we must regard as substantially certain not only the development of money out of exchange transactions, but also—and this is a separate proposition—out of the exchange-mediating function of whatever particularly salable commodity happened to be involved. If anything, the correctness of this conception is even clearer when it is applied to pieces of metal prepared for transaction purposes—that is, coins—which later linguistic development often came to characterize as true money (cf. the Latin *moneta* with its French, Italian, Spanish, Portuguese, and English derivatives, the Russian *denghi*, the Hungarian *penz*, etc.). Not only do the names of coins and the pictures on coins frequently point to commodity meanings (again: this kind of "symbolism" argues, not against, but precisely for, the derivation of money from the most salable commodity); not only is it often demonstrable that coins have replaced a commodity money used in the same locality at an earlier time; but step-by-step transformation of commodity money into coins is historically demonstrable.

We begin with units of the exchange metals in quantities common in the market. The next step, which can be traced in Mesopotamia and Egypt, is the appearance of authoritatively standardized weights and their confirmation by officials. Then follows the transfer, to the labeling of metal-pieces, of the old custom of marking the conclusion of contracts with a seal. This seal was at first purely private—say, the seal of a firm of merchants—as in the case of the Semitic shekel and the Chinese tael. The beginning of this practice used to be placed in the seventh century B.C., but new discoveries of coins and documents in India, Egypt, and also in Assyria and China, point back to much earlier times. Around the Aegean Sea, within the Greek sphere of influence, if not actually first in Greece itself, comes the further step: improved coinage technique and monopolization of coinage by the public power ("coinage authority," as an exclusive authorization to regulate coinage—in particular to determine the "standard weight" and the "standard of fineness" of the coins—and the "coinage privilege," as an exclusive right to undertake coinage operations). This is all exactly as it should be from the standpoint of a supporter of the view under discussion. If, indeed, one were to suppose that these developments proved something about the nature of money or even of coins, one would be going badly off the track. The reluctance of more recent, as well as of earlier, students of money to *define* a coin as a stamped piece of metal and to see in the *coinage-stamp* only an official *declaration of the fine content* of the coin rests upon an entirely correct feeling. But *historically* coins and mint-stamps were, at the outset, nothing else.

The objections affect only side-issues, insofar as they do not rest merely on misunderstandings or are completely meaningless—as, for example, the objection that this account of the genesis of money is rationalistic and individualistic and is therefore to be rejected a priori. If, nevertheless, the account as given is not fully satisfactory, this arises from a circumstance that may be referred to as the originally "subsidiary character" of indirect exchange.

In spite of everything we have said with respect to the expediency, indeed—from one particular point of view—the necessity, of indirect exchange, the latter is not only a *further* step analytically, but also a *later* step historically. True exchange transactions can exist for long periods without resulting in indirect exchange and the emergence of an exchange-mediating commodity. Of primitive instances, the one that stands out is so-called "silent trading" as it is practiced even today, for example, between the agricultural Negroes and the hunting pygmy peoples of the Upper Congo. The economic schema of exchange fits it perfectly, and yet it lacks a medium of exchange. The practice of exchanging directly what one wishes to give for what one wishes to have can be shown to be widespread even today, and occurs actually in Europe, as in the case of the peasants of southern Portugal. International trade, finally, was originally only direct exchange, and still is that, even today, in trade between peoples of very divergent cultural levels: a fact which explains why a trading people like the Phoenicians by no means took the lead in developing media of exchange.

In the first place, this opens up the possibility that, in the case of many peoples, indirect exchange with the help of a medium of exchange may have developed only long after the other functions that we usually associate with money must have been operative. But aside from this, it is to be noted that direct exchange is the more immediate of the two, and that indirect exchange may have come about by people beginning, in each case and in principle, to exchange directly, and adopting the roundabout method of direct exchange only when the direct way was not usable. And if indirect exchange was at first an emergency expedient, involving a *subsidiary medium of transactions*, the "most salable commodity" view would recede in favor of the view which concentrates on the commodity which one gives up unwillingly and only when forced to do so. And this latter viewpoint suggests the storing of value and not the mediation of exchange as the "most primary" function, out of which the other functions may have developed, even though these others later became more important and especially the mediation of exchange came to be the dominant element beyond doubt.

2. *Measure of Value*. By "value" is to be understood here "exchange value" expressed in money: hence, whenever what is involved is the quantity-unit commonly used in the market for a commodity—a material commodity or a service—"exchange value" means its unit price, or, if what is involved is a quantity other than the quantity-unit, "exchange value" means this price times this quantity. Thus, if one says that money functions as a "measure of value," one usually means, in *this* context, that the exchange ratios of commodities with one another are replaced by the exchange ratios between each of them and money; that therefore money is a "means of

expressing exchange ratios" and expressing the market worth of each quantity of commodity which is given by these exchange ratios [. . .].[15]

What becomes the "measure of value" is what forces its way into that position. If a medium of exchange is already in existence, and if exchange transactions play a sufficiently great role, it might easily be the medium of exchange that becomes the measure of value. But only then. Otherwise, it is more likely that the place will be taken by a particularly important object of property, even if this object is not the medium of exchange.

Now, this consideration fits very well one of the most important cases of primitive "money": namely, the custom—which we meet with very early, as well as in later documents which hark back to early conditions—of expressing services in terms of a number of *cattle*, and of giving an idea of the value of an object by equating it to a number of cattle. Linguistic relics (*pecunia*, the Gothic *faihu*, the Indian *rupya*) and pictures on coins attest to the extremely wide geographical and historical scope of this custom. At the same time, there is no proof that the cattle passed from hand to hand in exchange transactions. Nor is this at all probable. Laum[16] has called attention to the fact that it is not immediately obvious that cattle are adapted to such use—although this argument has full force only in those cases in which daily transactions also in small quantities of goods are part of the normal economic process. Moreover, the primitive man does not readily separate himself from his cattle, his most valuable possession from the Neolithic epoch on, any more than he readily slaughters it. The primitive nomad herdsman steals cattle, and pays fines

[15] [Editor's note: In order to lay the groundwork for the argument in the later chapters of his book, Schumpeter here engages in a detailed discussion of various economic-theoretical aspects of the concept of "measure of value." These pages have been excluded, and we have resumed where Schumpeter discusses "measure of value" from a sociological viewpoint.]

[16] Bernhard Laum, *Heiliges Geld* (Tübingen, 1924).

and tribute in cattle when he is forced to do so, but he engages as little in the trading of cattle as in eating their meat. Finally, he would never have thought of making cattle the trading-article κατ' ἐξοχὴν. If, therefore, cattle played a role—and this is certain—it may well have been only as a measure of value, first of all in the sense of a measure of exchange-value, but perhaps also in the sense of a measure of use-value.[17] Not without interest, in this connection, also, is the primitive custom of expressing exchange ratios in units of one commodity, but accepting the counter-values in other commodities. The macute, previously mentioned, gives an example whose value is not lessened by the erroneous interpretation of it, likewise mentioned above. If a slave was to be sold—so it is reported[18]—its price was first fixed in macutes. Then exchange-commodities were delivered, each of these commodities likewise being appraised in terms of macutes, until the full amount was reached. If one lets this report sink in, one recognizes without difficulty that it is not exactly nonsense.

3. *Standard of Deferred Payments.* This immediately understandable expression, complementing the concept of mediation of exchange, clearly includes the remaining transactions in which money intervenes. If, then, we sum up, under this heading, all payments which are not direct payments for a commodity, we at once find in the economic world of culturally undeveloped peoples very important—and appealing as being particularly "primordial"—cases that belong here: namely, religious offerings, payments of fines, and gifts arising out of relations of sovereignty. They often consist simply of all the

[17] In this connection, the following facts are interesting. An attempt was often made—as in the Zend Avesta—to moderate the shortcomings which attach to cattle-accounting by specifying the "unit" in terms of age and quality, and bringing it into a fixed ratio to other units in terms of domestic animals. And "money" or "other money," like the solidus of the Carolingian period, was connected with cattle-units of a specific quality—e.g., one-year-old cattle in the fall of the year—as being relatively stable in value.

[18] In the *Dictionnaire Universel de Commerce*, edited by Jacques Savary (Copenhagen, 1759–65), cited in Sommer, "Die Makute."

things which the dead, the gods, priests, and chieftains can use immediately and wish to have—such as food, etc. But very frequently, we meet here the tendency to use certain kinds of commodities preferentially for this purpose. This may be because the commodity in question is already the medium of exchange or measure of value. But this need not be so; on the contrary, it is entirely conceivable that the medium of payment, in this sense, might also be another particularly favored piece of property which does not perform these functions or at least had not previously performed them. And payments of the type indicated may have been precisely the occasion for the quantification of economic concepts, and hence the historical source of the measure of value function and, either *through* the latter or directly, of the medium of exchange function: much as, even in historical times, the money economy and the rationality of the money economy make their way into regions and strata which had previously been ignorant of them, as a result of the fact that a governmental authority standing outside the local cultural environment demanded the payment of taxes in money—as was the case, for example, in some of the Balkan provinces of the Byzantine empire. In such cases, one may certainly speak of an "imposed medium of payment" (Max Weber). But the main thing which is connoted by the latter method of expression is not essential and does not go deeply into the matter.[19] The imposed delivery must be objectively possible

[19] How superficially it penetrates is shown by the reflection that *if* it is correct, as M. Weber asserts, that the function of the "imposed means of payment" is historically the oldest (it would be different if we were speaking of an imposed *delivery*), and appears first in the case of deliveries by a subject to his chieftain (followed only secondarily by a delivery of the chieftain to his retainers), we are then faced with the question as to what the chieftain or his retainers do with what they have thus received. The case cannot be illustrated by a reference to the fact that in Carthage or in the Persian empire gold coinage arose "only for the provision of military means of payment, not of media of exchange" (*Wirtschaftsgeschichte*, p. 209), for this already presupposes a definite market value of these gold-pieces. This criticism is perhaps unjust, since the text of this posthumous publication did not have the final sanction of the author;

and objectively meaningful. And it is in this, and not in the imposition of the medium of payment, that the essence of the matter lies economically. The same holds for the religious element, which naturally is decisively prominent in the case of some of these deliveries: it still explains to us only the "how" of cultural history. It may be that what was involved in the genetically basic case, or at least in a primitive case, was, in the first instance, the commutation of human sacrifice into the blood of an animal; that subsequently the gifts to the priesthood were made predominantly in pieces of this type of animal, and that from this point on, this type of animal became a medium of delivery in general, and then also the measure of value, and eventually the medium of exchange. But here, too, this says nothing at all about the economic "Why."[20]

We have previously recognized the possibility that cattle may be used as a measure of value without having been *previously*—and, in principle, without *ever* having been—the medium of exchange. Although its position as the most important piece of property is entirely adequate to account for this, the result may have come about through the roundabout process of having previously performed the function of the standard of payments—in such a way, therefore, that it was the latter function which particularly emphasized cattle in the consciousness of people. We come across penalties and imposts

---

nevertheless, similar points of view are suggested in M. Weber's great *Wirtschaftssoziologie*.

In this context, M. Weber coins the concept of a "Money without Exchange," which may seem strange from the standpoint of a conception that is still frequently encountered; but it nevertheless makes good sense.

[20] Like many other historians of social institutions—a famous example is Fustel de Coulange in his *Cité Antique*—Laum, also, in his book cited above, exaggerates the explanatory value of such a derivation. But at least he did not overlook the fact that it is not necessarily antithetical to derivations from a state of affairs conceived by the observer, and he showed the existence of the possible connection between the two which is formulated in the following section of our text. The view that the cattle-unit can have been established only by way of dealings with the gods through sacrifice seems to me, to be sure, to go too far. The polemic of Burns (*Money and Monetary Policy*, p. 6, n.) is inadequate in various respects, and also in its translation of *menschlicher Verkehr* (human intercourse) as "human trade."

of all kinds in this form far back in history: thus, for example, in Rome fines were recomputed in terms of copper only around the middle of the fifth century B.C., having been expressed earlier in terms of cattle and sheep.

4. *Store of Value*. The holding of stocks on hand is found also outside man's economic activity, and, generally speaking, is genetically the first expression of economic behavior. It is plausible to suppose that it also became associated predominantly with the type of stock-holding which we call the *formation of treasure* or *hoarding*. To it would correspond the positive impulse—completely nonlogical—to *possess*. Just as "fighting" and "fighting for a rational goal" are quite different social phenomena and the former precedes the latter; just as, even today, the *impulse* to fight must be distinguished from the rational *goal* of the fighting, which often represents only a rationalization *ex post*: so the *nonrational desire to possess* is prior to—and even afterward still the true propelling force behind—the rationalized desire to possess. The behavior that we thereby make understandable to ourselves—in the present instance, make it understandable *ex visu* the mind of the decision-maker—certainly concerns itself, as a rule, with objects which at the same time give it a rational meaning (as, above all, in the case of food). But one finds an additional source of a desire to possess (even though this second source may itself be traceable to the source already indicated): namely, a desire to possess something with which only vague or even *no* conceptions of rational uses are associated—a desire to possess for the sake of possessing and excluding others from possession. The object of this desire may be any object which stands out from its surroundings—for example, a peculiarly shaped stone.[21] Each such item may become the object of the

[21] This might provide a principle of explanation for the "stone money" of the Caroline Islands, which consists of heavy fragments difficult to transport, and probably also for the "Vaygua" of the Trobriand Islanders (north of New Guinea), which includes various kinds of highly valued things, such as axe-blades and necklaces made of particular shells, which, however, are hardly ever actually used, but are

impulse to fight, and, in connection with this, there may emerge a note of social value or magical or ritual significance which is both the result of a first primitive attempt to rationalize and, in the further nexus of mutual interaction, the reason for the selection of the items toward which the desire to possess is directed: this is sufficiently explained by the considerations which are raised in connection with the sociopsychological phenomenon of fashion. As is the case with the whole mental world of primitive people, magically or ritually tinged social customs and *interpretations* thereof by the persons involved are much better explained by this kind of factual material, which corresponds throughout to the environment and the associative thinking of primitive people (Levy-Bruhl), than by assuming a practice, growing out of the requirements of commodity transactions, of "keeping reserves" in particularly salable commodities.

Nevertheless, our "observer's rationality" will lead us to the latter element as the "substantive" function of treasure-formation, and will suggest to us the observation that the primitive man who possesses a good amount of treasure is in a situation analogous to that of a man of our own day who has a large bank account. Against this, in turn, is the fact that in the case of a bank account what is involved is command over something which is already "money" for other reasons, and is held in reserve for precisely this reason. For just as it is possible to hoard what is money in the sense of something which performs the other functions of money, so what is desired as a means of hoarding can become money in the sense of something which performs other functions.[22] The mere fact, say, that the commodity in question does not have use-value

collected as symbols of wealth and are used for gifts to chieftains, etc. (cf. B. Malinowski, "The Primitive Economics of the Trobriand Islanders," *Economic Journal* 31 [1921]: 1 ff.).

[22] In particular, the relation to the "measure of value" comes to the fore: the objects of hoarding are more clearly perceived by the primitive man, and are more carefully watched over and paid than are other objects.

for other purposes is no more of a difficulty in this connection than it is a difficulty, for the valuation of a lap-dog, that the dog is "good for nothing." The hypothesis that we are dealing here with the earliest function of money is supported by the subsidiary character of indirect exchange, as indicated above, and by the compulsory character of most unilateral deliveries—a consideration which fits with the fact that the primitive man does not readily give up his hoard and, as a general rule, does so only when other means fail.

But we do not insist upon this conjecture. In contrast to a theorem which is *uniquely* true within its own system of assumptions, if it is true at all, different views concerning the historical genesis of a social phenomenon can be correct for different cases. Thus, indeed, it is *possibly* futile to strive for *the* correct "theory" (=doctrine) of the rise of cities. It is *certainly* false to believe that there can be only one correct theory.

* Reprinted by permission of the Harvard University Archives.