

'MONEY PRINTING' IN THE MODERN BANKING SYSTEM

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Numerous statements appeared in the financial press last year which equated so-called 'quantitative easing' with money printing and went on to claim that 'the printing of money' was certain to cause inflation. In his *Sunday Telegraph* column on 26 September, Liam Halligan of Prosperity Capital Management described quantitative easing as 'a polite, yet intellectually dishonest name, for "money printing"'. A few days earlier the investment magazine *Shares* had averred that 'in the long run' it could 'only see the further creation of cash out of thin air as inflationary'.

The phrase 'printing money' is pejorative. The thought seems to be that paper money – money not backed by hard assets – is bad, irresponsible and inflationary. By implication, the creation of money in tangible form – coin made from precious metals, money which is 'sound' because it makes a noise when dropped – is good, responsible and anti-inflationary. In turn the issue of paper money is acceptable only when backed by hard assets. In other words, money creation is to be endorsed when the *quality* of money – meaning its nearness to hard, tangible assets (such as precious metals) – is maintained, and to be condemned when that quality has been compromised.

As a comment on economic history and the development of monetary institutions, this line of thought is far from silly. When the convertibility of paper money into a commodity was maintained at a fixed rate (as under the gold standard), paper money held its value far better than since the abandonment of convertibility. But the world has now moved almost completely from commodity-based money to fiat money.

The modern world still has a residual kind of commodity money, namely coin. Coin is of course hard and tangible, and might therefore be deemed particularly virtuous by monetary conservatives of the Halligan school. But – as with paper money – its worth today depends on its legal-tender status, not on its intrinsic value. In any case coin – which is a liability of the Royal Mint, not of the Bank of England – is a trivial fraction of the total quantity of

money. The almost 30 billion coins in issue in this country are worth under £4 billion, equal to roughly 10% of the value of notes in circulation and a mere 0.2% of the overall money stock, where the money stock includes all the sterling bank deposits in the M4 money measure.

Since no part of the money stock nowadays has intrinsic value in any meaningful sense, it is absurd to single out 'printed money' or 'money printing' as specially wicked and inflationary. The reality is that, by the standards of the historical past, all modern money is trash. Moreover, the ranking of these forms of trash is different from that understood by naïve monetary conservatism.

Because transfers across bank accounts have become the dominant means of payment, bank deposits are the principal type of money. If the manufacture of new notes is inherently naughty, what is to be said about the production of new deposits? In the early twentieth century leading authorities such as Irving Fisher suggested that bank deposits were 'fountain-pen money', because bankers created new deposits by writing (with a fountain pen) identical entries on both sides of their balance sheets. Nowadays of course the entries are the result of typing symbols into various forms of electronic equipment. The shocking truth is that bank deposits – by far the most important contemporary form of money – are fabricated 'out of thin air' by secretaries tapping numbers into computers!

The expansion of the note issue by 'printing money' may sound bad, but the creation of deposits – typewriter keyboard money – is far shabbier. Halligan's notions that hard-asset money is superior to paper money, and that any issue of paper money is inflationary, are both wrong. The continued repetition of these obsolete ideas by a prominent columnist in a newspaper of *The Sunday Telegraph's* stature is peculiar and worrying.

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