

Funny Money: Serious Solution?

By Jorim Schraven¹

When your economy is in crisis, probably the last thing you want to do is damage its most fundamental institution: money. Yet, this is exactly what was done in Argentina. The point is, that in order to facilitate transactions people need cash. There needs to be sufficient cash and it needs to be efficiently redistributed according to transaction needs. This normally happens through the banking system, but this process was severely curtailed by the imposed 250 peso per week cap on withdrawals. At the same time, physical stock of cash had to fall as capital left the country. As a direct consequence of the currency board, the peso money supply is completely dependent on dollar trade and capital flows. Argentinean exports to the U.S. account for only a sixth of the total, so there is no *a priori* reason to believe these accounts should balance. In time of crisis, they almost certainly will not. This generates the perverse effect that once in crisis, the money supply must fall, choking off the capacity to transact efficiently, and thus exacerbating the recession.

These problems are by no means new, as Keynes noted, under the pre-war gold standard it was also the balance of payments that determined the 'domestic quantity of circulation' and the only 'means open to the authorities for countering unemployment at home was by struggling for an export surplus and an import of the monetary metal at the expense of their neighbours'.

Thus, as long as the economy fares well, the currency board provides stability but once things turn pear-shaped, it is destabilising because it hampers the economy's ability to facilitate domestic transactions. This is, however, not an argument to abolish the currency board, which does provide stability and credibility for international transactions and capital movements.

To solve the problem of the domestic money shortage, one merely needs to provide a mechanism to facilitate transactions that is not pro-cyclical as the currency board. Thus, the proposal of a parallel currency issued separately and independently of the peso and the dollar.

¹ About the Author:

Jorim Schraven graduated from Corpus Christi College, Oxford University in 2001 with an honours thesis on complementary currency systems. (See "The Economics of Community Currencies: a Theoretical Perspective" at www.jorim.nl/thesis.htm for references to the facts in the article)

Publications by the author on complementary currency systems can be found in the International Journal of Community Currency Research (2000 and 2001 issues: see <http://www.geog.le.ac.uk/ijccr/vol4-6/4toc.htm> <http://www.geog.le.ac.uk/ijccr/vol4-6/5toc.htm>)

However, the arguments about money shortages arising from international trade under a currency board apply equally to regional money shortages arising from inter-regional trade with a national currency. This is an argument against a single national currency. In fact, the lack of credibility of the national institutions combined with the relatively low interdependence of the provinces suggest that parallel currencies are to be issued by the provincial governments and backed by their taxing powers. This would also generate some welcome seigniorage revenue to counteract the cuts in transfers from the national government. Clearly, for national taxation purposes the dollar may function as a stable unit of account.

To deal with the low velocity of circulation due to the hoarding effects of deflation, this complementary monetary institution should be further enhanced. Instead of jeopardising the credibility of these new currencies by generating inflation, the provincial governments should institute a demurrage charge. This feature of money, which works like a negative interest rate, could take the form of the stamp scrip currencies proposed by Silvio Gesell (1862-1930) and championed by Keynes in his *General Theory*. The stamp scrip currency forces the user to revalue the notes each period by purchasing a revaluation stamp. One such currency, issued in the Austrian town of Wörgl during the crisis years in the thirties, had a velocity of circulation of 463 compared to 21 for the national Schilling and local unemployment fell by 25% in the year it was first issued.

Evidently, the problems of Argentina extend well beyond its monetary arrangements. However, these arrangements have greatly exacerbated the current crisis. An optimal adaptation of its monetary institutions would not just entail one parallel currency like the Argentine, but several regional ones with an inbuilt incentive to increase circulation.