

Getting Money Right

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If your education about the political economy of money has come from the heights of academia and the corporate media, many of the things you may think you know about money are dramatically untrue. Obscured by a dense array of common-sense and academic falsehoods, the truth of these matters is perfectly well understood by bankers and other ruling class players. They much prefer that you remain in the dark. Possibly, the entire edifice of establishment commentary in politics and economics is carefully constructed to foster ignorance¹ about the realities of money and its origins in society.

Even if it's just an oversight that the keepers of mainstream discourse tirelessly disseminate falsity, you should still want to know the truth. If you accept the conventional wisdom, you are likely to significantly underestimate the policy options that are available to the US government and other sovereign money issuers. You may fail to appreciate the dire consequences of ceding monetary sovereignty to external powers. You may overlook the vast power wielded by bankers through their legal authority (and near monopoly) to create money, subject to only the merest glance of democratic oversight. That power has been hijacked from society at large. Our challenge is to claw it back. Take a step towards regaining democratic sovereignty by understanding the realities of money and rejecting the ubiquitous lies.

¹ ../agnotology.html

Money is Complicated? *Not Really*

So what is money? Complex textbook definitions² invoke notions like medium of exchange, store of value, and unit of account. These definitions seem designed to obscure rather than illuminate. We say: *Money is a claim on the resources of the society that issues it.*³ More particularly, the salable resources, including all the goods and services available for sale in the society. That includes things like real estate, raw materials, manufactured products, and the many paid services that are provided by the efforts of the society's participants. When you have some money, you can exchange it for (hence, claim) some goods and services. Got more money? You command more resources! Kudos. Without money, you may still have some claims, but money gates access to everything salable in the whole society.

What I want to emphasize in this definition is the role of society. *Money is social.*⁴ Society defines it, creates it, uses it, and destroys it. What society offers (or demands) in exchange for money gives money its value. Society makes (and selectively enforces) the laws that govern money and its usage. That's policy. These are not natural laws like those which govern the weather or nuclear physics. We can change our policy for the better.

There is one genuine complication in understanding money that you must grasp firmly if you are to understand what follows. Money is social, but all participants of society are not equal before money. Money divides society into two distinct parts: sovereign and subject.

² [../money/textbook-money.html](#)

³ [../money/claim-on-society.html](#)

⁴ [../money/claim-on-society.html](#)

The sovereign is the issuer of the money. Typically that's a murky conglomeration of federal government and central bank in modern nations, with some notable exceptions like the EU. Everybody else in society is a user of the money. Those users I call subjects to emphasize the asymmetry of the money relation. Subjects don't get to issue money (unless they are banks, more on that later). Subjects can include persons, businesses, local governments, and even nations in case of the EU and other monetary unions. Even sovereigns are subject when they deal in the money of another sovereign. I emphasize the distinction between subject and sovereign because the sovereign has vast powers over the resources of the society, by virtue of that capability to issue money. Subjects, not so much.

In a democracy, sovereignty is said to rest with the people. But real sovereignty also (maybe even primarily) resides in the power to issue money. Who controls the money supply exercises huge influence, regardless of the theatrical appurtenances of government. Hence all the obfuscation and aura of mystery (artificial complications) around central bank, government treasury, and private banks, designed to limit democratic oversight.

Failing to distinguish sovereign from subject enables an especially pernicious lie which comes in various guises. Asserting or implying that the sovereign is just another subject serves as bulwark justification for all sorts of dereliction of duty by society's leaders, under the excuse that the money isn't available. For the sovereign, the money is always available; if the physical resources are also available, only the will to use it is what's lacking.

One useful criterion of a democracy is the degree to which the policies of money reflect the needs and values of the people of the society. When a tiny elite of bankers and their cronies monopolize the money sluice, furthering their own

enrichment while refusing to fund legitimate social needs on the grounds of not being able to pay, that's no democracy: it's an oligarchy.

Money is Finite? *Nope*

In historic times, money has sometimes been associated with a physical commodity, typically gold or silver. Governments or private parties have agreed to exchange money for the commodity at some fixed rate. Under this condition of convertability, the amount of money that could be safely issued in a society was capped by the amount of exchangeable commodity available. But nowadays, no society offers convertability of its money to a physical commodity. What we have today is *fiat* money, which means it's backed only by the say-so (“fiat”) of its issuer. Fiat money itself is neither a good nor a service, but it does represent claims on the goods and services available for sale in the society that issues the fiat money.

Although no convertability has been offered for the US dollar since at least 1972, political discourse and economic policy are typically presented as if there was still a physical backing of the money. This matters because a physically-backed money is fundamentally finite, hence subject to genuine scarcity. Fiat money has no physical limit hence its scarcity is a matter of policy not physical necessity. Consider the US dollar, issued by the US Federal Government (USG) operating through the US Treasury and the Federal Reserve. There's no physical limit on money issuance by the USG. A useful corollary to the unlimited nature of fiat money is that the USG can buy anything that's for sale in US dollars. Not that this would be a good idea! But there's no physical limitation preventing this, only policy. *Fiat money is unbounded.*⁵

You might be wondering how it is that a money with no physical backing and no physical limit on its issuance could have value such that people would be willing

⁵ [../money/unbounded.html](#)

to exchange it for goods and services. The answer is also simple: in all modern societies, money gets value because the sovereign requires that taxes and fees be paid in the fiat money. This creates a baseline of demand for the money. If you have to pay taxes, you must obtain sufficient money to make the payments. To obtain that money, you must sell goods or services (or issue debt, if you can). As long as a society has the power to compel tax payments, the money in which those taxes must be paid will have value. *Taxation ensures demand for fiat money.*⁶

⁶ ../money/taxes-drive-money.html

The Government Must Tax or Borrow to Spend?

Unh-unh

There's lots of loose talk⁷ about your taxpayer dollars paying for this and that. That's bunk when applied to the sovereign. The issuer of the money can buy anything that's for sale in the society. It doesn't need to wait around for taxes to get paid. Indeed, the causality is exactly reversed: the government as issuer must spend so that taxes can be paid! *Fiat money is created by government spending.*⁸ When the sovereign pays a subject, the subject gets money which can be used for taxes and as claims against goods and services for sale elsewhere in the society. Money is born. The part that doesn't go for taxes can circulate in exchanges of resources among other subjects.

The flip side to fiat money creation by sovereign spending is destruction of fiat money by taxation. Money dies. *When taxes are paid, fiat money is destroyed.*⁹ Now we have the whole money lifecycle: spent into existence by the sovereign, circulated among the subject parts of society, and eventually extinguished with payment by subjects of taxes, fees, fines, etc.

Let me reiterate: taxes do not fund sovereign spending.¹⁰ Indeed, the sovereign must spend so that taxes can be paid!

⁷ ../money/taxes-do-not-fund-sovereign.html

⁸ ../money/life-cycle.html

⁹ ../money/life-cycle.html

¹⁰ ../money/taxes-do-not-fund-sovereign.html

Most sovereigns, as a policy choice, emulate commodity money by issuing debt to match the difference between sovereign spending and taxation. This sovereign debt is a special asset for subjects. Unlike debt issued by a subject, for which an involuntary default is always a risk, the sovereign issuer of fiat money can never be forced to default. Sovereign default is entirely voluntary and only by policy choice, never by necessity. Because the risk of sovereign default should be nil, sovereign debt is a benchmark asset and fundamental store of financial wealth. Only the most reckless and irresponsible of sovereigns would choose to default on its debt as long as that debt is denominated in its own money.

Although the sovereign *may* issue debt corresponding to the excess of spending over taxation, or in any other amount, it need not do so. Debt issuance is a policy choice. As a practical matter, debt issuance with payment of interest is a subsidy for the wealthiest segments of society. Without interest-bearing sovereign debt, the only financial asset free of default risk would be the non-interest bearing money itself. *The issuance of interest-bearing sovereign debt is a policy choice.*¹¹

¹¹ ../money/sovereign-debt.html

The Government is Like a Household? *Not*

How often have you heard a politician or pundit cite the folk wisdom that their household or business has to balance its budget or be taken in bankruptcy, and the government is (obviously) subject to the same constraint. Not true for sovereigns! The sovereign creates money for subjects by spending, and destroys money in receipt of taxes and fees. It cannot be forced into involuntary bankruptcy. *Bankruptcy for the sovereign is purely a matter of policy.*¹²

Because the sovereign is the issuer of the money, it can only default by choice. Subjects, by contrast, as mere users of the money, can be forced into bankruptcy when their liabilities exceed their assets and they default on debt service payments. At that point, the owners of the liabilities get to use the forces of the state to divvy up whatever assets can be confiscated from the defaulter. Can't happen to the sovereign, except by its own choice.

Not all governments are sovereign. National governments can cede their sovereignty. The member nations of the Eurozone have given up their monetary sovereignty to the union, which is basically a banking consortium. That's what permits the spectacle of Greece breaking on the austerity rack, having ceded its sovereignty to the dour banksters of the Eurozone. Less drastically, some potentially sovereign nations have at times chosen as a matter of policy to attempt to peg their currency to some other sovereign's currency by fixing exchange rates.

A non-sovereign government must borrow from banks or other investors when its tax revenues fall short of its expenditures. Over the long run, without the support of sovereign issuance, non-sovereign governments can only grow their money

¹² [../money/sovereign-bankruptcy.html](http://money/sovereign-bankruptcy.html)

supply by running persistent trade surpluses. But few nations can manage that, since one nation's surplus is another's deficit. In a world of balanced national budgets, economic stagnation and trade war are the consequences to anticipate.

US state and local governments are subjects, although in historic times, states in the USA have been currency sovereigns. Today, all non-federal governments in the USA are subjects. Hence, they could be forced into bankruptcy and be involuntarily deprived of their assets. A contemporary example is Puerto Rico, which has recently defaulted on its borrowings, and will soon be subject to banker-mandated austerity with higher taxes and reduced services, along with seizure of public assets for transfer to private creditors. Of course, the sovereign US government could readily bail out its colony, as the debts are denominated in US dollars, of which there is unlimited supply. Whoops! They're not bankers, so no bailout! Detroit got whacked a few years ago. Illinois may be next. In the fullness of time, barring significant policy changes, I expect many if not most non-federal governments in the USA to be subject to bankruptcy and hence subject to looting by creditors.

The sovereign is the issuer of fiat money. There's no physical limitation on issuance. Subjects are users of fiat money and can only obtain money from payments by others. *Only subjects, never the sovereign, can be forced into involuntary bankruptcy and suffer the seizure of their assets.*¹³ When you hear a pundit or politician equate the US federal government to a household or any other subject, up to and including countries like Greece, ask yourself: ignorant or lying?

¹³ ../money/subject-bankruptcy.html

The National Debt is a Problem? *Negatory*

Only rarely will the payment of taxes exactly match the spending of the sovereign. Typically the spending exceeds the taxes, which is handy, since the excess of spending over taxes is the net amount of money sloshing around in the society for the use of all the subjects! Usually the excess of spending over taxes is called “the deficit” in reference to a specific period, or “the national debt” to refer to the total accumulation of spending in excess of taxation.

The US constrains itself to issue debt to correspond to the excess of spending over taxes. This is a policy choice, not a law of nature. The US further constrains itself by placing a limit on the accumulated excess of spending over taxes: the “debt ceiling.” These are purely matters of policy, not necessity. There’s no necessity for the USG to issue debt to match the excess of spending over taxation. There’s no necessity for the USG to cap the total amount of debt issued. Indeed, it’s a terrible idea, unless you happen to enjoy the periodic theatrical posturing of politicians threatening to upend the fundamental underpinnings of society’s financial wealth. *The national debt is the only component of subject financial wealth which is free of involuntary default risk.*¹⁴ We might do better to call “the national savings.”

¹⁴ ../money/national-wealth.html

Full Employment Drives Inflation? *Uh, No*

A sovereign that wishes to provide full employment need only facilitate the offer of paid work at a basic wage to any citizen who seeks employment. While the details of such a job guarantee are challenging, the principle is quite straightforward. *Full employment is a policy choice.*¹⁵ A job guarantee would set a floor on wages. Workers who lack appreciation for the glories of profit-seeking would benefit from much wider options for employment in public service, paid for by the sovereign. Everyone could have the satisfaction of participating in recognizably useful activity. Private employers might even have to compete for workers by offering training, better wages, and improved conditions compared to those of guaranteed employment. By setting the basic wage higher, wages could be boosted throughout the economy.

The spectre of inflation is frequently invoked to derail discussions of policies that tend towards full employment and hence the prospect of empowering workers to demand higher wages and better working conditions. Elders may still remember the 1970s when inflation and slow growth in the economy flummoxed economists and paved the way for the onset of neoliberalism. The European Monetary Union is perpetually haunted by the ghosts of hyperinflation in the Weimar republic of 1930s Germany. So we need to ask what causes inflation, what are the tools for dealing with it when it arises, and who benefits and who pays.

When there is actual scarcity, due to causes external to the monetary system, e.g. natural disasters or war, with consequent loss of productive capacity, it's common for prices to rise in response to shortages. This might be the closest thing to an actual law of economics. Policy for dealing with genuine shortages should use

¹⁵ [../money/full-employment.html](http://money/full-employment.html)

the collective resources of society to address the specific basis for the shortages, and to ameliorate the harms caused by the shortages. *Genuine scarcity makes real inflation.*¹⁶

In the absence of external forces acting on an economy, inflation is an indication that more money is circulating than is warranted by the current productive capacity of the economy. The proper tool for reducing excess money in circulation is taxation: raise taxes to drain demand from the economy. Taxation has the further potential of reallocating resources away from segments of the population and towards other segments. Keeping the wealthy segments of the society from concentrating enough wealth to corrupt public institutions is a pretty strong argument for confiscatory taxes on high incomes and large accumulations of wealth, such as we had during the closest thing to a golden era in recent US history: the postwar years of boomer youth. Failure to raise taxes under inflationary conditions which are not externally driven is a failure of policy. *In the absence of scarcity, inflation is a policy choice to fail to adequately raise taxes.*¹⁷

When wages are rising relative to prices, employer's profits are threatened. They may choose to raise prices to try to pass on the wage increase to their customers, or they must reduce their profit margins. Thus rising wages under stable prices is a policy for income redistribution away from profits and towards wages. But how to prevent employers passing on wage increases in prices? Taxes on profits could be raised considerably to counteract the inflationary potential. The degree of redistribution would be configurable with adjustment of the basic wage and the tax on profits. *Distribution of income in the economy between profits and wages*

¹⁶ ../money/inflation.html

¹⁷ ../money/inflation.html

*is a policy choice.*¹⁸ We could have a prosperous and secure middle class again in the US if we make the right policy choices.

Consider also the premise that inflation is always bad. Let's recall who are the beneficiaries of inflation, and who is harmed. When inflation comes on, debtors find their debts reduced in real terms, since the money they owe is worth less than it was when the debt issued. Creditors suffer the loss. A brief, sharp burst of inflation in a time of full employment and rising real wages would be greeted enthusiastically by debt-shackled workers. *Inflation can redistribute wealth from creditor to debtor.*¹⁹

Let's not overlook the converse to inflation: deflation. When prices and wages are falling due to a shortage of money, that's deflation. Deflation works opposite to inflation in transferring wealth from debtor to creditor. A debtor must repay debts in money more valuable (more scarce) than that in which the debt was issued. The illusion of scarcity of fiat money thus benefits creditors at the expense of debtors. That may explain why so many pixels are lit in support of that illusion.

¹⁸ ../money/income-distribution.html

¹⁹ ../money/wealth-redistribution.html

Banks Lend Deposits? *Naah*

Recall the lifecycle of fiat money: created when the government makes payments to subjects. Circulating among subjects in transactions exchanging money for resources in the society. Destroyed when taxes, etc. are paid to the sovereign. The residual of creation (spending) over destruction (taxation) providing the only financial asset free of default risk, hence the bedrock of private wealth.

Now consider private banks. Like the sovereign, banks create money, but banks *loan* money into existence, while the sovereign spawns money by *spending*. The distinction is important. The sovereign can never involuntarily default on its obligations in its own currency as fiat money is unbounded. But the parties to which a bank lends can and do default. Upon such defaults are financial panics made! Moreover, the lack of oversight with which banks operate and the amazing power of money creation creates a dangerously crimogenic environment.²⁰

When a bank makes a loan, it simultaneously creates an asset and a liability on its balance sheet. The asset is the promise of the borrower to repay the loan, with interest (which will provide revenue and eventually profit to the bank). The liability is effectively a deposit made to the credit of the borrower which is money the borrower may use to claim salable resources of society. Money is created for use by the borrower, subject to a promise to repay by the borrower. This is money creation by a private institution. *Loans create deposits.*²¹ Note also that the money created by the loan issuance is destroyed as the loan is repaid: the asset and the liability both shrink with each repayment of the loan principal.

²⁰ ../money/banksters.html

²¹ ../money/unelected-sovereigns.html

As with so many other monetary events, the conventional wisdom is inverted from the reality. We are told to think²² of banks as taking deposits from savers and investing the savings in loans to borrowers. While it is true that banks take deposits, those play very little role in the issuance of loans. The decision to issue a loan has mainly to do with the banker's perceptions of the credit-worthiness and business prospects of the potential borrower and the value of any underlying collateral, which the bank may seize in the event of default by the borrower. Deposits are liabilities of the bank; they are promises by the bank to repay the depositor. When banks fail, those promises may go unfulfilled.²³

Banks are subject to a lax regulatory regime in which they are required to maintain a modest cushion of equity capital as a safeguard against their own insolvency when their money creation goes wrong, but that equity cushion is typically a mere five or ten percent of their overall balance sheet, or even less. It doesn't take much to overrun that sliver, and that's what's happened so many times in history when banking panics have ensued with realizations that the assets of a bank (the loans it has issued) are dramatically mispriced in light of defaulting borrowers and overvalued collateral. Curious readers might want to explore the notion of the Minsky moment²⁴ when lenders to banks (depositors, bond holders, etc.) suddenly and catastrophically perceive the likely insolvency of the banking system.

What I will emphasize pertaining to policy alternatives in a democracy is the private, undemocratic nature of money creation by banks. Unlike the sovereign, which is at least nominally subject to the will of its citizens, banks exercise sovereignty — the creation of claims on society's resources — but are not directly

²² [../gobat-imf-banking.html](#)

²³ [../money/bail-ins.html](#)

²⁴ [../money/minsky-moment.html](#)

subject to much in the way of social control. Consider the possibility that it's banks that control society, and not the other way around! All this is possible because the power to create money is the power to commandeer any salable resource in the society, and that includes the direct and indirect purchase of corrupt politicians, media, and so-called public servants (beaureacrats, administrators, regulators, etc.). *Bankers are unelected sovereigns who create money by issuing loans entirely at their own discretion with the only the slightest oversight by the rest of society.*²⁵

²⁵ [../money/unelected-sovereigns.html](#)

We Can't Afford This, That, or the Other? *Utterly Untrue*

Some things are truly scarce. Material things are limited in quantity. Labor is limited by the size and skills of the workforce. But where the labor and the material inputs are available, only policy choices are preventing us from having something desirable. Many of the things we would like are services and hence not very demanding of material resources but requiring labor: people serving people. Care services. These could be universally supplied at no cost to all members of the society, given the political will. The sovereign can choose pay for these things. *Artificial scarcity is a policy choice.*²⁶

What kind of society do we want to live in? That's the question we should be asking. The answer could include things like universal provisioning of free or low cost healthcare, higher education, and care for pre-schoolers and the elderly. We could have full employment, living wages, generous pensions, secure childhood and old age. Ample, well-maintained public spaces. Clean, efficient, inexpensive public transportation. We can have all those services, by choosing to have the sovereign pay for them, if we can organize ourselves to provide them. We may lack the political will, the moral integrity, or possibly the material means to provide these services. But we will *never lack the ability to pay*²⁷ as long as we have fiat money.

²⁶ [../money/austerity.html](#)

²⁷ [../money/affording-what-we-want.html](#)

Enough with the Lies!

Is money complicated? No. Quite simply, money is a claim on society.²⁸ More particularly, a claim on the salable resources of the society that issues it. Society creates (and destroys) money and gives it worth. Money is social.

Is fiat money finite? No. Fiat money is unbounded.²⁹ Money gets value from taxation,³⁰ not scarcity. Lack of money, i.e. austerity, is a policy choice.³¹

Must the government tax or borrow to spend? No. Money is created by sovereign spending.³² Money is destroyed when taxes are paid to the sovereign.³³ The issuance of interest-bearing sovereign debt is a policy choice.³⁴

Is the government like a household? No. The sovereign is not a subject. Only subjects, never the sovereign, can be forced into involuntary bankruptcy³⁵ and suffer the seizure of their assets. Sovereign bankruptcy is a policy choice.³⁶

²⁸ ../money/claim-on-society.html

²⁹ ../money/unbounded.html

³⁰ ../money/taxes-drive-money.html

³¹ ../money/austerity.html

³² ../money/life-cycle.html

³³ ../money/life-cycle.html

³⁴ ../money/sovereign-debt.html

³⁵ ../money/subject-bankruptcy.html

³⁶ ../money/sovereign-bankruptcy.html

Is the national debt is a problem? No. The national debt is the only component of subject financial wealth which is free of involuntary default risk. We could just as well call it the national savings.³⁷

Does full employment drive inflation? No. Full employment is a policy choice.³⁸ Only genuine scarcity makes real inflation. Absent scarcity, inflation is a policy choice³⁹ to fail to adequately raise taxes. Distribution of income between profits and wages is a policy choice.⁴⁰ Inflation, as policy, redistributes wealth⁴¹ from creditor to debtor. Deflation, as policy, redistributes wealth form debtor to creditor.

Do banks intermediate between savers and borrowers? No. Bankers are unelected sovereigns⁴² who create money by issuing loans at their own discretion with only the slightest oversight by the rest of society.

Can we afford the things we want as a society? Yes! Artificial scarcity due to “lack of funds” is purely a policy choice. If society has the resources in labor, material, and willpower, lack of money is never an obstacle.⁴³

³⁷ ../money/national-wealth.html

³⁸ ../money/full-employment.html

³⁹ ../money/inflation.html

⁴⁰ ../money/income-distribution.html

⁴¹ ../money/wealth-redistribution.html

⁴² ../money/unelected-sovereigns.html

⁴³ ../money/affording-what-we-want.html