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The Principle of Sound Money

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The Classical Idea of Sound Money

The principle of sound money that guided nineteenth-century monetary doctrines and policies was a product of classical political economy. It was an essential part of the liberal program as developed by eighteenth-century social philosophy and propagated in the following century by the most influential political parties of Europe and America.

The liberal doctrine sees in the market economy the best, even the only possible, system of economic organization of society. Private ownership of the means of production tends to shift control of production to the hands of those best fitted for this job and thus to secure for all members of society the fullest possible satisfaction of their needs. It assigns to the consumers the power to choose those purveyors who supply them in the cheapest way with the articles they are most urgently asking for and thus subjects the entrepreneurs and the owners of the means of production, namely, the capitalists and the landowners, to the sovereignty of the buying public. It makes nations and their citizens free and provides ample sustenance for a steadily increasing population.

As a system of peaceful cooperation under the division of labor, the market economy could not work without an institution warranting to its members protection against domestic gangsters and external foes. Violent aggression can be thwarted only by armed resistance and repression. Society needs an apparatus of defense, a state, a government, a police power. Its undisturbed functioning must be safeguarded by continuous preparedness to repel aggressors. But then a new danger springs up. How keep under control the men entrusted with the handling of the government apparatus lest they turn their weapons against those whom they were expected to serve? The main political problem is how to prevent the rulers from becoming despots and enslaving the citizenry. Defense of the individual's liberty against the encroachment of tyrannical governments is the essential theme of the history of Western civilization. The characteristic feature of the Occident is its peoples' pursuit of liberty, a concern unknown to Orientals. All the marvelous achievements of Western civilization are fruits grown on the tree of liberty.

It is impossible to grasp the meaning of the idea of sound money if one does not realize that it was devised as an instrument for the protection of civil liberties against despotic inroads on the part of governments. Ideologically it belongs in the same class with political constitutions and bills of rights. The demand for constitutional guarantees and for bills of rights was a reaction against arbitrary rule and the nonobservance of old customs by kings. The postulate of sound money was first brought up as a response to the princely practice of debasing the coinage. It was later carefully elaborated and perfected in the age which — through the experience of the American continental currency, the paper money of the French Revolution and the British restriction period — had learned what a government can do to a nation's currency system.

Modern cryptodespotism, which arrogates to itself the name of liberalism, finds fault with the negativity of the concept of freedom. The censure is spurious as it refers merely to the grammatical form of the idea and does not comprehend that all civil rights can be as well defined in affirmative as in negative terms. They are negative as they are designed to obviate an evil, namely omnipotence of the police power, and to prevent the state from becoming totalitarian. They are affirmative as they are designed to preserve the smooth operation of the system of private property, the only social system that has brought about what is called civilization.

Thus the sound-money principle has two aspects. It is affirmative in approving the market's choice of a commonly used medium of exchange. It is negative in obstructing the government's propensity to meddle with the currency system.

The sound-money principle was derived not so much from the Classical economists' analysis of the market phenomena as from their interpretation of historical experience. It was an experience that could be perceived by a much larger public than the narrow circles of those conversant with economic theory. Hence the sound-money idea became one of the most popular points of the liberal program. Friends and foes of liberalism considered it one of the essential postulates of a liberal policy.

Sound money meant a metallic standard. Standard coins should be in fact a definite quantity of the standard metal as precisely determined by the law of the country. Only standard coins should have unlimited legal-tender quality. Token coins and all kinds of moneylike paper should be, on presentation and without delay, redeemed in lawful standard money.

So far there was unanimity among the supporters of sound money. But then the battle of the standards arose. The defeat of those favoring silver and the unfeasibility of bimetallism eventually made the sound-money principle mean the gold standard. At the end of the nineteenth century there was all over the world unanimity among businessmen and statesmen with regard to the indispensability of the gold standard. Countries which were under a fiat-money system or under the silver standard considered adoption of the gold standard the foremost goal of their economic policy. Those who disputed the eminence of the gold standard were dismissed as cranks by the representatives of the official doctrine — professors, bankers, statesmen, editors of the great newspapers and magazines.

It was a serious blunder of the supporters of sound money to adopt such tactics. There is no use in dealing in a summary way with any ideology however foolish and contradictory it may appear. Even a manifestly erroneous doctrine should be refuted by careful analysis and the unmasking of the fallacies implied. A sound doctrine can win only by exploding the delusions of its adversaries.

The essential principles of the sound-money doctrine were and are impregnable. But their scientific support in the last decades of the nineteenth century was rather shaky. The attempts to demonstrate their reasonableness from the point of view of the Classical value theory were not very convincing and made no sense at all when this value concept had to be discarded. But the champions of the new value theory for almost half a century restricted their studies to the problems of direct exchange and left the treatment of money and banking to routinists unfamiliar with economics. There were treatises on catallactics which dealt only incidentally and cursorily with monetary matters, and there were books on currency and banking which did not even attempt to integrate their subject into the structure of a catallactic system.[1] Finally the idea evolved that the modern doctrine of value, the subjectivist or marginal utility doctrine, is unable to explain the problems of money's purchasing power.[2]

It is easy to comprehend how under such circumstances even the least tenable objections raised by the advocates of inflationism remained unanswered. The gold standard lost popularity because for a very long time no serious attempts were made to demonstrate its merits and to explode the tenets of its adversaries.

The Virtues and Alleged Shortcomings of the Gold Standard

The excellence of the gold standard is to be seen in the fact that it renders the determination of the monetary unit's purchasing power independent of the policies of governments and political parties. Furthermore, it prevents rulers from eluding the financial and budgetary prerogatives of the representative assemblies. Parliamentary control of finances works only if the government is not in a position to provide for unauthorized expenditures by increasing the circulating amount of fiat money. Viewed in this light, the gold standard appears as an indispensable implement of the body of constitutional guarantees that make the system of representative government function.

When in the 'fifties of the nineteenth century gold production increased considerably in California and Australia, people attacked the gold standard as inflationary. In those days Michel Chevalier, in his book *Probable Depreciation of Gold*, recommended the abandonment of the gold standard, and Béranger dealt with the same subject in one of his poems. But later these criticisms subsided. The gold standard was no longer denounced as inflationary but on the contrary as deflationary. Even the most fanatical champions of inflation like to disguise their true intentions by declaring that they merely want to offset the contractionist pressure which the allegedly insufficient supply of gold tends to produce.

Yet it is clear that over the last generations there has prevailed a tendency of all commodity prices and wage rates to rise. We may neglect dealing with the economic effects of a general tendency of money prices and money wages to drop.[3] For there is no doubt that what we have experienced over the last hundred years was just the opposite, namely, a secular tendency toward a drop in the monetary unit's purchasing power, which was only temporarily interrupted by the aftermath of the breakdown of a boom intentionally created by credit expansion. Gold became cheaper in terms of commodities, not dearer. What the foes of the gold standard are asking for is not to reverse a prevailing tendency in the determination of prices, but to intensify very considerably the already prevailing upward trend of prices and wages. They simply want to lower the monetary unit's purchasing power at an accelerated pace.

Such a policy of radical inflationism is, of course, extremely popular. But its popularity is to a great extent due to a misapprehension of its effects. What people are really asking for is a rise in the prices of those commodities and services they are selling while the prices of those commodities and services which they are buying remain unchanged. The potato grower aims at higher prices for potatoes. He does not long for a rise in other prices. He is injured if these other prices rise sooner or in greater proportion than the price of potatoes. If a politician addressing a meeting declares that the government should adopt a policy which makes prices rise, his hearers are likely to applaud. Yet each of them is thinking of a different price rise.

From time immemorial inflation has been recommended as a means to alleviate the burdens of poor worthy debtors at the expense of rich harsh creditors. However, under capitalism the typical debtors are not the poor but the well-to-do owners of real estate, of firms, and of common stock, people who have borrowed from banks, savings banks, insurance companies, and bondholders. The typical creditors are not the rich but people of modest means who own bonds and savings accounts or have taken out insurance policies. If the common man supports anti-creditor measures, he does it because he ignores the fact that he himself is a creditor. The idea that millionaires are the victims of an easy-money policy is an atavistic remnant.

For the naive mind there is something miraculous in the issuance of fiat money. A magic word spoken by the government creates out of nothing a thing which can be exchanged against any merchandise a man would like to get. How pale is the art of sorcerers, witches, and conjurors when compared with that of the government's Treasury Department! The government, professors tell us, "can raise all the money it needs by printing it."[4] Taxes for revenue, announced a chairman of the Federal Reserve Bank of New York, are "obsolete."[5] How wonderful! And how malicious and misanthropic are those stubborn supporters of outdated economic orthodoxy who ask governments to balance their budgets by covering all expenditures out of tax revenue!

These enthusiasts do not see that the working of inflation is conditioned by the ignorance of the public and that inflation ceases to work as soon as the many become aware of its effects upon the monetary unit's purchasing power. In normal times, that is in periods in which the government does not tamper with the monetary standard, people do not bother about monetary problems. Quite naively they take it for granted that the monetary unit's purchasing power is "stable." They pay attention to changes occurring in the money prices of the various commodities. They know very well that the exchange ratios between different commodities vary. But they are not conscious of the fact that the exchange ratio between money on the one side and all commodities and services on the other side is variable too. When the inevitable consequences of inflation appear and prices soar, they think that commodities are becoming dearer and fail to see that money is getting cheaper. In the early stages of an inflation only a few people discern what is going on, manage their business affairs in accordance with this insight, and deliberately aim at reaping inflation gains. The overwhelming majority are too dull to grasp a correct interpretation of the situation. They go on in the routine they acquired in non-inflationary periods. Filled with indignation, they attack those who are quicker to apprehend the real causes of the agitation of the market as "profiteers" and lay the blame for their own plight on them. This ignorance of the public is the indispensable basis of the inflationary policy. Inflation works as long as the housewife thinks: "I need a new frying pan badly. But prices are too high today; I shall wait until they drop again." It comes to an abrupt end when people discover that the inflation will continue, that it causes the rise in prices, and that therefore prices will skyrocket infinitely. The critical stage begins when the housewife thinks: "I don't need a new frying pan today; I may need one in a year or two. But I'll buy it today because it will be much more expensive later." Then the catastrophic end of the inflation is close. In its last stage the housewife thinks: "I don't need another table; I shall never need one. But it's wiser to buy a table than keep these scraps of paper that the government calls money, one minute longer."

Let us leave the problem of whether or not it is advisable to base a system of government finance upon the intentional deception of the immense majority of the citizenry. It is enough to stress the point that such a policy of deceit is self-defeating. Here the famous dictum of Lincoln holds true: You can't fool all of the people all of the time. Eventually the masses come to understand the schemes of their rulers. Then the cleverly concocted plans of inflation collapse. Whatever compliant government economists may have said, inflationism is not a monetary policy that can be considered as an alternative to a sound-money policy. It is at best a temporary expedient. The main problem of an inflationary policy is how to stop it before the masses have seen through their rulers' artifices. It is a display of considerable naivete to recommend openly a monetary system that can work only if its essential features are ignored by the public.

The index-number method is a very crude and imperfect means of "measuring" changes occurring in the monetary unit's purchasing power. As there are in the field of social affairs no constant relations between magnitudes, no measurement is possible and economics can never become quantitative.[6] But the index-number method, notwithstanding its inadequacy, plays an important role in the process which in the course of an inflationary movement makes the people inflation-conscious. Once the use of index numbers becomes common, the government is forced to slow down the pace of the inflation and to make the people believe that the inflationary policy is merely a temporary expedient for the duration of a passing emergency, one that will be stopped before long. While government economists still praise the superiority of inflation as a lasting scheme of monetary management, governments are compelled to exercise restraint in its application.

It is permissible to call a policy of intentional inflation dishonest as the effects sought by its application can be attained only if the government succeeds in deceiving the greater part of the people about the consequences of its policy. Many of the champions of interventionist policies will not scruple greatly about such cheating; in their eyes what the government does can never be wrong. But their lofty moral indifference is at a loss to oppose an objection to the economist's argument against inflation. In the economist's eyes the main issue is not that inflation is morally reprehensible but that it cannot work except when resorted to with great restraint and even then only for a limited period. Hence resort to inflation cannot be considered seriously as an alternative to a permanent standard such as the gold standard is.

The pro-inflationist propaganda emphasizes nowadays the alleged fact that the gold standard collapsed and that it will never be tried again: nations are no longer willing to comply with the rules of the gold-standard game and to bear all the costs which the preservation of the gold standard requires.

First of all there is need to remember that the gold standard did not collapse. Governments abolished it in order to pave the way for inflation. The whole grim apparatus of oppression and coercion — policemen, customs guards, penal courts, prisons, in some countries even executioners — had to be put into action in order to destroy the gold standard. Solemn pledges were broken, retroactive laws were promulgated, provisions of constitutions and bills of rights were openly defied. And hosts of servile writers praised what the governments had done and hailed the dawn of the fiat-money millennium.

The most remarkable thing about this allegedly new monetary policy, however, is its complete failure. True, it substituted fiat money in the domestic markets for sound money and favored the material interests of some individuals and groups of individuals at the expense of others. It furthermore contributed considerably to the disintegration of the international division of labor. But it did not succeed in eliminating gold from its position as the international or world standard. If you glance at the financial page of any newspaper you discover at once that gold is still the world's money and not the variegated products of the diverse government printing offices. These scraps of paper are the more appreciated the more stable their price is in terms of an ounce of gold. Whoever today dares to hint at the possibility that nations may return to a domestic gold standard is cried down as a lunatic. This terrorism may still go on for some time. But the position of gold as the world's standard is impregnable. The policy of "going off the gold standard" did not relieve a country's monetary authorities from the necessity of taking into account the monetary unit's price in terms of gold.

What those authors who speak about the rules of the gold-standard game have in mind is not clear. Of course, it is obvious that the gold standard cannot function satisfactorily if to buy or to sell or to hold gold is illegal, and hosts of judges, constables, and informers are busily enforcing the law. But the gold standard is not a game; it is a market phenomenon and as such a social institution. Its preservation does not depend on the observation of some specific rules. It requires nothing else than that the government abstain from deliberately sabotaging it. To refer to this condition as a rule of an alleged game is no more reasonable than to declare that the preservation of Paul's life depends on compliance with the rules of the Paul's-life game because Paul must die if somebody stabs him to death.

What all the enemies of the gold standard spurn as its main vice is precisely the same thing that in the eyes of the advocates of the gold standard is its main virtue, namely, its incompatibility with a policy of credit expansion. The nucleus of all the effusions of the anti-gold authors and politicians is the expansionist fallacy.

The expansionist doctrine does not realize that interest, that is, the discount of future goods as against present goods, is an originary category of human valuation, actual in any kind of human action and independent of any social institutions. The expansionists do not grasp the fact that there never were and there never can be human beings who attach to an apple available in a year or in a hundred years the same value they attach to an apple available now. In their opinion interest is an impediment to the expansion of production and consequently to human welfare that unjustified institutions have created in order to favor the selfish concerns of money lenders. Interest, they say, is the price people must pay for borrowing. Its height therefore depends on the magnitude of the supply of money. If laws did not artificially restrict the creation of additional money, the rate of interest would drop, ultimately even to zero. The "contractionist" pressure would disappear, there would no longer be a shortage of capital, and it would become possible to execute many business projects which the "restrictionism" of the gold standard obstructs. What is needed to make everyone prosperous is simply to defy "the rules of the gold-standard game," the observance of which is the main source of all our economic ills.

These absurd doctrines greatly impressed ignorant politicians and demagogues when they were blended with nationalist slogans. What prevents our country from fully enjoying the advantages of a low-interest-rate policy, says the economic isolationist, is its adherence to the gold standard. Our central bank is forced to keep its rate of discount at a height that corresponds to conditions on the international money market and to the discount rates of foreign central banks. Otherwise "speculators" would withdraw funds from our country for short-term investment abroad and the resulting outflow of gold would make the gold reserves of our central bank drop below the legal ratio. If our central bank were not obliged to redeem its banknotes in gold, no such withdrawal of gold could occur and there would be no necessity for it to adjust the height of the money rate to the situation of the international money market, dominated by the world-embracing gold monopoly.

The most amazing fact about this argument is that it was raised precisely in debtor countries for which the operation of the international money and capital market meant an inflow of foreign funds and consequently the appearance of a tendency toward a drop in interest rates. It was popular in Germany and still more in Austria in the 1870s and 80s, but it was hardly ever seriously mentioned in those years in England or in the Netherlands, whose banks and bankers lent amply to Germany and Austria. It was advanced in England only after World War I, when Great Britain's position as the world's banking center had been lost.

Of course, the argument itself is untenable. The inevitable eventual failure of any attempt at credit expansion is not caused by the international intertwinement of the lending business. It is the outcome of the fact that it is impossible to substitute fiat money and a bank's circulation credit for non-existing capital goods. Credit expansion initially can produce a boom. But such a boom is bound to end in a slump, in a depression. What bring about the recurrence of periods of economic crises are precisely the reiterated attempts of governments and banks supervised by them to expand credit in order to make business good by cheap interest rates.[7]

The Full-Employment Doctrine

The inflationist or expansionist doctrine is presented in several varieties. But its essential content remains always the same.

The oldest and most naive version is that of the allegedly insufficient supply of money. Business is bad, says the grocer, because my customers or prospective customers do not have enough money to expand their purchases. So far he is right. But when he adds that what is needed to render his business more prosperous is to increase the quantity of money in circulation, he is mistaken. What he really has in mind is an increase of the amount of money in the pockets of his customers and prospective customers while the amount of money in the hands of other people remains unchanged. He asks for a specific kind of inflation; namely, an inflation in which the additional new money first flows into the cash holdings of a definite group of people, his customers, and thus permits him to reap inflation gains. Of course, everybody who advocates inflation does it because he infers that he will belong to those who are favored by the fact that the prices of the commodities and services they sell will rise at an earlier date and to a higher point than the prices of those commodities and services they buy. Nobody advocates an inflation in which he would be on the losing side.

This spurious grocer philosophy was once and for all exploded by Adam Smith and Jean-Baptiste Say. In our day it has been revived by Lord Keynes, and under the name of full-employment policy is one of the basic policies of all governments which are not entirely subject to the Soviets. Yet Keynes was at a loss to advance a tenable argument against Say's law. Nor have his disciples or the hosts of economists, pseudo and other, in the offices of the various governments, the United Nations, and diverse other national or international bureaus done any better. The fallacies implied in the Keynesian full-employment doctrine are, in a new attire, essentially the same errors which Smith and Say long since demolished.

Wage rates are a market phenomenon, are the prices paid for a definite quantity of labor of a definite quality. If a man cannot sell his labor at the price he would like to get for it, he must lower the price he is asking for it or else he remains unemployed. If the government or labor unions fix wage rates at a higher point than the potential rate of the unhampered labor market and if they enforce their minimum-price decree by compulsion and coercion, a part of those who want to find jobs remain unemployed. Such institutional unemployment is the inevitable result of the methods applied by present-day self-styled progressive governments. It is the real outcome of measures falsely labeled pro-labor. There is only one efficacious way toward a rise in real wage rates and an improvement of the standard of living of the wage earners: to increase the per-head quota of capital invested. This is what laissez-faire capitalism brings about to the extent that its operation is not sabotaged by government and labor unions.

We do not need to investigate whether the politicians of our age are aware of these facts. In most universities it is not good form to mention them to the students. Books that are skeptical with regard to the official doctrines are not widely bought by the libraries or used in courses, and consequently publishers are afraid to publish them. Newspapers seldom criticize the popular creed because they fear a boycott on the part of the unions. Thus politicians may be utterly sincere in believing that they have won "social gains" for the "people" and that the spread of unemployment is one of the evils inherent in capitalism and is in no way caused by the policies of which they are boasting. However this may be, it is obvious that the reputation and the prestige of the men who are now ruling the countries outside the Soviet bloc and of their professorial and journalistic allies are so inseparably tied up with the "progressive" doctrine that they must cling to it. If they do not want to forsake their political ambitions, they must stubbornly deny that their own policy tends to make mass unemployment a permanent phenomenon and must try to put on capitalism the blame for the undesired effects of their procedures.

The most characteristic feature of the full-employment doctrine is that it does not provide information about the way in which wage rates are determined on the market. To discuss the height of wage rates is taboo for the "progressives." When they deal with unemployment, they do not refer to wage rates. As they see it, the height of wage rates has nothing to do with unemployment and must never be mentioned in connection with it.

If there are unemployed, says the progressive doctrine, the government must increase the amount of money in circulation until full employment is reached. It is, they say, a serious mistake to call inflation an increase in the quantity of money in circulation effected under these conditions. It is just "full-employment policy."

We may refrain from frowning upon this terminological oddity of the doctrine. The main point is that every increase in the quantity of money in circulation brings about a tendency of prices and wages to rise. If, in spite of the rise of commodity prices, wage rates do not rise at all or if their rise lags sufficiently behind the rise in commodity prices, the number of people unemployed on account of the height of wage rates will drop. But it will drop merely because such a configuration of commodity prices and wage rates means a drop in real wage rates. In order to attain this result it would not have been necessary to embark upon increasing the amount of money in circulation. A reduction in the height of the minimum-wage rates enforced by the government or union pressure would have achieved the same effect without at the same time starting all the other consequences of an inflation.

It is a fact that in some countries in the 1930s, recourse to inflation was not immediately followed by a rise in the height of money wage rates as fixed by the governments or unions, that this was tantamount to a drop in real wage rates, and that consequently the number of unemployed decreased. But this was merely a passing phenomenon. When in 1936 Lord Keynes declared that a movement of employers to revise money-wage bargains downward would be much more strongly resisted than a gradual and "automatic" lowering of real wage rates as a result of rising prices,[8] he had already been outdated and refuted by the march of events. The masses had already begun to see through the artifices of inflation. Problems of purchasing power and index numbers became an important issue in the unions' dealings with wage rates. The full-employment argument in favor of inflation was already behind the times at the very moment when Keynes and his followers proclaimed it as the fundamental principle of progressive economic policies.

The Emergency Argument in Favor of Inflation

All the economic arguments in favor of inflation are untenable. The fallacies have long since been exploded in an irrefutable way.

There is, however, a political argument in favor of inflation that requires special analysis. This political argument is only rarely resorted to in books, articles, and political speeches. It does not lend itself to such public treatment. But the underlying idea plays an important role in the thinking of statesmen and historians.

Its supporters fully accept all the teachings of the sound-money doctrine. They do not share the errors of the inflationist quacks. They realize that inflationism is a self-defeating policy which must inevitably lead to an economic cataclysm and that all its allegedly beneficial effects are, even from the point of view of the authors of the inflationary policy, more undesirable than the evils which were to be cured by inflation. In full awareness of all this, however, they still believe that there are emergencies which peremptorily require or at least justify recourse to inflation. A nation, they say, can be menaced by evils which are incomparably more disastrous than the effects of inflation. If it is possible to avoid the total annihilation of a nation's freedom and culture by a temporary abandonment of sound money, no reasonable objection can be raised against such a procedure. It would simply mean preferring a smaller evil to a greater one.

In order to appraise correctly the weight of this emergency argument in favor of inflation, there is need to realize that inflation does not add anything to a nation's power of resistance, either to its material resources or to its spiritual and moral strength. Whether there is inflation or not, the material equipment required by the armed forces must be provided out of the available means by restricting consumption for non-vital purposes, by intensifying production in order to increase output, and by consuming a part of the capital previously accumulated. All these things can be done if the majority of citizens are firmly resolved to offer resistance to the best of their abilities and are prepared to make such sacrifices for the sake of preserving their independence and culture. Then the legislature will adopt fiscal methods which warrant the achievement of these goals. They will attain what is called economic mobilization or a defense economy without tampering with the monetary system. The great emergency can be dealt with without recourse to inflation.

But the situation those advocating emergency inflation have in mind is of a quite different character. Its characteristic feature is an irreconcilable antagonism between the opinions of the government and those of the majority of the people. The government, in this regard supported by only a minority of the people, believes that there exists an emergency that necessitates a considerable increase in public expenditure and a corresponding austerity in private households. But the majority of the people disagree. They do not believe that conditions are so bad as the government depicts them or they think that the preservation of the values endangered is not worth the sacrifices they would have to make. There is no need to raise the question whether the government's or the majority's opinion is right. Perhaps the government is right. However, we deal not with the substance of the conflict but with the methods chosen by the rulers for its solution. They reject the democratic way of persuading the majority. They arrogate to themselves the power and the moral right to circumvent the will of the people. They are eager to win its cooperation by deceiving the public about the costs involved in the measures suggested. While seemingly complying with the constitutional procedures of representative government, their conduct is in effect not that of elected officeholders but that of guardians of the people. The elected executive no longer deems himself the people's mandatory; he turns into a führer.

The emergency that brings about inflation is this: the people or the majority of the people are not prepared to defray the costs incurred by their rulers' policies. They support these policies only to the extent that they believe their conduct does not burden themselves. They vote, for instance, only for such taxes as are to be paid by other people, namely, the rich, because they think that these taxes do not impair their own material well-being. The reaction of the government to this attitude of the nation is, at least sometimes, directed by the sincere wish to serve what it believes to be the true interests of the people in the best possible way. But if the government resorts for this purpose to inflation, it is employing methods which are contrary to the principles of representative government, although formally it may have fully complied with the letter of the constitution. It is taking advantage of the masses' ignorance, it is cheating the voters instead of trying to convince them.

It is not just an accident that in our age inflation has become the accepted method of monetary management. Inflation is the fiscal complement of statism and arbitrary government. It is a cog in the complex of policies and institutions which gradually lead toward totalitarianism.

Western liberty cannot hold its ground against the onslaughts of Oriental slavery if the peoples do not realize what is at stake and are not ready to make the greatest sacrifices for the ideals of their civilization. Recourse to inflation may provide the government with the funds which it could neither collect by taxation nor borrow from the savings of the public because the people and its parliamentary representatives objected. Spending the newly created fiat money, the government can buy the equipment the armed forces need. But a nation reluctant to make the material sacrifices necessary for victory will never display the requisite mental energy. What warrants success in a fight for freedom and civilization is not merely material equipment but first of all the spirit that animates those handling the weapons. This heroic spirit cannot be bought by inflation.

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1. See Mises, *Human Action* (New Haven: Yale University Press, 1949), pp. 204-6.
2. See pp. 117-123 [7] above.
3. About this problem, see *Human Action*, pp. 463-68.
4. See A. B. Lerner, *The Economics of Control* (New York, 1944), pp. 307-8.
5. See B. Ruml, "Taxes for Revenue Are Obsolete," *American Affairs* 8 (1946): 35-36.
6. See pp. 187-194 [8] above; *Human Action*, pp. 55-57, 347-49.
7. Part 3 of this book is entirely devoted to the exposition of the trade-cycle theory, the doctrine that is called the monetary-or circulation-credit theory, sometimes also the Austrian theory. See also *Human Action*, pp. 535-83, 787-94.
8. See Keynes, *The General Theory of Employment, Interest and Money* (London, 1936), p. 264.

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