

The history of money

How inflation makes people poor and the Cantillon effect leads to an unfair distribution of money

The story of money is a captivating narrative that spans millennia, reflecting the evolution of human societies and their methods of exchanging value. From rudimentary barter systems to the sophisticated digital currencies of today, the journey has been marked by both progress and persistent challenges. This chapter delves into this fascinating history, exploring the transition from tangible commodities to fiat money, the insidious effects of inflation and the Cantillon effect, and the potential of Bitcoin to reshape the financial landscape.

Former Civilisation

In the earliest human communities, money as we understand it today was absent. Instead, people relied on direct exchange, using readily available goods as a medium of value transfer. Livestock, grain, and even seashells served as both a unit of account and a means of payment. These objects possessed intrinsic value, being useful in themselves, and were widely accepted within communities. A farmer might trade a cow for a certain amount of grain, or a fisherman might exchange fish for tools. However, this system of barter was often cumbersome and inefficient. It required a "double coincidence of wants," meaning that each party had to possess what the other desired. Furthermore, the divisibility and portability of these goods could be problematic. Trading a live animal for smaller items, for example, presented

significant logistical hurdles. This inherent impracticality spurred the search for more convenient and universally accepted forms of currency.

The Goldstandard

As societies evolved, so too did their monetary systems. Precious metals, particularly gold and silver, emerged as favored mediums of exchange. These metals possessed desirable qualities: they were durable, easily divisible, portable, and relatively scarce, giving them inherent value. Coins made from these metals were minted and became widely accepted as a standardized form of currency. This facilitated trade across greater distances and supported the growth of more complex economies. Later, paper money came into circulation, initially backed by gold reserves held by governments or central banks. This meant that each unit of paper currency could be exchanged for a specific amount of gold. The gold standard provided a sense of stability and discipline, limiting the ability of governments to inflate the money supply. It also streamlined large-value transactions, making them more secure and efficient.

Inflation and it's effects

A significant turning point in monetary history occurred in 1971 with the collapse of the Bretton Woods system and the subsequent abandonment of the gold standard. This marked the transition to a system of fiat money. Fiat money, unlike commodity-backed currencies, has no intrinsic value. Its value is derived solely from the trust placed in the issuing authority, typically a government. This shift gave governments greater control over monetary policy, enabling them to manage economic cycles and respond to crises.

However, it also introduced the risk of inflation. Inflation, defined as a sustained increase in the general price level of goods and services, erodes purchasing power. As the money supply increases, the value of each unit of currency decreases, meaning that the same amount of money buys fewer goods and services. High inflation can destabilize economies, creating uncertainty, discouraging investment, and harming long-term economic growth.

The Cantillon effect

A crucial, often overlooked, aspect of modern monetary policy is the Cantillon effect. This effect describes the uneven distribution of newly created money throughout society. When new money enters the economy, it doesn't reach everyone simultaneously. Those closest to the source of the new money, typically banks and governments, benefit first. They can purchase goods and assets at pre-inflation prices. As the new money gradually circulates through the economy, prices begin to rise. Those further removed from the initial distribution, often ordinary citizens and wage earners, experience the effects of inflation before they have had a chance to benefit from the new money, effectively reducing their real income and exacerbating economic inequality. The Cantillon effect highlights the inherent unfairness of inflationary monetary policies.

Bitcoin as a solution

Bitcoin, a decentralized digital currency, presents itself as a potential alternative to the traditional fiat monetary system and a possible solution to the problems posed by the Cantillon effect. With a fixed supply of 21 million units, Bitcoin aims to address the inflationary tendencies of fiat currencies. Its decentralized nature, governed by a transparent and predictable algorithm, ensures that no single entity can control its creation or distribution. This limited supply and decentralized governance aim to mitigate the risk of inflation and reduce the impact of the Cantillon effect, potentially leading to a more equitable distribution of wealth. While Bitcoin's role in the global financial system is still evolving, its underlying principles offer a compelling vision for a more just and stable financial future. It offers a potential pathway towards greater financial autonomy and a more level playing field for individuals in the global economy.



IF INFLATION FALLS, IT DOES NOT MEAN THAT PRICES WILL BECOME CHEAPER, IT
MEANS ONLY THAT PRICES WILL RISE LESS SHARPLY.