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The Economic Implications of Family Breakdown 3
Economic Flexibility 8
Why Schools Should Teach Young People about Personal Finance 17
Japan – Succeeding in Reflation by the Back Door 22
Inflation – Coming Back with a Vengeance? 25
Doing Business with the Japanese 26
The Credit and State Theories of Money 29
Past Economic Research Council Publications 36

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THE ECONOMIC IMPLICATIONS OF FAMILY BREAKDOWN

*Extracts from a talk given by Patricia Morgan, Senior Research Fellow at The Institute for the Study of Civil Society, to members of the Economic Research Council on Tuesday 3rd February 2004.**

Success in life may be measured for adults in terms of longevity, mental and physical health and in wealth creation, and, for their offspring in terms of their educational achievement, their avoidance of criminal or psychiatric trouble and their ability to become gainfully employed. There is now a plethora of evidence to demonstrate that married people overall, and their offspring, are consistently better off in these terms, compared to single adults and the children of one parent families.

Lone parenting

Though there are some important caveats, we can say that a child with a lone parent is far more likely to be poor than one with two parents. Because of the nature of childrearing, it seems obvious why this should be so. One parent cannot perform all parenting functions and provision the family at the same time – which is why all human societies have had marriage. Young single UK mothers (before age 23) are particularly likely to be in receipt of means tested benefits and, a decade later, to be in social housing, lack qualifications and have poor health. Even though the income of such mothers is doubled when they find employment their income is still lower than that of one-earner couples. Divorced mothers are little better off as the absent father is unlikely to contribute as much as when he lives with his children.

Around 50% of lone parents have no job so can the situation be improved by providing job training and encouragement to work? Unfortunately however, the sole parent is benefit dependent in as well as out of work and so costs tend simply to be shifted from income support programmes to tax credit programmes, from out of work to in work benefits. Instead of being housewife and full-time mother in relation to the subsidising state, the

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* During this talk, appropriate references were made to research material and these will be included in the forthcoming Economic Research Council Research paper 'Family Breakdown; Economic Implications' (working title), written by the speaker.

single mother becomes a secondary or supplementary earner to this primary provider. And high quality, low cost childcare is a contradiction in terms:

Today, the average lone parent with two children receives over 60% of their income from child contingency support, is 12 times more likely than couples to be receiving income support and is 6 times more likely to be receiving housing benefit and council tax benefit. Hence, the social security system – initially originated as a defence against want – has come to shoulder primary long term responsibility for large numbers of families, or a goodly proportion of the country's children. The state has become an alternative for a husband.

The economics of marriage

When couples form common households, incomes are redistributed between spouses and both benefit from economies of scale by sharing costs. Working households usually live in their own homes and benefit from an appreciating asset. When parents live together the children's standard of living is higher and they might have something to inherit. Couples make income gains over time, and are clearly more successful in improving their circumstances.

Statistically, at any one time, couples with children make up more of the 'poor' than sole parents but they exit this category twice as fast. In part this is simply because marriage can supply two earners or a second earner when income is insufficient.

Marriage is an institution where the pursuit of individual objectives is replaced by joint goals. Of course there are some very wealthy single people, but estimates of the per capita median wealth using measures which include pensions, real and financial assets and the value of the primary residence, show a tremendous disparity between married-couple and single-persons and divorced or separated households in mid to later life. Combined assets grows with the length of marriage. Conversely, the longer a separation or divorce, the lower the level of assets. And income measures cannot record the additional benefits derives from the home economy where exchanges take place through an altruistic sharing of goods, services and tasks among family members. Multi person households have greater value-adding opportunities. Goods purchased in the market are the raw materials with which the family then makes additional goods and services for its own consumption. Compared to singles, a couple has double the skills, time and ingenuity – and some benefits of specialisation.

Marriage initiates a personal social security system through a network of kin. Small groups can muster more information, energy and resourcefulness than can the members on an individual basis, including assistance during periods of illness or other crises. The pervasive evidence is that children who live with only one parent lack, on average, the connections of friends, neighbours, and other adults in the community that children in two parent families have.

Married couples save more at a given income level than single people. In the UK 70% of sole parents and 40% of single adult households have no savings.

Perhaps this is because they lack the same desire to make provision for a spouse or child and the expectations and requirements of married status are tied up with establishing and furnishing a home, which encourages the acquisition and maintenance of property.

In retirement, support from marriage partners comes in the form of direct income from pensions, shared living costs, and access to non-market services which people provide for each other.

Thus we can say that marriage encourages workers to achieve greater income levels and promotes greater personal service giving than does single adult living. This in turn means higher national earning and expenditure levels thus providing greater tax revenues and wealth accumulation whilst placing fewer burdens on state welfare expenditure. The state therefore has every reason to encourage rather than discourage viable marriages.

Idleness, Marriage and Economic Prospects

I have concentrated so far on women, in and out of marriage, with children to rear. But, over a longer term, male fortunes outside of marriage may also crumble, not least due to a loss of incentives for work and earnings. Changes in employment affect family patterns, but changes in family patterns influence employment and earnings. Male marriageability depends on employment and income. Marriage itself promotes male labour market involvement and success.

During the last half century there has been a generally downward trend in male economic activity of those aged 16 to 64 (as distinct from unemployment – which still counts as being economically active – which fell from 94% in 1959 to 79% in 1999) whilst female economic activity has risen. Men of all ages are less likely to be in work now than they used to

be. In 2003 there were almost a million more economically inactive men than there were in 1993.

Labour market detachment amongst men is now widespread throughout the English speaking world. Showing a steady, on going upward trend compared to the 'J' cyclical movement of unemployment, this male drop-out from the labour market shadows the rising numbers of welfare dependent sole parents. 0nly 3% of these men give 'looking after the home' as a reason to be idle. 25% claim 'sickness' and 20% say they are a 'student'. This not a problem affecting only one generation of relatively older men, or those displaced by the loss of manufacturing or industrial jobs; men born later are, at any age, less likely to be employed than those born earlier were at the same age.

This rising inactivity is unusual and should be a major cause of concern. It is likely to be put down to 'constrained' choices i.e. where there is a pay gap between previous and lower potential earnings in a new job. But one of the best kept secrets is that married men have dramatically higher rates of employment than single or divorced men, large percentages of whom are unemployed or otherwise economically 'inactive' and likely to be on basic benefits. Men in the National Child Development Study of 33-year-olds were six times more likely to be 'economically inactive' and over twice as likely to be unemployed if they were separated, divorced or widowed compared to the married. Never married men were three times more likely to be unemployed or economically inactive and to derive all their income from state benefits. It is another aspect of the way that growing numbers of single adult households (with or without children) have no earnings.

Indeed, while married women of all ages tend to have higher employment rates than those of divorced women, younger divorced and childless men are much less likely to be working even than divorced and childless women with similar occupations. Only two thirds of non-resident fathers were in employment compared with over 80% of resident fathers in the mid 1990s. The employment gap by marital status particularly affects minorities. A large proportion of young Caribbean men are unattached. However, if black men have qualifications, are attached, and do not live in a run down area, then their prospects are the same as a similar white person's. The absence of fathers in youth and the absence of wives in adulthood makes it very difficult to equalise opportunities or achievement between the races. And we may note that traditionally, in working class communities, marriage carried with it the right to be treated as adult and independent. A job was

more than just an activity which provides and income, it was the means of sustaining a household and of carrying out those responsibilities which define adulthood.

Putting it another way, we can note that a US study showed that, on average, married high school graduates earned 30% more than their never married contemporaries – equivalent to a difference in schooling of about two to four years. And the same pattern holds elsewhere. In Sweden, despite all the attempts to hold men back and push women forward, a study over a four year period showed that married men experienced a much greater growth in earnings than unmarried men did.

As an interesting footnote I might add that a recent UK analysis shows that working married women also do better than unmarried working women.

Public Policy

There seems to be a general hostility amongst academics and policy makers towards marriage and families. The tax/benefit system imposes penalties on two parent families. But all things considered, marriage is a highly beneficial institution for those involved, for society and for the state. Taxation and welfare measures, like law and custom, have the capacity not only to affect the behaviour of individuals, in both direct and devious ways, but to promote certain assumptions and values. In turn, values influence tax, welfare, legal and other policies. Public policy has been formulated for the last twenty years with the specific aim of breaking the conjugal family. There seems little or no appreciation of how much is at stake economically, or otherwise, when the state pulls the policy levers against marriage and two parent families, and facilitates a mass movement from a relatively cheap and efficient form of living and child-rearing to a comparatively expensive and inefficient one.

Some questions raised

Q. What about ‘partnerships’. Do they have the same effect as marriage?

A. No. The tendency for married men to earn more than single men by being more productive and successful at work is far higher than for cohabiting men who in these respects resemble single or divorced men.

Q. Does all this mean that younger males are affected in any way?

A. Yes, I think so. While much discussion centres on improving the school attendance and performance of lower class boys, or the intensive education and training efforts that are needed to help those who would have previously worked in industry, little or no thought seems to have been given to how the education system is going to motivate boys when the demands and 'ideology of the male provider' disappears.

Q. Do the trends you have identified help to explain growing inequality?

A. Equal opportunities may be said to be a powerful factor in the polarisation of society into rich and poor sectors: a division between an elite of 'two-career' families who live in affluence, and an underclass of 'no-work' families.

ECONOMIC FLEXIBILITY

A talk given by Mr Alan Greenspan, Chairman of the Federal Reserve Board, to the HM Treasury Enterprise Conference in London on January 26th 2004. He gave the case for only resorting to regulation when all else fails. Sadly, in the UK we have a tendency to regulate as a first choice which is causing more and more confusion to those in our business community.

As the Great Depression of the 1930s deepened, John Maynard Keynes offered an explanation for the then-bewildering series of events that was to engage economists for generations to come. Market systems, he argued, contrary to the conventional wisdom, did not at all times converge to full employment. They often, in economists jargon, found equilibrium with significant segments of the workforce unable to find jobs. His insight rested largely on certain perceived rigidities in labour and product markets. The notion prevalent in the 1920s and earlier--that economies, when confronted with unanticipated shocks, would quickly return to full employment--fell into disrepute as the depression festered. In its place arose the view that government action was required to restore full employment.

More broadly, government intervention was increasingly seen as necessary

to correct the failures and deficiencies viewed as inherent in market economies. Laissez-faire was rapidly abandoned and a tidal wave of regulation swept over much of the world's business community. In the United States, labour practices, securities issuance, banking, agricultural pricing, and many other segments of the American economy, fell under the oversight of government. With the onset of World War II, both the US and the UK economies went on a regimented war footing. Military production ramped up rapidly and output reached impressive levels. Central planning, in one sense, had its finest hour. The pattern of production and distribution depended on plans devised by a small, elite group rather than responding to the myriad choices of consumers that rule a market economy.

The ostensible success of wartime economies operating at full employment, in contrast to the earlier frightening developments of the depression years, thwarted a full dismantlement of wartime regimens when hostilities came to an end. Wage and price controls, coupled with rationing, lingered in many economies well into the first postwar decade. Because full employment was no longer perceived as ensured by the marketplace, government initiatives promoting job growth dominated the postwar economic policy framework of the Western democracies. In the United States, the Congress passed, and the President signed, the 'Employment Act of 1946.'

However, cracks in the facade of government economic management emerged early in the postwar years, and those cracks were to continue widening as time passed. Britain's heavily controlled economy was under persistent stress as it vaulted from one crisis to another in the early postwar decades. In the United States, unbalanced macroeconomic policies led to a gradual uptrend in the rate of inflation in the 1960s. The imposition of wage and price controls in the 1970s to deal with the problem of inflation proved unworkable and ineffective. The notion that the centrally planned Soviet economy was catching up with the West was, by the early 1980s, increasingly viewed as dubious, though it was not fully discarded until the collapse of the Berlin Wall in 1989 exposing the economic ruin behind the iron curtain.

The East-West divisions following World War Il engendered an unintended four-decades long experiment in comparative economic systems, which led, in the end, to a judgment by the vast majority of policymakers that market economies were unequivocally superior to those managed by central planning. Many developing nations abandoned their Soviet-type economic systems for more market-based regimes.

But even earlier in the developed world, distortions induced by regulation were more and more disturbing. In response, starting in the 1970s, American Presidents, supported by bipartisan majorities in the Congress, deregulated large segments of the transportation, communications, energy, and financial services industries. The stated purpose was to enhance competition, which was increasingly seen as a significant spur to productivity growth and elevated standards of living. Assisting in the dismantling of economic rigidities was the seemingly glacial, but persistent, lowering of barriers to cross-border trade and finance.

As a consequence, the United States, then widely seen as a once great economic power that had lost its way, gradually moved back to the forefront of what Joseph Schumpeter, the renowned Harvard professor, called 'creative destruction,' the continuous scrapping of old technologies to make way for the innovative. In that paradigm, standards of living rise because depreciation and other cash flows of industries employing older, increasingly obsolescent, technologies are marshalled, along with new savings, to finance the production of capital assets that almost always embody cutting-edge technologies. Workers, of necessity, migrate with the capital.

Through this process, wealth is created, incremental step by incremental step, as high levels of productivity associated with innovative technologies displace lesser productive capabilities. The model presupposes the continuous churning of a flexible competitive economy in which the new displaces the old.

The success of that strategy in the United States confirmed, by the 1980s, the earlier views that a loosening of regulatory restraint on business would improve the flexibility of our economy. Flexibility implies a faster response to shocks and a correspondingly greater ability to absorb their downside consequences and to recover from their aftermath. No specific program encompassed and coordinated initiatives to enhance flexibility, but there was a growing recognition, both in the United States and among many of our trading partners, that a market economy could best withstand and recover from shocks when provided maximum flexibility.

Developments that enhanced flexibility ranged far beyond regulatory or statutory change. For example, employers have long been able to legally discharge employees at modest cost. But in the early postwar years, profitable large corporations were dissuaded from wholesale job reduction. Contractual inhibitions, to be sure, were then decidedly more prevalent than today, but of far greater importance, our culture in the aftermath of

depression frowned on such action. Only when bankruptcy threatened was it perceived to be acceptable.

But as the depression receded into history, attitudes toward job security and tenure changed. The change was first evidenced by the eventual acceptance by the American public of President Reagan's discharge of federally employed air traffic controllers in 1981 when they engaged in an illegal strike. Job security, not a major concern of the average worker in earlier years, became a significant issue especially in labour negotiations. By the early 1990s, the climate had so changed that laying off workers to facilitate cost reduction had become a prevalent practice. Whether this seeming greater capacity to discharge workers would increase or decrease the level of structural unemployment was uncertain, however. In the event, structural unemployment decreased because the broadened freedom to discharge workers rendered hiring them less of a potentially costly long-term commitment.

The increased flexibility of our labour market is now judged an important contributor to economic resilience and growth. American workers, to a large extent, see this connection and, despite the evident trade-off between flexibility and job security, have not opposed innovation. An appreciation of the benefits of flexibility also has been growing elsewhere. Germany recently passed labour reforms, as have other continental European nations. U.K. labour markets, of course, have also experienced significant increases in flexibility in recent years.

Beyond deregulation and culture change, innovative technologies, especially information technology, have been major contributors to enhanced flexibility. A quarter-century ago, companies often required weeks to unearth a possible inventory, imbalance, allowing production to continue to exacerbate the excess. Excessive inventories, in turn, necessitated a deeper decline in output for a time than would have been necessary had the knowledge of their status been fully current. The advent of innovative information technologies has significantly foreshortened the reporting lag, enabling flexible real-time responses to emerging imbalances.

Deregulation and the newer information technologies have joined, in the United States and elsewhere, to advance financial flexibility, which in the end may be the most important contributor to the evident significant gains in economic stability over the past two decades.

Historically, banks have been at the forefront of financial intermediation, in part because their ability to leverage offered an efficient source of funding. But too often in periods of severe financial stress, such leverage brought

down numerous, previously vaunted banking institutions, and precipitated a financial crisis that led to recession or worse. But recent regulatory reform coupled with innovative technologies has spawned rapidly growing markets for, among many other products, asset-backed securities, collateral loan obligations, and credit derivative default swaps.

Financial derivatives, more generally, have grown throughout the world at a phenomenal rate of 17 percent per year over the past decade. Conceptual advances in pricing options and other complex financial products, along with improvements in computer and telecommunications technologies, have significantly lowered the costs of, and expanded the opportunities]’or, hedging risks that were not readily deflected in earlier decades. The new instruments of risk dispersion have enabled the largest and most sophisticated banks in their credit-granting role to divest themselves of much credit risk by passing it to institutions with far less leverage. Insurance companies, especially those in reinsurance, pension funds, and hedge funds continue to be willing, at a price, to supply this credit protection, despite the significant losses on such products that some of these investors experienced during the past three years.

These increasingly complex financial instruments have contributed, especially over the recent stressful period, to the development of a far more flexible, efficient, and hence resilient financial system than existed just a quarter-century, ago. One prominent example was the response of financial markets to a burgeoning and then deflating telecommunications sector. Worldwide borrowing by telecommunications firms in all currencies amounted to more than the equivalent of one trillion US dollars during the years 1998 to 2001. The financing of the massive expansion of fiber-optic networks and heavy investments in third-generation mobile-phone licenses by European firms strained debt markets.

* * *

At the time, the financing of these investments was widely seen as prudent because the telecommunications borrowers had very high valuations in equity markets, which could facilitate a stock issuance, if needed, to pay down bank loans and other debt. In the event, of course, prices of telecommunications stocks collapsed, and many firms went bankrupt. Write-downs were heavy, especially in continental Europe, but unlike in previous periods of large financial distress, no major financial institution

defaulted, and the world economy was not threatened. Thus, in stark contrast to many previous episodes, the global financial system exhibited a remarkable ability to absorb and recover from shocks.

The most significant lesson to be learned from recent economic history is arguably the importance of structural flexibility and the resilience to economic shocks that it imparts. The more flexible an economy, the greater its ability to self-correct in response to inevitable, often unanticipated, disturbances and thus to contain the size and consequences of cyclical imbalances. Enhanced flexibility, has the advantage of being able to adjust automatically and not having to rest on policymakers initiatives, which often come too late or are misguided.

I do not claim to be able to judge the relative importance of conventional stimulus and increased economic flexibility to our ability to weather the shocks of the past few years. But it is difficult to dismiss improved flexibility as having played a key role in the US economy's recent relative stability, in fact, the past two recessions in the United States were the mildest in the postwar period. The experience of Britain and many others during this period of time have been similar.

* * *

I do not doubt that the vast majority of us would prefer to work in an environment that was less stressful and less competitive than the one with which we currently engage. The cries of distress amply demonstrate that flexibility and its consequence, rigorous competition, are not universally embraced. Flexibility in labour policies, for example, appears in some contexts to be the antithesis of job security. Yet, in our roles as consumers, we seem to insist on the low product prices and high quality that are the most prominent features of our current frenetic economic structure. If a producer can offer quality at a lower price than the competition, retailers are pressed to respond because the consumer will otherwise choose a shopkeeper who does. Retailers are afforded little leeway in product sourcing and will seek out low-cost producers, whether they are located in Guangdong province in China or northern England.

If consumers are stern taskmasters of their marketplace, business purchasers of capital equipment and production materials inputs have taken the competitive paradigm a step further and applied it on a global scale.

From an economic perspective, the globe has indeed shrunk. Not only

have the costs of transporting goods and services, relative to the total value of trade, declined over most of the postwar period, but international travel costs, relative to incomes, are down, and crossborder communications capabilities have risen dramatically with the introduction of the Internet and the use of satellites. National boundaries are less and less a barrier to trade as companies more and more manufacture in many countries and move parts and components across national boundaries with the same ease of movement exhibited a half century ago within national economies. A consequence, in the eyes of many, if not most, economists, world per capita real GDP over the past three decades has risen almost 1-1/2 percent annually, and the proportion of the developing world's population that live on less than one dollar per day has markedly declined.

Yet globalization is by no means universally admired. The frenetic pace of the competition that has characterized markets' extended global reach has engendered major churnings in labour and product markets.

The sensitivity of the US economy and many of our trading partners to foreign competition appears to have intensified recently as technological obsolescence has continued to foreshorten the expected profitable life of each nation's capital stock. The more rapid turnover of our equipment and plant, as one might expect, is mirrored in an increased turnover of jobs. A million American workers, for example, currently leave their jobs every week, two-fifths involuntarily, often in association with facilities that have been displaced or abandoned. A million, more or less, are also newly hired or returned from layoffs every, week, in part as new facilities come on stream.

Related to this process, jobs in the United States have been perceived, as migrating abroad over the years, to low-wage Japan in the 1950s and 1960s, to low-wage Mexico in the 1990s, and most recently to low-wage China. Japan, of course, is no longer characterized by a low-wage workforce, and many in Mexico are now complaining of job losses to low-wage China.

In developed countries, conceptual jobs, fostered by cutting-edge technologies, are occupying an ever-increasing share of the workforce and are gradually replacing work that requires manual skills. Those industries in which labour costs are a significant part of overall costs have been under greater competition from foreign producers with lower labour costs, adjusted for productivity.

This process is not new. For generations human ingenuity has been creating industries and jobs that never before existed, from vehicle

assembling to computer software engineering. With those jobs come new opportunities for workers with the necessary skills. In recent years, competition from abroad has risen to a point at which developed countries' lowest skilled workers are being priced out of the global labour market. This diminishing of opportunities for such workers is why retraining for new job skills that meet the evolving opportunities created by our economies has become so urgent a priority. A major source of such retraining in the United States has been our community colleges, which have proliferated over the past two decades.

We can usually identify somewhat in advance which tasks are most vulnerable to being displaced by foreign or domestic competition. But in economies at the forefront of technology, most new jobs are the consequence of innovation, which by its nature is not easily predictable. What we in the United States do know is that, over the years, more than 94 percent of our workforce, on average, has been employed as markets matched idled workers seeking employment to new jobs. We can thus be confident that new jobs will displace old ones as they always have, but not without a high degree of pain for those caught in the job-losing segment of America's massive job-turnover process.

* * *

The onset of far greater flexibility in recent years in the labour and product markets of the United States and the United Kingdom, to name just two economies, raises the possibility of the resurrection of confidence in the automatic rebalancing ability of markets, so prevalent in the period before Keynes. In its modern incarnation, the reliance on markets acknowledges limited roles for both counter-cyclical macroeconomic policies and market-sensitive regulatory frameworks. The central burden of adjustment, however, is left to economic agents operating freely and in their own self-interest in dynamic and interrelated markets. The benefits of having moved in this direction over the past couple of decades are increasingly apparent. The United States has experienced quarterly declines in real GDP exceeding 1 percent at an annual rate on only, three occasions over the past twenty years. Britain has gone forty-six quarters without a downturn.

Nonetheless, so long as markets are free and human beings exhibit swings of euphoria and distress, the business cycle will continue to plague us. But even granting human imperfections, flexible economic institutions appear

to significantly ameliorate the amplitude and duration of the business cycle. The benefits seem sufficiently large that special emphasis should be placed on searching for policies that will foster still greater economic flexibility while seeking opportunities to dismantle policies that contribute to unnecessary rigidity.

Let me raise one final caution in this otherwise decidedly promising scenario.

Disoriented by the quickened pace of today's competition, some in the United States look back with nostalgia to the seemingly more tranquil years of the early post-World War 11 period, when tariff walls were perceived as providing job security from imports. Were we to yield to such selective nostalgia and shut out a large part, or all, of imports of manufactured goods and produce those goods ourselves, our overall standards of living would fall. In today's flexible markets, our large, but finite, capital and labour resources are generally employed most effectively. Any diversion of resources from the market-guided activities would, of necessity, engender a less-productive mix.

For the most part, we in the United States have not engaged in significant and widespread protectionism for more than five decades. The consequences of moving in that direction in today's far more globalized financial world could be unexpectedly destabilizing.

I remain optimistic that we and our global trading partners will shun that path. The evidence is simply too compelling that our mutual interests are best served by promoting the free flow of goods and services among our increasingly flexible and dynamic market economies.

WHY SCHOOLS SHOULD TEACH YOUNG PEOPLE ABOUT PERSONAL FINANCE

A talk given by Mrs Wendy van den Hende, Chief Executive of the Personal Finance Education Group, to members of the Economic Research Council on Thursday 25th September 2003.

Why schools should teach young people about personal finance

Young people leaving school today enter a complex and fast changing world. They can expect to live longer than their parents and will need to match how long they want to work against the kind of life style they want in retirement. They may have a number of long term relationships with varying family structures or may join the increasing number of people who live alone. They are unlikely to have the same job throughout their life and may experience redundancy, unemployment, self employment and retraining. In the middle years of the twentieth century many people would save and then buy. In the twenty first century the culture is to spend and repay. The emphasis is on personal responsibility and personal provision. Acquiring personal finance skills at an early age can both help people avoid the difficulties experienced through, for example, over-indebtedness, but can also enable them to participate enjoyably in society.

Young people themselves recognise the importance of being financially competent. A Mori survey carried out for the Qualifications and Curriculum Authority in 1999 found that 48% of pupils surveyed thought that more should be taught in schools on managing money. This was the top answer beating topics such as preparation for being a parent, politics and knowledge about sex.

There have always been some elements of personal finance education in schools and there have always been enthusiastic teachers who recognize the need to equip their pupils with financial skills. Examples might include linking it to work experience, budgeting for a holiday or using compound interest rates in maths. However it is by no means guaranteed that all children will receive any personal finance education during their years at school.

Financial capability now has a legitimate place within the national curriculum primarily within citizenship and personal social and health education but also in other subjects such as Maths, IT, history, geography and English. But timetables and teachers are under pressure and personal

finance is forced to compete with subjects ranging from drugs and democracy to the environment.

pfeg (The Personal Finance Education Group) is a charity, which works closely with government departments, teachers, consumer bodies, the Financial Services Authority and the finance sector. Our mission is for all young people to leave school with the confidence, skills and knowledge they need about financial matters so that they can participate fully in society.

So what do we mean by a young person being financially capable? People from the finance sector often offer to go into schools – they have this belief that if they tell children about how to open a bank account, how to budget or what the stock market is about, that is all they need to do. Apart from the fact that it ignores all the work that has been done on how people learn, it is not as simple as that. Unfortunately the attitude exists within schools too with teachers sometimes failing to address wider issues. Financial capability is not just about knowledge, for example, about knowing how to work out the APR for different credit cards, useful though this might be – it is about developing financial acumen, in this case challenging the assumptions around whether having a credit card in this first place is the right way for that individual.

Too much of the personal finance teaching that goes on in schools is about the mechanics of how you do things. Of course content and context are important but teaching should not concentrate on financial products and services in a mechanistic way. Financially competent young people would demonstrate a questioning approach, challenging many of the assumptions that govern the way society conducts itself. They would feel confident about the jargon used around financial services and feel confident about their ability to use financial information. They would know how to access information and be able to identify when they would need, and where they would be likely to find, advice. Each person would have identified their own attitude to risk and developed an understanding of how this would influence their financial decision making.

Financial capability is about what you are able to DO and HOW you do it, not about what you know.

The Department for Education and Employment produced guidance on Financial Capability through Personal Finance Education (DfEE 2000) setting out the three interrelated themes:

- *Financial knowledge and understanding* – the nature of money and insight into its functions and uses

- *Financial skills and competence* – being able to apply knowledge and understanding across a range of contexts, confidence and effectiveness
- *Financial responsibility* – wider impact at a greater societal level with social and ethical dimensions

However **pfeg** would also add financial enterprise accepting that it has a key role to play in developing financial capability, in particular the capability to handle uncertainty and respond positively to change, to create and implement new ideas and new ways of doing things, to make reasonable risk/reward assessments and act upon them in one's personal and working life (see Howard Davies Review of Enterprise and the Economy in Education).

How should financial capability look in practice?

Good practice in personal finance education will comply with Ofsted criteria for teaching and learning and will include:

- Recognition that people from other cultures may experience the financial world differently
- Structures to enable young people to be prepared to make informed and independent decisions in the future, looking at adult needs, wants and priorities
- Lessons that are interactive, rooted in the experiences of the pupils and are relevant to them
- Involvement of a wide range of contributing organisations, such as banks, building societies, credit unions and Citizens' Advice Bureaux
- Opportunities to make sense of the links between the personal, business and national levels

Representatives from the finance sector can make very valuable contributions to the development of financial capability. In addition to their expertise they bring in the realism of their organisational networks and provide a model of how social responsibility policies can work in practice.

Learning about personal financial issues does not take place solely within the classroom. Parents, other adults and young people's peer groups all have an important role to play. Children and young people bring a wealth of experience and knowledge with them.

Pfeg recognises that for many teachers, personal finance education is outside their comfort zone. They lack, or think they lack, the confidence and the competence to teach it. **Pfeg** has been running an innovative project, Excellence and Access, over the last few years, to create a critical mass of schools that have been integrating it into their school plans in a coherent and systematic way. One of the main benefits of the pilot work is the large number of examples of how teachers can get across the subject in an interesting and challenging way that engages children and young people. School advisers have worked with individual schools to show how it can be done. The results of this work will be shared with schools across the UK.

The following examples demonstrate the range of work that can be done.

Catford Girls school in Lewisham, South London, did an improvised role play in a Kilroy style format. The Ozlem Show used three case studies featuring how debt can mount up with door step lending, an addiction to scratch cards, borrowing difficulties if following Islamic law and problems getting credit when you have moved house several times. The lesson featured invited guests from a credit union and the local citizens' advice bureau.

The lesson illustrated the key message relating to financial education that good practice is rooted in the acquisition of skills and the development of a questioning approach, demonstrated by:

- Active participation by pupils
- Involvement of adults other than teachers
- Range of cultural groups as not everyone will see the world in the same kind of way and all are affected by the global economy.

Another example comes from a school in York where they held an industry day for 12 year olds. The aim was:

- To understand the present situation regarding national currencies and exchange rates
- To evaluate the effects that the introduction of the Euro may have on the traveller within the EU prior to its launch in January 2002 and today
- Develop key skills and personal confidence through the participation in group work and problem solving activities

As part of the activity students asked to imagine a trip when one traveller goes on a specified journey from one EU country to another exchanging

currency as they go but not buying any goods with it – 15 countries in total. Each student started off with £100. They were asked to predict how much money would remain at the end of the trip. They were given the real exchange rates on a particular day and had to calculate the actual transformation of their currency as the journey unfolded. The students' original estimates were that approximately £80–£90 would remain. The actual amount was only £26.12.

Pfeg believes everyone needs financial education regardless of socio-economic background or ability levels, those with special needs as well as those who are exceptionally able. Coming from an economically secure background does not necessarily equate to having financial skills and indeed children from wealthy homes are often protected from picking up financial information, whereas those from less economically advantaged households may have superior budgeting skills and be more aware of value for money.

Barbara Priestman School is a mixed special school in Sunderland that provides an example of how each person can improve their financial skills no matter the start point. The attainment of pupils is predominantly below level one of the National Curriculum. The school provides for a wide range of needs as students display challenges associated with autism, dyspraxia, spina bifida and a wide range of communication difficulties. 8 students aged between 16 and 19 had already done some work on coin recognition and money handling. The next stage was to work on an activity involving planning, saving, spending and budgeting as part of their working towards independence.

Staff and students decided on a visit to the London Eye and a two night stay in a London hotel. Emphasis was placed on student decision making including itinerary, length of residential stay, methods of transport, as well as methods of fund raising, banking and budgeting. Emphasis was also to be placed upon sharing responsibilities, care for all members of the group by one another and issues of independent living.

Once the itinerary was agreed a programme of tasks was generated that would fit into the ASDAN qualification programme such as, linking needs to a particular situation, planning, estimating costs, recording actual costs and reflecting upon actions.

The consequences of not teaching children personal finance skills are not optimistic. Those who are experiencing problems managing their finances will be less effective at work, relationships will suffer, and debt

will spiral out of control. Personal unhappiness will result in addition to the effect upon the national economy. Rather than add to the number of financially illiterate adults let us seize the opportunity to invest in the future – after all we have a captive audience at school.

The earlier examples related to young people in secondary education but like any skill, the earlier you start, the better. Getting a firm foundation, learning the language and building on skills and knowledge will lead to young people leaving school as independent, informed and discriminating consumers.

JAPAN SUCCEEDING IN REFLATION BY THE BACK DOOR

By John O'Donnell

Japan in the 1990s followed Keynesian policies to try and stimulate its economy with the result that Japan today is burdened with the highest public debt of any country in the developed world. And yet Japan remained in recession – it was not able to spent its way out of trouble. Failure was quite possibly due to structural constraints within the economy -economic 'rigidities' protected by vested interests and the deflationary pressures coming from South East Asia, especially China.

Now however, there is more optimism, if not by the 'man in the street' in Japan then at least by some Japanese companies and by foreign investors in Japan. In 2003 foreigners bought ¥9.777 trillion (£57bn) worth of Japanese equities, the largest amount since the IT boom in 1999. This was the first time in 34 years that direct financial investment recorded a net *inflow* of capital into Japan. What has brought about this change?

The strategy now being followed is to issue yen to buy dollars on a prodigious scale, to 'flood the world' with yen, knowing that some at least of these yen will return to Japan where they are likely to be used for investment in assets – primarily real estate. Significant rises in real estate values will reduce bank bad debts, stimulate building activity and reflate the economy.

But things have not been presented in quite this way. Action to buy dollars – with the support of the US – is ostensibly for the purpose of stabilising the yen against the dollar to help Japanese exporters in the face of mounting low priced imports. However, given that Japan continues to run an (albeit reduced) overall trade surplus, this justification should be seen more as a camouflage for wider macro-economic aims.

In 2003 Japan spent ¥20.4 trillion (£122bn) on currency intervention, which is approximately 50% of its total tax revenue for the year. Following this, in January 2004 alone, Japan is estimated to have spent ¥7.5 trillion net on currency intervention, which in one month is more than 25% of the 2003 total. Three quarters of this currency intervention has been going into US treasury bonds, at times buying at a faster rate than they were being issued. (This recycling of funds to the US is financing the US fiscal deficit – a fragile scenario which may break down later this year – or may go on for some time yet.)

One would normally assume that credit created for the purpose of buying foreign bonds would, when the money returns lead to 'sterilization' – a reduction in domestic credit, to offset the inflationary effects of such an increase in the 'money supply'. But when yen flows back into Japan it is not being sterilized and finds its way into Japanese real estate and Japanese equities. Some real estate funds are achieving good results. Goldman Sachs for example has for some time now been taking advantage by buying golf courses. Many streets in Tokyo are changing due to the rush of development and hotels are being built or redeveloped.

Such redevelopment is helping to revitalise Japan but in many areas it is causing huge overcapacity, aggravating rather than solving, the problem. For example the Okura Hotel is currently only achieving a 53% occupancy ratio, and is not believed to have the financial power to renovate. So far there are winners – but even more losers in the commercial property sector, and we have yet to see if all this activity will move into the housing market generally – and that will depend on the banks.

An improvement in real estate prices means that the collateral taken by banks against their lending will improve and so their 'grey assets' will start to shrink. The provisions that they have set aside for doubtful loans will be freed up. Money will become available to organisations like the Japan Real Estate Investment Trusts (JREITS) to invest in housing -which currently looks an attractive investment opportunity.

To see this opportunity it is worth looking at the following table compiled

Table 1 Rental yield comparison of major cities February 2004

	Approx. apartment size (square feet)	*Net benefit to investor after mortgage charges*
Tokyo	1,250	7.3%
Shanghai	1,000	4.5%
Hong Kong	1,400	2.8%
Bangkok	2,500	2.1%
Singapore	1,300	1.6%
Beijing	1,300	1.0%
Taiwan	1,400	0.1%
New York	1,100	-0.1%
London	1,400	-2.4%

by John Saunders, Head of Regional Property Estate Analysts of Hong Kong. Although yields in Japan have come down as property prices have risen during this year these figures for the beginning of February 2004 are revealing (see Table 10).

Further support for the banks is coming from their expanding loan activities. Direct mortgage loans, unsecured consumer loans an 'small and medium enterprise' (SME) loans, are all growing strongly and fee income is also improving. Bank of Japan data for last November and

December showed total loan growth of 0.5 to 0.6% per month. This is likely to result in rising bank shares which should be taken as a sign that the economy is improving so that investors interest should then spread out into the stock market. Hopefully a firm real estate and stock market will then spill over into consumption.

The strategy, for the moment at least, appears to be working. Japanese GDP growth during the last three months of 2003 was 1.7% in real terms, an annualised rate of 7%. This, plus the fact that much of the money used in currency intervention has yet to work its way through probably means that such intervention from now on will be reduced, even if this leads to a higher yen and difficulties for exporters. In any case, if renewed weakness should cause the Bank of Japan to consider increasing again its currency intervention the US would certainly be helpful.

But that is for consideration in the Autumn. For the moment, the stockbroker's assessment must be that currency intervention for the time being should ease because economic activity is on a more positive trend and because asset prices are on the rise and, right now, these moves look likely to continue.

INFLATION – COMING BACK WITH A VENGEANCE?

By Damon de Laszlo

The world economy continues to grow apace except in Europe. The US looks as though it is going to clock up a third consecutive quarter of above trend growth with no sign of the growth abating. Capital expenditure is up and employment is picking up as companies see continuing full order books. Shortage of capacity is appearing in the IT industry and in particular in the semiconductor sector. The demand for commodities is exceeding supply at a time of low stocks and the Central Bank in the run up to the November election has avowed to err on the side of inflation rather than deflation.

China is experiencing growth at an even faster rate than the US but the major difference is there is no shortage of labour or capital.

Japan, for the first time in ten years, is going into growth mode. Consumer expenditure is showing the first signs of life, and export sales are growing rapidly driven by China. Japan, like China, has no shortage of labour or capital.

The UK economy, like the US economy has very little real labour capacity and very little useable manufacturing capacity. More importantly, it also suffers the same constraint as the US as far as financial capital is concerned. Both countries' Government borrowing leaves little room for industrial borrowing for capital expenditure without pushing up interest rates.

Commodity prices have risen considerably and are likely to continue along with freight rates. Container ship capacity is at the limit having grown some 34+% in the last twelve months.

In economic cycle terms, we are at the end of the deflationary cycle and it is likely, bearing in mind the US – UK deficits that the economies are going to overheat rapidly.

China's inflation rate has gone 3%+ positive in January after five years of deflation and the Chinese domestic demand for consumer goods now not being 'discouraged' by the Government means that cheap goods from China to America and Europe will start to disappear, driving consumer inflation.

From a stock market point of view, company earnings are going to grow more rapidly than consensus and the enormous institutional underweighting in equities in the US, UK and Japan is going to drive markets, certainly for the next eighteen months.

Interest rates are, however, likely to rise as competition for capital between industry and Government heats up and interest rates could rise very rapidly if Japan and China start to sell US Treasuries for their own capital investment needs. The rise in interest rates at some point will precipitate a financial crisis as those holding long term low yielding bonds experience the inevitable depreciation.

Will the pension and insurance industry get caught again? Having moved out of equities at the bottom of the market into bonds; they will start moving back into equities as the bond market starts to crater next year. This will drive equities in '05.

These problems along with those created by rapidly rising commodity and oil and gas prices are more than likely not going to appear as serious constraints until we get to the end of 2004, beginning of 2005 when I think inflation will be back, in the US and in the UK, with a vengeance.

DOING BUSINESS WITH THE JAPANESE

By Geoffrey Bownas, David Powers, Christopher P Hood and Contributors.
2003 Direct Image. £14.95

Perusing the many 'Guide to Doing Business with Japan' books (such as Zimmerman 1976, Norbury & Bownas 1980, Deutsh 1983, Jenkins 1983, Thian 1992, Rice 1995, McAlinn1996) one is struck by the obvious need for a good text that is up-to-date, that includes assessment of the momentous changes now taking place in Japan, and one that is both engagingly readable and factually practical. And now, for those setting out

on the long road towards a successful business presence in Japan, that is just what this splendid and polished little volume provides.

The reader sets off with six pages from Sir Stephen Gomersall, Britain's Ambassador in Tokyo, flagging up the size and attractions of the Japanese economy and marketplace. This is followed by two assessments of current economic prospects, the first by a Japanese writer and the second by an outsider. Tomohiko Taniguchi is refreshingly objective, setting out Japan's post-war development in neat stages and concluding with the thought that Japan's economy seems to 'move in sync with the morale of its populace' and adding that this 'is at last finding a psychological upturn'. Anthony Rowley's analysis of current economic developments provides the best chapter of the book, clinically dissecting the strengths and weaknesses, observing the changing role of foreign firms (and individuals such as the formidable Carlos Ghosn at Nissan), appropriately raising concerns over Japan's fast ageing population in the longer term – and over Japan's parlous banks in the very much shorter term. Rowley's conclusion that 'a massive monetization (with attendant inflationary risks) seems likely to be forced eventually on the Bank of Japan' is altogether more alarming than Taniguchi's optimism.

In passing, let us pick a few minutiae to consider. I was particularly interested in Taniguchi's brief account of the challenge posed by China's low wage policies. It is well put and worth quoting in full.

'Chinese wage levels will be kept competitively low for longer than has been the case with any other developing country. The Chinese state divides the populace into two – those born in urban areas and those from rural areas. The sons and daughters of farmers are often unable to get job interviews in major cities. Should they wish to send their children to city schools, they have to pay more than city dwellers. The minimum wage requirements that apply to city workers do not apply to those from rural parts. Controlling the influx of migrant workers from rural to urban areas is one of the prime purposes of these discriminatory customs. As a result, workers with farm backgrounds rarely settle in cities, but tend to go back to their home areas after a limited period. Once jobs are vacated, new groups move into the cities from the rural areas, and start working for the lowest possible wages. As this practice is most likely to continue, the overall wage level of the Chinese economy will be kept accordingly low. No nation other than China has operated a similar system in the past.'

Secondly, for a British publication, I would want to alter Taniguchi's observation about corruption in Japan that 'many elite bureaucrats were

either arrested or had to resign'. In Japan, being arrested may be tantamount to being guilty but here one would hope that such a comment would either say that they were convicted or not mention it at all!

Thirdly, Rowley is misleading when he speaks of the period between 1985 and 1990 as being one of 'supercharged growth'. The 1950s and 1960s were a time when Japan boosted corporate capital accumulation (and thus investment) by a range of dubious policies and practices which could be described as supercharged (high) growth. But by contrast the late 1980s were a time of monetary irresponsibility giving only a superficial impression of modest growth involving much ill-judged investment. Rather than being called supercharged growth, this latter period is more usefully described as 'growth on steroids'.

Two chapters follow by David Powers, long-time BBC man in Tokyo, which assess the difficulties and opportunities for foreigners investing in or selling into Japan, together with four recent case studies of Brits who have successfully set up high tech type businesses there. These are chapters of enthusiasm and caution which rightly emphasize the advice that, if one has the right scheme or product and has a clear strategic focus plus a willingness to be polite, genuine and persistent, then Japan is a place where profits can be made. For those who might ask what schemes or products might be 'right', notes are provided on growth sectors and changing tastes.

The four case studies form what is perhaps the most original part of this book, drawing on the recent experiences of four British entrepreneurs and allowing them each to express in their own way the lessons they feel can be passed on to others. Here again, the verdict has to be very positive – subject only to details for dissent. For one thing, it would have been useful to have some case studies from a wider range of activities. For another, I felt uneasy with Clare Ridley's comment that 'the parable of the Good Samaritan wouldn't work in Japan, because the beggar wouldn't want to receive a good deed from a stranger, as he would then owe him a favour in return', because that does not represent my understanding of the parable's meaning.

But these are details. Let us go on, because this book is also a businessman's travel guide setting out the bones (if not the critique) of the legal formalities appropriate for setting up and running a Japanese business, then instructing the novice on those aspects of greeting and meeting where misunderstandings can so easily occur, and then even presenting vital travel 'inside' information to help in route planning and budgeting. This is all

admirably practical material – and is capped off by appendices on useful contacts, language tips and even weather information.

Well indexed, neatly composed and thoroughly to the point for those needing both a handy guide and a short reference for business, *Doing Business with the Japanese* deserves 'must buy' status for both business persons and students nervously approaching this extraordinary country.

For further information visit www.japanbusinessproject.org

J.B.

THE CREDIT AND STATE THEORIES OF MONEY: THE CONTRIBUTION OF A MITCHELL INNES

Edited by Professor L. Randall Wray and published by Edward Elgar Ltd. of Northampton, Massachusetts and Cheltenham, England, 2004.

This is not a review as I am a contributor to this book, but the subject of the book, the history of money, is naturally of the greatest interest to members of the Economic Research Council that I would like to bring it to their attention.

A few members will have read my 1994 book, 'Towards True Monetarism' in which I argued that all money is debt and the therefore it is the giving of credit which creates money. In theory any debt can become money by making it easily transferable. In the book I also suggested that the study of 'the money supply' should be replaced by the study of the whole credit supply, not just that small part of the credit supply which is represented by the assets which are added up to arrive at the 'money supply' in its 'M4' form. Since I wrote the book the ideas I was advocating have been given the formal name of 'Creditary Economics,' a name originally proposed by the ERC's director of research, Christopher Meakin.

Christopher, an Icelandic friend resident in America who once worked for the IMF, and myself developed a small discussion group by joining with a similar group based in America but with international membership. Professor L. Randal Wray was one of the Americans and is currently a

professor at the University of Missouri – Kansas City. (Kansas City is mostly in Missouri, not in the State of Kansas.)

Professor Wray discovered that the credit theory of money had once had a powerful advocate, Alfred Mitchell Innes, a British diplomat who, while working in the British Embassy in Washington, published in the US Banking Law Journal two important papers. The first, published in 1913, was called 'What is Money?', and the second, published in 1914, was called 'The Credit Theory of Money.' The title of the second paper would have been more appropriate for the first which does much more to establish the credit theory of money. The editors of the Banking Law journal expected these articles to cause a furious debate, but the advent of the 1914-18 War seems to have caused the subject to be forgotten, despite a review by John Maynard Keynes. Keynes was not then well-known so his interest was not enough to keep the debate going. I have little doubt, however, that Keynes was persuaded by Mitchell's well argued case.

The two papers show remarkable scholarship, especially with regard to what he says about the Babylonian financial system. One of the contributors to the new book is Professor Michael Hudson, who, besides being a professor of economics, is a leading Bronze Age archaeologist. Professor Hudson has organised several conferences on Bronze and Iron Age economics, the last being at the British Museum in November 2000 on ancient accounting techniques. Mitchell Innes' views about Babylonian economics are still acceptable to modern students of the ancient records, which, survive in the form of millions of baked clay tablets.

Professor Wray commences his book by republishing Mitchell Innes' two articles. They are beautifully written and a joy to read. They will not be popular, however, with those who think that there can be a form of money which is not based on debt. Money is the name we give to transferable (negotiable) claims on value. Any jurist will state firmly that there are no rights without balancing obligations, so a claim of value cannot exist without a counter-party, a debt. The fact that money is a right backed by an obligation leads Mitchell Innes to reject the definition of money as 'a medium of exchange.'

Another chapter in the book, by Professor John Henry recounts the development of money in Ancient Egypt. Professor Henry is an economist, not an Egyptologist, but he deals with the topic with great authority. Dr. Geoffrey Ingham, a Fellow of Christ's College, Cambridge, is both an economist and a sociologist. He contributes a scholarly and detailed historical account of the development of exchange systems in Europe.

My own chapter is principally about the way trade debt was monetised and became the main basis of money. The research for this chapter produced some fascinating discoveries which taught me how wrong some of our modern perceptions of money are. We think of money as a state thing, usually a state debt. Mitchell Innes makes it clear that the transformation of state debts into money was a difficult transition. In mediaeval times state debts were 'monnaie faible,' while merchants debts were 'monnaie forte.' The reason was simple: one could not sue a King for his debts, and even if one could there were no worthwhile assets to sell to meet the debt. Kings spent their money on paying mercenary soldiers, not on lasting assets. On the other hand if a merchant had borrowed money to buy a flock of sheep there was a chance he still had the sheep. The creditworthiness of any monarch rests on his capability to tax, not on his assets. Moreover if the taxes he raises can be paid by presenting the monarch's own IOUs the latter become acceptable as money. This is the basis 'State Theory of Money,' first propounded in 1905 by the German, G. F. Knapp.

Textbooks on the history of money tell the student that money was invented to overcome the problems of barter and 'to reduce transactions costs.' Mitchell Innes states that this view is quite wrong. Barter was never a viable system of exchange, and the trading of debts came first; the monetary system grew out of the credit system. Barter has a very small role, that of facilitating international trade. The same is true of full-value gold and silver coins. Coins were invented to pay soldiers or to facilitate international trade. They are quite unnecessary in a peaceful society where 'documentary credits' are far more convenient than bullion.

Mitchell Innes is adamant that all coinages have been tokens, worth more than the bullion content. Indeed I think most economists would accept that it is its use as money which gives bullion it value, not the other way around.

Of course the most common documentary credit is the bill of exchange. The temples of Babylonia were issuing bills of exchange as early as 2000 BC. Mitchell Innes refers to 'case tablets.' These consist of a baked clay tablet which on the outside has words which are a receipt by a temple for a quantity of silver. Concealed inside the tablet is another which directs the temple to hand over the silver to the bearer of the tablet. The fact that the tablets have survived unbroken seems to indicate that they were used as money and no more likely to be redeemed than Bank of England notes were later. One would love to know if the silver actually existed. My guess

is that it did not, for if it did the temples would have needed to keep careful records of their holdings and of how many receipts had been issued. No such records have been found, so far as I know. The British Museum hold nearly 700 case tablets.

The role of the ancient temples in the monetising of debt is something which will surprise many modern readers who are led to by the story of Christ's attitude to the money changers in the temple to conclude that money and religion are not compatible. But Christ must have been trying to change a practice with a 2000 year history behind it. The temples were the founders of the commercial and financial system. They devised and enforced the moral code without which a financial system could not exist. They invented the figures for keeping records. They invented writing to make written contracts possible. They authorised the merchants. They ran the factories of Babylonia which produced fine textiles for exchange abroad for raw materials. The temples gave trade credit to the merchants who conducted this trade.

Babylonia was a an alluvial plain with not much in the way of raw materials. Trade to obtain the raw materials was vital to the cities of the plain. To show the importance to them of trade they gave their principle god, Enlil, the tile of 'The Great Trader.' The trade links may have been very extensive. Copper to make bronze came from the Persian Gulf, but where did the tin come from? That is still a mystery though archaeologists assume that Afghanistan was the source, despite the fact that it now has no tin. They are unwilling to face the possibility that the ancient population of Mesopotamia got tin from the larger but distant sources such as the Malayan Peninsula, Portugal, Northeast Spain, Bohemia and Cornwall. The possibility of such distant trade networks in early Neolithic times seems too bold a concept. The contemplation of such a network has been held back by the adhesion of most archaeologists until very recently to the 'diffusion theory.' The easy survival of ancient artefacts in the deserts of Mesopotamia has wrongly led scholars to assume that that area is the original home of technology, and that the knowledge diffused slowly to distant areas, reaching last the barbarians of the North Atlantic Facade. But the Atlantic Facade was resource rich, a fact unwisely ignored. In 2003 I visited the museum of prehistory at Tautavel in southern France. The museum is looked after by the University of Perpignan. One of the exhibits is a map of sites around the Mediterranean basin of sites where metal objects have been found, and it is stated that at that time the working of metal was confined to the Mediterranean basin. But the basin was resource poor and some believe

that as a consequence the Bronze Age came late to the basin. Recent discoveries suggest the statement is completely wrong. Where were the resources? They were in Austria and Switzerland, in the Asturias and Galicia and in a 100 mile wide swathe of land continuing south from there to Andalusia, in Southern Ireland, in Cornwall, and in North Wales.

Such was the conviction that technology arrived late in Britain that in 1772 when ancient tools were discovered in copper working at Parys Mountain in Anglesey the great Welsh naturalist, Thomas Pennant, announced, 'Must be Roman; the ancient Britons imported all their brass.' That idea remained firm and unmovable until 1989 when the Llandudno Council decided it needed a new car park at the Great Orme. The proposed site was covered with spoil from copper workings dating from 1690 to 1860. It was decided that an investigation should be carried out to make sure there were no dangerous shafts underneath. A mining company was employed to remove 200,000 tonnes of spoil and underneath they found the ancient working with carbon dates from 1860 BC to 600 BC.

They have excavated four miles of galleries on nine levels and think there may another thirty miles. The mine proved to be the largest known copper mine in the Bronze Age world. The ore was malachite, the most readily smelted of all the many ores of copper. This discovery started people thinking again about Parys Mountain. Permission was sought to reopen the sealed mine. There was too much spoil to go into it from above so the investigators went in from below via ancient drainage adits. They found workings with carbon dates 3750 years before present. ('Present' is 1950.) An Irish mine is even older, 2400 BC.

Bronze was first made accidentally. Copper ores often contained arsenic which will harden copper. But the best bronze requires tin. Tin bronze seems to have come into general use about 1800 BC. Researchers believe the ancient Britons who cut the down trees in 2149 BC to create 'Seahenge' used 38 different bronze axes. Did the cutting of oak require tin bronze? If it did, the better form of bronze was in use in Britain 350 years before it was used by the advanced civilisations of Sumer. Bronze was recycled and recycled from ancient times to the present, so finds of bronze artefacts are rare. Indeed the end of the Stone Age and the beginning of the Bronze Age is not evidenced by finds of bronze but by the absence of stone tools.

When Parys Mountain came on stream in the 1770s as the largest copper mine of the time in the world, one use to which its copper was put was to make tokens for use as small change. The Heritage Centre at nearby Port Amlwch declares the tokens were exchanged at their intrinsic value as

copper. Mitchell Innes would deny that completely. I am sure that his view is correct. Professor George Selgin of Georgia is writing a book about the 'button-makers of Birmingham' who made the copper tokens which were the only readily available small money of the late 18th century and some chapters of the book are on his website. The governments of George III did not regard the provision of money as a necessary job for the state. Even when Matthew Boulton was finally commissioned to make decent copper coins, he found he had to put them into circulation himself. As for notes the British government provided none until 1917. In my chapter of the book I reproduce the figures gathered by a Mr Leatham in the 1830s which show that the currency of trade in Britain at that time was bills of exchange.

I hope that ERC members will find the new book worth reading. I wish it could become a standard textbook, as the subject of money is incredibly badly taught at present. The founders of the ERC felt the same way, and I think would have welcomed 'The Credit and State Theories of Money.'

Geoffrey Gardiner

LETTER

A Response to 'Retire with Care – Your National Pension Level is at Stake' (Britain and Overseas autumn 2003) from Mr Brian Lewis

Dear Sir

I have been thinking about your Autumn 2003 article on pensions – frozen for some countries abroad and not for others! The more I think about it the odder it seems. There is no rhyme or reason, and that detracts from good governance and undermines respect for equity in democracy.

Following official guidance, since retirement I have stuck to living in the UK, Spain, France, Austria and the Philippines. That sounds quite safe but is it? Where do I reside by official definition. That was quite clear when I worked, but is much less so when I am always on holiday! Maybe I am in Manila (and safer there) because HM Government does not like the governments of Australia, New Zealand and Canada. Is this the advice our

ambassadors in these countries are giving? Is there some secret intelligence that is hidden from ordinary British citizens about Australia, New Zealand and Canada. Is a frozen pension meant as a special tax on such unfriendly destinations?

Are there no arguments for reaching agreement on reciprocal arrangements that might counteract this bad opinion? What rights do Australians, New Zealanders and Canadians have in the UK compared to what Britons have over there? When does pension freezing take place officially? Is it at pensionable age if one happens to be in Australia, New Zealand or Canada at that moment? Can one safely go on holiday to Australia, New Zealand and Canada without having a pension frozen?

HM Government should come clean about these unreliable countries and tell us the truth. Clearly something awful is known to HM government about Australia, New Zealand and Canada that they cannot bring themselves to tell us about. Certainly things are bad in Australia with so much beer, cricket and rugby football, but is it worse than I thought?

But it is nice to know that I am safe and secure on my British pension in the Philippines! It is a puzzle sometimes that travel advisories sometimes contradict this pension advice, but they wouldn't give us financial incentives to live in the Philippines without being sure of their facts, would they?.

Brian Lewis
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The Economic Research Council has recently set up a new website www.ercouncil.org and has made the following historical pamphlets available for free download. More recent publications can be bought online.

Date	*Title*	*Author*
1956	Preliminary Survey of the Economic and social Implications of automation	Parliamentary and Industrial Committee of the ERC
1957	Where money comes from!	Edward Holloway
1966	Can we afford Politicians?	Patrick D, de Laszlo
1967	A programme for National Recovery	Various
1967	Government and Management	Lord Beeching
1967	Homes for the People	Norman Macrae
1968	A programme for National Recovery Expansion without inflation	Various
1969	A programme for National Recovery The Balance of payments and invisible earnings	Various
1969	A programme for National Recovery Taxation: the financing of public expenditure	Various
1970	A programme for National Recovery The use of resources in Britain	Various
1970	The 'Great Turnaround' in Britain's Financial Affairs 1964-1970	Frederick W. Tooby
1971	Export Credit and Government External Monetary Debt: is it all really necessary?	Patrick D. de Laszlo
1971	Inflation and the Function of Monetary Policy in Britain	Edward Holloway
1972	Japan and the crisis in International finance	G. C. Allen
1972	Excessive Taxes lead to Stagflation	Frederick W. Tooby
1973	Inflation	J. Enoch Powell
1975	Producer Cartels, Threat or Opportunity?	Susan Hart
1978	A critical look at the Constitutional Structure of Britain	James M Goldsmith
1977	The balance of payments or Are import restrictions necessary?	Dr Alan Clark

Date	*Title*	*Author*
1978	Excessive Taxes lead to inflation and unemployment	????
1980	Abolishing Unemployment	R S. Musgrave
1981	How Guernsey beat the Bankers	Edward Holloway
1981	Energy Conservation: Who can take the Initiative?	M. J. Plats
1982	The Economics of State Housing in the UK	Ken Dixon Arch.
1984	Opinion, Economics and the EEC Half-truths for Britain and Japan	James Y. Bourlet
1985	Investing in Britain's Future – the balance between capital and current expenditure in the public sector	Andrew Street
1985	Public investment – virtue or vice?	AP. de Boer of the British Road Federation
1990	Mr Lawson's Boom: A Monograph	Brian Reading
1993	The Creation of a Civil Economy in Russia – The Need for Mercantilism	Tony Baron & Robert McGarvey

NEW MEMBERS

The Council, as always, needs new members so that it can continue to serve the purposes for which it was formed; meet its obligations to existing members; and extend the benefits of members to others.

Members may propose persons for membership at any time. The only requirement is that applicants should be sympathetic with the objects of the Council.

OBJECTS

i) To promote education in the science of economics with particular reference to monetary practice.

ii) To devote sympathetic and detailed study to presentations on monetary and economic subjects submitted by members and others, reporting thereon in the light of knowledge and experience.

iii) To explore with other bodies the fields of monetary and economic thought in order progressively to secure a maximum of common ground for purposes of public enlightenment.

iv) To take all necessary steps to increase the interest of the general public in the objects of the Council, by making known the results of study and research.

v) To publish reports and other documents embodying the results of study and research.

vi) To encourage the establishment by other countries of bodies having aims similar to those of the Council, and to collaborate with such bodies to the public advantage.

vii) To do such other things as may be incidental or conducive to the attainment of the aforesaid objects.

APPLICATION FORM

To the Honorary Secretary   Date ....
Economic Research Council
7 St James's Square
LONDON SW1Y 4JU

APPLICATION FOR MEMBERSHIP

I am/We are in sympathy with the objects of the Economic Research Council and hereby apply for membership.

This application is for
(delete those non-applicable)

Individual membership (£25 per year)
Corporate membership (£55 per year)
Associate membership (£15 per year)
Student membership (£10 per year)
Educational Institutions (£40 per year)

NAME ....
(*If Corporate membership, give name of individual to whom correspondence should be addressed*)

NAME OF ORGANISATION ....
(*if Corporate*)
ADDRESS ....
....
....

PROFESSION OR BUSINESS ....
REMITTANCE HEREWITH ....
SIGNATURE OF APPLICANT ....
NAME OF PROPOSER (*in block letters*) ....
SIGNATURE OF PROPOSER ....