The Moscow Times
30 YEARS
INDEPENDENT NEWS FROM RUSSIA

Useless Money

By Boris Kagarlitsky

September 28, 2011

The history of paper money began with a scandal.

When Scottish financier John Law proposed in the early 18th century that French Regent Philippe d'Orleans replace gold coins with paper money, everyone was thrilled by the idea. This gave the French Treasury the ability to stock and control the supply of precious metals. Everything was going fine until someone from the French court asked Law, who by that time had become France's comptroller, to print a few extra bills to cover the country's debt. Law dutifully began printing more and more, which, of course, sparked inflation.

The frightened authorities canceled the free exchange of paper money and opted for gold, causing the value of stock market shares to plummet and ruining thousands of small investors. Law escaped from the angry mobs by hiding first at the palace of the regent and then fleeing France altogether.

Morals have not improved greatly since then. A review of the U.S. Federal Reserve initiated by Congressman Bernie Sanders discovered this summer that the agency had issued nearly $2 trillion in soft loans to foreign banks, all of which owed money to U.S. financial institutions.

The U.S. creditors threatened serious trouble if the foreign debtors went bankrupt. But now, if those debtors go belly up, it is not the financial institutions that will suffer but the U.S. government and taxpayers.

Many expect the dollar's imminent collapse, but it is growing stronger. The dollar, as a world currency, is the main guarantee of other currencies. Both China and Russia base their financial health on their considerable holdings of dollars in reserves. And as the number of dollars in circulation grows, the governments of the world respond by printing more of their own currencies.

They have no choice.

One can certainly argue about the need for a new international financial system, but it would be impossible to create it now. Any financial system relies on a corresponding economic system. A financial crisis merely reflects unresolved problems and imbalances in the economy, and trying to make corrections through reforms in the financial sector alone is the same as trying to improve your appearance by changing the mirror. Radical changes to the global financial order are possible, but only after radical social and economic changes occur.

Comparable reforms in the 20th century came at a huge cost — two world wars, half a dozen revolutions, the establishment of the welfare state in the West and the dissolution of Europe's colonial empires.

Today, political elite the world over are determined to avoid radical change and desperate to follow their habitual course, even if they have to pay an even higher price for doing so. In such a situation, not only the dollar, but money in general ceases to have any value.

That means that however difficult and even dire the problems are facing the United States, they pale in comparison to those that await other countries — and especially countries like Russia whose economies are heavily dependent on raw materials exports. This is because, at the peak of any economic crisis, currency devaluation is always accompanied by a drop in the price of raw materials.

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Original url: https://www.themoscowtimes.com/2011/09/28/useless-money-a9834