



The History of Money

BECO 3310 Fall 2027

What's money?

**Why do we use money?
Why don't we exchange the things we
have for things we want?**

Transaction costs.

Money lowers transaction costs.

Carl Menger

- Born in Vienna, 1840; died 1921
- Founded the Austrian School of Economics
- Revolutionary Insight: Subjective theory of value
- Key work: “On the origin of Money” (1892)
 - Core claim: Money is a SOCIAL, not a STATE institution.



Barter's Limitations

- Double coincidence of wants: Need what other has AND they need what you have.
- Transaction costs are enormous
- Example: Farmer with grain needs shoes
 - Shoemaker doesn't want grain, but wants tools instead.
- Menger: "Restriction of Exchange"

Menger's Solution: Saleability

- Saleability = Facility of disposing of a good at current market prices
- Characteristics of highly saleable goods:
 - Divisible, durable, portable recognizable, widely demanded, stable price.
- People eventually discovered which goods were most saleable.
- These goods naturally become money.

The origin of Money: Spontaneous Order

- Menger's radical claim: Money emerges WITHOUT government.
- Millions of individual traders independently prefer the most salable good.
- No central authority needed or involved
- Example: In Mesopotamia, traders gradually chose barley and silver.
- “Money has not been generated by law... It is a social institution”

Commodity Money: Ancient World (3000 BCE)

- Mesopotamia: Shekel (weight of barley) becomes standard
- Temple credit systems using clay tablets
- Why barley? High scalability in agricultural society
- Different goods in different places:
 - Cattle (pastoral societies)
 - Salt
 - Shells
 - Cocoa seeds



On the island of Yap in the Solomon Islands, you'll find the world's largest and strangest form of currency: the rai stone. Forget pocket change: these limestone discs with the hole in the center can run 12 feet in diameter and weight up to eight tons. Because Yap lacks the proper limestone for rei stones, the villagers would risk their lives to paddle their ocean-going canoes to Palau, where they would carve these behemoths from a mountainside and row them back to the island. "Part of the value i







Why Precious Metals Became Universal Money

- Gold and silver found across many civilizations
- Superior saleability to all other commodities
- Divisible without loss, durable over centuries, portable (high value-to-weight)
- Universally recognized, stable demand
- “Sought for exchange... not for consumption but for their special salability”

Coinage invention (600 BCE)

Reducing transaction costs

- Problem with raw metal: weighing, testing, verifying purity
- Solution: standardized coins with stamps.
- Stamps to certify a coin's weight.
 - Now every time someone sees that seal, they know that it is certified
 - Governments could stamp coins, giving coins more credibility.





Unclipped



Partially Clipped



Clipped

Credit: Chris Keating, @chriskeating





Reeding invented by Isaac Newton during his time at the Royal Mint, in the 1600s

Fractional Reserve Banking (1600s-1800s)

- Goldsmiths begin accepting metal deposits
- Issue receipts that circulate as money.
- They realized they don't need 100% reserves
- Creation of credit, but also instability.
 - Problems with confidence, bank runs occur.

The Gold Standard Era (1717-1914)

- 1717 — Newton establishes de facto gold standard for Britain.
- 1870-1914: Classical gold standard—major economies fix to gold
- Benefits: price stability, fiscal discipline, international trade
- Limitations: rigidity, cyclical, deflationary bias.
- Menger's position: he supported the system, but carefully managed.

Bretton Woods (1944-1971)

- Post WWII: Dollar becomes world reserve currency
- Dollar convertible to gold at \$35/ounce
- Tensions grew: US inflation, gold outflows
- August 15, 1971: Nixon ended gold convertibility

Fiat Money and Central Bank Credibility (1971-Present)

- Post-1971: Pure fiat money (currency by government decree)
- No commodity backing—Only government promise.
- Milton Friedman: Central bank independence + inflation targeting
 - Set rules, tie the central bank's hands
- Without credible institutions, Fiat money is fragile.

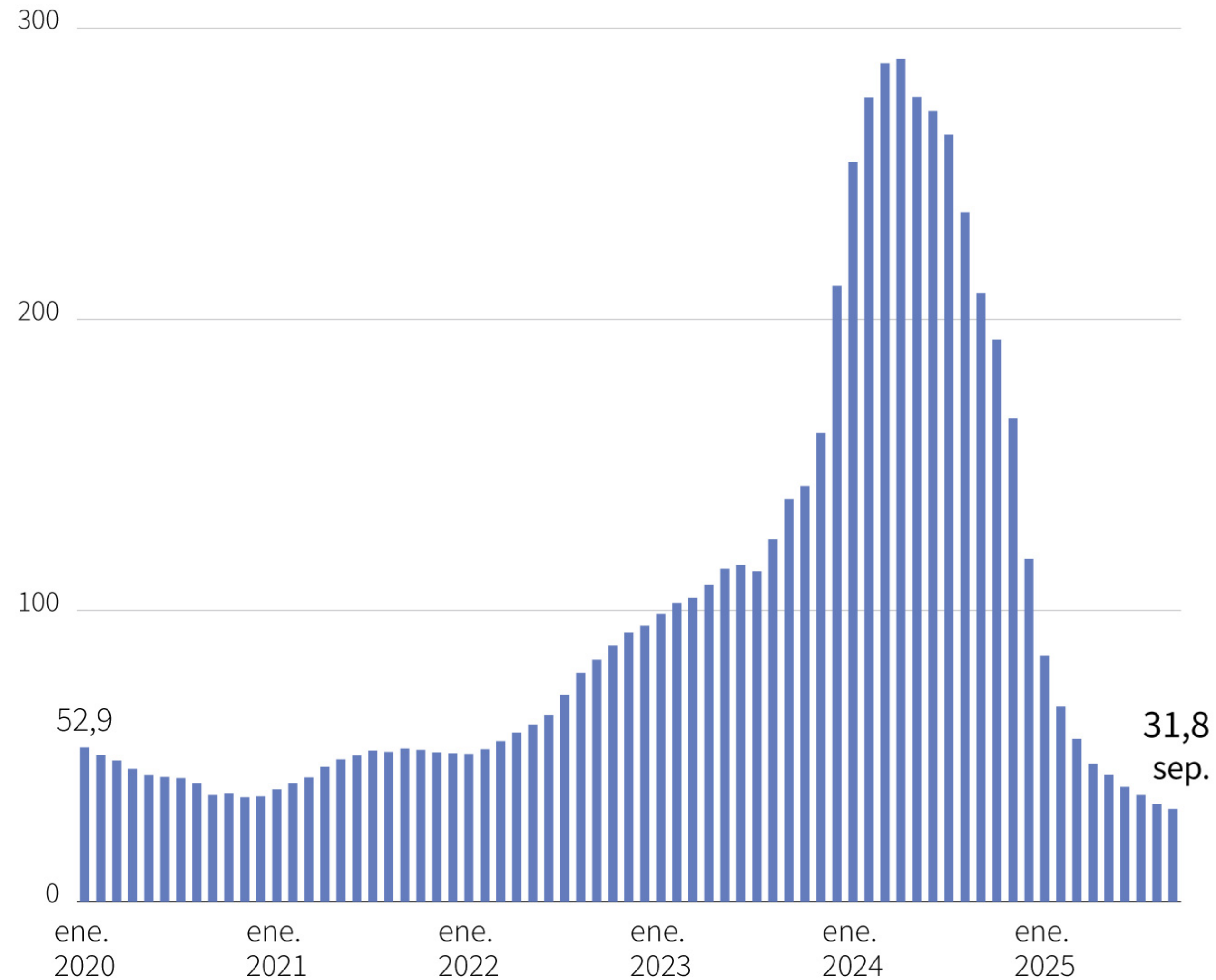
Rauchen
verboten





La inflación en Argentina

Evolución del IPC interanual, en %



Fuente: Banco Central de la República Argentina (BCRA)



**¡¡Te invito a festejar
mi primer
hiperinflación!!**



Te espero desde el 2020

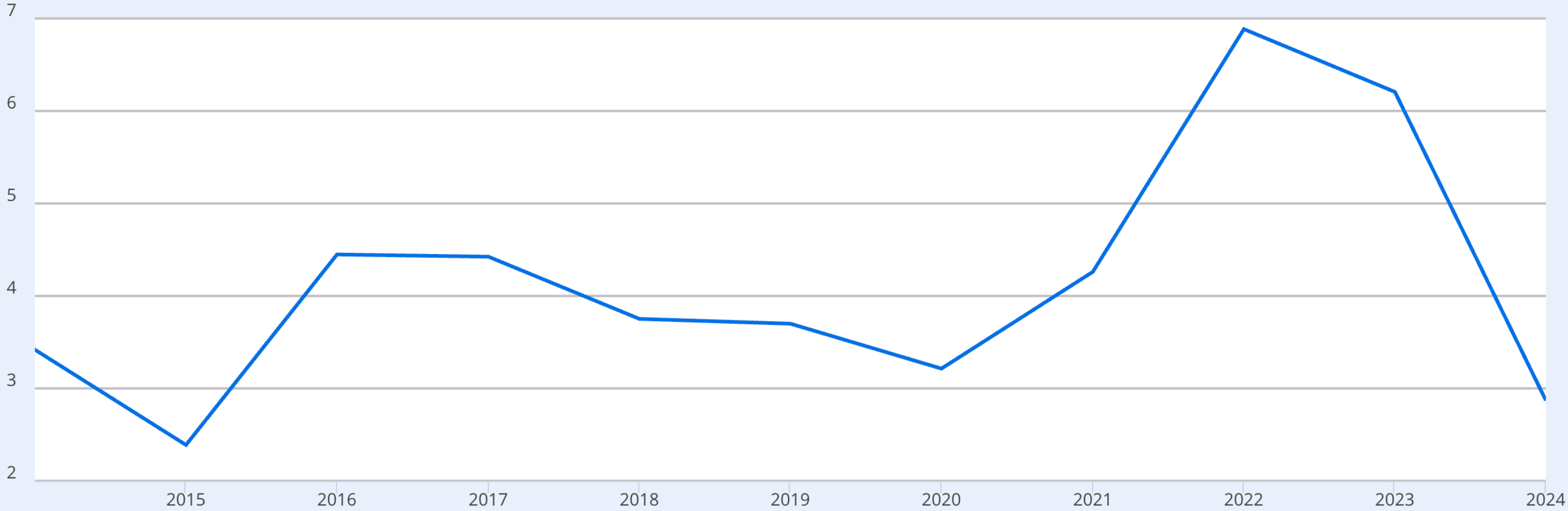
hasta el 2023

**NO
FALTES!!!!**

US inflation at 6.5%

Consumer Price Index for all urban consumers,
% change from a year ago





The future of Money: Menger's principles

- No one can “design” perfect money
- Money will continue to emerge from market preferences
- Successful monetary systems require:
 - Commodity backing or Credible policy rules

Money is a social institution.

End of Class.
Thanks for your attention.