Two REVIEWs
FOR:
Science Buzz Café # 173

Science Buzz Café

The Lie that Saved A Nation!

Associative Economics Café # 12

LAST Week SBC # 173 2 Reviews of Associative Economics Café # 12 June 16, 2011

Associative Economics and a fresh look at the functions of money took center stage last Thursday evening at the French Garden Restaurant. Before we all listened to a story about how an entire nation made a monetary course correction, the presenter briefly described some basic precepts of associative economics and also asked four economics related questions where the correct answer was rewarded with a handmade chocolate truffle from Sonoma Chocolatiers (Infusions Sebastopol). For example, "When did the global financial crisis begin?" As you can imagine there can be many 'right' answers, but there was a particular answer expected, as it was instructive and thought provoking. It came from a very recent book on the global financial crisis from Gower Publishing and offers a unique perspective from an English economic and monetary historian. In it the author asks: Why did the banks stop lending to one another, and why now? Oh right, the quiz answer about the start of the 'crisis': 'The end of the Napoleonic Wars with the emancipation of the money-market from the goods-market, dating roughly from the period 1810 – 1815.' In a sense, this was the birth of the dominance of the banking system.

Associative economics employs a descriptive and imaginative approach to understanding an ever-fluctuating economic life rather than exclusively relying on a method that only uses prescriptive and static definition. The presenter likened it to the collaborative approach recently taken up by scientists, where particle physicists (quantum theory and the science of the very small) and astrophysicists (relativity and the science of the great expanses) now collaborate, recognizing and appreciating the different 'logics' of both worlds. He said that the associative approach to understanding economics deliberately takes into account other 'schools of thought' in order to find common ground leading to a conscious, cooperative and productive revised view of the nature of economic life. He also stressed the idea that it is the individual human being that is the true agent of modern economic life and not the market or the state. I think he is trying to say that we all need to become 'economists' of sorts, considering that economic life is now the shared responsibility of all human beings.

The human being, he declared, can be both self-interested as well as show genuine interest in others. Even monetarily, we are citizens of two worlds, as it is possible to consider the other side of a transaction – thinking and acting on behalf of others – an enlarged and more 'symmetrical' view of the capabilities of human beings. He ended his brief description of associative economics by identifying the three sub-systems of our common social life and pointing to the need for them to be recognized on their own terms, yet each being understood in relationship to the other. What three? The cultural life comprises all we do to develop our capacities and talents, while the life of ‘rights’ between us includes politics, and economic life as the arena where we express our skills meeting each other needs in order to exist and thrive. Something like that.

In order to prepare the group for the audio story about how Brazil overcame their decades of money issues, Daniel used his recently acquired school ‘blackboard’ to sketch an image of the relationship between cash and credit. It is a critical concept from Finance at the Threshold: Rethinking the Real and Financial Economies. The real or ‘physical’ economy is related to CASH while the ever-growing financial economy is connected to the creation of CREDIT. He drew a horizontal line from cash on the left side moving across to credit on the far right where the arrow ended, indicating the notion that cash deposits, with its multiplier effect, cause and creates credit. Credit as a sub-set of cash. Below that he made the same sketch except the arrow pointed the other way, from credit to cash, indicating that it is possible to have the process work the other way; where over-heated credit creation can inflate the amount of cash. The point being that both are possible where cash and credit, each with their own characteristics, have a reflexive relationship that has to be taken into account for a true image of the process. I guess that is where he is going with this symmetry concept and why it is important to appreciate both logics and the possibility of resolving the polarity.

The last blackboard sketch had the ‘means of exchange’ (MX) on the left side (cash) and ‘store of value’ on the right side (credit) with a category called ‘unit of account’ (UA) in the middle and above the other two. As it turned out, the unit of account played a large role in reestablishing the efficacy of the trade currency (MX) for the Brazilian economy in the remarkable audio piece that we all then listened to as a group. It was astounding to learn how establishing confidence in an idea a denomination (UA) can serve to balance the relationship between the two kinds of money, the physical economy and the financial economy. In Brazil’s case it was the means of exchange money that was stabilized.
On July 14th at Coffee Catz in Sebastopol, Associative Economics Café # 13 will feature a story about the Federal Reserve and how they attempted to balance the ‘store of value’ (SV) or capital.

Guest Review by Craig Van Horn for:

Last weeks Science Buzz Cafe # 173 (Associative economics Cafe 12)
Last week Daniel Osmer led the group on an introduction to the wacky and somewhat imaginary world of money. He described the standard functions of money and then played a radio script about the Brazilian inflationary experience of the decades before the early 1990's. You think you remember inflation in the ‘70’s? Our experience with inflation was just a taste of what the Brazilians endured. INFLATION there reached 80% per *month*. Supermarket items were repriced daily. Merely the task of keeping track of the constantly moving prices and wages became an additional burden on commerce.   And the government couldn't stop it.

The whole thing had started much earlier, when Brazil's government elected to finance the immensely expensive construction of its new capitol by issuing excessive amounts of currency (the Real), but even when the printing presses were turned off, inflation continued unabated. The usual political expedients were rolled out by the usual fools - wage and price controls! With predictable results; goods and services dried up, retail shelves were bare, a black market flourished! The whole society was now conditioned to *expect* inflation.

The story concerned how a group of (conventional) economists and college drinking buddies saved the economy by a radical solution. They introduced a virtual currency - the URV (Unit of Real Value)! A currency which was never issued by the government, not printed, and not used as a medium of exchange - but each day the treasury would adjust the damn thing so that prices stayed the same, priced in URV's. It was very convenient. People began to depend on the URV's as the virtual unit for pricing goods and services, but then checked the current exchange rate and *paid* with the old Cruzeiro Real's (CR$) which were still depreciating daily. Papers advertised the specials in URV's, contracts were negotiated in URV's. The new 'money standard' began to have the effect of gradually reducing the high inflation rate. And finally, when people gained confidence in the stability of the URV, the treasury began printing the new 'Real' (R$) as its new official currency. It was an economic miracle. Brazil's economy was saved by a trick; a 'virtual' currency was used to train Brazilian citizens to trust the old and the new issue of the Real. The virtual 'unit of account' stabilized the means of exchange printed money, the real, which was tied to the US dollar.

In another era, back in 1930 we reached the height of absurdity when people could no longer trade for their basic needs because there was 'not enough' of this fantasy substance! There were plenty of resources, fuel, timber, crops to harvest, available workers, but the economy shut down for lack of - an agreement. This was the other side of the coin, too little of this ephemeral fantasy stuff.

So ultimately, money is . . . sort of a fantasy, but it is one extraordinarily persistent fantasy, and we have learned that our collective expectations possess much more power than any government policy.

- Craig Van Horn

Φ