# Why is this recession so unique?

By Paul Ferguson, Published by News Beacon Ireland, 20th March 2012
(http://news-beacon-ireland.info/)

Despite the efforts of politicians and central bankers, economies around the world remain stubbornly resistant to significant growth. Tracing our use of digital money could provide a reason why.

Somewhat under the radar, essentially all of today's money exists as numbers on a computer screen. While this does enable many efficient methods of payments, digital money has different properties to cash, not all of which are beneficial to the economy.

For example, cash becomes a permanent inclusion in the economy's money supply. In contrast, digital money is only a temporary addition.

The transient nature of digital money can be determined when tracking a bank loan application to its final settlement. When processing an application the bank will investigate that it meets the many necessary criteria. Once approved, the bank will increase the borrower's current account without lowering any other account. Finally, as a loan is repaid both the debt and the borrower's account return to zero which is why there can be less money during a recession.

Apart from its impermanent nature, digital money has another property which can be undesirable in excess. Because digital money is only ever created through the loan process every digital euro has a corresponding debt.

Today's economy, in which every unit of currency exists in parallel with a debt, behaves quite differently to the economies of previous generations in which a substantial portion of the money supply was created publicly and issued debt free.

However this change to a fully digital currency has happened largely through arbitrary advances in our electronics payments systems and not through careful consideration by economists. Having been leapfrogged by the recent digital money phenomenon, it's no surprise the economics profession is advising traditional remedies to kick starting the economy to no avail.

Ending this recession will most likely happen through introducing a second source of digital money to complement or replace the first.

To demonstrate how difficult our kick starting efforts might be until such a change bear in mind that every euro has a corresponding debt and lowering the debt lowers the money supply by the same amount. Any new money required for growth will also come with a matching debt. Hence the conundrum of controlling excessive debt while maintaining an adequate money supply for trading.

The soul solution with bank credit as the only source of new money would be to dwarf the existing money supply through higher collective borrowing year on year. Indeed, the money supply across Europe has doubled about every decade since the 60s. Doubling every decade, or quadrupling every twenty years, growth in the money supply has been intense in recent decades. While this explains the apparent functionality of our system during this time it should be clear that such a surge is not possible again. The main reason for this is that mortgages, from which most of our money originates, now take two concurrent careers to repay and cannot increase further.

For the first time in history new money can only be borrowed into existence and there is no one willing or able to borrow any significant amount. Looking forward to the resolution of a very unique recession, there are many possible ways in which we could run our economy better.

One such proposal is that of Sensible Money's. It would involve a public organisation, most probably the Central Bank, gauging the need for money sufficient for trading within the economy. The Central Bank would monitor signs that more money was needed to facilitate business. Factors such as rising unemployment, inflation trends, increased credit card use, population growth, the velocity of money and so on could indicate an adjustment to the money supply was needed.

Once the required alteration was needed a new balance would be typed into the Government's bank account whereupon the money would be indistinguishable from that collected through taxes. This money would be the modern day equivalent of the regular debt free additions of cash that previous economies required. Replacing cash with its digital form is the easy bit. Controlling the creation of money by banks needs a bit more thought.

Perhaps the best way to do this is to define digital money as legal tender, as opposed to an agreement to pay legal tender upon request. From then on banks could only lend existing money and would have to attract the funds they need for lending. No longer could they increase a borrower's account without lowering another.

Attracting funds for lending would be satisfied through the demographics of the country. A portion of the population would always be saving and assure the funds for would-be entrepreneurs. Inflation would be controlled through the permanency of the money supply. At present our money is regularly deleted through loan repayments. However under the proposal the money supply would rarely be lowered overall alleviating the constant pressure for new money, which can ultimately lead to inflation.

The transition would involve removing current accounts from the balance sheets of the banks. Still managed by the banks as legal tender, these accounts would have no place as liabilities of the banks. Debtors would also be removed as assets of the bank and would temporarily be accounted for at the Central Bank. As loans agreed before the transition date are settled the money would be transferred to the Central Bank whereupon it would be removed from existence as a victim of the double entry bookkeeping system which happens under the present system.

Since the vast majority of our money exists as the mortgage holders agreement to repay, we could expect the transition to last not longer than thirty years. After such a time, the entire money supply would exist debt-free overall and, if we got it right, business would be held back by things other than an inadequate medium of exchange.

For more detail on this proposal please visit www.sensiblemoney.ie.

***Paul Ferguson*** *has a background in engineering and mathematics and graduated from Trinity College Dublin in 2005 with a first class honours degree in both disciplines. He has studied economics informally for the last three years when there appeared to be a lack of understanding from economics graduates as to how there could be less money during a recession. He set up Sensible Money in January 2012 primarily to address the confusion over how digital money is created and by whom. Sensible Money is also promoting what they feel to be the optimum solution to the European debt crisis taking into account the many factors involved. He can be contacted via paul.ferguson@sensiblemoney.ie*