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by

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THE RELATION OF GOLD AND CREDIT TO PRICES WITH SPECIAL REFERENCE TO THE PERIOD OF THE GREAT WAR.

"Prices doubled in England and United States, trebled in Western Europe and increased ten to twenty fold in Russia. The result is, that the problem of the price level is, throughout the world, perhaps the greatest economic problem which the war has left."

The problem of the price level, although occasioning a vast amount of discussion and controversy is by no means a new phenomenon. At intervals during the last century, prices have risen to such a peak as to cause general alarm. At each period the public, as well as the leading economists of the day, attempted to account for such a rise, which resulted in a host of explanations more or less adequate.

However, upon the return to normal levels, the demand for solution became less imperative and under the stress of new troubles the problem became temporarily relegated as a subject of historical or academic interest.

The continuous and abrupt rise of prices from 1905 to the present has again brought the question into world wide prominence. The fact that the price level is so inextricably connected with such difficult problems as the wage adjustment, has made it a matter of universal concern. The uneducated as well as the scholar, the

business man, the housekeeper, the man with the fixed and precarious income, in fact all wage earners and spenders of income are demanding an immediate solution to this knotty problem.

Naturally from such a variety of investigators we would expect to find a vast range of analysis. Irving Fisher finds forty-one causes alleged and about an equal number of remedies prescribed. All aiming at a policy of economy and efficiency.

Possibly the chief obstacle to a clear logical investigation is that the great bulk of investigators are working under the fallacious assumption that one single cause is to be assigned, one single remedy applied and the problem is solved. But a consideration of the complex nature of society will at once show that the isolation of one cause is impossible.

The rise of prices in the twentieth century is the effect of a plurality of conflicting and assisting causes. Certainly this phenomenon connected as it is with the general economic and financial condition of all commercial countries of the civilized world, will not be explained by any such simple method.

It is only natural that the point of view from which an individual investigates any subject, is governed more or less by his occupation and his general interests. That is to say, those engaged in manufacturing are liable to

assign such causes as increased cost of production, freights, labor costs, risk or any other factors of production. Those again who are connected with monetary transactions might assign causes connected with our system of currency.

To facilitate the investigation all the causes may be placed in two groups. First those connected with commodities and second those connected with the currency. Since the rise in prices is manifested in the commodities themselves naturally the former group claims the first attention.

The report of investigation into the high prices made by the Confederation of Labor in Paris, declared the causes were to be found in quasi-monolopy of producers, the speculations of capitalists, tariffs, the eight hour day, etc. The problem is even prominent in political discussions, the opposition attributing the high prices and their evils to the extravagance of the party in power.

A bad harvest is a very popular explanation, but, though the rise in wheat may be connected with a bad harvest it cannot be ascribed to this for a period of any length, such as a persistent rise of over fifteen years.

As to increased demand due to such causes as scarcity under war conditions, this would account for the special rise in that particular commodity for which the demand is urgent. But we find a rise in the price of goods not used in war, such as diamonds, hemp, old coins, etc. That is to say, special causes working on selected commodities

will not explain a general change.

Those who attribute the cause to increased demand assume fallaciously that the demand for a commodity can be effective before there has been an increase in the supply of money and credit. Indeed, it would seem that this constitutes the main objection to all causes connected with commodities - this prevalent illusion that the demand can increase before the supply of money increases.

All those who offer such explanations as scarcity, monopolies, etc., look at the wrong side of the market, as Fisher states, "They seek the causes entirely in the commodities themselves, the price of which have changed, and not at all in the fold, the common measure in prices only expressed - due to the illusion that the price of gold is fixed - that the purchasing power of the dollar is a constant quantity."

It is evident that the causes connected with commodities offer in themselves no final satisfactory explanation for the rise in prices, and though we may not say that their influence is without its due effect, we cannot assign any dominating influence of prices to the commodities themselves, notwithstanding the undeniability of the fact that they have a temporary and special influence. For this reason we must seek the causes in the second group - those connected with monetary changes - and it would appear reasonable to expect that a consideration of the monetary conditions of currency and credit should

shed some light upon the fluctuations of prices. Particularly should this appear since the value of all commodities is expressed in terms of gold. A general rise in prices means a fall in the purchasing power of gold, and a fall in prices means an increase in its purchasing power.

Therefore, we will now proceed to investigate in more detail this second group of causes, i.e., money itself, and by a consideration of the price level and contemporary monetary conditions endeavor to arrive at some conclusions regarding the real relation of money to prices.

As a necessary preliminary it will be well to consider; firstly, the methods by which a number representative of the level of general prices is calculated and secondly, the significance of the word money. What is the meaning of the term and what are its functions?

The Index Number.

The index number performs an indispensable service in making an inquiry into the purchasing power of money. In the construction of this number a fairly representative list of articles must be taken, i.e., partially manufactured and partially raw materials. Any data on prices has always been hard to obtain, especially in the early days, and therefore the wholesale prices are taken in preference to retail. Allowance must be made too for differences in the quality of the commodity, and it was found necessary in

this connection to devise a system known as weighting, which gives due consideration to the degree of importance of different commodities.

With regard to the period over which this calculation is made, the years should include a time of depression as well as one of great speculation.

In arriving at the average the following four have been employed, namely, the arithmetic, geometric, the median and the harmonic.

A great many systems of the index number are before the public. Jevons was the first to show any scientific accuracy. His purpose was to discover the influence of the Australian and Californian gold on prices. The economist is practically a continuation of Jevons. Other reliable systems are those of Dr. Soetbeer, Sauerbeck and Bradstreet.

The index number does not pretend to be perfect in nice detail, but it is a most helpful instrument in many economic investigations. Another valuable feature is that these figures may be translated into curves, showing the trend of prices over a period of time, and thus comparisons may be made more easily.

The Function of Money.

To proceed then, to the question of the function of money. An exchange in primitive society was effected by barter. As commerce grew the use of currency became indispensable and metals were chosen for this purpose,

because of their durability and portability, and because of the fact that they could be subdivided without impairing the value. So, because of these characteristics money came to perform its function as a medium of exchange.

As a result of its universal acceptability, gold became naturally a standard of values, the measure of all contemporaneous values of all other commodities, the subjective want is expressed objectively in the amount of money offered for the gratification of that want.

Gold then, is a commodity in the same way that all other goods which constitute wealth are commodities; like them it performs a certain service to mankind. It is governed in the long run by the cost of its production, and its value is governed by the operation of the forces of demand and supply, i.e., the value of gold is determined by its utility and the limit of supply.

The natural consequence of it being the standard of value meant that it came to perform the function of a store of value. In connection with this it may be said that the miser who stores up gold is not wealthy, for gold is but one form of wealth and is of no value as mere gold. The mercantilists believed in the same fallacy also when they stated that gold is the essence of wealth. The fall of Spain is to be traced in great part to this same illusion, namely, their belief that gold in itself, is anything beyond a standard of exchange for necessary commodities. The detection of this error has brought us

to see that the amount of gold necessary is that which is just enough to carry on business transactions; any additional amount will decrease its demand and lower its value.

As a standard of value, the imperfection of the monetary system is made evident. This is especially noticeable in the case of deferred payments, where a great deal of injustice may be perpetrated, due to its fluctuations with time and place - to be a perfect medium of exchange it should possess absolute stability.

It differs from all other standards in this respect, the pund weight is a fixed mass, but the value of our monetary system is, to quote Layton, "The value of the gold sovereign is a human estimate which differs greatly in time and place." Its value can only be kept constant if its supply could be kept in the same ratio to the supply of commodities.

Early economists realized the instability of this standard and attempted to substitute labor notes as being a more stable means of determining values. The subject ever since, has been the cause of much speculation and thought. People in general, are under the illusion that gold is immutable and it is only a sudden jolt in prices brings the realization of its fluctuations home to them.

In answer to our next question - What is the meaning of money, it may be briefly stated that, although some regard money as metal only, the term is generally taken far