

THE
STATE THEORY
OF MONEY

BY

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AUTHOR'S PREFACE TO THE ENGLISH EDITION

The State Theory of Money appeared first in 1905; the 2nd edition followed in 1918, the 3rd in 1921, the 4th in 1923. Our translation is based on the 4th.

When the work had appeared in Germany, it was reviewed in England by Dr. J. Bonar in the *Economic Journal*, March 1922.¹ The somewhat unfamiliar features of the book could not have been more happily brought out than in this review.

Thereupon the Royal Economic Society determined to set on foot an English translation, in an abridged form. The work consists of four chapters, of which only the first three will be found here, translated with masterly exactness in spite of all difficulties. The fourth chapter contains the history of currency in England, France, Germany and Austria, as shown in the Contents. The author would not have advised this omission; but the ground is perhaps one of expense and lies in any case beyond his criticism.

Moreover, the same curtailment was made in

¹ Vol. xxxii, pp. 39-47. Mr. C. P. Sanger had reviewed it as early as June, 1906, in the *Economic Journal*, vol. xvi, pp 266-267.

the Japanese translation by Kiyozo Miyata, Tokio, 1922;—it might seem as if German writers laid greater stress on history than foreign writers.

In any case the author is grateful to the Society for carrying out the undertaking, doubtless at some sacrifice. In particular my thanks are due to Messrs. Keynes and Bonar, as well as to the honoured translator, Mrs. Lucas, and her adviser, Mr. Sanger.

G. F. KNAPP.

Darmstadt,
May 16th, 1924.

AUTHOR'S PREFACE TO THE FIRST GERMAN EDITION (1905)

I GAINED my earliest impressions as to currency questions in 1861 from a summer journey in the Tirol, where there was only paper money in circulation. I had my first teaching on the subject the following winter in Munich from Staatsrat von Hermann. My teacher was a well-informed and clear-sighted man, a silver metallist and an upholder of the theory that the use of paper money was based on credit. In the winter of 1862–63 his favourite subject was currency conditions in the United States, and I was again among his hearers.

When in Strassburg I myself began a small course of lectures on currency, I tried to keep theory in the background and to bring out clearly what is matter

of rule and ordinance¹ in the most important States, and I still think this heuristic method the best for lectures.

One of my pupils, Karl Helfferich, has far outstripped me in this art; for clearness of construction his works cannot be praised too highly. Another pupil, Philipp Kalkmann, by his studies on England, Holland and Switzerland, has greatly increased my knowledge. I would gladly have had him with me as an associate, had he not adopted another profession.

In the autumn of 1895, in a course of lectures in Berlin, I put forward my views fully for the first time, laying down: that the money of a State is not what is of compulsory general acceptance, but what is accepted at the public pay offices; and that the standard is not chosen for any properties of the metals, but for the deliberate purpose of influencing exchanges with the commercially important neighbouring States.

Soon after this Georg Simmel brought out his able book on the *Philosophy of Money* (Leipzig, 1900). As it treats only of the sociological side of currency, I do not need to regard my work as competing with his. I feel myself nearer to Otto Heyn, whose work (1894) is entitled *Paper Standard with a Gold Reserve for Foreign Trade* (Papierwährung mit Goldreserve für den Auslandsverkehr). It was a book that appealed to public men and deserved more attention

¹ *Das Pragmatische.*

than it received. For myself, I came to give up any attempt to influence public men, and I give the first place to the theory or philosophy of the subject, at the risk of displeasing both schools of monometallists, not to speak of the bimetallicists, who will not be any better satisfied.

On the other hand, I hope for the approval and perhaps the help of those who take the monetary system (or, better, the whole system of payments) to be a branch of political science. I hold the attempt to deduce it without the idea of a State to be not only out of date, but even absurd, however widely these views may still obtain. To avoid polemics, I have always called this the metallistic view, and have opposed metallism as such without naming its supporters, and also without opposing the use of metal.

I began to develop the State Theory of Money in September 1901, and I dare not confess how many false starts I made. A theory must be pushed to extremes or it is valueless. The practical man can, nay, must, content himself with half-truths. The theorist who stops short at half-truths is lost.

In order to attain my end and replace the metallistic view by one founded on Political Science, I was forced to invent a terminology of my own. Even if new expressions could have been formed in German, it seemed important that in this branch of science, which has nothing national in it, terms should be found that could go easily into any language, as being

erudite rather than popular.¹ I have renounced the advantages of a pleasing style to obtain the greater advantage of scientific treatment. My aim is with clearness and certainty to reconstruct the ideas at the bottom of the prevailing rules and ordinances about money.

I am sorry that I am not able to enter into the merits of my predecessors, Richard Hildebrand, Ignaz Gruber, Karl Knies, Lexis and Bamberger, and many others. To write a full literature of the subject would be a special historical work in itself.

I am making a first sketch, which others must complete.

My heaviest debt is to G. Th. Fechner, who never wrote a line on currency, and indeed knew nothing about it. From him, for example, from his little book on the Soul,² we learn how to distinguish the essential from the accidental, and, if anyone says that my own aim has been to discover the soul of money, well, so be it.

Strassburg,
July 5th, 1905.

¹ They will be found to be usually Greek, occasionally Latin, as in Chemistry and Botany (Tr.).

² *Ueber die Seelenfrage*, Leipzig, 1861.

NOTE BY TRANSLATORS

THE present is an abridged version of Prof. Knapp's book. For reasons of cost the translation has been confined for the present to the theoretical part; and Prof. Knapp's illustrations have been considerably abridged, while every effort has been made to preserve his essential arguments.

To show the scope of the whole book, translated and untranslated, we have given the "Contents" in the complete form, including Chapter IV and the Appendices, which are here omitted.

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piece should be valid. From the two together follows the *specific* content of the piece.

If the law lays it down that a certain metal may be physically converted into money *without limit*, this is a *genetic* relation between money and metal. We call this metal *hylie*. The *hylogenic* norm lays down how many units of value in money are to be produced from a unit of weight of the given metal. If this conversion takes place by means of free coinage, and if the content of the piece answers to the norm, we have *specie* money. All other is *notal*, whether coins or paper money pure and simple.

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In accordance with the regulations as to legal tender, money is divided into *current money*, purely *facultative* money, and *small change money*. There must be at least one *definitive* kind of money, *i. e.* which the creditor must take without being legally entitled to receive other kinds of money for it. There are also provisional kinds of money, legally convertible into definitive money.

The definitive kind of money which the State chooses as final for its own payments and makes compulsory in dubious cases, is called *valuta* money. All other kinds of money are called *accessory*. The *valuta* money is the "standard," in the narrower sense of the word.

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¹ Not here translated.

- 19a. *Austria, 1857–1892.*
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- § 19c. *Customs Payments in Austria, 1854–1900.*
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¹ Not here translated.

voluntary specie payment. No question of conversion of notes into gold. Further details as to the regulation of the inter-valuation exchange with the Western countries.

§ 20. "Value of Money" and Prices.

"Value" always implies a comparison, and in the particular object compared with it we have an expression for the value of money. These different forms of expression are mutually independent, cannot be interchanged, and still less be regarded as one. Money can also be compared with groups of commodities, but the composition of the group must be agreed upon. Index-numbers are a welcome indication of the alterations in price of the goods contained in the group. Other groups would give other index-numbers. There are always alterations in price, due to the condition of the market. They should not be explained as showing that the value of money has altered in the opposite direction, for that would be merely tautology. As to the value of money, price statistics a help, but need an interpreter. In the case of income, "producers" or "consumers" differently affected by price alterations. Alterations in price not alterations of the "validity" of a piece. The State Theory of Money to be kept separate from economic reflections on Money.

THE STATE THEORY OF MONEY

CHAPTER I

PAYMENT, MONEY AND METAL

§ 1. *Autometallism ; Nominality of the Unit of Value*

MONEY is a creature of law. A theory of money must therefore deal with legal history.

The favourite form of money is specie. As this implies coins, most writers have concluded that currency can be deduced from numismatics. This is a great mistake. The numismatist usually knows nothing of currency, for he has only to deal with its dead body; he has no ready way to the understanding of paper money pure and simple. It may be a dubious and even dangerous sort of money, but even the worst sort must be included in the theory. Money it must be, in order to be bad money.

Nothing is further from our wishes than to seem to recommend paper money pure and simple in such a form, for instance, as the Austrian State Notes of 1866. It is well for any State to wish to keep to specie money and to have the power to do so. And I know no reason why under normal circumstances we should depart from the gold standard. I say this at once to reassure the public man. Still, in this book

the silver standard too is carefully studied, and we have paid more attention to paper money than has been its lot hitherto. For on close consideration it appears that in this dubious form of "degenerate" money lies the clue to the nature of money, paradoxical as this may at first sound. The soul of currency is not in the material of the pieces, but in the legal ordinances which regulate their use.

All money, whether of metal or of paper, is only a special case of the means of payment in general. In legal history the concept of the means of payment is gradually evolved, beginning from simple forms and proceeding to the more complex. There are means of payment which are not yet money; then those which are money; later still those which have ceased to be money.

What then is a means of payment? Is there a wider concept under which means of payment can be subsumed?

Usually, "means of payment" are explained by recourse to the concept "exchange-commodity," which presupposes the concepts "commodity" and "exchange."

In defining one must start from some fixed point. We will venture to regard "commodity" and "exchange" as sufficiently elementary ideas.

If we assert, "Every means of payment is an exchange commodity," we are altogether wrong, for in the course of history we meet with means of

payment which are not in any way commodities of exchange in the proper sense of the term. "Exchange-commodity" is therefore not the wider concept we are seeking.

If, however, we say conversely, "Every exchange-commodity is a means of payment," we have not got what we wanted. There are exchange-commodities which are not means of payment.

If one man exchanges corn for another's silver, the silver is an exchange-commodity for the one, corn an exchange-commodity for the other, within this one transaction.

In this wide sense the concept "Exchange-commodity" does not yet serve our purpose; it remains uncertain whether the exchange-commodity is a means of payment. And this cannot be asserted either of silver or of corn, so long as we look only to one transaction.

When, however, in any society, for example, a State, it is a custom gradually recognised by law that all goods should be exchanged against definite quantities of a given commodity, *e. g.* silver, then in this instance silver has become an exchange-commodity in a narrower sense. It is called, therefore, within the range of its use, a general exchange-commodity. The general exchange-commodity is, accordingly, an institution of social intercourse; it is a commodity which has obtained a special use in society, first by custom, then by law.

Such a "socially" recognised exchange-commodity is, of course, always a means of payment, and therefore is included in the concept "means of payment." On the other hand, it is untrue that every means of payment is a socially recognised exchange-commodity. It is indeed always socially recognised and also is always used for exchange; but it is questionable whether it is always a commodity. In order to be a commodity it must, in addition to its use in the manner provided by law, also be capable of a use in the world of art and industry, and this is not the case with all means of payment. The sheets of paper, which are all the eye of the craftsman sees in paper money, are an example of an object which has no other industrial use. They are therefore not an exchange-commodity, though they are a means of exchange.

The result of our considerations, cautiously stated as theory demands, is as follows. In the socially recognised exchange-commodity we have an instance of a means of payment, and therefore not its definition; it is only a special case of a means of payment, and that the simplest that can be imagined. Let us assume that this exchange-commodity consists of a metal—which is not absolutely necessary, but occurs in the most important case—we can then give a name to this simplest form of the means of payment; it is "autometallistic."

Autometallism views metal only as material and

gives no juristic consideration to the form of the pieces. The quantity of the material is measured in a merely physical manner; in the case of a metal, by weighing. The exchange-commodity is always weighed out to the creditor.

There is no difficulty in conceiving autometallism; the only difficulty is with those means of payment which are no longer autometallistic (*e. g.* money). We shall therefore use autometallism in order to show what is the distinguishing characteristic of the concept "means of payment." Let us put ourselves in the place of the creditor. A man receiving a pound of silver (or copper or gold) in exchange for commodities, which are not means of payment, can use it in two ways. Either he can use the silver in some craft to make vessels such as goblets or plates, or perhaps even rings and chains for ornament, or else he can use it as a means of exchange, and obtain with it other commodities as he needs them. The holder can make use of his property in one of these two ways, but not in both at once. He can either use it in some craft, thus obtaining "real" satisfaction, or else obtain other commodities with it, when his satisfaction is derived from its value in exchange.

The possibility of "real" satisfaction is undoubtedly a necessary condition for any commodity becoming a socially recognised exchange-commodity. If metals had not been indispensable in handicrafts, autometallism would never have arisen. But there

is "real" satisfaction in every commodity which is taken in exchange. A man who barter a sheep for wooden dishes, takes the dishes only because they give real satisfaction, *i. e.* because he can use them. But the dishes do not thereby become socially recognised exchange-commodities. The possibility of "real" use is therefore essential if a commodity (*e. g.* a metal) is to be chosen as a socially recognised exchange-commodity; but this property is insufficient to make it a means of payment.

With the satisfaction derived from exchange¹ the position is quite different. It is a necessary and sufficient property of every means of payment, and of the autometallistic in particular. A man who can employ the exchange-commodity he has received for some craft, but cannot pass it on in circulation, owns a commodity, but not a means of payment. For example, the owner of a pound of copper would be in this position if in his country silver was the autometallistic means of payment.

It is of the greatest importance that this should be borne in mind. Even in autometallism (the simplest form of a means of payment) it is first the possibility of employing it in exchange that gives it the property of becoming a means of payment. The possibility of "real" use does not produce this property, otherwise all goods would be already potentially means of payment, for they all have a technical use.

¹ "Circulatory satisfaction."

The use in exchange is a legal phenomenon. Even autometallism is therefore a legal form of the means of payment.

Let us not forget, however, that autometallism is only one instance of means of payment.

Whenever a material, measured in some physical manner, is used as a recognised exchange-commodity, we will call this form *authylic* (*hyle* meaning matter). Autometallism is only the most important example of *authylism*; and authylism itself is only one instance of a means of payment, an instance, namely, where the holder can choose between "real" satisfaction and "circulatory."

What then is a means of payment? A movable object which can in any case be used for circulation. This, however, is a mere general hint, and you will please note that "real" use should not come into the definition. It would be equally wrong either to demand or to exclude it.

It is difficult to give a correct definition of a means of payment, just as in mathematics we cannot say what a line or a number is, or in zoology define an animal. Often the simplest case (straight line, positive integer) is taken, and one can then proceed to widen the concept, at first recognised in a given example.

Suppose we said, "A means of payment is a movable thing which has the legal property of being the bearer of units of value," this would be exactly what we mean.

But let us not give this as a definition, for it would assume "unit of value" as a self-evident notion, which it is far from being.

Let us say no more than is absolutely necessary for our purpose. First, the unit of value is nothing but the unit in which the amount of the payment is expressed. Every traveller entering a new country asks the name of this unit—whether accounts are in marks, francs, crowns or sterling. When this question is answered, the traveller asks what the usual means of payment look like and what they are worth in the unit of that country. He is then in a position to make payments himself. We see that the unit of value has everywhere a name which in some countries has remained unaltered for centuries (pound sterling), while in others (*e. g.* Austria) it has been deliberately changed (to krone since 1892). In any case there is a name, and the question is now what it means.

Can it be defined according to its technical use (that is, use in a craft)? For example, a mark is the $\frac{1}{139.5}$ th part of a pound of gold. The metallists would so define it.

Or is it absolutely impossible to define by technical use? If so, in what other way are we to define? This is the task of the nominalists.

The metallists tell us we can only speak of the value of a commodity by comparison with another commodity. A man purchasing a commodity says how much of another commodity he is prepared to spend

on it. A man selling a commodity says how much of another commodity he will take for it. Each time the equivalent is mentioned for comparison, so that the idea of the value may have only one meaning. It is equally clear here that the value is a fact which cannot be determined by observation, but rests on an agreement. A third person can, of course, observe what an object is worth, but only by observing the agreement of the buyers and sellers. If the commodity used for comparison is not expressly named, the value of an object then means the *lytric* value, that is, the value that results from a comparison with the universally recognised means of exchange. From this, again, it follows that we cannot in this sense speak of the value of the means of exchange itself. Only those commodities have lytric value which are not themselves means of exchange.

The metallist always conceives a means of exchange to be an exchange-commodity.

All these propositions are indubitably correct. It follows that the concept of lytric value can only arise from a comparison with a generally recognised exchange-commodity, which, as we have seen, is always the simplest form of the means of payment.

But there are means of payment which extend beyond this simple form, namely, those which are not commodities except in so far as law makes them so. The most important case is real genuine paper money. The name of the unit of value (*e. g.* gulden,

in Austria) continues to exist, but it is no longer possible to give it a technical definition such as "a gulden is the $\frac{1}{45}$ th part of a pound of silver," for it is plain to anyone that this is indeed a definition of a gulden of sorts, not of that gulden in which payments are made, but of a kind of gulden in which no one pays. What we must define is the unit of the customary means of payment, and this is impossible for the metallist in the case before us.

We have now reached the point where opinions differ. As long as autometallism prevails, the technical definition of the unit of value can be quietly accepted, at any rate as long as the metal once chosen is retained unaltered. The man in the street is, however (in secret and quite unconsciously), of the opinion that we still have autometallism, only slightly altered and rendered more convenient by coining. Hence the wide acceptance of the view that we can define the unit of value as a given quantity of metal.

The natural man is a metallist; the theorist, on the other hand, is forced to become a nominalist, because it is not always possible to define the unit of value as a given quantity of metal.

It cannot be done in the instance, already mentioned, of genuine paper money. Another fact, however, is more astonishing—it cannot be done at all when the means of payment are money, which is not yet the case with autometallism. But the strangest fact of all is this. Even in the case of autometallism, as soon as another

metal is chosen, the concept of the unit of value becomes independent of the former metal, *i. e.* technically independent of it. For the unit of value is always a historical concept.

The fact of the existence of debts gives the reason why it is not always possible to define the unit of value technically, but is always possible to define it historically.

Our theorists are inclined to think of payment as immediate; the craftsman supposes that coin is handed over in exchange for a given weight of silver. But, if payment has not been made on the spot, there are certain permanent obligations to pay, that is, debts. The State, as the maintainer of law, adopts a definite attitude to this phenomenon, which is not technical but juristic. Through its Courts of Law the State gives a right of action for debt. We are speaking here only of debts which are expressed in units of value (sterling, marks, roubles), yet not merely of those under the ruling monetary system, but of lytric debts generally, so that in times of autometallism we include debts expressed in pounds of copper or pounds of silver.

Debts which are expressed in units of value and are discharged with a means of payment (*lytron*) will be called *lytric* debts.

In what then does a lytric debt consist—especially in the case of autometallism, and, more generally, in the case of authylism?

