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292 "The Neapolitan, Ferdinando Galiani (1728-87), a typical eighteenth century abbe, sparkling with esprit, did for his time what Montanari did for the seventeenth century and and Davanzati for the sixteenth, century in his treatise Della moneta (1751)... One point about his work must be emphasized before we tear ourselves away from one of the ablest minds that ever became active in our field: he was the one eighteenth century economist who always insisted on the variability of man and on the relativity, to time and place, of all policies; the one who was completely free from the paralyzing belief -- that then crept over the intellectual life of Europe -- in practical principles that claim universal validity; who saw that a policy that was rational in France at a given time might be quite irrational at the same time in Naples...; and who properly despised all types of political doctrinaires, including the physiocrats.

319 Richard Cantillon (1680?-1734 p. 217). [318: ".. a strictly metallist conception of money invited, if it did not absolutely enforce, the attempt to draw a sharp dividing line between money and the legal instruments that embody claims to money and operations in money, and to bring the latter into the picture by means OF AUXILIARY CONSTRUCTIONS for which the legal concepts alluded to above offered suggestions...]

The auxiliary construction that is needed consists in an extension of the concept of velocity. The banker who issues notes in excess of his cash holding is not thought of creating or increasing means of payment, let alone 'money.' All he does is increase the velocity of that cash, which by proxy, as it were, effects many more payments than it could settle by going from hand to hand, and the same applies, of course, when he directly lends part of the cash deposited with him. The clear perception of the truth that a bank note and a checking deposit are fundamentally the same thing is in fact one of the strong points of this theory....

The outstanding authority for this theory is Cantillon, who carried it out in detail with as much common sense as brilliance. His bankers are essentially intermediary lenders of other people's money. They lend the deposits they receive , and by doing so they speed things up and lower the rate of interest. The logcal difficulties that lurk in this apparently simple statement are somewhat reduced by his emphasis upon the case in which bankers only lend what depositors, for the time being, do not need -- the case of time deposits, we should say -- so that a given sum of money only does one service at a time...

321 John Law [1671-1729 HEA 294] Ancestor of the Idea of a Managed Currency. A reconstruction of his thought as follows: The use of a commodity as a medium of exchange affects its value. This increment is distinct from the intrinsic value of the commodity, and the intrinsic value does not explain it. Money is not the value for which things are exchanged, but the value by which they are exchanged.

What has no intrinsic value of its own can have the value of the medium of exchange, viz., the value of what it buys.

~~477 .2. But there was something else [else where]~~

HEA 329: ".. Molina's pithy saying that 'money is the tool of the merchant's trade.'"

Ibid. ".. if I have caught his (Locke's) meaning... Again interest is a price for money lent. But the supply on the money market must be seen in relation to the debt situation and the state of trade -- high profits raising, low profits reducing, the rate. ... at a push, this may be interpreted as an embryonic form of of what is now known as the Swedish loanable-funds theory: interest is explained and determined by a demand proceeding from expected profits and meeting a supply of 'loanable funds.'"

Ibid. Barbon "There are, as far as I know, only the most elusive indications of it before 1690, when Barbon (Discourse on Trade) wrote the momentous statement: ; 'Interest is commonly reckoned for money... but this is a mistake; for the interest is paid for Stock,' it is 'the Rent of Stock, and is the same as the Rent of Land; the first is the Rent of the Wrought or Artificial Stock; the latter of the Unwrought or Natural Stock.'

330 If the reader is to understand the history of interest theory during the nineteenth century, and some parts of it even during the first four decades on the twentieth, it is absolutely necessary to realize fully what this means. .. it was the decisive step toward the real analysis of the nineteenth century, according to which money was just a 'veil' that it was the business of analysis to lift, which is precisely the c nter of the analytic difficulties created by Real Analysis.

.. Thus we easily slip into a position that may be characterized by the equivalent propositions that the business firm reveives interest or the lender receives profit...

For the whole of the nineteenth century and beyond, this shifted the analytic
331 task from interest // 331 // to profit. With the partial exception of abstinence and psychological-discount theories, the phenomenon to be explained was the net surplus of business, which, in turn, was essentially a surplus arising from the use of an assemblage of certain physical goods, that this surplus, cleared of accessories such as compensation for trouble and risk, had to be handed to some other person...

It is not too much to say that this was to be the dominant feature of the theorist's general picture and even of economic sociology for everyone: the businessman became the capitalist. Fundamentally his income was income from ownership of goods, an impersonal return.

A. Smith substantially accepted this theory of interest and of the capitalist process. The nineteenth century in turn accepted it from him.

334 (In A Smith) Essentially, profit is profit of stock, and interest which goes to the capitalist employer is received for 'stock' (goods) lent. Whether the stock be his own or borrowed from some other person, to supply the workmen with stock is the businessman's basic function. First and foremost, he is the capitalist and as capitalist he is the typical employer of labor...

N. B. 331 Barbon's Discourse, on this point at least, did not meet with success. The tract seems indeed to have been forgotten very soon Thus Barbon's fundamental idea remained in abeyance until 1750, when it was again expounded -- for all we know, independently rediscovered -- by (Joseph) Massie, whose analysis not only went further than Barbon's but also gathered force from its criticism of the views of Petty and Locke.

331 f Hume
332 f Turgot (1727-81) HEA 243-49 life sketch; 1227 f.
333 A Smith stereotyped the situation, dropped the most promising suggestions made by Hume, Turgot, Locke, so that his successors started from a formulation that was much more Barbonian than any of these writers...

HEA MONEY

62f Functions: medium of exchange, measure of value, store of value, standard of deferred payments.

297 1087f Further considerations

277 Real analysis proceeds from the principle that all the essential of economic life are capable of being described in terms of goods and services, of decisions about them, and of relations between them. This device can get out of order, and if it does it will indeed produce phenomena that are specifically attributable to its modus operandi. But so long as it functions normally, it does not affect the economic process, which behaves in the same way it would in a barter economy. Hence, money is said to be neutral, a garb, a veil... so that money prices must give way to exchange ratios between commodities, which are the really important thing. Moreover, savings and investment come to be conceived as saving some real factos and their conversion into real capital goods (buildings, machines, materials) that are 'really' lent when industrial borrower arranges for a loan.

Monetary Analysis means denial of the proposition that apart from disorders the element of money is of secondary importance in the explanation of the economic process of reality...
278 The reader should observe however (in explaining exceptions) without becom_ing aware that the monetary processes that account for disturbances do not cease to act even in the most normal normal course of economic life. We are thus led step by step to admit monetary elements into Real Analysis and to doubt that money can ever be 'neutral' in any meaningful sense. Monetary introduces the element of money on the very ground floor of our analytic structure and abandons the idea that all essential features of economic life can be represented by a barter-economy model.

Monetary analysis and macroanalysis. Moneary analysis means in addition Aggregative or Macroanalysis, i. e., attempts by analysis to reduce the variables of the economic system to a small number of social aggregates (total income, total consumption, total investment, etc.).
Since the alliance of the monetary approach runs through the the whole history of the monetary analysis, we shall hence forth restrict this term to analysis in terms of aggregates -- mainly
279/ as we have seen in our study of the tableau,/streams of expenditure. It was pointed out there that analysis of this type does not do away with real analysis, but only confines it to the description of the bahavior of individual households and individual households and individual firms.
Investment as a social total is the algebraic sum of a great many individual -- positive or negative -- investments. Monetary Analysis leaves the explanation of these to the theory of individual households and firms, and concerns itself only with that algebraic sum on the hypothesis that this is all that matters for the economic process as a whole... But it can be proved that this hypothesis need not be true (the sum might be zero, INVESTMENTS MIGHT BE COMPLEMENTARY OR COMPETITIve, etc.)

280 (b) Monetary Analysis and Views on Spending and Saving. .. Monetary Analysis is associated, not by necessity but nevertheless closely, with a characteristic set of views about Spending and Saving and, in connection with them, about monetary and fiscal policy. In fact, as soon as we see the economic process -- primarily or exclusively -- as a system of streams of expenditures, we shall be tempted to expect all sorts of distrubances from any obstuction to the even flow of these streams and, vice versa, to attribute any disturbance we observe in the economic process tosuch obstructions -- as at least a roximate cause. The way in which households and firms handle their money and react to monetary magnitudes will then acquire importance independently of the commodity aspect of their actions.... Thus monetary analysis not only qualifies as a too for economists who are 'spenders' and 'anti-savers' independently of any theory but also tends to produce in the minds of its votaries the 'spending' and 'anti-saving attitude by focusing attention on the process of generating monetary income behind which everything else disappears from sight.

Having cleared the ground we must now follow the fortunes of Real and //
281 Monetary Analysis during the epoch under consideration. Let us face at once the chief difficulty of this task. It arises from the circumstance that we meet the ideas, underlying or associated with, Monetary Analysis, as it were, on two levels -- on a prescientific and on a scientific one. Ever since wages began to be paid in money, every servant girl has felt that all would be well if only her employers spent their money freely enough, and ever since trading began to mean taking in money, every trader has felt that he would be able to sell whatever it was he wished to sell, if only there were money enough or if the people who had it could be persuaded to part with it. With exceptions that prove the rule -- in nineteenth-century Europe they almost ousted the rule -- this is and always has been a major item in the economics of the man in the street who never really believed in the gospel of thrift even when he paid lip service to it. The first thing that analytic effort does is to dispel some of these monetary illusions. But other analyic efforts keep on creating and re-creating a Monetary Analysis on a scientific level which is sometimes just as successful in its attacks upon Real Analysis as the latter has been upon those 'popular prejudices.' These two levels, however, are not unconnected, and this where the historian's trouble comes in. On the one hand, popular sentiments about money and spending proved invincible. They always survived and always manifested themselves in a literary current that ran sometimes outside and sometimes inside of 'recognized' economics. And they always lent powerful support to attempts to establish Monetary Analysis on a scientific level: just as the popular success of socialist arguments forged by trained economists is not due to their scientific merits but to the fact that they fall in with cravings of the human heart that defy rational foundation abd therefore are likely, particularly in times of stress, to be greeted with a sigh of relief.

The most effective propositions of Monetary Analysis are, in fact, those in which the public is able to discover a pointer toward the easy way out of difficulties and which bear a family likeness to what growling professionals call popular errors. On the other hand, these popular prejudices, like others, contain certain elements of scientifically provable truth so that association with themdoes not constitute a *prima facie* case for rejecting scientific Monetary Analysis. However the exponents of Real Analysis thought that it did: not only did they neglect those elements of truth, to the disadvantage of their own teaching, but they also used the opportunity in order to repres-

281 ent the results of Monetary Analysis simply as new versions of what
were indubitably popular fallacies. Later on, whenever they were in
a position to do so, the votaries of Monetary Analysis responded in
kind, the more zealously so because, in part, they actually did serve
up exploded error in new dressing. No indictment of subjective hon-
esty is intended. Such mix-ups will, however, arise as long as econ-
mists continue to analyze with an eye on practical programs they wish //
282 ro recommend or to combat, as most of them did and do.... However,
we shall now try, as far as seems possible, to straighten out the
tangle, first, in visualizing some broad contours of doctrinal develop-
ment and, second, by mentioning a few representative names.

The history of economic analysis begins with real analysis in poss-
ession of the field. Aristotle and the scholastic doctors all adhered
to it. This is perfectly understandable, for there was nothing to
ace them except the preanalytic sentiments of the public. But, as we
know, there is an important qualification to be made: they offered
monetary explanations for interest. Very roughly, this state of things
prevailed until the beginning of the seventeenth century. Again, the
history of economic analysis in the period under survey ends with a
victory for Real Analysis that was so complete as to put Monetary
Analysis practically out of court for well over a century, though one
or two efforts were made on its behalf in the court of scientific
econoomics, and though it continued to lead a lingering life outside
that court, in an 'underworld' of its own. The victory is also
understandable. It was of course greatly facilitated by vivid memor-
ies of monetary troubles -- medieval and more recent ones -- of spec-
tacular mismanagement of banking methods -- John Law's doings (p 321)
were still in everybody's mind -- and by the antagonism of 'mercan-
tilist' teachings. But powerful though they were, these factors
should not be overemphasized to the point of making us forget that
Real Analysis was also the result of of analytic advance and instrum-
emta in bringing about further advance.

283 (c) Interlude of Monetary Analysis (1600-1760): Becher, Boisguillebert,
and Quesnay. But between, say 1600 and 1760, there was an important
interlude of Monetary Analysis. The businessmen, civil servants,
and politicians, who then took up their pens, attended to the monet-
ary aspects of their troubles as a matter of course. They would as
more/ soon have doubted they got wet when it rained as that/money spelled
more profit and more employment, or that high prices were a boon, or
that high interest was just a nuisance. But though this literature
unmistakably took off from the preanalytic level of Monetary Analysis
and never quite lost contact with the servant girl's economics, it did
not stay there but eventually produced, barring technique, practically
everything that has come to the fore again during the thirties of this
century. Deferring consideration of the specifically 'mercantilist'
tenets and, for the moment, also of all other matters, we shall now
notice the emergence of Monetary Analysis in its most significant
sense, that is, in the sense of a theory of the economic process in
terms of expenditure flows. Though Quesnay's example suffices to show
that, in strict logic, it has nothing to do with protectionism, the
first document that presents such a theory with a clearness that is
beyond the possibility of doubt was a strongly 'mercantilist' tract,
Becher's Politische Discurs (1668). This tract contains the rudiments
of an analytic schema that turns upon people's expenditure on consump-
tion -- the prime mover or as Becher saidthe 'soul' of economic life.
In itself the observation that one man's expenditure is another's
income -- or that consumer expenditure generates income -- is as old
as it is trivial. But it can be turned into a principle of analysis
-- the principle that Quesnay, a century later, was to embody in his

283 tableau -- just as can the old and trivial observation and trival
observation that a body at rest remains at rest unless some external
force acts on it. We shall call it Becher's Principle, because he
seems to have been the first to realize its theoretical possibilities.
He did little to develop any system of monetary analysis and, of
course, left plenty for Lord Keynes to do....

284 It is not surprising that Becher found successors in Germany. The
German Consultant Administrators were far indeed from understanding
the analytic importance of his principle. But Monetary Analysis in
the sense defined works with concepts which, though actually very
abstract and indeed unrealistic, carry a surface meaning that is per-
fectly familiar to everyone. This surface meaning they absorbed
readily because it fitted in excellently with the rest of their
thought -- so much so that it is not even necessary to assume depend-
ence. Many of their diagnoses and recommendations may in fact be
co-ordinated and rationalized with reference to Becher's Principle.
Thus, many of them believed in the pivotal importance of high-level
mass consumption or, to put the same thing into their normative way
of expressing themselves, in measures that would stimulate mass con-
sumption. For some of them, Justi for example, this was the main
reason for putting so much emphasis on increase of population -- as
a means of expanding demand -- rather than the other way round.
Becher himself perceived the interaction of the two. His principle
was of course relevant, as it is today, to the appraisal of the
effects of high prices, saving, and luxury.

In England, neither Becher's Principle or anything losely related
was, / to it /as far as I know, explicitly formulated.... The French
literature offers, among others, the most noteworthy example of all
-- Boisguillebert's (Dissertation sur la nature des richesses, 216)
which is more interesting because, like Quesnay, he was in principle
a free-trader and laisser-faire advocate. He did not invoke state
management to secure the steady flow of monetary values (expenditures),
but on the contrary pointed out the state-made impediments to it:
the export duties, the internal barriers to trade, regulative inter-
ference with agriculture and manufactures, the vicious operations
of the most important direct tax, the taille -- all of which desolated
285 the countryside and impoverished the towns // because they restricted
consumers' expenditures. Also, while we look wage earners as the
most dependable spenders, Boisguillebert, in the social pattern of
his time, assigned this role to landowners. But these differences
serve only to emphasize the fundamental similarity both of his theory
and of his outlook upon practical problems with those of our own time.
Consumer expenditure was the active principle of economic life.
~~Boisguillebert in the social pattern of his time assigned this role~~
~~to landowners; while we look upon wage earners as the most~~
Equilibrium was an equilibrium of redciprocal demand, in terms of
money, of all groups, for the products and services of other groups;
it would realize itself only if every seller immediately became a
buyer. Anything that interfered with prompt expenditure on consumers'
goods would induce a fall in prices, hence a fall in incomes, then
in turn another fall in consumers' expenditure, and thus result in
cumulative deflation. Therefore his horror, never surpassed by
anyone's outside the United States Senate, of that worst if all
disasters -- cheap bread. With delightful naivete he warned physic-
ians, lawyers, actors, and so forth not to clamor for low prices
of agricultural products: by so doing they would be 'digging their
own graves'; for the landowners are .. intermediate spenders --
and in their income were reduced, they would [have to reduce their
spending on physicians, lawyers, actors, &c.]