Money is not wealth

The vast increase in government spending in response to the COVID-19 pandemic has caused many people to question their understanding of money. With any luck, such questioning will lead to a better understanding of money's proper function and its potential for abuse.

A common and understandable misconception is that money is wealth. After all, aren't people with a lot of money considered wealthy? However, while wealth and money are often found together, they are very different in their character and importance.

Wealth is in most respects more tangible and therefore easier to understand than money. Useful goods and services and, perhaps more crucially, the productive resources needed to create useful goods and services, are wealth. A loaf of bread is wealth, as are the farms, factories and human labour and ingenuity that are needed to grow and process the crops necessary to produce it.

Money, meanwhile, is best understood as a tool used to transform wealth from one form into another. For instance, your skills and ability to perform work are a form of wealth. So is the food you eat. The money paid to you in wages which you in turn pass along to the grocery store performs the simple yet crucial task of efficiently transforming your labour into food.

From this, it should be clear that the amount of wealth in an economy is much greater than the amount of money, as wealth only periodically and for a short time period turns into money before, usually, being turned into another form of wealth. To illustrate, imagine a small business owner who retires and sells their business. He or she is unlikely to keep the sale proceeds in their bank account or under their mattress. Instead, they will probably use the money to invest in other businesses (either directly or through the stock market) in order to generate income for their retirement. And, of course we all know that it seems like no time at all before our pay packets are transformed into food, housing, gasoline and the other necessities of life.

However, from the late 1990s the quantity of money in the economy has grown much faster than either wealth or economic output. Since the onset of the COVID-19 pandemic, this growth has accelerated enormously, even as economic lockdowns have caused output to fall.

Does this growth present any potential danger? The fact that we have not suffered from noticeable consumer price inflation has led to speculation that perhaps there is no limit to how much money governments can create to finance socially desirable objectives such as infrastructure renewal, a shift towards renewable energy or universal child care.

This thinking, though, makes the elementary mistake of mistaking money for wealth. Creating trillions of dollars of new money will not create the skilled labour or the other productive resources needed to achieve these ends, especially as in modern times most new money is created by banks issuing loans for property and other forms of speculation. Instead, at best it will simply direct wealth and productive resources away from those most able to use them wisely into the hands of those most likely to mismanage them. At worst, it threatens the viability of productive enterprises altogether.

To illustrate with an example, let's return to our small businessperson. If a large quantity of new money were to enter the economy during the time in which he sold up, the price of alternative forms of wealth would be sure to rise. Rising stock markets even amidst the economic wreckage

wrought by the pandemic and associated lockdowns are evidence of the impact of money creation on asset prices. Unfortunately for our retiree, his or her money, generated from the sale of real wealth, is now competing with newly-created money, created from nothing, to purchase income-generating assets. Their business wealth will not, therefore, be able to purchase as much wealth in other forms as would have been the case had new money not been created.

More troublingly, though, wealth is being reallocated away from a person who has demonstrated his or her ability to create and preserve wealth and towards people who, as well-connected insiders with access to unlimited sums of newly-created money, have every incentive to be reckless.

And so we have the situation now facing Canada and much of the rest of the developed world. Once-productive industrialized economies have, over the past 40 years, seen much of their wealth pass under the control of those large corporations, private equity and venture capital firms with privileged access to money. However, rather than using this money to invest in innovation and growth to create additional wealth, these new owners have chosen instead to loot the firms they control by compelling them to load up on debt in order to buy their own shares on the stock market.

While this has made both earnings per share and executive bonuses soar, it has also made firms more indebted and vulnerable to economic shocks as well as less innovative and productive. Wealth built up over decades has been squandered, and in the process income and wealth inequality have grown to such a degree as to threaten social stability.

As the insolvency specialist Roy Adkin put it in the documentary “Pandora’s Box - The League of Gentlemen” (directed by Adam Curtis): “The economists seem to think that the whole of the problems can be solved by money, by the use of money, rather than the creation of wealth. But they’ve never really got anywhere near it. So I would ask the question: Who’s money? What money? Where’s it coming from?”

Money is a tool. It performs a useful service when it facilitates the exchange of different forms of wealth. However, it is not wealth. Under our current monetary system, though, the power of money has grown to the point where it is no longer a servant of wealth but instead its master and destroyer. Given this, the continued and accelerated creation of money, while sold as a means by which we might create a better society, is more likely to lead us in precisely the opposite direction.