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The essence of inflation

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Abstract

When the supply of money increases and the supply of goods remains the same, inflation occurs. Thus, inflation is a monetary phenomenon. We discuss the essence of inflation in detail. An increase in money supply also affects the price structure, thereby creating winners and losers. The induced redistribution possibilities represent incentives for policymakers to manipulate monetary, fiscal, and regulatory conditions. However, citizens would benefit from the absence of credit and monetary manipulation. This explains why effective rules that limit discretionary monetary policy are relevant. We suggest that the market for central bankers should be opened to companies to foster competition and increase the credibility of stability-oriented monetary policy.

Keywords: Inflation, Competition, Market for monetary policy

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1. INTRODUCTION

High inflation has come back to the Western world, it is likely to stay for some time and its economic, societal, and political consequences are uncertain. Some policymakers and central bankers may have initially rejoiced when consumer prices started rising at the beginning of 2021. Many of them claimed that the phenomenon would be temporary and related to short lived, global supply-chain problems. When consumer prices rose even more in early 2022, the war in Ukraine became the new leading explanation for rising prices. Regrettably, explanations that attribute the cause of higher consumer prices to external factors tend to be popular in policy circles just like the belief that inflation is bound to vanish like magic. Such explanations and beliefs neglect central aspects of inflation and reveal an unwillingness to acknowledge past mistakes. Understandably, citizens are worried: consumer-price inflation dents their purchasing power, that is the amount of goods and services their current income stream or their accumulated wealth buys.

When markets are contestable, that is in a free-market context, prices are determined by the fact goods and services are in limited supply. Put differently, prices carry information regarding scarcity. When more money chases a constant amount of goods, money is relatively abundant, and goods are relatively scarce. Thus, prices for goods tend to rise. More generally, an excess of money can only have two fundamental causes that are not mutually exclusive: (1) Either production has dropped and too few goods are available for a constant amount of money, or (2) the supply of money has increased and the supply of goods has remained the same. In both cases, too much money is chasing too few goods and imbalances emerge. This is the essence of inflation. The imbalances and the associated loss of purchasing power come to an end once the rise in price levels eliminates the excess money balances people want to spend.

The present article discusses the essence of inflation in detail. Preferences are usually rather stable, the supply conditions for goods and services tend to adjust slowly, and

technologies steadily progress such that apart from unexpected, external supply shocks, the demand and supply for goods change only gradually. By contrast, monetary and fiscal policies as well as government regulation can change rapidly. Quick price increases are usually a consequence of these factors, rather than of changes in preferences or technology. Thus, policy in general and monetary policy in particular are key to understanding inflation.

In most cases, monetary and fiscal policies as well as regulation are influenced by politicians and their interest groups. This is because changes in these policies create winners and losers, that is, they offer redistribution possibilities. History shows that bullion convertibility (e.g., the gold standard), pegging to strong currencies, formal central bank independence and free capital movements (currency competition) are not sufficient to avoid monetary manipulation and discretion. Policymakers easily give up on metal standards and fixed exchange rates agreements if it suits their purposes. Moreover, central bankers' independence does not prevent collusion with policymakers or special interest groups. Competition between currencies could help to focus monetary policy on low inflation. Yet, competitive pressures are weakened by high transaction costs and policymakers do not hesitate to introduce capital controls in times of crisis. While citizens benefit from monetary stable conditions in the long-run, policymakers have incentives to manipulate monetary, fiscal and regulatory conditions and aim at centralized monetary intervention. By taking this fact as an unavoidable constraint, we argue for a new form of competition with a view to bringing monetary policy closer to the citizens' long-run interests. In particular, we suggest that the market for central bankers should be opened to companies and individuals regardless of their nationality.

In this light, section 2 examines the key mechanisms that generate price inflation, section 3 analyses the scope for taming monetary discretion and puts forward our own proposal in that direction. Section 4 concludes.

2. THE ESSENCE OF INFLATION

Money inflation, credit inflation and privileges

In most people's eyes, the term "inflation" identifies the proportional change in the consumer price index (CPI) or the proportional change in the prices of the goods and services produced in a given country, the so-called GDP deflator (e.g., Frisch 1977). The difference between the two measures relates to the fact that the GDP deflator includes the prices of what is produced but not consumed domestically (exports), while the CPI includes the prices of what is consumed domestically but produced abroad (imports). Political commentators usually (and mistakenly) measure the individuals' loss of purchasing power by referring to CPI inflation, while the real growth of production is (correctly) computed by taking into account the GDP deflator. Importantly, there are other categories of price inflation that exist next to CPI and the GDP deflator. For example, there are wholesale price indices, real estate price indices, asset price indices, among many others. These other prices may affect CPI or the GDP deflator with a time lag. In the end, which is the appropriate index that allows us to understand inflation? The short answer is "none of the above" (Colander 2014).

As recalled by Nussbaum (1943) and Bryan (1997), the term "inflation" originated in mid-19th century to define an expansion of the quantity of paper money in circulation without a corresponding increase in the metal deposits that guarantee full, that is 100%, convertibility. According to this definition, an increase in money without a corresponding increase in its collateral qualifies as inflation. Today's monetary regimes are not backed by metal deposits. But people expect to exchange their paper money against given baskets of goods and services. Hence, one may claim that in today's monetary regimes, increases in the money supply are inflationary if they do not go in tandem with the supply of those baskets.

Increases in the money supply are highly likely to generate differential changes in the prices of the various goods and services as well as in the individuals' incomes and stocks of

wealth (Hume 1742, Cantillon 1755). Thus, in most cases increases in the money supply create winners and losers and are linked to a mix of coercion and privileges related to political power.

The term “inflation” is also present in the notion of credit inflation (e.g., Nussbaum 1943), and refers to situations in which the monetary decision makers expand the supply of funds available to the credit market, possibly with a view to directing individuals’ behaviour within the so-called “business cycle”. It should be noted that these efforts are frequently ill-timed, and also interact with the political cycles, leading to so-called “political business cycles” (e.g. Nordhaus 1975). As a result, and not surprisingly, government action is frequently counterproductive and generates distortions that lead to an array of winners and losers.

The current debate on inflation tends to neglect the mechanism through which the cause (money and credit inflations) leads to the consequence (price inflation) and ignores that coercion is usually at the root of all (price-)inflationary episodes. Importantly, current explanations of inflation hide that inflationary episodes can be, and in fact have often been, purposefully designed to create winners and losers. Without proper analysis of coercion, political power and the role of interest groups in politics, many of today’s views of (price) inflation are at best useful exercises in descriptive statistics, but not much more than that.

Relative prices and changes in prices

When individuals are faced with inflation, the key issue is whether the compensation they obtain for employing one unit of their production capacity (for workers, it would be the wage rate) allows them to buy the amounts of goods and services they expect. Having the possibility of buying more is usually associated with more satisfaction. Likewise, individuals are also happier if less work effort is required to buy a basket of consumer goods that is at least as satisfactory as the basket they expect to buy. In both cases, we may say that the price of their consumption falls relative to the price of their labour. In other words, focusing on the price of a consumption basket per se is not so important: When an individual assesses his purchasing

power, he is not interested in finding out that the price of one unit of consumption or real estate is one dollar (or any other currency), unless he can express that dollar with his purchasing power, that is, with his income or wealth. At a country level, therefore, the relevant piece of information for the consumer is whether the CPI has changed relative to the GDP deflator, that is, whether the price of what individuals buy has risen or fallen relative to the price/remuneration those individuals get for devoting their time and skills to productive activities.

This line of reasoning helps to understand the so called “imported inflation”. *Ceteris paribus*, when the price of imports rises, the CPI increases relative to the GDP deflator. Put differently, the price of the value added produced in the country (GDP) falls relative to the price of the goods and services imported from abroad. This is what makes the country’s residents poorer.

A similar line of thinking applies to the intertemporal structure of expenditure, that is, one’s decisions to save, consume and produce. In this context, the interest rate is the price of transforming future revenues into today’s consumption. A drop in the interest rate encourages actors to increase their current expenditure and/or reduce their current working efforts, since current expenditure has become relatively cheaper. Consumers and producers borrow to buy more consumer goods and more machinery; and financial investors borrow to buy equity or real estate. Last but not least, lower interest rates affect governments who borrow more and expand public indebtedness. In the absence of active monetary policy and with constant preferences, the interest rate would be rather stable.

Changes in fundamentals that affect relative prices may easily offer seemingly justified opportunities for intervention. Suppose, for example, that individuals start fearing that their future income streams (or their pensions) will drop relative to the prices of the goods and services they plan to consume. They will most likely react by reducing their current consumption and/or increasing their working efforts to enhance their future purchasing power

by saving. The excess supply of value added reduces the relative price of current consumption, interest rates fall and the original equilibrium is restored. An inattentive observer might conclude that the drop in current consumption has provoked some sort of CPI deflation, and that more credit is needed. Yet, credit manipulation through active monetary policy would disrupt people's efforts to adapt to the new conditions, and lead to undesirable outcomes, that is, an intervention would be based on false premises and be unjustified.

The traditional views on price inflation

Expansionary monetary policy through the injection of additional money without a corresponding increase in the production of goods usually affects the price structure and thus relative prices. However, the traditional views on price inflation usually pay little attention to relative prices. These views are commonly known as the monetary, the demand-pull and the cost-push approaches.

a.) The monetary approach

The dominant version of the monetary approach links monetary inflation to price inflation, and claims that expansionary monetary policy affects all prices equally. It is assumed that new money falls from helicopters (Friedman 1969), and each individual picks it up only in proportion to his production or wealth. Since changes in relative prices are excluded, no real changes occur. Within this framework, money would thus be neutral.

Yet, this is not what usually happens when expansionary monetary policy is underway. Friedman's helicopters have pilots. Governmental decision makers and central bankers hardly ever ensure that the extra money ends up in everybody's pockets in neutral proportions and that all prices change equi-proportionally. Thus, and in contrast with the traditional monetarist narrative, winners and losers emerge, and real changes commonly occur. Put differently, politicians, central bankers and pressure groups have interests and may use monetary policy to fulfil them.

b.) Demand-pull inflation

A second popular view considers situations in which a rise in the aggregate demand for sets of goods and services brings about an increase in the price of those goods and services. When this phenomenon is broad enough, the price increases are termed demand-pull inflation. For example, this is often the consequence of an expansionary fiscal policy. Yet, such price increases happen at the expense of a decrease in the price of the goods and services that people no longer buy or of the assets that individuals sell to finance their new purchases. In this case, therefore, one may indeed observe CPI inflation, which is however offset by the falling price of assets. This also applies to debt-financed fiscal policy. If debt is financed by residents, these sell their assets or cut their consumption to buy treasury bills. If debt is financed by foreign investors, then the government is actually importing money and increasing the money supply. In the end, the outcome is the same: fiscal policy is not neutral and creates winners and losers.

Demand-pull inflation may also emerge when individuals decide to change the composition of their consumption basket. If they concentrate their demand on goods in short supply and no longer demand goods that were previously consumed, the CPI likely goes up and production falls for lack of buyers of a range of products. The conclusion is not that booming demand for selected goods leads to price inflation, but that the new structure of demand reduces the value of current production. Once again, too much money is chasing too few goods and, therefore, the relative price of money drops.

c.) Cost-push inflation

Finally, it may happen that key resources become scarce, and their prices rise. This is sometimes known as direct, cost-push CPI inflation. *Ceteris paribus*, this means that the price of one's value added has fallen relative to the price of those key resources.

It is possible that when people's purchasing power falls, some workers drop out of the labour force or prefer to stay unemployed or depend on the welfare state. Under such

circumstances, production suffers. As production suffers, for a constant amount of money too few goods are available and the relative price of money drops. Hence, the cause of price inflation is the fall in of production.

Thus, it is hard to uphold narratives about self-propelling price inflation, following which a drop in the workers' purchasing power encourages them to ask for higher wages, which in turn can increase the cost of production (i.e. indirect CPI inflation). Of course, self-propelling price inflation is possible when markets are not operating under competitive conditions: for example, when government sets minimum wages that are systematically above the level that would prevail under free markets conditions. Indeed, artificially high wage rates lead to distortions, that is unemployment. As unemployment rises, production falls causing prices to rise.

Manipulation and coercion

In a free market economy, CPI inflation is the outcome of spontaneous adjustments in the structure of relative prices. All mismatches of demand and supply create winners and losers. If no coercion applies and no actor enjoys privileges granted by political power, competition ensures that adjustments remunerate those better able to meet citizens' preferences and penalise those who fail to do so. Since a set of adjustments is a process, one can give opinions about the desirability of the outcomes, but general value judgements play no role.

Things are different when inflation is the outcome of deliberate actions executed by an authority with a view to creating or maintaining privileges for selected players: for example, specific groups of individuals, companies, governments. Under these circumstances, inflation alters the purchasing powers of selected groups of people and usually benefits the authority itself.

Inflationary policy-making resorts to two mechanisms: credit and monetary policies. Credit is created when a bank makes a portion of the depositors' money available to debtors,

who borrow to finance their expenditure in excess of their revenues. The extra expenditure then becomes part of somebody else's revenues, a portion of which is deposited and justifies another round of bank lending operations. In brief, the initial amount of deposited cash generates several rounds of lending, the size of which depends on the share of deposits that is lent out and on the share of revenues deposited in each round. Credit conditions depend on how much depositors trust their banks and their propensity to run a risk. In brief, it is all about credibility. For example, a bank that tends to select bad borrowers and exceeds in lending would not be the safest place to put your money, but it may be attractive if it offers high returns on deposits. The upshot is that all depends on the choices of the depositors, the quality of the bankers, the health of the economy. Excess credit kicks in when a bank gives away resources that borrowers fail to pay back. In a free market economy, adjustment is guaranteed as depositors and the banks' shareholders suffer losses due to their mistakes, depositors try to switch to better bankers, and some bankers go out of business. Manipulation occurs when the policymakers apply coercion and prevent spontaneous adjustments. For example, the authorities may force bankers to comply with given minimum reserve ratios or call for more or less stringent capital requirements. On the other hand, they can boost lending by subsidising or guaranteeing bad borrowers.

Monetary policy also creates winners and losers. Historically, currencies were made of metal or of paper notes for which the issuer would guarantee convertibility into metal (e.g. gold). Within this framework, therefore, monetary policy was possible but short lived: if the guarantor reneged on his promise to exchange banknotes for paper, the holders of the paper money would suffer losses, the issuer would lose credibility and his currency would be outcompeted by other currencies. By contrast, today's monetary systems feature inconvertible paper notes (or their digital equivalents) issued by a central authority. Thus, a monetary unit is used insofar as the government's promise to accept it as a means of payment remains credible. Since people need to interact with government and must use the prescribed currency in these

interactions, credibility is no major problem as long as the policymakers in government enjoy enough trust.

However, the policymakers are not benevolent dictators who try to maximise some kind of social welfare. They are vulnerable to pressure from interest groups and have incentives to influence markets by resorting to regulation and monetary policy. Their commitment to comply with the desires of the electorate is vague at best. While interventions are often presented as ways of protecting depositors and sometimes helping borrowers, markets are the best way to gather, reveal and distribute information (A. Smith 1776: IV.ii, §10, Hayek 1945) and select successful entrepreneurs. If policymakers really had better information than other market participants, their duty would consist in disseminating the information, rather coercing individuals. Moreover, appeals to an alleged social welfare function are deceitful (Condorcet 1785, Arrow 1950).

By increasing the money supply, a central bank can use the newly-created money to support preferred bond sellers (usually governments) who can thus rely on a generous, friendly and often obedient buyer. In particular, generosity comes in two forms. The presence of an actor ready to buy large quantities of selected bonds reduces the privileged debtors' cost of financing. Moreover, friendship can materialise in never asking the debtor to pay back his debt. In this case, debts are simply rolled over indefinitely. Not surprisingly, "rational mistakes" follow: for example, bankers no longer lend money to entrepreneurial borrowers and extend loans to unworthy counterparts who enjoy governmental guarantees and frequently hamper productive and innovative entrepreneurship. Thereby, regulation creates a class of privileged bankers and stifles competition in the banking industry, while the economy misses out on growth opportunities and misallocates resources to (bad) projects that would not be funded under normal circumstances.

The manipulation of the money supply generates privileges: sometimes to the benefit of "bad" bankers in need of cheap liquidity, most frequently to the benefit of highly indebted

governments. In this context, the alleged independence of the central banker is difficult to uphold in practice, especially given the fact that central bankers are chosen through political processes. Even when they are truly independent, their views and preferences likely mirror those of the politicians who choose them.

To conclude, price inflation is a monetary phenomenon. It is the consequence of monetary inflation and credit regulation, which in turn affects the money supply. Monetary inflation creates an excess supply of the means of payment, as a result of which money loses some of its purchasing power. Distortions and intervention in the credit market create inefficiencies, which generate a fall in production relative to the means of payment in circulation. Thus, monetary and credit inflation share two features that frequently go unnoticed. First, credit inflation often times feeds monetary inflation: the inefficiencies created by the former generate crises to which the government responds by increasing public expenditure. In the name of stability, monetary policy is loosened, leading to additional money supply to support higher expenditure. Second, manipulations in the credit and money markets are often processes through which selected actors obtain privileges. Citizens eventually pay the price.

3. IMPROVING MONETARY DECISION MAKING THROUGH COMPETITION

Rules for the monetary authorities

Injecting new money and regulating the credit and banking sector is appealing to policymakers and selected interest groups who eventually contribute to shaping it (Bofinger 2001). For example, export-oriented firms welcome monetary profligacy, since it leads to a weaker exchange rate. Never mind if the rise in domestic prices will later nullify the short-run exchange-rate benefit. The financial sector is also happy with regulation, which can become a powerful entry barrier against potential competitors. Bankers who made bad decisions profit

from bailouts. Finally, rising government expenditure gives politicians more leeway to satisfy special interests, especially when elections or political crises are round the corner and the range of potential beneficiaries widens.

A monetary policy that serves the interests of acting policymakers, firms or financial investors is usually volatile, expansionary, and short-term oriented. Little attention is de facto paid to long-term monetary stability and economic growth, which would be in the interest of citizens. As monetary policy is always driven by interests, manipulation will always occur (Mises 1949, chapter 31).

This explains why the economics profession has devoted considerable attention to shaping effective rules that would enhance monetary stability (e.g. Wicksell 1907 early last century or Taylor 2017 more recently). In particular, the debate on “Rules Rather than Discretion” (Kydland and Prescott 1977) emphasises the need to subject central bankers to a low-inflation straitjacket, lest they try to boost real output with expansionary policies. Since these efforts are anticipated by rational actors, they would bring about no benefits in terms of output, but would originate pernicious consequences in terms of price inflation (Barro and Gordon 1983).

The choice of the appropriate rules has focused on four main proposals: convertibility of the monetary unit into a metal, exchange rate anchoring to another currency, formal independence of central banks, currency competition. They all have theoretical and empirical shortcomings.

a.) Convertibility and fixed exchange rates

The obvious way to eliminate discretion consists in eliminating paper money and replacing it with commodity-based money. This is the essence, for example, of the gold standard, a regime according to which each monetary unit in circulation is made of gold or 100% backed by – and convertible on demand by the issuer into – gold. Since the entire

monetary system is based on the available quantity of gold (or another metal), this regime amounts to a loss of monetary policy autonomy.

A fixed exchange rates regime is a rule that commits a central bank to buying/selling unlimited quantities of its own currency vis-à-vis a given foreign currency. A slightly softer version consists in a commitment to buying/selling the domestic currency on the foreign-exchange markets to keep a constant exchange rate vis-à-vis a basket of currencies. If a central bank is committed to a fixed-exchange rule, it is effectively constrained by the monetary policy of its counterpart(s).

Thus, if convertibility into a metal or another currency could be upheld politically, such rules would credibly limit a central banker's discretion. However, policymakers have frequently reneged upon these rules, despite earlier solemn commitments. The main reason for so many broken promises is that these monetary regimes make it difficult to resort to "easy money" and solve political problems, especially in the presence of low growth, high unemployment, unexpected shocks or intense pressure by interest groups. True, real shocks require real adjustments, but monetary manipulation may postpone the cost of adjustment, and thus encourage well-organized groups or political rivals to raise their voice and ensure that the rules are weakened, and sometimes abandoned altogether: Metal standards were given up many times, fixed exchange rates under the Bretton Woods system lasted a comparatively short period of time and had to be sustained by widespread capital and foreign-exchange controls. Dollarization in Argentina, another type of fixed convertibility, was a flash in the pan.

b.) Independent central banks

What about cutting the cord between the central banker and the world of politics? Indeed, a relevant practice today is to have rule-guided central bankers. Two centuries ago, Ricardo (1824) wrote "It is said that Government could not be safely entrusted with the power of issuing paper money; that it would certainly abuse it; [...] But I propose to place this trust in the hands

of Commissioners, not removable from their official situation [...]” (pp. 10-11). Under representative democracy, central bank independence has the theoretical potential to guarantee monetary stability.

Nevertheless, as Ricardo was aware of (the Bank of England was a private bank until 1946), even a formally independent central bank can be influenced by the government and interest groups, especially when a central banker is appointed by policymakers with which the shortlisted candidates have presumably entertained good relations.

Moreover, a commitment to given rules is credible only if sanctioning mechanisms are in place and effective. Not surprisingly, these mechanisms are seldom present: Multi-level principal-agent relationships exist between voters, politicians and central bankers such that central bankers who act against the interests of the public at large cannot be easily and quickly identified. Moreover, it is not in the interest of the policymakers to dismiss central bankers that they themselves appointed, or open a public debate on the origins and nature of the banker’s bad performance. In brief, central bankers enjoy a great deal of discretionary leeway during their tenure and may pursue interests that are well beyond their mandate (de Haan, 2000).

The recent experience regarding inflation suggests that there is much room for interpretation of rules, and that the rules that supposedly tried to bind central bankers to low inflation turned out to be much softer than originally intended. The central bankers’ own ideas, and their connections with the world of politics and the main pressure groups are far more important than commitment to a rule. Put differently, “independence” does not correspond to an enforceable promise not to manipulate the money and credit market.

c.) Currency competition

Countries present different economic structures, traditions, and political institutions. This explains why unified policies do not work; and why monetary unions, currency boards or other common straitjackets are unlikely to last for long.

Some economists have disregarded the possibility that governments tie their own hands and throw away the key. Instead, they have argued in favour of currency competition and free banking, in hopes of replicating the results that characterise the markets for goods and services. If citizens demand low inflation – this is their line of reasoning – currency competition will force independent central banks to supply a currency that maintains its purchasing power (Klein 1974, Hayek 1976).

While intellectually appealing, the chances of realizing more competition between currencies are tiny. Klein himself pointed out that switching across many monies and many sets of prices involves substantial transaction costs. This explains why inertia is strong. Arguably, this should matter less in a world with where computers are ubiquitous, and the rise of cryptocurrencies may well prove to be a herald of free banking and competition of currencies.

A competitive market for good monetary policy

The discussion so far shows that the institutional approaches discussed in theory and implemented in practice with a view to enacting sound monetary policy have substantial shortcomings. While the future might see more currency competition, there is no doubt that today central bankers and policymakers are trying to keep out potential competitors and stick to centralised fiat money. The war on cryptocurrencies is the most evident example.

Thus, alternatives to rein in monetary manipulation are required. We propose establishing a competitive market for good monetary policy. The idea comes from the recognition that tampering with money results from individuals' action – in our case, central bankers and politicians. Currently, central bankers can only be individuals, while firms are not allowed to apply for the top job. This reduces competition among potential monetary decision makers. Trusting firms can have advantages over trusting individuals, since far less is known about the capabilities and goals of individual candidates than about firms or organizations. Moreover,

firms put their long-term reputation at stake and, therefore, have incentives to perform relatively well and comply with the rules set for a formally independent central bank. Performing well, that is ensuring monetary stability, enhances their reputation, makes them less vulnerable to organised interest groups, and enhances their position as candidates for future or concurrent central bank positions in general. While politicians may collude with individual central bankers and firms alike, collusion is less attractive for firms who need to be credible in the longer run. Importantly, firms (and individuals) should be able to present themselves to conduct monetary policy regardless of their residence or nationality.

Certainly, a competitive market for good monetary policy does not solve all incentive and agency problems. Policymakers will always try to intervene because monetary policy has the large potential to create different groups of winners and losers through inflation. However, once a market for good monetary policy is established, it is comparatively immune to interference. Moreover, even if policymakers withdrew their country from such a market and imposed new regulations, that is, if they chose more politically oriented central bankers, their change of tack would not lead to the large shocks that a sudden and surprising abandonment of fixed convertibility or the introduction of a parallel currency in a monetary union would bring about. Current competition between currencies would be supplemented by competition in the market for good monetary policy, and make excessive periods of inflation less likely.

4. SUMMARY AND CONCLUSIONS

Despite the current narrative, price inflation is a matter of relative prices: The purchasing power of the monetary unit drops when too much money chases scarce goods, services, land, financial assets, etc. Injecting new money to counteract the loss of purchasing power is useless and harmful. It is useless because you cannot create wealth by printing paper or digital money, and is harmful because monetary policy is a source of distortions. History shows that the policymakers seldom refrain from manipulating the credit and monetary markets. They resort

to easy credit to bail out overexposed commercial banks and uphold unsustainable level of public indebtedness, all of which is in their short-term interest. History also shows that policymakers can hardly resist the temptation to resort to inflationary policies to kick the can down the road to gather consensus and satisfy organised interest groups. International crisis often become welcome excuses to divert the blame for past mistakes.

Past attempts to introduce institutional rules to restrain abuse have failed. In the future, decentralised cryptocurrencies may have the potential to make central banking and monetary manipulation obsolete, but it is likely that policymakers will heavily regulate their use. To make present day monetary policy more stability-oriented, we suggest a different answer by increasing competition in the market for central bankers. This can be achieved by allowing companies to present themselves for the top job as central bankers instead of only individuals. A competitive market for good monetary policy and firms as central bankers would increase accountability and reduce the scope of collusion with the world politics widely understood. While our suggestion is no magic wand, it would be an improvement that is urgently required.

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