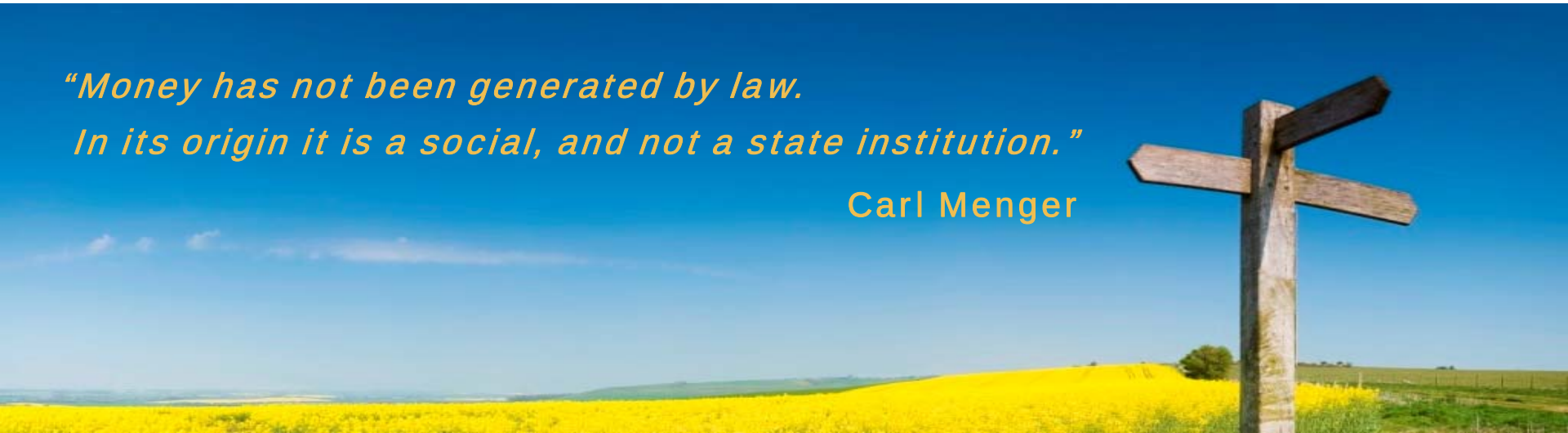
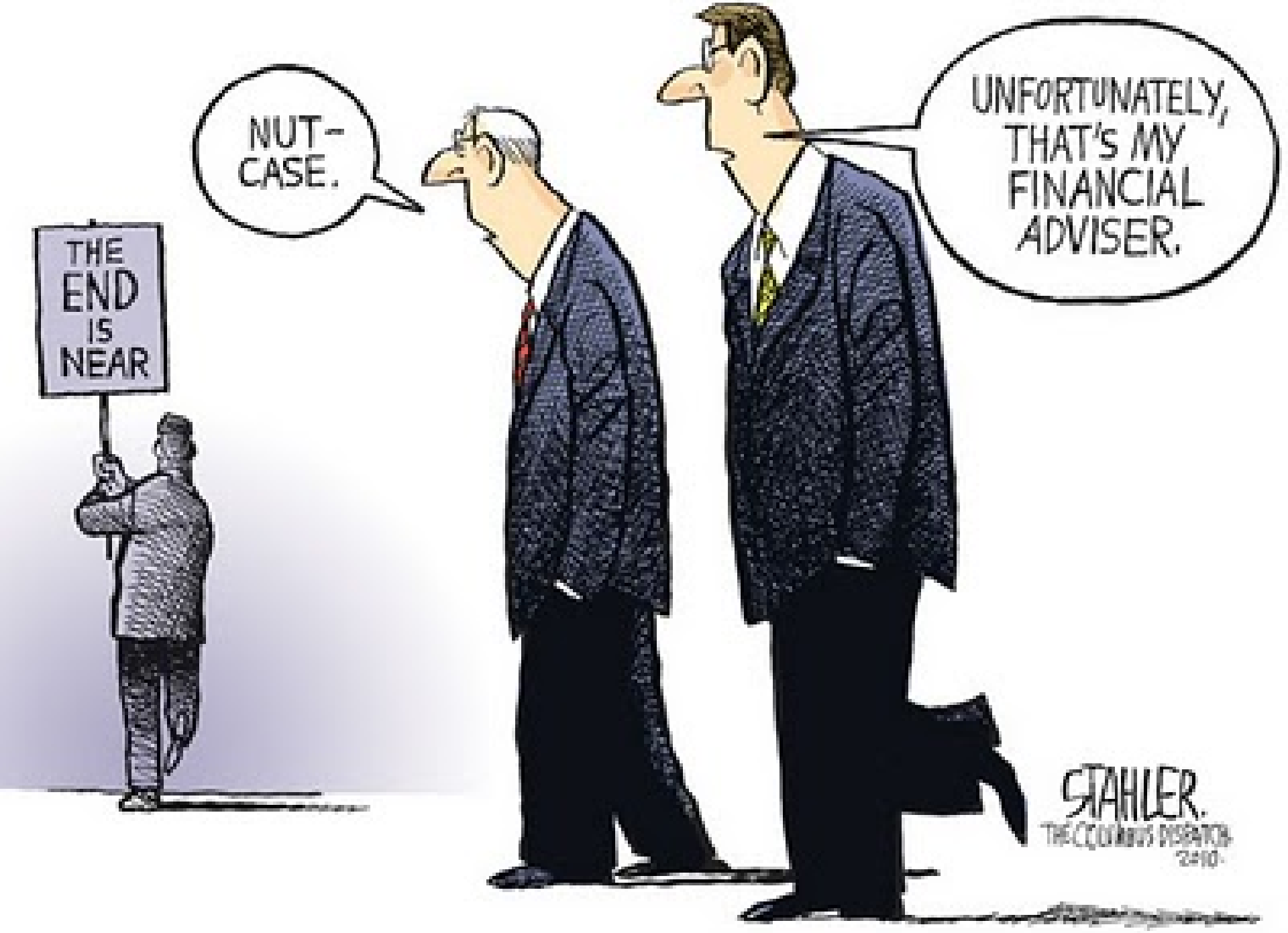
Sound Navigation requires... Sound Measurement

New Zealand Society of Actuaries Conference 2010

Presentation by Louis Boulanger & Professor Antal Fekete




THE END IS NEAR
NUT-CASE.
UNFORTUNATELY, THAT'S MY FINANCIAL ADVISER.
STAHLER.
THE COLUMBUS DISPATCH
2010

On the origins of money...

- Carl Menger's essay (1892) is the most important reading source to fully grasp and understand the true origins of money
  - a **social phenomenon** of practice/habit
  - money is... a social (**not** a state) institution
  - a gradual realisation of the different degrees of saleableness of goods and commodities
  - money is the "unpremeditated resultant" and "spontaneous outcome" of human actions

The role of the state...

- Came much later...
- Precious metals became money before ‘coins’
- Not as a rule, but because of their saleableness
- No accident or state compulsion effected this
- State *recognition* and state *regulation* of what people had already decided was money:
  - caused the state to coin (administrative role)
  - **perfecting** use of precious metals as money

What is money?

Money is anything that is generally accepted as payment for goods and services and repayment of debts.

The main uses of money are:

1. as a medium of exchange;
2. as a unit of account; and
3. as a store of value.

Is this ‘good’ (sound) money?

An example of fiat paper money

What of the ‘unit of account’?

- A standard numerical unit of measurement
- Used to describe economic activity (e.g. GDP)
- SO, maybe:
  - Our measurement of economic performance is only as good or reliable as our ‘money’ is
- IF SO, then:
  - How good is our currency as a measure?

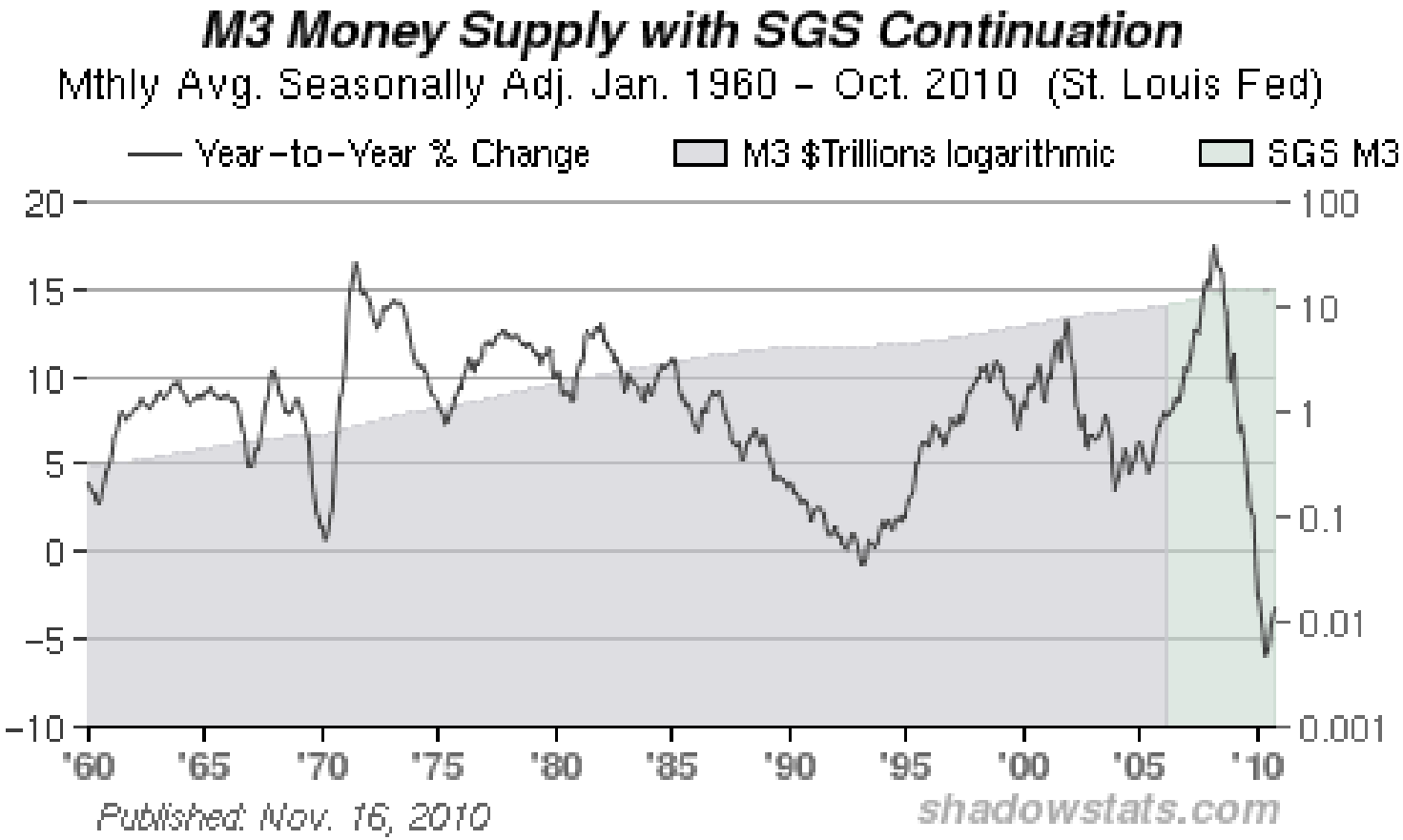
Measures of money

- Lots of aggregate measures of its supply
  - M0, M1, M2, MZM, M3, etc
- But what of the basic unit (of measure) itself?
  - Nothing to be found in **absolute** terms
  - Abundance of data/speculation in *relative* terms:
    - Currency exchange rates
    - Price level in terms of currencies

Scientific measurement?

- In all scientific endeavours, precision in the definition of the unit of measure has improved
- The ONLY exception is economics and, in particular, monetary economics
- ‘Money’ today, as far as its value is concerned, is based on government fiat, which is itself a highly ***elastic*** measure

Aggregate measure of money



Final thoughts

- The present financial crisis is far from over
- At its roots it's a belated gold crisis
- Gold has been exiled internationally from the monetary system and prevented from discharging its natural function
- So it is prudent to measure one's net worth in gold units rather than legal tender units