Is it "Money" or is it "Credit"? What is the Difference? By Paul Grignon (moneyasdebt.net)

Money is normally thought of as being very complicated. It's no wonder, given how it is created today. So… let's start with the basic question*. What is money?* Specifically what is "*cash"*?

Under our current system, the foundational form of "money" is *legal tender fiat currency* originated by the *central bank of the country*, the printed version of which is a paper note we usually refer to as "cash".

Strictly speaking, a note is a promise of payment in *something else*, like gold or silver, or wheat. However, legal tender notes are notes in name only as they cannot be redeemed for anything other than themselves. The paper wears out with use and therefore, legal tender notes are redeemable for new notes, nothing more.

As a medium of exchange, it doesn't really matter that they can't be redeemed for "stuff". As long as people accept them as symbols for value they function perfectly well as "money".

To *ensure acceptance*, the federal government decrees (fiat) that these notes issued by the often *privately owned* central bank of the country, are "legal tender". That means they *must be accepted* by law for the payment of all debts public and private. So, if you are offered (tendered) fiat notes in payment of a debt, you have to accept them or the courts won't enforce the debt.

So the next question… What are fiat notes? Are they just fancy pieces of paper the government gets to print and spend, as many believe? No. Life could be very different if that were true.

Fiat currency notes, or "cash" is money created by the *central bank*. The central bank is usually a consortium of the most powerful private banks, often international, usually run with token government involvement. It can also be a publicly-owned entity run primarily by personnel from these banks. In either case, the central bank works for the private banking system and determines how much "base money" or "cash" there will be.

This *private banking system currency* is our *national "money"*. It can be in the form of national paper notes or it can simply be an account credit at the nation's central bank. These *central bank account credits are potential cash*, that can be printed if need be.

How does the central bank create paper money or "cash" as most of us think of it? It just prints it, either through a government agency or a private company. Can the central bank just print new money whenever it decides to? Yes it can.

The government has little to no say in these decisions as a matter of "political policy" and, as is explained below, does its part by putting the taxpayer ever further into debt to pay the central bank for creating this new cash.

How exactly is cash created? All we are ever shown is the image of the presumably government owned printing press cranking out the national paper money. But that isn't how "cash" is *created*. That is just how it is *printed*.

The first step in the origin of "cash" is the federal government issuing an *interest bearing bond*, on which taxpayers, realistically, will be paying the interest forever to whomever holds the bonds. This is because government debt just grows perpetually and is never paid off.

The bonds are offered to all, but mostly those with lots of money will buy them, including banks. If the *central bank* wishes to add to the base money supply or total "cash", both paper and central bank credit, the central bank will either purchase some of these bonds, or take them as collateral for new cash it lends to the commercial banks via a perpetual buyback arrangement called a "repurchase agreement".

The cash the central bank creates is simply typed onto a computer screen. There it is… new "cash" or "base money" upon which much more new money can grow.

If paper cash is called for, the central bank has the privilege of being able to issue *legal tender fiat currency notes* simply by paying the costs of printing them… mere pennies. It then sells or otherwise provides these notes to commercial banks but can't spend the payment it receives, because it has to be able to refund these payments in full to the commercial banks at any time.

Therefore, because it cannot fund itself from selling notes to commercial banks, the central bank is paid for this service by the interest it receives on the government bonds it bought, or accepted as collateral. And, after the central bank's operating expenses are deducted, the remaining interest is usually refunded to the government.

Central banks can also create new cash in exchange for high quality *private* as well as government bonds. This is an exceptional emergency practice soothingly termed "quantitative easing", meaning creating more cash than the government bonds available will allow.

Interest payments on government bonds ultimately come out of the national income tax, that is to say, the taxpayers' pockets. Interest on private bonds ultimately comes out of prices, in other words, the consumers' pockets. So it is clear that, either way, *the public as a whole pays interest to private parties with sufficient excess wealth to buy bonds, in order for "cash" or "base money" to exist.*

In normal times, cash is created only to buy *government* bonds. Therefore, the following pertains to the usual practice of creating cash by the direct or indirect purchase of government debt by the central bank.

Government debt is never paid off. It usually just steadily increases. Government bonds that come due are replaced with more government bonds much like a Ponzi scheme. So, given that cash is based upon bonds on which interest will be paid ad infinitum by the public, the source of fiat currency or "cash" under the current system of creating it is, quite literally, *public debt increasing forever.*

Now, there is no reason that government can't simply create its own fiat currency debt-free, as many of us imagine it does now, spending it at face value on behalf of the taxpayer. This method of creating money would be as simple and clear as the current method is obscure.

Advocates sometimes try to sell the idea of such government spending as "free money" or a "citizen's dividend". Critics call it "funny money" that is sure to cause damaging inflation.

But neither claim stands up to scrutiny. Money *spent into existence* on government expenditures represents *value already delivered*. Thus it is not "funny" at all. It couldn't be more solid. Money spent on a bridge vital to transportation and thus the economy is *money representing the value of that bridge*.

However, spending such money cannot avoid affecting the money supply and prices and therefore, depending on whether an economy is in growth or contraction, none, some, all or more than was spent must be taxed back to the extent necessary to keep prices stable. In a sustainable economy with exact monetary balance, *taxes would have to equal expenditure*.

Failure to tax money out of existence would impose the general and indiscriminate tax on money called inflation. Thus such debt-free spending is not "free money" nor a "citizen's dividend" either. However, it could seem so during periods of *growth*. If the bridge enlarged the economy and the need for money, the money expended might *not* need to be taxed back. However, over the long term and in a stable economy, the bridge must be paid for in full by the taxpayers just as one would expect.

The BIG DIFFERENCE is that *no interest, no perpetual debt trap and no private profit* would be involved. That's the huge and qualitative difference between cash as it is now and *cash as it could be* if government just created it and spent it in the public interest. As stated earlier, life could be very different if government took back its rightful power to spend money into existence, debt and interest free, instead of borrowing it at interest from bankers who create it from the borrower's debt on the one hand and the taxpayer's guarantee on the other.

The next much larger room in the current monetary maze is bank credit, issued by commercial banks whose charters give them the privilege of turning the pledged debt of both private and public entities into "checkbook monies" which are bank "promises to pay cash".

Most of us equate "money in the bank" with "cash". But it isn't. A bank account is a bank's *"promise to pay"* cash, not cash itself.

The system allows the banks to issue, as "loans", many more promises to pay cash than there is cash in existence. In Britain, where banks are left to their own discretion, the banks reportedly hold 3% cash. International accords require banks to hold cash and *capital assets the bank can sell to raise cash* (without going out of business) equal to between 4 and 8% of credit issued, depending on the type of collateral backing the "loan". Loans to federal governments are exempt from any capital adequacy requirements.

Different nations impose very different standards as to how much checkbook loan money may be created relative to how much national cash exists, but everywhere, and especially in the Western countries, *far more promises to pay cash exist than there is cash to fulfill those promises.*

This is because, according to the fractional reserve principle, a bank credit promise created as a loan in one bank becomes a deposit of “money” in another, making possible another loan. As well, banks do business with each other in promises to pay cash, and most of those promises mutually cancel each other out at the end of the day, before any cash need change hands.

Thus, through this system, a small base of cash, both paper and central bank credit can grow to become an enormous inverted pyramid of commercial bank credit, upon which our economy is entirely dependent.

> "This is a staggering thought. We are completely dependent on the Commercial Banks. Someone has to borrow every dollar we have in circulation, cash or credit.
>
> If the Banks create ample synthetic money, we are prosperous; if not, we starve. We are, absolutely, without a permanent money system… When one gets a complete grasp of the picture, the tragic absurdity of our hopeless position is almost incredible, but there it is."
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> ~ Robert H. Hemphill, Credit Manager Federal Reserve Bank, Atlanta, Georgia (1935)

So… back to the title question, *Is it “Money” or is it “Credit”? What is the Difference?*

The answer is… with the exception of coins, ALL money, in whatever form and from whichever origin, originates as DEBT. ALL money represents a claim on physical resources and energy, including human energy, that is to be *extracted in the future* by those who simply create this “money as debt” by typing it in on a computer.

The fundamental distinction between “cash” and “credit” is in *the origin* of the debt.

“Cash” represents that portion of the (never-to-be-paid-off) *public debt of the federal government*, that *is purchased or held as collateral by the central bank*. Cash is issued by the central bank of the country as paper notes redeemable only for a new note, or simply as account credits at the central bank.

Put another way, cash is a potentially *limitless claim upon our future wealth* through perpetual public debt at interest. This unlimited claim on future wealth is used to create the limited claims upon our existing wealth we use as cash. The privilege of creating and destroying cash rests solely with the central bank, which is usually a consortium of the most powerful private international banks which control the nation’s money supply and thus its economy with minimum government involvement.

“Credit” is created by commercial banks and trust companies as “loans”. When the so-called “borrower” signs a document promising to pay the bank the amount of the so-called “loan”, plus interest over time, the bank balances the transaction by promising to pay the borrower the amount of the loan in “cash” on demand.

This *promise* to pay cash is a “bank account” and the borrower can spend it via checks or other means. All transactions can be carried out in bank credit promises alone, and most today are. Unless the borrower demands cash, or the bank ends up in a deficit position with respect to other banks that requires a transfer of cash to resolve it, no cash at all is required from the bank to honor its promises.

Put succinctly, “cash” is a claim on the *future productivity of the public as a whole* backed ultimately by income taxes. “Credit” is a claim on the *future productivity of a specific borrower*, whose pledges are usually backed by collateral, tangible real wealth that is to be forfeited if the borrower fails to pay back the credit. In contrast, the bank’s pledges are backed by only a tiny percentage of the total cash promised that the bank can actually deliver.

Despite the fact that checkbook money is only *a promise* to pay cash, most of which does not even exist, it is denominated and treated as if it were cash. Most people never think otherwise, including those who work in banks. We tend to refer to our “deposits” as having “money in the bank”, accompanied by a mental image something like gold in a safe, the *presence* of money.

However, all we really have is the bank’s IOU on a computer, the *absence* of “money”. We lent the bank our “money” when we deposited it. And unless our deposit was actually in paper cash or coins, what we deposited was *bank credit*, another bank account’s IOU, just numbers on a computer that keep track of these IOUs to determine who owes who how much of this cash that doesn’t exist.

Your bank account keeps track of what the bank OWES you. It is just numbers typed in on a computer screen that tell you what the bank has to pay you in cash *if you ask for cash*.

Confusing? One might suspect this obscure system was designed to discourage ordinary people from trying to understand it. On the one hand, the idea that a bank loan is created by the borrower's signature on a loan document seems too simple and outrageous to be true. That *the borrower is the source of the loan* is a concept often very difficult for people to accept.

On the other hand, the extraordinary convolutions of thought it takes to understand central banking convince us all to leave the monetary system to the "experts", the lawyers and technicians hired to keep in place this system where banks make huge profits *lending people their own credit.*

And when the borrowers' collective credit *falls through* in excessive amounts, as we are currently experiencing, the system collapses. It becomes clear that those numbers we thought were money were just "accounting" of borrowers' indebtedness and nothing more. It evaporates like a mirage in the harsh light of widespread default.

But, by the rules that make this system legal, banks must take *the losses* of this money that never existed until someone borrowed it. In good times, banks do absorb losses from loans that are not repaid, and this reduces their profits. In bad times of mass defaults and falling collateral values, the banks' capacity to write off losses can easily be exceeded, as the Banking Accords only require 4-8% "capital adequacy" to begin with. When too many of their "loan bets" fall through, banks become bankrupt and cannot issue any more "bank credit money". This is "failure of the money system", which results in economic, political and social collapse and, therefore, cannot be allowed to happen.

So, the government steps in. Now*, the government could just create new money itself,* debt and interest-free. In fact, that is clearly *a right and duty of government*, that may even be written into the nation's constitution.

But instead, worldwide, governments put the taxpayer ever further, and now *astronomically and impossibly* into DEBT to create the new money.

What happens is that government replaces *failed private indebtedness* where the maximum penalty is to lose our collateral and credit rating, with *guaranteed public indebtedness* where the potential penalty is a huge fine, a government lien against our wages and possessions and/or *time in prison*. This substitution of public for private debt, ultimately at gunpoint, is called a "bailout".

There are many problems with the arithmetic of bank credit, fractional reserves, lending in general and interest; far beyond what can be examined in this article. However, there is a simple alternative concept of cash everyone can understand.

If governments just created and spent cash directly, that *cash would originate as payment for whatever it was spent on*. The government, the public body, would be spending cash on behalf of the public, simply as current claims on the public's goods and services. Those claims would then circulate as money. Finally, the issuing government would accept those claims back as payment of current taxes.

Cash would NOT involve central banks, interest, or private profit. Cash would NOT represent a legacy of ever-growing debt chained to our great great grandchildren. Instead, cash would simply be a short-term charge for *value already delivered* to the public, that value being paid for by the public in current taxes, to the extent necessary to keep general price levels stable.

Why do we need a central bank putting all of us into perpetually escalating debt and calling the evidence of this unnecessary debt "money"? Is this not insane given that government has the right to create money itself, debt and interest-free? Why don't governments throw off this crazy system?

One would have to suspect that either politicians are just as baffled by the money system as most people, or they are compromised to the point they support it. Most of us have been "educated" in such a way that we live our whole lives never questioning the nature and source of "money" at all, which makes the task of advocating fundamental monetary change an extremely lonely one few politicians are brave enough to take on. This situation must not continue.

We need *a mass awakening of the public* to HOW the current parasitic and self-destructive system works. Only then will we be able to force a "cleansing of the monetary tapeworm" and a change to a healthy money system designed upon the foundations of sustainability and honest cooperative relationship. We must realize that only a money system *specifically designed* for freedom, sustainability and justice can sustain a *humane* human civilization into the future.