BSM 477

DR. GEORGE REISMAN **SYLLABUS SUPPLEMENT 1**

Overview of Course

1. Under the head of "The Process of Economic Progress," this course starts off with an analysis of the monetary framework within which economic progress occurs. This includes a detailed analysis of the factors determining the supply of and demand for money and its purchasing power, as well as the origin and evolution of money and the contemporary monetary system. Application of knowledge of changes in the demand for and supply of money is made to the analysis of the balance of trade and payments and its significance. This material is presented in the main text in Chapter 12, which is titled "Money and Spending."

2. The course then develops the proposition that economic progress is *a logically consistent economic benefit,* i.e., does not entail such alleged negatives as overproduction or mass unemployment. This material is presented in the main text in Chapter 13, titled "Productionism, Say's Law, and Unemployment."

3. The next main subject is an analysis of the determinants of real wages, i.e., the average wage earner's standard of living. This material is presented in the main text in Chapter 14, titled "The Productivity Theory of Wages."

4. Following the midterm, the course develops the aggregate economic accounting framework needed to analyze the process of economic progress. This includes an analysis of contemporary national income accounting and of the role of saving and productive expenditure in aggregate demand. In the main text, this material is developed in Chapter 15, titled "Aggregate Production, Aggregate Spending, and the Role of Saving in Spending."

5. The next main topic in the course, occurring usually in Week 9, is the integration of the above-mentioned aggregate economic accounting framework with the theory of capital accumulation presented in Chapter 14 of the main text in the Section titled "The Foundations of the Productivity of Labor and Real Wages: Capital Accumulation and Its Causes." In the course of this integration, the perhaps startling conclusion emerges that it is possible for national income and economic progress and prosperity to be inversely related, totally apart from the existence of inflation as the cause of rising national income. This is a conclusion of considerable relevance in appraising some of the arguments advanced in favor of increased government spending.

6. Following this, in Weeks 10 and 11, the course turns to an explanation of the determinants of the average rate of profit and interest in the economic system, both in terms of money and in real terms. The very important differences between the determinants of the rate of profit of individual companies and industries, on the one side, and the average rate of profit in the economic system as a whole, on the other, are explained. The significance of the average rate of profit and interest for economic progress and for the relationship between businessmen and capitalists, on the one side, and wage and salary earners, on the other, is also explained. Alternative theories of the rate of profit are explored.

7. Week 12 is typically devoted to leading applications of the theory of profit and interest, such as answering the questions "Do falling prices caused by increased production represent deflation by virtue of reducing the rate of profit and making the repayment of debts more difficult?" "Does continuing capital accumulation require a continually falling rate of profit?" "Does a rise in saving and fall in consumption place business in the contradictory position in which it is asked to increase its investment spending in the face of a fall in sales revenues?" "Could a very large increase in saving and fall in consumption place business in the position of being asked to buy for more than it sells?"

8. Week 13 is devoted to considering the leading ideas of Lord Keynes, especially his belief that full employment under capitalism requires an unacceptably low rate of profit and interest and thus is possible only on a foundation of large-scale government intervention, specifically in the form of government budget deficits and an expansionary monetary policy.

9. Week 14 deals with the subject of inflation, a phenomenon closely related to Keynesian ideas about fiscal and monetary policy. Here the course explores virtually all of the alleged significant causes of rising prices and investigates the effects of inflation on capital accumulation. Students are provided with the

tools of analysis that will permit them to judge for themselves the future outlook both for inflation and for the state of the government's budget.

I. Introduction to the Economist's Perspective

From the "broken window" to the "drive for exports." The seen and the unseen. The net loss or gain. The implicit assumption of a fixed aggregate expenditure—invariable money.

II. The Division of Labor and Money

A. Specific dependence of the division of labor on money

1. Problems of double coincidence of wants—money radically widens possibilities of exchange and thus division of labor.

2. Money and economic calculations and comparisons—of methods, products, industries, and jobs—allows existence of price system and its coordinating functions with respect to the division of labor, as described in Chapter 6.

B. Money Making and the Concept of Productive Activity (to be covered after the Midterm)

III. Money and Spending

A. The Quantity Theory of Money: the Formulas of M x V = D and P = D/S.

1. How more M raises D: the gold mining case and the social security case
2. The quantity theory of money as the explanation of rising prices
3. Fiat money versus commodity money; the increase in fiat money and spending versus the increase in the production of goods
4. Virtual impossibility of inflation problem with gold and silver; even now, prices calculated in gold and silver coins show much less rise or no rise.

B. The Origin and Evolution of Money and the Contemporary Monetary System

1. How rational self-interest led to the development of money out of barter
2. How it led to the selection of gold and silver as money.
3. How paper (including checkbook) money came into being.
4. Government and the demonetization of the precious metals: the Civil War, the National Bank Act, the Federal Reserve System, World War I (including the Federal Reserve and the pyramiding of gold reseves), the New Deal, the final break with gold in the 1960s.
5. Inflation and the potential spontaneous remonetization of the precious metals.
6. Recent change in the composition of the money supply and the deficiency of the weekly reported M_1 statistics

C. The Monetary System and Banking

1. Standard money—commodity money or fiat money.
2. The monetary base.
3. Fiduciary media: transferable claims to standard money, payable on demand, and accepted in commerce as the equivalent of standard money, but for which no standard money actually exists.
4. How fiduciary media are created.
5. Fractional-reserve banking and 100%-reserve banking.
6. Limits to the private issuance of fiduciary media: the clearing difficulties of more rapidly expanding banks; the public's demand for standard money.
7. Governmental encouragement of fiduciary media.

a. Expanding the amount of reserves—fiat money reserves and central banking.
b. Making reserves more potent: Rediscounting, deposit insurance, bank examinations, restrictions on bank competition, payments suspensions. Reinforced by the effect of additional reserves on the clearing and in meeting the public's demand for currency.

8. Contemporary money creation: open market operations.

Open market operations and deficits.

D. The Quantity of Money and the Demand for Money

1. Velocity as the reflection of the demand for money for holding.
2. General factors affecting the demand for money for holding—security of property and complexity of production.
3. Changes in the quantity of money as the cause of changes in the demand for money and thus the velocity of money.

a. The effect of credit expansion on the prospects for borrowing.
b. The ability to substitute other assets for cash holdings.
c. The anticipation of higher prices.
d. The effect of more money on the rate of interest, which, after a temporary drop, is to raise the rate of profit and thus to increase the demand for and reduce the supply of loanable funds.

E. The Demand for Money and the "Balance of Payments" Doctrine: A Critique

1. The meaning of the balance of trade and payments.
2. Historical origins of the concepts (Mercantilism) and notion of what is a "favorable" or "unfavorable" balance.
3. The concepts under a system of fiat money—no loss in an outflow of fiat currency.
4. Mainly fictional nature of the outflows.
5. Foreign investment as the source of an "unfavorable" balance of trade.
6. The balance under a precious metal or other world-wide standard.

a. Principle governing the distribution of precious metal money among the various countries.
b. Why gold mining countries export gold.
c. The tendency of the balance toward balance.
d. sufficiency of precious metal money to transact commerce—loss of precious metals due to not enough production of goods; potential destructive role of labor unions

7. Inflation as the cause of a gold or other reserve outflow.
8. Error of blaming the citizens.

Spending abroad does not cause a money outflow if the citizens have a demand for the money.

F. An Invariable Money

1. Variations in prices from the side of money and the side of goods.
2. The need to isolate
3. The contribution of invariable money to economic theory.