

Central Banking

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Introduction

Central banking is a central institution of modern economies, yet somewhat surprisingly, there is no separate treatment of “central banking” in the classic Austrian works. Ludwig von Mises wrote extensively on the nature of money and banking in both his *Theory of Money and Credit* (Mises 1953) and in *Human Action* (Mises 1998), but there are very few mentions of the term “central bank” or of derived terms. Vera Smith’s classic work on the history of banking theory deals with central banking as part of the general theory of banking (Smith 1936). Among contemporary Austrians economists, Huerta de Soto discusses central banking in his treatise on money and banking only incidentally to the theory of banking and historical debates on the topic (Huerta de Soto 2012, ch. 8). Examples could be multiplied from across the Austrian tradition, but these are enough to show the point: there is no independent analysis of central banking in Austrian economics.

This is not an oversight, however, but follows from the nature of central banking. Since central banks are monetary and financial institutions, the analysis of central banking is not a separate subject of economics but belongs to the theory of money and banking.¹ It also belongs to the theory of interventionism and the impossibility of socialism insofar as central banks only arise due to legal privileges granted by the government. It is the final outcome of the interventionist process whose origin lies in the granting of privileges to banks², and to the extent that central banks exert centralized control over the economy, it is a case of socialistic organization of the economy (Huerta de Soto 2012, 651–61).

The standard definition of a central bank since Bagehot (1873) as lender of last resort to the banking system is thus incomplete. While dominant in the contemporary world, the link between central banking and fractional-reserve banking is not essential, and it obscures the role of the central bank as producer of money (cf. Bindseil 2019). In fact, the monetary policy conducted by central banks is simply a special case of money production (Mises 1953, 219) directed to specific market actors for specific purposes. Historically, the main recipients of central-bank money have been private banks

1 Notes to relevant chapters in this volume.

2 Note to Bagus in present volume.

engaged in credit expansion and governments wanting to expand their operations beyond what their income in the form of taxes and their standing in credit markets would allow. This points directly to the nature of central banking.

A central bank is simply a privileged bank of issue. It is a bank of issue in that it issues liabilities that are on par claims to money, or, in a fiat money system, its liabilities simply are base money. And it is privileged by the state, since only special privileges can ensure the wide circulation of its issue. Coercive state action ensures the fiat equivalence (Hülsmann 2004) of central banknotes (and other liabilities) and other forms of money. Historically, banks of issue had to honour their promise to redeem their issue in commodity money, and a key development of the twentieth century is the liberation of the banks from this promise and the transformation of their issues into fiat money. The privileges accorded to the central bank are meant to widen the field for the use of its liabilities as money, i.e., to allow it to engage in inflation: to expand the money supply beyond what the public really wants (Hansen and Newman 2022). Thus, while modern monetary policy may look complex, it is ultimately only a question of the rate of increase of the money supply and the direction of the flow of new money.³

Having thus laid out the basic definition of central banking, the rest of our chapter falls into two major parts. We will first delve into the theory of central banking in greater detail, looking especially on the role of the central bank in causing hyperinflation, the relationship between the central bank and the banking system, and the role of the central bank in the business cycle. In the second major part, we will investigate a few controversies in the theory of central banking. Specifically, we will look at whether central banks really control the money supply, or whether they are irrelevant, since the private banks issue bank money with no regard for central-bank policy. Central bank digital currencies have become a key topic of controversy in recent year and we will examine it as simply another variation of monetary policy. We will then look at the global role of the American Federal Reserve System and end with a comparison of Austrian and mainstream approaches to central banking.

Theory of Central Banking

In order to grasp the nature of central banking, we need to distinguish between central banking on a gold (or other commodity) standard and central banking on a fiat standard. On a gold standard, the central bank is a bank like other fractional-reserve banks that engage in the issue of fiduciary media. Its privileges make it the most prominent bank in the banking system, but it is not essentially

³ Note to Newman chapter.

different. On a fiat standard, the central bank produces base money, it does not issue fiduciary media. Base money is the physical cash in circulation and the reserves of the banking system, what banking theorists also sometimes call outside money, since it is provided from outside the banking system (cf. Selgin 1988).⁴ The suspension of the gold standard fundamentally changed the nature of central banks, turning their issues of money substitutes into money in the narrow sense in a process Guido Hülsmann has aptly termed reverse transubstantiation (Hülsmann 2008, 162–64).

A central bank on a gold standard is in a privileged position to issue money substitutes, securing for them a wider circulation. It is not, however, freed from the obligation to redeem such substitutes. The central bank, like all private banks, must work to extend the use of its notes and deposits as money, it must acquire the good will of the public (Mises 1998, 431–33). While loss of public confidence is a real limit to the issue of a central bank, it is one rarely faced historically, since bank directors have been careful not to extend their issues too quickly. It is, however, real enough, and the loss of confidence almost invariably led to the suspension of redemption and the conversion of the central bank issue into credit money or fiat money.

Yet even when a central bank is careful in cultivating the trust of the public, economic forces will still limit its powers of inflation. Central banks have always been *national* central banks and their issues have only circulated in their own countries and in countries under the control or influence of their national governments. Thus, the issue of the central bank turn the currency of the nation into a mixed currency, as the classical economists called it, part gold (or silver) and part paper. The central bank can only inflate the supply of this mixed currency and the primary effects therefore appears in the domestic economy. Domestic prices rise and exports fall off, while imports rise, as they are now comparatively cheaper. The foreign exchange turns against the inflationary country. To finance the balance of trade, gold is exported, and the central bank is forced to stop its expansion and contract its issue to avoid losing all its reserves. This is of course the classic price-specie flow mechanism (Hume 1987), and it works powerfully to restrain a bank of issue on the gold standard (cf. Mises 1998, 437).

Modern central banks have been freed from the “golden fetters” of gold redemption and have been transformed into producers of fiat money. The considerations in formulating monetary policy have therefore changed. Neither an external drain of gold, nor a loss of confidence in the central bank’s ability to redeem its liabilities limit the freedom of action of central banks. The bounds within

4 The distinction inside/outside money was introduced into Austrian economics by George Selgin and the free banking theorists, but we should note that the distinction as used in mainstream economics differs in important respects. Specifically, only outside money is considered a net asset, leading to the erroneous conclusion that inside money is not really a present good to the possessor.

which a central bank can formulate monetary policy are much wider, but one important point remains the same: monetary policy is still a question of how high a rate of increase in the money supply the central bank can pursue and to whom the new money can be given. On the second point, the only limitations are of a legal and technical nature. Since the central bank acts by issuing liabilities, it can only issue these to those individuals it can reach and who are willing to hold central bank money. Concerns about the “unbanked” and “financial inclusion” are, from the point of view of the central bank, concerns about extending the circulation of its own money and that of the banking system it sponsors. Legislation may also constrain the range of action of the central bank, for instance by decreeing that the central bank may not buy government debt directly off of the government. Legislation can, however, be amended, and it can even be disregarded by the central bank if the other organs of the state go along with this course of action.

Hyperinflation

This does not mean that there are no limits at all on central bank action. Ultimately, the central bank cannot force the public to use its money, but the choice of the public is in this situation constrained. Either people accept central bank money, or they forego the use of money altogether.

Hyperinflation, where the value of money falls rapidly and makes the use of it impossible, is thus the only limit on modern monetary policy. Only the fear of hyperinflation can discipline a central bank, since it would mean the end of the bank’s ability to create money.

That said, we must realize that a very high rate of inflation can be consonant with central bank objectives. The first receivers of new money can still benefit in times of high inflation, that is, when the value of the monetary unit is rapidly falling, if the real value of their total nominal income is greater than it would be absent the inflation. That is, if they can still spend their income before prices rise, they benefit. The reverse has often been the case in inflationary episodes: society as a whole has often experienced a scarcity of money, since the value of money has fallen faster than the rate of increase (Mises 1953, 227–30).

A hyperinflation, in the sense of a very high rate of inflation, can thus be optimal from the point of view of the central bank. If this is the best means available to pursue the ends desired, inflation will be carried to this extreme. Episodes like the Zimbabwean and the German hyperinflation can be understood in this way. The central bank creates ever-increasing amounts of money whether it be to pay government employees, pay for state-owned enterprises, or some other purpose. In the German case, hyperinflation was at least in part a conscious policy to support striking workers in the Ruhr and to buy foreign exchange for war reparations (Feldman 1993; Mises 2006, 34–39).

Hyperinflationary policy cannot go on forever – when the public refuse the fiat money of the central bank and turn to other money, the policy comes to an end. In a process known as Thiers’ law (Bernholz 2003, 77, 110), good money (foreign currencies and commodity money) drive the hyperinflating currency from use, as even the strongest penalties imposed on the refusal to use the money of the central bank are impotent if the costs are too high (Mises 1953, 229–30).

The Central Bank and the Banking System

Central banks will usually not consciously aim at a hyperinflationary policy. Only when fiscal objectives are central to monetary policy, that is, when the central bank funds the government directly, is such a policy likely. In most western countries, the primary role of the central bank is to support the banking system – to be a lender of last resort in the classic formulation (Bagehot 1873). Central bank action goes much further than this, however, as the major central banks have also taken on the role of supporting financial assets prices. This grows naturally out of their classic role, however. The development of shadow banking and the use of repos as money substitutes have made financial assets central to the banking system. To avoid deflation, it therefore became necessary over the last 30 years or so for central banks to step into the role of “market-maker of last resort” and to maintain asset prices (Giménez Roche and Janson 2019).

If the goal is to avoid collapse of the private banking system and deflation, there is no other way but forward: the central bank must intervene in wider markets and with greater amounts to keep the private banks afloat. Indeed, the result of monetary policy in recent years has been to flood the banking system with reserves, breaking the traditional transmission mechanism. The classic system of private and central banking relies on an inflow of reserves only in response to demand for reserves, but after the crisis of 2008, reserves became abundant (Gertchev 2023). Quantitative easing after the great financial crisis of 2008 was a policy of buying large amounts of financial assets in order to overcome the effects of private banks contracting their business. The “liquidity trap” (cf. Baeriswyl 2015, 64–67) of private banking results when the banking system will not go along with monetary policy. Then, the central bank has to assert full control of the money supply in order to pursue its aims. The developments of CBDCs by various central banks in recent years are a step in this direction. On the other hand, a return to the classic system is still possible and may still be attempted.

It is impossible to say what an “optimal” policy would look like for a central bank aiming to support private fractional reserve banks. To keep the private banks afloat, ever greater infusions of money are necessary, leading to a situation like the present one. Optimal policy is, in any case, a

chimera. From the overall point of view of the market, there is no such thing as optimal monetary policy (Hülsmann 2003). There is nothing gained from an increase in the supply of money, whether the first receivers are private banks and their customers or the government. All that can be achieved is a redistribution of wealth and incomes. This is true also in the case of a mixed currency. Classical economists thought that there was a resource saving or a saving in the amount of capital devoted to cash holding, if part of the money supply took the form of paper money. Adam Smith famously compared paper money to a waggon-way through the air (Smith 1904, bk 2, chap. 2). The error consists in seeing the amount of money held as cash as “dead stock”, as somehow unproductive. For the individual merchant or businessman, of course, cash does not earn income, and he is better off the smaller a proportion of his capital he must keep as money; for the economy as a whole, this does not hold, since all a reduction in cash holding achieves only a rise in prices, just as an increase in the money supply only leads to higher prices. This argument has, however also been advanced by modern economists (White 2023), but it rests on the same error now as back then (cf. Hansen 2023).

The Role of Central Banking in the Business Cycle

The classic works on Austrian business cycle theory stress that what triggers the business cycle is an inflow of money into the higher stages of production through credit expansion (Mises 1953; Hayek 2008). It is thus important to stress that central banking is not strictly necessary for the business cycle to be set in motion. However, in the “classic” arrangement of a fractional-reserve banking system supported by a central bank acting as a lender of last resort, the central bank assumes a more active role. All banks are usually fully “loaned up”, that is, operate with the minimum amount of reserves economically and legally required. The economic minimum is also lower than it would have been without a central bank, since the banks are freed from the shackles of competing with each other. The central bank acts as a cartelization device for the banking system, enabling a much greater degree of credit expansion (Rothbard 2017, ch. 14). However, because the banks are fully loaned up, they are not able to initiate credit expansion on their own. Here the central bank takes on an active role as the provider of reserves for the banking system.⁵ Only the central bank can direct the entire banking system to expand credit by adding more reserves to the banking system (Rothbard 2008, 136). The exact institutional details of how this is done differ from country to country and over time. Open market operations, where the central bank buys assets, are the usual form in many countries, but it could also happen through a reduction in the central bank’s discount rate. This all depends on the institutional setting in the given case.

5 Reserves could also be added to the system if people deposit more cash in the banks, or, on the gold standard, if there were an inflow of gold from abroad.

Once the central bank has added reserves to the banking system, the banks are able to expand credit, setting in motion the business cycle: banks lend more money to business, the market rate of interest falls, prices for producer goods in the higher stages of production rise and so on. The process of credit expansion and its economic results are thus the same as in the absence of the central bank, but there are some important differences. First of all, the inflow of reserves from the central bank enable all banks to expand together. No bank loses reserves to other banks due to expansion. Second, the credit expansion can go on for much longer, as the central bank pumps reserves into the system, leading to a greater boom and a worse crisis and deeper recession. And third, just like fractional-reserve banking makes the economy more bank-centred due to the Cantillon effect in favour of banks, so the presence of a central intensifies this process. Finally, the banks become more dependent on the central bank, as their own fragile position is revealed in the crisis and they have to be rescued by the central bank.

There is thus an inherent tendency in the system for the central bank over time to become more and more important, and there is also a tendency for it to assert more and more control over the financial system (Gertchev 2023). The central bank begins to intervene and regulate the banks more closely in an attempt to prevent the recurrence of crises. This is an example of the interventionist dynamic (cf. Mises 2011b): since the central bank (and the financial authorities as a whole as well as the general public) are in error as to the causes of business cycles, that is, the nature of fractional-reserve banking and central banking, they view it as a case of market failure in need of correction. The regulations they impose thus do not touch the main problem and are therefore incapable of preventing future crisis. Yet with each new crisis another layer of regulations is imposed, slowly transforming the financial system until capital is almost exclusively allocated according to bureaucratic criteria, effectively nationalising the credit system (Mises 2011a, 107–15). Nikolay Gertchev (2023) has shown how this process has played out in recent years in the case of the European Central Bank and the Eurozone.

After the crisis of 2008 and the policy of quantitative easing, whereby central banks flooded the banking system with reserves, what we have termed the “classic” operation of the cartelised banking system ceased, at least for the time being. Credit expansion becomes of lesser significance, as the banks are in a “liquidity trap” and do not pass on the increase in reserves as loans to business. However, this does not mean that such a system of “full-reserve banking by accident” is not liable to the distortions of the business cycle (Baeriswyl 2015, 64–68). The business cycle is caused by the flow of new money to the upper stages of production. When the central bank injects new money into financial markets by buying private securities, this is enough to distort the economy; the private

banks are not strictly necessary for setting the business cycle in motion. Of course, direct grants of credit by the central bank are much more likely to be political and bureaucratic, that is, the central bank is likely, under political pressure, to finance the expansion of state activities and such private sector business as is politically approved and well-connected. The rise of “green finance” exemplifies this. Only the bureaucratic criteria laid down by the authorities and the central bank, as well as the liquidity provided by the central bank, could force financial actors to value green and ESG-rated financial products.

Modern Controversies regarding Central Banking

Central Banks and the Money Supply

Some modern controversies have arisen about the theory of central banking. The most interesting is perhaps the claim that central banks have no control over the money supply. Private banks extend credit by issuing fiduciary media, and they don't look at their available reserves when doing so. Only after the fact, when they have made their loans, do they act to raise the necessary reserves. Thus, central banks are simply irrelevant to the money supply and the wider economy.

This argument gained prominence when it was advanced a few years ago by economists of the Bank of England (McLeay et al. 2014). It however rests on a fundamental confusion. It is true that, in the English system, banks do not wait for an inflow of reserves from the Bank of England before they make new loans. They look at the expected profit from the loan compared to the costs of funding, and if the loan looks like a good profit opportunity, they lend the money and then look for funding. However, the costs of funding are obviously not independent of central bank action. Central banks usually set a policy rate, and at this rate they lend to all approved comers (or buy all assets offered them, as the case might be). Thus, the central bank directly sets the costs of funding bank loans and determines the amount of credit granted by banks and the overall money supply. This control over the money supply is indirect, but that is nothing new; that is the normal functioning of the classic system.

Another argument against the central role of central banks in controlling the money supply is that they cannot determine what counts as part of the money supply. A classic case is how savings deposits in the U.S. came to be regarded as money substitutes, since banks and bank customers all treated them as if they were demand deposits (cf. Rothbard 1963). Another case is the rise of Eurodollars from the 1960s on, dollar deposits outside U.S. jurisdiction in banks with no access to

the Federal Reserve, which nevertheless are treated as equivalent to dollars (Machlup 1970). Eurodollars and equivalent liabilities are to this day an important part of the global financial system (cf. Financial Stability Board 2023). While there is no official policy of supporting these “shadow banks”, they do in fact benefit from central bank support. The role that central banks have assumed of “market-maker of last resort” which we discussed above directly help these institutions, as did quantitative easing. It is probably true that these innovations arose without the support of central banks, but their continued existence depend on liquidity from official sources. Any institution that issues fiduciary media is inherently unstable and will face a crisis at some point. Only the central bank can keep it from failing. Hayek made this point already in 1931:

The characteristic peculiarity of these forms of credit is that they spring up without being subject to any central control, but once they have come into existence their convertibility into other forms of money must be possible if a collapse of credit is to be avoided... [O]nce additional money has come into existence in some form or other, *convertibility* into other forms must be possible. (Hayek 2008, 290)

The only point to add to Hayek’s discussion in *Prices and Production* is that only a central bank with a monopoly on fiat money production can ensure such convertibility.

Monetary Policy and CBDC

Central bank digital currencies (CBDCs) have been discussed since about 2015. These too must be viewed in light of monetary policy. That is, while other considerations do come into play, a CBDC would ultimately mean that the issuing central bank had total control of the money supply. Official discussions mostly do not emphasize this fact (European Central Bank 2020; Board of Governors of the Federal Reserve System 2022), with the Swiss National Bank providing an exception (Baeriswyl et al. 2021, 6). The SNB is also the only prominent central bank that does not aim to introduce a “retail” CBDC, that is, it only considers its use as part of the clearing mechanism between banks (Bank for International Settlements et al. 2020; Jordan 2024).

Academic discussion on CBDC has focused on the problem of the zero lower bound: normal monetary policy becomes impotent when the rate of interest is very low. A CBDC can overcome this problem, since the central bank would be able to impose a negative interest rate (Agarwal and Kimball 2019; cf. Andolfatto 2021). Since the goal of monetary policy is to stimulate the economy by lowering interest rates, a CBDC is therefore a useful tool. Only rarely do economists directly address the fact that only by abolishing cash or severely limiting its use can a CBDC fulfil the

function assigned to it. A worry sometimes presented is that a successful CBDC will lead to financial disintermediation (Keister and Sanches 2021; Williamson 2021; Fernández-Villaverde et al. 2021; cf. Brunnermeier and Niepelt 2019). Since deposits at the central bank are free from the risk of bank runs, the public may shift their cash holding from private banks to the central bank. Such a shift would lead to a collapse of credit on the part of private banks, constituting as it does a run on bank deposits.

The real problem of disintermediation is not, however, that there will be a collapse of credit, or that less capital will be available. Insofar as private banks grant credit by issuing fiduciary media, they do not add anything to the real stock of capital. Granting such circulation credit (Mises 1953, 263–77) only redistributes resources and leads to unsustainable investments. While the transfer of deposits from private banks into CBDC accounts at the central bank would lead to problems and a loss of business for the private banks, the elimination of fiduciary media and circulation credit is unproblematic for the economy as a whole (note that it would, in this case, occur without a monetary deflation). Problems only arise once we consider the further conduct of the central bank in this situation. The need to conduct monetary policy with and through the banking system imposes a real limit on central-bank activity. Disintermediation would remove the banking system completely from the realm of monetary policy, and central bankers would thus be free to do whatever they like. Since credit expansion and malinvestment can also happen in a 100-percent-reserve system, the economy would not even be freed from the business cycle (Baeriswyl 2015).

The Global Federal Reserve

Finally, there is the question of the role of the Federal Reserve in the world economy. A not unrespectable opinion sees it as central banker to the world (Hülsmann 2008, 164; Hoppe 2006). To be sure, until the end of the Bretton Woods System, the Federal Reserve was the central bank to the world – only its liabilities could be redeemed for gold. However, after 1971 the world is divided between national central banks, each of which issues its own irredeemable fiat money. At the very least, the major central banks must be recognized as independent of each other (Hülsmann 2008, 223–36), and the Federal Reserve is thus not in the strict sense the global central bank.

However, the dollar is still very much the dominant reserve currency of the world, and the Federal Reserve has a clear interest in ensuring this remains the case. It is true that other national currencies are not money substitutes for dollars like they were in the Bretton Woods system, but dollar assets are still the preferred type of reserves globally. Non-American financial institutions also continue to issue Eurodollars, adding to the global dollar supply. This is by no means to the detriment of the

American financial industry: these Eurodollars funnel savings from Europe and Asia into the U.S., greatly expanding the supply in American credit markets. This funnel also means a large transfer of capital from Europe and Asia into the American economy. However, these transfers are founded on the issue of fiduciary media, and thus a central bank is needed to prevent the system from imploding in a crisis. National central banks cannot do this, since they only have limited supplies of dollars available. The Federal Reserve has therefore stepped in and acted as lender of last resort also to Eurodollar banks. It did this most notably in 2008, 2012, and the spring of 2020 through the use of liquidity swaps with other central banks. These swaps, which originally were temporary makeshifts, have now become permanent (Board of Governors of the Federal Reserve System 2023).

Austrian Economics versus Mainstream Central Banking Theory

As we have seen, Austrian economics have a clear conception of central banks and their role in the economy as producers of money and as the ultimate guarantor of the banking system. It is worth pointing out that here the Austrian school is the clear heir of the tradition of classical economics and mainstream, nineteenth century works like Bagehot (1873). The earlier economists were despite their occasional flaws very aware of the monetary role of banks and the incipient central banks (Fetter 1965; cf. also Rothbard 2006).

Mainstream economics, on the other hand, has moved away from the focus on the monetary role of banking. Under the influence of Keynesian economics, monetary thought has overall deteriorated, as Keynes (1936) had no clear theory of money. This has led to a fundamental misunderstanding of the nature of money and the economic characteristics of bank and nonbank money, exemplified in the influential work of Gurley and Shaw (1960). Their distinction between inside and outside money overlaps the concepts of money proper and fiduciary media, but it engenders a false understanding of banking, since inside money is ultimately perceived as only a claim and not a present good (cf. Cochran and Call 1998). This change of focus distorts modern analyses of central banking as well. As banks are viewed as primarily financial intermediaries, fractional-reserve banking is recast in terms of maturity mismatching, that is, borrowing short and lending long, and problems of banking are understood in terms of the risks specific to such activity (Diamond and Dybvig 1983). The central bank is still central to the banking system, but it is here understood as an insurance agency against such risks. The monetary aspects of central banking are secondary in this analysis.

Another string of mainstream analysis looks at the role of central banks in providing macroeconomic stability (Blanchard 2020). While this runs in parallel to the Austrian analysis

focusing on the monetary role of the central bank, again the monetary aspect becomes secondary to the mainstream economists. Monetary policy, rather than being the defining feature of central banks, is just another tool which the macroeconomic regulator can use to guide the economy along his preferred track.

This evolution of mainstream thought on the issue of central banking goes along with the generally positivist or empiricist attitude of virtually all (non-Austrian) economists, which tends to produce an eclectic mix of ad hoc propositions and theories that are only valid until new experiences, new models, and more advanced techniques “advances” science.

Conclusion

Central banking is the necessary complement to fractional reserve banking. In order to save the banking system from collapse, a lender of last resort is necessary, and in order to fulfil this role, the central bank must have be a privileged issuer of money substitutes. In the modern world, it has become an issuer of money proper and has thus enabled an unprecedented expansion of banking and the financial system. Monetary policy – how much money should be created and to whom should it be given – is central to the modern world. While fiscal motives can influence monetary policy, it is mostly a question of serving the financial system (which of course has the side effect of greatly increasing the demand for government debt).

In all cases, monetary policy does not pursue a good end. That is, from the overall viewpoint of society as a whole, it only leads to redistribution, malinvestment and conflict. It destroys the harmony of interests in the free society and is of no benefit to the economy as a whole, and the institution of central banking is therefore essentially pernicious. It only exists due to intellectual error: people believe that it is necessary to prevent a collapse of banking, that deflation is evil, that economic growth requires an increasing money supply and so on. The Misesian analysis of central banking, which we have here sketched out, builds on the insights of classical economics and the currency school. Correct economics shows that an increase of fiduciary media or of fiat money cannot bring prosperity, a sound economy or a harmonious society. Therefore, the only policy conclusion it can lead to is the abolition of central banking.

We have so far avoided an ethical analysis, but we will conclude with this. It is true that central banking is an institution foreign to a free and just society, and that it can only exist due to special privileges. Central banking is not, however, fraudulent. There is nothing fraudulent in issuing fiat dollar or euro notes. The ethical problem lies in the coercive monopoly of fiat money production.

Were this to be abolished, the main moral issue of central banking would vanish. So would, of course, the institution itself.

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