

Joel M. Fiscus

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Dr. Herbener

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An Austrian Look at the Price Revolution

The currency of a society is the medium which facilitates the exchange of goods or services between individuals or groups of individuals in the market. Currency acts in such a manner because it represents the perceived value of goods or services at a specific moment in time and because it allows individuals to trade goods during a present time frame, then postpone the exchange of the currency which represents the value of that individual's present goods for other goods which he values more than the value of his previous goods, at a later point in time. However, if the role of money as a store of value is compromised, there can be severe consequences on the market, as can be observed historically through an analysis of the Sixteenth Century Price Revolution in Western Europe. The Sixteenth Century Price Revolution began to emerge as early as 1470 and lasted until as late as 1650, making it overwhelmingly the most prolonged and influential occurrence of widespread rampant inflation in modern history (Fischer 70). As is the case with many historical/political events whose repercussions were widespread and rampant upon society at the time of their occurrence, the Sixteenth Century Price Revolution became a watering ground for economic theorists and historians eager to test their own personal theories against the data present from the time and to make a name for themselves in the intellectual community based upon their findings. In fact, the complexity of the situation and the obscurity of data from the time period lend itself quite well to the testing of theories and the manipulation of data in order to prove these theories. This longstanding debate not only revolves around the impetuses which spurred and sustained the inflation in Western Europe, but also effects that this inflation had on the society in terms of the viability of inflation as a source of economic stimulation. A number of economically contested ideas, including the quantity theory of money, the

Malthusian population theory, Hamilton's profit inflation theory, which influenced Keynes's active fiscal policy and his multiplier effect theories, some of the models and ideas from Adam Smith's *Wealth of Nations*, and a number of other theories whose effects have been less dominant upon modern economic thought, claim close historical and economic ties to the information which these intellectuals gleaned from the Price Revolution. However, a comprehensive analysis of the viable data remaining from the time reveals that a number of the ideas which influenced many of these divergent views were involved in the Price Revolution to a lesser extent than the theorists may have emphasized and the dominant factor in understanding the phenomenon is the manipulation of the money supply and the effects that said manipulation had upon both the domestic and foreign economies of the time.

The Sixteenth century was a time of catalytic change in Western Europe. With the discovery and exploration of the New World abroad and additional technological advances which preceded and contributed to the modernization of the financial industry and the Industrial Revolution two centuries later, the face of Europe was beginning to change in a very substantial way. The Price Revolution was preceded by the Renaissance, which is overwhelmingly considered an era in which the populations of Western Europe experienced relative peace, harmony, and stability (Fischer, 63). In fact, one of the most substantial reasons that the Price Revolution protruded in such stark disparity from the Renaissance is that the countries of Western Europe had been experiencing equilibrium in terms of the prices of commodities and labor during the fifteenth century, and even a very subtle deflation, as opposed to the violent inflation experienced during the sixteenth and seventeenth centuries (Fischer, 51). The Bubonic Plague had wiped out nearly a third of

the population of Europe in the Fourteenth century, concentrating the previous wealth of these individuals in the hands of the remaining two-thirds (Munro). In addition to this, the Catholic Church had strict bans against usury, which is essentially the act of charging interest on currency loaned to others, and the mines which served as a source of precious metals were producing at a low, constant rate (Munro). However, technological advances in the mining industry, as well as the prolificacy of currency debasement by royals, and the emergence of Protestantism as an alternate to Catholicism began to disrupt this equilibrium in a way which, to this point, had not been thoroughly documented by historians. Also, structural changes in Mediterranean trade with Ottoman conquests, diverted more and more of the new silver flows away from the Levant to north-west Europe from 1517 (Munro).

One of the first historical references to the beginning of the price inflation phenomenon occurred during the festival of San Giovanni in Florence June 24, 1491 (Fischer, 65). A month before this festival of celebration of the economic prosperity of the country, the mint-masters had issued a new Florentine coin which they claimed would perform miracles on the economy (Fischer, 66). Shortly after this celebration, their leader Savonarola was seemingly murdered by his incompetent physicians, and the country was cast into widespread poverty and conflict, as Savonarola's son, as well as his son's replacement were both incapable of supporting and defending the country (Fischer 68). In response to the devaluation of currency and the political turmoil, prices surged to unprecedented rates during the 1490's as the economy began to fail, marking the beginning of what was about to become a widespread phenomenon across Western Europe (Fischer, 68). However, this debasement phenomenon was certainly not an

isolated occurrence. In fact, Henry VIII of England is infamous for his “Great Debasement”, a program which initially debased silver coinage by 11.11% in 1526, which he increased by an additional 23.14% in 1542 (Munro). Additionally, his successor Northumberland debased the fine silver content of the penny to an amount which was equal to an overall reduction of silver content by 83.1% from the 1526 coinage (Munro). Queen Elizabeth restored the silver coinage to the traditional fineness of 92.5% fine silver in November 1560, but by this point, the Price Revolution had come into complete fruition, and a number of other factors contributed to the continuation of rampant inflation in Western Europe (Munro).

As stated previously, the Sixteenth Century Price Revolution began to emerge as early as 1470 and lasted until around 1650, an incredible 180 years, making it by far the longest instance of prolonged price inflation in modern history (Fischer 70). Although the prices increased by average only about one percent per year during this period of time, making it seem almost insignificant in reference to modern rates of inflation, the most remarkable aspect of the era was the length which the inflation endured (Fischer, 70). As the inflation of prices become apparent in the early to mid-sixteenth century, England’s Parliament reacted in response to this peculiar phenomenon by forbidding the exports of food and wood until prices rose above a specified level (Fischer, 75). As is often the case with trade barriers, the institution of these “protective” tariffs are contagious and usually mimicked by other countries, crippling trade, and harming the economies of each of these countries in significant ways. The decade of the 1590’s was the furthest point of economic degradation during the Price Revolution (Fischer, 91). At this point, the real wages and industrial prices remained at a depressed level, while fuel and food costs

continued to climb at an increasing and unstable rate (Fischer, 92). However, by the mid-seventeenth century the crisis had come to an end, and equilibrium appeared once again throughout Europe after a period of economic transition and rehabilitation (Fischer, 102).

In order to clearly understand the effects of monetary inflation in the Sixteenth Century Price Revolution, it is essential to first have an understanding of the concepts of the supply and demand of money in a market economy. According to sound economic theory, “supply is the total stock of a commodity at any given time; and demand is the total market demand to gain and hold cash balances, built up out of the marginal-utility rankings of units of money on the value scales of individuals on the market (Rothbard, 160)”. One of the most unique aspects of money as a commodity is that it is not desired to be consumed (Rothbard 297). The demand-to-hold aspect of money is what gives it such a distinctive function of being able to be held as a stock for future sale, which is incredibly important in understanding inflation, which is the devaluation of currency in relation to the current stock of commodities in a market (Rothbard 197-198). In the market for money, a commodity which allows for the indirect exchange of goods and services by acting as a medium of exchange and a store of value, the supply of money is either very durable in reference to production at any moment in time in such systems as the gold standard, or it is determined exogenously to the market most usually by the government (Rothbard 297). One of the most unique aspects of the Price Revolution in Sixteenth century Western Europe was that the gold standard was disrupted by an unprecedented influx of new precious metals due to technological advances in the mining industry and the discovery of new mines in the Americas in the latter half of the Sixteenth

century as well as the emergence of monetary notes controlled exogenously by federally controlled financial institutions (Munro).

The inflation of currency is tempting to those increasing the money supply because the money which they inject into the money supply is not expected by the market, and it is accepted by others under the expectation of a stable money supply (Rothbard 300). Essentially, money represents the value of the good that it is exchanged for at the specific moment of the exchange. Because of this, the value of money is backed by previous production, and it allows for the distribution of goods in the market to be allocated in such a manner in which they represent the most desired demands of the individuals in that market. If an entrepreneur produces more of a good than is desired, that entrepreneur suffers a loss and is forced to sell the goods at a price at which those in the market are willing to pay for that good, and he will reduce the production of that good so that he will not suffer further losses. However, if currency, which is not backed by previous production, is introduced into a market, the currency will break this balance and the allocation of resources in the market will not actually reflect the demands of consumer. For this reason precisely, inflation is extremely attractive to inflators because it allows these individuals or groups of individuals to purchase the goods or services which they desire at little actual cost to themselves, yet at the market price in society which is based on the desired allocations of resources by others in the market. When this occurs, the demand for these goods rises along with the prices of these specific goods (Rothbard 300). Gradually, this new money makes its way through the economy raising the demand for certain goods as the prices for these goods on its way, eventually redistributing income and wealth to those who initially introduced the new money into

the market as well as those who received the new money early at the expense of those who received the new money later during this process or those who may have a fixed income and did not receive this new money at all (Rothbard 300). Because of this, there are two different types of shifts in relative prices caused by the increase in money: “(1) the redistribution from late receivers to early receivers that occurs during the inflation process and; (2) the permanent shifts in wealth and income that continue even after the effects of the increase in the money supply have worked themselves out. (Rothbard 300)”

In addition to this, the new money in the market causes a systematic distortion of the production structure, or a lengthening out of the production structure beyond what is actually sustainable in the economy. The reason that this occurs is that these investment processes which had previously not appeared to be profitable for investment appear to be profitable due to an increase in loanable funds not backed by savings which are consequently receiving investment from entrepreneurs. The production structure will lengthen and widen at the higher stages of production because these are the stages which had previously been unprofitable for investment. These new processes of production take time to complete, and this lengthening process is therefore justified if individual’s time preferences also go down, but since that money supply was increased by credit expansion, this is not the case. When these entrepreneurs begin the new supposedly profitable business ventures, they are forced to pay higher wages to their employees in order to bid them away from the employment stages already available in the existing stages of production. However, the price of natural resources and factors of production will increase due to the fact that there wasn’t actually any capital investment funding the increase in the money supply, raising the overall price of production for the employers.



Since these business ventures still appear to be profitable at first, the entrepreneurs continue to invest in them and to pursue them, and the demand for consumer goods will actually increase. In a vivid example of the Ricardo effect in reverse, the wages will begin to decrease faster than the price of consumer goods, and they will bid back down the structure of production to the lower stages of production which will now once again become more profitable than the production process at the higher stages of production. This reversal will cause a massive readjustment of the production structure in a number of ways. One of the most devastating effects of this reversal is that the entrepreneurs who had previously engaged in malinvestment now experience a cluster of entrepreneurial error. Because their investments are faltering, and they are no longer experiencing the profits necessary to fund their investments and complete them in a manner in which they could continue to experience profit, they will demand more loans to finish paying off these investments. However, the causal effect of an increase in demand upon any market, include the market for capital funds, is a shortage of supply which correspondingly results in an increase in the price of that commodity, which in this case is loanable funds. Because of the higher interest rates, some production processes that had been begun at the higher stages of production will not be finished because the entrepreneurs will have gone bankrupt and will not be able to finish their investment in these processes resulting in a waste in investment from sunk capital, resulting in less capital than had existed before the capital expansion. Some of the immediate effects of financial reversal of the boom are stock market crashes in addition to the increase in interest rates and loss of capital. The bust of the business cycle is the liquidation of the investments which should not have existed in the first place. This reversal happens because of consumer

preferences, and the fact that these processes were not backed by investment. The bust that occurs is asymmetric from the boom. The prices of capital goods and factories collapse and the process continues until the capital structure is shortened again in a manner which satisfies consumer preferences.

A few examples from history which exhibit this process in effect will be noted shortly below. Although numerous factors affected the money supply and contributed to the inflation of this time period, currency debasement most closely represents the framework set out by the Austrian business cycle theory, and thus will be the center of this discussion. By the mid 16<sup>th</sup> century, England had debased his currency a baffling 81.2% in less than thirty years (Munro, *American Treasure and the Price Revolution*). In addition to this, “the Spanish Habsburg Netherlands experienced a veritable financial revolution involving both negotiability and organized markets for public debt instruments (Munro, *American Treasure and the Price Revolution*)”. Given the insufficient historical data from this time period, it is difficult to analyze the production structure of the economies of Western Europe during this time period. However, any graphs depicting the price levels of certain products during this time period show very strong booms and busts following increases in the money supply, while the overall price level continued to increase. Also, it is historically evident that wages continued to fall as prices for goods increased.

Before considering an in-depth investigation of all how Austrian theory relates to the Price Revolution, it is first important to conduct an analysis of the popular causes which theoreticians over the last four hundred years have attributed to igniting the Price Revolution. It can be said that the long-contested historical debate concerning the Price

Revolution of the Sixteenth and Seventeenth century Europe originally commenced in an article written by Jean Bodin in 1578 which can be translated as “The Response of Jean Bodin to the Paradoxes of Malestroit and The Paradoxes”. It was not again until Georg Weib reasserted the classical thesis in 1895, though, that the debate was reignited in scholarly discourse. In 1928, Earl Hamilton published his first work on the role of monetary inflation in the Price Revolution of Sixteenth and Seventeenth Western Europe. After the publication of “American Treasure and Andalusian Prices, 1503-1660: A Study in the Spanish Price Revolution”, Hamilton published a number of other pieces asserting his basic argument that the root cause of the Price Revolution was monetary inflation and that this resulted in a disparity between the prices of goods and the cost of labor, which increased the wealth of capitalists and caused the industrial revolution, a phenomenon which he calls profit inflation. This argument was met violently by a number of opposing views ranging anywhere from the belief that monetary inflation was influential, but the profit inflation argument is insufficient, to an adaptation of the Malthusian argument, which argued that the Price Revolution was not caused by monetary changes at all, but by demographic adjustments.

Although the Malthusian approach to the Price Revolution was preceded by early explanations referring to the alteration of the money supply, it will be considered before these arguments, as well as the momentous Malestroit and Bodin debate because it completely sidesteps the debate concerning the effect of an increase in the money supply upon the economy. According to this argument, as a result of the relative prosperity and tranquility of mid-fifteenth century Western Europe, the population of these countries increased at an alarming rate during this period of time (Fischer, 72). For example, the

approximately two million inhabitant population of late fifteenth century England rose rapidly to a number exceeding four million by the end of the sixteenth century (Fischer, 72). The argument is that the population increased at a rate greater than that which was possible for the production of food products, since the tertiary land available for cultivation was of lesser value than the land which had currently been in cultivation (Fischer, 74). The rise in food prices was unmatched by the prices of industrial goods, but followed quickly by an increase in the cost of energy-related goods (Fischer, 74). However, while population growth may have played a role in influencing relative price changes, it is insufficient in explaining the massive economic change that occurred during this period of time. For example, the Malthusian population theory requires all productive land is already in cultivation and that as a result of an influx in population growth, nominal land is also brought into cultivation at a higher cost and with a lower output, making the prices for food sources go up, which results in the costs of other goods in society also going up. However, this theory operates under the assumption that all of the good land is already in use, while this may not be the case. In the Fourteen Hundreds, Western Europe was ravaged by the Bubonic Plague, and it was not until the Sixteen Hundreds that the population really began to reach previous levels, indicating that some good land could have still remain uncultivated at the point. Even more importantly that this, the theory is misattributing one of the effects of inflation to having caused this inflation initially. When inflation occurs, it reduces the real income of individuals. Because they have less money to spend, they spend this money on the commodities which their demand for is least; essentially the goods that are most important to them such as food and shelter. Because of this, the demand for these goods, relatively,

increases, and since an increase in demand not met by supply results in the price of these goods being bid up by consumers, an increase in the price of these goods soon follows. The cultivation of tertiary lands may increase the prices of production at some point, but if people aren't willing to pay these prices, the lands won't be cultivated. There must first be an increase in demand, and although a population increase could attribute to this to an extent, an influx of inflation caused by monetary factors is much more probable.

Although economics was not widely recognized as a school of thought until around the Eighteenth Century, a number of scholars had been dabbling in political philosophy for a long period of time before this. One of the first intellectual references tying monetary factors to the Price Revolution was made by Martín de Azpilcueta in the early Sixteenth Century, but the first modernly contested expositions on the subject was made by Jean de Bodin shortly after this. The article, "*La Response au paradoxe de monsieur de Malestroit, touchant l'encherissement de toutes choses, et le moyen d'y remedier*", written by Jean Bodin in 1568 in response to the article "*Du seigneur de Malestroit sur le fait des monnoyes*", written by Malestroid in 1566, establishes the link between the influx of gold in Spain and the rampant of inflation of Spain's primary trading partners in what can be considered one of the first expositions on the quantity theory of money (Steczowicz, 1). In Malestroit's analysis, he divides his study into two different arguments. The first argument deals with the prices of currencies such as gold and silver in terms of an abstract idea of money (Steczowicz, 6). He states that although the amount of currency required to purchase a certain good has increased, since the purchasing powers of other currencies has also increased, the price of that good has actually remained stable (Steczowicz, 6). The second argument focuses on income and

purchasing power (Steczowicz, 6). His claim is that the rise in nominal prices is responsible for inflation and its disastrous implications on the economy (Steczowicz, 6). However, he failed to realize that while this situation is detrimental to those with a fixed income, it is actually highly beneficial to others (Steczowicz, 7). Merchants, craftsmen, and farmers benefit by receiving profit, while common laborers become impoverished by the process (Steczowicz, 7). Also, creditors incurred losses, while debtors saw that the interest being paid on their loans was decreasing because of the devaluation of currency (Steczowicz, 7). In response to Malestroit, Bodin argues that the inflation was caused by an overabundance of gold and silver currency which was contradictory to the contemporary thought of the time (Steczowicz, 8). Bodin also attributed the Price Revolution to other causes, such as “monopolies of prices imposed by workers and proto-syndicates, the shortage of goods caused by excessive trade and waste, the whims of princes whose likes and dislikes dictate the value of things, and lastly, the alteration of the valuation of money (Steczowicz, 9). However, Bodin and Malestroit’s arguments are actually, in fact, complementary to each other. For example, Malestroit’s argument concerning the debasement of currency is applicable until about 1560 when the Spanish gold started to affect the French economy through inflation (Steczowicz, 10). As previously stated, this argument put forth by Bodin was one of the first clear expositions of the quantity theory of money. This led economist Henry Thornton in 1802 to assume that more money equals more inflation, and an increase in money supply does not necessarily mean an increase in economic output. A great number of advancements have been on this subject since then, but the primary assumptions still remain relevant.

One of the most major economic debates of all times, which still remains highly contested and is strongly debated by several different modern economic schools, deals with whether or not inflation can be viewed as a viable policy tool in economic expansion, and is drawn from theories which were first developed by the consideration of the Price Revolution. Earl Hamilton was a historical economist who focused much of his career on analyzing the Price Revolution from historical data and tying his own personal ideas and theories to the data that he had accumulated. Earl Hamilton claimed that the sustained era of inflation, from the early Sixteenth Century to the mid-Seventeenth Century was fundamentally the product of monetary factors. In addition to this, he developed a very interesting theory based on the data that he accumulated which directly influenced a number John Maynard Keynes's theories in his magnum opus "The General Theory of Employment, Interest, and Money". Regardless of one's own economic views, it is difficult to argue that the work of Keynes was not one of the most influential economic writings in accordance with public policy and political decision making in modern economics. In reference to this, it is essential consider the ideas which influenced him, and their validity in terms of historical accuracy. Essentially, Hamilton argued that the principal consequence of the Price Revolution was "profit inflation", which was the fundamental instrument in the birth of modern industrial capitalism (American Treasure and the Price Revolution in Spain). He argued the theory of profit inflation, which is the idea that the inflation we suffer from despite the recession which also occurring is caused by excessive profits far in surplus of the marginal worth of capital (American Treasure and the Price Revolution in Spain). Essentially, since there was a widening of the gap between prices and industrial wages, the profits of the entrepreneurs kept increasing,

making expansion profitable (American Treasure and the Price Revolution in Spain). In defense of this argument, he discussed how inflation affects certain sectors of the economy differently, altering the relative prices of a wide variety of individual goods and services (American Treasure and the Price Revolution in Spain). Since labor didn't rise in tandem with the CPI because of numerous factors, including Keynes' much contested sticky wages idea; he argued that the profits of entrepreneurs increased and that this was the catalyst for capitalism and technological advancement in the industrialization of Western Europe (American Treasure and the Price Revolution in Spain). The following quote very succinctly encapsulates his logic:

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Let us assume that of every 100,000 pounds' worth of goods produced by a capitalist in England or France at the beginning of the sixteenth century 60,000 went to wages, 20,000 to rent, and 20,000 to profits..... [It is not] unreasonable to suppose that at the close of the sixteenth century the same product would have been sold for about 250,000 pounds; that wages would not have amounted to more than 75,000; and, making the unreasonable assumption that rents did not lag behind prices, not more than 50,000 pounds would have gone to rent. Profits amounted to 125,000 pounds, or 100 per cent on the turnover. The lag of wages behind prices has quadrupled profits. The windfalls thus received, along with gains from the East India trade, furnished the means to build up capital equipment, and the stupendous profits obtainable supplied an incentive for the feverish pursuit of capitalistic enterprise (Hamilton, 356-57).

While this theory of "profit inflation" may seem plausible on the surface, there are a number of shortcomings which degrade its validity as well as the validity of many claims which Keynes made upon this assumption. A full analysis and critique of Keynes' theories was made most brilliantly by Hayek in his "Treatise on Money", to which Keynes responded with praise claiming that, having been moved by this writing, his thinking no longer reflected that professed in his previous work, while he did maintain his ideas concerning the validity of deficit spending in some circumstances (Hoover 152).



However, while this analysis cannot be expounded here due to the complexity and lengthiness of the argument, it is interesting to consider that the framer of much of modern economics in public policy actually admitted defeat to one of his intellectual opponents upon considering the logic of his arguments. Still, though, these ideas remain in practice even today, and although a full analysis and extrapolation on Keynesian economics will not be made within these paragraphs, a dismantling of one of the main ideas which influenced his theoretical framework will reveal the flaws in his thinking.

Attacks on the Hamilton Thesis were made by a number of different economists from many different schools of thought, including John Nef of the Chicago school of thought, one which professed what is now considered as Neoclassical Economics, and David Felix of Post Keynesian School of economic thought, which attempted to rebuild the theory of economics in light of the new insights and ideas presented by Keynes in his writings (Hayes). The attack made on the Hamilton Thesis by John Nef was expressed in his “Prices and Industrial Capitalism in France and England, 1540-1640”. A basic summary of his argument is as follows. One of his first arguments is that France seems to have much more “profit inflation” but England had much more growth, however this can be contested by the fact that England wasn’t affected by the wars which affected France during this period of time (Money, Prices, Wages, and ‘Profit Inflation’, 24). He claimed that, while there is a coincidence between profit inflation and the growth of industrial capitalism in three of the four periods that were held under consideration, more recent evidence on wages actually indicates that money wages rose at a much higher rate than previous data had professed (Money, Prices, Wages, and ‘Profit Inflation’, 24). In addition to this, if the standard of living of working people would really have fallen by

any approach approaching the proposed 50 percent, this lost of demand could easily have offset the advantage of the producers (Money, Prices, Wages, and 'Profit Inflation', 25). This argument very clearly expresses the basic framework of supply and demand theory, indicating that if the demand for a good is reduced by any factor in the economy, the suppliers will be faced with a surplus of production, which will then force them to reduce their prices in order to find buyers willing to purchase their products. Since much of the market for goods consists of workmen who represent a majority of those making purchases in an economy, if their real income rates were following, they would reduce purchases, which would reduce the demand for a number of goods in the economy, and would result in a fall in the actual prices of produced goods. This economic principle clearly undercuts Hamilton's Thesis because it is very difficult to rationalize how profits could continue to skyrocket, when no one is demanding and purchasing the goods being produced. Indeed, if there was a widening gap between wages and profits, there must have been some other cause to the advance of capitalism. This evidently seems to be yet another occurrence of a theoretician attributed an effect of an event to having caused that event, which raises the question of why capitalists were receiving increasing profits while the workman were not, and how this could have contributed to the advancement of capitalism. While it seems evident that a major factor in this historical economic situation lies in the idea of monetary theory and the fact that in during an instance of inflation debtors benefit greatly at the expense of lenders who receive diminished return on their loans due to the devaluation of currency, this discussion will be made in the following paragraphs.

The argument proposed by David Felix is summarized concisely by the following quote:

...industrial profit inflation is not much in evidence in the periods to which he refers ... [and] it is even possible that it was nonexistent, although this may be too bold a counterclaim in view of the gaps and obscurities in the evidence. But even if it did exist in a much reduced degree, it does not appear to have been a decisive force in determining rates of industrial growth' (Felix, 441).

His argument claims that there is no correlation between the degree of price inflation and the degree of profit inflation, or between the rates of profit inflation and the apparent rates of industrial growth (Money, Prices, Wages, and 'Profit Inflation', 28). He bases his depiction of inflation in terms of agricultural and wood product prices and indicates how price increases for many finished goods lagged behind the rise in the cost of their raw material components (Money, Prices, Wages, and 'Profit Inflation', 28). This change in the relative prices of the factors of production would have been enough of an incentive for technical change, and provides a better explanation to why capitalism would have advanced during this period of production than does Hamilton's Thesis (Money, Prices, Wages, and 'Profit Inflation', 28). According to the Austrian theory of money, an exogenous increase in the supply of fiduciary media, or commodity money to an extent in this case, will cause an unexpected widening and lengthening of the production structure, increasing the demand for factors of production. However, since these new production processes are not actually demanded by consumer preferences, many of them will fail, and a portion of these factors of production will have been wasted. Still though, with the prospect of diminished profits due to an increase in the prices of goods, many entrepreneurs in all levels of the production structure will look for more efficient and cost-effective ways to produce their goods. These advancements in technology; however,

do not expunge the damage that is done by wasting factors of production, and are instead, simply a by-productive of the situation. It cannot be argued concisely that these advancements could not have occurred without inflation and the damaging effects that it has on the economy, yet it is evident that this can be a catalyst. While economists strongly emphasize this as an advantage to inflation, they fail to realize that the disruption of the monetary system prevents a number of individuals from investing due to the fact that they are aware that they will receive diminishing returns on their money, and that economic growth as a whole will be impaired by this, while some technological advancements may have been made.

One of the most glaring oversights made by Hamilton in the exposition of his “profit inflation” theory is his claim that the lack of profit inflation caused Spain’s economic decline in the Sixteenth and Seventeenth Centuries. However, this is a huge historical oversight, which indicates that he had failed to fully comprehend monetary theory and had insufficiently considered the effect of the influx of currency in Spain because of the discovery of new precious metals in the Americas. Even a brief analysis of the history of Spain clearly indicates that the influx of new currency in Spain brought great wealth to that country for a period of time and caused them to import a vast amount of goods and services from other countries that were not experiencing an extension of their money supply. While this caused inflation in the other countries, as previously mentioned, it did also result in technological advancements in their production industries, while Spain seemed content on simply importing the goods and services which they desired from others. However, when their mines began to run dry, and the amount of new currency that they were receiving diminished, they were left with an economy that had

very little capacity for production, which consequently led to their decline. Another historical example which discredits his theory is that Brabant actually had “profit deflation” without negative consequences (Money, Prices, Wages, and ‘Profit Inflation’, 34). In conclusion to this debate, one may claim that studies in the behavior of real wages, let alone a search for potential “profit inflation”, tell us very little, if anything at all, about the sources of industrial and economic growth (Money, Prices, Wages, and ‘Profit Inflation’, 35).

The most promising and enveloping factor which can be used to tie the widespread rampant inflation in Western Europe to the industrialization and advancement which occurred shortly after, is the economic principle that long-term inflation cheapens the costs of capital investments. During inflation, real interest rates fall, and in a society which is unfamiliar with the effects of long-term inflation, many lenders may fail to realize that the real values of capital payments would have fallen, year by year, while the value of their outputs rose. This also explains why the layman of Western Europe were impoverished, while the debtors and capitalists actually profited off this and began to set the foundation for the Industrial Revolution.

One of the most interesting aspects of the Price Revolution debate lies in its relevance to current economic political actions in the United States. Although there were a few factors involved in the Price Revolution aside from the influx of new currency and the debasement of currency already present in society, monetary factors are truly essential to understanding the event. Henceforth, it is very obvious that the main reason that the inflation occurred initially was the debasement followed by the importation of currency at a rate greater than that which had previously existed. In this regard, it is very

interesting to analyze the event from a perspective which takes into context the current economic situation of the United States. Although the debasement of commodity money and the importation of new precious metals caused the economic situation of Sixteenth Century Europe to fall into a slightly different economic category than the present economic situation in the United States where a Federal Reserve bank is increasing the supply of currency by printing new money exogenously, the effects of inflation regardless of the cause are very consistent. Essentially, inflation in the economy is always caused in some capacity by intervention in the monetary market. In the modern American economy, intervention in the money market occurs in terms of the Federal Reserve board issuing fiduciary media to banks or by simply printing new money. In either case, the effect on the economy is the same: the new money that is being added to the money market is not backed by previous investment or goods, so although it may appear to be worth as much as the money that is backed by investment, its immediate effect will be that it will reduce the value of all of the other currency in the economy and cause the prices of goods to increase (Rothbard, 850). Those who receive the money first receive the most benefit for it because it is valued at the same rate as the real currency in the market, while those who receive it last actually will see a reduction in their income because they have been receiving a fixed wage while the prices of goods has been increasing (Rothbard, 51). The effect of monetary inflation in the Price Revolution was very grave. However, Hamilton, and later Keynes, manipulated the facts to make support the idea that monetary inflation can actually be beneficial to the economy, an idea which policy makers presently hold today. In fact, Ben Burnanke, the current chairman of the Federal Reserve board, was quoted recently saying, "The U.S. government has a

technology, called a printing press that allows it to produce as many U.S. dollars as it wishes at essentially no cost." Modern popular economics has ignored the great lessons from history and is on a straight track to repeating the same mistakes as have been made in the past. Despite any technological advancements which may or may not have taken place anyway without inflation, the price grain increased about six-fold, while real wages were cut in half (Fischer, 92). While production may have increased, the general living standards of individuals in this time period fell drastically. If the purpose of manipulating the money supply is supposedly to enhance the economy so that the constituents of politicians will benefit from this growth, then why are they undertaking a plan which has been shown historically to reduce the living standards of society and to cause massive readjustments in the production side of the economy, resulting in the waste of capital? Honestly, the answer to this is simpler than it may seem to be, and it relates directly to the structure of our political system. In order to maintain employment, politicians must please their constituents by making laws that will benefit them. Because American citizens rely on their politicians to respond to every negative situation in society with litigation, they are forced to manipulate the money supply so that they can afford to pay for all of these programs. In addition to that, once a country starts manipulating the money supply they get a boom and bust cycle and must monitor it heavily in order to prevent the busts from reaching rock bottom, which only postpones the economy from working itself out again to reflect actual consumer demands. In modern economics, the M1 money supply consists primarily of general currency and checking accounts. The M2 money supply, however, is more inclusive in that it includes all of the money counted under M1, plus savings accounts. In addition to this, the M0 money supply consists of

the currency in circulation, the money stored in bank vaults, and commercial bank deposits with the Federal Reserve. From January to December 2009, M1 increased 7.6 percent, while M2 grew by about 2.8 percent, and from January to December 2009, M0 grew by 19 percent. However, in a slightly longer period which includes the fall 2008 response to the economic crisis, it grew by a baffling 139 percent. As of December 2012, the Federal Reserve plans to promote a stronger pace of economic recovery through the purchase of \$600 billion of longer-term Treasury securities over the next eight months. Although all of this money will not immediately enter the economy, inflation is still bound to increase and it is probable that the recession which the United States is currently in will not be resolved until the United States adopts a different strain of fiscal policy.

The great inflation was caused primarily by monetary factors, in addition to other factors caused by trade and government intervention. While this increase in inflation caused a reallocation of resources in the economy, because the demand for factors of production was raised without a simultaneous increase in the overall demand for goods in the market, this raised the cost of producing for entrepreneurs, encouraging the technological advancements which eventually brought about the rise of capitalism. However, while this may seem to be a great accomplishment, these technological advancements could have occurred without inflation, and in the absence of all of the vast side effects of the debasement of currency. The standard of living of the average individual in society plummeted during this period of time, while the governments and the wealthy entrepreneurs continued to steal from the average workers through inflation. In essence, history has shown us that inflation is not a viable technique in boosting the



economy, and doing so will affect the economy negatively more than it will affect it positively.

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