A comparison of the Philosophies of John Law & Georg Simmel

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John Law, the 18th century theorist, is often remembered for his failed policies in France. John Kelly however, seeks to restore his profile as a theorist. He compares the work of Law to the philosophy of George Simmel, concluding that Law, as a theorist on the issue of money, was ahead of his time.

The difficulty lies, not in the new idea, but in escaping from the old ones, which ramify, for those brought up as most of us have been, into every corner of our minds.
John M. Keynes – ***The General Theory of Employment, Interest and Money***

...it is no argument against any thing propos'd for the general good, to say it is new, and what has not been practic'd.
John Law – *Money and Trade Considered*

Introduction

The lives of few economists would excite the interests of a Hollywood studio, but the exploits of John Law, the 18th century monetary theorist, would certainly make a compelling movie. Any A-listed actor would relish the role of the dueller, the professional gambler, the most eminent social climber of eighteenth century French society, and the Scottish murderer who eschewed the typically dour character of his native country to rise to the apex of the government of his adopted home. It is primarily due to these exploits that Law is only perceived as a man of action, whilst his monetary theory and reasoning are considered flawed, or not considered at all.

However, important elements of Law's thought should be more reappraised along broader lines, as he did not work within the structures of any school of economic thought. Law not only recognised money as a developmental process, but also made huge efforts to advance this process. I will argue that Law, instinctively rather than formally, grasped the true concept of money, and was more in sympathy with the monetary thinking of the 1930's than the 1730's. In particular, I will argue that *The Philosophy of Money*, Georg Simmel's (1990) seminal work, makes explicit the sort of implicit reasoning upon which Law based his monetary theory and policy. I will outline Simmel's philosophy of money, and then demonstrate its striking similarities with the theoretical construct that served as the basis for Law's monetary thought and policy.

The Theory/Practice Dynamic in Money & Banking

> *If the materialistic interpretation of money now appears to be an error, historical analysis shows that this error was not accidental but was the appropriate theoretical expression of an actual socio-logical condition, which had first to be overcome by the real force before its theoretical counterpart will be overcome in theory* (Simmel, 1990: 174).

Throughout the history of money, banking and finance theory has tended to follow rather than lead practice. In Law's era the banking activities of Goldsmiths were ahead regulation, and this can still be seen in financial innovations today. The pace of financial innovation, driven by self-interest, or in Law's case, national interest, will always be ahead of regulation, and ahead of theory. In this sense, theory serves not as a prior rational for practice, but rather a post hoc rationalisation of practice in an effort to make sense of the forces driving practice to better understand future circumstances. "The urge to explain has to rest content with investigating these processes and treating them as (unconsciously) effective causes, although they merely symbolize the real course of events"(Simmel, 1990: 145).

Therefore, it is quite conceivable that whilst Law could 'work out the economics of his scheme with brilliance', based upon an intuitive grasp of the philosophical nature of money through considered reflection, the formal exposition of the nature of money in a theoretical context might not occur for some time afterwards. This exposition is most thoroughly outlined in Georg Simmel's (1990) work, *The Philosophy of Money*. Law's vision of what money and the banking system could become was based on ideas consistent with much later reasoning, and was also strikingly similar to the structure of the modern banking system.

This is of considerable credit to the incisiveness of his thinking. As Murphy puts it, "Law failed as a policymaker. However, he displayed great theoretical vision in his writings, a vision close to the actual structure or our modern monetary system"(Murphy, 1994: 15).

Georg Simmel's Monetary Philosophy

(A) Money Objectifies Subjectively Imposed Values

Simmel (1990) contends that in philosophical terms, the natural order is one of equality between all concrete matter, whilst values are imposed by the individual, based not merely on the economic good in question, but also the individual's subjective relation to them. Economic value arises from 'distances' to initially unattainable goods, which are overcome through exchange. Thus it is the function of money as an exchange mechanism that constitutes its value, and "If the economic value of objects is constituted by their mutual relationship of exchangeability, then money is the autonomous expression of this relationship"(Simmel, 1990: 120, also 125, 128).

Money and value are linked not directly, but indirectly through exchangeability, and as this becomes more complex, the more value can be objectified via money. (Simmel, 1990) Money as the perfect tool for exchange seems itself the embodiment of objective value, whilst it retains its subjectively imposed value origins. Values undergo a Cartesian objectification through the process of exchange, facilitated by money. "Since everybody offers for exchange what is relatively useless to him, and accepts in exchange what is relatively necessary, exchange effects a continuously growing utilisation of the values wrested from nature at any given time"(Simmel, 1990: 292). Money, by facilitating the exchange process provides a compelling impetus to economic activity.

(B) Monetary Values as Relations

Whilst money might appear directly comparable with subjective value judgements at a superficial level, this is not case.

> *The equation between the value of a commodity and the value of a definite money does not signify an equation between simple factors but a proportion, that is an equation between two factors, the denominator of which, within a given economic area, is on one side the sum total of all commodities and on the other the total amount of money* (Simmel, 1990: 136, also 120, 147).

However, individuals need not be directly aware of these implicit denominators in their calculations to behave rationally. Simmel (1990) used the example of water flowing through a pipe to explain that whilst money and value are related this does not necessitate comparability.

(C) Money as a Process of Development

Simmel (1990) views money as a developmental process, at the end of which it becomes a pure symbol. This pure concept of money is equivalent to a Platonic ideal, and as such can only be approached incrementally, but never attained.

> *Whatever may be the historical origin of money- and this is far from being clearly established – one fact at least is certain, that money did not suddenly appear in the economy as a finished element corresponding to its pure concept. Money can have developed only out of previously existing values in such a way that the quality of money, which forms part of every exchangeable object, was realized to a great extent in one particular object; the function of money was at first still exercised, as it were, in intimate association with its previous value significance* (Simmel, 1990: 119).

Simmel (1990) cites the start of this development with Mercantilism, where money in the form of specie is fallaciously taken to directly represent value. Yet as exchange becomes more complex, the more value can be objectified via money, and the less is the need for it to be grounded in specie. He claims that this limitation on money was recognised as unnecessary in the 18th Century and that now there exists many forms of value not recognised as such before. The notion of value is extended to different ideas and implements in sequence as humanity learns to exploit them more fully, and old limits to the definition of money are rendered obsolete.

(D) Philosophical Nature of Money

> *Through all the discussions of the nature of money there runs the question as to whether money, in order to carry out its services of measurement, exchange and representation of values, is or ought to be a value itself; or whether it is enough if money is simply a token and a symbol without intrinsic value, like an accounting sum which stands for a value without being one* (Simmel: 1990: 131).

Based on Simmel's earlier reasoning the answer to this question becomes a tautology. Purely symbolic money cannot be inherently valuable; "Since it stands between individual objects and in equal relation to each of them, it has to be completely neutral"(ibid. p123). Whilst other objects acquire their value from being both scarce *and* inherently useful, money, with only the first of these characteristics, takes on a veil of value. "Since money is nothing but the indifferent means for concrete and infinite purposes, its quantity is its only important determination as far as we are concerned. *With money, we do not ask what and how, but how much*"(Simmel, 1990: 259, emphasis added).

The Progress of John Law's Monetary Ideas

In Law's era, the idea of paper money backed by land was mostly closely associated with the work of Sir Hugh Chamberlen. Indeed, J.K. Horsefield comments, "John Law criticised Chamberlen's plan, as we have already seen, but his own ideas did not differ widely from it"and this is essentially correct. (Horsefield, 1960: 217) The *Essay on a Land Bank* merely proposes a once-off recalibration of the Scottish monetary system to a land standard, based on the supposition that this would lend it more stability than specie. Law saw that the limit to the money supply caused by metallic money was constricting the development of the Scottish economy. However one cannot doubt the significance of *Essay on a Land Bank*, as it served as a stepping stone, a necessary precursor to Laws more advanced reasoning in *Money and Trade Considered.*

Some economic historians have put the gap between the writing of the *Essay* and *Money and Trade* at as little as five years, but this period represents a theoretical quantum leap, often compared to Keynes' change in emphasis between his *Treatise on Money* and *The General Theory*. Law is now concerned with the issue of unemployment in the Scottish context, and sees a solution in his earlier investigations into the nature of money. "A limited sum (of money) can only set a number of people to work proportion'd to it, and 'tis with little success laws are made, for employing the poor or idle in countries where Money is scarce"(Law, 1966: 13).

Law formulated an early version of the circular flow of income to show how money could drive trade, based on a money in advance requirement, whereby money is a necessary pre-condition for trade and economic activity. Law recognised that money supply and economic activity should move in concert, but whilst money may race ahead of activity (as it spectacularly did in Laws scheme in France), trade cannot expand beyond money, which can act as a fetter on the economy.

"Considering the present state of Europe, France and Spain being masters of the mines. The other nations seem to be under the necessity of setting up another money. The only reason can be given why it has not yet been done, is, that the nature of money has not been rightly understood"(Law, 1966: 77).

Law, however, grasped the nature of money more keenly that his contemporaries, and realises that an intrinsically valueless money could advance the national economy. "If a money be established that has no intrinsick value, and its extrinsic value be such, as it will not be exported; nor will it be less than the Demand for it within the Country: Wealth and Power will be attained, and less precarious"(Law, 1966: 102). Relying on an optimistic view of rate of real economic adjustment to monetary changes, Law later inundated the French economy, with paper currency backed by secured loans to his gargantuan Company of the West. The initial stability of value concern of the land bank scheme is nowhere to be seen in Law's so-called 'Mississippi System', and this indicates the degree to which John Law had advanced his monetary ideas by the time he had the opportunity to implement them, in 1719, when he became Controller General of the finances of the French economy.

Similarities Between Simmel and Law

(A) Philosophical Elements of Laws Thinking

"John Law (1671-1724), I have always felt, is in a class by himself. Financial adventurers – but is it fair so to call that administrative genius – *often have a philosophico-economic system of sorts*"(Schumpeter, 1981, p294). Law was not a disciple of any economic group, and relied more on his observations of banking systems as he travelled Europe to fuel his monetary ideas. He had a remarkable intuitive grasp of these issues, although perhaps less remarkable given his background as a professional gambler, and essentially worked from first principles, building his theory essentially uninfluenced by the economic orthodoxy. (Murphy, 1997) This imparts a certain Cartesian skepticism to Laws work, whereby no pre-existing economic tenets are accepted at face value. I would thus argue that the basis of Laws monetary thought and policy had a more meditative, philosophical content than any other economic theorist up to this time.

(B) The Development of Money as a Process

The development of Law's theories of the fundamental nature of money in terms of its inherent value constitute a segment of the developmental process of money towards a purely symbolic ideal envisioned by Simmel (1990). "With the growing need for means of exchange and standards of value it (money) changes more and more from a connecting link between value equations to a symbol of these equations and thus becomes more independent of the value of its material"(Simmel, 1990: 144). Simmel recognises the need for money to escape its roots as an intrinsic value if it is to be exploited to the full extent as a tool for human advancement. Law's contemporaries, and even he himself in his earlier writings, had a conception of money firmly based on its link to intrinsic value, "...but Law later moved away from the land bank proposal to a fractional specie reserve based bank, to a bank issuing irredeemable paper currency, to a system creating both paper money and company shares which were traded like money"(Murphy, 1994: 39). Thus Law provided a significant impetus to the process of development of the monetary system.

(3) Money as a Relation

Simmel goes to some pains to explain the role of a quantity of money as the numerator of a fraction, with the total sum of money as a denominator, as the value relation to any goods or services. (Simmel, 1990) In an interesting comparison, Law gives as terse a statement of this idea as one could hope. "The proportion of value goods have to one another is known by money."(Murphy, 1994: 55) Law's analysis of the relative price changes of gold and silver also shows an incisive understanding of this numerator over denominator monetary determination of value. "Gold is not more valuable, it is less valuable, but silver has fallen more in its value than gold"(Murphy, 1994: 86). Law argues that changes in the total supply of silver (augmented by newly exploited American mines) have significantly altered the value relation between discrete quantities of gold and silver. Law's view that other proponents of the Land Bank scheme did not 'understand' the nature of money, to the extent that they may not have clearly seen this value ratio, may have been correct. Indeed, David Ricardo was still grappling with the issue of relative price changes between goods (in his case corn) and a monetary standard in his *Principles of Political Economy.*

(4) Money as a Tool

Simmel considers money to be the purest form of tool for human utilisation, "Money is the purest reification of means, a concrete instrument which is absolutely identical with its abstract concept: it is a pure instrument."(Simmel, 1990: 211) Law also saw money in this instrumental sense, and identified two categories of money, based the extent to which different financial instruments, such as shares, could fulfil the functions of the monetary tool. Law was to utilise money as a tool to leverage growth in the French economy to an unprecedented extent, and in the process unwittingly pushed it almost to the point of collapse.

Causes and Consequences of the Failure of Law's Scheme

Over expansion of the money supply will always be a danger with paper credit schemes.

> *The specific significance of money for the pace of economic life is further substantiated by the fact that the crisis that occurs after the excessive issue of paper money retards and paralyses economic life to a corresponding degree* (Simmel, 1990: 500).

The spectacular fall of Law's Mississippi Scheme, after an equally spectacular rise, was also the result of a combination of other factors. Outside his control was the fact that,

> *It is possible to exchange the most valuable things against a printed form only when the chain of purposes is very extensive and reliable and provides us with a guarantee that what is immediately valueless will help us to acquire other values* (Simmel, 1990: 142).

Paper money will only function in an economy when the assumption that it will be accepted elsewhere is beyond doubt. Law's policies failed because he overestimated the sophistication in the French economy on this point, and also because at this time it was an extreme case, crippled by government debts. Law became more concerned with debt issue, and this was to sound the death knell to his scheme. Law tried to solve not only a monetary crisis, but also a debt crisis, with a tool (paper credit) that could deal with only the first issue, and attempted to do so in less than accommodating circumstances.

The Mississippi Scheme is an estimate of Law's self-belief at this point that he felt his scheme could provide a solution for both problems. A charitable interpretation of this might appeal to Law's spirit of optimism, and his belief that all economic difficulties could be overcome. A cynic might wonder whether Laws ego or the French Economy had been inflated more by the success of his system up to this point. To this extent the failure of the Mississippi system was a product of Law the man, who failed to see the limitations of his vision. This is, I feel, overly unfair on Law, especially when one remembers that whilst Versailles and the opulence from the reign of Le Roi Soleil have survived, time has not been so kind to Law's ideas, which tried to wrest the French economy from the ruin that was to be the cost of this affluence.

Any cursory examination of the history of money will reveal the robustness of the development of money as a concept. It has been formulated in innumerable ways inappropriate to the modern context - the Lydians used an incredibly rare alloy of gold and silver called electrum, and the Greeks employed a form of credit secured on the debtors' personal freedom – all of which have been abandoned, but the concept of money has survived. Whilst Law's exertions may not have lead to the rejection of paper credit schemes, they did bring it into disrepute in economic circles, and in Schumpeter's (1981) view, considerably impeded progress towards the modern banking system. (Schumpeter, 1981: 283)

Conclusion

Unusually, John Law possessed both the intellect to understand the accepted parameters of the notion of money and its necessary properties for his time, but also the vision to see that these parameters were not fixed, and that the conception of money had, and would continue to change. J A Schumpeter draws an important distinction between success in theory and in practice, and whilst Law did fail as a policy-maker, this should be considered separately from his theoretical contributions, which extended far beyond those discussed in this paper. Unfortunately this has not been the case, and subsequent economic thinkers have denigrated Law's work. Even Keynes, for whom Law would have provided an obvious theoretical bloodline, failed to mention Law. It is ironic to think that Law may have been as esteemed as Keynes himself, if only he had been content to remain within the realms of theorising, as any theory that is never tested can never be rejected.

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