Inflation and Interest

Some twelve years ago I wrote a paper called "A World Inflation?" which is reprinted in my *Essays in World Economics*. It is not a paper of which I am particularly proud. Many of the the things I said in it I would still stand by; but the general tone is too optimistic. I recognised that the rise in prices which had already occurred in very many countries during the nineteen-fifties could not be adequately discussed by looking at each country separately; it was already a world phenomenon. But it is clear, in the light of what has happened since, that I attributed too much of what had then happened to special causes of that time: to the dismantling of controls on the suppressed inflation of war time and to the effects of the British devaluation of 1949. (The latter was indeed a more general change than the more recent British devaluation, since many more countries followed Britain in the first case than in the second. It was not implausible to hold that it was an excessive reaction to a disequilibrium which, being so generalised, might have very general disturbing effects). There is, I would still hold, something in that; but I am now quite convinced that I gave it too much attention. I did have something to say about less special causes; but still I was looking at the matter too much from a British point of view.

It is very clear, a dozen years later, that there is a World Inflation, not reducible into the behaviour of any one country, certainly not the U.K., not even the U.S. This is overwhelmingly apparent if one takes the table, with which I began my former discussion, and brings it up to date. In Table I I show the percentage rise in the consumer good price-index, not for quite so many countries as in my former table, but for what I think is a sufficient sample, over successive five-year periods. The first (1953-8) is pretty much what I showed in my old table. I have added two columns for the successive quinquennia, 1958-63 and 1963-8. I have also put in a fourth Column, showing the rise from mid-1968 to

mid-1969, exhibited as a five-year increase (to make it comparable with the other columns). That is to say, it shows the rise which would occur if the actual rise from 1968-9 were continued, at the same rate, over five years. It is evidently not to be taken as seriously as the other columns, but I think it still gives a useful impression.

As I said on the former occasion, I have no more than a limited faith in consumer-price index-numbers; certainly I have no great faith in some of those in my table. If one were proposing to use them for direct comparisons between the performances of the various countries, they would at the least require to be given considerable annotation. But that is not the way I propose to use them here. I want to concentrate upon the general phenomena which they reveal, and for that purpose it can hardly be doubted that they are quite good enough.

The first of these phenomena is the most obvious: that the rise in prices which was experienced, so generally, during the first quinquennium, has continued to the present. There is not even any general sign of retardation; such change as there has been has been mostly the other way. It is true that there are a number of cases (Denmark and Spain, Argentina, Turkey, India for instance) where rates of inflation that were quite out of line with the general experience have been (or appear to have been) very considerably slowed up. And there is one extraordinary case, among the countries selected, in which there has been, on the average since 1953, *no* rise in prices. The case of Malaysia can surely only be explained in terms of a fall in the price of rice which has offset other rises. It is unlikely that the constancy can apply to those classes in Kuala Lumpur who have more varied budgets. And if one looks at the statistics of the Malaysian economy more generally, it would seem most unlikely that its price-stability can be much longer maintained.

At the least, the Malaysian case is an interesting exception; but it may be a bit more than that. We can perhaps discern a tendency, among the "less developed" countries, for price-stability to be relatively attainable, though by no means always attained. If the representative budget consists mainly of food, the consumer-price index will be highly sensitive to food prices. If there is a bad harvest, it will shoot up; but if productivity in agriculture is steadily rising, falling food prices will make it vastly easier to stabilise the general index. The movement of prices in India is surely to be explained in these terms; I do not know how far it applies to

Egypt (where the rise in prices that is shown in the table ante-dates the war of 1967). What is clear is that in these countries the consumer-price index is less useful than it is in the more "developed" as an indicator of "inflation".

My table, of course, says nothing about exchange-rates. All price-levels are measured in terms of the respective national currency. That, from the point of view I am going to take here, is rather an advantage. It must surely be recognised that even if all consumer-

TABLE I

PERCENTAGE RISE IN CONSUMER PRICE INDEX

	1953-58	1958-63	1963-68	1968-69
Austria	10	15	19	16
Belgium	9	6	18	16
Denmark	16	21	37	16
Finland	28	17	38	5
France	21	25	18	40
Germany	9	11	13	16
Greece	31	4	11	16
Ireland	16	10	25	46
Italy	14	17	19	16
Netherlands	18	13	25	40
Norway	16	14	23	16
Portugal	5	11	26	53
Spain	40	28	44	10
Sweden	19	15	23	16
Switzerland	8	11	19	10
U.K.	16	12	21	33
Argentina	115	390	212	46
Canada	9	6	17	28
Mexico	50	11	16	22
U.S.	8	6	14	33
Australia	14	9	16	16
India	10	16	60	5
Iran	47	28	8	22
Israel	39	29	27	10
Malaysia	− 6	0	5	0
Japan	9	27	29	40
N. Zealand	18	2	22	28
S. Africa	15	6	16	10
Turkey	71	43	38	22
U.A.R.	− 5	− 1	35	5

1968-69 figures are the rise from mid-1968 to mid-1969 expressed, for comparability, as a five-year rate.

price levels had been stable, or had been rising at the same constant rate in all countries, over the whole of my period, there would still have been exchange difficulties, and might well have been exchange crises, from differences in rates of increase of productivity and from such like causes. Some of the devaluations (and revaluations) which have occurred during my period can be ascribed to the domestic inflation having got out of line, but by no means all. We can quite usefully allow ourselves to forget about the question of realignment of currencies, simply observing that however reckoned, the general tendency to a rise in price (a fairly steady rise in prices) has been present, nearly everywhere, throughout the whole of the period with which we are concerned.

There is indeed sufficient uniformity for us to be able to fit what has happened into a simple theoretical pattern. Not that it can be a perfect fit, but it can surely be a good enough fit to be suggestive. We can allow ourselves to think (or to begin by thinking) of the whole "developed" world — Western Europe, North America and Japan — as if they formed a single *closed economy*. What is known about the behaviour of such an economy, even from purely theoretical considerations, should have at the least some relevance. No doubt there is not much which we can spin out, purely *a priori*; but the case is one in which there should be something to be learned from the theoretical models.

There is a particular model, much used by economists, which looks like being a starting-point. It is the model of Wicksell's *Interest and Prices*. It has of course had much work done on it since Wicksell. It played a great part in Keynes's *Treatise* (less, I think, in the *General Theory*, which is mainly concerned with a different problem). A very important contribution to it was made by Myrdal. I have done a good deal of work on it myself, both in *Value and Capital* (1939) and in *Capital and Growth* (1965). I shall draw on all these in what follows.

Wicksell's famous condition — market rate of interest equals natural rate — was a condition for price-stability. He was assuming a perfectly competitive economy, with freely flexible prices. He was (implicitly) starting off from a condition in which prices had been stable; he was asking what was the relation which would ensure a continuance of stability. He did not seriously distinguish between short and long rates of interest, for so long as his stability was maintained, he took it that they would maintain their normal

relation. Se long as his *natural rate* is not changing, or not changing or not changing much, this may perhaps be allowed. And then one may perhaps allow — at least in a theoretical model — that *the* rate of interest is under the control of *the* Monetary Authority.

When these qualifications have been observed, it is evident that Wicksell's construction can be no more than a beginning. One has to ask oneself how it should be modified when these restrictive conditions cannot be accepted, even as approximations.

The particular condition which for my present purpose I most obviously have to modify is the condition that one is starting off from a position of price-stability, already attained. In Wicksell's world, the previous establishment of stable prices is taken to imply that businesses (or just "people") expect the continuance of stable prices; or (putting the same point more loosely and perhaps more realistically) neither general inflation nor general deflation are possibilities that are given much weight in the making of business calculations. That was a condition which in Wicksell's day would (often at least) have seemed quite realistic; but for the questions with which we are here concerned it quite clearly will not do.

What are the adjustments which we have to make to Wicksell's construction if we start from a condition, clearly so common nowadays, in which prices have been rising, for quite a long time, at round about 3% per annum? I think there are several. In particular, there are some things which Wicksell did not have to distinguish but which must now be distinguished.

In Wicksell's world, people were expecting the continuance of stable prices. If prices did in fact remain stable, their expectations (at least to that extent) would not be cheated. So the maintenance of a constant price-level was not merely, in his model, a matter of arithmetical constancy; it implied the maintenance of equilibrium in a more fundamental economic sense. The prices which people assumed in their calculations would on the whole be the prices which were actually realised. Their rational calculations could thus be carried through.

In "our" world, on the other hand, this sort of equilibrium does not imply price stability. If people expect prices to rise but they do not rise, expectations will be cheated. Wicksellian equilibrium, in our world, implies the continuance of the habitual rise at the same rate, neither accelerating nor being slowed up. If prices have been rising at 3% per annum, that is what they must go on

doing. Whether or not this is in fact desirable, it is what Wicksell's construction, fitted to our problem, must be made to mean.

The second adjustment that is needed concerns the *natural* rate. This, in Wicksell, was a rate of interest that corresponded to a normal rate of profit — the profit which business could normally expect to earn on new investment. Prices being stable, this normal rate of profit was also a *real* rate of profit, a rate of profit which could be taken to be determined (by productivity and thrift or what not) in real terms. But in our inflationary case, the rate of profit which is expected is put up above the real rate of profit by the rising prices. If prices are expected to rise at 3% per annum, a one-year investment of capital will be expected to yield, in money terms, 3% more than it would have been expected to yield if prices had been stable. So what corresponds to Wicksell's natural rate, in this sense, is 3% higher than it would have been if the rise in prices wat not occurring.

One can refine upon these adjustments a good deal further; there are several other ways in which the Wicksell model, for the use we want to make of it, can be improved. Yet even at the point we have now reached, it is highly suggestive. It is not hard to find facts which, at least at a first glance, it seems to fit.

Consider my second table, which shows Government Bond Yield (when I can get a figure from *International Financial Statistics*) for periods that correspond, as closely as I could make them, to those of my first table. I am very well aware that one must not put too much weight upon these figures. Every country has consumers, who pay prices in the shops; but not every country has a market in Government Bonds. When there is a market, it is frequently small and easily "managed". Thus it is often quite uncertain how far the yield, as quoted, has any close relation with what an economist would recognise as *the* rate of interest. Yet it is possible to make all these reservations, and still to find the picture which is revealed in my table quite striking. If one compares the first and the last columns, one finds a 2½ to 3½ per cent rise in the rate of interest (very much what the theoretical analysis would have led one to expect) in no less than eight of the seventeen countries shown; and there are a couple of others which are not far behind. Only Australia, and some of the Common Market countries (France, Belgium and Italy) show a less than 1 per cent rise. (I am aware that the more substantial rise has now come in Italy, though at a date too late for inclusion in my table).

TABLE II

GOVERNMENT BOND YIELDS

	1953-57	1958-63	1964-67	1968-69
Belgium	5.0	5.4	5.6	5.6
Denmark	5.5	5.7	7.2	8.6
France	5.5	5.2	5.3	6.1
Ireland	4.9	5.7	6.3	7.9
Italy	6.4	5.4	5.8	6.0
Netherlands	3.7	4.2	5.3	6.5
Portugal	3.2	3.7	4.2	5.1
Sweden	3.7	4.4	5.1	6.2
Switzerland	3.0	3.1	4.0	4.5
U.K.	4.4	5.5	6.3	8.0
Canada	3.5	5.0	5.4	7.1
U.S.	3.0	3.9	4.4	5.6
Australia	4.7	5.0	5.0	5.4
India	3.8	4.2	5.2	5.0
N. Zealand	4.3	5.0	5.2	3.5
S. Africa	4.6	5.4	5.6	6.5
U.A.R.	3.4	3.7	6.0	6.8

(1968-69 figures are averages of 1968 and first three quarters of 1969. Inclusion of the fourth quarter of 1969, when it was available, would of course nearly always have raised the average quite appreciably).

I would however repeat that I do not put much faith in the detail of these figures. Even in the U.K., where the size of the National Debt is (I suppose) exceptionally large and where it is undoubtedly actively traded, it is notorious that there has been a great deal of "management". Thus it cannot be an easy matter to sort out those changes in interest which are fundamentally due to changes in the "sentiment" of the market from those which are to be attributed, at least in the first place, to changes in the policy of governments. Still less can one distinguish those changes which are the result of a positive governmental, or Central Banking, decision from those which are just to be ascribed to weariness — to an unwillingness, in the end, to swim any longer against the tide.

One might hope for enlightenment, on this last distinction, from the pronouncement of governments, of finance ministers and of bankers; but I much doubt if one would get it. It is inevitable that any change of policy, even if it is no more, at bottom, than a passive response to external pressures, will be presented, if possible, as a

positive initiative. How (otherwise) is confidence, or such confidence as is attainable, to be maintained?

My own guess at the explanation of the interest-rate history, as shown in my table (abstracting, as before, from exchange-rate crises, and looking at the broad picture, rather than at the experience of individual countries) would be roughly this. Though it was already the case, in the fifties, that prices were rising rather generally, at not much short of the 3 per cent rate which has since become established, the habits of mind established by long experience of old-style price-stability had not altogether lost their force. This applied (in Northern Europe, in North America and in Switzerland) to the general public, to many specialised financiers, and not least to the bankers themselves. In technical economic language, we might say that there was still an *expectation* of long-run price-stability — an expectation which was already breaking down in particular circles, and in particular countries, but was not yet sufficiently decayed to make the Wicksell model, with which I began — a model with a *natural* rate that is effectively *in real terms* — altogether inappropriate.

Already, indeed, even at that stage, there was management of interest rates. We might press it into Wicksell's schema, regarding it as a reduction of the market rate of interest below the natural rate (the natural rate — the real natural rate — being at that stage still rather abnormally high, as a result of post-war shortages not yet completely overcome). But I would not press the point, for I do not myself regard this monetary mechanism as being particularly important, at that stage, as a cause of inflation.

Whatever its causes, the inflation continued. The longer it continued, the more rational it became to expect its continuance. The more general, therefore, the expectation of inflation became.

Now what would we expect to happen if there is imposed upon a situation in which prices are already rising (say at 3 per cent per annum) a rise in price-expectations, in the sense that it is now assumed, more generally than it was before, that the inflation is likely to continue? This is again a question on which theory can throw some useful light.

I think it is better, at this point, to use a model which is slightly more complicated than Wicksell's. It could be taken in various forms, but I may perhaps be allowed to take it in my own form, the form I gave it in *Value and Capital* (having the benefit,

of course, of many hints which I got from Keynes.) I simplified to the point of considering a system in which there were just three sorts of things being traded — Commodities (including all sorts of real goods and services), Securities (Bonds), and Money. It is not necessary to suppose that the Commodities, or the Bonds, are homogeneous; but it is nevertheless the general price-level of Commodities in term of Money, and the general price-level of Bonds in terms of Money (expressible, of course, as a rate of interest), which are the two key prices with which the model is concerned. One could use this model (as I did in my book) to study the structure of interest rates for different periods; but I shall not involve myself in that side of the matter here (1).

Now what happens, in a model of this kind, if there is a change in expectations, so that people believe that the prices of goods are going to rise more rapidly? All we can do is to compare the state of the model as it would be with one set of expectations and with the other — everything else, as usual in such comparisons, being supposed not to change. Let us distinguish these two states by calling one the state of Low Expectations, and the other the state of High Expectations. What would be the effect on our two key variables — the current price-level of goods and the current rate of interest — of a change from Low to High (or Higher) Expectations?

It is easy to jump to the conclusion that both prices and interest will rise; but I think it is useful to look at the matter in more detail and to ask "why?". One can only do that by asking for what reasons the failure of either to rise may have to be rejected. If there was no change in the current price-level of goods, or in the rate of interest, the profit to be expected from holding goods, or from using them to start new processes of production which take time, would be increased; and that would be all. But we may surely suppose that this increased profitability would stimulate a demand for goods, either to hold or to use as inputs; and that this would tend to cause a rise in their current price-level. (There may be an exception in the case of an underemployed economy, in which some goods, or services, are in very elastic supply — the Keynes

(1) The rates of interest that are shown in Table II are not always clearly distinguished on the side of maturity; but I have taken the longer rate whenever a distinction is made.

case — but it is surely of little relevance to my present problem, so I may exclude it). The straightforward effect of a change from Low to High Expectations is a rise in the goods price-level.

Now it is possible that this rise in current prices may react back upon expectations of prices, driving them higher still. I made a good deal of this in my book, giving it the name *elasticity of expectations*, which has impressed it on the minds of students. It does have a part to play in the story, but I now think that in my book I brought it in too quick. It can be a quick reaction, but an economy in which it is very quick is already in a condition of hyper-inflation. That, fortunately, is not our present problem; so for the present analysis it had better be held over.

If there is no such reaction (or before there is any such reaction) the rise in current prices of goods will diminish the rate of profit which can be expected from holding (or using) them. Thus the rise in current prices will be limited, even if the rate of interest does not change. There will be a limited rise in prices, which will restore a normal relation between the rate of profit and the rate of interest. Why then should the rate of interest change?

In order to answer that question, we have to look at the Money aspect. Everyone, I think, would now agree that there would be (or might be) a monetary reaction, though there could be some disagreement about the form which it would take. Let us notice, however, the precise question that is being asked. We are supposing that current prices have risen far enough for the expected rate of profit to be reduced to its former level; and we are supposing that there has been no rise in the rate of interest (or price-level of bonds); so the rate of interest and the rate of profit are just the same as they would have been if expectations had been Low. So there is no incentive to substitute one kind of asset for another as a result of a change in yields. Will there nevertheless be a change in the Demand for Money?

This is a question about which there has been a great deal of discussion. Some would prefer to say that though there is no substitution effect (since there is no change in yields) there will be a "wealth effect". The money value of total assets is increased, because of the rise in the prices of goods; this must be expected to raise the value of each type of asset which the representative individual will desire to hold in his portfolio. This is a way of putting the matter which is quite in line with my *Value and Capital*

approach; but I do not nowadays feel it to be very convincing. After all, the analysis should apply to the case (though it is a more special case than that which I am here discussing) of a simple stock exchange boom; and it is not very evident that stock exchange operations are subject to a strong "real balance effect" — though one can always say that it is masked in that case by a substitution effect which goes in the opposite direction. I would prefer to emphasise another reaction, which seems to me to be more reliable. The *initial* rise in the prices of goods can occur, like a rise in stock exchange prices, with hardly any actual trading; but if the rise is *general*, as we are supposing, the goods will subsequently be changing hands at the higher prices, circulating in a normal manner along the regular channels of production and trade. We should then expect that larger money balances, held somewhere in the system, would be required in order to circulate them. That is the simple point — the increase in demand for money for transactions purposes — on which I would mainly rely.

Whith this in mind, let us look back at the position we had reached in the former argument. We had supposed that the change from Low to High Expectations had simply resulted in a rise in the price of goods, leaving the expected rate of profit unchanged, and the rate of interest unchanged. We must now take account of the increase in the transactions demand for money, which we had left out of account. When we do so, we see that if the adjustment is to take place in the way described (with no rise in the rate of interest) there must be an increase in the supply of money, in some sense, to satisfy this increased demand. If the banking system meets the demand which is thus made upon it, in the way in which banks are accustomed to meet the "needs of trade", then there is no reason why the rate of interest should rise. Our provisional equilibrium can be the complete result of the change from Low to High expectations — or so it would appear.

But in coming to that conclusion, have we not been cheating? I have been taking the change from Low to High Expectations as being a single, once for all, change; but that is not what I ought to have been discussing. In the real world (or in my hypothesis about the real world) people have not woken up all at once to see what has been happening to prices; they have woken up gradually. So the change which I ought to have been analysing is not a once-for-all change; it is a change which has been spread out

over a considerable period. And that, quite clearly, makes a difference.

For if the change in expectations is spread out in this way, and if it is allowed to express itself (as we have been supposing) upon the price-level of goods *and on that alone*, the prices of goods will rise more rapidly, over the whole period, than they would have done if the change in expectations had not been occurring. And we must surely expect that if it occurs in that way, it will react, sooner or later, upon expectations. The High Expectations will become higher (in *Value and Capital* terminology, expectations will become more elastic); so the rate of price-rise will increase. We have in fact come back, along a different route, to Wicksell's Cumulative Process.

If that is to be avoided, there must (it would appear) be some degree of monetary restriction. That is certainly the case in terms of my model, and I do not think it is a very controversial statement, even with respect to the Real World. For if we are thinking of the multi-national economy, on which (throughout) I have been fixing my attention, that economy has no single government, no national budget, so that stabilisation through budgetary control can never be more than partial. There is nevertheless a sense in which it does have a single financial system: a system of banks which by now are pretty closely connected.

Let us thus return to the model; and, for the moment, to the simple shift from Low to High Expectations. If businesses cannot get all the funds that they need — all the increase in funds that they are needing — by borrowing from the banks, they must borrow elsewhere, or sell securities elsewhere. This must tend to raise the rate of interest. (If the banks supply the money to the securities market, in order to prevent the rate of interest from rising, they are of course just supplying equivalent money "through the back door").

Now if we assume, as we surely may, that funds are readily shiftable between our markets, there can be no equilibrium, even temporarily, unless the expected rate of profit bears a more or less normal relation to the rate of interest. So if the rate of interest rises, the rate of profit will have to rise. But that means — so long as the state of expectation, though High, is given — that current prices will rise less than they would have done if the rise in interest had not occurred. Current prices must rise less, in order

that a higher rate of profit should be earned in turning present goods into future. Thus the rise in the rate of interest does something, as we should expect, to damp down the inflation.

Let us now revert to the more interesting, and more realistic, case of the gradual rise in price-expectations — people settling more and more into the belief that the 3 per cent per annum rise in prices is *normal*. If there is no monetary restriction, prices would in fact rise faster than the 3 per cent; a very severe monetary restriction could stop the rise in prices; a moderate restriction, which allowed the rate of interest to rise to a level which "corresponds" to the inflation, would be consistent with "equilibrium", in the Wicksellian sense with which I began. But a rate of interest at this level does not stop the inflation; all it does is to prevent it from accelerating further. At a lower level of interest the monetary system is feeding the inflation. At the "corresponding" rate (which on our figures is 3 per cent higher than what it would have been if the price-level had been stationary) the monetary system is neutral. That is all.

Some people might think that could be the end of the story, but I doubt if it can be. Suppose we go on to a point at which the adjustment I have been describing, and attempting to analyse, is complete. Expectation of inflation — a particular rate of inflation — has now, we will say, become general; everyone (more or less) is expecting the 3 per cent annum rise in prices, and interest rates have been adjusted so that the 3 per cent rise is just about what actually occurs. The "Wicksellian" equilibrium has been attained. Could it be held? I rather doubt it. For I have really said nothing, in all that precedes, about the causes of the inflation. I do not believe that its causes are monetary, though monetary maladjustment may accelerate it, and with better monetary measures it can to some extent be restrained. I wonder very much if we could hope that with monetary adjustment complete, the real causes of inflation — even of accelerating inflation — would be removed.

For it will be observed that it is a characteristic of the inflationary "equilibrium" that while the value of money is falling, the rest of the relative price-system will be much the same as it would have been if the money price-level had been stationary. And that surely means that real inputs and outputs also will be much the same. For the real proceeds of time-using production will be much the same as they would have been without inflation. During the preced-

ing process of adjustment, many business will have been getting money returns which were better than they had expected; in terms of the analysis of Keynes's *Treatise*, they were getting windfall profits. These windfall profits were a stimulus to expansion, to *real* expansion. But when *equilibrium* has been restored, the windfall profits have disappeared, and the stimulus to expansion is removed.

This (surely) is borne out by experience. We have already seen, in the case of countries such as Argentina and Indonesia, how a reduced rate of inflation, less than it has been but still quite considerable, can engender many of the symptoms of trade depression. This a stronger case than that which I am here considering, but (though of course to a lesser degree) I think that the same still holds. I would think it most probable that an inflationary equilibrium (in which inflation still persists, but is kept to a steady pace by high rates of interest) would appear, relatively to past experience, as a state of under-activity. There would be all kinds of pressures to take *more* inflationary measures, so as to give the economy, by one means or another, a further stimulus.

The pressures which would build up on the side of wages are not quite the same, but can probably be analysed in a fundamentally similar manner.

I am therefore by no means of the opinion that the attainment of an *inflationary equilibrium* (prices rising just about as rapidly as they are expected to rise, and rates of interest adjusted to these inflationary expectations) is a suitable objective of policy, and particularly of banking policy. If no more than that is aimed at, something more inflationary still will almost inevitably result. If inflation is to be controlled — and by control I do not necessarily mean prevention — something more than that is needed.

As will already have appeared in this paper, I am not much in sympathy with the *New Monetarism* (as Kaldor has lately called it) — the revival of the Quantity Theory of Money which is the work of Milton Friedman and his numerous associates. I am not convinced by their doctrine when it is considered as an analysis of the way the monetary system works. I would nevertheless grant that its appearance, as a historical phenomenon, is not a thing to be altogether regretted. I cannot accept that regulation of the Quantity of Money, by some arithmetical rule, is a dependable way of avoiding inflation; for I do not think that we know, or can know,

well enough what the Quantity of Money is. It is bound to be defined, for purposes of regulation, in some arbitrary manner; and the ingenuity of business is such that it will always (in time) find a way of escaping from a limitation of the money supply, in so arbitrary a sense. But in our present predicament, it would do no harm if the Friedman gospel were accepted for the moment, as a way of helping us round the difficulties that lie ahead. For if it were to be widely accepted, it could do a good deal to moderate inflationary expectations. This, I hope I have made clear, I would very much welcome. Who was it who said "If there were no God, he would have to be invented"? I feel much the same about Milton Friedman.

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