Conventional wisdom had assumed that a profit-seeking bank would immediately print too much money. But Hayek pointed out that this course would be self-defeating. If a bank overissued its currency, causing it to depreciate, people wouldn't want to accept or hold it, preferring that of more conservative banks. The offending bank's currency would go to a discount and, in short order, the bank would have to curb its enthusiasm. Competition, Hayek said, would do a better job of compelling private institutions to maintain their money's value than politics had with public institutions like the Fed.

Maybe—but let's be practical. How would I buy my groceries? Suppose the prices were marked in Rockefellers and all I had were Wristons? Suppose I'm a New Yorker in San Francisco? San Franciscans might prefer BankAmericas. What good would my Wristons be? How could a merchant function if his customers kept coming in with different kinds of currencies? How could a businessman keep his books?

The answer to these interesting questions depends partly on which of the several different proposals for privatizing money is under discussion. Hayek's version is particularly radical. In most historical episodes of private money, banks issued their own notes but denominated them in the national unit of account—the dollar, the pound. These notes usually exchanged at par and would be discounted only as a last resort in specific circumstances, such as overissue.

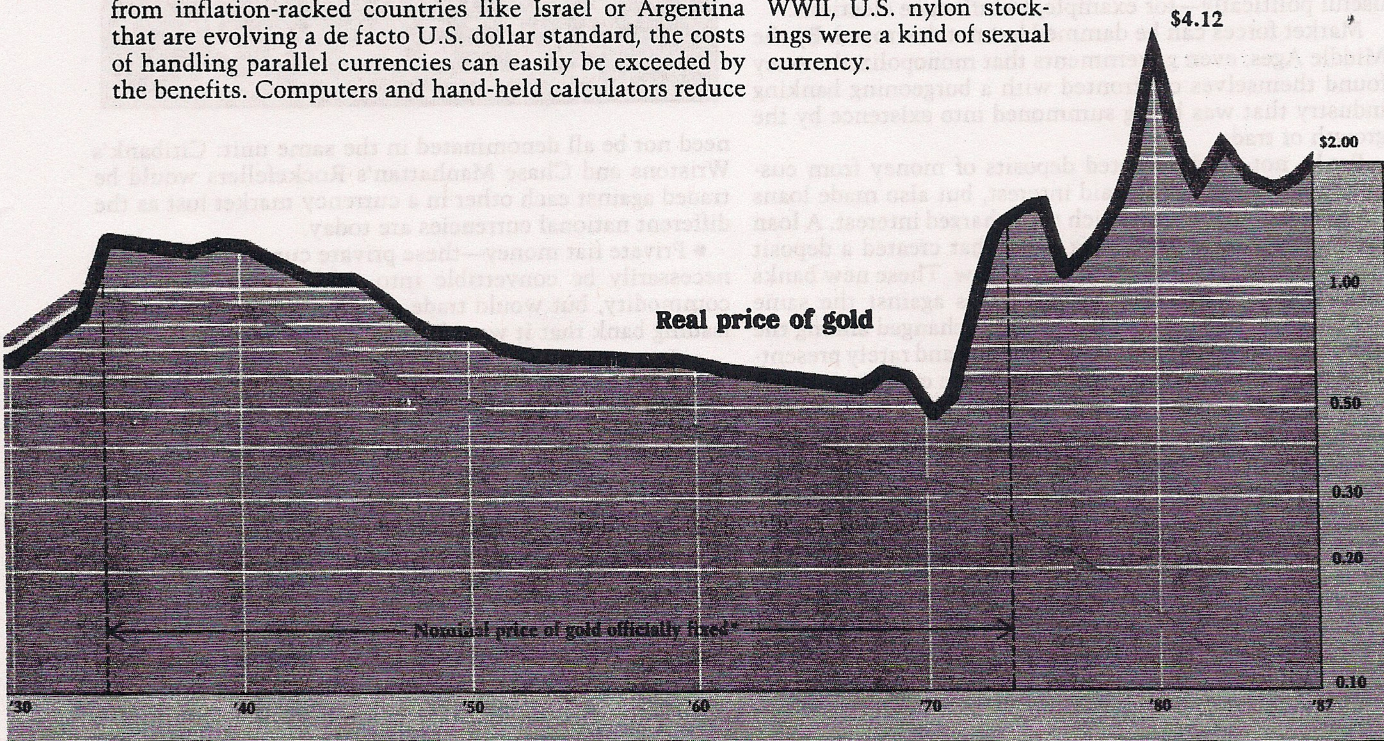
But more generally it is clear from the response of merchants in border zones like Tijuana or Toronto, and from inflation-racked countries like Israel or Argentina that are evolving a de facto U.S. dollar standard, the costs of handling parallel currencies can easily be exceeded by the benefits. Computers and hand-held calculators reduce the confusion, just as they have helped business to handle international floating exchange rates.

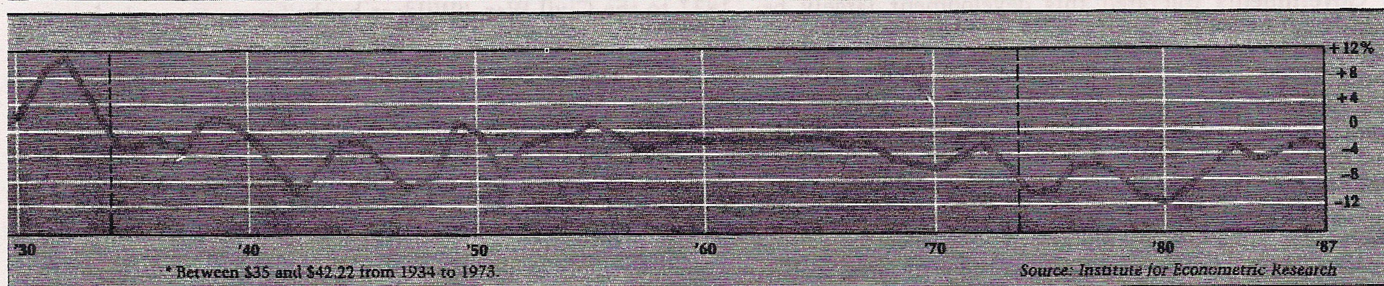
The fact is that free markets don't produce chaos. Efficiency will probably dictate that just a few kinds of monies, perhaps only one, will become universally accepted—exactly as the international computer industry has spontaneously evolved standard operating systems.

To understand Hayek's proposal and the whole competing currencies concept, you have to think about the nature of money. Most laymen, and some economists, assume that money is a collective convenience requiring government to organize, like national defense. But the historical evidence seems to be that in reality money developed all by itself. Merchants just agreed upon common stores of value and mediums of exchange because they found using them more efficient than barter—an example of what Hayek calls "spontaneous order."

Coins are traditionally supposed to have been invented in the 7th century B.C. by the Lydians, whose King Croesus became a legend for his wealth. But significantly, David Glasner reports, the earliest surviving coins appear to have been privately issued. The Lydian royal minting monopoly was only later imposed—by another king for whom the Greeks invented the word "tyrant."

Recent observations have tended to confirm the private origins of money. In one famous case, cigarettes spontaneously evolved as the medium of exchange in a World War II prisoner of war camp. In much of Europe after WWII, U.S. nylon stockings were a kind of sexual currency.





*Between $35 and $42.22 from 1934 to 1973.

Source: Institute for Econometric Research