If you said that a principal cause of the 2008 financial crisis was an explosion in credit, most economic commentators would nod their heads in agreement. If you then said this credit boom was due to lax monetary policy, you’d still earn a healthy fraction of nods. If you then asserted that America’s departure from the gold standard caused the lax monetary policy, not many folks would be nodding. Nevertheless, this attenuated causal chain has been embraced by a motley collection of wonks, cranks and presidential candidates: Michele Bachmann, Glenn Beck, Steve Forbes, David Stockman and politicians whose last name is Paul. These gold bugs have a deep suspicion of fiat currency. They fret that governments that can just print money will be tempted to print even more, triggering inflation, currency depreciation and worse. Most citizens do not share this obsession, but they might share an unease about the dollar being backed by nothing more than a social convention to treat greenbacks as if they are worth more than the paper they are printed on.

It is this unease that Kwasi Kwarteng tries to tap into with “War and Gold.” A Cambridge-educated historian, Conservative member of Parliament in Britain and the author of the excellent “Ghosts of Empire: Britain’s Legacies in the Modern World,” Kwarteng attempts to recount 500 years of monetary history in accessible prose. He makes his thesis clear at the outset: The history of money is one of oscillation between “periods of monetary chaos,” when governments issue fiat currency, and “periods of relative order,” when currencies are linked to gold. The bulk of “War and Gold” is devoted to observing that things seemed much, much better during eras when currencies were tied to gold. In his introduction, Kwarteng explicitly says he is not advocating a return to the pre-1914 gold standard. Rather
than echoing Rand Paul, Kwarteng writes more like a Tory nostalgic for the solidity of Robert Peel in 19th-century England or the Eisenhower era in 20th-century America.

At the outset, Kwarteng says, “This book is a work of history. It is not a tract of economic theory.” His statement reveals both the biggest strengths and weaknesses of “War and Gold.” One strength is in the lucidity of Kwarteng’s narrative style. “War and Gold” manages to sweeten the abstruse parts of his monetary history with anecdotes about the major actors — gamblers like John Law (a Scotsman who engineered a massive financial bubble in 18th-century France) or statesmen like Joseph Dodge (an American who tamed inflation in post-1945 Germany and Japan). Kwarteng has a flair for the elegant turn of phrase. He describes the Bretton Woods system that prioritized policy autonomy over open capital markets as one in which “domestic policies would be lead partner in the dance.” As a good historian, Kwarteng also acknowledges some occasions when the facts do not go his way. He is candid, for example, that the United States’ adherence to the gold standard helped cause the credit bubble in the 1920s that led to the 1929 stock market crash.

When it comes to fiat currency, however, “War and Gold” tries and fails to convert modest correlation into strong causation. Kwarteng is correct to point out that before 1918, fiat currency tended to be associated with massive economic uncertainty. This elides the rather important fact that countries usually issued such currencies during times of war or revolution, and maybe it was those events, and not the paper currency, that were responsible for the economic chaos. Kwarteng should be aware of this — the book is called “War and Gold” after all — but he focuses much more on the paper currency and much less on the reasons behind it.

Unfortunately, that is not the only problem with this book. Even as history, Kwarteng’s account is incomplete in ways inconvenient for hard money fans. There is no discussion of the link between the gold standard and the prevalence of deep recessions and crippling deflations during the late 19th century. There is no mention that the countries that stayed on the gold standard the longest during the interwar period — including America and France — were among the ones that suffered the deepest economic pain from the Great Depression. They were also more likely to resort to trade protectionism after the 1929 stock market crash.

Kwarteng stumbles further when he tries to connect his historical narrative to
current monetary debates; these are the places where a better grounding in economics would have served him well. At one point, he paints modern advocates of quantitative easing — printing more money even after slashing interest rates close to zero — as “the intellectual descendants of John Law.” The obvious inference the reader is supposed to draw is that quantitative easers are fated to repeat the bubble that Law created 300 years ago. Similarly, in his discussion of Keynesianism, Kwarteng argues that “the country which best typified this new, ‘gold-free’ approach to finance” was Nazi Germany. Both assertions have a weak reed of plausibility, but they obscure far more than they reveal. Since modern central bankers all believe in fiat currencies and expanding the money supply to stimulate economic growth, they are all the intellectual descendants of John Law. Quantitative easing is simply another policy consistent with this belief. The parallel between Nazism and Keynesianism is even more off-base. A raft of Depression-era governments boosted government spending; what made the Nazis unique was the tight rationing of credit as a policy tool. Keynes has been accused of a lot of things over the years, but advocating credit rationing during a depression is not one of them.

I doubt Kwarteng was trying to be disingenuous with these comparisons. Rather, he is genuinely uncomfortable with the ability of countries to issue paper money to perpetuate fiscal profligacy, expand credit and erode currency values. Kwarteng’s worries are understandable given what has happened in the past, but “War and Gold” overlooks compensating trends that mitigate some of these concerns. The rise of independent central banks over the past half-century was designed to be a bulwark against monetary authorities kowtowing to politicians. Insulated from political pressures, central bankers can take unpopular actions to cool off inflation. Independence allowed the Federal Reserve chairman Paul Volcker to wring inflation out of the United States economy in the early 1980s, and the Bundesbank’s Helmut Schlesinger to do the same following German reunification in 1990. Kwarteng’s qualms are not entirely groundless, but recent history shows that the greater concern should come from monetary authorities obsessing about inflation at the expense of growth (see: eurozone, crisis of).

Kwarteng has written an engaging but radically incomplete history of money. Gold bugs will embrace it. I sincerely hope the Fed does not.
WAR AND GOLD

A 500-Year History of Empires, Adventures, and Debt

By Kwasi Kwarteng


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