Where does money come from?

The nature of money creation and financing for development

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Abstract

Development strategies deal extensively with the question of how to spend money in order to most effectively further economic development. A subset of these policies called Financing for Development discusses the source of this money, i.e. where it should come from rather than where it should go to. Recently a focus on taxation to increase domestic revenue mobilization has come to the fore. At the same time, where money comes from at all – that is, how money is continuously created – has been subject to economic debates particularly since the financial crisis in 2008. Formerly mainstream neoclassical economic theories have been challenged by more systemic theories of money which assert that money in modern societies is created differently and by other financial institutions than previously conceived.

Bringing together these two current trends, this thesis investigates how conceptions about money and banking are embedded in the development sector and may implicitly guide its financing for development strategies. I study such perceptions from the donor perspective, using the Norwegian Agency for Development Cooperation (Norad) program Skatt for Utvikling as a case study of a Financing for Development strategy. I employ qualitative methods, mainly through eight interviews with development practitioners in the sector. As my theoretical basis I employ mainstream neoclassical economics and monetary theory contrasted with two more systemic theories: State Theory of Money and Credit Creation Theory of Money. The latter two have been increasingly accepted by academic and professional economics since the financial crisis in 2008.

I argue that the development strategies and the practitioners display a thinking about money and banking that is rooted in mainstream neoclassical economics, a branch of economics that, peculiarly, has little to say about these topics. My findings indicate a blind spot when it comes to the subject of money as a systemic phenomenon, and especially regarding the aspects of creation and deletion of money. This implicit endorsement of neoclassical economics among development practitioners explains a striking pattern that emerged in my interviews: When I asked about money creation, my interviewees consistently talked about moving money. Even though the theoretical situation is changing in economics, this change seems to not yet have reached the Norwegian tax for development strategy.
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Norad  The Norwegian Agency for Development Cooperation
STM  The State Theory of Money
CCTM  The Credit Creation Theory of Money

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1 Introduction

I am at the opposite end of town. The fancy part, I have heard. The large building, Hydrobygget, was originally built for Norsk Hydro – one of the companies which ensured Norway its wealth through the country’s economic transformation around the 1970s. Now Norad – the Norwegian Agency for Development Cooperation – has their head offices in the building. I have several meetings with different Norad employees during these months, some of them economists who have worked with macroeconomics, international economics, finance, and banking through their careers. Most of them has extensive experience in the development field, some has have been working for the World Bank and some are now in Norad’s program Skatt for Utvikling – Tax for Development. We talk about the rationales behind taxation as a financing strategy for developing states for financing the realization of the Sustainable Development Goals. Today, while discussing sources of financing, I timidly try to ask the Norad economist about money creation: How and by whom is money is created? Does this issue have a role to play in financing development? What role it is already playing in developing economies? We are struggling to have a conversation about the aspect of creation of new money. It is easier to talk about where it should be moved from. It is extremely complicated to talk about how it comes into existence: Where does money come from? The interviewee says sceptically: “Well, the money has to come from somewhere!”

In this thesis I investigate conceptions of money in the development sector. My motivation is threefold: 1) A current change in consensus on theories of the nature of money and banking is underway within the professional and academic fields of
economics. 2) At the same time, the discussion within the institutional development field about proper strategies for financing development is shifting. Finally, 3) popular perceptions seem to be changing among workers in the professional development field towards the proper role of money in development.

Money is the stuff we use to pay for our groceries, or pay our rent, and which we are paid by our employer. Money can be experienced as physical cash, or as electronic money in our bank account with which we can pay or be paid through payment apps and bank transfers. In academia, money is normally defined by its three main functions as: a medium of exchange, unit of account, and a store of value (Holden 2016, 268).

Money is an element in the economy, and this thesis will dive more into the details of its definitions and disagreements. But it is not a thesis in economics, it is a thesis about the specific issue of money – an issue that is sometimes dealt with in economics, but equally by other academic fields such as geography, sociology, anthropology and law. Where economics usually take a quantitative approach to studying the world, this thesis takes on a qualitative approach.

Development strategies extensively deal with the question of how to spend money in order to most effectively further economic development. However, the Financing for Development discussion focuses on the source of this financing, i.e. where the money should come from rather than only where it should go to. Where money comes from at all has been at the center of economic debates particularly since the financial crisis in 2008. Neoclassical economic theories have been disputed by more systemic theories of money which are increasingly becoming mainstream, asserting that money is created differently and by other financial institutions than previously conceived. In this thesis I investigate how money creation is understood in the institutional field of development. As is seen in the professional field of development, common attitudes towards the role of money in development interrelate with the popularity of different development strategies. A basic tenet of this thesis is that our conception of the world shapes how we act in it, and therefore, that development workers’ conceptions of money creation shape their work with financing development. Driven by the current change in consensus within economics about the nature of money and banking, I seek to explore how the development field considers money creation, at this specific juncture. Since Financing for Development deals with the source of finance for development, I seek to explore the employed conceptions of where money comes from, that is how money is created. To
do this, I focus on the case of the Norwegian Norad-program Skatt for Utvikling (Tax for Development), which was initiated following the third international conference on Financing for Development in 2015. This thesis, then, is an empirical exploration of conceptions of money creation followed by a theoretically driven discussion, relating the empirical findings to the current shifts in theoretical consensus within economics. In order for a development aid institution to make effective strategies for financing sustainable development, it is essential how it understands the fundamental concept of financing, i.e. where money comes from.

Below, I expand on the threefold motivation for the thesis. Then my research question will be presented, followed by an outline of the thesis.

1.1 The role of money in development

The way money is talked about in the professional development sector is changing. The discourse has continuously evolved, first from aid to trade strategies as the preferred and popular solution to global inequality and poverty in developing countries. Then micro credit and financial inclusion emerged as buzzwords and policies – often by offering credit to the poor through formal financial institutions. Just as quickly as these measures became popular, they also attracted a growing body of critique (see e.g. (James 2014)

Direct cash transfers in different forms (in practice most often conditional in some way or another although inspired by the unconditional basic income idea) are now “the talk of the town” among development professionals, giving rise to different attitudes towards morals around money. Cash transfer programs started in Latin America and are now expanding throughout southern Africa. Recent proponents of the direct cash transfer view are Hanlon, Hulme and Barrientos, who in 2010 published the book Just Give Money to the Poor – its title depicting well the change in attitude towards the role of money in development strategies (Hanlon, Hulme, and Barrientos 2010). In 2015, James Ferguson published Give a man a fish in which he concludes:

The point of this all-too-brief review is only to say that something is in the air with respect to the grounds and rationales of distribution – or, to put it rather more precisely, many things are in the air. […] here we see the
prospect of various forms of direct distribution linked to *new kinds of arguments, and new kinds of claims*, that hint at quite fundamentally different sorts of politics than those usually associated with “social assistance.”

(Ferguson 2015, 197, emphasis added)

Ferguson’s book is related to cash transfers specifically, but it characterizes a more general change in attitudes towards money where new kinds of questions are being raised in the development field: *What* is money, *whose* money is it, to *whom* should it be directed, and *how* and *where* does money come from?

### 1.2 Financing Development

Financing for development has been a global debate for at least 20 years. Mobilizing domestic resources within the developing countries themselves has been taken up as a stated strategy since the first conference on Financing for Development in 2002 (United Nations 2020). Recently, this focus on domestic resource mobilization has gained increased attention in connection with an upsurge in debates on better taxation systems, generally and in developing countries in particular: In 2015, the third conference on Financing for Development was held in Addis Ababa, Ethiopia (United Nations 2015). The Addis Ababa Action Agenda is not formally linked to the Sustainable Development Goals. However, the intentions of the two documents are closely related. The same year, the Norwegian government and other large aid donors signed up to the Addis Tax Initiative, committing to a stronger focus on taxation systems to promote domestic revenue mobilization in developing countries as an important strategy to finance sustainable development (Addis Tax Initiative 2020b).

The negotiations that led to the 2015 SDGs and the Addis Tax Initiative (ATI) developed the importance of DRM [Domestic Revenue Mobilization]. One of the SDGs [Sustainable Development Goals], SDG 17.1, specifically encourages increased international efforts to: ‘strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection’.

(Lundstøl 2018b, 13)
In 2016, the current Norwegian program Skatt for Utvikling (Tax for Development) was established through the Norwegian Agency for Development Cooperation (Norad). Taxation as a development strategy is currently expanding rapidly as a result of the Addis Tax Initiative, where donor countries committed to doubling their budgets in this area by 2020 (Norad 2020a).

The funds administered through the SfU [Skatt for Utvikling]-secretariat increased from 2 million kroner in 2017, to 56 million kroner in 2018, and is expected to increase further to 175 million kroner in 2019 and 210 million kroner in 2020.

(Lundstøl 2018a, 4)

Skatt for Utvikling works to promote a focus on taxation in the international policy arena and also includes grant agreements, country programmes, financially supporting international funds, and work to strengthen civil society within this domain (Lundstøl 2017). Norad is pairing up with research institutes to produce knowledge for the advancement of development taxation policies, often emphasizing that this is a new shift in development policy – both of which became clear to me through my fieldwork.

There are several objectives built into the tax agenda, including state building and redistribution, but the main objective remains to raise domestic funds for financing development.

The goal of the SfU [Skatt for Utvikling]-initiative and increased action for domestic resource mobilization by 2020 is to effectively support developing countries in increasing their own public revenue to finance expenditures and investments related to the sustainable development goals.

(Lundstøl 2018a, 1)

1.3 The nature of money and banking

After the financial crisis in the Western economies in 2008, various discussions about money, banking and finance have risen academically and in the public debate. Academically, the debates have centered on three interrelated questions. A) What is money - commodity or debt? B) How do banks function? Do they lend out existing
money, or extend credit – thus creating money? C) And hence: By whom – or how – is money created? By the state or by the banks?

Mainstream neoclassical economic models have long treated money as a special type of commodity, and most economics textbooks feature a version of the origin story that claims the concept of money to historically originate from barter economies, functioning to “grease the wheels.” (Holden 2016, 267; Mankiw 2016, 613). The “money multiplier” is the common model of banking in neoclassical economic theory. While popular perception might depict banks as institutions that lend out others’ savings, neoclassical monetary theory perceives that banks “multiply up” savings by lending out more than what is saved in the bank by some ratio. Following this model, the neoclassical economic view is that a central bank ultimately has the control over the money supply, i.e. the creation of money in an economy, via its creation of the monetary “base” which banks then multiply, as well as by deciding the ratio by which they can multiply the deposits (Mankiw 2016, 93f). While the money multiplier and fractional reserve are neoclassical monetary theories, neoclassical economics generally does not see the money supply to be particularly important (Ingham 2004, 7). Chances in the money supply is characterized as neutral over the long term: An increasing supply of money is ultimately seen to result in increased prices across the economy with no specific consequences in any particular area (Horwitz 2016). What is held to be important is that the money supply is not increasing too rapidly, to avoid too high inflation. Since a (moderate) increase in prices is seen to be economically neutral, money creation is not an explicit element of most neoclassical economic modeling, and is often described as a “veil” over transactions in the real economy (Ingham 2004, 33).

The neoclassical view of money is increasingly being challenged by the State Theory of Money (STM) and the Credit Creation Theory of Money (CCTM): What I in this thesis choose to collectively call “systemic theories of money”. Economists supporting these alternative views dispute the neoclassical view of the historical origin of money as well as its engagement (or lack thereof) with money and money creation in understanding the functioning of the economy. In 2011, the economic anthropologist David Graeber published a now widely acclaimed book, Debt – the first 5,000 years, where he demonstrates that money essentially is debt, and originated as such (Graeber 2011). In the book, he draws on historical anthropology, including a paper by Cambridge anthropology professor Caroline Humphrey where she makes clear that:
No example of a barter economy, pure and simple, has ever been described, let alone the emergence from it of money; All available ethnography suggests that there never has been such a thing.

(Humphrey 1985, 48)

Economic scholars, such as Steve Keen, Richard Werner, and Perry Mehrling, have brought attention to CCTM, emphasizing that banks do not lend out other people’s money (Keen 2001; Werner 2014b; Mehrling 2010). Rather, banks extend credit, thus creating new money through the lending process – in line with the view that money is debt. This view has increasingly been approved by central banks and bank professionals. In 2015, the Bank of England published the working paper Banks are not intermediaries of loanable funds - and why this matters, where they insist that, contrary to popular belief: "Saving does not finance investment, financing does." (Jakab and Kumhof 2015, 4). The reason why it matters that banks are in fact not intermediaries, has to do with the mechanism of financing: Neoclassical economics hold that bank lending is based on preceding deposits, that is other peoples’ savings. On the contrary, CCTM holds that bank lending, regardless of preceding deposits, will result in an increased money supply – which in turn shows up as more deposits. In other words, the mechanism is the other way around: saving in the form of deposits does not lead to investments. Investments in the form of bank lending creates deposits. “Saving is therefore a consequence, not a cause, of such lending.” (Jakab and Kumhof 2015, 4). Or in the words of Schumpeter: “It is not deposits that make loans, but loans that make deposits.” (Schumpeter 1954, 1080).

Concurrently, STM is also gaining traction. Especially a branch of STM called Modern Monetary Theory has gained popularity as a revival of this theory that is based on chartalism – the view that money is a juridical concept, issued by the state by definition. Proponents include scholars such as Geoffrey Ingham, L. Randall Wray, Mariana Mazzucato, and Stephanie Kelton who works with the American Democrats’ proposal for a so-called Green New Deal (Ocasio-Cortez 2019). This view also builds on the essential view that money is debt, and that banks create it. But more importantly, it holds that the most trustworthy debt is debt to the state, which in turn is created through state expenditure. A main point is therefore that the state, by definition, cannot run out of money, since state spending is the source of the money supply. Here too, the direction of causality runs opposite of what is otherwise held by neoclassical
economics. The latter views the state budget like that of any other economic agent: Its spending is limited by its income. According to neoclassical economics, the state has to first collect taxes (or other sources of income) before it can subsequently spend. Contrarily, STM points out that, since money is issued by the state, the state cannot collect taxes before spending. The causality runs in the opposite direction: The state spends, thus creating money, then collects taxes to avoid undesirable levels of inflation (Wray 2014).

To summarize the discussion so far, mainstream neoclassical economics of the last century has dealt little, if at all, with the question of money creation. Especially, since money is seen by neoclassical economics as a neutral medium of exchange – a more efficient way of bartering – money creation is seldom part of economic modelling. Now, systemic theorizing about money, such as STM and CCTM, is increasingly supported by growing numbers of academics and by authoritative economic institutions, like the Bank of England (McLeay, Radia, and Thomas 2014). Not only do systemic theories of money offer an explicit theory of money creation, these theories also disrupt neoclassical and layman reasoning around financing, by arguing for a directly opposite direction of causality. Furthermore, there are a number of effects on the economy that neoclassical economic models and theorizing neglect when the economy is modelled as an advanced version of a barter economy, rather than as a money economy. Some of these effects, pointed out by proponents of CCTM are: the boom-bust cycle of the economy and crises like the financial crises in 2008; inflated and self-reinforcing housing prices along with too little investment in the real economy, and other distributional effects; what institutions accrue seigniorage (the income derived from issuance of money); spatial and economic centralization following financial centers; and ineffective monetary policy due to incorrect modelling (Hougaard Nielsen et al. 2018; Ryan-Collins et al. 2012; Jackson and Dyson 2012). Proponents of STM are more concerned with the financial limitations on state policy: If the state holds the power as a primary issuer of money, tax revenue should not be treated as a limit on state spending, but rather an effect thereof. Advocates often argue that the main macroeconomic objective of a state should be to ensure full employment, and that this can be achieved through better integrating the money-creating ability of the state with an expanded policy space for directing new funds towards productive – or sustainable, as argued in the Green New Deal – sectors in the real economy (Nersisyan and Wray 2019; Wray et
Some features of money and banking are still widely disputed and heavily discussed in academic circles – for example the question of exactly how, and to what degree, central banks have control over the money supply (see e.g. Huber 2014). But some issues that systemic monetary theorists bring up are quickly becoming mainstream. Academic economics is progressively reaching consensus that new money is created when private banks extend credit, in line with the above-mentioned Bank of England paper. Both standard economics textbooks at two large Norwegian universities have recently had their explanation of money creation revised in accordance with this growing new consensus (Holden 2016 at University of Oslo; Steigum 2018 at BI Norwegian Business School). Despite these debates and changes in academic consensus, some economist have complained that the ideas that used to be mainstream, but which are now strongly disputed, live on among practitioners, and through popular perceptions:

Today, the vast majority of the public is not aware that the money supply is created by banks, that banks do not lend money, and that each bank creates new money when it extends a loan.

(Werner 2016, 376)

A British poll done by the British polling company Dods in 2017 showed that 15% of MPs agreed with the growing consensus on money creation among academic economists, while 70% of MPs supposed that only the government creates money, in line with common popular perception (Positive Money 2017; Williams 2017). So even the elected officials that citizens trust with making their country’s economic policies hold on to this traditional understanding of money which is no longer sufficient.

**The nature of money enters the public debate**

The nature of money is not only being discussed in academia. Since the financial crisis of 2008, a number of monetary issues have also been raised in the public debate. One much-reported incident was when Queen Elizabeth II of England asked the simple question of economists from the London School of Economics at a prestigious event in 2008: Why had these experts not seen the crisis coming? They replied: “systemic risk”. Everyone had done their own job well individually, but it turned out no one had a
broader overview of the system as a whole (Martin 2014, 185). Another object of public debate has been non-state cryptocurrencies, which have increasingly popped up, the most well-known being Bitcoin (Nakamoto 2008). Last year, in 2019, Facebook launched their plan for an alternative, Libra (Libra Association 2019). Both Bitcoin and Libra have given occasion popular discussion about alternative monetary systems. A third monetary event, which caused public debate, was when the European Central Bank started effectively creating trillions of euros after the financial crisis of 2008 through their ‘Quantitative Easing’ program to inject liquidity into the financial markets. The unprecedented scale of the policy made headlines across the world (see e.g. Duncan 2009; and BBC News 2015). Lastly, the Democratic Party in the United States has via their ‘Green New Deal’ proposal brought state money creation into the national political debate (Kelton 2019).

In conclusion, the nature of money has emerged as a hot topic in public debate since the global financial crisis in 2008. However, it seems that the specific changes in the academic consensus on the nature of money, and the place of money within economics models, has not necessarily reached public knowledge.

1.4 Rationale, aim and research question

In the three previous sections, I have introduced the threefold motivation for this thesis: Firstly, the debates and incipient consensus change in economics on the nature of money and banking, which theoretically drives the thesis. Secondly, the empirical case, Skatt for Utvikling, which is situated in the international agenda of financing development. Both will be further elaborated in chapter 3 and 4, respectively. Thirdly the ongoing change within the development field regarding perceptions of the proper role of money in development has been briefly touched upon, as well as how the nature of money has been subject to public debate since the financial crisis in 2008. Neither of these are specific subject of study in this thesis but presents additional occasion for investigating perceptions of money in the development field. While attitudes towards money are shifting in development and new kinds of questions are flourishing, the consensus shift in economics about the nature of money has, however, not necessarily reached the development field. But the growing consensus in economics, that
neoclassical economics has not been getting money creation right, and that money creation therefore is not properly incorporated in economic models, having real economic implications, is of relevance also for development policy. In 2015, in a working paper for United Nations Research Institute for Social Development, Jem Bendell, Matthew Slater and Will Ruddick criticize the development field for not engaging with the monetary field:

Recent years of intergovernmental discussion on financing for development have ignored the most simple aspect of their mandate — the nature of the very thing they are talking about — money.

(Bendell, Slater, and Ruddick 2015, 2).

The nature of money is exactly what is at the center of the shift in economic debate: what money is, how it is created and by whom.

Especially when working with financing development, understanding and dealing with the nature of financing, i.e. where money comes from in a systemic sense, is essential. While financing a business is a microeconomic issue that solely requires understanding of how to raise money for the business, creating policies for financing sustainable development in whole societies is a macroeconomic issue. When dealing with macroeconomic issues, it is not only important to understand how to raise funds for a single business or sector, but also to understand how funds — i.e. money — emerges in an economy at all. Understanding these issues is to some extent, but not exclusively, a technical academic matter. Popular conceptions permeate the language and affect macroeconomic experts and experts in other fields. Exploring these conceptions — whether technically and academically grounded or non-technically and non-academically grounded, is the purpose of this thesis. I will not address cultural and moral values around money, like those in James Ferguson’s earlier mentioned work, or the classical work of Bloch and Parry (Parry and Bloch 1989), but rather conceptions of how the monetary system works — with a specific focus on conceptions of money creation in an economy. I will explore empirically such conceptions and how they relate to preferences for certain development strategies over others, and I will discuss these conceptions in relation to monetary theories and the current changing consensus on the matter. In this way, this thesis is not an economic treatise, but rather a highly qualitative analysis. It is a theoretically driven discussion based empirically on interviews and document analysis. The following research question guides the thesis:
How are conceptions of money and banking embedded in the Norwegian tax for development strategy, and how are these conceptions related to the ongoing consensus shift in economics on the nature of money and banking?

In order to answer this question, the analysis examines Financing for Development and Skatt for Utvikling reports, in addition to eight qualitative interviews with employees in the development sector in Norway. Literature on three different perspectives on the nature of money and banking forms the basis for the theoretical discussion. The analysis is carried out in three parts: First, I examine the role of the state in the monetary system, as perceived in the empirical interview material and in the economics literature. Secondly, I analyse the perceived role of banks in the same manner. In both cases, I argue that the Norwegian Skatt for Utvikling/Financing for Development strategy seldom pays attention to money creation as a concept. When it does, it seems to rely on neoclassical and popular perceptions of money. Perspectives of the State Theory of Money and the Credit Creation Theory of Money are nearly absent despite gaining increasingly support in the economic literature. Thirdly, I analyse and discuss how neoclassical and popular perceptions are embedded in the language of my interviewees, and through popular economic discourse. I argue that the development strategies and practitioners that I engage with in this study display a thinking about money and banking that has roots in mainstream neoclassical economics, a branch of economics that, paradoxically, has little to say about these topics. This implicit affiliation with neoclassical economics among development practitioners explains, moreover, a striking pattern that emerged in my interviews: why it turned out to be so difficult to talk about these issues, in the first place.

This thesis does not aim at finding the most proper monetary theory to use in policies for financing development. It is a qualitative study of the way conceptions about money and banking are embedded in the Norwegian development sector, and which may implicitly guide its financing for development strategies.
1.5 Outline of the thesis

In this first chapter, I have introduced the topic and the puzzles that motivate this thesis, the rationale, and the research question. In the following chapter, I turn to the methodology I used to find answers. Chapter 3 gives a brief introduction to the context of Financing for Development in which Skatt for Utvikling is situated. In chapter 4, I lay out the theoretical framework on which the discussion is based, with a particular focus on the debate about the nature of money and banking in the current literature. The analysis is divided into three chapters according to three themes: Chapter 5.1 and 5.2 deal with the perceptions of money and banking found in the data and discuss these through the theoretical framework. The former covers the role of the state in the monetary system. The latter covers the role of banks in the monetary system. The third part of the analysis, chapter 5.3, takes a slightly different form, in that it examines more broadly the ways money and banking are dealt with, thought of, and talked about, and how a general lack of distinctness about this topic was reflected in the interviews. Chapter 6 summarizes the key findings from the three analysis chapters and discusses some implications of these for the development field, academically as well as professionally.
2 Methodology

This is not a thesis in economics. While economics originated with Adam Smith establishing it as a field – an entity of the world which can be studied – economics has come to be characterized, rather, by its method (Sandmo 2007). Accordingly, in the introductory textbook used at the Economics department at University of Oslo, Holden writes that economists use macroeconomic models based on variables and equations which in mathematical form explain important connections between variables. Economics uses quantified models, definitional connections, equilibrium models, static models and dynamic models – all based on mathematics (Holden 2016, 25-27).

This thesis does not. Rather, it makes use of qualitative methods from the field of human geography, which is also my academic background. While for example development economics is the endeavour of studying development with economic, i.e. quantitative, methods, this thesis is better characterised as economic geography, or geography of finance, since it studies the language of finance in relation to uneven global economic development, using qualitative methods: interviews and text analysis. The concern is with global inequality in distribution of material wealth as caused by the design of the monetary system – a systemic view which fits well within the field of geography. This concern is studied primarily through a focus on language and perceptions about the issue – an approach which lies within the field of human geography and critical social science, building on the assumption that such perceptions interrelate with language and influence, for example, policy (Winchester and Rofe 2010, 21-22). It might strike the experienced development researcher that the concept of “developing countries” is over-generalised in this thesis. While I acknowledge this is often a problem, I allow myself this generalisation here, since my point is not to find solutions for specific countries, but to discuss the overarching ideas and thinking that are employed in the sector. The main aim of the thesis is to combine the discussions of the two debates: on the nature of money and on financing for development.
2.1 Case study

The initial motivation for writing this thesis was my discovery that there is no agreement over the nature of money and the functioning of the monetary system, prompting a frustration that I had not encountered this fundamental issue earlier in my long social science education. Astonished that most social scientists are not concerned about the effects of the design of the monetary system, I wondered if that was so in the development field as well, and especially in the field of *financing* development.

Wishing to study the donor side rather than the receiving side in development, and because Norway plays such a significant role on the international development scene, I found it relevant to study the Norwegian development sector. The Norwegian Agency for Development Cooperation (Norad) was of main interest since the decisions on how the development budget is distributed are made here. I soon found out that Norad had recently (re)established the program Skatt for Utvikling, which is linked to the global Financing for Development agenda (described in detail in chapter 3), and I thought: if anybody should contemplate the monetary system, it would be people working with development strategies for better taxation systems. Thus, Skatt for Utvikling functions as a specific case within the global and expansive field of Financing for Development.

The empirical data collected for thesis are interviews with people employed in the Norwegian development sector, including in Norad’s Skatt for Utvikling. Since Skatt for Utvikling is surrounded by other Norad strategies as well as international work on tax for development and Financing for Development, data from these broader strategies supplement the case to give a more thorough understanding of the rationales and narratives within the objective of financing development.

2.2 Documents

Three documents have been central in the analysis, since they pertain closely to the core case: Three published Skatt for Utvikling papers: a strategy document; a plan for scaling up of the program; and a working paper by the head of the program (Lundstøl 2017, 2018a, b). These three documents have undergone the same analytical coding as the interviews and are similarly used and quoted in the analysis chapters, since they reflect the thinking about the subject which applies for the Skatt for Utvikling strategy.

In addition, two reports from the broader international field have been included in the
data collection: The Addis Ababa Action Agenda and the Financing for Sustainable Development Report 2019 (United Nations 2015, 2019). However, since these reports does not deal with the aspect of money as a system, I ended up deciding not to code and include them to the same extent. However, I have read them, and they have contributed to my overall insight into, knowledge of, and impression of the field that Skatt for Utvikling is part of. Apart from such official organizational documents, I have followed the Norwegian *Bistandsaktuelt* (Development Update) closely. It is an editorially independent news medium published and funded through Norad, which publishes articles and opinion pieces on development, focusing on Norway and its development partners. Especially, I have read articles related to the topic of the thesis and articles and opinion pieces written by my interviewees. These have not been part of the coding and analysis either, but similarly served to give a broader understanding of the field.

All of these documents lie within the public domain, and while the Bistandsaktuelt articles and the Addis Ababa Action Agenda and Financing for Development documents are also written for the public, the Skatt for Utvikling documents are written for use inside the organization. All of them are however not produced on request for this research, and so are not primary data (Bryman 2016, 43).

In addition to the theoretical framework presented in chapter 4, the third part of the analysis draws on sources from anthropology and sociology. Since the thesis discusses the way money creation is talked about and understood, including by non-experts, I find it natural to incorporate sources from media that non-experts are exposed for.

### 2.3 Fieldwork

I attended several events hosted by Norad on subjects related to that of the thesis. Here, as well as in public documents, the monetary system was not mentioned specifically, and I did not want to intrude with my questions at these events. Therefore, attending such events served mostly to strengthen my general insight into the field and to get a broader understanding of the language and understandings which are at play there (Bryman 2016, 430). I attended an internal seminar at Norad as well as several public events hosted by Norad, and other public events hosted by other organizations related to the topic or field. Among these events where a number of “Norad Policy Forums” – presentations on topics relevant for Norad’s development strategies, hosted by Norad
but with speakers from outside Norad; and a seminar hosted by the think tank Agenda, which had made a report on Norad development strategies on the occasion of the appointment of a new Minister of Development. At all events, I attended as part of the audience. At the Norad seminar, I accompanied one of my interviewees and greeted a few of their colleagues, taking the role as ‘the visiting student’ (Kearns 2010, 251). I originally wished to attend a larger number of internal events but was eventually not allowed to, just as I was not allowed to the workshop part of the Norad seminar, but only the presentations. This might be due to Norad’s position as an official and governmental institution, but also turned out to depend on varying opinions by my contacts there: While some were very open to me attending, one in particular was very strict about not allowing me access to the internal events by principle. I chose to be as courteous as possible and comply with the wish of the person not wanting me to go, rather than accepting the invitation from the person that was open to me attending.

Attending these events was a sort of observation, about which Kearns writes that “observation research requires seeing, smelling, touching and hearing the observed environment” (Kearns 2010, 241). What I did was primarily listening, supplemental to the interviews, also a verbal source; at some of the events there were slideshow presentations, which will be a sort of visual source. This fieldwork functioned as complementary research method to the more structured data collection through interviews (Kearns 2010, 242). Observing these events did contribute to my sense of what topics are discussed in the Norwegian development sector generally, and what issues Norad is focusing their work and considerations around. It contributed to a better general understanding of the language used about development and what issues are commonly addressed. I took field notes during and after these events, which contributed as a valuable source for reflection.

2.4 Interviews

The main data collection was done through interviews. I conducted eight interviews in total. Five of the interviewees are currently employed in Norad, three of those in Skatt for Utvikling and two from other departments. Of the other interviewees, one is retired from Norad with a long experience in the field. One has been working in the academic
field of development and is currently in a development NGO. One has been working in development NGOs and is currently employed in Utenriksdepartementet (Ministry of Foreign Affairs). The eight interviewees had different academic backgrounds: Five are economists, one a geographer, one an anthropologist, and one from political science. The interviews were conducted in the spring 2019, and all the interviews lasted around an hour and were conducted one-to-one. Most took place in office meeting rooms, except two which preferred to be meet in a café instead, and one who requested it to be over phone. The interviews were audio recorded for the purpose of transcription, and because it allowed me as the interviewer to me more attentive, thus following the semi-structured form better as well as maintaining a more conversational style (Kvale and Brinkmann 2009, 159). Additionally, I took notes during and after the interviews, which served to better remember specific thoughts I had during the interview, as well as things that were not captured by the audio recording. Especially in one interview this proved useful, as the interviewee unexpectedly kept on talking for a long while after we had ended the interview and I had stopped the recording (Bryman 2016, 487; Dunn 2010, 119). The one phone interview is only partly recorded due to practical obstacles regarding me figuring out how to record over the phone, so I took more comprehensive notes during this interview, which is also why this interview is more often paraphrased rather than quoted in the thesis (Bryman 2016, 488).

The interviews can be characterized as expert interviews, in that these interviewees by virtue of their positions and experience are experts on what this thesis investigates: how money is conceptualized in the job that they are doing. Accordingly, the interviewees were chosen through purposeful or criterion sampling, because they are all important workers in the Norwegian development sector, working more specifically with macroeconomic issues, so they are the most equipped regarding the issue at hand (Bryman 2016, 418f). There was an element of snowballing in that I initially reached out to contacts of my supervisors, then through those reached more contacts (Bradshaw and Stratford 2010, 75).

The interviews were semi-structured and open-ended. Roughly the same interview guide was used for all interviews with minor changes over time when finding out some questions were not well understood, for instance. I adjusted the guide somewhat to each interviewee in accordance with their working experience and background as well as any
of their writings I had read prior to the interviews (Bryman 2016, 473; Dunn 2010, 104). The reason for my choice of interviews as my main research object is that the monetary system is not normally talked much about, nor in general, neither in the field of development. Interviews allowed me to pose the question and make the interviewees reflect upon it even though they would not normally do so. However, the questions were highly open-ended, and the interview design exploratory in style, as I wanted the reflections of the interviewees on the issue. As Dunn writes, interviews are highly useful for investigating motivations, meanings, and experience, and for allowing the discovery of what is relevant for the interviewee (Dunn 2010, 103). Using semi-structured open-ended interviews allowed a conversation-style interview with room for the interviewees to reflect and think about aspects that are not necessarily part of their regular considerations. The interview guide served as a backbone to make sure there was a common thread in the interviews and that we talked about some of the same issues in more than one interview, but at the same time the guide allowed for large flexibility to let the interviewees talk about issues that they related more to, had more experience with, or more opinions about. It also allowed me as a researcher to explore and ask the interviewees to elaborate on issues which appeared relevant (Bryman 2016, 473; Dunn 2010, 104). Following Dunn, in the thesis I have been continuously conscious about not making it look like I have discovered the specific truth about conceptions, as well as not claiming that my findings apply to all of Norad – or all of the Norwegian development sector for that matter (Dunn 2010, 102). Rather, my aim is to give an insight to a truth, limited in time and space to the interview settings, about reflections on the issue of the specific interviewees, yet certainly existing as a part of their context, professionally and otherwise.

The audio recordings of the interviews were transcribed and coded by hand. The codes were partly informed by the literature and partly emerging during the transcribing and coding process, as I discovered new patterns in what was said in the interviews. Thus, I initially created many codes, then, when seeing patterns and interconnections among these, some were merged, some were left out and or renamed, and then the transcriptions were coded again (Bryman 2016, 576f). While coding and reworking the codes, I applied the literature to relate to relevant themes and subthemes, while maintaining an eye for the context of the code’s parts and bits, including the position
and backgrounds of the interviewees. Codes and themes were developed looking for repetitions of topics, metaphors and analogies, similarities and differences, missing data and particularly theory-related material (Bryman 2016, 580). Thus, the analysis of the data is an interpretative form of qualitative content analysis (Dunn 2010, 125).

2.5 Positionality and ethics

All the interviewees have job positions that could be seen as the advancement of the same education I am in; thus my interview approach has some similarities with elite interviewing, or at least a form of ‘studying up’ (Aberbach and Rockman 2002; Richards 1996; Nader 1972; Dowling 2010, 32). All interviewees held at least a master’s degree in one of the social sciences, and most of them had been working in large international organizations such as development banks, development agencies or government institutions in Norway and abroad. While the interviewees in this thesis may not be elite in a strict sense, they all had senior positions in the same field as mine, as well as important positions in the institutional structure whose decisions have major effects on society. Therefore, I find it useful to acknowledge some elements considered important for elite interviews. Important functions for such interviews are to understand the perceptions of and to get an insight into the mindset of the interviewees (Richards 1996, 199, 204). Referring to the task of studying perceptions, Aberbach and Rockman emphasize the aspect of examining “the parameters that [guide] their definitions of problems and their responses to them.” (Aberbach and Rockman 2002, 674). This is exactly the aim of this thesis. In addition, Richards, Aberbach and Rockman emphasize several aspects of interviews like these that are important to bear in mind, which guided my approach to the interviews. Among them are: Being very well prepared on the subject as well as the background of the interviewees (Richards 1996, 202; Aberbach and Rockman 2002, 673); Using open-ended questions, because: “Elites especially – but other highly educated people as well – do not like being put in the straitjacket of close-ended questions. They prefer to articulate their views, explaining why they think what they think.” (Aberbach and Rockman 2002, 674); Ask difficult or peculiar questions around the middle of the interview, when rapport and understanding of the object of study has been established (Richards 1996, 203).
Despite that attending events in the field did contribute to my familiarity with the language within the field, it proved challenging that the interviewees and I were familiar with different ‘jargons’ about the topic (Dunn 2010, 115-116). When the interviewees sometimes seemed to not understand a question, I made sure to use strategies such as restating the question, using alternative wording or providing examples, while making sure to leave adequate room for reflexive silence (Dunn 2010, 116-117). In addition to the interview guide, I had printed a sheet of paper with illustrations of three different theories of money creation: the money multiplier, state theory of money and credit creation of money. It was surprisingly awkward to ask the question “how do you believe money is created”, so I used the sheet as a way to handle that question better myself, and also for the interviewees to have something more concrete to relate to. The illustrations worked well for this purpose, even though it simultaneously felt awkward for both of us to use such textbook-like illustrations as the basis for a somewhat elite-like interview.

Robyn Dowling recommends engaging in critical reflexivity when dealing with the social relations of research (Dowling 2010, 30-31). I have attempted to exert critical reflexivity throughout the research, and I would like to comment on it here because I believe some of the reflections I have had partly explain the nature of the awkwardness of the interview situations as well as of the subject of the thesis.

Emphasizing that it is close to impossible to maintain an objective relation to one’s object of study, Dowling asserts that critical reflexivity calls for the researcher to “become aware of the nature of [one’s] involvement” (Dowling 2010, 35). I come from a geography and anthropology academic background and have additionally been engaged in heterodox economics studies and discussions. Thus, my vocabulary as well as my perception of economics – and of the monetary system in particular – derives from a heterodox economic perspective combined with a critical geographical and anthropological perspective. Before my interviews I read up on neoclassical economics. However, a concern turned out to be the differences between the interviewees’ and my own vocabulary about the same economic and monetary phenomena. Some interviewees had an interest in heterodox economics themselves but had been educated in mainstream neoclassical economics. Thus, my position as coming from and wishing
to talk about heterodox economics sometimes established me as an ‘insider’ in relation to the interviewee, and sometimes as an ‘outsider’ (Dowling 2010, 36). This could vary even during the same interview.

Another thing to be reflexive about regarding one’s own position in relation to the research is one’s own presumptions about the issue at hand. The interviewer must aim to be open to become surprised and to find something else than expected. I have been engaged in this topic for a while, and what I found mainly aligns with what I had expected regarding conceptions of money and the monetary system, based on my own conversations with economists and laypeople alike. What did surprise me, though, was the high extent to which it felt awkward to carry out the interviews – to establish and maintain the conversation about the subject. I believe this to have been influenced by the aspect of elite interviewing or ‘studying up’. I believe too, that the divide between heterodox economics and mainstream neoclassical is such an established one that it not only contributed to the insider/outsider relation during the interviews, but also is an intrinsic aspect of the issue at hand. This divide is partly a reason why the subject of the monetary systems and its effects is a peculiar issue to discuss, in the same way as this divide contributes to a significant difference in language, vocabulary and thus perception of the issue.

2.5.1 Research positionality

Apart from my relation to the interviewees it is important to consider my own positionality in relation to the research. As Bryman writes, qualitative data analysis depends on the researcher interpreting the data. Therefore, not only does the data collected through my interviews consist of the interviewees’ subjective knowledge, the analysis is also done through my own subjective knowledge as a researcher. In the introduction, I presented the motivations for the thesis in academia and real-world developments. My own motivation stems from my background as a student of social science – very broadly. All my study work during university has been interdisciplinary within the field of social science including courses in sociology, political science, economics, human geography and critical anthropology. I am trained most extensively in qualitative research and have been especially interested in how language, culture and perceptions of the world interrelate and influence reality. During my early studies, I came across a Danish NGO called Gode Penge, which works with issues around the
nature of the monetary system to raise public awareness and knowledge about this. This sparked my curiosity in relation to my own topics of interest: of inequality, environmental issues, sustainable development, and especially in what ways such issues are thought to be linked to the economy – and specifically to money, although I have never been taught about the monetary system in my university studies. This led me to join Gode Penge and later also the Norwegian organization Rethinking Economics Norway, in addition to reading extensively about the topic in books, academic articles, and in the media. Because unequal global development has always been an interest to me – informed to a great extent by my university studies – I started wondering about the potential link between the two fields. Being based in Norway, I began reading up on the Norwegian development strategy, and when discovering the Norad-program on taxation I thought they must be proficient in the connection between the monetary system and economic development. From my work in the above-mentioned organizations I had long experience with how complicated it is to talk with lay people about money creation, but I was surprised how difficult it proved to talk to professionals about it too. This led me to include an extensive focus in the thesis on the way the monetary system is talked and thought about.

Being trained in qualitative research I do not believe it is ever possible to be a fully objective researcher. Instead I have sought to be reflexive about my own motivations and presumptions (Kvale and Brinkmann 2009, 268). I have tried to put aside my own opinions – partly as they follow from my affiliation with these two NGOs – as much as possible, but I wish to also acknowledge the potential influence of my personal interest in the topic and involvement with it as an activist.

### 2.5.2 Ethics

The data collection has been approved by the Norwegian Centre for Research Data. All interviewees have been ensured anonymity, including those who did not necessarily wish for it. Seven interviewees where men, and only one a woman; therefore, to ensure them anonymity I have chosen to use the gender-neutral singular pronouns they/them in the thesis. The interview-data was collected with informed consent and has been treated according to current data protection standards. Audio recordings and transcriptions will be deleted by the end of the research project (Kvale and Brinkmann 2009, 89).
Thorough ethical considerations are important, especially when collecting sensitive information or working with informants in vulnerable positions (Kvale and Brinkmann 2009, 51, 81). This research does not address a particularly sensitive topic, and the interviewees are all in rather resourceful and economically advantaged positions. While the research topic is not sensitive, it did turn out to be peculiar, which caused me to consider the interview situations carefully as discussed in the beginning of this section, 2.5.

An item of concern is that translation bears the risk of distorting the original meaning of the speaker. I have sought to handle this risk by keeping the original language as long as possible in the process of analyzing the data. The interviews were transcribed and coded in their original language (the interviewees speaking Norwegian, I Danish), and the parts that are quoted in the analysis were translated to English only at that point. Thus, all quotes are translated to English by myself in a way that I found conveys the original meaning best, sometimes entailing a non-literal translation. Additionally, I have made an effort of representing the statements of Norad and the interviewees in a respectful way, loyal to their world views, while keeping a critical view on the topic at hand.
3 Financing development – the context

In this chapter I present the context in which the chosen case of Norwegian development policy exists. The purpose is to show the broader landscape of taxation as a development strategy, of which Skatt for Utvikling is a part. While Skatt for Utvikling is recently established, the focus on tax in development aid has a longer history through the international Financing for Development agenda. Skatt for Utvikling builds on Financing for Development through formal agreements as well as more informally through previous knowledge and ideas. Financing for Development can be said to have its beginning as a specific focus in the international development sector when the first Financing for Development conference was held in 2002. While the Financing for Development agenda includes a broad spectrum of goals and strategies, recently a particular focus of taxation as a strategy has come to the fore. This chapter aims to tie the links from this broader international field up to the specific case of the current Norwegian program Skatt for Utvikling (Tax for Development) which was launched in 2016. Skatt for Utvikling will be in special focus in this thesis as a particular case of financing development. For a specific discussion of the definition of the case, see chapter 2.1. The aim of this chapter is, rather, to introduce the context of which it came about, and to show how Skatt for Utvikling lies within a broader international strategy on better taxation systems as a development strategy – to finance sustainable development.

3.1 Skatt for Utvikling – Tax for Development

Skatt for Utvikling is a program in the Norwegian Agency for Development Cooperation (Norad) under the division Kunnskapsbanken (the Knowledge Bank). It was established in 2016 based on Norway’s commitment to the Addis Tax Initiative (Addis Tax Initiative 2020b). While Norad has had projects before in a few countries on improving taxation systems within the Oil for Development program, when the taxation strategy was relaunched in 2016, these projects have now been transferred into the
independent program Skatt for Utvikling instead. Improving tax systems has become an increasingly important strategy for financing development in the Norwegian development strategy as well as internationally, and the rationales and strategies in Skatt for Utvikling are consistent with those of the Addis Ababa Action Agenda (United Nations 2015) and the Addis Tax Initiative, described below. However, while mitigating illicit financial flows is part of the international agenda on tax for development, in Norad these fields belong in different divisions. Issues related to tax heavens and illicit financial flows lie, in Norad, under the division dealing with corruption related issues. Two main rationales are in focus for Skatt for Utvikling. One is state building: to build more stable state institutions that function more smoothly. The other is raising state revenue to finance development: to build a stronger taxation base and thus raise revenues for government expenditure long term. This thesis will primarily consider the second rationale, which builds on the economic assumption that a state needs to collect revenue before being able to spend. This rationale is related to the broader concept of Domestic Revenue Mobilization (elaborated below) which targets raising funds from within the developing country itself, either instead of or in addition to funding from donor countries.

In addition to agreeing on development assistance, we must also agree to increase the mobilization of resources in developing countries, for example through better tax systems and higher tax revenues.

(The Norwegian Minister of Foreign Affairs, Børge Brende, quoted in The Norwegian Government 2015)

A commonly used phrase is that one krone invested in tax aid gives 100 kroner in increased taxes in return, something which Norad claims to have on its track record from their taxation cooperation with Zambia and Tanzania (Norad 2020a).

By signing the Addis Tax Initiative, Norway as a development partner has committed to double tax-related aid from 2015 to 2020. The funds allocated increased 40% the first three years, from 134 million kroner in 2015 to 189 million kroner in 2018 (Norad 2019a). In 2019, 231 million Norwegian kroner was allocated through Skatt for Utvikling, while the total Norwegian aid funds were 37.8 billion kroner (Norad 2019b, 2020b). Currently, there are four employees in the Skatt for Utvikling department, three of whom are economists. At the time of my fieldwork for this thesis, the program was in a launching phase examining the field and building partnerships. Some main partner
countries include Tanzania and Mozambique, which are also large Norad partners in other regards (Norad 2019a). Other partner countries include Rwanda, Zambia and Nepal, and generally there is, like in elsewhere in Norad, a large focus on African countries and less on Asian and Latin American countries (Lundstøl 2018a). Skatt for Utvikling works to support dissemination of research-based knowledge in the international policy arena and to promote a focus on taxation in for example the World bank and regional development banks, particularly the African Development Bank. Skatt for Utvikling includes grant agreements, country programmes and financial support to two IMF funds, and efforts to strengthen civil society within its domain (Lundstøl 2017).

3.2 Addis Tax Initiative

Addis Tax Initiative is an international initiative with large supporting organizations including the International Monetary Fund (IMF), Organization for Economic Co-operation and Development (OECD) and the World Bank. Through the initiative 25 donor countries have committed to doubling tax related aid. 20 receiving countries has signed up. Skatt for Utvikling was launched as the result of Norway’s commitment.

The aim of the Addis Tax Initiative is to increase domestic revenue mobilization in order to finance sustainable development in developing countries. Domestic Resource or Revenue Mobilization (the two terms seem to be used interchangeably) addresses various measures, from public-private partnerships to improving and raising tariffs and royalties. The main focus of Domestic Revenue Mobilization is on expanding, improving and raising taxation for the long-term purpose of raising state revenue to finance the Sustainable Development Goals. Thus, the overall aim of the Addis Tax Initiative is to help developing countries more effectively mobilize their own resources for financing development through better taxation systems.

Committing to the Addis Tax Initiative fosters partner countries’ efforts to increase reliance on domestic revenue to fund their development agenda and meet the Sustainable Development Goals (SDGs) by 2030.

(Addis Tax Initiative 2020a)
The economic assumption on which the Addis Tax Initiative is built is that taxes can be a source of financing the fulfillment of the Sustainable Development Goals. The Addis Tax Initiative was initiated in the course of the Third International Conference on Financing for Development in Addis Ababa in 2015, in relation to the outcome of that conference, called Addis Ababa Action Agenda.

### 3.3 Addis Ababa Action Agenda

The Addis Ababa Action Agenda contains seven action areas which are concerned with both domestic and international, and both public and private finance covering topics from debt to trade to innovation. Relevant to this thesis are the areas relating the most directly to finance and monetary issues. Raising public revenue through taxes, the approach to both public and private finance, and debt issues, all relate very closely to the nature of what financing is and where money come from, including whether or not to create money and how.

The Addis Ababa Action Agenda calls for increased Domestic Revenue Mobilization. An argument for this strategy is that the domestic economy is already the biggest source of financing in developing countries. Domestic resources will therefore be the most significant source of funding for any developing country, according to European Network on Debt and Development (Anderson and Chonghaile 2015). At the same time, international tax evasion and avoidance cost developing countries hundreds of billions of dollars every year. Domestic levels of revenue thus have good potential to increase by establishing better taxation systems. To give a sense of the magnitude of the sums, the following numbers are compared by the Norwegian government: Private investments in developing countries total around USD 760 billion a year and remittances from individuals around USD 418 billion a year, aid remains only around USD 135 billion a year. Illicit capital flows out of developing countries are estimated around USD 630 billion to 980 billion per year (The Norwegian Government 2015). Even a modest recuperation of avoided tax could achieve a notable expansion of domestic investments.
This third and most recent International Conference on Financing for Development was held some months before the United Nations General assembly where the Sustainable Development Goals were formally agreed. The Addis Ababa Action Agenda “supports implementation of the 2030 Agenda, including the Sustainable Development Goals.” (United Nations n.d.). It follows up on the previous Financing for Development conferences and also incorporates the concurrent development agendas. Norway was leading the preparations for the conference together with Guyana, and stated that “the focus of the conference is financing for the new sustainable development agenda.” (The Norwegian Government 2015).

The two previous International Conferences on Financing for Development were held in 2008 in Doha, Qatar, and in 2002 in Monterrey, Mexico. The Financing for Development process, which is led by the United Nations, concerns following up on the commitments from the three conferences as well as other major United Nations conferences and summits in related fields relating to the 2030 Agenda and the Sustainable Development Goals. The focus of the Financing for Development process remains the lack of financing, and the aim is to close the financing gap through domestic and international sources.

### 3.4 Assuming that tax is a source of financing

Skatt for Utvikling is a case of the larger and more broad strategy of financing development. While Skatt for Utvikling has broader goals than the financing of development, and while Financing for Development has several other means than taxation to reach its goals, this thesis focuses on the place where these two agendas overlap: Their shared objective of increasing taxation to finance development. While other development strategies have been discussed in the interviews and will be mentioned in the thesis, and while development practitioner from outside Skatt for Utvikling have been interviewed, all my sources in various ways relate to the concept of taxation to finance development. My reason for choosing this focus is that where taxation relates to financing development is where the current debate in economics on money and banking, i.e. financing in a macroeconomic perspective, is relevant: Because when the very nature of macroeconomic financing is questioned scientifically, it
necessarily have implications for a strategy seeking to finance development macroeconomically, and because employing new theoretical perspectives can have practical implications, maybe even a more effective financing for development strategy.

In this chapter, it has been presented how Skatt for Utvikling is part of a wider and increased focus on taxation as a development strategy globally. The rationale of Skatt for Utvikling, as well as the international focus on taxation, is that taxation can help finance the fulfillment of the Sustainable Development Goals. The assumption is that there is a funding gap which need to be covered in order to fulfill the Sustainable Development Goals in development countries. This gap should, according to Financing for Development, Addis Tax Initiative and Skatt for Utvikling, be covered to an higher degree by funding from within the developing countries themselves, of which taxation is seen to be a favorable source. This is relevant in relation to the current debates in economics on money and banking because the perception laying the ground for the taxation strategy is that taxation is a form of financing. This perception even treats taxation as a way to finance macroeconomic goals, such as the Sustainable Development Goals. As stated in the recently published Skatt for Utvikling-strategy: “There is currently a significant financing shortfall for the SDGs. This shortfall must mainly be covered by domestic resources, first and foremost by taxes.” (Norad 2020c).
4 Theoretical framework

The field of monetary theory is currently under rapid development. Divisions between the different schools of thought are not crystal clear and are often disputed in academic literature and in public debate among monetary theorists (see e.g. Huber 2014; and Wray 2007). In this chapter, I present the schools of thought and the differences among them, which are employed in this thesis. I seek to offer a division which is clear also for academics who are not deeply engaged in the discussions in the field, while not giving a complete and detailed review of all nuances and disputes. The very fine details are not necessary here because the objects of this thesis are the more general views of money and how the monetary system functions. I will make a distinction between neoclassical economics, including neoclassical monetary theory, versus what I have chosen to call ‘systemic’ theories of money. Among the systemic theories I differentiate between the State Theory of Money (STM) and the Credit Creation Theory of Money (CCTM).

![Diagram of Theoretical framework](image)

**Figure 1: Theoretical framework**

All the terms are established in the literature, except ‘systemic theories of money’, which is the collective term I choose to use to describe the two theories which view the monetary system more explicitly as a system including creation and deletion of money.

This chapter will focus especially on three issues: A) What money is: commodity or debt. B) How banks function: Whether they lend out existing money or extend credit – thus creating money. C) And hence: By whom – or how – money is created: By the state or by banks. The neoclassical and systemic theories differ substantially on the issues, and they are currently being avidly debated in the economics discipline. This thesis will discuss these three specific issues in relation to development policy. While
questions of financing are often microeconomic questions – how to finance my business, for example – the theoretical framework for this thesis is concerned with financing on a macroeconomic level. Consequently, the main question is not where money for a specific project comes from, but rather where money in an economy comes from: How money is created.

4.1 Neoclassical economics and monetary theory

While other social science-fields often implicitly presume that economics covers the economical field of society, the discipline of economics is defined, rather, by a specific method. The first and influential economists were broad social scientists employing history, political science, anthropology and sociology. Classic thinkers such as Karl Marx, Adam Smith, John Maynard Keynes and Karl Polanyi are all examples of this broad approach to economic analysis. However, since the birth of the formal discipline of economics the field has come to be defined by the mathematical and statistical methods with which it studies all areas of human activity (Sandmo 2007). Another difference between economics and other social sciences is the often-criticized dominance of one school of thought, namely neoclassical economics. University programs in economics often first and foremost teach neoclassical economics, while other economic schools of thought are relegated to elective courses. Hence, in public perception ‘economics’ has come to mean ‘neoclassical economics’.

Neoclassical economic theory tends to not be occupied with theorizing about money, and when it does, it does not ascribe the nature of money much importance (Ingham 2004, 7). Neoclassical economic theory builds its theoretical understanding of money around the barter history of origin, which Adam Smith made popular. This explanation employs an understanding of money called ‘commodity-money’ and is present in many economics textbooks around the world today (Graeber 2011, 22f). The commodity-view of money expects money to operate more or less under the same laws as other commodities (John Stuart Mill 1848 in Martin 2014, 205). According to this explanation, money originated as a replacement for simple barter. Instead of people exchanging goods and services directly, one commodity was chosen as the general ‘medium of exchange’. It could be generally useable commodities like salt, tobacco, or
cod, but precious metals – sometimes minted – was the generally preferred mediums of exchange (Smith 1776 in Martin 2014, 9). This explanation is essential to understanding the view of money in neoclassical economics:

For economists, it is in a very real sense the most important story ever told. It was by telling it, in the significant year of 1776, that Adam Smith, professor of moral philosophy at the University of Glasgow, effectively brought the discipline of economics into being.

(Graeber 2011, 24).

This origin-story of money is so widespread that it is taught not only to economists: “[…] by now, this story has become common sense for most people. We teach it to children in school books and museums. Everybody knows it.” (Graeber 2011, 28).

Therefore, this story also forms the basis for popular perceptions of money among laypeople: What Braun calls the folk theory of money (Braun 2016). In economic theory generally, money is described as “a store of value, a unit of account, and a medium of exchange.” (Mankiw 2016, 82). Neoclassical economics often describes money as a ‘veil’ over the real economy. Because its function is simply to make barter more efficient, money is not seen to be of particular importance in itself (Ingham 2004, 33, 66). The significance of the amount of money in an economy is seldom considered. As a numerical measure of the real economy, by definition, more money is seen to cause inflation and less money to cause deflation. While deflation is thought to have negative consequences, moderate inflation is seen as desirable and at the same time perceived to be neutral in its effect on the economy over the long term. An inflation rate of around 2 % is commonly agreed to be the appropriate level (Mankiw 2016, 126).

Neoclassical economics conceives of banks as financial intermediaries. Some textbooks describe banks as intermediaries more or less in the same manner as other financial intermediaries, in the sense that they channel funds from savers to borrowers (Mankiw 2016, 583; Holden 2016, 319). When neoclassical economics does explicitly consider aspects of money creation, the most common approaches are the ‘fractional reserve’ and ‘money multiplier’ models. These models, in slightly different ways, state that the central bank creates the monetary ‘base’. Banks then ‘multiply up’ this money by lending out more money than what was deposited with them. This process is explained as a ‘fractional reserve system’, where the bank holds a fraction of deposits in
reserves, while lending out the rest. Through the continuous lending and re-lending this process ends up ‘multiplying’ the total money supply (Mankiw 2016, 95). The reserve ratio is regulated by monetary authorities. These theories are described in economics textbooks, often briefly and scarcely integrated with other economic topics. Unsurprisingly, therefore, Mankiw ends the first brief chapter about money and banking in his textbook like this:

For our current discussion, these details are not crucial. It is sufficient to assume that the Fed (or any other central bank) directly controls the supply of money. (Mankiw 16, 84).

Later in the book a longer chapter elaborates on fractional reserve banking and the ways in which the central bank can and cannot control the money supply, but again the topic appears separate from the rest of the book.

To sum up, neoclassical economics does not view money as particularly important, and the neoclassical monetary theory that does exist consist primarily of the fractional reserve and money multiplier theories.

The perception of money as a commodity is intuitive to most people, and it is closely linked to money’s existence as gold and silver coins (Braun 2016, 1073). The systemic theories of money, on the other hand, claim that coins (and electronic account money) are only physical (or electronic) tokens representing underlying credit and merit systems. In the following, two such credit theories of money will be presented: first the State Theory of Money (STM), then the Credit Creation Theory of Money (CCTM).

### 4.2 The State Theory of Money

The State Theory of Money (STM) has its foundation in a juridical perspective, also called chartalism. The state theory of money has recently had a revival as Modern Monetary Theory, with proponents such as Larry Randall Wray and Mariana Mazzucato (Wray 2015; Mazzucato 2018b). STM sees money as essentially a legal construction: A sovereign state with a sovereign currency has the final legal power to determine the
nature of money within its jurisdiction. Pieces of paper or numbers in an account are, through the legal framework of the state, turned into purchasing power. Money is not seen as tied to any real valuables, but seen essentially as a legal debt-relation between a state and its citizens.

STM conceives of the monetary system in a somewhat more systemic way than neoclassical economics, as it deals explicitly with creation and deletion of money in the monetary system. Money is seen to be created through state expenditure: When the state spends money, the money supply increases. Similarly, the state deletes money from the economy through the collection of taxes. In this view there is no technical limit to amount of money the state can create, and therefore spend – as long as the state has its own currency and is willing to accept the potential inflationary pressures in the economy (Wray 2014, 28). The inflationary potential is seen to be determined by the productive capacity in the economy: If the economy is running below full productive capacity, increasing the money supply will not cause inflation. In case it is necessary to create more money – e.g. to cover specific necessary government spending – than the productive capacity can absorb, taxation can be increased to counter inflationary effects.

STM agrees with The Credit Creation Theory of Money that private banks create money when extending loans (elaborated further in section 4.3), rather than lending out already existing money. STM perceives this arrangement as the state giving banks a mandate to run parts of the monetary system, which is determined ultimately by the legal framework developed by the state. Money issued through private bank lending is money because: The state accepts it in tax payments, the state uses it through state spending, and because it is backed or guaranteed by the state (Martin 2014, 29; Wray 2014). Thus, according to STM, while both the state and banks create money, the state ultimately holds the power over both types of money creation – given that the state is monetarily sovereign. In order to have monetary sovereignty, it is necessary for a state to: issue its own currency, impose taxes in that same currency, only issue debt (i.e.: government bonds) denominated in that same currency, and have a floating exchange rate (Wray 2007, 7). A state which is not monetarily sovereign faces some difficulties. “In contrast to the sovereign nation, the non-sovereign government promises to deliver third party IOUs (that is, dollars) to service its own debt (while the U.S. and other sovereign nations promise only to deliver their own IOUs).” (Wray 2007, 9).
The barter story of money has been the empirically dismissed (Humphrey 1985; Graeber 2011), and the systemic theories of money build on another conception of the historical origin of money, namely as credit rather than commodity. According to STM, money’s historical origin is from the accounting of penalties or taxes – debts between the state and its citizens (Ingham 2004, 91). The simplified state origin of money story sounds something like: A state issues money, in which it pays its soldiers and other state employees. Simultaneously, to make that money useful in its economy, it imposes on its citizens a tax to install a demand for its money. In this historical view is a higher focus on power than in the barter history of money. Also regarding the current monetary system, the systemic theories of money have a higher focus on power relations ingrained in the design of the monetary system, and neither of these theories views money as ‘neutral’ on the economy (Wray 2007, 1, 7).

### 4.3 The Credit Creation Theory of Money

The Credit Creation Theory of Money (CCTM) differs from other theories of money, in that it is based strictly on current empirical studies. In that way, proponents could argue that it is a description of the monetary system rather than a theory of it. CCTM empirically studies the current banking system which holds the vast majority of money (Ryan-Collins et al. 2012).

Recent studies by the economist Richard Werner, who got access to and followed transactions chains in a commercial bank, show how banks create deposits when making loans and delete deposits when loans are repaid. Werner concludes that a bank creates the money on a customers’ account when it makes a loan, and this is the case for all loans made by the bank studied – no transfers were made from other accounts at the bank when a loan was made. Additionally, the bank did not have to make sure that it had sufficient reserves at the central bank because any additional reserves needed where acquired at a later stage. This means, Werner argues, that instead of deposits generating loans, loans generate deposits (Werner 2014b, a). Such studies disprove the commodity theory of money and the notion that banks act as ‘intermediaries of loanable funds’, and thus rebut the money multiplier and fractional-reserve theories (Werner 2016). The
CCTM view is becoming increasingly mainstream in both academic and professional economics circles because of its explanatory power. While the fractional reserve theory may have explained the functioning of banks once, CCTM explains the current monetary system in most economies better. The nature of the monetary system has been transformed in tandem with global markets and new technology (including the internet). For example, The Bank of England has promoted this view since 2014 (McLeay, Radia, and Thomas 2014; Jakab and Kumhof 2015), and economics textbooks at two big Norwegian universities have been changed recently (Steigum 2018 at BI Norwegian Business School; Holden 2016 at University of Oslo).

In countries that adhere to the Basel accord, what limits the money creation by banks is not their reserves at the central bank but each banks’ equity – and especially the possibility of profitable lending. Therefore, “despite private bank credit money being guaranteed by the state, the state has no control over private bank lending, and thus neither the money supply.” (Jackson and Dyson 2012, 80). This implicates that even though the fractional reserve theory is being used by neoclassical economists as an ideal model, in reality it holds true only in a limited number of countries throughout the world (Gray 2011, 54-55). While some countries do have reserve requirements, these do not always pose a limitation to money creation by private banks. Because if the capital requirements are bigger than the reserve requirements, the bank can at any time swap the types of assets it is holding to adhere to reserve requirements and thus the reserve requirements become obsolete.

In the neoclassical literature, the money-creating capacity of the banking sector is only vaguely addressed as something that drives up inflation; instead the focus is on the central bank as a driver of inflation (Mankiw 2016, 105f; Holden 2016, 282). According to CCTM, however, money creation by banks is much more important, since it accounts for 90-95% of the money supply – at least in all developed economies (Ryan-Collins et al. 2012). While the credit creation by banks may not empirically cause inflation in consumption goods, which is the traditional measure of inflation – it does cause high inflation in financial assets including real estate, which indirectly has an influence on the real economy. CCTM proponents imply significant problems with the distribution of newly created private bank money, to which I will return in section 4.5.
4.4 Differences and similarities between the theories

It is an ongoing discussion to what extent the State Theory of Money (STM) and the Credit Creation Theory of Money (CCTM) agree on all details regarding the functioning of the monetary system. Especially the question is disputed to what extent the state has control – juridically or practically – over the money creation done through private bank credit. Additionally, the specific and detailed definitions of monetary sovereignty for specific states are debated among theorist from the two schools of thought. However, the state and the banking theories correlate to a much higher degree than any of the two does with neoclassic economic theory. This is particularly evident on the point that they both are credit theories of money, and thus see the source of money to be *endogenous* – that is, as a function of the workings of the economy itself. On the contrary, commodity theories of money perceive the source of money to be *exogenous* – that is, a function external to the economy (Skidelsky, 35).

4.4.1 Systemic monetary theories vs. neoclassical economics

Both systemic theories of money, STM and CCTM, deal explicitly with aspects of money creation and deletion, and the effects these have in the economy. Contrarily, neoclassical economics considers money a neutral ‘veil’ over the economy. In this latter view, the economy is essentially seen to be an advanced version of a barter economy, and as such money creation and deletion is not explicitly dealt with.

Another contrast is that the systemic theories of money perceive the monetary system as a *system*. This facilitates a more explicit examination of how money enters the system through money creation, and how money leaves the system through money deletion. Neoclassical economics does not explicitly conceive the monetary system as a system, but considers it, rather, as the total of monetary transactions.

A third way in which the two systemic theories differ from neoclassic economics, is that both STM and CCTM highlight the role of institutions. In each their way, they emphasize the impact which the state and banks have on the economy. On the contrary, neoclassic economics considers the economy as constituted by rational individuals – the so-called ‘economic man’.
4.4.2 State vs. credit creation theories of money

The two systemic theories of money are motivated by different critiques and have emerged independently of each other with different focuses. The two theories build on different foundations: a juridical and an empirical one, respectively. They differ from each other with regard to their claims to fact: STM highlights the fact that *juridically*, it can be established that money is a construct of law, therefore the state has juridical power to create money. Conversely, CCTM highlights the fact that *empirically* it can be established that private banks effectively create money when extending credit.

Another important difference between the two theories is what they emphasize to be the most important traits of the monetary system, regarding the creation and deletion of money from the system: STM emphasizes how money is created through state expenditure, and consequently that new money is distributed this way. In the same way money is deleted when collected through taxes to the state, something which also has distributional effects. On the contrary, CCTM emphasizes how money is created through credit extension by private banks and deleted when the loans are repaid. That means new money is distributed into the economy through the lending decisions by private banks.

STM acknowledges the empirical fact that private banks create money independently but hold that money creation by private banks is nevertheless constrained by state regulation. CCTM acknowledges that the state legally can decide to create money but insist that the state practically has no control over private bank credit creation. Furthermore, CCTM emphasizes that private bank money creation accounts for a significantly larger amount of money in circulation than state issued money, and thus in practice exerts greater influence on the economy.

4.5 Normativity

An additional way in which the three economic theories differ are in their normative aspirations. Proponents of the systemic theories often make more or less explicit
normative arguments, highlighting the consequences of the monetary systems and sometimes proposing changes that could be made, given the employment of their theory rather than a view of money as neutral. While neoclassic economics does view money as a neutral veil over the economy, and thus tends to neglect any consequences of the monetary system, this perception in itself could be characterised as a normative perspective. Neoclassical economic theory sees banks as intermediaries, channeling funds from people with surpluses to people who lack financing, i.e. from savers to borrowers. Through this mechanism, money supposedly flows to the places in the economy where there is the most need for them, seeking a so-called credit equilibrium. The implicit normative aspect here could be said to be that the (re)distribution of money is politically neutral because it is the result of the most rational and effective distribution of money possible.

On the contrary, the systemic theories of money more or less explicitly raise – and answer – normative questions in regard to two aspects: Firstly, which institution(s) should determine the money supply? Both theories assert that this aspect is more important for monetary stability than is inflation. Secondly, which institution(s) should determine the distribution of new money int the economy? Both theories address what some scholars call pre-distribution, which stands in contrast to redistribution. While taxes redistribute existing money, predistribution denotes the distribution of new money. New money is always more valuable because the first time money is used it holds the value before any inflationary effects occur (Huber and Robertson 2000, 65). This aspect of distributive power is integrated in the systemic theories of money, while it seems to be absent in neoliberal economics and monetary theory. The systemic monetary theories make this aspect of power explicit and seek to integrate it in economic analysis.

Those with the power to create new money have enormous power – they can create wealth simply by typing figures into a computer and they decide who can use it and for which purpose.


This distributional power can be relevant too in development economics and development policy. The two systemic theories of money promote different policy recommendations according to each their driving critique.

The State Theory of Money (STM) promotes the normative view that the state can
and therefore *should* employ money creation to solve societal needs. This is often seen in the real world in the occurrence of wars and of banking crises like that in 2007/8. STM promotes the view that the policy tool of money pre-distribution should be used especially to ensure full employment. Some promote the view that state money creation should be employed to solve the climate crisis, as argued in relation to Green New Deal proposals (Ocasio-Cortez 2019). It could be argued that state money creation also could be employed to solve social problems such as poverty. Therefore, it follows from that a state should pursue monetary sovereignty, which enables it to employ such policy. The limit for non-inflationary money creation is seen to be determined by the productive capacity of the economy within the domain of a given currency. It could be argued that if it is necessary to create more money in order to solve a certain crisis than the productive capacity can match, the state can use taxation to draw money out of the economy again to limit the inflationary effect. In this way, a state can redistribute money in the economy more effectively through money creation and subsequent money deletion, rather than waiting for the collection of taxes first, in order to be able to spend subsequently.

The Credit Creation Theory of Money (CCTM), on the other hand, emphasizes the influence on the economy of the distribution of newly created money from bank lending. Because banks are private firms, such lending is done based on profit incentives. Therefore, most new money goes to financial assets such as real estate, and to more specialized financial products. Less new money goes to smaller firms, entrepreneurs, and the real economy, simply because such lending is not as profitable for the bank. Some CCTM proponents argue that such a distribution of new money has numerous harmful consequences.

To state it very clearly, in stark contrast to the quote by the standard neoclassical textbook by Mankiw in the beginning of this chapter, systemic theories of money assert that “how money is made matters” (Desan 2014, 5).
5 Skatt for Utvikling – A case study

So far, the empirical context of Skatt for Utvikling as part of the wider international agenda on development strategy, Financing for Development, has been outlined. The theoretical framework has been presented discussing the differences and similarities between different strands of monetary theory involved in the current debates, and the emerging consensus shift within economics on the nature of money and banking. The following three analysis chapters concerns the connections and discrepancies between the conceptions found in the empirical data and in the economic theoretical literature. The conceptions found in the data are those perceptions expressed by the interviewees about the nature of money and banking in relation to the development strategies they work with. The first part of the analysis focuses on the role of the state in the monetary system: In what way government spending is restricted by incoming tax revenue, what role the money supply has regarding inflation, and to what extent the state creates money itself and what consequences that has. The second part of the analysis focuses on the role of banks in the monetary system: Whether banks need deposits in order to lend; Whether deposits make loans or loans make deposits; Which factors limits private bank money creation; And what distributional effects banking has. These first two chapters deals with the primary focus of the two systemic theories of money and banking: State Theory of Money (STM) and Credit Creation Theory of Money (CCTM). As such they are theoretically driven discussions, widely based on economic theory, however also including some of the anthropological and sociological scholars whose research informs and engages with these theories. The third part of the analysis takes a slightly different form in that this part concerns the role of language in conceiving of money and banking: Whether the language used about banking is logically misleading; How language and popular perceptions interact with origin stories of money and banking; And, how a limited language about money and banking may lead to a limited understanding of the nature money and banking. Because this topic is in rapid development at the moment and not yet as widely investigated academically, as well as because of the nature of the topic, this part will apart from the empirical data and academic literature include some popular literature as well as popular media articles from scholars engaged in the current discussions.
The main findings in the coming chapters are that the conceptions of money in the Norwegian development strategy as found in the data are based on neoclassical and microeconomic rationales and perceptions of money and banking, while the systemic perspectives as well as their influence in the ongoing consensus shift is only fragmentally present. Moreover, in several ways, language about money and banking proved an obstacle, if not in conceiving of money and banking then at least in having meaningful conversations about the topic.

5.1 The role of the state in the monetary system

According to neoclassical economics, the state is positioned in the monetary system almost similar to regular economic agents such as firms and individuals. This means the state is perceived to need an income, in the form of tax, in order to spend. The following four sections identify the conceptions that the interviewees held about these issues and their perceived implications along with statements from Skatt for Utvikling reports. The findings are discussed in relation to neoclassical economic conceptions and State Theory of Money (STM).

5.1.1 The state as a money user

First, let us look at the interviewees’ view of the state as simply one of the many users of money in an economy.

State income for covering development expenditure

When asked about the objective of Skatt for Utvikling, an interviewee responded:

To finance these sustainable development goals – which all countries have committed to, it’s a shared responsibility… It’s because financing those has to happen primarily domestically, – not through aid for example, or foreign lending. That’s why Skatt for Utvikling has been established as a program. Because one wishes to help the country obtaining its own funding to finance the
public expenditures necessary to achieve the Sustainable Development Goals. (Int. 6)

The interviewees and the Skatt for Utvikling and Financing or Development reports all describe tax as an income for the state. Efforts to achieve the Sustainable Development Goals are perceived to pose an expenditure for the state, and in order to cover this expenditure the state needs to increase its income, i.e. collect revenue through taxes. The interviewees as well as the written material on Skatt for Utvikling use the Norwegian word “inntekt” or “skatteinntekter”. In Norwegian, the word for revenue and income is the same. The aspect of how language about money, and conceptions of the workings of money, interrelate deserves more scrutiny, and I will return to this in the third part of the analysis, chapter 5.3. For now, I want to note that I will sometimes choose to translate the word ‘inntekt’ to ‘income’ rather than ‘revenue’, also when denoting state revenue, because this interpretation aligns with their general premise of taxes as an income for the state, similar to that of a firm or a household.

Skatt for Utvikling has more than one objective, and while state building is a significant one, which I will return to in section 5.1.3, the main objective is to increase state revenue. When asked whether Skatt for Utvikling has two main objectives: state revenue and state building, a Skatt for Utvikling employee replied: “Yes, so, but in a way Skatt for Utvikling has one main objective, and that is to increase domestic taxation. To achieve better taxation, that is, increased tax revenues for the state.” I followed up: “So, income for the state?”, and they responded: “Yes, income for the state, right. That’s the main objective.” (Int. 6). They explained how customs revenue (import tax) comprises up to one third of tax revenue in many countries and is an area with a potential for higher efficiency, and therefore a good area by which to increase state revenue.

The choice of taxation to increase income to finance the Sustainable Development Goals is due to the belief that this source of income has the highest potential, especially considering that tax is already the biggest source of state revenue in developing states. A Skatt for Utvikling employee said “The reason to do it… It is already so, that the main part of public revenue is not aid, and not foreign lending, and not foreign investment. It’s tax revenue which is the most important. The biggest part of public revenue in virtually every country.” (Int. 6). This sort of comparison with other large money flows into developing countries was made regularly by the interviewees.
Another interviewee said: “If you add together all the large money flows: aid… remittances and investments… Then that amounts to one fourth of the total income from tax, now today.” (Int. 7). The same thing has been stated by the Norwegian government (The Norwegian Government 2015). Although private remittances and investments do not necessarily result in state revenue (Ndikumana and Blankson 2015), it is a well-communicating picture that all money flows into a country represent a value and all add to that country’s wealth.

“We know that there is a potential for increasing national revenue through taxation.” (Int. 8). One interviewee pointed out the “huge potential revenue from extractive industries” (Int. 3), the collection of which Norwegian tax advisors help to build systems for. Another worked with so-called “sin taxes”: taxes adding to the price of health-harming products like alcohol, tobacco, and sugary products. The interviewee argued that while sin taxes in developed countries are mostly applied in order to reduce use of these products, in the context of developing countries “one would rather use the argument of revenue generation, or maybe saving of future health costs, as the reason [for imposing such taxes].” (Int. 5). In this person’s reasoning, the image of state expenditures as something that would have to be financed through first collecting an income was also clear:

Taxing especially alcohol, tobacco, and sugary drinks, especially soda… We see that that generates a very large potential revenue for a country, if they wish to use it. And there, they can also – if they want to – earmark these for health for example, which would be a natural thing to do because it is connected to a health effect. So, we observe in some countries, that they have managed to double the health budget through these means.

(Int. 5)

**Neoclassical and microeconomic theory**

The way Skatt for Utvikling treats the role of the state is consistent with neoclassical economic theory: that the state budget is equivalent to other economic agents’ in the way that the state is *user* of the currency. If an economic agent needs to spend money it does not *yet* have, it can take out a loan. It will then need to pay back that loan later. It can, so to speak, spend future income in advance. Through neither of these actions,
however, is any of the agents issuing or creating money, their role remains fundamentally money users.

5.1.2 The state as a money issuer

The State Theory of Money (STM) sees the role of the state in the monetary system as radically different from that of other economic agents (provided that the state is sovereign, which I will return to in section 5.1.4). The state is not simply a money user like firms and households, but the issuer of money. This has extensive implications for how the economy, and especially the monetary system, is perceived. According to STM, the constraint on state spending is not how much money it has “in its coffers” so to speak. “[T]he sovereign government's ability to make payments is not revenue-constrained precisely because it spends by emitting IOUs.” (Wray 2007, 8). Because the state can issue new money when spending, then by definition, its spending cannot be limited by the amount of money it “possesses”. That does not necessarily mean that the state can spend unlimited. But instead of revenue being the constraint on state spending, according STM the constraint is instead “real resources offered for sale for the state’s currency.” (Wray 2014, 31). If the money supply is increased by much above the productive capacity of the economy, inflation may occur, but then taxes can be used to counter the inflationary effects. I will return to a discussion of the perceptions of inflation in section 5.3.2. The point here is that STM perceives the monetary system to work the opposite way of the view of neoclassical economics. The view of STM is that the state creates money through its spending, then withdraws it through taxes. “To put it very briefly, the spending logically comes first before government obtains tax revenue or sells bonds.” (Wray 2014, 29).

No magic money tree

During the interviews, I asked the interviewees how they thought of this STM perspective: that the state creates money, and therefore has a position in the monetary system that does not require it to collect money through taxes before spending. It was
clear, firstly, that they did not agree with that perspective and insisted on the neoclassical economic perception on the monetary system. Secondly, it became clear— as discussed in the methods chapter—that they were not used to talking about money creation at all. Since money creation is seldom dealt with in neoclassical economics, this is not surprising, and it shows how limitations in economic theory are reflected in the profession as well. One insisted skeptically: “Well, the money [that the state spends] has to come from somewhere.” (Int. 6), thus refusing the possibility of the state creating money itself, insisting it needs to acquire them from somewhere (else). This is the quote with which I started this thesis. It highlights very precisely the neoclassical economic as well as popular perceptions of money, which do not discuss money creation.

Everywhere in economic debate, including Financing for Development, it is asked “where should the money come from”, meaning “where is money already lying around that we can move over here instead”. No one seems to ask “where does money come from, at all” or more specifically “how is money created”. Another interviewee more implicitly rejected state money creation as an option for financing development. When replying to my question specifically about state creation of money, they did not mention money creation at all, but instead related to terms of economic organization:

“Well, then, one could of course have organized the economy differently, in a way where state revenue or state power was achieved in a different way: One could have a fully planned economy, or another way of organizing it. But in a capitalist economy, this is usually how it works. That you collect taxes and duties from the private sector in some way or another, whether it's from firms or individuals or others. And then, obviously, if individuals, firms, and other actors has low wealth creation and doesn’t have any particular surplus, then it’s a very thin basis for taxation. That will make it difficult, also for the public sector, to fulfill its role. So there is a form of symbiosis there, between the private and public sector.”

(Int. 3)

However, in contrast to what the interviewee implies, STM is not a proposal for an alternative organisation of the economy. Rather, it is an alternative explanation of, or way of viewing, the economy as it is today. Secondly, the interviewee’s reservation about “a very thin basis for taxation” demonstrates a perception which is common also
in popular perception: That the private sector creates wealth, and the state taxes and then spends it. This notion from daily speech and reasoning often adds to the confusion around where money is created and the link between value and money (see e.g. Mazzucato 2018a). I will return this issue in section 5.3.3.

Some of the interviewees agreed that a state technically can create money to cover its expenditures. But they dismissed it as an option in the real world due to the risk of inflation. “I think it’s rather dangerous. It might be possible to use in some cases… to increase the supplying of money into the economy, without doing anything else, budget-wise. But it’s high risk. Very high risk.” (Int. 7). Most interviewees disagreed with STM that the state creates – or has a realistic opportunity to create – money through government expenditure. However, as this last quote show, some reluctantly agreed that it would be theoretically possible.

The central bank creates money and then what?

While the interviewees dismissed the option of a state creating money to cover its expenditures, they held that it is the central banks’ role to create money. One emphasized the role of the central bank in managing inflation – a risk seen as tightly linked to the money supply and thus especially to increased issuing of money (Int. 3). Another interviewee replied, when I asked them directly who issues money: “Yea that’s mainly – or I mean that varies – but mainly it’s the central bank who does that, still.” (Int. 6). They continued by noting that private banks in Hong Kong once where allowed to issue their own paper notes, and that cryptocurrencies are issued in yet another way, but emphasized in conclusion that money is mainly issued by central banks. The interviewees agreed with neoclassical economic theory that money is issued by central banks, but they were not clear on how this newly issued money then enters the economy. STM, on the contrary, is very clear that because the central bank is a state institution, and thus the state’s bank, the money it issues enters the economy through the state budget. According to systemic theories of money, money can be created for – and enters the economy through – state expenditure.
The view that the state must collect taxes in order to spend, held simultaneously with the view that money is created by the central bank, reflect an interesting contradiction in the conception of money creation, made possible by the lack of a comprehensive theory of money creation in neoclassical economics.

5.1.3 State building: Social contract or commercial contract?

Aside from revenue collection, state building is the other major objective of Skatt for Utvikling, which was also often mentioned in the interviews:

We try – at the same time – to not only focus on international companies, because we also want to increase the tax base, that is, the number of people and firms that pay taxes domestically. And this is where this democracy aspect enters. That, if you hand over part of your personal income to the state, then you’re more concerned about who controls that money, and how it’s being used. So that’s where there’s thought to be a component of democracy. “No taxation without representation” as it’s said in the US, right. You’re not justified in imposing taxes unless I also have an influence on how that money is actually being used.

(Int. 6)

According to the interviewee, as important as it is to increase the amount of money collected in taxes, another major objective is to make sure that also smaller taxpayers are included: To increase the tax “base”. This is to build in an aspect of state legitimacy and a sort of engagement and agreement between the state and its citizens. Taxes are seen as a way to make citizens more engaged in the functioning of the state, and thus politics too – because taxpayers will want to know how their tax money is spend.

And of course, you can say there are alternative ways to do that. So, it’s one thing that you receive health services in return, or education for your children, roads to drive on, or what it might be. But the main point is, that the more you pay, or at least the more people who pays… I mean, if you pay one krone in taxes, then of course, that isn’t much for any of us, but if you pay like 10… 20… 30… 40% of your income, then you’ll start to think: OK, now I want something in return. Because you want to know what this money is being used for. You won’t just say … [whatever]. And then you’ll become
more concerned who’s the president, or who are the elected officials, etc. And you’ll follow the domestic political debate more closely.

(Int. 6)

It was emphasized by several interviewees that taxpayers will “want something in return”, aligning with the neoclassical economic view that tax is payed to the state, then spent. Not like the view of the State Theory of Money (STM) that the state creates money through spending, then collect it in taxes to prevent inflation or regulate the economy. A reason for increasing the tax base, thus making as many citizens as possible concerned with what happens to their tax money, according to this interviewee is then, to make people follow domestic politics more closely – a democracy building aspect. Another interviewee referred to the tax relation as a social contract:

I think, if you look at early state building, one of the first things you do, - the first coordination between people and state, often on a local level… In Norway it was at municipality level. I have worked the last four years in Somalia with local taxes, and there, what you are seeing is that: OK, we collect market taxes, we collect property taxes, and then we build a small road. It’s trivial amounts of money, but it creates some revenue, and it creates a relation. So the social contract that arises is in focus.

(Int. 8)

A social contract is also described in a working paper by the International Centre for Tax and Development, which was written in relation to the initiation of the Skatt for Utvikling work:

The relationship of civil rights and duties within a jurisdiction is at the centre of the social fiscal contract between citizens and rulers. Different selection and election processes can show citizens’ revealed preferences in terms of governments that can provide them with the best goods and services for the least cost (tax), but these systems depend on access to and use of the right to vote.

(Lundstøl 2018b, 8)

The view of a social contract is in my sources described in a way which aligns strongly with a neoclassical market view of the economy, with the state remaining a type of market actor. The dynamics between the tax-paying citizen and the tax collecting state providing services to the citizens in exchange, appear transactional like that of a
membership or a subscription: Customers pay a company for providing services in exchange. In the same manner, the state is described to be obliged to provide its tax-paying citizens services in return, in reasonable equivalence to the amount they pay. That is, the service should represent the price payed for it, and the language around what is fair resembles those of market-determined prices. The above quote from the International Centre for Tax and Development working paper reflects this view even stronger than the interviewee, in that it refers to a “social fiscal contract”, and that the state should provide taxpayers “with the best goods and services for the least cost.” (Lundstøl 2018b, 8, emphasis added).

In contrast, in the view of STM taxes are seen as establishing of state power, especially in a historical perspective. “Early state building”, which the interviewee mentioned earlier, is in the STM perspective not seen as a social contract where people start paying taxes voluntarily in agreement with the state to receive services in return. Instead of such voluntary commercial or free-market-like contract between citizens and state, STM emphasizes how early state building was tightly connected with issues of law and power. Coinage has been part of implementing and maintaining power throughout the history, in medieval Europe as well as colonialist times in South America (Graeber 2011, 251-329; Ingham 2004, 55). “[…] modern sociological analysis tends to forget that monetary sovereignty was established to a large extent by extreme physical coercion such as branding on the forehead with coins and execution for counterfeiting.” (Ingham 2004, 65).

The idea reflected in the data, that the market is there first and subsequently a state is built through a fiscally fair commercial-like contract, aligns with neoclassical economic theory. On the contrary, STM proponents argue that states in many ways create markets (Wray 2007, 4; Mazzucato 2018b, 274f). This is not to claim that STM advocates violent measures to install state authority nowadays. The point is that STM promotes a higher focus on the legal and institutional aspects of a state’s economic actions, rather than the free-market, rational-agent view of neoclassical economics. STM recognises taxation as an inflationary control and for promoting and discouraging certain areas of the economy but emphasises that taxes are not inherently necessary to finance state expenditure.
5.1.4 Monetarily sovereign states

According to State Theory of Money (STM), state building is crucial, just as Skatt for Utvikling asserts (Ingham 2004, 124). What is central in STM, though, is monetary sovereignty. A monetary system cannot function properly only on free market conditions but must be enforced by an authority (Ingham 2011, 49). Monetary sovereignty depends on the ability of the state to prevent the use of foreign currencies in its domain and to impose taxes in its own currency. In order to effectively impose taxes, it is imperative that citizens have confidence in the state. To illustrate, Ingham mentions a modern case where this is not so: “For example, all attempts to create a modern currency under central bank control in early twenty-first-century Afghanistan are compromised by the ability of local warlords to print their own money for the payment of their soldiers and the collection of local tribute,” (Ingham 2004, 77). Currently, a large part of the Afghan state budget consists of foreign currency received through development aid from abroad (Int. 2). To build “an authoritative imposition of a money of account over a geographical space” is a necessary precondition for the creation of monetary sovereignty (Ingham 2004, 33).

The economist Fadhel Kaboub works with the importance of monetary sovereignty in a development context. According to him there are four major elements of monetary sovereignty of which two are more possible to achieve for most governments: to issue its own currency and to impose taxes in that currency. The next two elements are more complicated and can be harder to achieve. To only issue debt (i.e. government bonds) denominated one’s own currency can be difficult for development countries who may not have a well-established credibility in the global financial markets. And to operate under a flexible exchange rate regime is complicated to manage for countries dependent on imports. Monetary sovereignty is rarely perfectly fulfilled and STM sometimes describes it as a spectrum. Fully monetarily sovereign states include USA, Japan, Canada, Australia, and the UK. Fully ‘dollarized’ countries – i.e. entirely non-monetarily sovereign – include Ecuador and the Franc of the Financial Community of Africa (CFA) countries in central and west Africa (Kaboub 2019).

The degree to which a state can make use of monetary policy according to STM heavily depends on its monetary sovereignty (Wray 2015, 41). But even though Skatt for Utvikling has state building as a major objective, whether the developing countries
are monetarily sovereign or not, is not an apparent concern for them. It was mentioned neither by my interviewees nor in the Skatt for Utvikling or Financing for Development written material. According to STM this should be a central concern, because it highly affects the answer to what “actually finances state expenditure – taxes or bonds; and, as it is the ultimate source of all money, whether the state needs its citizens’ tax money at all.” (Ingham 2004, 79).

**Different reasons for state building**

Building a well-functioning state is a desirable objective according to both the State Theory of Money (STM) and neoclassical economics. Both theoretical perspectives agree that a well-functioning state will contribute to the redistribution of wealth from very rich people and companies to the poor part of the population within developing countries. However, the reason for promoting state building differs between the theories: In the neoclassical economic perspective a well-functioning state is simply a means to redistribute wealth effectively and legitimately from rich to poor. But to STM, the aim of building a well-functioning state is to strengthen its sovereignty on order to keep (or regain) control over its own currency and direct its currency to the advantage of its citizens and the domestic economy. The two theories disagree heavily on whether the state is dependent on tax revenue in order to be able to fund necessary public services such as sustainable development. Although Skatt for Utvikling declares state building as an aim, all of my data indicates that the overriding objective is to collect sufficient revenue to finance development. I assess this prioritization to be rooted in the neoclassical economic conception and the popular perception of money as a limited resource – not something the state can provide in case of need. If Skatt for Utvikling were to integrate STM perspectives, the program might put a stronger focus on state building rather than on revenue collection. It could open for discussions of what and how a state ought to provide for its citizens to gain legitimacy, rather than what it can afford.

This chapter has analysed perceptions of the role of the *state* in the monetary system. Despite their significant disagreements both the systemic theories of money (STM and CCTM) – and to some extent also neoclassical economics – hold that banks create money. The following chapter will analyse conceptions of the role of *banks* in the monetary system.
5.2 The role of banks in the monetary system

A stereotypic model of banks is as a place where people with too much money put their spare money, so people with too little money can borrow it. That is a simple explanation which is easy to understand, and it corresponds to the way we use the word ‘bank’ in other contexts: foodbank, knowledge bank, etc. The explanation figures in various versions of economic textbooks as well. It is clear, though, that banks do not have a physical vault where some people’s money are put, and those same money are then lent out. That description is too simple. However, it is less clear, and increasingly disputed, how exactly the link between deposits and credit works, and to what degree banks are dependent on receiving deposits to be able to extend credits. This chapter will discuss the opinions about that link held by the interviewees, and the perceptions employed in Financing for Development and Skatt for Utvikling reports and compare them with the models employed by neoclassical and systemic theories of banking.

Two theories will be discussed: the neoclassical theory of the money multiplier, which assumes credit to be issued on the basis of initial deposits or reserves, and the Credit Creation Theory of Money (CCTM), which assumes credit extension to create deposits rather than oppositely. Additionally, the interlink between savings and investment in an economy as a whole will be discussed. Issues of credit allocation and its effect on the economy will be raised, with the purpose of discussing redistributional versus predistributional effects. Lastly, issues of currency exchange through the banking systems, and the connectedness between currencies or lack thereof will be raised, primarily from a theoretical perspective.

5.2.1 Multiplying money

It is commonly held that credit extension creates money in some way. However, it is disputed and discussed within the academic and professional field in what way exactly. What is taught in most economic textbooks is the money multiplier model, which asserts that banks collectively create money through multiplying up initial reserves provided by the central banks. According to this theory an individual bank is dependent on initial deposits, from which it can lend out a multiple.
When discussing with my interviewees how money is created through bank lending, often I did not get a very clear picture of how exactly they considered this to work. However, one interviewee in particular was very clear about their support of the money multiplier theory and opposed openly the idea that banks should be able to create money or credit without initial deposits. We were discussing the M-Pesa (a mobile payment system run by Vodafone and Safaricom, widespread in several African and other countries), and I asked whether it was only a payment system for transferring of money (like Vipps in Norway), or if money where created through or by M-Pesa as well. They replied: “Well, it can be both, but M-Pesa is basically just a payment system. While, for example… one could accept deposits – M-Pesa deposits – and then lend out money that way as well. That’s how banks do here, I mean.” (Int. 6). When I suggested that in a regular big Norwegian bank (DNB), the money you borrow is not someone else’s actual deposit, they interrupted:

Yes! Yes it is! Yes it is. But I mean, yes, it is so. I mean, it’s legislation, it’s the financial regulators in Norway which have decided that: Do you [the bank] have for example one million kroner, then you can lend out 10 million kroner, because our calculations say it's fine. Right. So they can then give 5 million to companies and 1 million to credit cards, et cetera, right. So there’s a… they’re dependent on getting deposits in some way or another.

(Int. 6)

This interviewee held that banks create money when lending, though insisted that they can do that only on the basis of deposits, and thus, that the amount of credit created is a ratio to the amount deposited in the bank. When presented the sheet containing the three different theories of money creation, they also stated that the money multiplier model was the mainstream. Initially they agreed with the credit creation model as well, but eventually resisted:

No, but, new credit card companies are regulated too. For example, Bank Norwegian started with consumption credits. And then that’s… some of the theory here is that… You can ignore the regulation that existed. Because it [the credit] originated from nothing, right. But in my opinion, it’s still kind of the old model, where, actually, I mean, they’re having capital requirements, because they need to be sure that the money they lend are actually repaid. So therefore, there are some requirements that the Financial Supervisory Authority has established. That presumably they’ll lose 10
percent of the money, right, so that they’ll have to have at least 20 percent in reserve, and that sort of thing.

(Int. 6)

The only other clear response I got from the interviewees to the sheet of models of money creation, was agreement that the money multiplier model is the mainstream, which was often stated. Another interviewee said: “Much of the thought within economic theory and economic practices and politics is based more on the thinking up here”, pointing at the money multiplier model (Int. 3).

### 5.2.2 Money and credit

The Credit Creation Theory of Money (CCTM), in disagreement with the money multiplier theory, however, asserts that credit is created without the need to check the vault at all. Credit extension creates deposits, rather than derives from them. For long, this view existed in the fringes, and has been picked up again after the financial crisis in 2008. The Bank of England published an article on the issue in 2014 called *Money creation in the modern economy*, and a working paper in 2016 called *Banks are not intermediaries of loanable funds - facts, theory and evidence* emphasizing clearly that banks are in fact not intermediaries, and that the money multiplier model is outdated (McLeay, Radia, and Thomas 2014; Jakab and Kumhof 2015). CCTM theorists emphasize the difference between capital requirements, liquidity requirements and reserve requirements. While a large number of countries have no – or no practically effective – reserve requirements, they do have capital and liquidity requirements. Deposits in itself, though, cannot serve to fulfill the capital requirements, since they by definition are a liability for the bank. Deposits can nonetheless add to the liquidity of the bank if they are transferred from another bank, since, in this way the receiving bank acquire additional central bank reserves as well (Jackson and Dyson 2012, 74). Some theorists have pointed out that liquidity is not often an issue, since the role of the central bank is often to ensure that the payment system runs smoothly, and thus the central
bank will provide liquidity to banks more or less on request (Ryan-Collins et al. 2012, 21).

None of my interviewees and nowhere in the written material from Norad are banks described to be creating money when issuing loans. I brought up CCTM in some interviews, with either little response or some skepticism. Only one interviewee agreed, when I brought up whether there was a difference in of the amount of money created as bank credit in western economies versus developing economies:

Yeah that’s a very good question. That’s a good question. It’s probably in varying degrees. In rural areas it’s… Most places in the world, there will be little access to private capital, or credit. While in city centers, for example Kampala or Kigali or… there it’ll be the same mechanism: that the biggest part of the money in circulation is credit.

(Int. 7)

This quote is the closest any of the interviewees came to state money to be credit. On the other hand, neither did anyone disagree openly to the idea of money being credit. I usually brought it up in connection with the sheet I brought with the three different theories of money creation. Most responded to the credit creation model by almost not responding, but rather nodding and saying “hmm” or “mmh”, when I mentioned the theory. Some replied that they didn’t know much about the matter of money creation at all. I will return to this issue in the third part of the analysis, chapter 5.3.

If money is created as credit without a basis of initial deposits, one could speculate if developing countries could invest more simply by expanding the credit extension allowance for local banks, rather than having to wait for them to acquire enough deposits or borrowing from banks abroad. I asked an interviewee this question, and they replied:

To create money in the private market through especially local banks, that’s fully possible. But the challenge is that it depends on a certain savings rate to do that. And the savings rate is very low in Africa or Asia or wherever… very low-income countries. And that makes it difficult for banks to take high risk, to just create that money, because it will impact negatively the banks’ capital.

(Int. 7)
The interviewee mentioned in the previous section, arguing for the money multiplier, asserted that initial deposits were important because the banks needed capital in reserve. This latter interviewee argues that savings are important for the capital in the bank. Thus, while using slightly different terms (capital or capital reserve, and whether deposits or savings), they agree that banks are dependent on some sort of security to not go bankrupt if too many loans are not repaid.

### 5.2.3 Savings and investments

Although the role of deposits is disputed with regard to credit extension and thus investment, certainly someone’s money *can* be invested. People or firms can invest their money directly or via financial institutions such as investment funds, pension funds or others, including banks. This process is primarily not, or not necessarily, money-creating. This, neoclassical economics and the Credit Creation Theory of Money (CCTM) agrees upon. The investment of savings is a redistributive mechanism, where already existing money is moved from one economic agent to another, from one part of the economy to another. In that way, savings can be an important factor for the level of investments in a society.

Savings are also seen as an important factor for investment in another more theoretically specific way, namely in the sense employed by neoclassical economics in the context of the National Income Accounting Identity. It defines savings as equal to investments, in the way that savings is defined as that part of the income which is not spent on consumption – thus invested. Less money spent on consumption and more money invested will lead to higher incomes in the future. Thus, *saving* in this sense does not necessarily mean someone’s money in a deposit or a savings account. Neither does it mean that those exact money are re-lent from that savings account. It does mean, however, that in an economy as a whole, if less is spent on consumption, a higher proportion will – all else being equal – be investments (Mankiw 2009, 61). One interviewee was particularly concerned with the levels of savings in developing economies:

> It’s important with national saving, private as well as public saving. Because… Public savings takes the form of real investment. Practically
speaking that’ll be infrastructure. And the government budget surplus – that is, the deficit – that’s the sum of public savings. So financial savings plus real investments. So that plays an important role! That’s important!

(Int. 2)

They assert that government investment is especially important because it is more likely to be “real” investment, that is, investment in infrastructure, agriculture and industry, a point which I will return to in the last section of this chapter. Another point is, that private as well as public savings can be a cheap source of investment. Therefore, higher levels of savings in an economy are assumed to lead to cheaper, and consequently more (real) investment, they explain:

It’s a big problem that the savings rate in Africa is very low. And that’s the reason these countries now have to borrow from the international credit markets to 6, 7, 8 or 9 percent in interest rates. The country that has the highest public debt to GDP ratio in the world is Japan. Their debt to GDP ratio is around 250 percent. But they pay almost no interest. Because the savings rate in Japan is 30 percent.

(Int. 2)

National (citizen’s) savings, thus, make it cheaper for the nation to borrow. According to neoclassical economics, and emphasized by this interviewee in particular, this is due to supply and demand mechanisms in the credit markets. If more funds are available for investment, interest rates on loans will decrease.

It is also so, that countries which manage to get high savings rates, have higher growth rates on average. Because it’s a cheap source of financing investment projects. Because when you have high access to private savings, then the equilibrium in the credit markets makes it cheaper to borrow. So you’ll get cheaper financing.

(Int. 2)

Emphasis on supply and demand, and the expectation of natural equilibriums in the market – here the credit market – are at the core of neoclassical economic theory.

In neoclassical economics, while the amount of savings is equal to investment by definition, it is generally implied that the causality runs from savings to investments. Thus, increasing savings rates become a strategy towards increasing investment. However, the direction of the causality has been contested from other economic
perspectives, and already by John Maynard Keynes in 1936. He argued that, similar to the fact that credit creates deposits, investment also create savings. Because when investing more (without the need of saving up deposits in advance) by definition savings increase (Keynes 1936, 36f, 105f).

Another interviewee mentioned savings as an important development strategy as well. They held that borrowing money could be beneficial as long as the conditions where good.

But, one of the problems is savings. Usually we are very focused on the taxation part, the income part, but to build a robust economy that can service loans and investments, also investments for the SDG’s, they’ll have to strengthen local saving. Not savings in Switzerland, not savings in Cayman Islands, but national saving.

(Int. 8)

Whether savings lead to higher and/or cheaper investment or it is the other way around, one could argue that the savings rate is important, since, when one borrows money, one still have to be able to service repayments with interest. Thus, if one doesn’t save before being able to spend later, but rather takes a loan to spend money now, one still have to “save” later in the form of the interests – thus “saving” defined as the part of the income that is not spent on consumption.

5.2.4 Credit allocation

The lending decisions by banks have distributional effects, since they affect where large sums of money are allocated. Several interviewees agreed on this when asked specifically about it:

Yes, yes absolutely! Definitely. So that’s… I mean that’s definitely true. There is much power in financial institutions which distribute between various companies or persons and say like: ‘you can borrow this much’ or ‘you can’t take out a loan’.

(Int. 6)
None of the interviewees mentioned this distributional power themselves, however, and neither does the Skatt for Utvikling written materiel. It is alluded to in the Sustainable Development Report 2019 though:

… regulations create incentives in the financial system, including for lending and investments that advance, or hamper, achievement of environmental and social goals. […] the modalities of financial sector development, which are strongly influenced by the regulatory framework, have important implications on inequality.

(United Nations 2019)

After this, the chapter in the report goes on to discuss risks on the financial sector of inequality and the environment – the opposite issue. One interviewee described some more specific distributional effects of banks’ lending decisions:

And obviously it makes a difference where the credit goes afterwards. How much goes to households, how much goes to companies. That has very different impacts on the economy. Households, that results in more net import. And slightly lower growth than if the credit goes to companies. […] This is a very central point, really, in a way. If you take a look at these east-Asian countries, they had very strict credit rationing. They forced people to save. It was difficult to obtain loans for housing and consumption. And they gave cheap credit to infrastructure, agriculture, and industry, especially export industry. All these countries did that. And Norway too in the ‘50s, ‘60s and ‘70s in a way. So, that increases the savings rate. Increases national savings and investment, and allocates the savings in the direction of infrastructure, agriculture and industry.

(Int. 2)

Another interviewee also pointed to state versus market effects when discussing the distributional effects of bank lending in the economy and how to make sure the result of that distribution is desirable:

How they [east-Asia] managed to reach such high levels of savings and investment rates, was that they ran a very shielded politic. They didn’t liberalize the finance, credit and banking sectors. They’ve had strong state management. And have also had strong national banks and development banks, which have had a strong management as well with respect to savings, how that was managed, and how the funds where channeled with respect to
investments. From an overarching strategic thinking on sectors and capital investments. (Int. 3)

This interviewee had the opinion that, while the World Bank and the IMF often promote financial liberalization as the path to development, this strategy mostly has not worked well. Often, they claimed, liberalization policies result in oligopoly-like situations with ill-developed credit markets where lending mostly goes to consumer credit and consumption. The interviewee held the idea that credit for consumption was bad, while real investment is good, since another undesirable consequence of liberalized finance, they claimed, is that:

Much of the capital – this is what I typically saw in Zambia and Tanzania – is being used to buy up government bonds or treasury bills. Which aren’t real investing… aren’t investments in the real economy either, right. It’s just kind of financial investments, which in a way just go in circles without creating a foundation for long-term value creation.

(Int. 3)

So two interviewees asserted that state investment tends to go to real investments, whereas a liberalized financial market tends to result in consumption credits or financial speculation. They perceived these practices to have an important impact on economic development and growth. One interviewee mentioned that their preference for state investment over liberalized finance was out of fashion and in opposition to policies promoted by the IMF and the World Bank. Since most developing economies now have liberalized financial sectors, this interviewee suggested state regulation of the private sector as a solution. Another interviewee agreed:

Yes, but it is regulated, right. Maybe not in developing countries… I mean, in South Africa they’ve had cheaper loans for young people and subsidized loans for start-ups. So they do have… there is some subsidizing and regulation. But it’s little! We [in Norway] have a lot of that.

(Int. 7)

This person continued, as the only one of my interviewees, pointing to some structural incentive mechanisms aside from regulatory ones:

But it’s really interesting, especially, this thing about who gets to borrow, and why. But that’s… I also think that’s important, I mean, in the countryside in Norway, hehe, often there you’ll get a loan, not just based on
your personal financial situation, but also on the basis of your parents’ finances, and if you know someone in the bank, and, etc. That’s like almost a corrupt system. And that exists in Oslo as well, because lots of people who come from outside Oslo get credit from other banks, because they’re known as good payers. And I think that’s the same in small credit markets in developing countries.

(Int. 7)

Additionally, they referred to the Financing for Sustainable Development Report 2019 (United Nations 2019), which says that concentration of market power is one of the biggest threats to development in poor countries: “That should really include the banking sector too”, the interviewee concluded (Int. 7). On that account, both interviewees disagreed with neoclassical economic theory according to which liberalization will let the market find the optimal lending decisions due to supply and demand equilibriums and natural price mechanisms. In line with neoclassical economics, the distributional effects of lending are seen as re-distributional. Even though it is accepted (albeit not promoted) that bank lending is money creating, banks are essentially seen to be intermediaries – maybe especially so in relation to the redistributing role they have in the economy, as channeling money from people or sectors with financial surpluses to people or sectors with financial needs. The above cited interviewee emphasizes where in the economy credit is extended to, but utters not a word about where the funds are mediated from, implicitly assuming them to originate from other sectors’ surplus money, i.e. savings.

Contrary to the view of neoclassical economics, CCTM economist Joseph Huber argues that because credit extension creates money, allocation of that new money is pre-distributional, rather than re-distributional (Huber and Robertson 2000, 65). Richard Werner argues along the same lines of the above-cited interviewee that one of the most important questions for economic development is what credit is provided for, and that policy should be put in place to make sure credit is issued to investments in the real economy. He also points out the same East Asian economies as prime examples of the effectiveness of this type of policy, namely:

[…] imposing regulations on banks concerning the quantity and allocation of bank credit. Known as ‘credit guidance’ or ‘window guidance’, such policies have also been at the heart of the high growth in the successful East Asian economies such as Japan, Korea, Taiwan and China. Using such
guidance, bank credit for non-GDP (i.e. asset) transactions could be suppressed, so that asset bubbles and subsequent banking crises were avoided. When instead bank credit was guided towards productive use, high, stable and non-inflationary economic growth could be achieved. […] The highly successful economies of Japan, Taiwan, Korea and China all used mechanisms to guide domestic bank credit to productive use.

(Werner 2016, 375-376)

Instead of targeting private savings rates, Werner argues that the most effective policy is credit guidance. Since money is created directly when private banks extend credit, the most effective way to govern the credit markets is not to first transfer the funds to the state via taxing or other means of increasing savings and subsequently transfer the investment decisions to the state. Instead, he argues, regulate private bank credit extension directly.

In the era when the credit creation theory of banking was dominant, its proponents pointed out that bank credit creation and growth in economic activity are connected, and credit for different types of transactions has a diverging effect on the economy. They have thus favoured bank regulation that directly targets bank credit, both its quantity and its quality (i.e. the type of transaction that gets funded by bank credit), whereby economically desirable bank credit is encouraged, and economically harmful credit creation is forbidden or restricted quantitatively.[…] Before the use of reserve requirements, capital adequacy or interest rate targeting became dominant in the second half of the 20th century, central banks focused more on controlling bank credit directly.

(Werner 2016, 377).

This approach targets pre-distribution of new money, instead of subsequently addressing re-distribution of already existing money, which is what taxation and investment of existing funds do.

5.2.5 More than one circuit

While the rationale of domestic resource mobilization is for the country to be less dependent on foreign capital, the interviewees generally held views along the lines of: “Certainly, to have foreign debt is completely okay, as long as the money is used
sensibly.” (Int. 2). An interviewee from Skatt for Utvikling said that increasing taxes would “never be enough to fully finance the SDGs”, and that other measures must be taken as well, including loans and investments from the private sector: “To borrow money is not a bad thing in itself. It’s just the conditions for the loan and such.” (Int. 8).

All interviewees held that borrowing money from abroad is not necessarily a bad thing if used responsibly, e.g. for real investment. Economist Richard Werner argues from the point of the Credit Creation Theory of Money (CCTM), or more specifically the Quantity Theory of Credit challenging this view. He points out the empirical fact that foreign loans in foreign currency cannot enter the national monetary circuit:

If and when such foreign currencies are exchanged by developing countries into domestic currency, they will merely result in an increase in credit creation by the domestic banking system, denominated in domestic currency. However, this is something any developing country can arrange for without the need to borrow from abroad at all. (Werner 2016, 375).

Systemic theories of money and banking generally treat different currencies as separate circuits, or “systems”, rather than just different denominations of measurement. When looking at currencies as different circuits, foreign exchange starts to look more central to international finance. Because money is created as credit, it will be created in the domestic banking system, not depending on deposits – whether in domestic or foreign currency. Foreign loans do not add money to the economy in a way that could not have been done without that foreign loan. Werner holds that, economic models following the “[...] financial intermediation theory of banking, argue that savings are necessary for investment and hence economic growth. These theories have supported the IMF and WB policies that developing countries should “obtain the allegedly ‘necessary’ savings for investment and economic growth from foreign lenders, and to substitute for their lacking ‘domestic savings’.” (Werner 2016, 375) Instead, he argues, borrowed money from abroad does not enter into the monetary system in the domestic economy.

In many, if not most cases, the countries would have been better off by not borrowing from abroad at all. The foreign money never entered their economies: the accounting reality of international banking shows that US dollars stay in the US banking system, and euros stay in the European banking system. Bank money stays within the respective banking system of the currency of denomination. […] In other words, the dollars that created
the ‘Third World Debt’ problem never even entered the borrowing countries.

(Werner 2016, 375)

However, not all foreign money has to be exchanged into national currency to be of use, since a country usually imports some amount of goods. Foreign currency can therefore be spent in foreign countries without the need for exchanging them into domestic currency. Indeed, a rather significant portion of foreign aid and foreign lending to developing countries is spent on imports, since dependency on imports is a typical problem for developing economies.

Some interviewees emphasized that foreign debt is a much greater problem than domestic debt.

The most important is probably foreign debt, that is, debt to foreign countries. [...] Because when you have debt in foreign currency, you have to go through the central bank, and you have to obtain this foreign currency somehow, whether it’s state or private debt.

(Int. 2)

Another interviewee said: “The difference is, though, that very much of the credit is debt to international banks, which presumably take out interest margins.” (Int. 7).

Because the foreign loans must be repaid in foreign currency, you have to obtain foreign currency through other means to repay the loan. And loans carry interest rates, which are also to be paid in foreign currency. So, to service the loan you need to obtain more foreign currency than the amount of the initial loan. To pay back more than you borrowed means that in total, money is flowing out of the borrowing country, and into the lender country.

On this matter, while they diverge on the matter of necessary savings, these two interviewees align with CCTM economist Werner in that foreign loans transfer money out of the domestic economy:

The large and rising amounts of payments to service their foreign debt may explain what otherwise is a puzzle in economic theory, namely why international financial flows seem to be directed from poor countries to rich countries [...]. As a result, a transfer of net resources from the less well-off
countries to the rich countries has been taking place, putting the former ever more at the mercy of the latter.

(Werner 2016, 375)

The interviewee who was most clear in their view that large amounts of money are created though bank lending, mentioned precisely this issue as well, however briefly:

But if it’s by international banks, which draw out interest margins in form of exporting money, then that’s, then it’s not *creating* money, then it’s *reducing* the amount of money in the economy.

(Int. 7)

Both investment and consumption locally is commonly seen to strengthen the local economy. This was probably the point implied by some interviewees: that borrowing is fine as long as the money is used sensibly. If invested locally it promotes the domestic economy, while it does not if spent on consumption goods from abroad.

The other side of the coin is the immense difference it makes where you are borrowing *from*. When borrowing from a bank within the country, the loan repayment and the interest rates stay within that country’s economy. The bank will pay salaries to employees within the country, it will pay rent within the country, as well as hopefully pay taxes within the country. Obtaining a loan domestically thus keeps the money flow within that country’s economy. Conversely, when borrowing from a foreign bank the loan repayment as well as the interest payment flow out of the domestic economy. Additionally, salaries, rent and taxes that the foreign bank pays from the profit made off the loan is often also paid outside the borrowing country. To conclude, foreign debt extracts money from an economy in numerous ways, some of which where only mentioned briefly and by few interviewees, while more strongly emphasized by CCTM.

5.2.6 Taxes, savings and real investment

With this in mind, one may wonder why developing countries are still advised to borrow from abroad, and whether they have alternatives. The answer may lie with savings. The risk of lending is often bigger in developing countries, since borrowers are
poor and the economy is unstable, a higher proportion of loans are not repaid. That means banks must demand higher interest rates in order to turn a profit. As discussed in section 5.2.3 on ‘Savings and investments’, neoclassical economics holds that savings can counter the need for high interest rates, and thus make domestic lending cheaper. An interviewee explained about the well-functioning Japanese economy that the government

… borrows almost for free in the domestic market. […] They issue government bonds in Japanese homes. And there, the nominal interest rate is near zero, and then maybe they have some inflation, so the real interest rate ends up at 0.5 or 1 percent or something like that, on the Japanese government loans that Japanese households buys. Exactly how this happens can be discussed, but the reality is that domestic savings are so high that the government borrows at near zero interest rate.

(Int. 2)

Thus, in countries with low domestic savings and small banks with high risk, borrowing domestically is expensive. International loans, often from large international banks, carry lower risk and are therefore cheaper. For a poor developing country foreign borrowing will seem cheaper and more appealing in the short term: Therefore, the above-mentioned advocacy for increasing domestic savings. According to neoclassical economic theory, domestic savings will make it cheaper to borrow at home and less tempting to borrow abroad.

Following the neoclassical understanding of savings as equal to real investments, the act of moving purchasing power away from consumers to the state is seen to shift the proportion of money spent on consumption in the economy, towards more money invested in the real economy. Thus, according to the National Income Accounting Identity definition, taxes are savings, which equals investment.

And taxes, then, increase domestic savings.[…] If you think about it in terms of the real economy, then it’s clear that taxes draw in purchasing power, and that then allows for increased public spending in the real economy. I mean, it allows for the public sector to use more of the resources in that society. That’s how most economists think about this. Then of course, you have all the other aspects of taxation, but.

(Int. 2)
This assumption, however, applies only if the government invests in the real economy.

The special problem in sub-Saharan Africa is that they have such unbelievably low savings rates. Private savings. For different reasons. Of course because people are poor, live in the countryside, have big families, and in a way “save” in the form of their children. And the banking system isn’t well developed. But also because, in Africa, you’ve performed credit liberalization. So you don’t have that… I mean, it’s easier to get a loan – if you can pay! […] If you think about the old days in Norway, or East Asia, you had credit rationing. So that people were forced to save. But in a way, in many African countries you’ve had credit liberalization. Before that, credit mostly went to domestic industry and with very high tariffs. Then, in connection with the aid Africa received in the ‘80s and ‘90s, credit markets where liberalized. That was one of the conditionalities of the debt cancelations, to put it like that. […] And liberalization often reduces the savings rate in a country.

(Int. 2)

While one interviewee holds – in line with neoclassical economics – that taxation increases savings by definition, another interviewee argues, rather, that increased private sector savings is a means to achieve better conditions for loans from the private sector and will promote an economy which overall is equipped to service private sector loans and investments. However, this person also states that increasing savings is not a strategy currently integrated in Norad’s taxation-related work.

We have talked a bit about it here in Norad, how we can integrate this more. But yea… So far it’s not something we have included in our work within Skatt for Utvikling.

(Int. 8)

Neoclassical economics and systemic monetary theories are in agreement that investment in the real economy is crucial to economic development. Both perspectives also agree that high proportions of consumption credit can be harmful to the economy. However, the means to handle this issue are rather different, partly related to their contrasting views on money creation. Neoclassical economic theory does not integrate money creation, and therefore focuses mainly on re-distribution of existing funds. The Credit Creation Theory of Money (CCTM), on the other hand, integrates the aspect of the economy in which new money is created and concurrently enters the economy through the lending decision of banks; this theory covers pre-distribution of money.
The fact that banks create credit and money out of nothing which, if used productively, results in non-inflationary growth, is important for developing countries. Often it will not make sense to borrow from abroad in order to stimulate domestic growth: the foreign money does not enter the economy, and the country gets ensnared in spiraling foreign currency debt, when actually the foreign banks just created the money out of nothing, something the developing country could have arranged for through its own domestic banks. It also has implications for the question of who should pay for bank bailouts, shifting the pendulum from burdening tax-payers towards central bankers.

(Werner 2016, 377)

Ensuring that new money is used for real investments will increase savings, given the National Income Accounting Identity definition. This in turn should lower interest rates, making future credit cheaper. While that would be a better long-term strategy following CCTM, it remains a question from this discussion, whether it is possible in practice for poor developing countries to rely on domestic borrowing at high interest rates and avoid foreign, without causing too much disadvantage for its population in the short term.

5.3 Conceiving of money creation

In the two previous chapters, I have discussed how, according to neoclassical economics, the state can only spend money it has collected first through taxes, and banks can essentially only lend out money on the basis of money collected first through savings. Both institutions seem to be just moving existing money from one part of the economy to another. From these conceptions, the question of where money comes from in the first place remains.

This is not a question asked by Financing for Development, neither have I heard anyone in the field raise the question, and it proved incredibly complicated for me to raise the question in the interviews. These observations align with the fact that the interviewees’ perspectives mainly agree with neoclassical economics which does not raise the question itself and seldom engages with it. Conversely, systemic monetary theories to a high degree engage with this issue and its implications. So perhaps the Financing for Development field could benefit from engaging with systemic monetary theories in order to clarify where money comes from – and thereby consider that there may be more options available to finance development.
What I think is difficult here, is that I am not really sure what… But, I mean, that’s sort of an empirical finding, not just an issue. It is that, I am not really sure what you mean, when you’re talking about ‘money’. And you’ll probably encounter this when talking to others as well.

(Int. 1)

5.3.1 Grasping money creation

Hard to get to talk about

“Well, the money has to come from somewhere!” This exclamation was said by one of my interviewees when I asked about their opinion on the State Theory of Money (STM): that money has to be created by the state in the first place, before it can be returned as taxes. The interviewee replied this, that the money has to come from somewhere, rather sceptically and with emphasis on somewhere, then continued: “it’s not like the state, I mean, a state can’t provide any services, if it doesn’t have any income, right.” (Int. 6). In all the interviews, it was a struggle to get to talk about creation of new money. It seems easier to talk about money in a way that resembles the microeconomic experience of oneself: I can not spend any money if I do not have an income. It is much easier and more common to talk about moving already existing money from one place to another. That is, to talk about transactions. Another interviewee was less resistant to the idea of money creation, but when they thought out loud, seeking to elaborate on when money creation occurs, it was obviously not straightforward and still reflected the more common conception of money as transactions. “Money is… it’s circulation in the economy.” (Int. 1). They suggested that money which lie dormant in certain types of investments could be activated, thus increasing the amount of circulating money, but ended up concluding, that “So, no, that’s not actually creating money” because even though more money circulates, it does not increase the amount of money which exist. When asked about STM and the state’s money creation, this person agreed that the state can spend money before collecting taxes, but still described this possibility as a possibility to borrow (already existing money). They said that the state can make use of deficit spending if the tax revenue is currently not large enough, but if the state then subsequently still does not collect
expected amounts in taxes, then it is left in debt. So, while STM argues that the state’s deficit is the amount of money available in the economy, this interviewee saw the deficits to necessarily be loans in the same way it would be for a company. Thus, state deficit spending was not money creating, but merely moving money that already exists from one place to another. That the act of spending should create money felt unfamiliar and seemed strange to relate to. I got similar reactions to the notion that bank lending should create new money and be able to inflate the economy into an economic bubble. This is the case not just to my interviewees and to most laypeople. The Nobel Prize-winning neoclassical economist Eugene Fama has said in an interview:

People who get credit have to get it from somewhere. Does a credit bubble mean that people save too much during that period? I don’t know what a credit bubble means.

(Cassidy 2010)

Fama here reflects the conventional view of banks as intermediaries: savings in, credit out, no creation of money, only moving of money that already exists. But according to systemic theories of money, money creation through bank lending is central to explaining economic bubbles, that are

disrupting the lives of millions of wage earners and homeowners. That way, money-creation-through-bank-lending is an insight that deserves to be widely appreciated, not only by economists and finance and banking professionals, but also by the general public.

(Ravn 2015, 93, my translation)

The science writer Ib Ravn points out that the fact that bank lending creates money “is often met with incredulity: “What do you mean, created?” (Ravn 2015, 92). Correspondingly, it is an unfamiliar fact that money is also deleted. According to the credit theory of money, just as money is created when credit is extended, money is deleted when the loan is repaid. In an example explained with a loan of 80.000 kr., which is then repaid, he writes:

That means the money supply is reduced by 80.000 kr. That money has disappeared, been demolished, destroyed. One seldom hears the term […]. Maybe shocking for the faint-hearted: The banking system destroys money!

(Ravn 2019, 25)
Both aspects: creation and deletion of money are unfamiliar concepts for most people. Generally, the concept of a monetary system is seldomly spoken of. “How can money constitute a system? It is not obvious for anyone.” (Ravn 2019, 34). In this book, Ravn mostly writes about conceptions by non-economists. But also neoclassical economics does not explicitly conceptualize the monetary system as a system – given that money is seen as a “veil” over essentially a barter economy, consisting of multiple transactions which are merely made more efficient with money. During one interview I suggested viewing the monetary system in a geographical way, attempting to point to its systemic features. The interviewee claimed to agree and said they had focused on the systemic features of money in their university studies, however at the same time they described this as a focus on barter. Our conversation continued for several minutes confusingly trying to agree what we meant by “system” in relation to the monetary system. While I related to the technical systemic features, they understood systemic as the culturally and socially organizing features. We lacked a common language to express what we meant by “system”. When I initially described the overall topic, this person’s response was a disarming “Haha, big questions.” (Int. 8). Like other interviewees, they saw the concept of money as something very abstract and unfamiliar. Later in the same interview, when talking more specifically about money creation, this interviewee related to political ideologies and said that when working with financial and tax policy, it will be a good idea to make sure that the involved parties agree ideologically: That they share an understanding of how the world works or should work. However, this person also believed discussion about the monetary system in this regard to be a very theoretical exercise and warned against getting stuck in such theoretical discussions, reflecting a view that other interviewees shared: That specifying the nature of the monetary system is sort of an abstract philosophical exercise which might be fun, but nevertheless unimportant for real world issues and mostly linked to other abstract issues, for example ideology.

The reason why money appears to be such an abstract matter is that it is so deeply embedded into our daily lives, argues Felix Martin, economist and former World Bank official. He refers to an old Chinese proverb that “The fish is the last to know water”, meaning we are so accustomed to and surrounded by money in all our lived experience that it is difficult to discern. He argues that while it is easier for the natural sciences to see its object of study from outside – to be a fish out of water, so to speak – all the
“‘social’ or ‘human’ sciences – anthropology, sociology, economics and so on” cannot just view their object of study from outside, since we are studying ourselves. “The closer an institution is to the heart of our daily lives, the trickier it is to step outside of it in order to analyse it – and the more controversial will be attempts to do so.” (Martin 2014, 21). The interviewees do not only have academic and professional knowledge of the monetary system, they also hold common popular knowledge and personal lived experience: They read the news, receive salaries, pay rent and other expenses. Professionals and academics are not fish any further out of water than any other persons with lived experience. Money is abstract among social scientists, economists included. Geoffrey Ingham points to the complicated study of money:

Only very little probing into these well-known observations reveals long-standing puzzles and paradoxes. Perhaps the greatest paradox is that such a commonplace as money should give rise to so much bewilderment, controversy and, it must be said, error. It is not well understood.

(Ingham 2004, 5)

Perhaps it is not surprising that the monetary system is not well understood, given that it is seldom talked about. I was struck by how difficult it proved to carry out interviews on the subject; to have a conversation about the monetary system. Money certainly seemed to be exactly like water is for fish; it has a place in life like air, it is just something that is there, it is taken for granted. In one interview, after initially attempting to explain the topic for some minutes without a response, I had to nervously ask whether it made any sense what I was talking about. The interviewee replied:

Hehe yea. But in a way, the fundamental question about what money is must be related to something, or some situation. And of course, we don’t sit down and think about ‘So, what is actually money’. Money is something we take for granted. And it is the same for our development partners. So, I don’t think it’s easy to link an understanding of money to the various issues here…

(Int. 4, emphasis added)

Another interviewee said the same, namely that money is not a theme which is thought about much in the development sector, rather it is something which is taken for granted (Int. 5, emphasis added). Ingham shares the impression that money is most often taken for granted in the social sciences, which he criticizes since money is such an important part of the workings of the economy.
It might seem to be unnecessary to draw attention to the fact that money is an essential component of the capitalist system. […] Somewhat paradoxically, however, money’s role in the development of capitalism is largely taken for granted in the social sciences. Economic development is seen to be triggered by other factors – the division of labour, technology, population growth, property rights and so on. There is a strong implication that money simply emerges in response to the functional needs of expanding economic activity. […] However, […] money does not appear spontaneously in this way; it is rather a fragile socially and politically constructed institution.”

(Ingham 2008, 65, emphasis added).

The fact that money is an institution – which is constructed and exists by virtue of its design – is especially not part of the taken-for-granted-ness of money. Other national and international institutions, laws and regulations are extensively discussed. Their suitability is regularly questioned in minor or major aspects. But, money and the functioning of the institution the monetary system is seldomly discussed. Money is taken for granted, which was explicitly stated by these interviewees.

Shortly after the Bank of England published their first paper on private bank money creation, Money Creation in the Modern Economy (McLeay, Radia, and Thomas 2014), David Graeber wrote in an opinion piece in the British newspaper The Guardian positing that “The Bank of England let the cat out of the bag.” (Graeber 2014). He argues that while the neoclassical view of money is wrong, it “allows us to continue to talk about money as if it were a limited resource like bauxite or petroleum, to say "there's just not enough money.” He suggests that some might believe it to be a socially stabilizing circumstance that most people do not understand the monetary system well:

Back in the 1930s, Henry Ford is supposed to have remarked that it was a good thing that most Americans didn't know how banking really works, because if they did, "there'd be a revolution before tomorrow morning". […]

Just consider what might happen if mortgage holders realised the money the bank lent them is not, really, the life savings of some thrifty pensioner, but something the bank just whisked into existence through its possession of a magic wand which we, the public, handed over to it.

(Graeber 2014)
The interviewees seemed not to be familiar with the money-creation part of banking, and they were not familiar with other explanations of money creation either. Because it was so hard to get to talk about money creation, I brought to the interviews a printed sheet of three different models of money creation as textbook-like illustrations. The three models where: the money multiplier of neoclassical economics, which is taught in bachelor-level economics textbooks; state creation of money, according to the State Theory of Money; and private bank creation of money through credit extension, according to the Credit Creation Theory of Money. When introduced to the models, the interviewees seemed to remain confused. When asked to reflect upon the models further into the interview, one interviewee recognized the money multiplier model but not the others, and concludingly responded that money creation was not their “strongest suit” (Int. 2). Even for the interviewees who, like this specific person, have a degree in economics and long experience in the development field, money creation is not a familiar concept. For the interviewees who where not economists, it was even less familiar.

What I have sought to show in this section is how difficult it proved to talk about money creation, and how unfamiliar and alien the concept seemed to my interviewees. The next section will relate this matter to: neoclassical economics, to its cultural significance and to its importance for the discourse in macroeconomics.

**Neoclassical orthodoxy**

Mainstream economics consists of mainly one theoretical perspective: neoclassical economics. On the contrary, heterodox economics is a whole range of different theoretical perspectives. While in most other social sciences, students are taught at least some different theories about their subject, in economics students are mostly taught neoclassical economics. The economist Kate Raworth writes:

A standard introductory course that originated in the United States – and is widely known as Econ 101 – is now taught throughout the world, with students from China to Chile learning from translations of the very same textbooks used in Chicago and Cambridge, Massachusetts. […] Even for those who never study economics, the language and mindset of Econ 101 so
pervades public debate that it shapes the way that we all think about the economy: what it is, how it works, and what it is for.

(Raworth 2017, 7)

Paul Samuelson’s textbook Economics was the first basis of the course which became so dominant. He writes:

[Even in the most advanced industrial economies, if we strip exchange down to its barest essentials and peel off the obscuring layer of money, we find that trade between individuals or nations largely boils down to barter.

(Samuelson 1973, 55; quoted in Ingham 2004, 15)

That money evolved from presumed barter-based economies as a tool to make these more efficient is a story told in most basic economic textbooks (Martin 2014, 10; see Graeber 2011, 22f for examples). And due to the preponderance of these textbooks around the world, the views reflected there become widespread.

In other words, the vision of the world that forms the basis of economic textbooks, which Adam Smith played so large a part in promulgating, has by now become so much a part of our common sense that we find it hard to imagine any other possible arrangement.

(Graeber 2011, 33)

Keith Hart comments: “It is remarkable how deeply inserted into the popular consciousness of Western societies is this idea that markets evolved from primitive barter.” (Hart 2001, 266).

The result is that economists and non-economists alike share the same ideas stemming from neoclassical economics. Another idea, which follows from the myth of barter, is that money is a ‘veil’ over the economy. Since money simply makes barter exchange more efficient, money is just sort of a reflection of the underlying “real economy”. Altogether, neoclassical economics does not perceive money to be of any particular importance (Martin 2014, 209; Ingham 2004, 7; Juselius 2019, 29). This view was often reflected by my interviewees. I asked an interviewee about the main difference between the monetary theories: whether money is seen as created by the state or by private banks, and they replied: “Yes exactly. Yes, that’s a discussion. It is so. But… the question is how important this is really.” (Int. 2). Referring to economics university
studies, they recalled “the discussion about the neutrality of money” (Int. 2) But said that “in Norway, this thing about monetary theory has never been prioritized much, because they’ve been very concerned with the real economy.” (Int. 2)

Money is seen to be neutral, not having much importance, especially not compared to the so-called real economy, which is what is important. When I asked one interviewee whether they thought the topic of the nature of the monetary system was relevant at all in relation to Skatt for Utvikling, they said after a long pause:

Yes, well, it’s relevant to the extent that – I think, personally – it influences how we work. But the theoretical discussion for the sake of theory itself, that we don’t have time for. […] I don’t think this [models of money creation] is really… Regarding my daily work, then this isn’t that important really. I think. For my position. For the work I do, its not particularly important which of these models is correct, as long as its working, right.

(Int. 6)

Most of the interviewees, economists included, did not think money and monetary theory was their particular field of expertise, and all interviewees without exceptions suggested me to ask elsewhere. One Norad economist referred to another Norad economist, who then referred me to Norges Bank (the Norwegian Central Bank), where they believed there would someone working with the issue of money creation. But concluded that they were not sure exactly who would have some certainty about it (Int. 2). I experienced a sentiment of that “the economists will know”, but among economists, this sentiment remained in the form of “other economists will know”.

Economists have increasingly, since the beginning of the discipline economics, been treated as the experts on many things related to society. Although the founding fathers of economics were in heavy dispute regarding economic paradigms, John Maynard Keynes and Friedrich von Hayek agreed that such high status is not fit for economics. Keynes said that: “The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else.” (Keynes 1936, 383; quoted in Raworth 2017, 8). Nobel Prize-winning Hayek did not approve of a Nobel prize in economics at all, since that much authority was not suitable for the field (Raworth 2017, 8). Economist Katarina Juselius writes about the elitism in economics from the perspective of personal experience. In one case she had written a critical research article together with Søren
Johanson about how the presumptions of a certain model did not prove true when investigated empirically. Even though they were some of the most cited economists at the time, they did not get the article published in the renowned journal *Econometrica*, with the explanation that they must had come to the wrong empirical results (Juselius 2019, 117). Economics is a highly elitist field that possesses high authority in political decision-making and the public debate and also maintains strong hierarchies within the discipline. This is the case in development economics as well, according to an interviewee. They told about their experiences as an expat country economist, that:

> Monetary policy was often up to the IMF, very much, you could say. They where kind of the experts on that matter. They came in, ran massive models and computations, and in a way said what was the smart thing to do and what wasn’t, kind of.

(Int. 3)

The interviewee explained that many of the development practitioners in the field was not economics experts, but generalists or specialists in other fields, such as health and agriculture. The IMF-team, on the other hand, was often highly educated economists. Therefore, the local development practitioners did not feel fit to enter into debates with the IMF-team, which “could run these massive models of theirs and give advice that everyone then pretty much took at face value” (Int. 3). They explained that especially when the developing country had just had foreign debt cancelled, or received large amounts or aid or foreign private investment, one would be even more careful to try to challenge the IMF.

> You shouldn’t rock the boat, so to speak. Or give the wrong impression regarding something that could jeopardize aid or reputation in relation to private investments. So the discussions where limited. And its also seldom that, I mean, I seldomly experienced in the ministry of finance or the central bank, or in the economic milieu on country level in developing countries, that you’re particularly openly in opposition to the IMF or the World Bank, or bring in a completely different theory. There are some instances where you sometimes could, especially if you’re a bigger or more powerful developing country for example. If you’re a small low-income country, with high foreign debt, are aid dependent, then typically you follow what’s orthodoxy. Rather that, than trying to protest and be like ‘Nah, we have another thinking regarding monetary theory or the role of money, regarding
competitiveness or structural changes in the economy’. (Int. 3)

In this case, it was the elite of the field which dictated what is right or wrong, because they were seen – by the rest of the profession – to be better equipped, simply to know better.

5.3.2 Money supply – What importance does the amount of money have?

In the previous section, I discussed how difficult it was to talk about money creation in my interviews. One reason for money creation to be an unusual subject, is the subconscious idea that there is a fixed amount of money. Another reason is the immediate risk of inflation which seemingly rationally will follow money creation. This notion is build on neoclassical economic theory, following Milton Friedman in that “inflation is always and everywhere a monetary phenomenon”. (Friedman 2012, 181). Systemic monetary theories, however, challenge this notion. Empirically, money creation does not always lead to inflation. These theories argue that the inflationary effects of money creation depend on where the new money is spent in the economy, and that inflation to a higher degree is a political phenomenon.

When not having enough one must borrow

The question of whether there is a fixed amount of money or not, is a tricky one. In public discourse we often hear phrases like we as a society can’t afford this or that. One interviewee said that they knew they implicitly held the presumption that:

The world has a specific amount of money. And our job, us who are engaged in the field of development policy, is to move as much of that money as possible from the North to the South.

(Int. 1)

This is very much a layman perspective, and this interviewee was not an economist. Following this layman understanding, and integrated in neoclassical economics, is the
notion that if one is in immediate need of more money than one already possesses, one must borrow it. This notion is rooted in lived experience, as people and firms cannot create money themselves; however, this notion is very often transferred to the whole of society as well. We often hear about government debt and how the state has to borrow money for this or that. The underlying assumption is that there is a fixed amount of money and that money is a scarce resource; the option of creating more of it is rarely mentioned. This was also true in my interviews. When asked about their opinion on money creation versus taxation versus borrowing, one interviewee replied that taxation has a good potential, but since it “will never be enough”, borrowing will be a necessary supplement, to ensure enough money for financing development (Int. 8). They did not respond to the aspect of creation of money. The same interviewee later referred to an opening speech at a Financing for Development Forum in 2019 where responsible borrowing was emphasized. The interviewee, too, emphasized that the important thing is that the loans are responsible. They said:

Even Somalia can borrow money in a responsible way if the conditions for the loans are clear. [...] Because you know, you think: Ok, its important to get the economy going, and we don’t have enough money to do it ourselves. (Int. 8)

The rationale is: if you do not have enough of the limited amount of money, you will have to borrow. In the same way, while the State Theory of Money considers deficit spending by the government to be creating money in the economy, it is more common to consider deficit spending to be the government taking up loans.

Well I guess you could print more money or run a government deficit. But it’s kind of the same as countries which take on high levels of debt. You want to spend money that you don’t have. (Int. 5)

This interviewee also mentioned that Norway is sometimes criticized for encouraging developing countries to take out more loans and making developing countries dependent on foreign loans through strategies such as leveraging of IDA loans. The interviewee him/herself did not agree with this critique. Rather, they believed that Norway contributed to developing countries taking out more fair loans. “I think, if countries don’t get fair loans, then they’ll enter the capital markets instead, which will give them much more
expensive loans.” (Int. 5). They held that countries need to obtain money from outside the country due to a lack of money within the country itself. So, also macroeconomically, money is seen to be a scarce resource. Creating more money is not an option when a country lacks money. One reason this is that an increased money supply is widely perceived to result in damaging inflation.

**Money creation necessarily results in inflation**

When I insisted on talking about the option of creating more money, all interviewees rejected it on the same basis: That it will simply create inflation. That creating more money will result in inflation is also a presumption which follows from neoclassical economic theory (Mankiw 2016, 106). Additionally, this presumption is backed by popular perceptions. Zimbabwe and Venezuela are recent examples of hyperinflation, which are often mentioned, and references can be drawn to earlier classic cases:

Zimbabwe printed money in 2008-9, which created a situation like that in the interwar period in Germany, which in the case is classic. It was caused by a government that wouldn’t face economic realities at all.

(Int. 4)

The reference to the inflation caused by the government in the interwar period of Germany is indeed classic. While the inflation is a historical fact, there is disagreement over the reasons for it (see e.g. Schacht 1967). Generally, however, inflation is seen as tightly linked to the money supply. An interviewee remarked that especially in developing countries, there is a perceived danger regarding politicians who cannot help but issue too much money for personal gain, resulting in damaging inflation (Int. 7). The interviewees were, like neoclassical economics generally concerned about inflation. State creation of money instead of borrowing, was dismissed because it would lead to inflation, and additionally, monetary policy was generally seen to consist narrowly of dealing with issues of inflation (Int. 3; Int. 8). So developing countries cannot just create more money “without it having [bad] consequences” (Int. 4). But receiving aid money, earning money on exports, or borrowing money from abroad will also increase the amount of money within the country. I asked an interviewee if these activities also lead to inflation? Or what difference does it make that that money comes from outside the
country? They had not thought about it before and did not know what to say. This illustrates effectively that these are questions not commonly dealt with, even among people who deal with policy and strategies in the development sector.

Proponents of systemic theories of money argue that inflation is not just an effect of increased money supply:

The two basic monetary disorders of capitalism – inflation and deflation – are not simply economic phenomena. They can also have political causes and consequences, and both are very closely tied to the strength and viability of the state.

(Ingham 2011, 80)

Ingham writes that while inflation can have political consequences, very often “causation runs in the opposite direction. Severe political crises undermine confidence in the state and, consequently, its currency.” (Ingham 2011, 81) Thus, the order of causality does not go like this: too much money leads to inflation, which leads to political instability. Very often, he says, it goes like this: political instability leads to inflation. So to prevent inflation, the aim should not be to limit money creation by the state, but rather to strengthen the institutions and thus the stability of the state. One could say that Skatt for Utvikling will result in strengthened state institutions. But this is a secondary objective of the strategy. Perhaps the state could be strengthened more directly in order to become able to more appropriately control and thus make use of issuing of its own money.

Two of the interviewees, who were the most receptive to talk about money creation, shared the general resistance towards the possibility of creating new money because of the immediate risk of inflation. However, they did not dismiss it as impossible, and agreed that money is in fact being created continuously: that there is not a fixed amount. Both emphasized the importance of when new money is created. They stressed that new money must be created at the same time and pace as new value is created. Otherwise inflation will occur (Int. 7). “It’s related to value creation in the economy… To create money. Regarding what’s the underlying value creation then, or like, the basis for the creation of that new money, right. Regarding inflation and such.” (Int. 3).
Increasing the money supply does not necessarily lead to inflation

While most of my interviewees shared the perception that the creation of money entails the immediate risk of detrimental inflation, the systemic theories of money present a different perspective. While an increased money supply may lead to inflation, that is not always the case (Yue and Leung 2011). After the financial crisis in 2008, the European Central Bank created trillions of euros through its Quantitative Easing program. This did not lead to inflation in consumption goods in the EU, but it has lead to inflation in financial assets, e.g. the housing market (Demertzis and Wolff 2016). Empirically, it is the case for private banks’ credit as well that rises often lead to increased prices of housing and other financial assets and no or little inflation in consumption goods (Jackson and Dyson 2012, 16f).

Inflation in consumption goods is the conventional measure of inflation. This measure does not capture asset price inflation, which means that economists and lawmakers often overlook some of the inflationary consequences of some forms of money creation.

The inflationary effects of money creation highly depend on where the newly created money is used. In addition to the important distinction between consumption goods and services versus capital assets, the productive capacity of the country in question plays a role. The productive capacity is a characteristic of the country’s real economy: it denotes its ability to produce goods and services. If everybody works and all production equipment is in full use, the productive capacity is fully utilized. Conversely, if the country has unemployment, idle production plants and arable land lying fallow, its economy is not running at full capacity.

In principle there are four scenarios for the effect of money creation: A) The economy is not running at full capacity, and newly created money is spent on production; this will result in increased production of goods and services, thus an increase of Gross Domestic Product. B) The economy is running at full capacity, and newly created money is spent on goods and services; because real production cannot expand (in the short term), the extra money will lead to inflation in the real economy. C) If the newly created money is not spent in the real economy, but in financial markets; in principle the extra money may be used simply for increased activity in financial trading. In practice, what often happens is: D) Newly created money not spent in the real economy leads to asset price
inflation (Werner 2005).

According to the systemic theories, instead of avoiding money creation under any circumstances, the government should deliberately employ its power of pre-distribution. The government should be considerate of where newly created money will go in the economy and regulate to ensure that the new money will be directed according to the specific needs of the economy. The State Theory of Money emphasizes that the limitation to state spending, i.e. money creation, should be the productive capacity of the economy, in accordance with scenario A above. CCTM calls specifically for more carefully considering and regulating the distribution of private bank lending, i.e. very deliberately seeking to avoid scenarios C and D by installing regulation aiming towards A.

5.3.3 What is money?

Money’s correlation with value is a whole topic by itself. Here I want to briefly outline how, also in my interviews, it relates closely to the way money is conceptualized in daily language.

Materiality

Money is often illustrated as coins and notes, - physical money. Physical money seems easier to think and talk about than other types of money such as debt accounts and electronic money. Of all the features of money one could mention, its physical representation is often discussed. “Traditional money history focuses excessively on anecdotes about Caesar’s gold coins, coin cutting, money transports in horse-drawn carriages, counterfeiting, and fanciful notes, - that is physical cash.” Ib Ravn writes, not “the account money which completely dominates the picture today.” (Ravn 2019, 74). Ingham points out that regular money users often have more extensive lived experience with physical cash, while the proportion of the money supply which is physical cash is decreasing. While physical cash in 2004 was used in 85 percent of the number of all monetary transactions, this only amounted to 1 percent of the value of transactions.

In other words, actual media of exchange are now a relatively insignificant element of most monetary systems; but consciousness of money is still
formed to a significant extent by the small-scale transactions.

(Ingham 2004, 5)

In the same way, it appeared natural in the interview situations to talk about cash and to associate to physical printing of money when talking about creation of money. “Yes, for example, in some places you can print a loan, I mean, and you’re allowed to issue notes”, one interviewee started. Do you mean physical cash, I asked?

Yes. Yes, some places they can do that too. I think in Hong Kong, they had that system. At least before. I mean I don’t know that system exactly, but I’m pretty sure there it was a permission by the authorities to print a certain amount of money. So they were the ones that issued the physical money, and then it said on the note which bank had issued it.

(Int. 6)

Nowadays, however, in most economies only a few per cent of the money supply is physical cash (Ryan-Collins et al. 2012, 6). The vast majority is electronic account-money created by banks. But the physical money-printing by banks was a more immediate association for this interviewee.

“The transformation of money by electronic communications begins with plastic credit and debit cards. […] Ever since then [the post-war period], the banks have led the way in mechanizing money, encouraging their customers to write fewer checks, for example, by paying for utilities through monthly direct debits. […] Banknotes remain a staple of everyday life for all but the very rich. But one consequence of all the above is that electronic media have been substantially replacing paper money.”

(Hart 2001, 272-273)

Another interviewee said multiple times “cash, or, that is, money” as if those two words meant the same in their understanding. They explained that they try to give most aid money in electronic form and equaled that with being part of a “modern economy”. Even though for example Kenya was ahead of Western countries with their mobile payment service M-Pesa, aid recipients in poor countries often do not have bank accounts. The interviewee emphasized this obstacle as the reason that ‘cash’ often has be actual physical cash. The distinction between physical and electronic money was to them related only to the means of delivering the money. They said they had not thought about that the two forms of money were issued by different institutions. To them it was
only a practical question of payment method, in that electronic payment is part of a modern economy and is more secure and convenient for the recipient than “being handed a paper bag of physical cash” (Int. 5). Again, this is a conceptualization borne by lived experience.

In the same way, the interviewee recognized how they themself used the word ‘resources’ and ‘money’ almost interchangeably (Int. 5). However, another interviewee remarked “I’ve read a bit about the monetary system and such, so I do know that large parts of what we call money, doesn’t necessarily have any equivalents in real value” (Int. 1). It can be argued, that in some periods in time, money has had equivalents in physical values, for example during the ‘gold standard’ where the value of money was “backed” by actual physical gold. But the gold standard officially ended worldwide in 1976 (Ryan-Collins et al. 2012, 45-47). While money has been taking physical forms, and sometimes even being backed by or itself being different sorts of real value, research shows that money did not originate as such. “All evidence points to the historical origin of money as a means of calculating obligations and debts in pre-market tribal and clan society.” (Ingham 2004, 105-106). Graeber notes, that “Conceptually, the idea that a piece of gold is really just an IOU is always rather difficult to wrap one's head around” (Graeber 2011, 46), and that coins “still sit in our heads as the quintessential form of money.” (Graeber 2011, 75).

**Origin stories**

The connection between money and real value was also evident when one of my interviewees discarded the State Theory of Money (STM) on the grounds that rulers had always needed revenue. They asserted that before democratic states emerged

… the king went and collected revenue from noblemen who then collected the income from farmers beneath them, and farmers collected from peasants beneath them again, right. So, taxation came first, and then democracy came later on.

(Int. 6)

They did not agree with the rationale from STM, that the ruler would have had to first issue the money before it could be collected in taxes. And even though they did not claim that money was created by the peasants themselves either, they did draw on a
story that money essentially emerged as a replacement for trading or taxpaying with real resources.

There are many ways to pay taxes, and you could in principle pay by potatoes. They did that in the old days. Or you could pay with your labor for example - before the monetary system existed. And then it emerged later on, because they were like ‘okay, it’s cumbersome to collect so many potatoes, right.

(Int. 6)

Even though taxation is not barter, the idea here follows from the same logic as the myth of barter which is so predominant in neoclassical economics. The belief is that money essentially was invented to ‘grease the wheels’, that money is only a ‘veil’ over barter or over trading with real goods (Skidelsky 2018, 22-24).

The essence of this fable is that though it was convenient to make contracts in money, behind the veil of the contracts were real things being traded for each other at their real (i.e. barter) prices. The theory of the bartering savage is heavily indebted to the classical anthropology of Adam Smith’s day, at the heart of which is the figure of homo economicus, who pursues his self-interest in isolation from society. That this still underlies neo-classical psychology is made clear in Paul Samuelson’s famous textbook, where we read: ‘A great debt of gratitude is owed to the first two ape-men who suddenly perceived that each could be made better off by giving up some of one good in exchange for some of another.’ Most economists have favoured the bartering savage story, because it leaves out society and government.

(Skidelsky 2018, 24)

This ‘fable’, as Skidelsky calls what Graeber calls ‘the Myth of barter’ advances the general view of money’s neutrality. Because it is so commonly taught in textbooks it is a widely held idea between both economists and laypeople. The mainstream neoclassical perception of money as a “neutral veil” over the real economy leads to the implicit conclusion that is “uninteresting”, not worth paying scholarly or professional attention to. “Money and its dynamics can be largely ignored; hence, the roles played by banks, the financial sector in general and money creation in particular are poorly understood by the orthodox economist and the layperson.” (Ravn 2015, 96)
The importance of language

One could ask why this “Myth of Barter” is still taught in textbooks, if historical anthropology has proved it wrong, and why do so many people still conceptualize money from the logics of that story. “The answer seems to be that the Myth of Barter cannot go away, because it is central to the entire discourse of economics”, writes David Graeber with reference to the genesis of the discipline which also evoked the idea that there even exists something called ‘the economy’ — something distinct which we can study and which operates according to its own laws much like the physical laws (Graeber 2011, 43). Economist Robert Skidelsky also points to the power of the language of mainstream economics:

Today’s textbooks on banking and finance do little more than echo Aristotle [on his view of money]. Banks simply ‘intermediate’ between buyers and sellers. This arcane phraseology serves the protective purpose of disguising the actual power of finance – and financiers – in the economy.

(Skidelsky 2018, 22, emphasis added)

From the notion that banks are ‘intermediaries’ comes the language about the functions of banks, which adds to the confusion about what banks really do: “The language of banking – ‘taking’ deposits and then ‘lending’ them out – reflects the original function of banks as storehouses and intermediaries. But most ‘deposits’ today are created by the banks themselves when they make loans.” (Skidelsky 2018, 34). This language was widely evident and a source of confused conversations during my interviews. One interviewee spoke of money creation by banks, but at the same time used the language of “savings” and the bank’s own “capital” as the source of its lending:

It’s completely possible to create money in the private sector through local banks, but I think the challenge is that you depend on a certain savings rate to make it possible. And the savings rate is really low in Africa, Asia or at least low-income countries, and that makes it difficult for banks to take on high risk, to just create money, because it comes at the expense of the banks’ own capital.

(Int. 7)

This interviewee was of the few who agreed that banks create money when lending, but they still made use of language which builds on and furthers the idea that banks are
intermediates, lending out money that they have received. The prevalent language is a mold for thought:

[It] is undoubtedly the conventional view of money as a commodity, of monetary exchange as swapping goods for a medium of exchange, and of credit as the lending out of the money commodity, that has enjoyed the lion’s share of support from theorists and philosophers over the centuries, and thereby dominated economic thought – and, for much of the time, policy as well.

(Martin 2014, 16)

If it were only economists and certain experts who were using imprecise language about things that they were fully aware work differently, it would not be of importance, one could say. But the language influences policymakers who might not know how money, banking, and finance work exactly, and the stories and the language of economics influence laypeople as well. The influence extends to ethics, argues Martin: “Modern, orthodox economics is a uniquely powerful set of ideas which pervades not only the world’s central banks and finance ministries but popular culture and personal ethics as well – and the conventional view of money is ingrained in its core.” (Martin 2014, 268).

David Graeber describes an instance of exactly that. He recounts chatting with an attorney about her opinion on his previous work for cancelation of Third World debt.

“But,” she objected, as if this were self-evident, “they’d borrowed the money! Surely one has to pay one’s debt.”

(Graeber 2011, 2)

If one carries the idea that the bank lends out money that other people have deposited, maybe even other people’s personal savings, then the obvious moral conclusion is that they ought to get their money back. However, if it were a bigger part of popular perceptions that the bank creates the money it lends out, maybe morals about paying such debt would change. As Graeber writes about the British royal debt which founded the Bank of England: “To this day, this loan has never been paid back. It cannot be. If it ever were, the entire monetary system of Great Britain would cease to exist.” (Graeber 2011, 49). Framing it this way certainly turns the moral about ‘paying one’s debt’ somewhat on its head. Ingham, drawing on the historical economist Michael Hudson’s work, elaborates how etymological evidence shows how closely linked ethics and the language of economics is.
In all Indo-European languages, words for "debt" are synonymous with those for "sin" or "guilt", illustrating the links between religion, payment and the mediation of the sacred and profane realms by "money." For example, there is a connection between money (German Geld), indemnity or sacrifice (Old English Geild), tax (Gothic Gild) and, of course, guilt.

(Ingham 2004, 90)

The Norwegian word for debt ‘gjeld’ and Danish ‘gæld’ are related to this word root, and the Swedish word for debt ‘skuld’ bears the meaning guilt. As such, the etymology of some parts of finance is closely interrelated with that of ethics in the Scandinavian languages that were used in my interviews.

An interviewee asserted that:

A historical change in development aid, is that many Western countries, Norway included, has stopped lending to developing countries’ authorities. It was very common to do before. Now you give credit to private companies, but not loans.

(Int. 1, emphasis added)

When I asked them to explain the difference, they distinguished between the politics in giving to authorities versus private sector. Again, the term for the monetary relationship also distinguished between: credit to private companies, loans to authorities. So, I asked the interviewee if they meant different things by the two words ‘credit’ and ‘loan’.

“Yeah well… for me, I think about the same. But in my language use it seems more fitting to say credit when talking about private companies, ehh, hehe, I don’t know why.” (Int. 1). It adds to the confusion that economics generally does not distinguish, even though it could be specified that a credit is technically money “on tick”, whereas a loan is like a loan of anything else, like a book or a bicycle. In the first instance, the issuer of the credit does not need to possess the money to be able to lend them to you, in the second instance the lender must possess the thing before it can be lent out. Richard Werner writes about the unclear terminology of banking:

[B]anks create money when they grant a loan: they invent a fictitious customer deposit, which the central bank and all users of our monetary system, consider to be ‘money’, indistinguishable from ‘real’ deposits not
newly invented by the banks. Thus banks do not just grant credit, they create credit, and simultaneously they create money.

(Werner 2014b, 74)

The whole language – terminology, or “phraseology” as Skidelsky said – about money creation, lending and banking is a jumble. Graeber describes how this language is much more confusing than it has to be. He points out that many credit instruments are made to look like complicated new inventions in the age of computers and internet, incomprehensible to the lay person. Gold and paper money are by popular perception seen as the original form. But “historically, credit money comes first, and what we are witnessing today is a return of assumptions that would have been considered obvious common sense in, say, the Middle Ages – or even ancient Mesopotamia.” (Graeber 2011, 17). Thus the modern consensus change in economics about money creation could be argued to constitute a movement to an “old” understanding of money. Or at least another pendulum swing towards a more general understanding of money as credit, following the pendulum swing of the actual nature of money: Away from its physical representations of the last many years, towards – again – a less physical, more pure ‘credit’ form, which has followed since the internet and the deregulation of finance since the 1980ies. Katarina Juselius argues that the language of economics is abstract and for the non-economist much economics is concealed by complicated language. To make it possible for practitioners in other fields, and also for the general public, to engage with economics, she urges scholars to demystify the language and to make clear the assumptions that economic theory is built on. Only that way important and qualified questions can be raised about economics (Juselius 2019). Ravn emphasized that such professional or academic barriers are significant for economics in particular, because money is so engrained in everyone’s lived experience.

It is a commonplace that the technical jargon of economics, finance and banking is a barrier to public understanding. In the case of money creation by commercial banks the challenge, however, is exacerbated, because this process flies in the face of many things we “know” about money, whether we are laypersons or economists.

(Ravn 2015, 93)

The problems arising from this obscurity of economic language are perhaps especially important in the development field where workers come from many different
disciplines, and where the core purpose of the field is dealing with unequal economic distribution.
6 Conclusion

The aim of this thesis has been to investigate the conceptions of money that are employed in the Norwegian development sector. In the context of current debates in economics about the nature of money and banking, I have explored the conceptions of money that Financing for Development is based on through the case of the Norad program Skatt for Utvikling. I have been particularly concerned with the question of money creation, since this is at the heart of the ongoing consensus shift in economics, which is characterized by the increasing integration of systemic perspectives on money and banking into mainstream economics. Additionally, the question of money creation seems to potentially have a special relevance for Financing for Development since, in order to finance development, it is essential to comprehend where money comes from on a macroeconomic level. I have investigated conceptions around money and banking through interviews with experts in the Norwegian development field and investigated these conceptions through a theoretically driven discussion. The research question which have guided the analysis is:

How are conceptions of money and banking embedded in the Norwegian tax for development strategy, and how are these conceptions related to the ongoing consensus shift in economics on the nature of money and banking?

In order to answer this question and discuss some possible implications, I will begin the conclusion by summarizing the main findings of the thesis.

6.1 Summary of findings

In chapter 5.1, I discussed the role of the state in the monetary system and found that the Skatt for Utvikling strategy is based on a view of the state as a user of money. Wealth is by the interviewees often described as being produced in the private sector, subsequently collected, and then spent by the state. The core reason for focusing on tax as a development strategy seem to be that, being perceived as a money user, the state appears to be dependent on income to finance its expenditures – including development expenditures. These ideas, I have argued, are built on neoclassical economic ideas about money. The State Theory of Money (STM) on the contrary, claims that the state has a
role in the monetary system fundamentally different from other economic agents, in that it is the most important issuer of money in the economy. Thus, the sequence of functions in the monetary system is claimed to run the opposite way: Taxes are not primarily a source of income to cover state expenditure. Rather, the primary function of taxation is to control inflation and to steer the economy in a given direction. For a state not to be dependent on income to cover its expenditures, however, requires monetary sovereignty. This is something that developing countries have to varying extents. Proponents of STM consider it essential for a country to obtain full monetary sovereignty to create economic development. But the aspect of monetary sovereignty appears to be absent in the Financing for Development discussion.

In chapter 5.2, I discussed the perceived role of banks in the monetary system and the extent to which the development practitioners consider banks as intermediaries, or producers of money. While the Skatt for Utvikling strategy does not explicitly deal with the nature of private bank lending, the interviewees shared with me their views on this topic. Most interviewees agreed that banks create money through lending to some extent. Some explicitly referenced this function as the ‘money multiplier’ or as ‘fractional reserve’, which are both neoclassical monetary theories. All interviewees agreed that bank lending depends on initial savings in the form of deposits, or at least depends on a certain level of savings in the economy overall. These two explanations both build on the foundational idea that banks essentially are intermediaries, which is a central tenet of neoclassical economics. Several interviewees mentioned problematic distributional effects of bank lending, arguing that market liberalization of the banking sector leads to inappropriately high levels of consumer loans and to asset price inflation. While they considered it a possible problem where bank lending goes to, no one appeared to recognize any similar problem with where that money comes from. This, I argue, is related to the popular perception that lending ultimately stems from savings of people, or firms’ excess money. Credit Creation Theory of Money (CCTM), on the contrary, argues that the sequence runs in the opposite direction: that lending enables investment which create savings, and that banks consequently are not dependent on initial savings to extend loans. Most interviewees seem to agree with CCTM in recommending strong credit regulation. However, following CCTM another important priority is a preference for domestic loans over foreign loans. This is because of two things: the lack of flexibility due to denomination of the loan in foreign currency, and
the extraction of profits out of the borrowing country. While some interviewees agreed about the challenges with loans denominated in foreign currency, only one seemed to agree with the issue that foreign loans essentially extract money from the borrowing country. Additionally, some CCTM theorists highlight the difference between redistribution and predistribution, i.e. distribution of already-existing money as opposed to distribution of newly created money. I argue that the view of banks as intermediaries, shared among my interviewees and by neoclassical economic theory, implicates an element of redistribution of money in the economy. In contrast, the view of bank lending as money-creation implicates a pre-distributonal role. Consequently, CCTM promotes an even stronger justification and recommendation of credit guidance together with a weaker emphasis on the levels of savings.

The analysis in both of these chapters, 5.1 and 5.2, on the role of the state and of banks respectively, indicate that the Norwegian financing for development strategy is predominantly based on neoclassical economic thinking, which was also explicitly confirmed by interviewees a few times. I argue that this thinking primarily concern redistribution of money – moving money from one place to another. The third analysis chapter, 5.3, raises more explicitly the question of where money is perceived to come from: How money is created – and why it turns out to be so complicated to talk about. I find that interviewees consistently talked about moving money when I asked them about money creation. I found it complicated and awkward to get my interviewees to talk about money creation. I interpret this to indicate that they are unfamiliar with of the ideas of creation and deletion of money. Most interviewees found the topic interesting but abstract and practically irrelevant. I argue that we can trace this taken-for-granted position back to the dominance of neoclassical economics, which, again, holds that money is primarily a medium of exchange that facilitates what the economy essentially consists of, namely barter-like transactions in the real economy. On the contrary, systemic theories of money perceive the monetary system as a system, rather than the sum-total of all transactions. Both STM and CCTM see the monetary system essentially as a system, having certain mechanisms by design – including the aspects of creation and deletion of money: the beginning and the end of the circuit, so to speak. Both these mechanisms are almost absent in neoclassical economic theory, as well as in popular perceptions of money. Additionally, I found strong agreement among the interviewees on the perception that
creation of money first and foremost carries with it a high risk of producing a damaging inflation, a notion that seems to play a major role in their aversion to discussing money creation as a policy tool. This aversion could be informed by the similarly strong focus on inflation in neoclassical economics. Again, we see a mirroring effect of neoclassical economics and taken-for-granted conceptions about money. While systemic theories of money do not claim that the amount of money is irrelevant regarding inflation, these theories hold that other factors, such as political stability and allocation of the new money, have more influence on inflation. Proponents of systemic theories of money explicitly consider how both states and private banks do create money—continuously and in significant amounts, in all major economies. While systemic theories of money address potential problems regarding the amount and allocation of such newly created money in different ways, it seems to be largely absent among neoclassical economists, as well as in the Norwegian financing for development strategy.

Finally, I discuss how conceptions of money and value can lead to an inconsistent language about these concepts. The language about money, among my interviewees, seems to be influenced by popular perceptions of money’s materiality and its association with different forms of “real” value, such as gold. This may be interrelated with different origin stories of money, of which the most common is that money originates from simple barter economies—the explanation promoted by neoclassical economics. Systemic theories of money, on the other hand, emphasize the historical origin of money from complex credit systems. I wrap up by returning to a point I raised in the introduction: That the way we talk about money influences how we conceptualize money, which in turn guides policy. For that reason it could be of great importance for development policy-making, not only how economic scholars conceptualize money, but also how professionals in the wider economics-related fields comprehend the nature of money.

6.2 Perspectives

While the main finding from this thesis is that money creation is not an explicit part of the framework in the Norwegian tax for development strategy, my intention is not to suggest that additional money creation would necessarily be a solution to financing
development efforts. However, money is already continuously created by different institutions, in varying amounts, and for various purposes, all differing among countries, depending on each specific legal framework, financial architecture, international relations, and the shape of the economy. This thesis illustrates that this already-ongoing continuous money creation does not appear to be explicitly incorporated in the strategic thinking for the financing of development.

I set out to uncover how conceptions around money and banking are embedded in the Norwegian tax for development strategy and I demonstrated how Skatt for Utvikling is based on neoclassical economic monetary theory. What is more, my interviews seemed also to reflect neoclassical economics’ lax attitude towards the importance of monetary theory itself. Money creation appears to be a somewhat vague subject which is not clearly articulated or actively dealt with, and the very topic seemed strange to my interviewees. Many of them said they took the nature of money and banking for granted. The findings in this thesis indicate that the development sector has a blind spot when it comes to the subject of money as a systemic phenomenon, and especially regarding the aspects of creation and deletion of money. This fuzziness is reflected in both the practitioners’ perceptions and in the policy. Even though the theoretical status quo is changing in economics, this change does not currently seem to be reflected in the Norwegian tax for development strategy.

For anyone concerned with the question of how to finance economic development, it seems the time is ripe to expand the toolbox of strategies to include money-creation related considerations and tools. Examples of useful new insights are: the pre-distributional potential of state financing of domestic development; the pre-distributional effects of private bank credit issuing; and the implications of perceived dependence or non-dependence on savings for state and credit creation of money creation respectively. Examples of possible tools could be: embracing monetary sovereignty and enable the state to create money, to contribute directly to the financing of sustainable development; and integrating the possibilities of credit guidance policies towards private bank money creation to direct funds more accurately to the desired development purposes. It is my hope with this thesis to inspire agents in the development sector to take one of many future steps toward a wider range of even more powerful development policies.
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