A CRITIQUE OF MONETARISM

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Introduction

Monetary policy is nearly impossible to escape, as it is one of the most widely discussed areas of economics. Every major newspaper publishes countless stories regarding Federal Reserve actions, and relating them to numerous schools of economic thought. However, in the last 50 years, no school of thought has been as influential as monetarism. Many of the policies of the Federal Reserve, and other central banks across the globe, are based, at least foundationally, on monetarism, or its modern contemporaries. Despite this global appeal, and relatively fast adoption by numerous economics experts, it is a deeply flawed economic theory. Monetarisms goal, like all schools of thought, is to bring about economic stability and prosperity. The issue, however, is that the policy implications of monetarism are, at best, counterproductive, and, at worst, can cause the recessions they are trying to prevent. This paper will discuss the main arguments of monetarism itself, and will attempt to demonstrate, through an Austrian lens, the flaws in its arguments. As well, this paper will discuss what monetary actions should be taken to truly meet the goals of economic stability and prosperity.

A history of Monetarism

The first action, however, must be to review the prominent thinkers of the school, and its historical development. Irving Fisher, a notable economist who lived from 1867-1947, is one of the foundational thinkers for the monetarist school of thought. He was not a monetarist, in fact that term was not even coined during the course of Fisher's life, but he is vitally important for providing the basis upon which the school was built. He is notable for his work on the quantity theory of money. Of course, there were thinkers who worked on this issue before him, most notably, Simon Newcomb. Newcomb was the first to create an exchange equation based on quantity theory, however, it was Fisher that developed the most famous version of this theory, and it is that theory which became the foundation of monetarism as we know it today.(Tobin 2008) The equation, known as MV=PT is known widely as the Fisher-Newcomb equation. In the section of this paper titled "The Monetarist Theory", this specific equation will be discussed in far greater depth.

This advancement on the part of Irving Fisher took place in his 1911 paper entitled *The Purchasing Power of Money*. Out of this equation comes the quantity theory of money, which, once again, will be discussed at greater length in the following section of this paper. For the purpose here it is simply worth noting that the quantity theory of money, and therefore the equation from which it is derived, are foundational for the views of the monetarists. Fisher was working from Yale, however, it was the University of Chicago that was the most influential in the development of monetarism. The two earliest influences from Chicago were Henry Simons, and Lloyd Mints, who wrote from the 1930s-1950s. Simons was one of the earliest advocates for using the stock of money as a way to achieve price stability, and Mints expanded those ideas and proposed specific programs for achieving that stability. (Tobin 2008)

However, Milton Friedman, another professor at the University of Chicago, would become the chief advocate of monetarism, and was responsible for the formation of the various ideas into one, single school of thought. Friedman's 1956 restatement of the quantity theory of money was fundamentally responsible for helping to push monetarism into mainstream economic spheres. This school of thought was seeking, primarily, to return economic thought to some of its more classical monetary views, and to move it away from the Keynesian movement that had started around the time of the Great Depression.

Their business cycle theory would prove to be one of the chief reasons that monetarism grew in popularity so rapidly in the 1970s. Clark Warburton wrote one of the most influential papers in monetarist theory, and it was releasing in 1946. (Cagan 2008) It was the very first explanation of the business cycle on the grounds of monetary factors. Milton Friedman and Anna Schwartz, in 1963, wrote an extension of this paper. They demonstrated that every business cycle since the Civil War was preceded by a notable change in monetary growth rates. They found that on average the lag between monetary change and business cycle fluctuations was about 6 months, but this fluctuated greatly, and sometimes it was more like 2 years. (Friedman & Schwartz, 1963a, 60)

Later that same year, Schwartz and Friedman published *A Monetary History of the United States* which would become one of the most influential books from the monetarist school. The book included a thorough discussion of business cycles and, even more importantly, attempted to explain the Great Depression in monetarist terms. They argued that the business contraction of 1929-1933 was caused by monetary contractions that were exceptionally large in the preceding years. (Friedman and Schwartz, 1963b, 230) This stood in opposition to the Keynesian example that prevailed at the time.

In the 1970s, monetarism rose rapidly among economists and central bankers, do largely to its difference from Keynesianism. During this decade, the Bretton Woods monetary system collapsed, and the following year were the infamous oil shocks of 1973. At that point, Keynesianism was unable to account for these events. There was simultaneous high unemployment, and rising inflation. (Cagan 2008) The prevailing

Keynesian policies would call for a decrease in government spending to slow the inflation, and, at the same time, an increase in spending to drive down unemployment. These, obviously, are mutually exclusive, so policy makers began looking for a new economic framework that could better account for these issues.

In 1979, Paul Volcker became the head of the Federal Reserve, after having been appointed by President Carter. It was Volcker who, in the United States, first actively pursued monetarist policies. He restricted the money supply, in order to drive up interest rates, and, therefore, halt the rapid inflation. His tactics were successful at their stated goal, but had the unintended consequence of raising unemployment as well.

At the same time, however, in the United Kingdom, a far more successful demonstration of monetarism was taking place. In 1979, Margaret Thatcher, a member of the Conservative Party, won the office of Prime Minister. At this time in Britain, there was severe inflation, and in response Thatcher implemented strict monetarism. It is abundantly clear, is that the actions of Volcker and Thatcher, and their apparent successes, launched monetarism into the mainstream economic world, and its influences are still seen widely today, nearly 40 years later.

The Monetarist Theory

Now that the foundation has been laid, and the development of monetarism has been discussed, it is time to look at the fundamental beliefs and theories of the monetarist school of thought. This section will discuss both the monetarist theory itself, and its implications for monetary policy.

To start, let us turn our attention to the foundation of monetarist thought: the quantity theory of money. This theory argues that the general price level is directly related to the amount of money in circulation. Leading up to the rise of monetarism, Keynesian economics was far and away the most widely accepted economic school of thought. They differed, greatly, on matters of policy. As was alluded to earlier, the members of the Keynesian school firmly believed that fiscal policy, often in the form of government expenditures, was the best way of impacting the economy, whereas the monetarists, as the name suggests, prefer to use monetary policy. The reason for this great difference is because of their views of the quantity theory of money.

Both Keynesians, and monetarists, have developed an equation to describe how the money supply impacts the price level, but they disagreed over the role that the velocity of money played. They both developed their own equation, but a comparison of these is not relative for the purpose here. However, the monetarist equation, often known as the Fischer-Newcomb equation, is clearly worth discussing. In its simplest from, it is written as $MV=PT$ where M is the total amount of money in circulation, V is the velocity of money, T is an index of the real value of aggregate transactions, and P is the general price level. T, therefore, is a constant and does not change. As well, the monetarists believe, generally, that the velocity of money is stable. For that reason, they treat it very much like a constant. Therefore, changes in the money supply result, proportionally, to changes in the general price level. The fundamental result of this is the belief that, in the long run, there is neutrality of money. In other words, an increase in the stock of money will lead to an increase in the price level, but will not affect real economic factors like output or consumption.

However, this raises the question of what do monetarists believe occur in the short run, and for that one must discuss the Phillips curve. Once again, monetarists developed their theory in direct response to Keynesian theory, so it is important to start there. For the Keynesian the Phillips curve describes a trade-off between unemployment and inflation. It was created by tracking historical evidence, which showed that, in general, when inflation increased unemployment decreased, and vice verses. Prior to the rise of monetarism, this basic theory was widely accepted, and was very influential in the policy of that day.

Milton Friedman, however, was unconvinced of the long run implications of the Phillips curve, and helped develop what is now known as the Expectations-Augmented Phillips curve. Fundamentally, Friedman argued that in the long run the Phillips curve is perfectly vertical. The implication of this being that there is a natural rate of unemployment, which is fundamentally fixed. However, he does agree with the Keynesians that, in the short run a trade-off does exist.

When inflationary policies occur, the market becomes flooded with cheap credit, which incentivizes consumption. This, in the short run, leads to an increase in hiring, and an increase in inflation. However, the monetarist notes that individuals will not, immediately, recognize the actions as inflationary, so there is a short period where the unemployment rate falls below the natural rate of unemployment. After a short period, individuals start to recognize the inflationary practice. In order to compensate for this, individuals push for higher wages, and this leads, ultimately, to a return to the natural rate of unemployment, but at a slightly higher price level. It is also worth noting that Friedman argues that the more these inflationary shifts occur, the more likely economic agents are to identify the policy as inflationary quickly, and thus with each increase the economy return to the natural rate of unemployment quicker and quicker. (Fisher 2008) Friedman's goal here was to do away with the various Keynesian polices that attempted to shift between inflation and unemployment.

That being said, Milton Friedman was a huge proponent of a continual increase in the rate of inflation, even though that may sound counter intuitive at first. This belief of Friedman stems from his views on the nature and causes of the business cycle. According to Friedman, periods of extreme inflation are caused by excess money supply created by a central bank. However, he believes that there are certain situations where the money supply must increase in order to avoid economic recessions. Friedman believes that deflationary periods are caused by the central bank's failure to sufficiently increase money supply when there is a liquidity crisis. (Friedman & Schwartz, 1963b, 412) A liquidity crisis, for Friedman, refers to a period where cash is in short supply, but the demand for it is relatively high. The result, then, is deflation, as loans are charged higher and higher rates of interest, and the loans themselves get harder to attain.

This leads then to the fundamental policy implication of the monetarists: the Federal Reserve should continually increase the money stuck, thus increasing inflation at a constant and expected rate. This would avoid any excess money supply that would lead to extreme inflation, as well, it would stop any liquidity crisis from arriving if the central bank failed to act properly. This came to be known as the k-percent rule. It was developed primarily by Milton Friedman. It is known as k-percent because Friedman never truly selected a percentage by which he felt the money supply should be continually increased. In 1962 Friedman argued that this rate should be somewhere around 3-5%. However, just three years later, in a meeting with the Governors of the Federal Reserve, he argued that the rate should be between 4-6%. (Hazlitt 1976)

Criticism of the Monetarist Framework

Monetarist theory has had a deep and profound impact on the political sphere since the 1960s, yet the theory itself is highly flawed. Not only are its fundamental beliefs riddled with economic issues, the policy implications are openly detrimental to the stated goals. Of course, all economic theory aims to stabilize the economy, and to provide growth. However, the monetarist school of thought, and their subsequent k-percent rule, are simply not capable of meeting that goal.

The quantity theory of money is the basis of monetarist thought, and therefore it is the first thing worth discussing here. The quantity theory equation is, fundamentally, a gross oversimplification. For the monetarist there is one single use for money, and that is to purchase goods. According to their equation, then, the total money stock must always buy the total stock of existing goods. It is incapable of buying more or less. This is reflected by the equation MV=PT. If the money stock is doubled, and purchasing goods is the only use of money, and the stock of goods remains exactly the same, then the price level must double. This, of course, is not at all what happens. It does not take much thought to realize that there are many uses for money. (Hazlitt 1976) One that comes to mind easily is simply holding it. Some people, nearly all in fact, derive value from holding money. It provides a level of safety. Money is useful as a store of value, not simply as a medium of exchange.

However, that is not the end of this discussion. The value of money is not derived from a cut and dry formula, as would be the implication of the Fisher-Newcomb equation. It, like every other good in the market, is subject to the laws of supply and demand. It is not simply mechanical in nature. There is, of course, some aspects of this equation that are true, for example it is abundantly clear, through both theoretical and historical accounts, that an increase in the money supply will increase inflation. However, it does not follow a carefully structured, mechanical formula like the one presented by monetarists.

It is vitally important to remember that human action plays an incredibly important role in economic activity. People are rational actors, and those actions must be foundational to economic theory. Henry Hazlitt wrote a critique of the quantity theory of money that was based around his belief that there are numerous scenarios where strict quantity theory is simply wrong. To demonstrate this, Hazlitt identifies what he refers to as the three stages of inflation. The first stage of inflation occurs when people do not yet realize that currency inflation is occurring. (Hazlitt 1976) During this stage, they increase their cash holdings and do not engage in much spending, as they think that it is just a momentary increase in the money supply. In this stage, inflation does not occur as the quantity theory would estimate.

The second stage is when people begin to identify that inflation is taking place. They realize that the central bank is the reason for the inflation, and realize that the inflation will likely occur well into the future. So people spend a lot more money than they did before, as they realize that prices are only going to get higher in the future, and they want to get all the value from their money that they can. The final stage of inflation demonstrates the most clearly the issues of strict adherence to the quantity theory of money. In this stage, fear reaches and all-time high, and inflation increases at an insanely high rate, far higher than the quantity theory would say is possible. This occurs as people begin to fear inflation more and more, so they spend as much money as possible as soon as possible. (Hazlitt 1976)

This is not just a theoretical observation, there have been numerous, real-world examples that corroborate this. The most notable, of course, is the hyperinflation that occurred in Germany. Keep in mind, strict quantity theory would state that for a given increase in the money supply, inflation will increase by a proportional amount. Hazlitt, and the historical example in Germany, clearly refute that. In Germany, in 1923, the entire stock of paper money was billions of times higher than it was a few years earlier, before the inflation had started. However, it had a gold exchange value that was only 1/16 of what it was originally. (Hazlitt 1976) Eventually, the paper money became completely worthless. This example, as well as the theoretical discussion of the three stages of inflation, demonstrates two main points. Firstly, it shows that strict adherence to the quantity theory of money is not reasonable. Secondly, it demonstrates that an understanding of inflation based primarily on the quantity theory of money fundamentally misunderstands inflation, and how it effects the economy.

The velocity of money also proves to be a large issue for the monetarists, as it does not truly function as they argue it does. For the quantity theory of money to be at all effective, it requires that the velocity of money be relatively stable, and function much like a constant, otherwise conclusions based on this equation are relatively useless. However, it is quite clear that, in the real world, the velocity of money is not at all stable.

There are no direct statistics on the velocity of money, so for our purposes here the turnover of bank deposits will be used, as these account for approximately 88% of all media of payment. In December of 1975, the average annual rate of turnover of demand deposits in New York City was 351.8, compared to 118.7 in 6 other large US cities, and 71.8 on average in smaller communities across the country. (Hazlitt 1976) Though some of this discrepancy is accounted for by the fact that transactions in New York are often taken by multinational corporations making huge transactions, it cannot account for all of it.

It is also worth noting that, even if the velocity of money were somehow stable across the board, it is still not a good way to determine price. Goods that are exchanged on the market to not derive part of their value from the number of times that they are exchanged. Velocity, in and of itself, implies exchange. It is not a one way sale, as there must be a buyer and a seller. A good must also be bought if it is being sold. Therefore, the number of times a good changes hands has no real effect on the price of an individual good. Hazlitt described this occurrence when he wrote that:

> When 100 shares of a stock are sold, their value is not thereby necessarily depressed, because the shares are also bought. Every sale implies a purchase, and every purchase a sale. When a man buys a commodity, he "sells" money; but the seller of the commodity "buys" money. There is no necessary connection whatever between changes in the "velocity of circulation" of money and changes in the "level" of commodity prices. "Velocity of money" is merely a resultant of a complex of other factors, and not itself a cause of any important change whatever.(1976)

The velocity of money, therefore, is a huge gap in the thinking of the monetarists, and it calls into question their quantity theory of money. This is obviously a huge issues for the monetarist framework, as it is one of the most fundamental aspects of their school of thought.

Let us shift gears here a little bit and move on to the next major issue with monetarism: it fundamentally misunderstands the negative implications of inflationary policies. Keep in mind that the K-percent rule calls for a continuous, and never ending, inflation of the money supply. The chief issue with this policy, however, is that there is almost no way to determine what that percentage should be. Milton Friedman recommended somewhere between 3-5%, and later 4-6%. Others, like Sumner H. Slichter, of Harvard University, believe a 2-3% increase in the money supply every year is the correct amount. (Hazlitt 1976) The chief issue is this: how can you even create this policy? Assume that theoretically there was a rate at which the money supply could be set, and it does in fact bring about the goal of economic growth. There would be no way to determine what that amount is, unless you wanted to undertake the slow process of guess-and-check until you came across the correct answer by change.

However, that is not the only issue with the K-percent rule. As was discussed earlier, this rule was developed to take the power out of the hands of the central banks, as Friedman felt that they were responsible for both inflation, and deflation. However, if this rule were ever to be implemented it would have to be done by politicians. It should be abundantly clear, right off the bat, that politicians would likely be unable to pass the law at all, let alone get it correct. In addition, what is to stop the politicians from changing the law at some point down to road, and give themselves the power, once more, to manipulate the money supply. In fact, Friedman's plan would fall victim to the political agenda, and politicians, which is the very thing he was attempting to avoid in the first place. It is simply not a practical policy.

However, just because the plan lacks practicality, does not mean that its theoretical foundation is sound. Monetarists, by relying on the oversimplification that is the quantity theory of money equation, fail to realize the true negative impacts of inflation. Firstly, the price level does not immediately rise by a set degree for every person. In fact, some people actually gain wealth as the result of these policies. The people who receive the money first, after it enters the economy, experience a great benefit, as the prices have not yet increased, but they have a larger degree of money available to them. However, people who do not receive this initial influx of newly created money are harmed, as each dollar they hold becomes less and less valuable as time goes on. It is simply an unequal policy.

In addition, monetarists fail to take account of the fact that inflation of the kind recommended by the K-percent rule are very likely to lead to vastly more inflation than they originally estimated, or it will be completely ineffective. (Hazlitt 1976) Imagine an economy where there was a 5% increase in the money supply every single year, and everyone was aware that it occurred. This would lead to a system where every loan would have a 5% added on every year, unions and employees would expect a 5% wage increase every year, and so on. This would lead to the economy reacting so fast, after a long enough period of time that the inflationary policies are functionally ineffective. (Hazlitt 1976) The inflation would begin to increase at a faster and faster rate, and it would have a very negative impact overall. It would not stimulate the economy in any real sense, rather it would be incredibly disruptive and harmful for individuals within the economy

In addition to that, it can lead to severe mal-investment. The inflationary policies of the central banks, combined with the fractional reserve banking system, cause interest rates to be far lower than they would be if the market were completely free. As a result, a far greater number of activities appear to be profitable, when they would not have before. These businesses come about through mal-investment. There is not enough real demand for these services to be brought about on the free market, and the inflationary policies allow for resources to be directed toward these actions. Thus, there is an opportunity cost, as those resources are not going to their most highly valued ends, as they would in the absence of inflationary central bank practices. This leads, necessarily, to recession. These mal-investments inevitably fail, as they were not truly good investments in the first place. The recession is a corrective measure and it gets rid of the mal-investment within the economy.

However, under monetarism, especially if the government instituted the K-percent rule, this process would go on and on without end, and it would get progressively worse over time. This period of mal-investment, and the bust that follows, are caused by inflation. It is clear, therefore, that the monetarist school of thought is not actively working to stabilize the economy, the truth is that their policies have the exact opposite effect.

Modern Day Monetarists

Monetarism has fallen out of favor in recent years, as New Keynesians and others like them have come into mainstream economics. However, in the last few years there was a revival of monetarist teachings in the form of the school of thought known widely as market monetarism. This school of thought is built up, fundamentally, from monetarist teachings, as the name would imply. It is an attempt to rethink classical monetarism, and formulate it correctly. For that reason, it is valuable to discuss the fundamental beliefs of this modern school of thought, and the flaws with it as well.

Market monetarism, which has been developing in the wake of the Great Recession, is based primarily upon the writings of Scott Sumner and David Beckworth. This theory places an extraordinarily high weight on the role of expectations of the future, and they view them as being vastly more important than the current situations. Specifically, market monetarists believe that it is expectation of Nominal Gross Domestic Product (NGPD) that are most important, and they place less emphasis on interest rate, or the current money supply. Unlike classical monetarists who argued that the price level was based on the money supply, market monetarists believe the price level is set due to future expectations of NGDP. As a result, successful monetary policy will stabilize these expectations, and thus no large economic disturbances will occur. Market monetarists deny that they are Keynesians, although, functionally, they are. (Ritenour 2013) According to this school, the 2008 recession was caused by the realization by investors that the Federal Reserve would not prevent a decline in NGDP. Therefore, they believe that aggregate demand should be propped up during periods when real outputs fall (Ritenour 2013). This, of course, they argue should be done through inflating the money supply.

The first issue with this school of thought lies in an over reliance on aggregate models in the formulation of its economic theory. The AD/AS model is a fundamentally flawed one. There is no real value in the economy where AD and AS intersect in any meaningful way, and that makes evaluating NGDP targeting exceptionally problematic.

(Ritenout 2013). Shawn Ritenour, a professor at Grove City College, argued that the primary flaw of the market monetarists was the faulty AD-AS model. He wrote that:

> The social economy is made up of a vast network of distinct markets that are integrated into a complex division of labor through the inter-temporal production structure and the use of a general medium of exchange. Productive activity, therefore, is the result of a vast number of decentralized decisions made by a multitude of different entrepreneurs at different places in the production structure. Capital is not a blob of homogenous schmoo, so investment is not a homogenous 'I'. (Ritenour 2013)

Ritenour, quite correctly, identifies that the very framework upon which this theory is built is faulty. As a result, their beliefs are not built up out of sound economic reasoning.

In addition, this school of thought fails to properly understand the role that expectations play in an economic setting. All action, on the part of entrepreneurs, is fundamentally linked to expectations. No one would produce a good now, if they did not expect that they would be able to sell it in the future. Production takes time, therefore expectations play a crucial role. However, economics is not capable of making judgements about what the expectations of individuals are, as expectations are tied to goals, and goals are individual in nature. (Ritenour 2013) Everyone has a unique expectation, and it is impossible to say, on the grounds of economic theory, what the source of those expectations are.

The final point worth noting about this specific school of thought is that it, once again, perpetuates the very recessions it is trying to avoid. This school, at its core, is recommending increases in the money stock to counteract economic downturns. As a result there will be mal-investment, and a corrective bust, as was discussed in the previous section of this paper.

A Better Way Forward

It should be abundantly clear the monetarism, and its more modern versions, are deeply flawed schools of thought. However, it is very clear that central banks and economics across the globe still make decisions based upon their fundamental teachings. They argue that, even though their framework may not be perfect, it is the best thing we have, so we should continue to use it. That is simply incorrect. A return to the gold standard, and a removal of powerful central banks, like the Federal Reserve, would be far more effective at achieving the goals of stabilizing the economy, and providing economic growth.

The main benefit should be abundantly clear. In the absence of a central bank, the monetary units would be far more stable. This allows for entrepreneurs to act without fear that, at any point in the future, inflation could devalue their assets. As well, it would entirely remove a governing body from having the ability to arbitrarily influence the currency. Milton Friedan felt that, fundamentally, the central bank was the source of much of the economic issues, and thus wanted to institute the k-percent rule to take that power away from the bank, and by extension, the legislators. The return to a gold standard would completely eliminate this issue. Free market control would be a far better option to provide a stable environment for saving and investing to occur. As well, there would be no issues of mal-investment, as the monetary supply is not being artificially inflated constantly.

Milton Friedman, however, stood in opposition to the gold standard due to his belief in the liquidity crisis. He was worried that if there was deflation then there would be no way to combat it, and secondly, he feared that if a liquidity crisis arose then there would be a recession as, once again, there would be no way to stop it. The truth is that neither of these issues are of great concern. Deflation, and by extension a lack of liquidity, are not inherently evil. Remember, as was discussed earlier in this paper, that one of the chief issues associated with monetarist policies is that they lead to mal-investment.

Deflation has the unique ability to counteract these mal-investments, to the overall benefit of the economy. When a deflationary period occurs, those specific industries are hit far harder, as they could only exist in the first place due to inflationary policies. The most important for this specific discussion, is the existence of fractional reserve lending systems, which are supported in the United States by the Federal Reserve. (Shostak 2008) These systems fundamentally undermine savings, as money is functionally being created out of nothing, so money can be lent, and subsequently invested, even though it was never saved. According to Frank Shostak, ”Under deflation, it is those non–wealth generating activities that end up having the most difficulties in serving their debt, because these activities were never generating any real wealth and were really supported or funded, so to speak, by genuine wealth generators.”(2008)

The result of all of this is that deflation is, functionally, a healing process of the previous inflationary periods. Those numerous businesses that were not wealth generating, but rather were propped up by inflationary policies, find it impossible to continue operating. This allows a far wider array of goods to move toward their most highly valued ends, rather than being redistributed by inflation.

Conclusion

Monetarism has been one of the most influential schools of economic thought over the last 50 years, and its impact can still be felt today. It was developed, primarily, as a response to the rise of Keynesian revolution that occurred around the time of the Great Depression. It was developed primarily by Milton Friedman, and other thinkers at the University of Chicago, however earlier thinkers like Irving Fisher, and Simon Newcomb played an important role as well.

Monetarism theory is based primarily on the quantity theory of money, and the belief that the increase in the money supply will lead to an increase in inflation as well. This leads, directly, to the most influential policy implication of the monetarism, the K-percent rule. There are many fundamental issues with this monetary tactic. Firstly, it is nearly impossible to actually identify a percentage to increase the money supply by every year, as well, given the nature of politics, it would be nearly impossible to implement such a program. As well, theoretically the monetarist framework in general has some very gaping holes, most notably in their formulation of the quantity theory of money. However, the largest issue, by far, with monetarism is its reliance on money inflation as a means of economic stability. It is clear from the analysis in this paper that inflation leads to mal-investment, which, in turn, leads to recession. In other words, monetarism actively works against itself.

The final two areas of this paper focused on the modern implications of monetarism, stating with the rise of market monetarists. This new school built itself up out of both classical monetarism, and new Keynesianism, and it developed a highly flawed theory as a result. The AD-AS model on which many of the schools presumptions are based, is incredibly weak. As well, the school fails to understand the role that expectations truly play in an economy. However, the schools primary failure, like classical monetarism, is that its primary monetary policy is inflation. This, once again, puts the economy on the path to recession.

However, the economy does not have to continue down the path laid out for it by the monetarists. It is not the best school of thought we have to work with. In order to stabilize the price of money, and simultaneously grow the economy, the central bank must be removed, and the gold standard must return. This would put an end to the inflationary issues that have plagues the global economy for decades, and would take the power away from central bankers and politicians, a goal Milton Friedman himself would gladly support. A return to the gold standard would also help to correct the mal-investments that currently exist in the economy, as a result of constant central bank inflation. The fact of the matter is this: the only monetary policy that will lead to long run growth is the return to the gold standard.

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