

Fiat, Digital, Crypto-Currency, & Economic Fluctuations

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The efficient functioning of the economy requires a common currency to facilitate the exchange of goods and services. In order to have a smooth functioning of complex and multiple financial transactions a common acceptable medium of exchange is required. Any currency serves this fundamental use of medium of exchange.

Since time immemorial, currencies have existed and have changed forms from barter to more general ones. Other than barter system, there is no natural currency in its pure form, all are but artificial human construct. Main types of currencies are:

- **Commodity Money:** Commodity money is similar to a barter system and a slightly refined form of barter system. Generally, materials used are comparatively rare and of high value so to perform functions of medium of exchange, purchasing power and measurement of account. The key aspect of commodity money is that its value is determined by the literal value of the commodity itself. Commodity money may consist of gold, silver, spices, shells, etc.
- **Gold Standard:** Monetary system where the currency of country is pegged against gold is known as currency based on gold standard. The amount of gold it possesses determines the value of the currency. The money can be converted to the amount of gold corresponding to its value. For instance, the Bank of England fixes the price of gold at GBP 1,000 per ounce, the value of one pound would be 1/1000th of an ounce of gold.
- **Fiat Money:** All prevalent currencies (Dollar, Pound, Yen, Rupee etc.) are fiat money. These are supported and approved by governments and recognized by monetary authorities. Material used in making notes or coins do not determine the value of bank note or coin rather it is government devised system which determines its value.

In other words, Fiat money is currency because respective government says it is a currency. Without common medium of exchange, working of economic system will be inefficient and unreliable. Almost all countries follow fiat monetary system and issue fiat currency and control money supply through central bank via commercial banks. Trust of public as well as power to enforce in issuing government or central bank makes it acceptable. Military power, economic robustness and political stability are the main factors that make a country strong and consequentially will help in ascertaining value of fiat money.

As per the international monetary system, central banks through government regulations are authorized to issue fiat money viz., paper money and coins.

Digital currency: It is an intangible medium of exchange which exists only electronically on some computers and related devices. Any kind of digital currency is merely an electronic representation of the commercial value of a particular currency. It has no physical existence. It can be called electronic currency, electronic money or digital bills, etc.). Further, there are two distinct types of currencies, namely electronic money and virtual currency.

Though digital currency is still in development and there is not any strict classification, yet monetary specialists distinguish digital currency into:

- *Electronic money:* when monetary exchange happens with the approval of monetary authorities and is a legal tender. Examples are Paypal & Pingit (Barclays).

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- *Virtual currency*: When currency is not officially approved by monetary authorities and not considered as a legal tender. Virtual currency is further sub divided into centralized virtual currency and de-centralized virtual currency (or crypto currency).
- *Cryptocurrency*: It is a currency which is electronically shielded by cryptography. In fact, all cryptocurrencies are digital currencies, but all digital currencies are not necessarily cryptocurrencies. The current functioning of Cryptocurrency is an eye-catching novelty.

Implications of Government issued Currency

Fiat, a government-sponsored prime currency, is also partially crypto. It is a simple paper but when encrypted by the government, becomes legal tender. It cannot be accessed or issued by everyone, only authorized entities can manage and issue.

They issue through central bank and their agents (banks). “Whoever controls money, controls the world” Currency has always been used as a tool of power and control.

Libertarians take extreme view regarding governments and fiat currency that both are essentially evil and nothing good comes of it. This assertion requires holistic analysis; however, it cannot be denied that they are generally abused yet their beneficial aspects cannot be ignored as well. Factually, government/authority and currency are necessary requirements for managing economy.

Keeping that in view, we have to determine what is the best alternative. Currency on one hand can be a cause of boom and bust but essentially a weapon for managing / correcting imbalances. If used well as deficit financing, it can produce good results by providing monetary resource to entrepreneurs and to masses for consumption that can stimulate economy by providing employment, capital investment, raising standard of living and building infrastructures.

It can be used for growth and progress, provided authorities are competent and morally upright, if not it can create havoc which we do observe in most of the less developed countries. Those who are competent and scrupulous will issue with prudence and appoint talented people and distribute in fair proportion to competent people and keep check on misuse by both lenders and borrowers. It is a delicate balance and slight disturbance can result in acute ramifications and economy can bust.

On the other hand, corrupt authorities can manipulate a lot. Currency is also used as a tool of power and control. Management of money is all about political economy. Head of the Central Bank or his sponsors can pass inside information to people in financial trading and whilst making decisions based on this information they can gain exponential profits at the loss of others. They can devalue / overvalue for their vested interests. Hence, Who is going to manage? How it is allocated? What kind of reward and penalty system is maintained? and, How is it being managed?, determine the outcome.

On the negative side, it can be used as a tool of suppression by favoring any particular group over another. As well as it can be used as tool of progress and prosperity by providing financial resources to competent and deserving people and promoting developmental projects. As far as a tool of oppression and other negative actions, it is outright evil. Even the good part requires extreme prudence to ensure progress and growth. If not channeled in proper way, it can have adverse repercussions, reverse effect, and create vicious circle. It can have compound effect more on the negative side than the positive. Moreover, it has an inherent inflationary element in it but that can be offset if it is managed professionally and ethically.

Future of Digital & Crypto:

One cannot say with certainty about the future of Crypto currency; for sure it will stay as long as monetary authorities' crackdown on it or they keep overlooking. It largely depends on the founders/ people connections within monetary system/authorities. At this moment, it is highly risky. Three likely possibilities are:

- a. It will become completely defunct.
- b. It will be converted into digital currency where it will be regulated by monetary authorities and will follow procedures, protocols, and other requirements. However, it will not remain fully encrypted and will not remain fully decentralized.
- c. It will remain a speculative tool with limited use and that also till monetary establishment will let it remain so.

Most probably it will stay till digital currency comes into force, then Crypto will merge or just vanish. Crypto at this moment is insignificant and does not have any impact on boom or bust. It can be replaced by fiat and have the same effects as fiat. Authorities are not clear how digital currency will work and are experimenting and figuring out. For now, the impact of all kinds of digital currencies on boom and bust is minimal because the overall volume is insignificant as compared to fiat currency.

Conclusion

In a nutshell, management of fiat currency requires utmost caution in order to get beneficial results. Possibilities of misuse and abuse are immense as these are very difficult to detect in the beginning but worsen by leaps and bounds with time. The monetary system is more of a political matter rather than financial. All faults lie in the fact that the political part of currency is not given proper attention even in general while in academic curriculum it is barely mentioned.

One major failing is that they are presenting it as all good, cure-all solution to monetary matters, without duly highlighting the possible adverse effects. They do not educate masses about the negative effects and provide material for the politicians to exploit and manipulate who are expert in pandering on biases. Besides, when they come in power, they favor their own supporters and vindicate opposition by using fiat money system.

Libertarians were enthusiasts of crypto currency as a way of escaping governmental clutches but in their naivety, they provided solid base to develop and control on all aspects of new digital currency.

The future of crypto currency is bleak, but use of government regulated digital currency is imminent. Currency as a tool of control and power is one of the prime goals of governments and digital currency can serve this purpose much better than fiat currency. There is a great possibility that fiat will be replaced by digital currency with probable merging of Crypto into Digital Currency.

The monetary system is not based on altruism but on hard and crude profitability. However, as a derivative, if used properly, it can help benefit the general welfare of society. Main reason for authorities' interest for adopting digital currency is that they can trace it more effectively than traditional fiat money.