Stripping the mystery from the money markets

Ray Cunningham

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Most people only worry about currency exchange rates when they're changing money for a holiday, but over the last few years, they have become increasingly hard to ignore. Government ministers appear on TV to inform us that interest rates will have to go up or down, or reassure us that, having spent hundreds of millions of pounds, our standing in the ERM is now safe. What are they talking about?

Part of the move towards European integration, indeed, one of the main reasons for this move, is making sure that the value of all the European currencies stays at more or less the same level. If the pound today is worth 5 francs, 100 pesetas, or 1,000 lira, then it should always be worth about 5 francs, 100 pesetas, or 1,000 lira. This is because, if a business is exporting stuff to Germany, it wants to be sure that the 10,000 marks it gets paid is worth as much as when the price was agreed, otherwise it could end up making huge losses.

Speculators

The problem is that the value of a currency depends ultimately on how much other people are willing to pay for it, and that, in turn depends on millions of other things, like the general strength of the economy, that no-one can really control. When, as happened with sterling, speculators (basically the big banks and investment companies) think that the price is too high, they start selling the currency — forcing its price down. To try to keep the price up, governments will increase interest rates, so investors will save their money in that country, or buy as much of the currency as they can.

Naturally, we're the ones who have to pay for all of this. If interest rates go up because of speculators attacking a currency, our mortgages and bank loans become more expensive. When governments use their reserves to buy up currency, they then have to spend the next few years building their reserves back up, which means less public spending and more taxes. And no matter how much of our money the government spends, they still have little chance of fixing the value of the currency.

No-one's in charge

The problem isn't simply one of having the wrong government in power — no matter how 'socialist' the ruling party, they will still be faced with the same situation. If a price for the currency is not fixed, then companies will go out of business, with the attendant loss of jobs, through losses incurred as their payments are changed from one currency to another. (Not to mention the complications in terms of EU membership raised by dropping out of the ERM) On the other hand, because it is not the only player in this game, the state simply isn't in a position to set the price of its money.

Just as manufacturers try to produce the most profitable goods, investment companies and banks are drawn to the most profitable markets. They speculate on currencies because they are trying to make a profit for their shareholders and investors, even if these are the same people who end up losing if a currency is devalued. Whatever happens, they are in the position of enforcers for the 'iron law of the market', and until that 'law' is challenged, we're going to keep going in the same old circles. Capitalism, by its nature, is chaotic. A rational economy requires a new system — anarchism.

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