R_5: Why a dual currency system not inflationary

Increasing the amount of liquidity in an economy under *ceteres paribus* conditions is indeed inflationary. If the amount of goods and services produced stays the same but the amount of money created to buy them increases, then inflation is the consequence. This also seems to be the case when Central Banks increase their base money aggregate (M0). And M0 has in fact been massively inflated over the last two decades by most (if not all) Central Banks worldwide. In addition, aging societies in some advanced economies (where consumption outweighs saving), and further de-globalization associated with a shortage of labor, taken together have the potential to increase the consumer price index (CPI). Whereas M0 increased cyclically over the last 30 years, further monetary aggregates (M1-M3) increased in a linear manner. These monetary aggregates roughly resemble the volume of money that did not enter the real economy, but instead has been parked in bank accounts. Once the monetary regulator has created the money as fiat money, the money is out there (M0), as cash (bills and coins) and as loans on the balance sheets of commercial banks. And once the money is on the balance sheets of the commercial banks, the Central Banks cannot simply sterilize the amount or write it off. Inflation is the inevitable result.

There is some truth to this argument, but only at first glance. If we adopt an overly linear and narrow view of this important topic, we easily overlook further relevant aspects. Empirically, the increase in base money actually is not associated with an increase in the price level. The amount of additional liquidity parked on the balance sheets of the commercial banking sector has caused an increase in the API (asset price index), but not the CPI. There are several factors that would prevent a dual currency system from being inflationary.

These include the fact that the dual mechanism favors regional value chains, which tend to reduce costs such as transportation. Furthermore, it reduces damage costs and generates multiple positive externalities. The broader the overall tax base becomes, the less inflationary this additional liquidity will be. We should be aware that the largest inflator in our conventional economy is the price of oil itself. Any activity that lowers our dependency on the oil price will lower the inflationary pressure on the CPI. Potential inflationary pressure can be countered via an adopted interest rate and the issuing of additional state bonds in the ‘green parallel marketplace’. The initial ratio of consumptive versus investive projects will make it possible for political decision makers to identify the potential inflationary challenges.

In short: currently, we do not assume that collecting additional liquidity through additional taxation, regulating offshore havens, private pledges, ODA, blended

finance or debt relief would be less inflationary than simply generating the amount of liquidity targeted to SDGs through a dual system. Collecting money through conventional channels simply activates unproductive liquidity to finance our future. The same is true of a parallel system. We simply will be creating the money rather than collecting und redistributing it to finance our future. By the way: according to standard monopoly theory, any monopoly reduces the quality and increases the price. This holds true for a monetary monopoly, too.

There is a saying that 50% of economics is applied psychology. In fact, the expectation and the perception of how the CPI will develop in the near future determine whether the price level of the CPI basket is more likely to increase or decrease. If the economic agents anticipate a rise in wages and costs, they will tend to spend their money or request higher wages to cover an expected rise in the CPI. In a world with a dual currency system in place, designed in the way we have been proposing, the expectations and perception of the CPI's future development will rather be that it decreases. A lower dependency on the fossil industry, regional value chains, lower costs for damage control, reduced illicit transactions and reduced black market activities are among the reasons why we expect inflation will actually be lower with a dual currency system. This is why introducing a dual currency system with a targeted, digital, blockchain-associated design in fact operates as an anti-cyclical and anti-inflationary stabilizer.

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