

What discussion there is, is confined almost exclusively to technical factors, such as the impact of gold flows on member-bank reserve positions. While this is as would be expected in the first three editions, it is rather surprising that external objectives are not given more emphasis in the 1961 edition.

Monetary policy or credit policy?—I have thus far been using the term “monetary policy” in its broadest sense, as it is usually used. Within the generic context, however, controversy has long existed as to whether “monetary policy” is or should be concerned directly with money, with credit, or with both. Considerable confusion is apparent on this matter in at least the first three editions of *Purposes and Functions*.

For years quantity theorists have urged that a clear distinction be made between “money” and “credit,” and consequently between “monetary policy” and “credit policy.” To the Chicago school, the volume of money is unique, identifiable, and of crucial significance in spending decisions. It is a legitimate object of government intervention, while credit is not. It remained, however, for Gurley-Shaw and the Radcliffe Report to inculcate an awareness of this distinction in a wider audience.⁶ Ironically, they did this by arguing exactly the opposite: that money is not unique and if central banking is to be effective it must operate directly on a wide spectrum of financial assets. In the process of rushing to the defense of orthodox central banking, many an economist discovered, somewhat painfully, that he was more of a quantity theorist than he had realized.

Technically, “money” refers to the

liability side of commercial bank balance sheets, at least insofar as it consists of demand deposits. “Bank credit” properly refers to the *asset* side of commercial bank balance sheets, to their loans and investments. “Credit” in general refers to lending by *any* economic unit. Now money may be uniquely related to commercial banks, but credit is not; many economic units, financial and non-financial, extend credit (supply loanable funds) besides banks. Thus if the central bank believes its function is to control the money supply, it can logically confine its direct regulation to the commercial banks. However, if it believes its function is to control the extension of credit, then the rationale for confining its regulation to the commercial banks rests on rather shaky foundations.⁷

Throughout the 1939 edition, the System’s responsibilities were described as altering bank reserves in order to regulate both “money and credit.”⁸ It was made clear that “money” referred to currency plus demand deposits, while “credit” referred to *bank* credit, or the asset side of the commercial bank balance sheet. It was also made clear that the concern was twofold because the creation of money stemmed from the extension of bank credit.

In the 1947 edition the concept of regulating both “money and credit” was

⁷ “The supply of credit which can be immediately used for exercising demand is no monopoly of the banks; the power of the banks to create credit (and it is credit, not money, that is relevant here) thus provides no justification for control of the banks while other credit agencies are left uncontrolled” (R. S. Sayers, “Monetary Thought and Monetary Policy in England,” *Economic Journal*, LXX, No. 280 [December, 1960], 714; see also Sayers’ “Alternative Views of Central Banking,” *Economica*, N.S., XXVIII, No. 110 [May, 1961], 111–24).

⁸ I have supplied the emphasis in this and all subsequent quotations that contain italicized words or phrases.

⁶ I am myself indebted to John Dawson, of Grinnell College, and Paul Volcker, of the Chase Manhattan Bank, for the many hours they spent patiently giving me instruction in the new catechism.