

THE CASE AGAINST THE FED

By Professor Murray Rothbard

Reviewed by Zia H Shah MD

Those who devour interest stand like one whom Satan has smitten with insanity. That is so because they keep saying: The business of buying and selling is also like lending money on interest; whereas Allah has made buying and selling lawful and has made the taking of interest unlawful. (Al Quran 2:276)

The fact that the history and ownership of Federal Reserve Bank in this age of information and inquisitiveness is shrouded in mystery bordering onto mysticism, should lend enough credibility to the so called conspiracy theorists. The human condition is, as Plato would make Socrates say in the Republic (7.514a ff.), comparable to that of prisoners of an underground cave, whose unfortunate fate is to confuse reality with passing shadows created by a fire inside their miserable abode and kept in motion by clever manipulators, who in the name of politics, religion, science, and tradition control the human herd.



If you can believe Plato's assertion then you are ready to go on a journey to demystify interest based economic systems. Very few bankers and MBAs and so called financial experts are aware of the status of the Federal Reserve Bank and how the whole system works and as a result in any conversation on this issue they become immediately defensive and have an inherent desire to hide their lack of information. There is a certain mystique and aura that surrounds any discussion of Federal Reserve. For example the Encyclopedia Britannica,

despite offering information on millions of less important subjects does not offer a single word of information on the topic of Federal Reserve and chooses to refer to the official websites of the twelve regional Federal Reserve Banks, that are an integral part of the Federal Reserve Bank. The twelve regional Federal Reserve Banks are not part of the Federal Government, but are 12 private corporations incorporated May 18, 1914.

John Gribbin writes in the first chapter of *Scientists: a History of Science Told through the Lives of Its Greatest Inventors*, "The renaissance was the time when Western Europeans lost their awe of the Ancients and realized that they had as much to contribute to civilization and society as the Greeks and Romans had contributed. To modern eyes, the puzzle is not that this should have occurred, but that it should have taken so long for people to lose their inferiority complex." Today Muslims stand at a similar spot in relation to the interest based Western financial system.

The illusion of prosperity has been created by a web of debt. All Western countries, states, corporations, and individuals in the form of mortgages, student loans and credit card loans owe trillions of dollars to the International Central Bankers. It is not only GM, Chrysler and more than 40 regional banks that have gone bankrupt, since September of 2008, but states and countries appear to be on the brink of bankruptcy. In a July 2009 news item, CNNmoney.com wrote an article titled *California: Teetering closer to junk*. The article stated that the Fitch Ratings downgrades the state's bond rating to BBB, just above junk status. Citing the Golden State's ongoing budget upheaval, Fitch Ratings on Monday downgraded California's long-term debt to BBB, one category above junk bond status. As California legislators haggle over how to close a \$26.3 billion budget deficit, the state is expected to send out \$3.3 billion in IOUs this month to pay its bills to the private contractors, state vendors, and people getting tax refunds and local governments for social services. It is the first time since 1992, and just the second time since the Great Depression, the state has sent out notes promising repayment at a later date instead of paying its bills on time. This is however, the tip of the iceberg in the international drama titled *Smitten by the Satan*.

Bank bailouts and recession-fighting measures will explode the debt of the advanced economies to at least 114 percent of gross domestic product in 2014. Those living in USA may recall that at the time President Bill Clinton left office the national debt stood at approximately 5 trillion dollars now in less than ten years, according to U.S. National debt clock, the Outstanding Public Debt as of 7th July, 2009 at 12:14:21 PM GMT is: \$11,504,844,223,798.72. The estimated population of the United States is 306,503,956 so each citizen's share of this debt is \$37,535.71. **It is projected that by 2019 the debt will balloon to 20 trillion dollars.** It is very plausible that Iraq and Afghanistan wars had something to do with the exploding Federal debt. The National Debt has continued to increase an average of \$3.86 billion per day since September 28, 2007! Concerned? The financial news channel should not be talking about how

many cents a company made in a quarter but of this \$3.86 billion per day. The fact that CNBC and Bloomberg never talk about this should alert the viewers to a doomsday scenario. The four biggest debt holders of the Federal debt, in order, are the Federal Reserve Bank, China, Japan and Mutual Funds. The deficit in the calendar year 2009, that will add to the national debt will be up to 1.85 trillion dollars.

So much about the state and the Federal governments! Now a little glimpse of the businesses: More than 14,000 companies filed for bankruptcy in the first quarter of 2009 according to the American Bankruptcy Institute. Since then, there have been many more bankruptcies, including from some of the most widely-recognized names in corporate America, such as auto companies General Motors and Chrysler, amusement park operator Six Flags and retailer Eddie Bauer.

According to Government figures, in July of 2009, close to 10% of the population in USA is unemployed and that is an understatement as the Government reports only on those who are actively seeking employment. The actual number is 16-17%. It is not only in the jobless numbers or other dismal economic parameters that the analogy of 'smitten by the Satan' becomes befitting; rather it is in the sociopolitical influence that it creates for the Central banks over the Governments and the societies. In this review, however, we will limit ourselves to trying to understand the system only and not the consequences. We no longer have the luxury of burying our proverbial head in the sand. Time is now to understand the financial system, and task may not be as difficult as it seems at the first blush for authors like Professor Murray N. Rothbard make it easy for us. Why is the only superpower in the world in such a dire and sorry state with national debt of more than eleven trillion dollars and majority of the states struggling to keep pace with their budgets? The simple and short answer in two words is 'Federal Reserve,' or briefly in one syllable 'Fed.'

The author, Professor Murray N. Rothbard (1926-1995) was the S.J. Hall distinguished professor of economics at the University of Nevada, Las Vegas, and dean of the Austrian School of economics. He served as vice president for academic affairs at the Ludwig von Mises Institute, was editor of the *Review of Austrian Economics*, and his writings appeared in many journals and publications. Rothbard received his B.S., M.A., and Ph.D. from Columbia University, where he studied under Joseph Dorfman. For more than ten years, he also attended Ludwig von Mises's seminar at New York University. He is the author of thousands of articles, and his 17 books include: *A History of Money and Banking in the United States*; *The Panic of 1819*; *Man, Economy, and State*; *Power and Market*; *America's Great Depression*; *The Mystery of Banking*; *For a New Liberty*; *The Ethics of Liberty*; the four-volume *Conceived in Liberty*; the two-volume *Logic of Action*; and the two-volume *An Austrian Perspective on the History of Economic Thought*.

To understand the concept of Fed we need to first have a concept of what is money?

WHAT IS MONEY ANYWAYS

In another of his books, *What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar*, Murray N. Rothbard has in very simple language explained the concept of money starting from the early barter system. Before the moneys were invented barter system was in vogue. If someone had surplus eggs and wanted sheep he could exchange these with some one who had surplus sheep. But what if the person with surplus sheep did not need eggs? This is an issue expressed in economics as 'coincidence of wants.' Invention of money was a solution to this problem. When the monetary system was first invented several commodities were used as money in different societies. Rothbard writes:

"Historically, many different goods have been used as media: tobacco in colonial Virginia, sugar in the West Indies, salt in Abyssinia, cattle in ancient Greece, nails in Scotland, copper in ancient Egypt, and grain, beads, tea, cowrie shells, and fishhooks. Through the centuries, two commodities, gold and silver, have emerged as money in the free competition of the market, and have displaced the other commodities. Both are uniquely marketable, are in great demand as ornaments, and excel in the other necessary qualities. In recent times, silver, being relatively more abundant than gold, has been found more useful for smaller exchanges, while gold is more useful for larger transactions. At any rate, the important thing is that whatever the reason, the free market has found gold and silver to be the most efficient moneys."¹

We have learned that all money has originated, and must originate, in a useful commodity chosen by the free market as a medium of exchange. The unit of money is simply a unit of weight of the monetary commodity-usually a metal, such as gold or silver. Under freedom, the commodities chosen as money, their shape and form, are left to the voluntary decisions of free individuals. Private coinage, therefore, is just as legitimate and worthwhile as any business activity. Gold is simply a commodity. It differs from other commodities in being demanded mainly as a medium of exchange. But aside from this, it is a commodity and like all commodities, it has an existing stock, it faces demands by people to buy and hold it, etc. Like all commodities, its 'price' in terms of other goods is determined by the interaction of its total supply, or stock, and the total demand by people to buy and hold it. People 'buy' money by selling their goods and services for it, just as they 'sell' money when they buy goods and services. So what is the benefit of having money rather than a simple barter system? Murray N. Rothbard writes:

"The emergence of money was a great boon to the human race. Without money--without a general medium of exchange--there could be no real specialization, no advancement of the economy above a bare, primitive level. With money, the problems of indivisibility and 'coincidence of wants' that plagued the barter society all vanish."²

The 'price' of money is its purchasing power in terms of all goods in the economy, and this is determined by its supply, and by every individual's demand for money. Any attempt by government to fix the price will interfere with the satisfaction of people's demands for money. If people find it more convenient to use more than one metal as money, the exchange rate between them on the market will be determined by the relative demands and supplies, and will tend to equal the ratios of their respective purchasing power. As long as all the countries were following the gold standard there was a common sense and easily understandable method of exchange. Murray N. Rothbard writes:

"It is obvious that the size of the common unit chosen in trading makes no difference to the economist. One country, on the metric system, may prefer to figure in grams; England or America may prefer to reckon in grains or ounces. All units of weight are convertible into each other; one pound equals sixteen ounces; one ounce equals 437.5 grains or 28.35 grams, etc.

Assuming gold is chosen as the money, the size of the gold-unit used in reckoning is immaterial to us. Jones may sell a coat for one gold ounce in America, or for 28.35 grams in France; both prices are identical.

All this might seem like laboring the obvious, except that a great deal of misery in the world would have been avoided if people had fully realized these simple truths. Nearly everyone, for example, thinks of money as abstract units for something or other, each cleaving uniquely to a certain country. Even when countries were on the 'gold standard,' people thought in similar terms. American money was 'dollars,' French was 'francs,' German 'marks,' etc. All these were admittedly tied to gold, but all were considered sovereign and independent, and hence it was easy for countries to 'go off the gold standard.' Yet all of these names were simply names for units of weight of gold or silver."³

Once there is enough supply of a metal to permit the market to choose it as money, no increase in supply can improve its monetary function. An increase in money supply will then merely dilute the effectiveness of each ounce of money without helping the economy. An increased stock of gold or silver, however, fulfills more non-monetary wants (ornament, industrial purposes, etc.) served by the metal, and is therefore socially useful. But money differs from other commodities in one essential fact. And grasping this difference furnishes a key to understanding monetary matters. When the supply of any other good increases, this increase confers a social benefit; it is a matter for general rejoicing. More consumer goods mean a higher standard of living for the public; more capital goods mean sustained and increased living standards in the future. The discovery of new, fertile land or natural resources also promises to add to living standards, present and future. But what about money? Does an addition to the money supply also benefit the public at large? Murray N. Rothbard answers the question:

"What would happen if overnight, some good fairy slipped into pockets, purses, and bank vaults, and doubled our supply of money. In our example, she magically doubled our supply of gold. Would we be twice as rich? Obviously not. What makes us rich is an abundance of goods, and what limits that abundance is a scarcity of resources: namely land, labor, and capital. Multiplying coin will not whisk these resources into being. We may feel twice as rich for the moment, but clearly all we are doing is diluting the money supply. As the public rushes out to spend its new-

found wealth, prices will, very roughly, double-or at least rise until the demand is satisfied, and money no longer bids against itself for the existing goods.

Thus, we see that while an increase in the money supply, like an increase in the supply of any good, lowers its price, the change does not--unlike other goods--confer a social benefit. The public at large is not made richer. Whereas new consumer or capital goods add to standards of living, new money only raises prices; i.e., dilutes its own purchasing power. The reason for this puzzle is that money is only useful for its exchange value."⁴

THE PRIVILEGED POSITION OF THE FEDERAL RESERVE

Federal Reserve Bank is the Central Bank for USA. According to the Encyclopedia Britannica:

"Central Banks are institutions, such as the Bank of England, the U.S. Federal Reserve System, or the Bank of Japan, that is charged with regulating the size of a nation's money supply, the availability and cost of credit, and the foreign-exchange value of its currency. Regulation of the availability and cost of credit may be nonselective or may be designed to influence the distribution of credit among competing uses. The principal objectives of a modern central bank in carrying out these functions are to maintain monetary and credit conditions conducive to a high level of employment and production, a reasonably stable level of domestic prices, and an adequate level of international reserves."⁵

But, Federal Reserve in some ways is unique and may be different from Central Banks of other countries, as it is privately owned. In addition to the central office it also comprises of the twelve regional Federal Reserve Banks that are not part of the Federal Government, but are 12 private corporations incorporated May 18, 1914. According to Wikipedia, "These twelve regional banks are organized much like private corporations—possibly leading to some confusion about 'ownership.'" It is a quasi-private and quasi-public organization. Wikipedia explains it further:

"The Federal Reserve Banks issue shares of stock to member banks. However, owning Federal Reserve Bank stock is quite different from owning stock in a private company. The Federal Reserve Banks are not operated for profit, and ownership of a certain amount of stock is, by law, a condition of membership in the system. The stock may not be sold or traded or pledged as security for a loan; dividends are, by law, limited to 6 percent per year."⁶

It is said that no body is above the law not even the Presidents of USA, but some organizations and by proxy their owners are above the law. This may turn out to be an understatement the more you learn about Federal Reserve and other central banks. It is also said that our government in USA as designed by the founding fathers is a system of checks and balances. But not true in the case of Federal Reserve! Murray N Rothbard succinctly summarizes the privileged position of the Federal Reserve in the first two paragraphs of the introduction to his book *the Case against the Fed*:

By far the most secret and least accountable operation of the federal government is not, as one might expect, the CIA, DIA, or some other super-secret intelligence agency. The CIA and other intelligence operations are under control of the Congress. They are accountable: a Congressional committee supervises these operations, controls their budgets, and is informed of their covert activities. It is true that the committee hearings and activities are closed to the public; but at least the people's representatives in Congress insure some accountability for these secret agencies.

It is little known, however, that there is a federal agency that tops the others in secrecy by a country mile. The Federal Reserve System is accountable to no one; it has no budget; it is subject to no audit; and no Congressional committee knows of, or can truly supervise, its operations. The Federal Reserve, virtually in total control of the nation's vital monetary system, is accountable to nobody-and this strange situation, if acknowledged at all, is invariably trumpeted as a virtue.⁷

This is what the official website of Federal Reserve has to say about this issue:

"The Federal Reserve is structured to be independent within the federal government. The Federal Reserve System follows its Congressional charter; the Chairman of the Board of Governors reports to Congress; but the Fed's decisions are independent of both the Congress and the President of the United States — hence the phrase independent within the government."⁸

As the White House raised its 10-year cumulative budget deficit projection by \$2 trillion on August 25, 2009 to approximately \$9 trillion; that would push the national debt up from more than \$11 trillion now to more than \$20 trillion in 2019; joining President Barack Obama in a school hall in the town of Oak Bluffs, Ben Bernanke, Federal Reserve Chairman, shook hands with the President before praising his support for a strong and 'independent' Federal Reserve. Such statements lend support to what Rothbard has to say about the privileged position of the Federal Reserve.

FRACTIONAL RESERVE BANKING

Prior to the 1800s, savers looking to keep their valuables in safekeeping depositories deposited gold coins and silver coins at goldsmiths, receiving in turn a note for their deposit. Once these notes became a trusted medium of exchange an early form of paper money was born, in the form of the goldsmiths' notes. As the notes were used directly in trade, the goldsmiths observed that people would not usually redeem all their notes at the same time, and they saw the opportunity to invest their coin reserves in interest-bearing loans and bills. This generated income for the goldsmiths but left them with more notes on issue than reserves to pay them with. A process was started that altered the role of the goldsmiths from passive guardians of bullion, charging fees for safe storage, to interest-paying and interest-earning banks. Thus fractional-reserve banking was born. However, if creditors (note holders of gold originally deposited) lost faith in the ability of a bank to redeem (pay) their notes, many would try to redeem their notes at the same time. If in response a bank could not raise enough funds by calling in loans or selling bills, it either went into insolvency or defaulted on its notes. Such a situation is called a bank run and caused the demise of many early banks. Repeated bank failures and financial crises lead to the creation of central banks. In many countries the central banks are government institutions that oversee and regulate commercial banks, impose reserve requirements, and act as lender-of-last-resort if a bank is low on liquidity.



By its nature, the practice of fractional reserve banking expands money supply (cash and demand deposits) beyond what it would otherwise be. Because of the prevalence of fractional reserve banking, the broad money supply of most countries is a multiple larger than the amount of base money created by the country's central bank. That multiple (called the money multiplier) is determined by the reserve requirement or other financial ratio requirements imposed by financial regulators. Fractional reserve banking is perhaps the most important factor influencing money supply in any country.

According to Rothbard:

“Government paper, as pernicious as it may be, is a relatively straightforward form of counterfeiting. The public can understand the concept of ‘printing dollars’ and spending them, and they can understand why such a flood of dollars will come to be worth a great deal less than gold, or than uninflated paper, of the same denomination, whether ‘dollar,’ ‘franc,’ or ‘mark.’ Far more difficult to grasp, however, and therefore far more insidious, are the nature and consequences of ‘fractional-reserve banking,’ a more subtle and modern form of counterfeiting. It is not difficult to see the consequences of a society awash in a flood of new paper money; but it is far more difficult to envision the results of an expansion of intangible bank credit.”⁹

WHO HAS MONOPLY OVER THE PRINTING OF MONEY

Murray N Rothbard explains in a very lucid and simple manner:

“Having examined the nature of fractional reserve and of central banking, and having seen how the questionable blessings of Central Banking were fastened upon America, it is time to see precisely how the Fed, as presently constituted, carries out its systemic inflation and its control of the American monetary system.

Pursuant to its essence as a post-Peel Act Central Bank, the Federal Reserve enjoys a monopoly of the issue of all bank notes. The U. S. Treasury, which issued paper money as Greenbacks

during the Civil War, continued to issue one-dollar 'Silver Certificates' redeemable in silver bullion or coin at the Treasury until August 16, 1968. The Treasury has now abandoned any note issue, leaving all the country's paper notes, or 'cash,' to be emitted by the Federal Reserve. Not only that; since the U.S. abandonment of the gold standard in 1933, Federal Reserve Notes have been legal tender for all monetary debts, public or private.

Federal Reserve Notes, the legal monopoly of cash or 'standard' money, now serves as the base of two inverted pyramids determining the supply of money in the country. ...

Of course, the Fed can print at will. Unlike the days of the gold standard, it is impossible for the Federal Reserve to go bankrupt; it holds the legal monopoly of counterfeiting (of creating money out of thin air) in the entire country."¹⁰

A note issued by a central bank, such as the Federal Reserve Note, is bank currency. These notes are given to the government in exchange for an interest-bearing government bond. The primary means to pay for the interest on these bonds is to borrow more bank notes, thus beginning a vicious cycle that ultimately ends with the complete destruction of the currency and bankruptcy of the nation. History is replete with such occurrences. Ellen Hodgson Brown JD writes in the introduction section of her well researched book, *the Web of Debt*.

"At one time, the right to issue money was the sovereign right of the king; but that right got usurped by private moneylenders. Today the sovereigns are the people, and the coins that make up less than one one-thousandth of the money supply are all that are left of our sovereign money. Many nations have successfully issued their own money, at least for a time; but the bankers' debt-money has generally infiltrated the system and taken over in the end. These concepts are so foreign to what we have been taught that it can be hard to wrap our minds around them, but the facts have been substantiated by many reliable authorities."¹¹

HOW THE MONEY SUPPLY IS INCREASED OR DECREASED

It is fairly simple to understand the money supply once one is willing to trust one's intelligence and wisdom and is able to discard the numerous smoke screens that are put out there. Federal Reserve Bank is the main central bank for US and buck literally stops there. They are the sole and the ultimate controllers of the money supply.

If the Fed purchases any asset, therefore, it will increase the nation's money supply immediately by that amount; and, in a few weeks, by whatever multiple of that amount the banks are allowed to pyramid on top of their new reserves. Let me repeat that so the reader can memorize this fundamental fact that when Fed purchases an asset the money supply increases and conversely if Fed sells an asset the money supply decreases. If it sells any asset (again, generally U.S. government bonds), the sale will have the symmetrically reverse effect. At first, the nation's money supply will decrease by the precise amount of the sale of bonds; and in a few weeks, it will decline by a multiple, say ten times, that amount. Thus, the major control instrument that the Fed exercises over the banks is 'open market operations,' purchases or sale of assets, generally U.S. government bonds. Another powerful control instrument is the changing of legal reserve minima. If the banks have to keep no less than 10 percent of their

deposits in the form of reserves, and then the Fed suddenly lowers that ratio to 5 percent, the nation's money supply, that is of bank deposits, will suddenly and very rapidly double. And vice versa if the minimum ratio were suddenly raised to 20 percent; the nation's money supply will be quickly cut in half. Ever since the Fed, after having expanded bank reserves in the 1930s, panicked at the inflationary potential and doubled the minimum reserve requirements to 20 percent in 1938, sending the economy into a tailspin of credit liquidation, the Fed has been very cautious about the degree of its changes in bank reserve requirements. The Fed, ever since that period, has changed bank reserve requirements fairly often, but in very small steps, by fractions of one percent. It should come as no surprise that the trend of the Fed's change has been downward: ever lowering bank reserve requirements, and thereby increasing the multiples of bank credit inflation. Thus, before 1980, the average minimum reserve requirement was about 14 percent, then it was lowered to 10 percent and less, and the Fed now has the power to lower it to zero if it so wishes.¹² These are the two fundamentally important ways for Fed to increase or decrease the money supply, the rest is smoke screen or petty change.

Every two months the over night interest rate for borrowing between banks is announced with much fanfare after the meetings of the Federal Reserve bankers. However, this is like the stroke of goldsmith as compared to the prior two major factors that are akin to the bold and powerful stroke of the blacksmith. Fed could buy any assets and value them at any price it so desires. For example, Shobhana Chandra and Kristy Scheuble reported for Bloomberg.com on August 12, 2009, "The anticipated expansion in the coming year won't be enough to prevent the unemployment rate from reaching 10 percent for the first time since 1983, the survey also showed. That will force the Federal Reserve to forego raising its benchmark interest rate until the third quarter of 2010, according to the median projection. The Fed's policy-setting Open Market Committee will today keep the target rate at zero to 0.25 **percent and retain plans to buy as much as \$1.45 trillion of housing debt by year-end to help secure a recovery.**"¹³ All the facts mentioned are petty details except for the fact that Fed will buy, '\$1.45 trillion of housing debt.' Assuming that all this purchase is from the banks, the money supply will as a result increase by several times, as outlined by the principle of 'fractional reserve banking.' In other words, Fed can choose to buy from the commercial banks what has been labeled as 'toxic assets,' during the down turn of 2008 and 2009. To quote from the source directly, here is a quote from the Fed Statement Following August 2009 Meeting:

"As previously announced, to provide support to mortgage lending and housing markets and to improve overall conditions in private credit markets, the Federal Reserve will purchase a total of up to \$1.25 trillion of agency mortgage-backed securities and up to \$200 billion of agency debt by the end of the year. In addition, the Federal Reserve is in the process of buying \$300 billion of Treasury securities."¹⁴

As all banks are highly leveraged they are extremely vulnerable to collapse in any downturn. So, Fed in fact chooses during those times to let some sink and salvage others based on its own sweet will. No one can notice as the records of Fed are for their consumption only. In 2009 alone 75 different banks of different sizes went bankrupt.

When the money supply is increased the businesses grow, new companies pop up and prices creep up, what is called inflation. When the money supply is decreased the artificially created bubbles burst and the vulnerable companies go bankrupt but this decrease in supply is carefully engineered to avoid deflation which is an enemy of the Central Bankers.

WHY WOULD FED INCREASE OR DECREASE THE MONEY SUPPLY

Before the reasons are outlined let me quote from the Founding Fathers of USA. President Thomas Jefferson once said:

“I believe that banking institutions are more dangerous than standing armies ... If the American people ever allow private banks to control the issue of their currency, first by inflation, then by deflation, the banks and the corporations which grow up around them will deprive the people of all property until their children wake up homeless on the continent their fathers conquered.”

‘The colonies,’ said Benjamin Franklin in his autobiography, ‘would gladly have borne the little tax on tea and other matters had it not been that England took away from the colonies their money, which created unemployment and dissatisfaction. The inability of the colonies to get the power to issue their own money permanently out of the hands of George III and international bankers was the prime reason for the revolution.’ The money supply is increased or decreased to create business cycles of boom and bust. Sometimes the increase in money supply can be limited to particular industries or regions to develop or restrain specific industries or locations.

INTEREST BASED ECONOMIES AND WARS

Hadhrat Mirza Tahir Ahmad ^{rt}, the fourth successor to the Promised Messiah ^{as} writes in his book *Islam’s response to the contemporary issues*:

“The warning about a war from God in the verses just cited (2:279-280) means that the laws of nature governed by God would begin to punish the capitalist society when the factors which have been discussed earlier ultimately lead man to economic imbalance and warfare. Disorders, disturbances and wars always follow exploitation and usurpation of the rights of the poor. We warn you about a war with God and His Messenger means that the state, which thrives on interest, would inevitably end up in a situation where the nations will rise in arms against each other.

Time does not permit me to elaborate this aspect of interest. In the Holy Quran, verses prohibiting interest always follow verses on warfare. This indicates the inter-relation of interest and war. Those who are familiar with the history of the First and Second World Wars would remember that capitalism played a disastrous role in not only causing but also prolonging those wars.”^{15 16}

A careful study of economic literature and history of economics in the last two centuries will afford numerous links between interest based economies and wars. In this book by Professor Murray Rothbard *the case against the Fed* we find at least two mentions of such association:

“As luck would have it, the new Federal Reserve System coincided with the outbreak of World War I in Europe, and it is generally agreed that it was only the new system that permitted the US. to enter the war and to finance both its own war effort, and massive loans to the allies; roughly, the Fed doubled the money supply of the U.S. during the war and prices doubled in consequence. For those who believe that U.S. entry into World War I was one of the most disastrous events for the U.S. and for Europe in the twentieth century, the facilitating of U.S. entry into the war is scarcely a major point in favor of the Federal Reserve.”¹⁷

And again:

“During World War I, Benjamin Strong promptly used his dominance over the banking system to create a doubled money supply so as to finance the U. S. war effort and to insure an Anglo-French victory. All this was only prelude for a Morgan-installed monetary and financial policy throughout the 1920s. During the decade of the twenties, Strong collaborated closely with the Governor of the Bank of England, Montagu Norman, to inflate American money and credit so as to support the return of Britain to a leading role in a new form of bowdlerized gold standard, with Britain and other European countries fixing their currencies at a highly over-valued par in relation to the dollar or to gold. The result was a chronic export depression in Britain and a tendency for Britain to lose gold, a tendency that the United States felt forced to combat by inflating dollars in order to stop the hemorrhaging of gold from Great Britain to the U.S.”¹⁸

THE PRESENT STATE OF AFFAIRS

Murray Rothbard summarizes the situation in this ominous note:

“The other major monetary change accomplished by the New Deal, of course, and done under cover of a depression ‘emergency’ in the fractional reserve banking system, was to go off the gold standard. After 1933, Federal Reserve Notes and deposits were no longer redeemable in gold coins to Americans; and after 1971, the dollar was no longer redeemable in gold bullion to foreign governments and central banks. The gold of Americans was confiscated and exchanged for Federal Reserve Notes, which became legal tender; and Americans were stuck in a regime of fiat paper issued by the government and the Federal Reserve. Over the years, all early restraints on Fed activities or its issuing of credit have been lifted; indeed, since 1980, the Federal Reserve has enjoyed the absolute power to do literally *anything* it wants: to buy not only U.S. government securities but any asset whatever, and to buy as many assets and to inflate credit as much as it pleases. **There are no restraints left on the Federal Reserve. The Fed is the master of all it surveys.**”¹⁹

EPILOGUE

Sometimes it is claimed that the real problem may be the debt and not interest. But why would anyone want to loan out large sums of real money backed by gold, if it were not collecting interest. Murray N. Rothbard concludes one of his

books, *What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar*, with the following words,

"For someone must propagate the truth in society, as opposed to what is politically expedient. If scholars and intellectuals fail to do so, if they fail to expound their convictions of what they believe the correct course to be, they are abandoning truth, and therefore abandoning their very *raison d'être*. All hope of social progress would then be gone, for no new ideas would ever be advanced nor effort expended to convince others of their validity."²⁰

So, what is the fundamental truth that Rothbard wants to preach? Advocating The 100 Percent Gold Tradition he writes:

"I therefore advocate as the soundest monetary system and the only one fully compatible with the free market and with the absence of force or fraud from any source a **100 percent gold standard**. This is the only system compatible with the fullest preservation of the rights of property. It is the only system that assures the end of inflation and, with it, of the business cycle? And it is the only form of gold standard that fully meets the following argument of the Douglas subcommittee against a return to gold: An overriding reason against making gold coin freely available is that no government [or banks?] should make promises. ... which it would not be able to keep if the demand should arise. Monetary systems for over a century. ... have expanded more rapidly than would be permitted by accretions of gold."²¹

The eventual elimination of the term 'dollar,' using only terms of weight such as 'gold gram' or 'gold ounce.' The ultimate goal would be the return to gold by every nation, at 100 percent of its particular currency, and the subsequent blending of all these national currencies into one unified world gold-gram unit. This was one of the considered goals at the abortive international monetary conferences of the late nineteenth century.²² In such a world, there would be no exchange rates except between gold and silver, for the national currency names would be abandoned for simple weights of gold, and all the world's money would at long last be freed from strangle hold of 'interest' seeking bankers. President Abraham Lincoln paid much of the cost of the Civil War with Government-issued debt free money, the greenbacks. In other words he understood the monetary principles and took debt and interest out of the monetary policy of the Government. To state the obvious, no Bankers would be interested in controlling or issuing money if they cannot collect interest on it. An interest free or debt free money that is in keeping with the Islamic ideals fixes this problem. To learn from his authority and experience, here are the words attributed to Abraham Lincoln:

"The government should create, issue and circulate all the currency and credit needed to satisfy the spending power of the government and the buying power of consumers. The privilege of creating and issuing money is not only the supreme prerogative of Government, but it is the Government's greatest creative opportunity. By the adoption of these principles, the long-felt want for a uniform medium will be satisfied. The taxpayers will be saved immense sums of interest, discounts and exchanges. The financing of all public enterprises, the maintenance of stable government and ordered progress, and the conduct of the Treasury will become matters of practical administration. The people can and will be furnished with a currency as safe as their

own government. Money will cease to be the master and become the servant of humanity. Democracy will rise superior to the money power.”

Murray Rothbard concludes his book *the case against the Fed* in the following words:

“One great advantage of this plan is its simplicity, as well as the minimal change in banking and the money supply that it would require. Even though the Fed would be abolished and the gold coin standard restored, there would, at this point, be no outlawry of fractional-reserve banking. The banks would therefore be left intact, but, with the Federal Reserve and its junior partner, federal deposit insurance, abolished, the banks would, at last, be on their own, each bank responsible for its own actions. There would be no lender of last resort, no taxpayer bailout. On the contrary, at the first sign of balking at redemption of any of its deposits in gold, any bank would be forced to close its doors immediately and liquidate its assets on behalf of its depositors. A gold-coin standard, coupled with instant liquidation for any bank that fails to meet its contractual obligations, would bring about a free banking system so ‘hard’ and sound, that any problem of inflationary credit or counterfeiting would be minimal. It is perhaps a ‘second-best’ solution to the ideal of treating fractional-reserve bankers as embezzlers, but it would suffice at least as an excellent solution for the time being, that is, until people are ready to press on to full 100 percent banking.”²³

So if the USA Government takes on the responsibility of controlling money supply that originally belonged to it in the constitution the Federal Government or the State Governments will not be in the sorry state that they are in at present. In a Government owned monetary system even if interest related issues were not immediately sorted out, conceptually they will not be much different from taxation and hence in keeping with the Islamic ideal wherein interest is prohibited.

When a democracy owes trillions of dollars, approaching 12 trillion to date, several times the actual annual budget of USA, before the deficit spending, to the Central Bankers, then it has for all practical purposes changed into a plutocracy, government by and for the few rich. In such a situation the social and the political matters are not decided by the popular vote or by the principles of fairness but for the benefit of the rich who are in charge. This is perhaps why the Holy Quran describes interest based economy as ‘a war with Allah and His Messenger.’

O Ye who believe, be mindful of your duty to Allah and relinquish your claim to what remains of interest, if you are truly believers. But if you do it not, then beware of war from the side of Allah and His Messenger. If, however, you desist you will still have your capital sums; thus you will commit no wrong, nor suffer any wrong yourselves. (Al Quran 2:279-280)

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- ¹ Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Pages 26-27.
- ² Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Page 28.
- ³ Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Page 30-31.
- ⁴ Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Page 40-41.
- ⁵ "central bank." Encyclopædia Britannica. 2009. Encyclopædia Britannica Online. 05 Aug. 2009 <<http://www.britannica.com/EBchecked/topic/102342/central-bank>>.
- ⁶ "The Founding of the Fed." FEDERAL RESERVE BANK of NEW YORK. 24 Mar. 2009 <<http://www.newyorkfed.org/>>.
- ⁷ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 3.
- ⁸ <http://www.federal-reserve.org/>
- ⁹ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 29-30.
- ¹⁰ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 137-139.
- ¹¹ <http://www.webofdebt.com/excerpts/introduction.php>
- ¹² Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 143-144.
- ¹³ <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=am1k9zt0.A60>
- ¹⁴ <http://blogs.wsj.com/economics/2009/08/12/fed-statement-following-august-meeting/>
- ¹⁵ Hadhrat Mirza Tahir Ahmad. Islam's response to the contemporary issues. Islam International Publication Ltd, 2007, Page 189.
- ¹⁶ <http://www.alislam.org/library/books/IslamsResponseToContemporaryIssues.pdf>
- ¹⁷ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 120.
- ¹⁸ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 129.
- ¹⁹ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 132.
- ²⁰ Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Pages 186.
- ²¹ Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Pages 176-177.
- ²² Murray N. Rothbard. What Has Government Done to Our Money? Case for the 100 Percent Gold Dollar. Ludwig Von Mises Institute, 2005. Pages 184-185.
- ²³ Murray N Rothbard. The case against the Fed. Ludwig Von Mises Institute, 2007. Pages 150-151.