
Money: A Historical Look

TYPES OF MONEY: COMMODITY, SPECIE, FIAT

MONEY AND WORLD TRADE, POWER, AND TECHNOLOGY

THE EVOLUTION OF MONEY IN CANADA

THE EVOLUTION OF BANKING IN CANADA

CENTRALIZING AND ORGANIZING MONEY IN CANADA

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TYPES OF MONEY: COMMODITY, SPECIE, FIAT

Today, our money has little, if any, value in and of itself. Our paper currency really only has value in terms of what we can acquire with it. The coins aren't worth much either. There isn't 10 cents worth of silver in our ten-cent piece or 5 cents worth of nickel in our five-cent piece. The coins are worth more in terms of what they can acquire (their purchasing power) than they are in terms of their metal value (their intrinsic value). This is probably just as well, or people would be melting down the coinage for its value.

This hasn't always been the case. At one time, money did have value in and of itself. Let's introduce some terminology to help us understand the differences in types of money.

An object used as money may have intrinsic value, that is, value because of its inherent usefulness. Over the course of history, a variety of objects have served as money. When an object is used as money, it is referred to as commodity money. If we decided to use compact discs as money, the CDs would be a form of commodity money. (Pause and think for a moment whether or not CDs could serve as money according to the criteria discussed in the first background reading.)

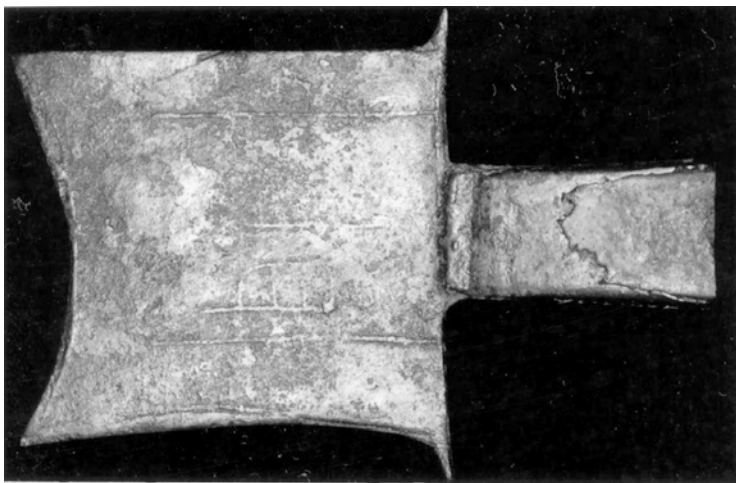
When money isn't an object but, rather, is made from one of the precious metals such as silver or gold, it is called specie money. A silver dollar that contains about a dollar's worth of silver is specie money.

When something is used as money, but only represents value without having value in and of itself, it is called fiat money. Our \$10 bill can acquire \$10 worth of goods and services. But the piece of paper that serves as that \$10 bill is not worth \$10. Instead, it represents \$10 worth of purchasing power. It is fiat money.

The distinction between commodity money, specie money, and fiat money is important. In the early days of money, people were very skeptical about accepting an object that only represented value and wasn't valuable in and of itself. Think how willing you might have been a few thousand years ago to accept as payment a piece of paper with a picture and a 10 on it. A willingness to accept something that represents value requires a significant amount of faith, something that early users of money didn't have. As we learn about the history

and evolution of money, we will see that events took place that increased people's willingness to accept fiat money. And it is a good thing they did, or our economy today might be in some trouble. (Think about why.)

It is not known for certain, but many believe, that the use of money, in the form of commodity money, began in China. Since it was considered very important that money be worth something in and of itself, the Chinese chose tools. Tools had value, and they became valuable as a form of money serving as both a medium of exchange and a store of value. The tools represented a form of commodity money. The Chinese later switched to using metal coins (specie) but, true to their



Hollow Handle Spade, Chou Dynasty, 580-476BC, China. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.

past, they made the coins in the shape of tools. Hence, spade money evolved in China—money that looked like a little shovel or spade.

Beads, shells, cattle, and many other commodities have served as money in various societies in the past. However, it was much more common for the earlier civilizations to use specie money, some form of metal such as gold or silver.

In the time of the ancient Greeks, the Greeks used primarily gold and silver coins as their form of money. The Greek coins were probably the first form of money to be used internationally for trading between different countries. Before that, money was used in the area or country of origin and not regarded as a medium of exchange by other countries. But the conquests of Alexander the Great between 334 BC and 324 BC spread the use and acceptance of Greek coinage.

The acceptance of Greek coins as money in other countries reflected the expanded economic activity that was occurring in the world. Trade between nations was expanding, and traders in different countries needed a way to settle accounts. The Greek civilization led the way in this respect.

Not surprisingly, the nations that came into positions of world dominance militarily were the same ones that became dominant economically. For example, with the rise of the Roman Empire, Roman coins came to replace Greek coins as the money used in trade between nations.

The Roman coins were quite militaristic in design. This reflected the importance of military strength and activity in Roman society. Because the Romans used bronze in their weapons, early Roman coins tended to be bronze. Eventually they began to mint a silver coin called a denarius. This was worth 10 bronze coins and was considered to have the value of a day's pay for a skilled tradesman.

In many ways, coins came to reflect the state of a society, particularly in these earlier civilizations. As the Roman Empire began to decline, less and less silver was used in the silver coins, reflecting the deteriorating state of its economic power. The coins evolved to where they were made out of copper and were silver-plated. Finally, toward the end of the Empire, they were made totally out of bronze.

Many years later, as England was rising to be a world power, early coins minted in England reflected the Roman influence there. The coins were similar in appearance and design to the Roman denarius. As England became more militarily and economically developed, English coins came to be accepted as money on the European continent, helped by the fact that their weight and fineness were known quantities. The history of money, as we can see, can reveal much about history itself.

The acceptance in other countries of the coinage of various world powers is a reflection of the fundamental characteristic that is required for any object to serve as money—people must be willing to accept it. What better money to accept than the coinage of the current world power? Hence, Greek coins were widely accepted during the period of Greek strength and dominance, Roman coins during the period of the Roman Empire, and British coins as the British Empire began to develop. Today, the currency of the United States is used widely in international exchange, reflecting its global position.

Over the course of history, as nations set to sea and developed more and

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Noble, Edward III, 1351-1361, England. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa. (A hammered coin)



Gold Louis, Louis XIV, 1670, France. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa. (A pressed coin)

more trade, the world economy flourished. To support the significant increase in transactions, more and more money was required. We can see how the use of commodity money could have become more and more difficult, depending on the “commodity” used for money. Problems could arise in terms of quantity, portability, and widespread acceptance. Therefore, as commerce expanded, there was a tendency to make more extensive use of metal coins (specie money) and less use of commodity money.

But, over time, other changes occurred in money. The Renaissance brought improvements in technology. In the past, coins had been hammered. The invention of the screw press resulted in more stylized coins, more consistency and standardization in their production, and more security codings being placed on coins to inhibit counterfeiting. Coins became much more ornate and artistic. The better quality coinage, and the improved standardization made possible by the new technology, also helped to increase the widespread acceptance of money.

At the same time, as people throughout the world became more used to money and the acceptability of specific coins, there was less concern about the intrinsic value of the coins. People were increasingly willing to accept that a particular coin might be worth more in terms of what it could buy than in terms of its intrinsic value.

As a note of interest, a large silver coin called the taler was minted in Bohemia. In Holland, a coin of this size was called a daalder. This became dollar in English and was the popular term for the Spanish eight reale piece. Hence, the origin of the term we use today in Canada.

The coins of two major exploring and trading nations, England and Spain, eventually came to be used throughout the world. In the early settlement days of what was to be Canada, Spanish dollars were widely used. As our journey through history brings us to the time of European settlement in Canada, let’s look more closely at the evolution of money specifically in Canada.

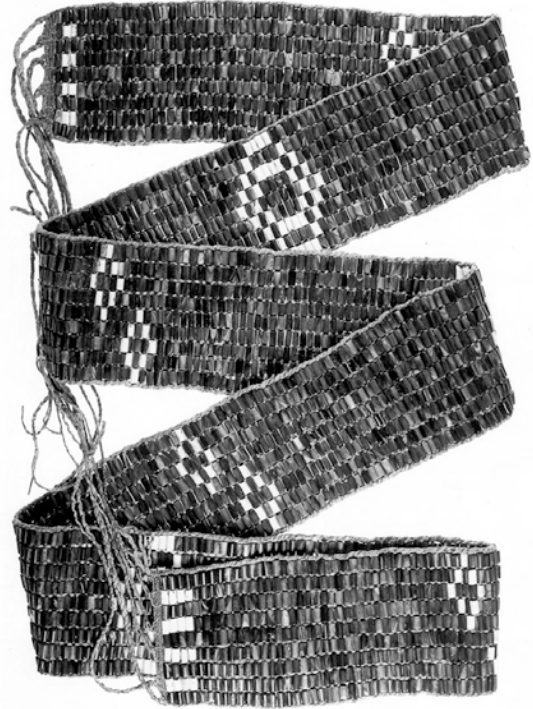
THE EVOLUTION OF MONEY IN CANADA

Early European settlers to Canada used commodity money. Furs, in particular, became a major form of money—being accepted as a medium of exchange. Furs were not the only commodity to be used as a form of money for exchange. Prior to the arrival of the Europeans, an economy operated among the aboriginal people. In that economy, one form of commodity money was shells, which were strung as beads. Wampum, the Algonkian word for them, was not actually exchanged that frequently among the Indians. It served more as a store of value. It could, however, be exchanged to settle large-scale debts, particularly between villages and tribes.

One interesting point to note is that wampum had served the Indians effectively as a form of money until the Europeans arrived. It ceased to serve as money soon after their arrival because the Europeans found that they could produce counterfeit wampum. In doing so, they increased the supply and destroyed the value of wampum and its usefulness among the Indians as money.

The value of an item that served as a medium of exchange was not constant in all areas. Because commodities were initially used as the medium of exchange and had some intrinsic value, their value was subject to the laws of supply and demand. For example, furs were more valuable in the Prairie regions than in central regions because fur-bearing animals were less common there. Shells had more value inland than they did by the sea, again because they were less common inland.

Over time, some standardization of value evolved with the unit of account called the made-beaver, which was equivalent to the value of one prime quality skin from an adult beaver. Beaver fur took on particular importance because of the popularity of the beaver hat in Europe. The Europeans found the beaver pelts to be of particular value, and the value of one prime pelt became the made-beaver and the unit of account.



Wampum Belt, n.d., Pre-Colonial/Early Fur Trade.
National Currency Collection, Bank of Canada;
photography James Zagon, Ottawa.



1 made-beaver, Hudson's Bay Co. (Eastmain), n.d., Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.



In his book, *Company of Adventurers**, Peter Newman provides the following information about the made-beaver.

At the fur-gathering end of the commerce, all goods were quoted in terms of their beaver equivalents, so that two otter skins, eight pair of moose hooves or ten pounds of goose feathers each equalled one made-beaver.¹ A moose hide or the fur of a black bear would fetch goods worth the equivalent of two made-beavers. Indians could get an impressive array of goods for their catch, as shown in this tally taken from the standard of trade as it existed at the Hudson's Bay Company post at Albany Fort in 1733:

<i>Coloured beads</i>	$\frac{3}{4}$	<i>pound</i>	<i>for</i>	<i>1</i>	<i>Made-Beaver</i>
<i>Kettles, Brass</i>	<i>1</i>	"	"	<i>1</i>	"
<i>Lead, black</i>	<i>1</i>	"	"	<i>1</i>	"
<i>Gun-Powder</i>	$1\frac{1}{2}$	"	"	<i>1</i>	"
<i>Shot</i>	<i>5</i>	"	"	<i>1</i>	"
<i>Sugar</i>	<i>2</i>	"	"	<i>1</i>	"
<i>Tobacco, Brazil</i>	<i>2</i>	"	"	<i>1</i>	"
<i> Ditto Leaf</i>	$1\frac{1}{2}$	"	"	<i>1</i>	"
<i> Ditto Roll</i>	$1\frac{1}{2}$	"	"	<i>1</i>	"
<i>Thread</i>	<i>1</i>	"	"	<i>1</i>	"
<i>Vermilion</i>	$1\frac{1}{2}$	<i>ounce</i>	"	<i>1</i>	"
<i>Brandy</i>	<i>1</i>	<i>gallon</i>	"	<i>1</i>	"

¹ "Made-beaver" constituted the money of the new frontier, not in the sense of a medium of exchange but in the sense of a unit of account. When coins were eventually introduced to facilitate the fur trade, they were made-beaver tokens. Minted of brass or stamped out of the copper bindings of kegs shipped to the bay from London, they were imprinted with whatever fraction of made-beaver they represented and could be spent like cash inside HBC stores. A prime quality beaver usually represented a dozen tokens; a bear skin, twenty. The last tokens were aluminum pieces for use in the white fox trade, issued in the eastern Arctic by the HBC in 1946. The standard fluctuated from time to time and from factory to factory, depending on the trading circumstances.

As the economy in this new land developed and more settlement occurred, more traditional forms of money found their way into use, particularly European coins from exploring/trading nations such as England, France, Spain, and Portugal. But the two nations to be most significantly involved in this new land would be Britain and France.

Where the French power was stronger, French coinage was used. But a problem arose for the French in Canada because there was a shortage of French coinage. This problem was compounded by the fact that the mother country (France) expected that payments be made from the colony in coin (that is, in silver and gold). This put a drain on the cash available in the French colonies.

Due to the shortage of coinage, around 1685 the French settlers developed an interesting form of money—playing card money. This playing card money was a form of fiat money since the cards didn't have intrinsic value or,

* Source: From *Company of Adventurers*. Copyright © Power Reporting Limited, 1985. Reprinted by permission of Penguin Books Canada Limited.

at least, not anywhere near the value that they had as money in exchange for goods and services. Playing card money was one of the early forms of paper currency in Canada. It eventually evolved into what was called card money in 1729 and continued to circulate as money until the fall of New France.

Playing card money worked as follows. The playing cards were cut into quarters, halves, and so on. The seal of the treasurer of the colony was affixed to each card with wax. Then the signatures of the Governor, the Intendant, and the Clerk of the Treasury were placed on the card. These cards were then accepted as money and, as such, as payment for goods and services within New France. It is interesting to note that there is no surviving example of playing card money.

After the fall of New France, the British eventually refused to redeem the card money that the French colonists had been using. Whenever money is not generally accepted, it loses its value and ceases to function as a medium of exchange. This, of course, was a particularly harsh blow to the French settlers who suddenly found that their card money had no value. The result was a considerable distrust of paper money among early French Canadians, and it caused them to be hesitant about accepting it in the future. Mind you, the French were not the only ones to be skeptical, but they had a particularly good reason to be so.



50 livres, French Regime playing card money - Reproduction, 1714, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.

In the early days of the developing economy in Canada, there were many different coins being circulated as money. Even flattened buttons were used as a form of money. The variety of forms of money began to make the exchange process confusing. People didn't know what to accept and what not to, and they became confused as to the cost of various goods and services in terms of the various forms of coinage.

As a result, efforts were made to standardize the system and lessen the confusion. In the early 1800s, a law was passed in Lower Canada that authorized the banks to issue copper tokens. It was hoped that this would reduce the confusion and make the exchange process more efficient. For that law to come into place, banks had to have evolved to where people used and trusted them. Let's turn our attention to the evolution of banks in Canada. [Note that there is a brief discussion in the next background reading on the evolution of banking in general and a look at banking operations.]

Early efforts to establish banks in Canada were an attempt to replicate banking activities that were under way in nations such as Scotland, Holland, and Italy.

The first bank established in Canada in the 1790s (specifically, the Canada Bank or, as it was also called, the Canada Banking Company) failed. It failed because it had trouble gaining the acceptance of the people. In the same way

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\$1, Quebec Bank, 1835, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.



\$1, Montreal Bank, 1819, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.



5 shillings, Bank of New Brunswick, 1820, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.



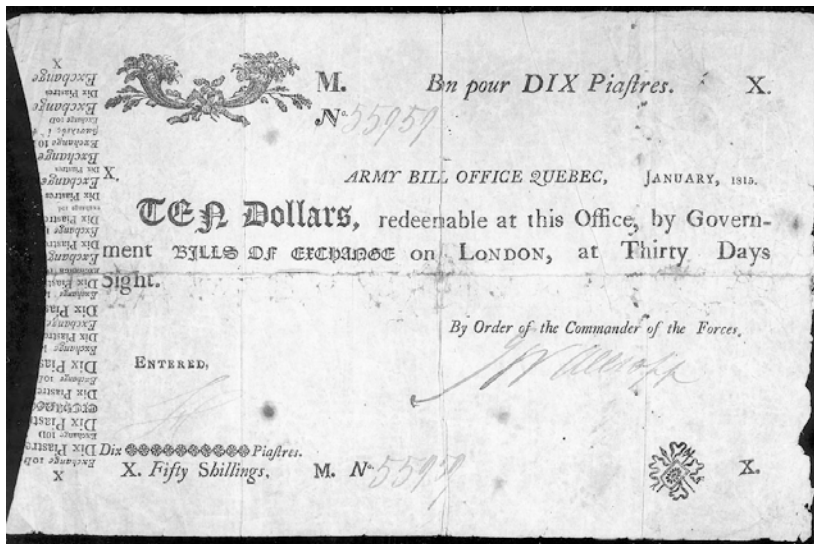
that money depends on the trust of the people and their willingness to accept it, banks, too, depend on people's trust and their willingness to do business with the banks.

We mentioned earlier that there were problems with coinage in the early economy in Canada. But there were also problems with establishing an accepted banking system.

Amid all the nervousness about the different forms of money and the early banks, in 1812 the United States declared war on Britain. Sir Isaac Brock,

who had recently been appointed governor of Upper Canada, thought that the Americans might attempt to move into Canada. Brock realized that weapons and other equipment would have to be acquired in order to prepare for war. He was hampered, however, by a shortage of currency in the colony. Without money, he couldn't buy the weapons and other equipment he needed.

To address the problem, Brock ordered that paper currency called Army Bills be issued to pay wages and to acquire the goods that were needed. These bills were issued in Spanish dollar denominations. At first, there was resistance to accepting them, but they gradually won the confidence of the merchants. After the war was over, these bills were redeemed by the government for silver and gold. They didn't lose their acceptance and value. This helped restore people's confidence in paper currency.



\$10, Army Bill, 1815, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa.

With people's restored confidence in paper currency, efforts were renewed to establish banks. The first successful bank was the Montreal Bank, established in 1817. This eventually became the Bank of Montreal, which received its charter in 1822. Although the Bank of Montreal was the first successful bank, it was not the first to be given a charter. The position of first chartered bank belongs to the Bank of New Brunswick, chartered in 1820. It was eventually taken over by the Bank of Nova Scotia.

With the establishment of banks, the use of paper money (fiat money) increased. The banks would issue paper notes that served as money in much the same way that our paper currency serves as money today. People could exchange the bank notes in payment for the goods and services of merchants because people were confident that the notes could be redeemed on demand at the issuing banks for gold or silver. The Montreal Bank issued notes denominated in U.S. dollars.

We mentioned earlier that the Spanish eight reale piece was popularly referred to as a dollar. These Spanish dollars were cut into quarters, and one quarter of a Spanish dollar was equal to two reales or "two bits." That is why some people, to this day, refer to our quarter as two bits. The Spanish dollars that circulated in Canada weren't minted here but in places such as the Spanish colonies in Central and South America and in Mexico. It wasn't until 1931 that the Royal Canadian Mint was established in Canada.

As more and more banks were established, more and more notes of various forms were issued by these banks. Some of these new banks failed. And with all the new banks, some succeeding and some failing, new confusion, concerns, and problems arose. People became more nervous about accepting the various bank notes. A merchant quite some distance from one of the banks might be afraid to accept a note issued by that bank for fear it had failed.

The ambiguity and confusion created a perfect environment for counterfeiters—and they flourished. Ghost, or phantom, banks were established. They didn't have a head office and, frequently, no offices. Unscrupulous people

\$1/5 shillings, The Commercial Bank of the Midland District, Kingston, 1843, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa. (A legitimate bank note)



\$4/20 shillings, Commercial Bank of Fort Erie, 1836, Canada. National Currency Collection, Bank of Canada; photography James Zagon, Ottawa. (A ghost bank note)



would pick a name that resembled the name of a well-known Canadian bank and approach a printing firm to produce paper currency in that name. These bank notes would then circulate in Canada and the United States. This went on for a while until the merchants and others caught on to what was happening. That these unscrupulous promoters could get away with this deception was a sign of the banking problems that existed. Change was needed to restore confidence in money.

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It became apparent that there was a need for a uniform currency—a single currency to be used by all people for all transactions. Sir Francis Hincks, who was involved in journalism, politics, and the development of the railway in Canada, played a major role. He pushed to establish a national currency. But his efforts were resisted by the British treasury officials for a number of reasons, including the fact that incomes were being earned by a variety of

institutions issuing currency. These institutions didn't relish the notion of losing that income by losing the ability to issue currency.

By legalizing transactions in decimal currency for the first time, the Province of Canada Currency Act of 1853 started us on the road to a decimal-based currency. Then the Currency Act of 1858 required that all government accounts be kept in decimal currency, and this decimal system has continued to the present day. By this Act, the dollar was adopted as the official unit of account by the Province of Canada, and coins were struck in denominations of 1 cent, 5 cents, 10 cents, and 20 cents.

Interestingly, though, it wasn't until 1867 that government notes (rather than just bank notes) were issued—first as Provincial notes and, subsequently, as Dominion notes. (“Notes” is simply another term for paper currency.) It was after Confederation that Parliament really confirmed its control of the currency. The Bank Act of 1871 repealed any provincial acts that were in conflict with federal control of the currency and guided the issuance of notes (paper currency) by the banks. Chartered banks issued notes in the denominations of \$4, \$5, \$10, and so on. The government was also issuing notes—\$.25, \$1, \$2, \$50, \$100, \$500, and \$1,000—covering the larger and smaller denominations. Over time, the government would take over issuing all notes. You might assume that people used primarily paper notes rather than coins for transactions, as is the case today. In fact, this wasn't the case in the 1800s. It wasn't until the First World War that paper money overtook coins as the primary form of currency in day-to-day life.

Over time, as prices rose and commerce and industry expanded, there was a need for wider circulation of higher denominations of paper currency. So the government assumed the issuing of \$4 notes in 1882 and \$5 notes in 1912.

Operating under the guidance of the Bank Act, the individual banks in Canada issued currency until 1944. Revisions to the Bank Act in 1934 provided a schedule for the reduction in the issuing of currency by the banks up to 1944. It was at this time (1935) that the Bank of Canada was established to take over as the central bank to eventually assume total responsibility for issuing currency.

In 1944, Bank Act revisions stipulated that the banks were required to cease issuing or re-issuing notes as of January 1, 1945. As of January 1, 1950, all the chartered bank notes still outstanding became the liability of the Bank of Canada. (Note: The Bank of Canada received a payment from each chartered bank equal to the amount of notes each bank had outstanding at that date.)

Even today, if you have one of the redeemable bank notes issued by a chartered bank, the Bank of Canada is legally obliged to accept it. In fact, there are still about \$8 million unaccounted for that would still be accepted. The likelihood is that most of these bank notes have been destroyed. However, when cleaning up the attic or rummaging through your grandparent's basement, don't hastily discard any currency that you might find!

To this day, the Bank of Canada maintains responsibility for issuing paper currency in addition to its other responsibilities. Essentially, the Bank of Canada took over a centralizing function for the entire financial system. As far as money is concerned, though, the Bank of Canada is responsible for paper currency, whereas the Royal Canadian Mint looks after coins. Periodically, the Bank has changed the style of the currency issued. The first major change

occurred in 1937, followed by other changes in 1954. A more modern style was introduced in 1969. In 1985/86, the Bank began a further series of changes in the style of our paper currency, and these designs, along with some new alterations, continue today.

As we near the end of our brief look at the history and evolution of money, it is important to draw particular attention to the significance of the evolution from commodity and specie money to fiat money. We spent some time examining people's reluctance to accept fiat money. Today, because of our secure financial system, fiat money is commonly accepted. People will willingly accept a piece of paper legally denoted as having \$100 worth of purchasing power. People widely accept these relatively worthless pieces of paper that represent money and the power to purchase goods and services. The acceptance of fiat money paralleled the development of our financial system—and people's trust in that system. Fiat money refers to paper notes, not cheques. However, people's willingness to accept fiat money opened the door to the use of cheques.

This wide acceptance of fiat money has had important consequences for the economy. As our economy has grown more and more and produced more and more output, the number of exchanges has grown rapidly. Millions and millions of exchanges now take place in our economy each year.

The acceptance of fiat money has enabled us to provide a large quantity of money to the economy at relatively little cost and has greatly enhanced the efficiency of exchange in our economy. It is very important to stress the significance of this particular evolution.

As we said, the evolution to fiat money paved the way for people's acceptance of chequing accounts and cheques. Your deposit with a financial institution represents a quantity of money that is denoted by a figure in your account. If you have \$200 in a chequing account, you don't have \$200 in currency sitting somewhere waiting for you. Instead, you have a number—200—recorded in your account indicating the amount of your deposit. When you write a cheque, you simply instruct the relevant financial institutions to adjust the numbers in your and other people's accounts appropriately. No items of real value are moved from one account to another.

Cheques have been very important in the evolution of the modern, sophisticated financial system that supports our economy. Today, if you want to buy a \$175,000 house, you do not have to carry around \$175,000 in cash. Cheques have simplified the process of making larger payments, and they have made the process safer and more secure as well.

Our system continues to evolve to where the debit cards we discussed in the first background reading, enabling us to access our bank deposits directly with a card as opposed to writing a cheque, are becoming increasingly available.

This brings us to the end of our journey through the history and evolution of money, both in the world and in Canada. Today, millions of people engage in billions of transactions, and billions of dollars are invested each year to enable our economy to continue to grow and expand. And we have an efficient, sophisticated financial system to support such activity. We now take another turn on our journey, which will bring us to a look at the financial system that has evolved in Canada to support the use of money in our economy.