

# Funding the Future

Article URL

Published: January 12, 2026, 7:20 pm

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Martin Wolf [wrote an article in the FT yesterday](#) in which he argued that the Swiss should vote for monetary reform this weekend.

I have [already discussed](#) the dangerously oppressive nature of these reforms which would remove the right of commercial banks to create credit, and pass the whole responsibility for creating the country's money supply to its central bank.

I have also drawn attention [to the role of Positive Money](#) (which Wolf supports) in promoting this idea.

Wolf argues three things. The first is that bank failures cost us a great deal. He's right: we know they do.

And he argues that reform has not happened since 2008. He's right. But then, [he sat on the UK commission](#) that created the absurdly feeble and slow-paced recommendations for reform that the Tories adopted, so I can lay part of the blame for that on him.

And third, he argues that in that case we have to do 'something'. As he puts it:

*I hope ... that the Swiss vote in favour of the [Vollgeld proposal](#) in the referendum on June 10. Finance needs change. For that, it needs experiments.*

With respect: no we don't need experiments. What we need is some recognition of the truth.

Let me first say what the truth is not. It's not, as Wolf puts it, that we need to:

*...make the system safer [by] strip[ping] banks of the power to create money, by turning their liquid deposits into "state" or "sovereign" money. That is the idea backed by the Vollgeld initiative.*

Of this Wolf says:

*An alternative way of achieving the same outcome would be via 100 per cent backing of deposits by claims on the central bank – an idea proposed by free-market Chicago*

*School economists in the 1930s.*

Actually, they're the same, in effect. And that this is a Chicago School / Friedmanesque monetary policy is [made clear by Positive Money](#) in their claim for this policy which said:

*The central bank would be **exclusively responsible** for creating as much new money as was necessary to promote non-inflationary growth. It would manage money creation directly, rather than through the use of interest rates to influence borrowing behaviour and money creation by banks. Decisions on money creation would be taken independently of government, by the Monetary Policy Committee (or a newly formed Money Creation Committee). The Committee would be accountable to the Treasury Select Committee, a cross-party committee of MPs who scrutinise the actions of the Bank of England and Treasury. The Committee would no longer set interest rates, which would now be set in the market.*

The central bank would continue to follow the remit set for it by the nation's finance minister or chancellor. In the UK this remit is currently to deliver "price stability" (defined by an inflation target of 2%), and subject to that, to "support the Government's economic objectives including those for growth and employment." The inflation target acts as a limiter to stop the creation of money becoming excessive, but subject to that, the central bank is able to create additional money.

The objections flow, almost without limit.

First, this puts inflation at the core of economic policy. Put it another way, the interests of those who have money are prioritised. The 1% (or less) are favoured. Any other economic objectives, such as full employment, the creation of a sustainable economy, or the provision of high quality public services, are ignored. Money comes first.

Second, in the process Wolf, and those who promote this idea show that they have no idea what money is. Money is debt. It is only created by government spending and bank lending. It is literally the double entry that surrounds those two processes that create money: there has to be a debt and a creditor accepting obligation to each other for money to have value. But at the core of the Positive Money proposal, and at the core of what Wolf is suggesting, is the idea that you can, somehow, create and distribute money at the central bank as if it has some tangible real quality that simply does not exist. Quite literally printing a pile of cash does not create money: it only creates tokens that represent money. It is the spending of those tokens, and the government's willingness to accept them in payment of tax, that creates value, which underpins the currency. This is why it is so important that counterfeit money is challenged: fake currency undermines the value of the real debt that gives money its value. And the token money that the Swiss proposal would create would be exactly the same: they would be a fake currency because there would be no debt, in the process the value of this money would be undermined, or even destroyed. That's not an

experiment anyone can want to participate in.

Third, the very real danger is that a central bank would underestimate the amount of money needed in an economy because their perpetual concern would be the risk of inflation meaning that they would always be on the side of caution. The consequence would be obvious: it would be perpetual underemployment, less than full capacity economic activity, the crushing of credit that creates business opportunity and indications this has the public services near-perpetual economic stagnation, if not the recession.

Fourth, give central bankers control of the money supply, and you can forget democratic control of the economy for evermore.

Fifth, since central bankers would also then control the ability of the government to create money to spend on its own programs guarantee that this would also mean perpetual austerity, and enforced government balanced-budget, with all the crushing implications that this has for the public services.

This, apparently, is what Martin Wolf wants.

And he wants this despite the fact that he, like Martin Sandbu, also of the FT, **who I quoted recently, knows that the reality of money. They know it is bank made. They know banks are not intermediaries. They know money creation is costless.**

**And yet they don't want to use this knowledge to put money to use: instead they want to use it to constrain the use of money for the purpose of preserving wealth by promoting an idea that has banker control of inflation at its heart and which denies the very essence of what money is to achieve that goal.**

**There is an alternative, of course. It's hardly even an experiment. It's to simply use what actually happens for the common good, and that is modern monetary theory. As I have written recently:**

*As I explained in my Book 'The Joy of Tax', if a government with its own currency in which it requires settlement of tax liabilities wants taxation to be paid then it must first of all spend to put the currency in question into circulation. No other option is possible. It does, as a result, follow that tax does never fund government expenditure. Instead, that expenditure is funded by the creation of new money on the government's behalf by the Bank of England, which it wholly owns. That the Bank of England can create funds in this way has been proven by the quantitative easing programme that has been in existence since 2009. £435 billion of new funds have been created by that programme without any cost to the taxpayer simply by the operation of double entry bookkeeping. The **Bank of England acknowledged that this is the way in which***

**banks, including themselves, can create new money in a paper published in 2014. The difference between new money created by government spending and taxation revenue received is at present made good by the issue of government bonds, although this is not strictly necessary: except for EU legislation that prevents direct lending from the central bank to the government that owns it this shortfall could, instead, be managed by an overdraft arrangement between the government and the central bank on which no interest would need to be paid.**

**The Bank of England might have acknowledged this reality, but as yet HM Treasury has not. The result is that it is not as yet acknowledged that the true role of tax in the modern economy (i.e. that where there is only a fiat currency, which has been true almost worldwide since 1971, at least) is to cancel government money creation for the purpose of controlling inflation. If this were understood there would be significant change in the way in which the government managed the macroeconomic environment in the UK.**

We need no experiment. We just need to acknowledge this truth. And the fact that it puts employment and fiscal policy at the core of economic management.

We live in a dangerous time when the FT promotes a form of hardline, and deeply undemocratic monetarism.

It's dangerous that some on the left have bought into Positive Money's ideas.

The battle for money has begun. It is essential that it is won.