

What is money? The argument based on logic

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A few days ago I [posted an explanation of economics](#), based on the logic of an if/then argument. It seemed to be popular.

The aim was to work my way logically through a thought process to explain the conclusions I have reached on that issue.

It was never my intention that this should be a one-off exercise, and that I should use the process again. I decided to do so with money, which is almost indefinable, as I have already noted this week [when suggesting](#) it may be nothing at all.

This exercise proved to be much harder than that on economics. I cannot recall how many drafts the following post went through, but I imagine it was at least twenty. The result is not perfect, but the time has come to give it an airing, and to learn from doing so.

This [morning's video](#), and the [essay series to which it relates](#), are both in part based on the logic of this post, and the previous [one on economics](#).

Part 1: Government creates money

- * If a government exists, then it has purposes to fulfil and resources it must mobilise to fulfil them.
- * If a government must mobilise resources, then it needs a means of claiming them from the economy it governs.
- * If a government is to claim resources, then it must first create a unit of account in which those claims can be expressed.
- * If a government declares a unit of account to be legal tender, it establishes the only means by which any claim in the economy can be legally enforced. No debt, no obligation, and no claim of any kind can be compelled to settlement except in that unit.
- * If the unit of account is the only means by which claims can be legally enforced, then

it becomes the signal through which all economic obligations are expressed, recorded and settled. It carries no value in itself. Its coherence derives entirely from the accounting system within which it operates, and that system is relevant only because of the signal flows that through it. The two are different but symbiotic: each creates the functioning and relevance of the other.

- * If a government brings that signal into existence, then it does so by spending: creating new entries in its accounting system and transferring them to those whose resources or labour it has claimed.
- * If government spending creates money, then taxation cannot be its source of funding. Government must spend before it can tax.
- * If the government taxes, it withdraws money it has already created from the economy, thereby regulating the consequences of its spending rather than financing it.
- * If taxation regulates rather than funds, then its purposes are to prevent excessive claims on real resources, to redistribute purchasing power, and to shape economic behaviour.
- * If government both creates money by spending and regulates it through taxation, then government is the foundation of the monetary system, not merely a participant within it.

Part 2: Society extends money

- * If government has created a unit of account, declared it legal tender and brought it into circulation as a signal within its accounting system, then society can use it to record its own obligations, claims and settlements, all of which can only be enforced in that unit.
- * If commercial banks create deposits denominated in that unit whenever they lend, then banks further extend the accounting system, creating additional monetary claims within it.
- * If money is a signal within the accounting system rather than wealth itself, then increasing the quantity of that signal alone cannot make society richer.

Part 3: What money records

- * If money records claims, then the question is: claims upon what?
- * If real wealth consists of people, their knowledge, skills, creativity, relationships, institutions, infrastructure, and the natural environment, then money records claims on that societal capital and on what it can provide.
- * If every claim must ultimately be settled in legal tender, then every claim requires real societal capital to back it, which can be exchanged for that legal tender if all claims are to be capable of settlement.

- * If the accounting system is complete, then it records three things:
 - * the stock of claims and obligations at any point in time;
 - * the flows of activity that generate, maintain or deplete societal capital over time; and
 - * the cash flows that reconcile the two, showing how claims are created, transferred and settled across time.
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- * If the accounting system records all three, then money is not merely a record of what is owed. It is a record of whether society is building, maintaining, or consuming its capacity to meet needs, and whether the recorded claims can actually be settled from the capital generated by that activity.
 - * If we lose sight of what the accounting system records and treat financial balances as ends in themselves, we have confused the record of society's activity with the purpose of that activity.
 - * If we judge success by the condition of the accounting system rather than by the condition of society, then we mistake the map for the landscape.

Part 4: What follows

- * If money is a signal within the accounting system rather than a resource in its own right, then neither the signal nor the system can ever be a real constraint upon society. The constraints are always and only the real things that money and the accounting system together exist to represent.
- * If the real constraints are people, knowledge, technology, energy, ecological capacity and time, then those are the resources that economic policy should seek to develop.
- * If society possesses unused resources capable of meeting unmet need sustainably, then money should enable their use rather than prevent it.
- * If money exists to help society realise human potential by meeting need sustainably, then good economic policy is policy that improves society, not merely its financial accounts.

Conclusion

The mistake we make is to think that money is the purpose of the economy.

It is not.

Money is a signal within an accounting system that the government created to mobilise resources, and which society then adopted to organise itself. Like every accounting system, it exists for a purpose beyond itself. No business exists simply to produce accounts. Its accounts exist to help it achieve its objectives. The same is true of government, and of society.

The purpose of that accounting system is to help us manage the relationships between people and the resources available to them, so that need can be met, potential can be realised, and wellbeing can be sustained.

Once that is understood, almost every economic argument changes.

Deficits become accounting outcomes, not policy objectives. Public debt becomes part of the accounting system, not a burden on future generations. Tax becomes a tool for managing the economy, not the source of government funding. Economic success ceases to be measured by financial balances alone and is instead judged by whether society is becoming more capable of meeting need and enabling everyone to realise their potential.

The real question is not whether we have enough money. It is whether we are using the accounting system we have created to build the society we actually want.