THE USE OF MELT SHOULD BE ABANDONED
BECAUSE MONEY DOES NOT MEASURE LABOUR TIME DIRECTLY.

When gold was reduced from being money to being a commodity in general, which is what happened in 1973 when convertibility was abandoned, the laws governing its role in society changed. First and foremost, instead of being priceless, it developed a price in common with all other commodities. It lost its state of pricelessness because it could no longer act as the **standard of price**. Nor could it act as measure of value because that role had been usurped by paper money.

After this time gold responds to the same laws of demand and supply as do other commodities. Instead of always facing the world of commodities as the universal commodity, expressing their value by its weight, it now turns its back on the world of commodities to face its nemesis, paper currency. This is the only way to explain the movement in the price of gold during the business cycle which we shall examine as it is key to understanding MELT.

MELT.

I do not favour using MELT. I was asked to comment on the "*MONETARY EXPRESSION OF LABOR" IN THE CASE OF NON-COMMODITY MONEY* by Fred Moseley published in 2004. I will begin with what I agree with, which is his criticism of Duncan Foley: "*Since the MVA is determined by the MELT, the MELT cannot be determined by the MVA. The theoretical determination of the MELT remains 'hanging'".*

This is reminiscent of Kautsky's criticism of Hilferding a century ago. Here Kautsky accuses Hilferding of twisting the relation between money and commodities. He quotes Hilferding: "*Of course, all commodities are still (in pure paper currency), as before, expressed, 'measured,' in money. (Not gold! – K.) Money appears still, as hitherto, as the measure of value. But the greatness of the value of this "measure of value" is no longer determined by the value of the commodity which creates it, the value of the gold, the silver, or of the paper. <u>On the contrary, this value is in reality determined by the total value of the commodities to be circulated</u> (the date circulation remaining the same). The real measure of value is not money, but the bank-rate is determined by that which I should like to call the socially necessary value of circulation."* (Page 29, Das Finanzkapital, Third Volume, Vienna 1910. My emphasis)

Now I am not sure whether or not Mr Foley has changed his mind and whether my criticisms are outdated, but it is important to reject the idea, that because paper money has no intrinsic value, it value must derive from the value of commodities its circulates. That instead of measuring their value, its value is measured by the commodities thus reversing the role between commodities and money.

Turning to MELT, at best the "monetary expression of labour time" could only exist in the abstract, with capital in general, where exchange is held to be equal so that individual prices never deviate from individual values and there is no such thing as the business cycle or industrial cycle as described by Marx. Only then does gold become a "direct" measure of the labour time in the commodities it circulates.

In reality, this abstract world does not exist, it is an artefact prepared for the purpose of simplified analysis. If MELT refers only to gold itself, that is unproblematic. If MELT refers to the relation between gold and the commodities it circulates, that is problematic. In the case of gold acting as money, it is priceless because it acts as the standard of price. In this case, a weight of gold will be the direct incarnation of the weighted average labour time currently needed to produce it and its weight will act as the measure of this expenditure and indeed as the measure for all other commodities. The value of gold is unaffected by the value of the other commodities except the ones consumed in its production which forms the constant and variable capital used up in gold mining and refining. One ounce of gold will always represent one-sixteenth of the labour time needed to produce a lb of gold and it will always circulate one-sixteenth the volume of commodities (assuming their value is unaltered) presuming we are on the gold standard.

In Volume 1, Marx makes the point that if the value of gold increases, the price of all other commodities deflates, because it takes less gold to circulate them. Conversely if the value of gold falls the price of all other commodities inflate. But this depends strictly on the assumption that commodities exchange at their value or what is the same thing, that all exchanges are equal, such that the same value of money is received as is found in the commodities sold, as will be the case later with the commodities bought with that sum of money. What Marx does not address here, is how the quantitative relation between gold and commodities can and does change despite no change in either the value of commodities or gold itself.

This is an assumption that cannot be sustained in the real world, the world where the labour of the individual becomes part of the labour of society only indirectly, through being exchanged. In such a world, an incongruity between price and value is not only possible, but necessary. This is what Marx addresses in Volume 3. Here he analyses and discusses what happens when the prices of commodities inflate or deflate regardless of changes in the value of gold. In other words, we are confronted by the transformation problem. In my article on the transformation problem, which I now consider solved on the same methodological terms as Marx:

(theplanningmotivedotcom.files.wordpress.com/2015/09/transformation-solution-pdf.pdf)

I mistakenly referred to only two cases where the transformation of values into prices takes place which are, (a) within an industry with the emergence of market prices and, (b) between industries with the equalisation of the rate of profit and the emergence of market prices of production. In fact, there is a third transformation which we will now focus on. It is the business/industrial cycle, where prices deflate during the phases of crises and stagnation and re-inflate during the period of prosperity and overproduction such that over the course of the industrial cycle, total prices equal total value. "*If this is the supposed sense of the contention that the money capital of a country is reduced in times of pressure, it is identical with saying that commodity prices have fallen, Such a collapse in prices, incidentally, only balances their earlier inflation.*" (Volume 3, page 622, Penguin Edition)

If we were to confine money to gold coin this translates into the following. During times of pressure, where prices are falling and the volume of commodities is reduced, the total circulation now absorbs fewer gold coin. As a result, more coins are hoarded. The value in circulation is now priced by fewer coins. A ton of steel, which before was priced by five gold sovereigns, is now priced by four. Conversely in the period of prosperity and over-production, it now takes six gold sovereigns to circulate one ton of steel. What happens during the down-phase is that gold prices fall and they rise in the up-phase regardless of changes to the actual cost of producing these commodities or gold.

And by gold price we mean the price of commodities measured in gold. Here terminology is important. When the expression "gold price" is used, it refers to gold as the standard of price, i.e. the price of commodities being expressed by a weight of gold. The "price of gold" as an expression refers to the time when gold is no longer priceless, when it no longer acts as the medium of exchange or the standard of price, when gold has been reduced to the status of a commodity because of inconvertibility. The price of gold, in common with other commodities means its monetary price measured by paper currency.

To conclude on this point, Labour Time Money, Labour Money (1), MELT is a non-starter because it is impossible to measure labour time with money directly in a society based on unequal exchange caused by the movement of capital or its non-movement.

What about paper money divorced from commodity money (gold)?

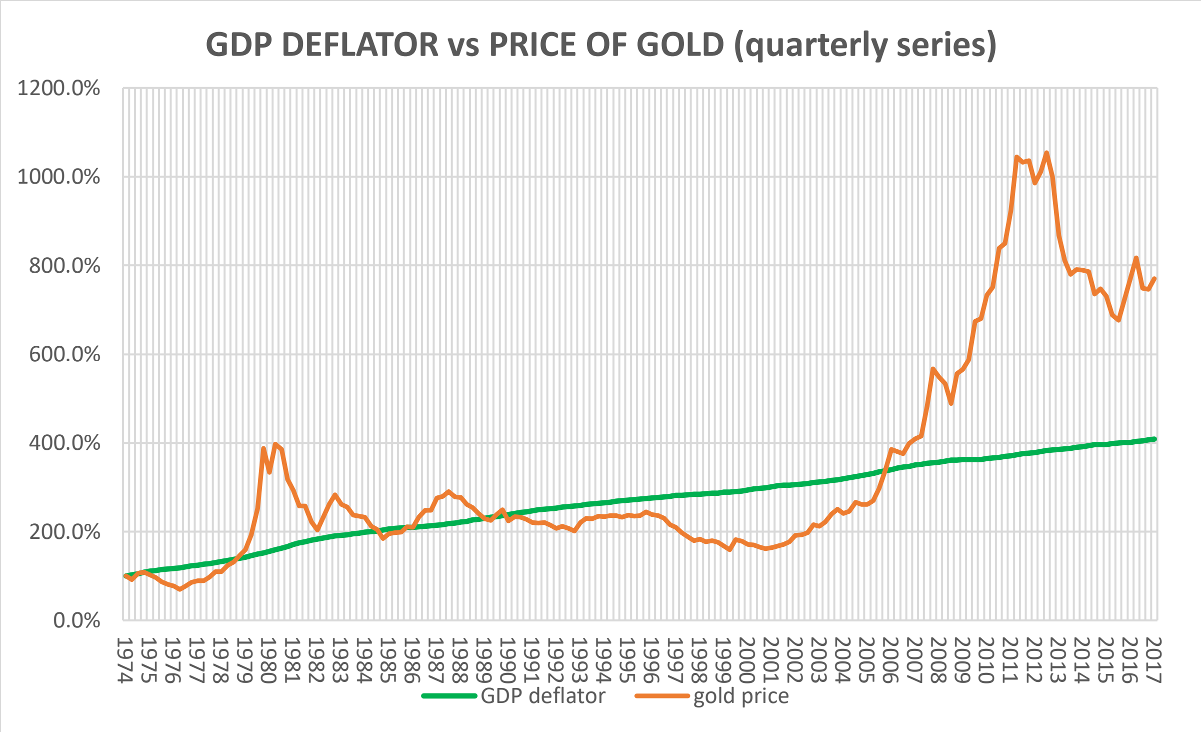
Capitalism works, not because of exchange but because of unequal exchange, and because of this inequality, money cannot directly measure labour time. Commodities circulate in a fully developed market economy, not as products of labour but as products of capital whose prices always diverge from values. As such the substitution of paper money for gold presents no problem. That is why it is possible for a note whose value is only 20c (actual cost of producing a $100 bill including unpaid labour) to circulate commodities priced at $100. It is a form of unequal exchange that presents no problems for the functioning of the capitalist system because this particular unequal exchange is backed by the resources of the state using its monopoly of taxation.

Marx had no problem with paper currency. He explained its genesis in Chapter 3 on *Money or the circulation of commodities* in Volume 1. More importantly, on page 129, he talks of the "*transient nature*" of money as it "*passes from hand to hand*", the purpose of which is to "*replace commodity by commodity*" so that "*the mere symbolical existence of money suffices*". "*Its functional existence absorbs, so to say, its material existence*", to which he further adds, this forced function imposed by the state is confined to its own jurisdiction. (New World Publishers, 1992 edition.)

Moseley extracts a quote from the same area of the Chapter to substantiate his presentation of MELT as it applies to inconvertible currency: *If the paper money exceeds its proper limit, i.e. the amount of gold coins of the same denomination that could have been in circulation, then ... it will still represent within the world of commodities only that quantity of gold which is fixed by its immanent laws. No greater quantity is capable of being represented. If the quantity of paper money represents twice the amount of gold available, then in practice £1 will be the money-name not of 1/4 of an ounce of gold, but of 1/8 of an ounce. The effect is the same as if an alternation had taken place in the function of gold as the standard of prices. The values previously expressed by the price of £1 would now be expressed by the price of £2.* (Marx 1867, p. 225 or page 128 in the New World Edition).

The criticism of using this example is that it is abstract. If gold cannot measure labour time directly, then how can paper currency as a multiple of gold measure labour time directly. It cannot. If the primer is inaccurate it does not really matter what the multiple is. Nor does elegant maths and the substitution of terms alter this. Will double the supply of paper money result in a doubling of prices, maybe, maybe not. It could leak into speculation, be repulsed by market conditions, who knows.

I will shortly look at this more concretely in terms of the business/industrial cycle. But first it will be useful to plot the price of gold against inflation which is done in the graph below.



(Sources: FRED Tables GOLDAMGBD228NLBM for price of gold, GDPDEF for GDP deflator)

Both the price of gold and the GDP deflator have been indexed at 100 in 1974. This is an interesting graph because it shows the price of gold falling below the trend in inflation before rising above it. We note that the price of gold fell in real terms between 1980 and 1999. From 1999 it reversed its fall to gain a new peak in 2013. At its earlier peak in 1981 it was 2.4x higher than the deflator and in 2013 it was 2.7x higher, a not too dissimilar a figure taking into account chaining. (Chained dollars over the longer term presents problems. In the case of the deflator used here it is indexed to 2009.)

Now many theorists have looked to the rise in the price of gold since 1999 as coinciding with the phase of financialisation and the increase in the money supply. They have therefore attributed its rise to the depreciation of the dollar due to the increase in the supply of dollars. There is however another and more prosaic explanation. In 1999 the cost price of gold was $360 per ounce, its production cost then doubled over the next ten years to $717, from there to $950 by 2015 and by 2016 it was touching $1000. Cost price here is based on the AISC convention (All-in sustaining costs) agreed in 2013. (Source: *Gauging the Long Term Cost of Gold Mine Production*, is a useful source. Ibma.org.uk/assets/Aich6001Fellows.pdf) This was due to declining average ore grades as older deposits were mined due to the dearth of newer finds.

The result is that while the price of gold increased by 447% between 1999 and 2016, the cost of producing gold went up 278%. Relatively the price of gold rose only 60% faster. This compared to the ratio for the price of gold versus the dollar which amounted to 217%. Accordingly, three quarters of the rise in the price of gold was due to rising costs of production. Hence it is inadvisable to use the simple gold price to measure the growth in GDP or assets, without taking into account the changed value of gold itself.

It is also worth mentioning that the ratio of the gold price to the dollar in 1980 and 2012, the two peaks in percentage terms, were similar, though on the graph the gap looks bigger in 2012 because of the difference in the absolute size of the figures. This being the case it is likely that the ratio between the price of gold and the dollar, adjusted for production costs, has oscillated in a narrower band than is generally assumed.

Focusing on MELT, I don't think that the long-term trend in the gold price is as important as its movement around the business cycle itself. Earlier we discussed how the periods of crisis and stagnation would witness deflation which would then be compensated for by the inflation found in the phases of prosperity and over-production. In aggregate, this would result in an averaging out process so that over the duration of the cycle TV = TP where TV equals total value and TP equals total prices. (It seems the industrial cycle solves the transformation problem on its own.) This would result in less gold being absorbed by circulation and more hoarded in the down-phase, whereas in the latter up-phase the increased circulation would see more gold coin absorbed and less hoarded.

This is the test. If gold is now an ordinary commodity having taken its place within the family of commodities, then in the down phase of the cycle its price should fall in common with other commodities and it should rise in the up-phase. It does pass this test, but with a heavy qualification. It spikes during the credit emergency when safe havens are sought. In this respect, it embodies its relic – a store of value. Aside from this, the price of gold tends to fall in the period of stagnation and begins to rise in the period of prosperity and especially over-production. This is true for the falls after 1982 and after 2012 and for the rises to 1980 and up to 2008.

Comparisons to earlier periods do not help. The period 1974 to 2016 of forty-two years is the longest continuous period when no major country was on the gold standard. It also embraces 5 business cycles which ended in 1980,1990, 2001, 2008 and 2015 (the last has not been recognised yet). Hence the period is of sufficient duration and complexity to enable robust conclusions to be drawn. (I attach the graph produced by FRED below which highlights these recessions.)

In conclusion MELT is an abstraction with little merit. I do not believe Marx ever used it. Instead Marx used the expression MEV the monetary expression of value which is different. "*Money as a measure of value, is the phenomenal form that must of necessity be assumed by that measure of value that is immanent in commodities, labour time.* (First page of Chapter 3, the chapter on money.) Immediately below this quote, in the footnote, Marx asks and answers the question as to why money cannot directly measure labour time, so although his analysis in this Chapter is abstract, nonetheless he already dismisses the notion of "labour money" or "labour time money" within a commodity producing economy. Instead of the acronym MELT, I would use MELTI, or "money expresses labour time indirectly".

(1) *Marx's Critique of Socialist Labor-Money Schemes and the Myth of Council Communism's Proudhonism*, January 21, 2013 published by the Marxist-Humanist Initiative. This is a useful critique of labour money and recounts the debates that occurred around it in the 1960s.

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