The Interest Pattern

In search of the lost monetary anchor

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Synopsis

The world is experiencing a monetary exuberance and an abnormal benchmark interest rate. More than 150 countries have monetary identity problems. At the end of 2023, the FED and the European Central Bank had to support the Central Bank of Sweden to prevent the collapse of the Swedish Krown.

For five hundred years man has been intensively trying to design an impeccable monetary issue system that determines the optimal amount of money in circulation, but he has not succeeded. A monetary system is optimal when it is neutral, in capillary and sequential supply, with a store of value (with endorsement) and under the needs of the market.

Thanks to the *Interest Pattern*, discovered in Madrid in the year 2013, man will be able to inject money according to the needs of the market so that the four fundamental variables of the economy (4FV pág.7) evolve proportionally because the healthiest economies are not those that grow the most but those that best harmonize the growth of 1) its capital goods, 2) its public goods, 3) the monetary mass or money supply, 4) according to the evolution of its human resources.

This paper 1) will describe the *Interest Pattern* foundations, 2) the new money distribution way, and finally, 3) it will show the empirical data that supports the *Interest Pattern*.

Many economists continue to think that man cannot know the amount of money the economy needs. That is precisely his Achilles Heel and the spine from which he developed all of his economic thinking. That is why many economists adore Keynes, the Gold Standard or, the most skeptical and childish, the free issuance of money.

In the future, thanks to the *Interest Pattern*, economic depressions will disappear and the greatest engine of social differences in the history of humanity also will go away: the crazy emission of money.

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1. In search of the lost monetary anchor

We spent more than twenty centuries of monetary childhood, with different metallic standards, such as the Gold Standard or the Bimetallic Standard. In all industrialized countries, during the 18th and 19th centuries, sequential bank runs were observed approximately every ten years, preceded by a sustained deflationary process. The conclusions obtained from the use of these primitive monetary tools and the needs of the market made us evolve towards the current fiduciary system. This step was taken intuitively, since we did not have a monetary theory that, ex-ante, would tell us the exact amount of money to print. The decision we had to make was also not supported by empirical evidence. Keynes´ General Theory promoted the leap into the void, which took place definitively and officially in 1971.

We naively thought that the economy would function better by limiting or anchoring the issuance of currency to certain indices. All economists thought

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that if the Central Bank observed the evolution of inflation and monetary aggregates, operating ex-post, corrective measures could be adopted to stabilize prices and thereby allow the correct functioning of the industrial market. After the Second World War, an overwhelming majority of economists around the world were convinced that the Central Bank and the Government, using the discount interest rate, the fractional reserve banking ratio, asset purchases, fiscal measures, etc., could manage to keep inflation under control and the value of the currency certainly stable.

But history has taught us (i) that politicians often use the Central Bank and monetary substitutes to benefit their political interests or, worse still, their interests; (ii) Secondly, we have also learned that the inflation index is not a reliable tool, since its effects are observed with a delay of 18 to 24 months.

Entering the 21st century, we have realized that the leap into the void we took creates a feeling of apparent well-being and avoids banking crises every ten years but, on the contrary, causes massive global crises every thirty or forty years. We are also belatedly aware that the fiduciary system leads the market towards business concentration (oligopolies), forces the technological cycle (man vs. machine fight), causes forced unemployment, abnormally widens social differences, encourages an abnormal drop in birth rates, etc.

All economists are astonished to observe how economic cycles continue to happen and that there is no way that, at any given moment, we will lose control of inflation or that a crisis will be inevitable that will trigger a severe adjustment of the economy. There is something in the fiduciary system that makes noise, that does not work well, but we do not know how to precisely prescribe the problem. Never in the history of humanity have there been more economists, more statistical data and more available media at play than in the last 50 years, but "we can´t find the key." In truth, we have made very little progress in monetary theory. The measures we have been adopting over the last fifty years are nothing more than monetary and banking patches, like the Basel banking reforms.

2. *The eternal question: What's the exact amount of money?*

Then, how to know the exact amount of money to inject into the market? How to overcome fiat monetary puberty? What monetary anchor should we use?

For five hundred years man has been *intensively* trying to design a monetary system that supplies money to the market according to its needs, to maintain the purchasing power of money; in other words, so that the monetary unit of account is stable.

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Economists were and are aware that by knowing the exact amount of new money to issue, major economic crises would be avoided. But the frustration of knowing the long-awaited data was passed from generation to generation, from crisis to crisis, because the optimal monetary mass depends not only on the amount of money in circulation but also on the speed with which it moves, the volume of products available on the market, the population involved, investments of capital and public goods, etc. The utility of the Q*uantity Theory of Money* is proof of frustration.

Faced with so much impotence, many economists innocently mythologize monetary infancy, extolling the benefits of the Gold Standard and cornering its great defects. Other economists, even more dangerous and unconscious, mythologize the free issuance of money (which encompasses free banking), ignoring the history of the United States and Europe. Murray Rothbard, one of the Argentine President Javier Milei´s economic myths, in his book *The Myth of Free Banking in Scotland*, provides a series of arguments that demystify this issuance system, the reason why private central banks emerge, which will later be nationalized in almost every country.

It is paradoxical to observe how the economist and President Milei consider historical figures who held the exact opposite of what he defends as myths, such as Juan Bautista Alberdi (anti-dollarization) or Murray Rothbard (anti-free banking). Curious, very curious.

Many of these unconscious economists also forget that in the United States, in the mid-19th century, the period known as the *American Free Banking* degenerated into such monetary chaos that it slowed down commercial traffic. The existence of more than 8,000 different types of banknotes (denominated in dollars) issued by private banks, insurance companies, railroads, etc. each with its own deposits and backup system criteria, generated such noise and monetary confusion that it stopped the good progress of economic activity, all despite being referenced in dollars and being considered legal tender currencies. Even barbers and tavern keepers competed with banks in issuing banknotes. Almost all citizens considered the issuance of money as a constitutional right.

3. *Ideal issuance monetary system*

Analyzing history I concluded that a fair issuance monetary system, the optimal system, would allow the issuance of money:

1) In a capillary way, so that the money reaches the real economy as soon as possible and avoids the distortion of relative prices. The false purifying banking sieve or banking filter should disappear.

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2) Sequentially, to avoid monetary stress processes. The Gold Standard was a system whose supply depended on the whims of nature and commerce, absurdly creating moments of shortage or abundance (Hume's Price Specie Flow Mechanism).

3) With a store of value. Money is used, in essence, for the exchange of work; therefore, must represent a prior and effective value (work). Austrians are afraid to use the word "work" because they consider it a term close to socialist ideas, an enemy of subjectivism. Observe, it is not a minor detail, that in the conference before Argentine businessmen in September 2023, President Milei avoided using the word "work" to define what money is. Thus he says "Money is an indirect medium of exchange".[1] It would be more understandable to say "It is a medium of labour exchange". We liberals have to overcome this taboo.

4) In a neutral way. Money must be the neutral arbiter of the market arena. In other words, one that cannot be manipulated politically or financially. A fair monetary system must respect the monetary needs of the market, that is, only supply the amount that the market itself demands. Central Banks are to blame for the current scenery, for having allowed extremely low interest rates for years and, now, being forced to hastily raise the interest rate. In 1962, Milton Freedman opened the debate on the independence of the Central Bank, which we are now moving to close with this paper.

5) Finally, you must revere the synchronicity of the four fundamental variables (4FV). The better economy is not the one that grows the most, but rather the one that grows respecting the synchrony of the four variables, the one that grows proportionally. Obvious cases that corroborate this theory were the Spanish desynchronized growth at the beginning of the century and that of China today, which will spend the next 10 years in restructuring due to abnormal economic growth. Today India or Mexico is industrially more competitive and commercially more transparent than China.

4. *The Interest Pattern foundations*

Having reached this deadlock, living in this monetary alley, where the world monetary theory has been for five hundred years, where no Economic School and no economist has been able to articulate a solid monetary theory, in despair, we can only ask: **given that money is one more product of the**

[1] *Milei stood up to all the businessmen and gave a furious presidential speech* (Buenos Aires: Youtube, 2023) September 6

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market, how do other industries to determine the quantity of products to offer?

Let us see! No authority ever considered creating the European Central Bank of Tomatoes, to plan the amount of tomatoes with which the Europeans live, and much less setting a reference price for tomatoes than to condition all market prices. Nevertheless, this is exactly what happens with money. Crazy, right? Therefore, what is the magic formula, what is the algorithm, and what is the computer system used by the food industry to determine the amount of tomatoes to offer? Easy. It handles an old economic golden rule: past consumption determines future production. So, the farmers will try to produce a quantity similar to that sold in the last harvest. If they achieve this goal, the price of tomatoes will be stable

But how can we know the amount of capital consumed by the market? Just as a pear is the fruit of the pear tree, the interest generated by the market (ΣI) is the fruit of capital, of money in circulation. Therefore, if we grow pears or print money based on the number of pears consumed or capital consumed (ΣI), the amount of interest generated by some and consumed by others, the price of pears will be stable and so will the price of money (interest rate).[2] The amount of interest generated by the market (ΣI)[3] is precisely the amount of new money that we need to print, for the monetary policy to be neutral in the market arena.

Thus, in 2013, a historical event occurred in Madrid that changed the history of the economy, such as the definition of *The Progressive Growth of the Money Supply Principle*, which determines the exact amount of money that must be issued so that prices are stable under normal economic and political circumstances.[4] This principle was stated in the following way:

> *«Any monetary system, whichever one we select, past or future, requires continued growth of the money supply in an amount equal to the aggregate interest (ΣI) created by capital loaned (financial and industrial) during the preceding period.»* [5]

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[2] Some of you will think that capital is not consumed, it circulates. However, capital is like the pear-tree, which is also not consumed. What the market consumes are its fruits, that is, the aggregate interest (ΣI).

[3] Added amount of interest or aggregated amount of interest (ΣI)

[4] Wars, pandemics and natural disasters are not normal conditions.

[5] Pedro Gómez Martín-Romo, *The Wealth of Nations in the 21st Century* (Almería: Editorial Círculo Rojo, 2019), p.92

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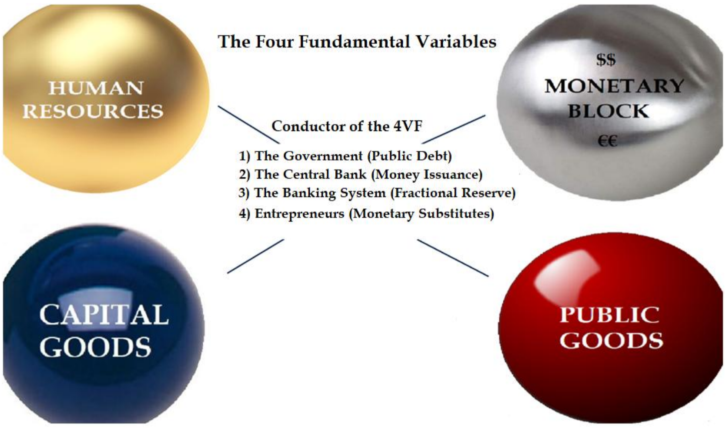
5. *The four fundamental variables*

Seen from another point of view, basically this theory states that if the population or its purchasing power increases, public goods,[6] private production goods and the money supply have to increase in identical proportions. And the natural and main driving force that should tell us how many goods and services we need is the population through the market.

It would not make sense that if the population increases no more sewage treatment plants, more roads or more airports were built; and vice versa, it would be absurd to build more airports, more sewage treatment plants or more roads if the population stayed the same.



With private production goods, the same thing happens; it is absurd that if the population increases or its purchasing power lets us not increase industrial production and services; and vice versa, it is equally nonsense.

Something similar happens with the monetary mass. If the money supply does not grow in the same proportion, there will be less money for more people, for more activity and, therefore, prices will suffer a compression or reduction. And to this economic phenomenon we call it deflation. If the quantity of money grows above what society needs, just the opposite effect occurs: inflation.

And the only instrument that can coordinate these growths correctly is the interest rate. The concept of the 4FV is an economic conceptual revolution that the Austrian School of Economics (ASE) is formally unaware of. The ASE

[6] Even admitting that all goods can be supplied and managed by private companies, which is a lot to assume, public goods are those whose legal ownership is common (air, water, justice, etc.). My concept of public good is jurist, not Anglo-saxon or economist.

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intuits these concepts but has never defined them with the clarity and precision the *Interest Pattern* does.

With the satisfaction of having discovered *The Progressive Growth of the Money Supply Principle*, in 2013 there were three no-small challenges ahead. 1) The first was to describe how the new money was distributed. 2) The second empirically demonstrates this principle. 3) Third, some countries in the world would try to implement these ideas.

6. *How to distribute the new money?*

To achieve the five monetary issuance objectives (page #4), the new money issued by the Central Bank will be distributed as follows:

a) Monthly, the Central Bank will issue money in an identical amount to the aggregate interest generated by the entire system (industrial and financial).

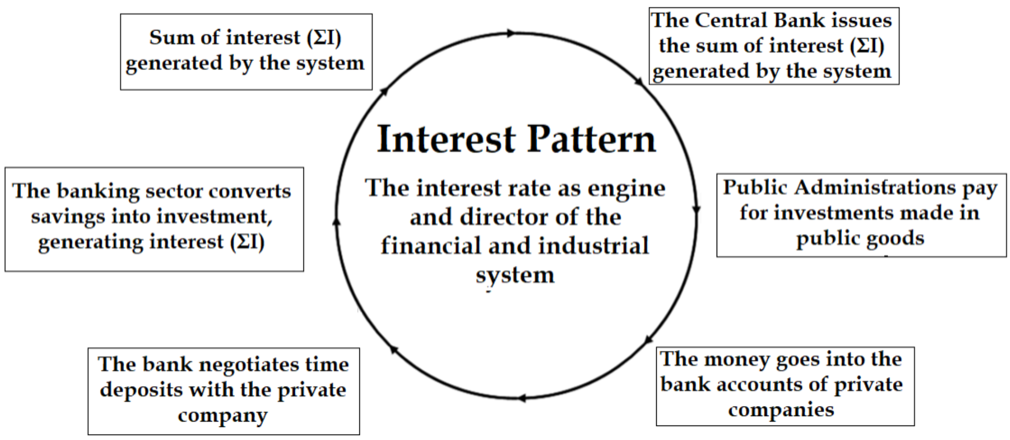
b) The new money will be distributed among public administrations depending on their level of activity, for the payment of public investments (ports, roads, hospitals, etc.): capillarity.

c) The money will enter the accounts of private companies,

d) and the banks, negotiating with private companies, will use this money to grant new loans.

e) The new credits will generate interest and the interest aggregate *(ΣI)* will cause the issuance of new money the following month, restarting the monetary cycle.

We are facing a circular monetary process, as demonstrated by the following image:



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With this simple circular mechanism, we will have achieved several goals:

1) First, the industrial and financial markets will be perfect and automatically coordinated by the interest rate.
2) Second, the four fundamental variables (4FV) will evolve proportionally.
3) In this way, savings and investment will always have the same sign, one of the essential pillars of liberal economic policy.
4) *The Interest Pattern*, regarding *The Modern Monetary Theory,* has another advantage. He has a mathematical emission ceiling to avoid monetary inflation.

The interest rate becomes the director and driving force of the financial and industrial system, overthrowing the four current failed directors, who are:

a) The Government, with the public debt
b) The Central Bank, by issuing money
c) Entrepreneurs through monetary substitutes: promissory notes, bills of exchange, etc.
d) And private banks using the fractional reserve banking system.

Such a simple mechanism of issuing and distributing money I called the Interest Pattern or Interest Standard.

We are facing the greatest evolutionary economic conceptual framework of the last five hundred years, since the end of the Middle Ages. But this theory, which was taking shape, had to be demonstrated empirically. It would be necessary to verify that this logic was supported by reality.

7. *Empirical verification of the Principle.*

According to this monetary theory, in a healthy economy, interest aggregate (ΣI) should be equal to public investment, since the new money will be used to pay for public goods built by private companies. In this way, money will always represent previous and effective work (public good). But is this monetary phenomenon observable in reality?

After many efforts in locating the data, it was a great surprise to see how empirical evidence confirmed this theory. Thus in Spain, the data on public investment and the net aggregate of interest generated in the financial system have been:

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	Millions Euros	
Year	Public Investment	Interest Aggregate
2011	39,935	35,051
2012	27,148	30,332
2013	23,276	30,300
2014	22,428	27,291
2015	27,244	27,640
2016	21,901	30,332
2017	23,183	23,968
2018	25,175	24,150
2019	25,372	24,179
2020	25,187	24,172
2021	20,681	23,829
2022	24,518	24,415
2023	33,446	37,244

Source: Banco de España + IGAE

But in the future, these figures will not be similar, but the same, given that both columns will be located in the assets and liabilities of the future National Balance of Money Supply.

National Balance Sheet Money Supply	
Asset	Liabilities
Public Goods	Money Supply

8. *Consequences that the Principle will have*

The Progressive Growth of the Money Supply Principle is the monetary anchor that would limit the debauchery of different monetary actors, for the money value is stable. With the *Interest Pattern* you can, in one fell swoop, eliminate:

- The **monetary dominance** that the Central Bank exerts in the market when issuing money. *The Progressive Growth of the Money Supply Principle* is the lost monetary anchor.
- Except in extreme situations, public debt will be prohibited, so there will be no **fiscal dominance**. All public investment will be monetized up to

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the limit set by the *Principle*. The primary deficit must be zero (see more details in the book on Tax-Flat and extraordinary monetizations).

- **Banking dominance** will also disappear with the prohibition of fractional reserve banking systems. See more details in the book about the Myth of the Monolithic Monetary Block that would generate this ban.

From a doctrinal point of view, the reader has just witnessed two crucial events in the history of economics: 1) In the first place, the interest rate staged a coup d'état and overthrew the failed and hackneyed coordinators of the four fundamental variables, crowning himself the sole director of the monetary orchestra. The interest rate is the only reliable tool that gives us a precise and real value of the new money that an economic zone needs to maintain the purchasing power of money. In the future, the Central Bank will limit itself to issuing money according to the aggregate interest (ΣI) of the preceding period and will not intervene, directly or indirectly, in the formation of the interest rate. 2) Likewise, the reader has witnessed the unveiling of one of the greatest enigmas of the economy during the last five hundred years: determining the mathematical amount of new money that the market needs.

9. *Implementation of these ideas in some countries*

No country in the world issues money according to the Interest Pattern. It is the first monetary theory that ex-ante allows us to know with certainty the amount of money to be issued to maintain its purchasing power.

We are working on the dissemination of these ideas since more than 150 countries have monetary identity problems.

With the knowledge we have today:

1) **Inflation has ceased to be a monetary phenomenon and has become a political phenomenon.** If politicians want to put an end to monetary inflation, today we have enough knowledge (Interest Pattern) to be able to control it.

2) It is absurd that Argentina or any country is dollarized. The Austrian School of Economics (ASE) is really strong in everything except monetary theory. That is why many Austrians long for the Gold Standard and others for free issuance of currency. Precisely because the ASE does not have a cutting-edge monetary theory, Austrian economists defenders, such as Javier Milei, leave all doors open. The American Plan (ISBN 9788409557349) is against dollarization for 17 technical reasons and other comparative economic reasons. The more

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> Argentina embraced the dollar, the worse things got. For all these reasons, one of the objectives of the American Plan is to expel the dollar from the minds of Argentines in the first term. Exactly the opposite of what many Argentine economists defend.

Argentina is in an extreme situation, but it can turn this situation if it transforms its fiduciary economy into an economy with a store of value through the *Interest Pattern***.** Few countries in the world could adopt the Interest Pattern. Few countries in the world have the characteristics of Argentina: rich, cultured, democratic, independent of blocs and... they are up to their necks in water.

10. How capitalism will work.

In two centuries the economy will work as follows:

1) The Central Bank will have automatically established the exact amount of money to be issued (ΣI). It will be a constitutional rule; the breach of which will be criminal and severely punished.

2) In the future, public administrations will not be able to issue public debt, since the Central Bank will deliver to them, month after month, the money that, in pure economic logic and mathematical rationality, the market needs; therefore, waste and megalomaniacal works will be difficult to execute.[7]
All public services will be covered by fees. (i) When a fee cannot be applied to a public service, for example, the expense of the State security forces and bodies, their expense will be met through taxes. But taxes should be an exception to the system and not the general rule. (ii) In extraordinary circumstances Parliament will authorize ad hoc issues of money (see more details in the book)

3) On the other hand, the banks will lose the privilege of the Fractional Reserve Banking System (scriptural money), since this privilege encourages economic cycles and weakens the balance sheet structure of any bank entity: negative working capital. See more details in the book *Pattern Interest* the chapter regarding *the myth of the monolithic monetary block* that this ban would create, a myth that all defenders of the fractional reserve fall into.

4) All payments between industrial and commercial companies will be made in cash. In the same way that we pay in cash when we go to buy a baguette

[7] In Spain, during the euphoria of the bubble at the beginning of the century, politicians even built two airports (in Ciudad Real and Castellón Province) that were closed for years, as they were not profitable due to the low air traffic in the area.

or when we go to have a beer, the operations between industrial or commercial entrepreneurs will be carried out in cash. If a company wishes to grant loans to its clients, it will have to establish a financial company that will be governed by criteria very similar to that of deposit institutions (banks). The financial company will give a credit to the client, which will be used to pay the invoice of the group's commercial or industrial company. Therefore, industrial and commercial activity will be separated from financial activity. With this measure, we will achieve:

- The prohibition of monetary substitutes, which have historically distorted the logical monetary block in circulation. For the Interest Pattern to carry out its work, we cannot allow back doors to circumvent the entire monetary coordination mechanism. If a private company wishes to make a large issue of bonds, promissory notes, etc., it must request special authorization from the Central Bank. If the amount is small, it will only have to notify its printing and issuance conditions (see more comments in the book)
- This measure will favour trade and increase GDP due to the certainty of operations. This is so because, as capitalism matures and new economic activities appear, the weight of services in industrial and agricultural activity is increasing; In other words, the added value that, year after year, man adds to the products of the land is higher. Service companies (SMEs), by collecting their invoices in cash, will be able to reach cruising speed faster and more robustly than with the current model.
- By separating the industrial and financial activity of the companies, we will ensure that all companies present greater solidity and clarity in their financial statements. More than 80% of European companies do not exceed two years of life due to financial problems. The economy will be more robust.

The Interest Pattern will eliminate two great viruses that have plagued society for as long as we have a solid record, since classical Greece:

1) The virus of economic cycles. In the future, there will be economic fluctuations, but economic depressions will disappear.
2) Finally we will destroy the biggest engine of social differences in history: the crazy printing of money.

The Interest Pattern will be the tool that economists will use in a few years to issue money, for being a solution that cannot be manipulated, robust, logical and seamless due to the simplicity that defines it. Let us remember what

Leonardo Da Vinci said about the simplicity of solutions: "Simplicity is absolute sophistication".

As that today it is difficult for us to understand how England could become the first world power at the end of the 18th century, with more than 700 monopolies managing its economy (of pins, bricks, tobacco, cotton, etc.) it will be difficult for the 24th century economists to understand how our economy works: the pre-capitalist economy.

A more serious economy, with a store of value, is possible.

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