Abstract

In recent years, a growing number of economic historians have argued that countries with well-developed financial institutions have faster rates of economic growth due to financial innovation. Missing in this "finance-led growth" literature is the due emphasis on the importance of paper currency as a financial innovation. Adam Smith argued that one of the main benefits of the introduction of a paper currency was that it resulted in significant savings on the resource cost of the monetary system by replacing specie (usually gold and silver), with paper bank notes, which is a much less costly medium of exchange. Smith argued that this resource cost savings was one of the main drivers for Scotland's high rate of finance-led growth in the late 1700s. Some economists and notable figures in financial history emphasized this concept resource savings as the primary benefit of paper currency over a strict commodity standard, yet it seems most modern economic historians have neglected the importance of this resource savings. This article examines the role that resource savings of paper currency played in the finance-led growth of Scotland and England, and examines the relevance of the argument in historical debates over ideal monetary systems.

Honors College
Ball State University
Muncie, IN 47306