Money in a Credit Economy in the Presence of Shocks

Abstract: I model an economy where the agents participate in gift exchange (credit relationships) supported by complete knowledge of all past transactions. There is a small probability that the record system breaks down. I show that the presence of money makes gift exchange more likely to emerge in the first place. With money, the agents become more specialized and the welfare is higher even though money exists only as an option when a bad shock is realized.