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THE
THEORY AND PRACTICE
OF
BANKING.

THE
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OF
BANKING.

BY

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Testimony is like the shot of a long bow, which owes its efficacy to the force of the shooter; argument is like the shot of a cross bow, equally forcible whether discharged by a giant or a dwarf.—BOYLE.

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P R E F A C E

TO THE

S E C O N D E D I T I O N .

THE earlier part of this Work has been entirely remodelled. When the first edition was written, the Author found the fundamental principles of the current books on Political Economy so unsatisfactory, that he was obliged to examine them at considerable length. Since then he has published the *Elements of Political Economy*, and especially the *Dictionary of Political Economy*, in which the foundations of the Science are thoroughly examined; and, therefore, it is less necessary to do so in a Work specially devoted to Banking.

In this edition, those fundamental conceptions and general laws only are investigated, which are exclusively necessary for the Theory of Credit.

Since the first edition was published, the doctrines established in it have constantly obtained increasing influence.

After pointing out the arithmetical errors, and the unphilosophical conceptions upon which the Bank Act of 1844 is founded, and also that the theory it seeks to enforce was expressly condemned by all the great Banking authorities of former times, the Author demonstrated that the only true way of controlling the

Paper Currency, or Credit, is by sedulously adjusting the Rate of Discount by the Bullion in the Bank, and the state of the Foreign Exchanges.

This doctrine, but very imperfectly understood, and extremely unpopular at that time, is now universally acknowledged to be the true one, and is adopted by all the great Banks in Europe. The Usury Laws in France have been modified in order to enable the Bank of France to adopt it.

An Imperial Commission was subsequently appointed to examine into the whole subject of the Usury Laws, with a view to their abolition, before which the Author was examined as a witness.

In the former edition an attempt was made to investigate the Theory of Accommodation Paper, and to point out exactly wherein its true danger consists. In 1861, the failure of *Laurence, Mortimer, and Schrader*, popularly known as the great leather fraud case, took place. In his very long and elaborate judgment in this most important commercial case, Mr. Commissioner Holroyd quoted the explanation given in this work at great length, thereby giving the sanction of his high authority to its correctness.

In 1862, M. MICHEL CHEVALIER presented an elaborate report on the Author's Works to the Academy of Moral and Political Sciences of the Imperial Institute of France, in which he declared his unreserved adhesion to their principles. This report was published at length in the *Journal des Economistes* for August, 1862.

In 1863, M. HENRI RICHELOT, a gentleman holding a high position in the Ministère du Commerce, published a volume entitled "*Une Révolution en Economie Politique: exposé des Doctrines de M. Macleod*," giving a full exposition of the doctrines maintained in the Author's Works. M. ROUHER, then Minister of Commerce and Agriculture, ordered this Work to be officially distributed to all the Chambers of Commerce in the Empire.

The subject of Credit and Banking has assumed such increased importance in recent years, that the Emperor has appointed an Imperial Commission to investigate it thoroughly. The Commission has drawn up an exhaustive series of questions, and requested the Author to send in an answer to them.

There can be but little doubt that a similar course must before long be adopted in this country. Symptoms are not wanting to warn us of the approach of one of those periodical monetary cataclysms which have always been attended with such terrible consequences. When that event occurs, if not before, a searching inquiry must be instituted into the whole subject, and then the Author hopes that it will be made manifest that the principles maintained in this Work, which are in strict accordance with, and a development of, those of the most celebrated authorities of former times, are proved to be true equally by Reason and Experience.

CAMPDEN HILL,

May 4th, 1866.



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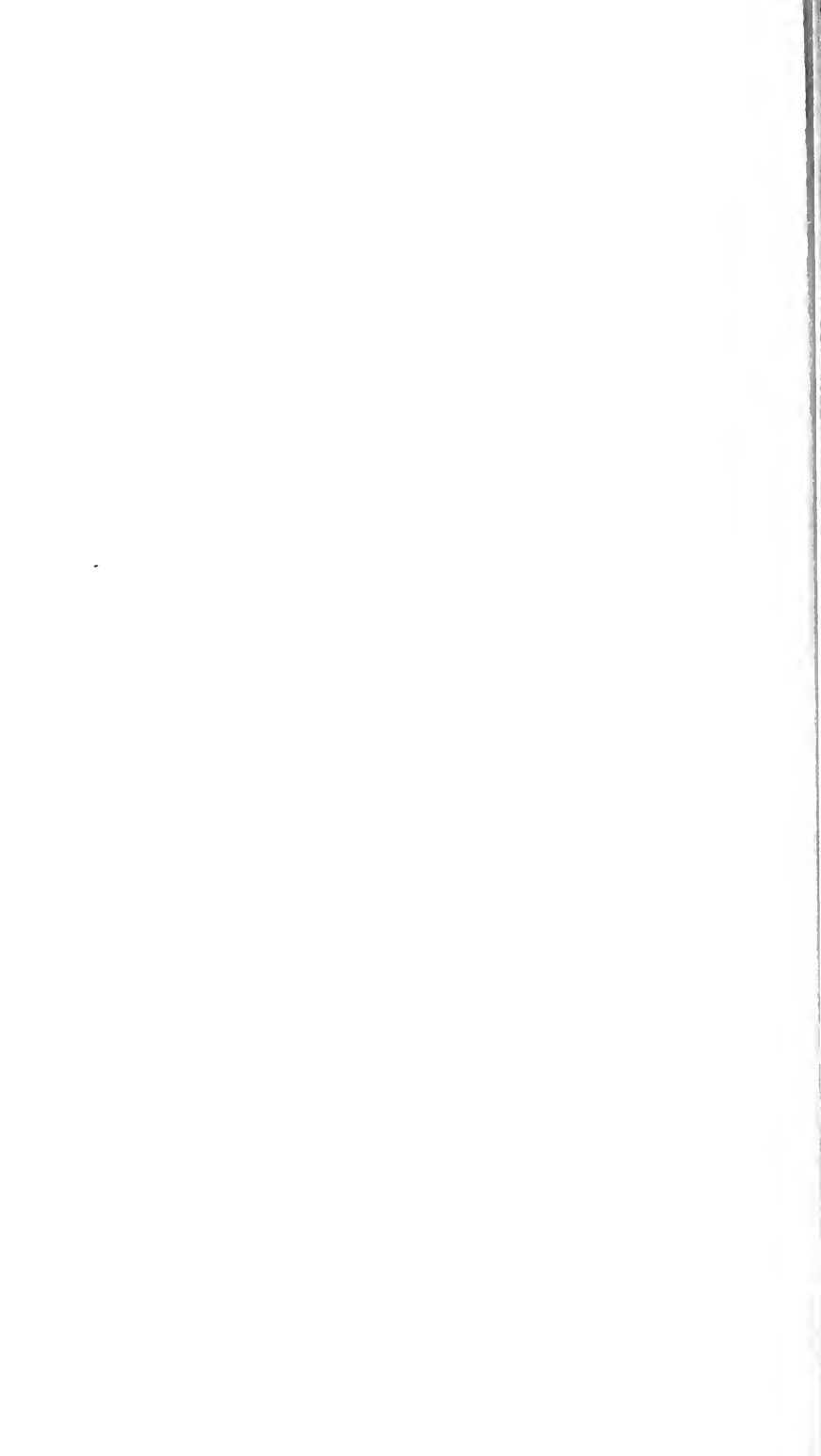
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THE

THEORY AND PRACTICE

OF

BANKING.

INTRODUCTION.

THE following work is an attempt to explain, in as clear and simple language as possible, the elementary principles of Currency and Banking, their progressive development in practice, and the laws at present affecting them.

Many of the works already existing on these subjects are excellent in several respects, and contain much valuable information; but it must be admitted that the widest and most fundamental differences of opinion upon almost every point prevail amongst them, and that there is no one so comprehensive and systematic, or which has investigated the subject with such accuracy, as to be generally accepted as an authority.

The fact of so many conflicting and contradictory views prevailing among writers, certainly argues the necessity for a more thorough consideration of the subject, but it acts as a warning against undertaking lightly what has hitherto produced so little that is generally received as satisfactory.

It appears that what is required, and what is most likely to lead to satisfactory conclusions, is a more careful investigation and examination of the fundamental conceptions and general laws of the subject, before considering their application in practice.

It appeared, therefore, that there was room for a work which should endeavour to treat the subject more as a science; and in a more methodical and systematic manner than has hitherto been done. Like every other science whatever, the monetary system has ideas and principles which are peculiar to itself, and if these could be as thoroughly and carefully investigated as is done in every other science, it would necessarily assist in removing some of the differences of opinion and contradictory views on the subject. It is because such care has been taken in ascertaining

and settling the elementary ideas and principles of the physical sciences that they are so well understood, and so few differences of opinion prevail about them; and it is because such care and attention has never yet been bestowed upon settling the definitions and elementary principles of Monetary Science, that it is still in so confused, controverted, and unsatisfactory a state.

Considering, then, the great importance of the subject, it is certainly desirable that some attempt should be made to supply this want, and the following work is a contribution towards it.

One great difficulty that besets this subject is the extremely unsatisfactory state of the great science of Political Economy, of which Banking and Credit are in modern times one of the principal divisions.

At the last meeting of the British Association, Lord Stanley, the President of the Economic Section, said that, in his opinion, Political Economy, in its present state, is rather a collection of practical maxims, supported by reason and tested by experience, than a science in the same sense as astronomy and optics. This opinion is, to a great extent, but not altogether, true; and this leads to some general considerations regarding the science of Political Economy.

If there be one race of men more than another to whom the undying gratitude of future generations is preeminently due, it is that illustrious band of thinkers in France, Italy, Great Britain, and Spain, who, during the last and present centuries, have founded the Science now called Political Economy, and brought about that great revolution in opinion which, after a long and arduous struggle, finally established the doctrines of Free Trade in this country.

But, however deep our debt of gratitude to them may be, and however warmly we may acknowledge it, it is not given to any men, however illustrious, to arrest the progress of thought, and to impose limits upon Science. It is the sacred duty of those in succeeding generations, who would aspire to walk in their steps, to sift and examine their doctrines by the light of further experience, even as they examined the doctrines of their predecessors, and to carry on the Science from whence they left it.

It has happened, we believe we may say with scarcely an exception, that every Science has undergone a complete transformation, from the mode in which it was conceived by its founders. And there is, besides, in every science, a certain stage, at which it becomes necessary to introduce more powerful and refined methods of investigation, more comprehensive forms of expression, and more minute and exact observations.

The science of Political Economy, as it is commonly called, forms no exception to the usual progress of science. It has already undergone one transformation from the conception of

its founders, and it is now in the course of undergoing a second and final change of conception of its nature and limits.

In fact, the history of Political Economy bears a strong analogy to the history of optics. In this latter science two different theories of light were thought of very much about the same time—the corpuscular and the undulatory. The former obtained the adherence of the great name of Newton, and made great progress. The latter, though adopted by so distinguished a name as Huyghens, languished for upwards of a century, overshadowed by the authority of its rival. Time, however, has been on the side of truth, and the undulatory theory, though bitterly assailed with the most contemptuous abuse, now holds undivided supremacy.

It is very much the same with Political Economy. The same year, 1776, gave birth to two works, the *Wealth of Nations*, and Condillac's *Traité de Le Commerce et le Gouvernement*. The former professed to treat of the production and distribution of wealth, the latter defined Economic science to be the science of commerce or exchange, or production and consumption, giving the words production and consumption the meaning we have given them. The work of Adam Smith immediately obtained wide and permanent popularity: the work of Condillac was utterly unheeded, and is even at the present day scarcely known.

Highly as we may esteem the great Economists of this and other countries, it is essential to bear in mind the character of the great Economical contests up to the present time. They have been almost entirely *destructive*. They have been to beat down and abolish false doctrines of various kinds: to extirpate bad and mischievous laws, interfering with the natural order of things: to abolish Legislative interference with wages, with prices, with the interest of money, and with the commercial intercourse of nations: to establish, in fact, freedom of contract. And in this Economists of all schools are thoroughly agreed.

The Repeal of the Corn Laws in England, in 1846, may be regarded as the close of the destructive era of Economical Science in this country. We have now arrived at a new and distinct phase of the science; that, in fact, in which the period of *destruction* has ended, and that of *construction* has come.

Now, without going into too much investigation, it may be stated that the judgment of the majority of the most distinguished Economists in Europe is gravitating to the opinion that the definition of Economic Science adopted by Condillac in 1776 is the true one; and, in fact, the only one which can be adopted as the basis of a distinct Science.

The Author of this work has elsewhere investigated the history of ideas on the nature of Economic Science, and given, as he thinks, ample and overwhelming reasons for adhering to this

view, which numbers among its supporters, besides ARCHBISHOP WHATELY, the most brilliant of the modern French Economists, FREDERIC BASTIAT and MICHEL CHEVALIER.

Thus Whately says: "The name I should have preferred as the most descriptive, and, on the whole, least objectionable, is that of CATALACTICS, or the "Science of Exchanges. * * * I think it for this reason more convenient, on the whole, to describe Political Economy as concerned universally and exclusively about *exchanges*."

The Definition of the Science we have offered is this:—

POLITICAL ECONOMY, or ECONOMIC SCIENCE, is the Science which treats of the Laws which govern the relations of Exchangeable Quantities.

And M. Michel Chevalier has expressed his opinion that this is the best definition of the Science that has yet been proposed.

We have also shewn that this view is in strict accordance with the meaning of the word. For *oikos* is the term in Attic Law to denote all a man's substance, or property, of whatsoever nature; and, therefore, Economics is the natural term for denoting the Science which treats of the Value, or the Exchangeable relations, of Property.

Be that as it may, however, it is an undoubted fact, that there is a great Inductive Science, which treats of VALUE, or of the relations of Exchangeable Quantities, which is a Science as certain, as definite, and complete as astronomy, optics, or any other Physical Science whatever.

This great science is based upon certain fundamental conceptions, and upon certain general laws.

Many persons are apt to think that controversies in Political Economy are mere logomachy, vain and unprofitable disputes about words, and of no real consequence. They are apt to think the Physical Sciences treat about things, and Political Economy only about words. But those who think so display a total want of knowledge of the history of science. The early history of all sciences is full of controversies about the meaning of words. Many may think that Physical Science being about things, there is no difficulty in giving a name to what is seen so readily. This is a lamentable error. On the contrary, it almost invariably happens, that names get into a science, and acquire a position in it before any one can tell precisely what they mean. Thus, in mechanics, the words *Momentum*, *Vis viva*, *Uniform Force*, *Accelerating Force*, and several others acquired a position in it before any one could tell what they really meant, and all the philosophical world of the day was engaged in the wordy war to settle their meaning, and obtain true definitions. Consequently, it is an entire error to suppose that controversies in Physical Science are not about words. On the contrary,

it was in the true definitions of words that the whole foundations of these sciences are laid. And it was just because all the great mathematicians of the day so thoroughly understood the supreme importance of ascertaining the true meaning of words, and sought out the meaning of each separate one with such perseverance, that they at length arrived at such unanimity of agreement, and these controversies have now been almost forgotten. Few persons are aware of the wrecks of the fierce controversies which lie buried beneath the calm and placid surface of modern science, like those of mighty armaments below the summer sea.

And why has Political Economy not yet attained the same rank as mechanics as an exact science? Because the same care has never yet been given to settle its definitions and axioms. Economic Science is now, like mechanics in its early stages, overrun and infested with words, whose meaning has never yet been settled on certain principles, and which are scarcely ever used by any two writers in the same sense, nay, few even of the best writers are consistent with themselves. The men who have cultivated Economic Science are probably of as great natural ability as those who have cultivated Physical Science; of course, with the exception of certain unapproachable examples. Why then have they not come to the same unanimity as their brethren? The simple reason is that they have not adopted the only means that could by any possibility ensure success, namely, a thorough discussion and settlement of the meanings of words, nay, they have systematically despised it. Now what the words *momentum vis viva*, &c., were to mechanics in its early stages, that *wealth*, *value*, *currency*, *capital*, &c., are at the present day to Economics.

And yet there are writers, of no mean acquirements too, who entirely discourage such a course of proceeding, who consider such a course pedantic, and mere waste of time—who would admit that in every other branch of human knowledge clear and precise technical terms are absolutely indispensable, and yet, in Economics alone, think there is no need of anything of the sort. Now we affirm that if Economics is ever to emerge from the turbid regions of *opinion* into the serene atmosphere of *demonstration*, it can only be done by Economists laying aside the unhappy idea that controversies about words are unimportant and superfluous, by following the example of their brethren the Physicists, who have cleared their path to such brilliant success, and, by bringing their whole force to discuss and settle the first elements of the subject, namely, its Definitions and Axioms; and when this is done it will be found that Economics is a science as clear, as precise, as sharply defined, and as capable of being erected into an exact science as any other whatever.

Let us give an example or two of the supreme importance of settling the fundamental conceptions of Economics. Archbishop

Whately says of the definition of WEALTH: "It were well if the ambiguities of this word had done no more than puzzle philosophers. One of them gave birth to the mercantile system. * * The results have been fraud, punishment, and poverty at home, and discord and war without. * * *It has for centuries done more, and, perhaps, for centuries to come will do more to retard the improvement of Europe than all other causes put together.*"

Is it of no importance to determine the true Definition of WEALTH?

So, the same writer says of VALUE: "As value is the only relation with which Political Economy is conversant, we might expect all Economists to be agreed as to its meaning. There is no subject as to which they are less agreed."

Another doctrine, which was implicitly believed in for 200 years, by the most eminent statesmen, was the "Balance of Trade." Now, J. B. Say says, that during the last 200 years, during which statesmen were blinded by this strong delusion, no less than *fifty* were spent in commercial wars arising directly out of this stupendous folly. Fifty years of war, with its unutterable horrors, waged for a chimera—a fiction—a thing which had absolutely no existence at all!

Are true views of Economics of no importance to mankind? Economics has turned the light of science on a single expression, and the result has been to destroy a fallacy which let loose upon the earth the demon of war for 50 years!

Again, the Bank Act of 1844, one of the most important Acts in the Statute book, is founded on a peculiar definition of the word CURRENCY, and is for the express purpose of carrying out a peculiar Theory of Currency.

The definition of currency upon which it is based is a modern innovation, quite contrary to the doctrines of the older writers; and the Theory of Currency which the Bank Act of 1844 was intended to carry out, has been repeatedly tried in practice, it has been found uniformly to fail, it was expressly condemned by the Bullion Report of 1810, and by all the great banking authorities of that age, by the framers of the Act of 1819, and by Sir Robert Peel himself so late as 1833.

Now, at certain periods of commercial crisis, the whole fabric of British commerce is menaced with utter ruin, on account of a peculiar *definition* of CURRENCY, and a peculiar *theory* of Currency.

Is it not of the deepest national importance to institute a thorough and searching investigation as to the accuracy of that peculiar definition of currency, and the soundness of that peculiar Theory of Currency?

The great founders of Economic Science wrote when the public and the administration were infected with an immense

mass of noted prejudices, errors, and abuses. Their first efforts were, therefore, naturally directed to sweep these away. The early treatises were filled with long controversies and discussions, which, though of the greatest importance at that time, may now be dismissed in a few lines. But, as in all young and growing sciences, further experience and new phenomena have shewn that many of the early opinions and doctrines require modification and correction. Many isolated doctrines have been established, and, on certain points, a considerable amount of truth has been ascertained. But this has never hitherto been formed into a coherent system, based upon general conceptions, after the manner of a physical science.

But the time has now arrived when this must be done. During the last century vast masses of facts have been accumulated, on every single point the most conflicting opinions have been put forth, so that it is probably not possible to say anything *new* upon any one of them.

The time has now come to methodize, digest, and arrange this huge mass of materials; to examine each fundamental conception and each general law, in succession; to bring together all conflicting opinions on each point seriatim, and to judge them by the established standards of reasoning in inductive philosophy, and then by thus obtaining true conceptions and axioms from reality itself by proper methods, and not by arbitrary dogmatism—by proceeding step by step, definition by definition, axiom by axiom, may be built up a great science of Political Economy on everlasting foundations.

Now, adopting the general definition of WEALTH in its widest signification as given by Aristotle, and which is now seen to be the true one, as being everything that is exchangeable, we have shewn that there are *three* distinct species of exchangeable quantities, each of which may be exchanged with each of the others, thereby giving rise to six distinct species of exchanges. The *general* science of Economics comprehends the whole of these *six* species of exchange; and its general conceptions must grasp *all* the kinds of exchangeable quantities, and its general laws must grasp *all* the different kinds of exchange. The subject matter of this work comprehends only two of the six species of exchange, namely, the exchange of money for debts, and that of debts for debts.

This does not necessitate the investigation of all the fundamental conceptions of Economics, but only of some of them. However, such as are necessary must be made general.

This work, therefore, consists of three parts. In the first, the fundamental general conceptions which are necessary, such as *Wealth, Value, Currency, Money, Credit, Capital, &c.*, are thoroughly investigated. Next the General Theory of Value is investigated so far as is necessary for this subject. An exposi-

tion is then given of the actual mechanism of Commercial Credit and Banking, wholly independent of any particular application of it. Then comes an investigation of the Theory of the Coinage. An exposition of the Theory of the Exchanges concludes this portion.

Having thus investigated the abstract and theoretical science, we trace its rise and progress in actual application in several countries, and give an authentic account of the great Economic phenomena, such as the great commercial crises, and so on, which actually took place; the course of conduct of the Bank and the Government during each of them, and the diverse and conflicting theories which have been held. The reader himself, therefore, having all these facts and reasonings brought together into a comparatively small compass, can perfectly form his own judgment as to their merits, and which of them experience has proved to be true.

The concluding part of the work is an exposition of the practical business of Banking, and of the Laws which at present affect it.

CHAPTER I.

DEFINITIONS AND ILLUSTRATIONS

OF THE

TERMS USED IN MONETARY SCIENCE.

“ Καλὴ μὲν οὖν καὶ θεία, εὐ ἴσθι, ἡ ὀρμή, ἢ ὀρμῆς ἐπὶ τὸν λόγον· ἔλκουσον ἰὲ σαυτὸν καὶ γύμνασαι μᾶλλον ἢ τῆς δοκούσης ἀχρήστου εἶναι καὶ καλουμένης ὑπὸ τῶν πολλῶν ἀτολμασχίας, ἕως ἔτι νέος εἶ· εἰ δὲ μὴ, σὲ ὑαφεύξεται ἡ ἀλήθεια.”—*Πλάτο.*

“ Know well, then, that worthy and godlike is the zeal with which you rush upon definitions. Apply yourself to it, and practise it, while yet you are a novice—all the more, because it seems useless, and is called trifling by the vulgar: for if you do not, the truth will escape you.”

CHAPTER I.

DEFINITIONS AND ILLUSTRATIONS OF THE TERMS USED IN MONETARY SCIENCE.

WEALTH—PROPERTY—VALUE—MONEY, CURRENCY, CREDIT,
CIRCULATING MEDIUM, CIRCULATION—PRICE AND DISCOUNT
—SECURITIES FOR MONEY AND CONVERTIBLE SECURITIES—
CAPITAL, FIXED AND FLOATING—PRODUCTION AND CON-
SUMPTION, SUPPLY AND DEMAND—RATE OF INTEREST AND
RATE OF PROFIT.

On the Definition of Wealth.

Economists are agreed that their Science treats about things so far as regards their being Wealth. But what is *Wealth*? And what is that quality of things which constitutes them Wealth? Adam Smith entitles his work "*An Enquiry into the Nature and Causes of the Wealth of Nations*," but it is wholly impossible to discover from his work what he means by "Wealth."

There is one expression, however, which he uses in his introduction, which seems to give some indication of what he meant. He says "the real wealth, the *annual produce of the land and labour* of the Society," and, from the number of times this phrase is repeated throughout the work, we shall not be far wrong, if we consider that as the nearest idea of what he meant.

Now, on examining this phrase, it will at once be seen that it is ambiguous. It is not clear whether he means the annual produce of the land alone, and the produce of labour alone, or the produce of land and labour combined. It is probable that he meant the latter.

Whichever way we take it, it is manifest that the expression is far too wide; because if it be laid down absolutely that the "produce of land and labour," either separately or combined, is wealth, it follows that every useless product of the earth is wealth as well as the most useful, the tares as well as the wheat. Every useless work done would be wealth. Thus if a number of labourers were to raise a mound in Salisbury Plain, that would be wealth; so children's mud pies are wealth. In fact it is so clear as to require no further argument.

On the other hand, the definition is far too narrow, for even Adam Smith acknowledges things to wealth which are certainly not the produce of land and labour. Thus under the head of

fixed Capital he enumerates the useful and acquired abilities of the inhabitants, which he says are a capital fixed and realized in their persons, and which as they make a part of their fortune, so do they likewise of that of the Society to which they belong.

It has often been said that Adam Smith confines his work to *material* wealth. But we see from the above passage that this is an error. He expressly enumerates the abilities of the inhabitants as part of the wealth of the Society. Now, how are the abilities of the inhabitants the "produce of land and labour?" It is clear that abilities are not the produce of land, nor of land and labour combined; and though abilities may certainly be improved by labour, still it is manifestly absurd to call abilities the produce of labour. These by subsequent writers, whom we shall mention afterwards, are called Moral or Immaterial Wealth.

There are besides many other things which are "Wealth," which are clearly not the produce of land and labour. Thus cattle, timber trees, minerals in the earth, &c., &c. It is evidently quite incorrect to say that cattle, and trees, and domestic animals of all sorts, are the produce of land and labour. Labour may be employed in tending animals, though many valuable animals are not tended by any labour at all, but certainly animals are not the produce of labour. Nor is it correct to say that trees are the produce of labour.

Furthermore, the land itself is valuable; whenever a country becomes populated, the land itself, the simple space upon which houses are built is wealth. Now the land itself is certainly not the "produce of land and labour." The notion is clearly absurd.

Labour itself, as every one knows, is a valuable commodity. We speak of the labour market as of any other market. Now labour itself is certainly not the "annual produce of land and labour."

Hence, besides certain material products which are the produce of land and labour, we find enormous masses of wealth, which can in no way be described as the produce of land and labour, and we have already observed that there are two distinct species of wealth—material and immaterial.

But we shall find that there is a third species quite different from the other two, which is acknowledged to be wealth. Thus Smith says, B. ii., c. ii., "Let us suppose that the whole circulating money of some particular country, at a particular time, amount to one million sterling, that sum being then sufficient for circulating the whole annual produce of their land and labour. Let us suppose too that some time thereafter different banks and bankers issued promissory notes payable to the bearer to the extent of one million, reserving in their different coffers two hundred thousand pounds for answering occasional demands. There would remain, therefore, in circulation eight hundred thousand pounds in gold and silver, and a

million of bank notes, or eighteen hundred thousand pounds of paper and money together." Now we see by this extract, among innumerable others, that Smith fully recognizes the fact that these bank notes are exchangeable property, he puts the £1,000,000 of bank notes on exactly the same footing as the gold and the silver. He admits that bankers, by issuing this million of notes, augment by that much the mass of exchangeable property. Now what are these bank notes? They are simply so many circulating debts. They are a species of property which is also called CREDIT, whose nature we shall have to investigate at great length hereafter. All that we wish to observe here is, that Smith treats a million of paper currency exactly on the same footing as a million of specie, and that he admits that the creation of these debts augments the mass of exchangeable property. Now these circulating debts are certainly not the "produce of land and labour."

Here, therefore, is a third species of exchangeable property, of a totally different nature from the two preceding ones, of material and immaterial products. But there are enormous masses of property of a similar nature. A man who had £1,000,000 in the funds would be called a wealthy man. Are the public funds the produce of land and labour?

But in fact these are only part of a gigantic species of valuable property, which includes copyright, shares in commercial companies of all sorts, patents, the goodwill of a business, tolls, ferries, ground rents—which, in legal language, is termed incorporeal property—which in this country is worth many thousands and thousands of millions of money, which can by no possibility be called the annual produce of land and labour, either separately or combined.

Hence we see that Smith's definition of wealth—assuming that we have interpreted him rightly—entirely fails. It is at once far too wide and far too narrow. It *includes* a mass of things which can by no possibility be called wealth, and it *excludes* the immensely greater portion of what Smith himself admits to be wealth.

But such a definition of wealth is open to many further serious objections, which are patent from his own work.

If it be laid down absolutely that the produce of land and labour be wealth, then it clearly follows that if a thing be wealth at any time and in any place, it must be wealth at all times and in all places. Now, there is nothing more notorious than that a thing may be wealth at some times and in some places, and not at other times and in other places. This requires no examples to prove it.

But Smith, after telling us that the annual produce of land and labour is wealth, says, B. ii., c. ii., "A guinea—which may be considered the produce of land and labour—may be con-

sidered as a bill for a certain quantity of necessaries and conveniences upon all the tradesmen in the neighbourhood. The revenue of the person to whom it is paid, does not so properly consist in the piece of gold, as in what he can get for it, or in what he can exchange it for. If it could be exchanged for nothing, it would, like a bill upon a bankrupt, be of no more value than the most useless piece of paper."

We see thus exemplified the utter incongruity of Smith's conceptions of the very fundamental word in the whole Science. He first tells us that the produce of land and labour is wealth, and then he says that unless it is exchangeable it is not wealth. Now it is manifest that these two fundamental conceptions—produce of land and labour, and exchangeability—do not coincide, for we may have the produce of land and labour which is not exchangeable, and we have shown that there are stupendous masses of exchangeable property,—nay in this commercial country enormously the greater proportion—which are in no way whatever the produce of land and labour.

We may, therefore, without further discussion, dismiss the criterion of wealth as being the produce of land and labour, and adopt that of *exchangeability*.

2. And this is, in fact, the earliest definition of wealth. Thus Aristotle says, *Nicomachean Ethics*, B. iv., c. i. :—

Χρήματα δὲ λέγομεν πάντα ὅσων ἡ ἀξία νομισματι μετρεῖται.

"And we call Wealth everything whose value is measured by money."

Or rather we might say everything which is exchangeable—money itself being an exchangeable quantity.

The same idea appears in modern times, when Economics began to be studied as a science. Thus Baudeau, one of the most distinguished of the first school of Modern Economists, the Physiocrates, says, in his introduction to *Economic Philosophy* :—

"The objects proper for our enjoyment, either useful or agreeable, are called goods (*bîens*), because they conduce to the preservation, the propagation, and the well-being of mankind on the earth.

"But sometimes these goods are not wealth, because they cannot be exchanged for other goods, or be used to procure other enjoyments. Natural productions or the works of art, the most necessary or the most agreeable, cease to be wealth when you lose the possibility of exchanging them and to procure other enjoyments in exchange for them. One hundred thousand feet of the most beautiful wood in the world would not be wealth to you in the middle of North America, where you could not divest yourself of its possession by means of an exchange.

“The title of wealth, therefore, includes two things; first, the usual qualities which render the objects useful and agreeable, and fit for our use, which constitutes them *goods*; secondly, the possibility of exchanging them, which enables these goods to procure others for us, which is the thing which constitutes them WEALTH.

“This possibility of exchange supposes that there exist other goods for which they can be exchanged.”

So also J. B. Say says:—“The exclusive possession which, in the midst of a numerous society of men, clearly distinguishes the property of one person from the property of another, is that which in common usage causes this sort of goods to be the only one to which is given the title of WEALTH. * * * * * Thus among these are included not only the things capable of satisfying the wants of men directly, such as nature and society has made them, but those things which can only satisfy them indirectly, in furnishing the means to procure what satisfies them directly, such as money, *instruments of credit*, the public funds, &c.”

The only other writer whom we think it necessary to quote is Mr. Mill. He says:—“Everything forms therefore a part of wealth, which has power of purchasing; for which anything useful or agreeable would be given in exchange.”

In these passages we find a fundamental general conception of what *Wealth* is—it is anything whatsoever, whatever its nature be, that is exchangeable—which may be bought and sold—everything which can be exchanged separately and independently of anything else.

The only criterion, then, of anything being Wealth is this, can it be valued? Can it be bought and sold? Can it be exchanged separately and independently of anything else?

This criterion may seem very simple, and we have seen that it is admitted by many writers; but, in fact, to apply it properly, to discern what is and what is not separate and independent exchangeable property, requires a thorough knowledge of some of the most abstruse branches of law and commerce.

On the Three Species of Wealth.

3. When, therefore, we firmly grasp the fundamental criterion of Wealth, or of an economic quantity, that it is merely exchangeable property, and see that all notions of labour, utility, &c., are to be dismissed, it is clear that all things which can be bought and sold are economic quantities, or Wealth, and from what we have said, it appears that they are of *three* different species.

1st. Material products, such as corn, manufactures, houses, &c., &c., which every one admits to be Wealth.

2ndly. The economic quantities, which may be summed up

under the title of **LABOUR**. Every one who earns a living by an exertion of the mind, whether the instrument be the tongue or the hand, is a labourer. Thus professional men of all sorts, lawyers, doctors, clergymen, teachers, and all who give some personal service in exchange for a reward, may be classed as labourers.

A few writers have denied the admission of such things as knowledge into the category of wealth. It would occupy far too much space here to examine the arguments which they have brought forward, especially as it is not necessary for the main purpose of this work. It may be sufficient to say that this very question is the subject of the earliest economic treatise in existence. In a dialogue called *Eryxias*, which is on the Definition of Wealth, which is frequently printed along with those of Plato, and is attributed to Æschines Socraticus, though the critics deny its genuineness, the writer puts the following argument into the mouth of Socrates. After showing that the same things may be useful and exchangeable in some places and not in others, and therefore Wealth in some places and not in others, he proceeds—

“*Socrates*—But those things would appear to be wealth by which we could obtain what is useful to us.

“*Eryxias*—O Socrates, I could never be persuaded of this, that gold and silver, and other things of this sort, are not wealth. For I am firmly convinced that the things which are useless to us are not wealth, but that what is most useful to us for this purpose is wealth. Yet I am not sure if these things are not useful to us in life, if we can obtain what we do want by means of them.

“*Socrates*—Come, then, how shall we settle this matter? are there certain persons who teach music and reading, or any other science, and obtain in return for this instruction the necessaries of life as a remuneration for such things?

“*Eryxias*—Certainly, there are.

“*Socrates*—Therefore such men as these could obtain their living by such science, exchanging some of it for necessaries as we do for gold and silver.

“*Eryxias*—I agree to that.

“*Socrates*—If then they gain by this means what they require for their living, this thing would be useful towards their subsistence. For we said that silver was useful for this purpose, that we are able to acquire by it what is necessary for life.

“*Eryxias*—It is so.

“*Socrates*—If then these sciences are useful for this purpose, they appear to us to be **WEALTH**, for the very same reason that gold and silver are so, and it is plain that those who possess them are richer, &c., &c.”

The argument in this passage is perfectly conclusive. We

have shewn above that Adam Smith expressly enumerates the abilities of the people as Wealth. The great majority of modern writers have done the same, and give the name of Immaterial Wealth to this species, and Mr. Senior justly says the profits, or the sums given in exchange for these immaterial products, far exceed those given for material products.

We observe that we may absolutely part with the first species of economic quantities. Although immaterial products are vendible, and we receive a reward for exercising our faculties in some one's service, we do not part with them; we may sell our knowledge, but it is not gone away from us. Like a candle which communicates light to others, it does not diminish our own light. Though a man sells his instruction, it does not diminish his own store.

3dly. The third species of economic quantities are, however, of a different nature. Intangible and invisible, like the second species, they are yet transferable like the first, and when we exchange, or sell, them, we divest ourselves absolutely of the property in them, as we do of the first species. This property, such as copyright, shares in commercial companies of all sorts, instruments of credit of all sorts, the public funds, is technically known by the name of incorporeal property.

4. Now it is a matter of every day experience, that quantities of these three different species are the subjects of exchange. Thus we may exchange a material product for a material product, such as a piece of gold money for so much corn, or manufactures; we may exchange a material product for an immaterial one, such as so much money for so much instruction, or other personal service; or a material product for incorporeal property, as we may give money to purchase a copyright, a patent, as shares in a commercial company, or a bill of exchange, or bank note, or so much of the funds.

We may exchange an immaterial product for another immaterial product, as so much instruction of one kind for so much instruction of another; or an immaterial product for so much incorporeal property, as we may give so much instruction and receive a bank note, or a cheque, *i. e.* a debt, in exchange.

Or lastly, we may exchange one species of incorporeal property for another; thus we may buy or sell a copyright, or patent, for a bank note, or cheque, or bill of exchange. Or we may exchange, or sell, one kind of debt for another debt, as when a banker buys, or discounts as it is technically termed, from his customer, a debt payable at a future date, by creating a debt in his favour, payable immediately, which is the great business of Banking, and the subject matter of this volume.

Hence we see that there are three distinct species of economic quantities, which being all exchangeable *inter se*, and the subject

of commerce, give rise to six distinct species of exchanges. And it clearly follows that no general definition, and no general axiom or law, can be received as true in Economic Science, which does not apply to all the three species of economic quantities, and all the six species of exchange equally and indifferently. We may observe that one of the principal sources of error and confusion in economic science arises from the fact that most writers only contemplate one class of cases, namely, the exchange of material products against material products, and they lay down definitions and laws which only are even apparently applicable to that single class of cases, and not even in reality to that, and which the least experience and reflection shew are wholly erroneous when applied to other cases, and are therefore not general, and are manifestly false when applied to the last species of exchange, namely, that of debts against debts, which is the subject matter of this volume.

On some confusion in the expression National Wealth.

5. It is not only necessary to ascertain clearly the meaning of fundamental conceptions, but also to call attention to errors and ambiguities in the terms in common use. One of the most frequent of these is the expression "National Wealth." Such and such a thing is admitted to be individual wealth, but is denied to be National Wealth. Thus Mr. Mill says, "Funded property therefore cannot be counted as part of the National Wealth," and he compares the fundholders to the mortgagees on an estate, and the funds to a mortgage on the National Wealth, in which he is quite in error, as is more fully explained in the chapter on Credit. Now when such things as the funds, or debts, *i. e.*, credit, are spoken of, it is admitted that the man who holds so much stock, or so much credit, has wealth, *i. e.*, that the property is his own individual wealth, but it is said that it is not National Wealth. Now the ambiguity arises in the word National. No one would say that a man's debts are part of *his* wealth, although they may be, and are, exchangeable property. Now when we say that wealth means exchangeable property, the expression National Wealth, can only mean property which belongs to the nation in its corporate capacity, such as public lands, public forests, dock-yards, the navy, &c., which do not belong to any private individual. No one would say that property which belongs to individuals is national wealth. My money belongs to me and not to the nation. The funded debt is the right, or property, residing in certain individuals to demand certain payments from the nation, and therefore it is *their* wealth. It is sometimes alleged that when it is said that the funds are wealth, that it is maintained that they are National Wealth. But this only arises from the confused conception of the expression National Wealth. The funds are certain rights created by the nation in favour of

certain individuals who have done certain services to the nation, and they are similar to a debt created by an individual in exchange for services. When we say, therefore, that the funds are wealth, it means nothing more than this—that they are exchangeable property—they may be bought and sold. There is no assertion made that they are National Wealth.

On the Meaning of the Word Property.

6. We have in the preceding sections endeavoured to establish the fundamental conception that wealth, or an economic quantity, means nothing else but exchangeable property. We shall find that it will throw a flood of light over the whole of Economic Science, and remove all the difficulties to which the considerations regarding the word wealth have given rise, to understand clearly the original and true meaning of the word PROPERTY.

Most persons, when they hear the word Property, think of some material things, such as money, tables, chairs, houses, and other goods. But that is not the true meaning of the word Property. The real meaning of the word Property is a *Right* residing in some *person* to certain things. To apply the word Property to the things themselves is a comparatively modern corruption of the word, which we do not believe occurs in older writers. Thus in Bacon the word Property is never applied to lands or goods. Thus, he says that one of the uses of the law is “to dispose the Property of their goods and lands;” and he explains the different methods by which the “Property in land is got and transferred,” and of the various methods in which “Property in goods and chattels” may be acquired. In no single instance does he, or, we believe, any writer of his time use the word Property to denote the things themselves, nor can we state when this corruption of language began.

Property, therefore, in its real original sense, means *ownership*, or the Right residing in a person to some certain things; and when we speak of an *exchange*, it always means that the ownership, or Property, in certain things is ceded, or given in exchange for the ownership, or Property, in certain other things. Thus if we sell or exchange money for a book, it means that we exchange the Property in the money for the Property in the book. And there can be no exchange without the Property passing from one to another. If a man merely lends his horse or his book to a friend that is no exchange or transfer of Property.

7. Property, then, being a Right residing in a person, there are two grand divisions of Property, which are the subject of sale or exchange.

I. There may be Property in a specific material chattel which is already in existence. Thus we may have Property in a watch,

or a house, a horse, or a carriage, or any other goods. These things are in a complete state of existence. This species of Property is termed in English law corporeal property, because it is the Property, or Right, to a certain specific corpus.

II. But there is also a second species of Property, which is equally the subject of exchange. We may have a Property, or Right, wholly separate from and independent of any specific thing, and we may have a Property, or Right, to a thing, which is not even yet in existence. And this species of Property is termed in English law, INCORPOREAL PROPERTY, because it is Property separated from any specific corpus.

Thus a COPYRIGHT is the exclusive Right to receive the profits to be made by the sale of works of literature and art.

The GOODWILL of a business is the Property, or Right, to receive the profits to be made by the business.

A PATENT is the Property, or Right, to receive the profits to be made by the sale of a mechanical invention.

A SHARE in a Commercial Company is the Property, or Right, to share in the profits to be made by the trading of the Company.

A PRACTICE is the Property, or Right, to receive the profits of a professional business.

Besides these there are other species of Incorporeal Property which we need not mention here, as we merely wish to give a few examples.

There is one species of Property to which we must specially advert, viz., the value of land.

Suppose we purchase an estate in land for £100,000, where is the value for our money? Does it consist in things which have a present existence? The veriest tyro would answer—certainly not. Where then is the equivalent for the purchase-money?

Every one knows that the purchaser of the land buys the right to receive the actually existing produce of the land *together with* the right to receive its annual produce for ever, say £3,000 a year. Now, though these actual profits only come into existence at definite intervals of future time, yet the Property, or Right, to receive each annual profit when it does come into existence, is *present*, and may be bought and sold like the property in a table or chair. That is to say, that each of these annual future profits has a PRESENT VALUE, and the purchase-money of the land is simply the sum of the present value of this series of profits for ever.

Hence the present value of each of these future payments for ever is an actually existing article of Exchangeable Property, and, therefore, by our definition—Wealth.

Now we may say that when a purchaser has paid for the land, it owes him a series of annual payments for ever, and as he bought the land merely on the *belief* that he would receive them, we may call this the *credit* of the land.

Hence we see that the price, or value, of the land is made up of two distinct elements—the price, or value, of its past produce, and also the price, or present value, of its future produce.

Now a man exercising any profitable business is an economic quantity which bears in many respects a strong analogy to land. He may have accumulated a quantity of money, the fruits of his past industry. But he also produces a series of profits in the future, and of course he has a Property in them. Thus the value of man as an economic quantity, like that of land, is the Property in the products of his past industry, together with the Property in the products of his future industry. And there are two ways in which he may trade. He may purchase goods, &c., with his money, the fruits of his past industry; or he may purchase goods, &c., by giving in exchange for them the right, or property, to share in the produce of his future industry. And when he does so this right, or property, which he gives to another person is a species of incorporeal Property which is termed CREDIT, or a DEBT.

We must clearly understand that a Debt, or Credit, is not money owed by the debtor, but a Right, or Property, residing in the person of the Creditor to demand money at a certain period, and as it is a mere abstract right, wholly severed from any particular sum of money, it is incorporeal Property, of the same nature as copyright, &c.

This incorporeal Property called Credit or Debt, is of enormous magnitude in this country, and its creation, sale, or exchange, and extinction, is the great business of Banking, and the subject matter of this work.

On the Definition of Value.

8. Economic or exchangeable quantities are, as we have seen, of three distinct species, corporeal or material, immaterial, and incorporeal, each of which may be exchanged at any time for any of the others, giving rise, as we have shewn above, to six distinct species of exchange. Now, if at any given instant, any economic quantity A be exchanged for any given economic quantity B, then the quantity A is termed the VALUE of the quantity B, and B is likewise termed the VALUE of A. Now as each of the three species of economic quantities may be exchanged for either of the others, any quantity may have Value in terms of the others. Now suppose that at any given instant, 1 oz. of gold will exchange for 15 oz. of silver, then it is said that 1 oz. of gold is equal in value to, or of the value of, 15 oz. of silver, which is simply the following equation:—

$$1 \text{ oz. gold} = 15 \text{ oz. silver,}$$

which is the following proportion:—

$$\text{Gold} : \text{silver} :: 15 : 1.$$

Hence we see at once that value is the sign of equality between any two economic quantities, as Aristotle said long ago:—

Ἦ δ' ἄξία λέγεται πρὸς τὰ ἕκτ' ἀγαθὰ.

“Now the term VALUE is used in reference to EXTERNAL GOODS.”

We have then this definition—

The Value of any economic quantity is any other economic quantity for which it can be exchanged.

Hence any economic quantity has as many values as quantities it can be exchanged for, and, of course, if it can be exchanged for nothing, it has no value. This shews that there is no such thing as absolute value, or universal value, because there is probably nothing which can be exchanged universally throughout the world.

Now, without anticipating the general theory of value, which we shall have to discuss in the next chapter, we may observe that since a thing which cannot be exchanged has no value, the value of anything depends not upon the person who offers it for sale, but upon the desire of the purchaser. However much a person may wish to sell any product of his own, yet if no one will buy it, it has no value. If an exchange takes place, it can only do so from the reciprocal desire of each for the product of the other. Hence it is clear that *value necessarily requires the concurrence of two minds.*

Value, therefore, from the very definition, like distance, requires two objects. We cannot speak of absolute, or intrinsic, distance. An isolated object cannot have distance. If we are told a certain object is distant—we immediately ask—Distant from what? So it is equally clear that a single object cannot have value. If we hear of an object having value, we must always enquire, *Value in what?* And it is clear, that as it is absurd to speak of absolute, or intrinsic, distance, so it is equally absurd to speak of absolute, or intrinsic, value.

*On Money, Currency, Credit, Circulating Medium,
Circulation.*

9. We have shewn that the fundamental notion of the word Wealth, or of an economic quantity, is anything which may be exchanged, or bought and sold, whatever its nature be, and that there are three distinct species of economic quantities. There is one species of economic quantity, however, of such great importance, and which is so peculiarly the subject of this work, that we must devote special attention to it—and that is Money and Credit.

In the primitive ages of the world we have abundant evidence that there was no such thing as money. When persons traded they exchanged the products directly with one another. Thus we have *Iliad*, vii., 468:—

Νῆες δ' ἐκ Λήμνου παρέστουσιν οἶνον ἄγουσαι
 * * * * *

"Ἐχθεν ἄρ' οἰνίζοντο κάρη κομόωντες Ἀχαιοί,

"Ἄλλοι μὲν χαλκῷ, ἄλλοι ἔ' αἰθωνι σιδήρῳ,

"Ἄλλοι ἔ' ῥινόϊς, ἄλλοι ἔ' αὐτῆσι βόεσσιν,

"Ἄλλοι ἔ' ἀνῆριπύθεσσι.

From Lemnos' isle a numerous fleet had come

Freighted with wine. * * *

* * * * * All the other Greeks

Hastened to purchase, some with brass, and some

With gleaming iron; some with hides,

Cattle or slaves.

Lord Derby's translation.

The inconveniences of this method of trading are palpable. What haggling and bargaining it would require, to determine how much leather should be given for how much wine; how many oxen for how many slaves! Some ingenious person would then discover that it would greatly facilitate traffic, if the things to be exchanged were referred to some common measure. There are many passages in the *Iliad* and *Odyssey*, which shew that even while traffic had not advanced beyond barter, such a standard of reference was used. We find that various things were frequently estimated as being worth so many *oxen*. But it must be observed that these oxen did not pass from hand to hand like money. The state of barter still continued, as it is quite common at the present day where the precious metals are used as a common measure. Such a state of things in no way implied money, or currency, or circulating medium.

The necessity for money arose from a somewhat different cause. So long as the things exchanged were equal in value there would be no need for money. If it happened that whenever one man required the services of another, that other at the same time required an equivalent amount of service to be rendered in return, such transactions could take place with great facility, and the amount of services on each side being equal there would be an end of the business. But it would often happen that when one man required the services of his neighbour, that neighbour would not require an equal amount of service at the same time, or even perhaps any at all. If then such a transaction took place between them, with such an *unequal* result, there would remain due a certain amount of difference, or amount of service due from the first to the second, and this would constitute a *DEBT*—that is to say, a Right or Property would be created in the person of the creditor to demand something at some future time from the debtor.

The second would, however, require at some future time to have the balance of service due to him performed, and the debt discharged. Moreover, for his own security, he would like to

have some evidence, or memorial, to prove the debt, and accordingly he might require the debtor to give him some sign or token of the fact. If writing had been known in these days, a statement in writing acknowledging the debt, and promising to render the service due whenever called upon to do so, would be a natural form of such evidence.

We may now suppose that the second person has dealings with a third, and requires his services, but that the third has no immediate use for the services of the second, but requires those of the first. Now if the parties were so circumstanced, what would be more natural than for the second to transfer to the third the debt due to him from the first? A similar operation might be repeated an indefinite number of times, and so this written obligation, or this evidence of a debt, enabling the possessor of it to demand some service to be rendered by the debtor, would pass from hand to hand, or be *current*; and from this use of it the thing itself has, by a confusion of ideas, come in recent times to be called a CURRENCY.

This currency is nothing more than the evidence of service having been rendered for which an equivalent has not been received, but which may at any time be demanded. It is obvious that as soon as it has been rendered, the evidence of its being due must be given up to the debtor to be destroyed, and it will be no longer current. And if any man can render services to his neighbours, he must in return receive either other services, or the evidence of their being due; and if he renders more services than he immediately requires in return, he will accumulate a store of this evidence for his future wants.

These simple considerations at once shew the fundamental nature of a currency. It is quite clear that its use is to measure and record debts, and to facilitate their transfer from one person to another; and whatever means be adopted for this purpose, whether it be gold, silver, paper, or anything else, is a currency. We may therefore lay down as our fundamental conception that *Currency and Transferable Debt* are convertible terms; whatever represents transferable debt of any sort is *Currency*, and whatever material the currency may consist of, it represents transferable debt and nothing else.

10. That this is the true nature of money has been seen by many writers. Thus Aristotle says, *Nicomach. Ethics*, B. v., c. v.:—

Ἐπεὶ δὲ τῆς μελλούσης ἀλλαγῆς (εἰ νῦν μηδὲν δεῖται ὅτι ἔσται, ἐὰν δεηθῇ) τὸ νόμισμα οἷον ἘΓΓΥΗΤΗΣ ἔστιν ἡμῶν· δεῖ γὰρ τοῦτο φέροντι εἶναι λαβεῖν.

“But with regard to a future exchange (if we want nothing at present, that it may take place when we do want something,) money is as it were our security. For it is necessary that he who brings it should be able to get what he wants.”

So an old pamphleteer in 1710 (*an Essay on Public Credit*) saw the same truth. He says, "Trade found itself unsufferably straightened and perplexed for want of a general specie of a complete intrinsic worth as the medium to *supply the defect of exchanging*, and to make good the balance where a nation, or a market, or a merchant demanded of another a greater quantity of goods than either the buyer had goods to answer, or the seller had occasion to take back."

So also Baudeau, the Economist, whom we have already quoted, says:—

"Cet argent monnayé n'est dans la circulation, comme je l'ai dit antrefois, qu'un titre efficace sur la masse générale des jouissances utiles ou agréables qui font le bien-être et la propagation de l'espèce humaine.

"C'est une espèce de lettres de change, ou de mandats acquittables à la volonté du porteur.

"Au lieu de prélever sa portion en nature sur toutes les subsistances, et sur toutes les matières premières annuellement renaissantes, le souverain en exige en monnaie le titre efficace, le mandat, la lettre de change."

So also Adam Smith, in the extract we have already quoted in page 5, expresses the same idea; and the same thing has been observed by many other distinguished writers, whom it is superfluous to quote.

The necessity of having something to represent, and measure the debt that would arise from an unequal exchange, has been felt by most nations from a very early period. Different nations have used different substances for this purpose. The Hebrews we know used silver; although no money existed at the period of the Homeric poems, copper skewers were soon afterwards employed as money throughout Greece, which were superseded by the silver coinage of Pheidon. The Æthiopians were said to have used carved pebbles. Throughout the islands in the Eastern Ocean, and many parts of Africa and India, shells are still used. In Thibet, and in some parts of China, little blocks of compressed tea serve as money. Salt is used in Abyssinia; in Newfoundland dried cod was used in the last century, in the West Indies sugar, in Virginia tobacco. Adam Smith says that in his day a village in Scotland used nails. In some of the American Colonies powder and shot, in Campeachy logwood, and among the Indians of the American Continent belts of wampum served the purpose of a currency; and no doubt many other things have been used by other nations.

But when we consider the purposes for which money is intended, it is easily seen that no substance possesses so many advantages as *metal*. The use of money being to preserve the record of services being due to the owner of it for any future time, it is clear that it should not be liable to alter by time. A

money of dried cod would not be likely to keep very long, nor would it be easily divisible. One of the first requisites of money is that it should be divisible into very small fragments, so that its owner should be able to get any amount of services at any time he pleases. Taking these requisites into consideration, it is manifest that there is no substance which combines these qualifications so well as metal. It is uniform in its texture, and it can be divided into any number of fragments, each of which shall be equal in value to another fragment of equal weight; and, if required, these fragments can always be reunited, and form a whole again of the aggregate value of all its parts. By this means if we can establish a relation between the *quantity* of the metal and the *amount* of the debt, then whatever that relation be, or whatever quantity of metal be taken to represent any amount of debt, then any fragment of such metal will always represent a proportionate amount of the debt.

Such then is the fundamental conception of money, and we must carefully observe that we are not required to enter into any investigation here of the general laws which regulate the specific quantities of metal which at any time shall exchange with specific quantities of other things. Whether a greater or smaller quantity of metal is required to perform a certain function, the fundamental conception remains the same. Such an investigation is proper to a general treatise on Economics, but is not required for this work.

Now let us ask, why do people take a piece of money in exchange for services, or products? They can neither eat it, nor drink it, nor clothe themselves with it. They can make no direct use of it. The only use they can make of it, is to exchange it away again for something else they want. And the only reason why they take it is that they believe, or have confidence, that they can do so whenever they please. It is therefore what is called CREDIT. As Edmund Burke says of gold and silver, "the two great recognised species that represent the lasting conventional CREDIT of mankind."

Hence we obtain the fundamental definition or conception of Credit—

CREDIT is anything which is of no direct use, but which is taken in exchange for something else, in the belief or confidence that it can be exchanged away again.

Credit is therefore the right, or power of demanding something else when we require it. It is the right to a future payment; and we observe that it is not the transfer of something else, but is itself the name of a certain species of exchangeable property.

Now, as money is always exchangeable throughout the commercial community, it is evident that it has a general and a permanent value; that is, it is exchangeable among *all* persons and

at *all* times, and in *all* places of the same country. It is therefore the highest and most general form of Credit.

Some might say, however, that when a person has received money for his services he is completely paid. But this is not the case. Economists long ago pointed out that a complete exchange is always a barter, that is, some service is exchanged for a service. And the eminent French Economist, J. B. Say, most aptly calls a sale a *demi-échange*, which expression is strictly true.

So long as communities are barbarous and uncommercial, money in the form of some tangible material substance is the only form of credit, or pledge for future payment. And we see what a great extension it gives to traffic. But it is easy to see that trade would often be embarrassed for want of money itself; commercial and civilized nations therefore devised a new form of credit which has given a prodigious extension to commerce.

Supposing that a merchant wants to trade, but has no money to buy goods with. He may have good grounds for believing that if he had the goods, he could sell them with a profit. He goes to some one who possesses them, and if the owner of the goods believes in his capacity and honesty, he may sell him the goods, not for money, but for a pledge or promise to pay money at a future time. The owner of the goods gives the property in them to the merchant, and, in exchange for them, receives the Property, or Right, to demand so much money at a future time. And this Property, or Right, is called a *Debt*, or *Credit*. This Debt may be recorded on paper, for the convenience of transferring it; and such paper documents are called *Instruments of Credit*, and their nature and varieties will be more fully discussed in a future chapter.

Hence we see that credit and debt are merely two names for the same species of property. It is often supposed that a debt is money owed by the debtor; but that is an error: a debt is a right residing in the person of the creditor, to demand money at a future time.

There is also another expression in common use, which is apt to mislead. People are said "to give credit." Now what this may mean is not very clear. But it must be remembered there is no "giving" in the matter. Merchants don't give their goods away for nothing; nor do they incur debts for nothing. It must be clearly understood that, when a merchant sells his goods for credit, it is as absolute a sale as if he had received money for them. The property is absolutely gone away from him, and what he receives in exchange is the abstract property, or right, to demand payment at a future time; and when the time comes he goes and exchanges this property for money from the debtor, and gives up the property which is thereby extinguished. Hence we see that this property has been created and extinguished by the mutual consent of the parties.

Now, as we have observed above, that money is a species of property, or merchandize, quite distinct from commodities, and is exchangeable for them, but does not represent them, so it is easily seen that credit, or a debt, is also a species of merchandize quite independent of its ultimate payment. Our old writers all consider a bill of exchange (one form of recording a debt) as merchandize. It is one of the most elementary principles of law that a debt is a species of property. Thus says Mr. Williams, *Law of personal Property*, p. 5, "Choses in action (*i. e.* debts) having now become assignable, become an important kind of personal property." Again, p. 8, "A legal chose in action constitutes a valuable personal property." Also p. 155, "In addition to goods and chattels in possession, which have always been personal property, and to *Debts* which have long been considered so." And Mr. Justice Byles, in the preface to his *Treatise on Bills of Exchange*, published more than 30 years ago, says, "This species of property is now in aggregate value inferior only to the land or funded debt of the Kingdom." At the present day there can be no doubt that the mass of credit greatly exceeds the funded debt. The fact also that debts are exchangeable property is fully admitted by all Economical writers. We have observed above that Adam Smith admits that bankers by issuing notes augment the quantity of currency by so much. All writers when speaking of bills of exchange enumerate them, and rightly, as so much independent property. As money is a merchandize used to circulate commodities when there is either no, or an unequal, exchange, so credit is used to circulate money, and commodities, when there is no money. Daniel Webster, the American orator and statesman, says truly, "Credit is to money what money is to commodities."

The only real difficulty in the case consists in understanding that credit is the name of a certain species of incorporeal exchangeable property, whereas it is very commonly supposed to be the *transfer* of something. But we hope we have removed any doubt on that subject, if any remained. This species of property may be bought and sold exactly like any other, and is so to the amount of many millions of money daily. There are shops for the express purpose of buying and selling this species of property. As there are shops for dealing in bread, clothes, furniture, &c., so there are shops for the express purpose of buying and selling debts, and these shops are called BANKS.

And as there are fish markets, and corn markets, and many other sorts of markets, so also there is a market for buying and selling foreign debts, which is called the ROYAL EXCHANGE. Thus Banks are nothing but debt shops, and the Royal Exchange is the great debt market of Europe.

It is so important to grasp the true conception of credit that we will present it in another way. Suppose a man has a pay-

ment certain to be made to him on a particular day. He has the present right to that payment, which is his property. He may sell and transfer that right to any one else, and that right so transferred is *Credit*. And it is clear that the amount of the credit is the present value of the future payment. Now this abstract property may effect exchanges just in the same way as money; and if the payment be fixed at some distant date, as three months, it may pass through a hundred hands and effect a hundred exchanges, before it is paid and extinguished itself. Moreover the money itself, which will pay and extinguish the credit at some future time, may be circulating and effecting any number of exchanges during the same interval. Consequently we have at the same time, both the money itself and the promise to pay it circulating simultaneously and effecting exchanges. Now what is true of one payment is true also of every other. Thus every future payment, or transfer of money, has a present value, which may circulate in commerce. And this is what is meant by the common expression the magic of credit. It means that an abstract promise to pay produces exactly the same effects as money itself. But, like other potent magicians, it sometimes overmasters its creators. It is easy enough to call credit into existence, but not always so easy to extinguish it.

The definition we have obtained above of credit,—that it is the present right to a future payment—at once points out the limits of credit. The debt is created with the intention of being extinguished, and so long as it is extinguished at the appointed period, the credit is not excessive. The various methods by which credit, or debt, are extinguished are fully explained in a subsequent chapter.

Credit being an exchangeable merchandize must be measured in order to be brought into commerce. The unit of debt, or credit, is the right to demand £100 at one year after date, and it is always usual to refer all other debts to this measure.

Of Currency or Circulating Medium.

11. Having thus examined the function of money and credit, and shewn that the latter is a species of exchangeable property of the same nature as, but inferior in degree to, money, we have now to consider the words "Currency" and "Circulating Medium" which have given rise to protracted controversies in comparatively recent times, and we take them together, because all writers use them as absolutely equivalent.

To apply the word currency to money is one of the most extraordinary abuses of language that has ever occurred. In old times men used to speak of money being current, as it passed from hand to hand. Hence arose the expression, the *currency* of money. So late as the case of *Miller v. Race*, in 1750, Lord Mansfield says of money that it cannot be recovered after it has

passed in *currency*, but before money has passed "in currency" an action might be brought for it. He says the same of a bank note. An action could not be brought for it after it was paid away *in currency*. Hence the word *currency* was manifestly applied to a certain action of money—namely, its passing from hand to hand. But about the beginning of the last century, by a most extraordinary confusion of ideas, and, as far as we have been able to discover, it arose in our American colonies, the money itself was called *currency*. This name occurs but rarely in Adam Smith, but since then has become very common.

To shew the extreme absurdity of this name we have only to consider a few similar cases. Nothing is more common than to say that such an opinion, or such a report is current, and we speak of the *currency* of such an opinion, or such a report. But who ever dreamt of calling the opinion, or the report, itself *currency*? It is very common to speak of the *currency* of the Session of Parliament—but who ever dreamt of calling the Session itself *currency*?

Now how can it be more rational in a scientific sense to call money *currency*, than to call a report, or an opinion, or the Session of Parliament, *currency*?

Such as it is, however, this Yankeeism is far too firmly fixed in common use to be abolished; and hence we must now accept it, and endeavour to ascertain in a scientific sense what it includes.

The expression *circulating medium* came into use about the last decade of the last century, and is a far more correct expression. The circulating medium is manifestly the medium by which the circulation of commodities is effected, and clearly, by the very force of the definition, includes money and credit of all sorts. The metallic *currency* is termed money, and the paper *currency* of all sorts is termed *security for money*. These securities for money, or the paper *currency*, are divided into two general species, first, *promises* to pay money called PROMISSORY NOTES, and secondly, *orders* to pay money, called BILLS OF EXCHANGE. Each of these general divisions has several varieties, which are treated of in a subsequent chapter.

The paper *currency* represents a pledge for a future payment, exactly as money does. The latter, however, is always a pledge payable on demand. In the case of paper, this pledge is frequently not payable on demand, but at a fixed period after its creation. Now, it is clear that, though the period of payment is deferred, it cannot alter the fundamental nature of the instrument. It may affect its value, and its negotiability, or facility of transfer, but it cannot affect its essence. A pledge to pay in three months' time is clearly of the same nature as a pledge to pay on demand, nor does it in any way signify whether it is recorded on paper, or exists merely in the abstract form of a debt.

The word *currency* itself is a complex term involving two

simple ideas. From its first representing a debt, its fundamental idea was that it was something that denoted power of demanding services, and secondly, it also passed from hand to hand itself. Of these two ideas it must be especially observed that the former is the fundamental one, but it has received its *name* from the latter. Resolved into these ideas it denotes—

1. That which *circulates* commodities, *i. e.*, which causes commodities to circulate, where circulate is an *active* verb.

2. That which *circulates* itself, where circulates is a *neuter* verb.

From the first of these ideas is derived the term *circulating medium*, and from the second *currency*.

The amount of the currency, or circulating medium, in any country is the aggregate amount of it belonging to every individual. Now whatever represents the amount of debt due to any individual, over and above his possessions in commodities, in whatever form that debt may be recorded, whether metal or paper, or whether it exists simply as a debt, is the amount of currency belonging to him. Adopting this definition, we may enumerate the different species of currency as follows:—

1. Coined money; gold, silver, and copper.

2. The paper currency, *i. e.*, promissory notes and bills of exchange, with all their varieties.

3. Simple debts of all sorts, such as credits in bankers' books, called deposits, book debts of traders, and private debts between individuals.

It is obvious that there is no distinction in principle between the two latter species. They each denote that a transfer of some sort has taken place, and are a title to future payment. As a matter of convenience some of these are recorded on pieces of paper. It is certainly true that some of these descriptions of currency are more eligible and secure than others, and perform the same duties with different degrees of advantage. The metallic currency rests upon the credit of the State, that it is of the proper weight and fineness, and the universal readiness of people to receive it in return for services. Paper currency, in this country at least, rests entirely upon private credit, and is of all degrees of security, from a Bank of England note down to a private I O U. These different species of currency, therefore, though they possess different degrees of circulating power, though they may be more or less eligible or secure, represent but one fundamental idea—DEBT. From these considerations it follows that the amount of currency or circulating medium in any country is the *sum total of all the debts due to every individual in it.*

12. The observations contained in the preceding paragraphs shew that the idea of "currency" is quite independent and essentially distinct from that which we usually call "money," regarded

as it is by many writers as an intermediate and equivalent merchandize. It is quite possible to have a currency, even though its most useful and general form, money, had never been thought of. If transactions take place between individuals, it is scarcely possible to imagine that there should not be debts, or balances of services arising from unequal exchanges between them, and this is the basis of a currency. But it does not necessarily follow that there must be money. If the way of conducting commerce by means of money had never been invented, a grocer and a wine merchant might trade with each other. If they agreed that a bottle of wine and a pound of tea should be considered as equivalents, the grocer might want so many bottles of wine, and if the wine merchant did not want so many pounds of tea he might let the grocer have the wine on his giving his promise, a pledge, to pay the tea when demanded. And this note or promise might pass through a hundred hands before the owner of it demanded the tea. It would perform exactly the same function as money in circulating goods. It would therefore be *currency*, but it would not be money in the sense of being an intermediate and equivalent merchandize. Money has, no doubt, enormous advantages over such a currency, but these advantages are purchased at a very heavy cost, and in modern times, in a severe public pressure from war, the luxury of a metallic currency is one of the first to be dispensed with. The true nature of a currency is revealed when gold and silver disappear. This was well exemplified in America, during the recent civil war. Private tickets of all sorts superseded specie. Instead of money, people had their pockets filled with bread tickets, milk tickets, and railroad tickets. If a man went to have his hair cut and tendered a dollar, he could not get change, but he received so many tickets promising to cut his hair so many times. In one case we saw in the papers, payment was made in tickets promising to pay strawberries when the season came on.

13. We must now demonstrate a proposition of the greatest importance in Political Economy, and on which errors of the most serious nature are very prevalent. It is this:—

The quantity of money in any country bears no necessary relation whatever to the quantity of other goods, &c., in it, nor to their price.

Many writers on Political Economy have supposed that the quantity of money in a country bears some necessary relation to the quantity of commodities in it; many more think that the prices of commodities are determined by the proportion which the quantity of money bears to the quantity of commodities. That this is a very grievous error may very easily be shown. Let us suppose that A and B are reciprocally indebted to each

other for the sale of goods. Let us suppose that A has bought goods from B to the amount of £10, and B has bought goods from A to the amount of £13. Then it is quite clear that there are three different ways of settling their dealings.

1. Each may send a clerk to the other to demand payment in full of his debt. This method would require £23.

2. A may send £10 to B to discharge his debt, and B may send it back to A with £3 more to discharge his debt. This method would require £13.

3. They may meet and set off their mutual debts against each other, and pay only the difference in coin. This method would require only £3.

Now it is quite clear that a very different quantity of money would be required to carry on any given amount of business, according as either of these three methods was adopted. Between the first and the third there is a difference of £20, but there would be no difference in the prices of commodities. These £20 would not influence prices, but be required to settle debts in a clumsy way. So it is clear that by a simple change in the method of doing business, £20 may be withdrawn from circulation altogether, and applied to new transactions.

From these considerations it appears that there may be large quantities of money in a country which may exercise no influence on prices, and the proportion between money and commodities may vary greatly, according as one or other of these methods of doing business is adopted. Now if a country which habitually adopted the first method, were to change its custom and adopt the *third*, it is perfectly clear that a very large quantity of money would be disengaged from circulation, and may be applied to promote new operations, and therefore in all its practical effects it would be an addition to the previously existing quantity of money. Hence the various methods of economizing the use of money are to be considered as an increase of the resources of the nation. If by an improved method of doing business we can dispense with £500,000 in settling transactions, that is equivalent to adding that sum to the resources of the nation. It is one of the great functions of a bank to promote such a change of doing business, and to bring people together to balance their mutual debts without the intervention of money, and it will be shewn in a subsequent chapter how greatly the skilful employment of such methods economizes and develops the national resources.

On Circulation.

14. When commodities, &c., are interchanged directly for one another it is called **BARTER**, or **EXCHANGE**. When commodities are interchanged for money, that money is only taken in order that it may be interchanged again for something else. Hence,

J. B. Say aptly said, that when money is used, the transaction is the *half of an exchange*, which is true. It is also called a SALE. A *Sale* always denotes a transaction in which one of the quantities exchanged is money or credit, that is, when one quantity is a useful commodity, and the other only the right to demand one; that is, when the interchange is of things of an unlike nature. An *Exchange* is always an interchange of things of a like nature, either commodities for commodities, or currency for currency. Thus we speak of the Foreign Exchanges, or the value of the currency of one country in terms of the currency of another; or we ask for the change (*i. e.*, the 'change or exchange), of a £5 or a sovereign; so we speak of exchanging a picture for a statue, or one book for another. When the interchange is of commodities for currency, the one who gives currency is said to BUY the commodity, and the one who gives the commodity is said to SELL it. Thus we buy a horse or a house with currency. An officer buys a commission in the army, but he *exchanges* from one regiment to another. So in *Lear*, when Albany throws down his glove to the traitor Edmund, the latter throwing down his own says, "There's my exchange," meaning like for like. So in *Hamlet*, Laertes says—

"Exchange forgiveness with me, noble Hamlet."

A transaction in which currency is given for commodities is, as just said, a *Sale*. The sum total of these sales is properly termed the CIRCULATION. Hence a single piece of money may add considerably to the circulation, for every time it is transferred it is an addition to the circulation, though it is no increase to the currency. We must observe that the word *Circulation* is often used in a very corrupt sense, as being synonymous with money and bank notes, more particularly the latter. Thus the number of notes issued by the Bank of England, or any other bank, is frequently termed its *Circulation*, more especially by American writers, from whence we believe the absurdity of calling money currency originated. Of all the terms in common use this is one of the most objectionable. To call the notes which circulate the *circulation*, seems as great a confusion of ideas, as to call a wheel a *rotation*. We shall accordingly never use the word circulation to mean the amount of issue of a bank, the correct expression evidently is to say, the number of its *notes in Circulation*. We shall always use the words currency and circulation to mean different things; the former to denote the substance itself, the second the amount of its transfers from hand to hand. It is also clear that the currency and the circulation do not bear any fixed relation to each other, for there may be a large amount of currency in a country, yet, if the industrial operations be few, there will be a small circulation. On the other hand there may be a small amount of currency, but if the

people be active and industrious, it will pass frequently from hand to hand, and there will be a large circulation.

On Price, Discount, and Interest.

15. When one economic quantity is exchanged for another, each is termed the value of the other. But when one of the economic quantities exchanged is money or credit, the sum of money or credit receives a peculiar name. It is called the PRICE of the other. From the considerations presented in § 8, it appears that price is the same thing as value in money, or credit. But, as it is invariably the custom in modern times to estimate the value of every commodity by its value in money or credit only, or its price, and not by its value as regards other commodities, the words value and price have become almost identical and interchangeable expressions, though no doubt we must remember the technical difference between them. The price of any commodity is therefore the quantity of money, or credit, given in exchange for it, at any moment.

Now, as the value of the money is the commodity received in exchange for it, it is manifest that the greater the quantity of the commodity received for it, the greater is the value of money. Or if the quantity of the commodity be fixed, the value of money is greater, as *less* money is given for the commodity. Hence it is clear that *the value of money varies inversely as price.*

The value of the property called debt, or credit, is however estimated in a peculiar way. We have taken the sum of £100 payable one year hence as the unit of debt. The negotiation of debts is a branch of modern commerce of supreme importance. Now a debt of £100 payable one year hence, being a saleable commodity like a quarter of corn, the sum given for it is its price, just as we speak of the price of anything else. And of course the value of money rises as the price diminishes. Now as money naturally produces a profit, it is clear that the price given for a debt payable a year hence must be less than the *amount* of the debt. The difference between the *price* of the debt and the *amount* of the debt is called DISCOUNT. Therefore, clearly the price together with the discount equals the amount of the debt; and as the price decreases the discount increases. Hence, as the discount increases, the value of money, or the price, increases also. Now, in estimating the value of debts it is universally the custom in commerce to mention the *discount*, and not the price; and to buy or purchase a debt is always in commerce termed to *discount* it. Now, if a banker buys a debt of £100 payable a year hence for £95, it is manifest that the discount is £5, and he is said to *discount* it at 5 per cent. per annum. Should the price of debts fall, the discount rises; and since the value of money varies inversely as price, it varies directly as discount.

Hence we have this :—

The Value of Money varies inversely as price, and directly as discount.

To discount a bill of exchange at 5 per cent., means to give a price for a debt in the proportion of £95 for every £100 of its amount payable one year hence.

The expression, however, that the value of money varies directly as discount is sometimes misinterpreted. Thus it is often said that if the price of debts has fallen from £96 to £93, and therefore the discount rises from £3 to £6, the value of money has doubled. This, however, is erroneous. Debts which formerly sold for £96 now sell for £93; and, therefore, it is clear that the value of money has risen in the proportion only of 93 to 96, and not doubled.

When a person advances money to another, and agrees to defer receiving the profit until the end of the year, the profit is termed INTEREST. If he lends, as it is called, £100 at 5 per cent. interest, he in fact pays £100 down for the purchase of a debt of £105, payable at the end of a year, and the £5 is the interest.

This method of making profits, though not uncommon among private persons, is never used in banking. Bankers invariably subtract the profit agreed upon at the time of the advance. Thus they always make profits in advance. In this case the profit is termed DISCOUNT. Thus, if a banker discounts a bill of £100 at 5 per cent., he only pays his customer £95, and retains the £5 at the time of the advance, as profit. In reality he pays £95 down for the purchase of a debt of £100, payable a year after date; and the £5, or the difference between the price of the debt and its amount, is the *discount*, and his profit.

It is manifest that this latter method of trading is the more profitable, because in the former case he makes £5 profit on the actual advance of £100, in the latter case he makes £5 profit on the actual advance of only £95; and besides that, he has the £5 in his hands to trade with immediately, instead of waiting till the end of the year. In the large amounts of money which banks deal with, this makes a very sensible difference in their profits, especially when the rate of discount is high.

On Securities for Money and Convertible Securities.

16. The expressions *Securities for Money* and *Convertible Securities* are very frequent in banking business, and we must now explain them. A *security for money* always means an obligation, or security, for the payment of a definite sum of money from a definite person at a definite time. In a security for money, therefore, there is always some obligor, or some person who is bound to pay it. There are different forms of such securities, such as bank notes, promissory notes, bills of exchange, Exchequer bills, Navy bills, and debts of all sorts.

Convertible Securities mean securities which no particular person is bound to pay, but for which, under usual circumstances, a purchaser can readily be found in the open market. Thus any property which can be readily sold is called a convertible security. This species of property includes the Public Funds, shares in all sorts of commercial companies, and all title deeds to property of a moveable description of which the property passes by simple delivery, such as dock warrants and bills of lading. The fundamental distinction between these latter and instruments of credit of all sorts, will be clearly explained in a future chapter. Now, as convertible securities mean property which is readily convertible into money, of course there are all degrees of convertibility. There is no absolute distinction in principle between the different species of property. But of all species of property the Funds are the most readily convertible, and land, or real property, the least readily convertible, in consequence of the artificial difficulties thrown in the way of its transfer by our law.

Thus securities for money *never* represent any specific money, but are *always* a claim on the person. Convertible securities are *never* a claim on the person, and certain kinds of them are *always* a title to certain specific goods. Sometimes a security for money may be changed into a convertible security. This is done in what is technically called *funding the unfunded debt*. The Government sometimes raises money on its bills like individuals, and it is bound to pay those bills at maturity, like an individual. These Exchequer bills, therefore, as they are called, are like any other bills of exchange, *securities for money*. Sometimes when these bills amount to a large sum, it is very inconvenient for the Exchequer to pay them in full, and it gets its creditors to agree not to demand the repayment of the whole debt, but to receive only the interest on it in perpetuity. When this is done the creditor loses the right to demand payment of the principal sum from the Government, but he may sell this right to any one else in the open market. It then becomes a *convertible security*, and is called the Public Funds, or Stock. This operation is termed *funding the unfunded debt*.

On the Definition of Capital.

17. Any economic quantity whatsoever, may be employed in two different ways. The proprietor may either use it himself for his own personal enjoyment, or he may use it so as to produce a profit. When an economic quantity is thus used *productively*, *i. e.*, so as to produce a profit, it is termed CAPITAL. And also whatever produces a profit may be termed capital. Mr. Senior says very justly, "Economists are agreed that *whatever gives a profit* is properly termed CAPITAL." And Stephens, in his Thesaurus, defines the word thus:—

"Κεφάλαιον. Caput inde fructus et reditus manat. Capital, the source whence any profit or rent flows."

It is clearly to be understood that there is no such thing as absolute capital in a country. Whether any economic quantity is to be termed capital or not, in no way whatever depends upon the *nature* of the thing itself, but exclusively on the *method* in which it is used. If I have a sum of money which I spend in purchasing things for my own use and enjoyment, it is not capital; but if I use it so as to produce a profit in any way, it then becomes capital. Thus if I lend it out at interest; or buy goods with it to sell again at a profit; or invest it in a commercial enterprise of any sort; or if I spend it in acquiring the knowledge necessary to exercise a profession; such money is capital. And the things or commodities purchased, for the purpose of producing the profit, are termed capital as well; because, though the money was originally employed in acquiring them, they are again employed in purchasing money, and there is no profit unless they sell for a greater sum than is employed in purchasing them.

Now there are two fundamentally distinct ways by which capital may increase—

I. By direct and actual increase of quantity. Thus, flocks and herds, cattle, corn, &c., increase by adding to their numbers or quantity.

II. By exchange: that is, by exchanging something which has a low value in a place for something that has a higher one.

Now it is clear that money produces a profit, and therefore becomes capital, by the second of these methods. We do not sow sovereigns in the ground like corn, nor do they produce a crop of half sovereigns. But money becomes capital by exchanging it for some goods, &c., which may be sold or exchanged again for a greater sum than they cost. And it is also clear that any economic quantity whatever, which is used as a substitute for money to purchase goods and for a profit, is capital, as well as money, by the force of the very definition which Mr. Senior says all Economists are agreed upon.

18. Adam Smith says, “that capital may be employed productively in four ways: 1st. In procuring the rude produce annually required for the use and consumption of the society; 2ndly. In manufacturing and preparing that rude produce for immediate use and consumption; 3rdly. In *transporting* either the rude or manufactured produce from the places where they abound, to those where they are wanted; or, lastly, in dividing particular portions of either into such small parcels, as suit the occasional demands of those who want them.” Now it is clear that the last two ways are identical in principle, and include the business of the foreign merchant, the wholesale and the retail dealer—that is, the whole operations of commerce, or exchange. Hence, we may say that Smith enumerates three distinct methods of employing a capital productively—agriculture, manufactures,

and commerce, or exchange. Now, without inquiring yet, what the technical economic definition of *Production* is, which is done a little further on, we see at once that Smith enumerates exchange, or purchase, as one species of production. Now Mr. Mill says that "anything which is susceptible of being exchanged for other things, is capable of contributing to production in the same degree," and that "bank notes, bills of exchange and cheques, circulate as money, and perform *all* the functions of it."

Now money becomes productive capital by being employed to purchase things to be sold again at a profit. And if a man can purchase things by means of his credit, that is, if he can purchase them by giving his promise to pay at a future time, and by so doing sells the goods at a higher price, and so has a profit, after paying and discharging his debt, it is quite clear that credit has been capital to him in exactly the same way that money would have been.

Let us take a very simple example. Suppose a tailor wants to make clothes for a customer. He pays, say £10 in cash to the cloth merchant, and after making up the clothes he sells them, perhaps, for £15. Then he has used this money as capital. He has £10 at the beginning of the operation, and £15 at the end of it; or, he has made a profit of £5.

Suppose the tailor has no money to buy the cloth with, then, if he cannot buy it on credit, he cannot make the clothes, and he cannot have any profit.

Suppose, however, the cloth merchant, believing in his honesty and capacity to pay, sells him the cloth in exchange for his promise to pay money three months after the time. As the payment is deferred, and as, of course, there is some risk of loss, he will, by way of insurance, charge him a somewhat higher price than the cash price. Suppose he sells his cloth in exchange for the tailor's promise to pay £11 three months after the time. Now this is as much a sale as if the price had been paid in money. The property in the cloth is gone to the tailor, and what the cloth merchant has received in exchange for it is the right, or property, to demand £11 three months after date. Now this property is called a debt, or credit.

The tailor having purchased the cloth by creating a debt against himself of £11, payable in three months' time, makes up the clothes as before, and is paid £15 by his customer. At the end of the three months he pays £11 out of this to the cloth merchant, and has, of course, remaining for himself a profit of £4.

Now by the cash operation he is better off at the end by £5, and by the credit operation he is better off by £4, than he was at the beginning. It is true he has not made so great a profit by credit as by cash. But still he has made a profit by his credit, which he could not have made without it. Hence, by the

very definition, his credit has been capital to him, and has produced exactly the same circulation of commodities, and employed the same quantity of labour that cash would have done. Hence we see that credit is productive capital in exactly the same way and in the same sense that money would have been.

This very simple example must suffice here to illustrate the doctrine that credit is capital, which has been strenuously denied in recent years. As we wish at present simply to place elementary ideas in a clear light, we shall not now discuss the views of those writers who ridicule the doctrine that credit is capital. That is done in a future chapter.

On Fixed and Floating Capital.

19. The true definition of Capital, then, is any economic quantity whatsoever used for the purposes of profit. But capital itself may be used in two different ways so as to produce a profit. It may either remain in the owner's possession,—and then it is usually called **FIXED CAPITAL**—or he may part with the possession of it, and it may be replaced to him with a profit; in this case it is called **FLOATING** or **CIRCULATING CAPITAL**.

Smith, B. ii., c. i., enumerates four species of fixed capital. 1st. Useful machines and instruments of trade; 2ndly. Buildings used in all sorts of trade; 3rdly. Improvements of land; 4thly. The acquired and useful abilities of the members of the Society.

He also enumerates four species of floating capital. 1st. The money by means of which the other three are circulated and distributed to their proper consumers; 2ndly. The stock of provisions in the hands of various dealers; 3rdly. The materials in the hands of different work-people to be made up; 4thly. The same materials when made up into finished products and ready for sale.

It is clear that this enumeration is very far from being complete, because there are many species of property omitted, which yet are capital. But under the term floating capital he enumerates money. And under the term money, he always includes paper money of all sorts and descriptions. Since Smith's day a distinction has arisen between "paper money" and "paper currency," but he always includes every species of paper under the term money, or the wheel of circulation, which he terms floating capital. Now this paper currency is simply **CREDIT**. And hence we see that Smith expressly enumerates credit under the title of capital.

It is clear that if the return be made in one operation, it must include the whole sum necessary to replace the article, as well as the intended profits. But if the return be made by instalments at fixed periods, say a year, each instalment must consist of a sum partly to replace the deterioration of the article itself during that period, and partly to form the excess, or profit, of

the capitalist, so at the end of the term, when the article is worn out, the sum of all these instalments should be sufficient to replace the original article together with the profits.

It is clearly to be understood, that it is according to the intention of the person who produces an article, and the purpose for which it is produced, that it receives either of these names, and not according to the nature of the article itself. The same article may receive different names, according as it passes to different owners, who produce it, or cause it to be produced for different purposes. The same article may be *floating capital* in the hands of one man, and *fixed capital* in the hands of its next possessor, if the first produces it for the purpose of selling it, and the second purchases it for the purpose of deriving an income from its use.

This distinction may also be stated thus. That if the whole price of the article is paid out of the current income of the country, it is *floating capital*; but if only the interest, or revenue derived from its use, then it is *fixed capital*. This distinction is often overlooked, and the term fixed capital is applied to articles of a certain nature, and floating capital to articles of another nature. Thus, houses and lands, machinery, railways, and ships are frequently termed fixed capital. But this is extremely erroneous. If a person employs his capital in building houses for the purpose of selling them immediately, they are floating capital in his hands, for their price is paid in one operation. But if another man buys them for the purpose of letting them out to tenants, and so only deriving a revenue from his capital, they become fixed capital in his hands. Many persons buy land on speculation, for the purpose of selling it again at a profit. The land in the hands of these jobbers is *floating capital*, but if another buys that land for the purpose of letting it out to farmers, or cultivating it himself, and so only making a revenue of it, it becomes *fixed capital* to him. So with machinery; to the machine maker, who makes it for the purpose of selling it to the manufacturer, it is floating capital. In the hands of the manufacturer, who buys it for the purpose of increasing the quantity of his productions by its use, and so only making a profit of it, it becomes *fixed capital*. Hence, we may state generally, that all articles, whatever be their nature, while they are in the hands of a person who deals in them, that is who produces or buys them for the purpose of selling them again, as soon as he can, are *floating capital*. As soon as they pass into the hands of a person who only makes a profit by interest derivable from their use, they are *fixed capital*.

The articles we have just mentioned are, it is true, generally produced with the intention of their ultimately becoming fixed capital, but we have shown that they may, or they may not, be fixed capital, when they are produced, according to different

circumstances; and, unless we know what those circumstances are, it is impossible to decide which name is to be given to them. It may also be easily shown how articles which are usually classed as floating capital may become fixed capital. Furniture and clothes would usually be termed floating capital, because they are generally made for the purpose of being sold. But if a person made them for the purpose of only letting them out for hire, they would become fixed capital in his hands. An ordinary tailor usually makes clothes to be sold to his customers, so they are floating capital to him. But in the hands of Nathan, who lets out uniforms and dresses for particular occasions, they become fixed capital, just as much as a house or a mill. So, if a cabinet-maker makes furniture, for the purpose of letting it out for hire, that furniture is as much *fixed capital* as any railway.

We thus see how improper it is to apply the term either of floating or fixed capital to any object, whatever be its nature, unless we know the intention of its owner in using it. And unless an article is incapable of being applied to more than one of these purposes, it is not correct to call it by either name. There are very few articles to which the name of fixed capital may be invariably applied, the only one to which it is necessarily applied is the knowledge, skill, and capacity of an individual. Those to which it may be applied with the least risk of error are Railways, Canals, Docks, and agricultural improvements. The instances are very rare in which such things as Railways, &c., are made for the purpose of being sold. If that did happen, they would have to be called floating capital, in the hands of such a person, or company. So that we may safely say that there are no articles which are necessarily fixed capital. Nor are there any which are necessarily floating capital. The mode of expending capital, which is almost invariably floating capital, is the wages of labour. In all ordinary cases in this country, the wages of labour are floating capital. But in slave countries the case is different. There the slaves are fixed capital. The same thing occurs in this country, where people sometimes enter, as it were, into a species of modified servitude. Sometimes people hire themselves out to others for a certain period, who are allowed to let them out for particular occasions, and receive the money for their performances. Thus, it is not unusual for the most eminent singers and musicians to agree to serve the large music-sellers for a definite period, during which their employer has the right to let them out on occasions, just like instruments or plate.

To the capitalist who lives merely on the profits of his capital, it may make very little difference whether he reaps that profit in one operation or in many, as the result must always be the same to him in the end. But to the class of persons who live by their daily labour—the workmen in his business—the difference

in the mode of employing capital is of vital importance. Thus, if the builder of a ship means to sell it immediately, and be paid the whole price of it at once, he will employ that money in building another ship, and the full amount of the price of the ship, deducting the part which goes to support himself, will be expended in the wages of the shipwrights, and on the producers of the materials for the new ship. In this case it is floating capital. But if the builder of the ship means only to let it out for hire, and receive a periodical instalment for its use, he can only employ the part of that instalment which represents its deterioration in building a new ship; consequently, if he changes the nature of his business very suddenly, that is, if he suddenly turns his floating into fixed capital, the fund applicable to the promotion of labour will be greatly diminished, and it must infallibly cause great distress among the persons who were dependent on him for their support. By seeking other employments they may, perhaps, ultimately be as well off as before; but it is quite clear that if a large number of persons have been accustomed to have a particular kind of labour found for them, any sudden change by which the system is disorganized, must produce at least temporary distress. It might be said that the capital of the purchaser of the ship, instead of going to the builder of the ship, and being spent among that class of workmen, might be employed in encouraging other species of industry, so that the result to the whole community would be the same. But the overthrow of any system upon which a great number of people depend, must be followed by much suffering. It appears then, that the conversion of floating into fixed capital, requires to be done with great caution, and only in certain quantities, to avoid its being injurious to the interests of large classes of persons. And if a large class of the public are seized with a sudden mania to convert an unusual quantity of their floating into fixed capital, it must inevitably be followed by at least temporary distress.

On Production and Consumption.

20. The words *Production* and *Consumption* are two of the fundamental terms in Economics, and are always used as correlatives. It is said that *Consumption* is the end of all *Production*. But unfortunately, the meaning of neither word is settled, and they are frequently used in senses which are manifestly inadmissible.

J. B. Say was the first writer who defined Political Economy to be the science which treats of the Production, Distribution, and Consumption of Wealth; and this definition, with more or less variation, has been adopted by many writers.

We must now inquire into the meaning of *Production* and *Consumption*, and shortly state the doctrine of these writers, to see whether it is agreeable to experience.

Production, Say defined to be employing labour to add value to the particles of matter. He says that it is equally impossible to create out of nothing, as to annihilate, a single particle of matter, but that by labour, we can create out of nothing the qualities which give value to the rude particles of matter. This labour may be employed in separating, transporting, combining, and transforming particles of matter. It changes the condition of the body, and that is all. This production, therefore, creates a value by giving or increasing the utility of anything; and everything whose value is created, or augmented, is a product. He enumerates agricultural, manufacturing, and commercial production; the latter consisting of augmenting value by the transport, or distribution, to consumers of products already existing.

Consumption is defined by Say to be the opposite, or reverse, of Production. As Production is the creation of value, so Consumption is the destruction of value. He says that everything which is produced is consumed, and consequently that every value created is destroyed, and was only created for the purpose of being destroyed.

This doctrine that every product is consumed, or destroyed, has been repeated by a multitude of writers. Thus Malthus defines Consumption to be the destruction wholly or in part of any portion of wealth.

“By Consumption,” says Mr. McCulloch, “is meant the annihilation of those qualities which render commodities useful or desirable. To consume the products of art and industry, is to deprive the matter of which they consist of utility, and consequently of the exchangeable value communicated to it by labour. Consumption is, in fact, the end and object of human exertion, and when a commodity is in a fit state to be used, if its consumption be deferred, a loss is incurred.”

Now with respect to the meaning given to the words Production and Consumption by these writers, we may say that if Economic Science treats of the production of wealth in their sense, it must profess to treat of the whole business of farming, and all the processes in every species of manufacture. But every Economist would at once repudiate such a doctrine. He would at once say that all the processes in agriculture and manufactures are no part of his science. It has nothing to do with the arts and processes by which things are produced, but only with their value, or exchangeable relations, when offered for sale.

Again, with respect to *Consumption*, it is manifestly erroneous to say that all things are produced for the purpose of being destroyed. It is true that some are, such as food, and destruction is incidental to the use of some, such as clothes. But Economic Science has nothing to do with that. If a man eats a dinner, or

smokes a cigar, or wears out a pair of shoes, is that an economic phenomenon?

But there are multitudes of things produced which are not destroyed at all. If a sculptor carves out a statue, is it made for the purpose of being destroyed? Is a picture painted for the purpose of being destroyed? Are books printed for the purpose of being destroyed? Many things, such as gems, medals, &c., are absolutely indestructible, except by violence. In many cases, such as houses, the greatest care is taken to preserve the products from destruction.

If then consumption means destruction, it is clearly false to assert that consumption is the end of all production, and that whatever is produced is consumed, and all correlation between the terms is lost.

What then in commercial language is *Consumption*? and who or what is the *Consumer*?

Now, without overloading our text with too many quotations, we will make one from Adam Smith. He says, B. ii., c. ii. :—

“Though we frequently, therefore, express a person’s revenue by the metal pieces which are annually paid to him, it is because the amount of these pieces regulate the extent of his power of *purchasing*, or the value of the goods which he can annually afford to *consume*. We still consider his revenue as consisting in this power of *purchasing* or *consuming*, and not in the pieces which convey it.”

Here we see that Smith uses the word *consume* as synonymous with *purchase*, and, therefore, *consumption* as equivalent to *purchase*. And this is the true commercial meaning of the word. The consumer is simply the purchaser or customer, and Economic Science has nothing to do with what the purchaser does with the product after he has bought it.

So Dr. Johnson, explaining the first elements of trade to Dr. Wetherell, Master of University College, Oxford, says, “Here are three profits to be paid between the printer and the reader, or, in the style of commerce, between the manufacturer and the *consumer*; and if any of these profits is too penuriously distributed the process of commerce is interrupted.” Here we see again that the consumer means simply the purchaser.

It may be observed that the Latin word *consumere*, besides meaning to destroy, also means *to buy*.

The ambiguity has probably come from the French. In that language there are two words *consumption* and *consummation*, both in a certain way represented by our single word *consumption*. *Consumption*, in French, means destruction, but that is not the technical economic word in French. It is *consummation*, which is the Latin *consummatio*. Now it is clearly pointed out in the French dictionaries, that *consummation* means completion or perfecting, as in English, *consummation*. Now, who

is the consumer? He is the person who completes, or brings to perfection, or consummates the work of the producer. The producer brings forward something and offers it for sale. But it is the purchaser who gives value to it; it is he who crowns the work, and consummates the desire of the producer, by purchasing it, and thereby giving it value. And the work is not consummated, or perfected, until it is sold, and the economic phenomenon is complete. Until the product is sold, the labour is not consummated.

And what is the meaning of *producer* and *production*? To ascertain this, we have only to look at the genuine meaning of *producere* in Latin, which is to bring out, and to cause an increase of quantity is only the secondary meaning. It is the technical word used for *exposing to sale*. Thus Terence, *Eunuchus* I. ii. 55, says—

“pretium sperans illico
PRODUCIT; vendit.”

“*Hoping for a good price, offers her there for sale; sells her.*”

And in the *Heauton timorumenos*, I. i. 90—

Ancillas, servos * * *
Omnes *produxi* ac vendidi.

“*All the slaves, male and female, I put up for sale and sold.*”

So, to produce in English, is to draw forth—to cause to come near. To produce a thing is simply to place it where it is wanted. If a witness is told to produce a deed in court, it means that he is to bring it into court and to place it there. So a gaoler is ordered to *produce* the body of his prisoner in court, that is, to place him there. So in Isaiah xli., 21, it is said, “*Produce* your cause saith the Lord, bring forth your strong reasons saith the King of Jacob.” And the marginal note says, “*Produce*—cause to come near.”

Thus the producer, in economic language, is the person who brings forward some product for sale in a given place, no matter how he obtains it, whether by growing it, such as corn, or purchasing it as retail dealers do. Adam Smith calls a retailer a “productive labourer,” and how is he so? Because he purchases things which his customers want, and places them where they will want them.

The producer, then, is simply the person who offers anything for sale, and the consumer is the purchaser or customer. And we now see how consumption is correlative to production. Bastiat says, “We give and receive services; we supply and we demand values; we make purchases and sales; we work for others, and others work for us; in a word, we are *Producers* and *Consumers*.”

This, then, is the only sense in which the doctrine that consumption is the end of all production is true, and in fact, it

becomes tautology, for it is reduced to this, that people offer things for sale for the purpose of being sold.

Two parties who wish to exchange their products, are each producers of their own, and consumers of each others' product. And it is the reciprocal consumption, or purchase, which gives value to the reciprocal production, and the complete transaction constitutes an exchange.

The quantity produced or offered for sale, is frequently called the SUPPLY, and is equivalent to it. The person who purchases or consumes it, *demand*s it. Consumption, therefore, in a certain way, may denote demand. But yet, these two words are not absolutely synonymous. The quantity actually sold is the consumption, but is by no means equivalent to the demand. Suppose there is a limited quantity of an article in a country place. All of a sudden a number of rich people flock into the place. They naturally bid against the inhabitants of it, and thus the *demand* is greater, and raises the price of the article, while the production or supply, is the same, and also the consumption, or quantity sold.

Although people are not divided into producers and consumers generally, yet in respect to each particular article they are. Nor is it any objection that some are both producers and consumers of the same article, as a farmer is of corn, and a cloth manufacturer is of clothes, a baker of bread, &c. Nothing is more common than for a man to act in two capacities, apparently inconsistent with one another. Thus, a man may lend to himself, and borrow from himself. He may be the shareholder in a joint-stock bank, and also be a customer of that bank, and he may borrow money from that bank. He therefore both lends to and borrows from himself. He is both his own banker, and his own customer.

The series of persons who deal in any article of commerce are alternately consumers and producers of that article. Thus, the foreign merchant or the importer is a consumer of that article as regards the foreigner, he is then a producer of that article as regards the wholesale dealer. The wholesale dealer is a consumer as regards the importer, but a producer as regards the retail dealer. The retail dealer is a consumer as regards the wholesale dealer, and a producer as regards his customer, who is the final consumer, and for whom all the series of previous operations took place.

On Rate of Interest and Rate of Profit.

21. We have now to call attention to the definition of an expression which has been the cause of immense confusion in Economics. Every one knows what *Rate of Interest* means. When people speak of interest at 5 per cent., they always mean that £5 is given for the use of £100 for some given time—as a year. It is

perfectly clear that we can have no conception of what rate interest is, unless we are told in what time it accrues.

By a most extraordinary oversight, however, this has been quite overlooked in the definition of *Rate of Profit*. It will scarcely be believed, that no Economist has seen that *Time* is a necessary element in the definition of rate of profit. Thus McCulloch says, "The *rate* of profit is the proportion which the amount of profit derived from an undertaking bears to the capital employed in it." The whole of Ricardo's doctrines of wages and profits are full of fallacy arising from this obvious omission. So Malthus defines rate of profit to be the per-centage proportion which the value of the profits upon any capital bears to the value of such capital. Even Mr. Mill has not seen the defect in the definition. He says, B. ii., c. xv., "The cost of labour, then, is, in the language of mathematics, a function of three variables: the efficiency of labour; the wages of labour (meaning thereby the real reward of the labourer); and the greater or less cost at which the articles composing that real reward can be produced, or furnished. It is plain that the cost of labour to the capitalist must be influenced by each of these three circumstances, and cannot be affected by any other. These, therefore, are also the circumstances which determine the rate of profit; and it cannot be affected except through one or other of them." What? is not the *rate* of profit affected by the *time* in which it is made? Suppose a given amount of profit to be made on a given amount of capital, is it the same *rate* of profit whether it be made in a year or a day? According to the definition in general use among Economists, a profit of £10 made upon £100, is exactly at the same *rate* if it be made in a year, a month, a week, or a day!! Nay, according to Mr. Mill, the rate of profit *cannot* be affected by the time in which it is made!!

This definition is so manifestly erroneous that it is only necessary to call attention to it to be at once admitted. It is quite clear that time is a *necessary* element in the definition of *rate of profit*. In fact it is simply unintelligible without it. If we were told that a trader had made a profit of £10 on £100, it would be as impossible to conjecture what the rate of profit had been, as it would be to determine a horse's rate of speed if we were only told that it had galloped 20 miles.

It often happens that the rate of profit is the greatest when the actual profit is the least. If a trader were to make 50 per cent. profit on one transaction, that would be a high profit; but if he only made one transaction in the year, he would not increase fast in opulence. His rate of profit would be 50 per cent. But suppose that he only makes a profit of 5 per cent. on a transaction, but makes that profit in one day, then the rate of that profit is upwards of 1,500 per cent. per annum, and if he could make a transaction at that profit each day, his actual profits

would be upwards of 1,500 per cent. Hence the rate of profit would be high, while the actual profit is low. And if the trader reinvested the profits as they occurred, as capital, his rate of profit on his original capital would increase at compound interest, and be enormously greater.

Bacon saw clearly what has been far too much overlooked by Economical writers, that the frequency of return is of far more consequence than the magnitude of each case of profit. He says, "The proverb is true that light gains make heavy purses, for light gains come thick, whereas great come but now and then," and this is entirely in accordance with what modern experience demonstrates as the true axiom of trade—*small profits and quick returns*.

The rectification of this error in the definition of rate of profit, which must be admitted as soon as stated, clears up a vast deal of obscurity which involved the subject of profit. Thus, when profits are said to be reduced to 10 per cent. it seems somewhat paradoxical to say that interest can be paid at 15 per cent. It is, nevertheless, true, and constantly happens; the apparent paradox only arises from the difference of estimating rate of interest and rate of profit in common language. When traders pay interest, it is always calculated at the rate *per annum*, but it is too common to measure profits by the actual transaction, without reference to the time. Thus, if a trader pays interest at the rate of 15 per cent. per annum, he makes profits, perhaps, at the rate of 10 per cent. per week, or per day, which is at the rate of 520 or 3,130 per cent. per annum, allowing for the number of working days in the year. This at once dissipates the apparent paradox, and explains how trade can be carried on at rates of interest which would seem incredible. In ordinary times in London, the second class bill-brokers charge their customers one shilling in the pound on three months' bills, which is, in reality, discount at the rate of 20 per cent., or interest at the rate of 25 per cent. per annum. In ancient times, and in the middle ages, and in America at the present day, the rate of interest is even higher than that.

These rates are, however, as nothing compared to the rates paid by petty provision dealers, and may serve to shew the utter absurdity of the Usury Laws which were so long in force in England, and are so still in France, though they will probably be abolished there very shortly. Gerard Malynes, a writer in the days of Charles I., observed that the petty provision trade of London was carried on with money borrowed at the rate of 400 per cent. per annum. In the days of Turgot penalties of the most terrible severity were enacted against the infringers of the Usury Laws. To shew their absurdity, Turgot instances the advances which money lenders at Paris made to the petty dealers, who bought victuals in the market, to retail them in different

parts of the capital. The charge was 2 sous a week for the loan of a crown of 3 francs, which was equal to interest at the rate of 173 per cent. per annum. The whole of the small provision trade of Paris was carried on by means of these loans. "Nevertheless," says Turgot, "the borrowers do not complain of the terms of this loan, without which they could not carry on the trade by which they live. And the lenders do not get very rich, because the exorbitant interest is only the compensation for the risk their capital runs. In fact, the insolvency of a single borrower sweeps away all the profit which the lender can make out of thirty of them."

The idea that trade could flourish upon money borrowed at 173 per cent., seems somewhat startling, until we analyse the operation. No doubt the borrower paid two sous a week for the loan of a crown, but then the probability is that what he paid a crown for in the morning, he sold again the same afternoon for three francs and a half, or more. Now if he repeated this operation once every day, it is clear that he would have gained at the end of the year 3,130 sous, omitting Sundays. That is, with a capital at no time exceeding 60 sous, he would gain a profit of 3,130 sous in the year, which would be at the rate of 5,216 per cent. per annum, and out of this he would only pay 173 sous for the loan of the money.

M. Gustave de Puynode, quoting from the speech of a Member of the last Legislative Assembly of France, gives an instance which is even more startling than the last. He said, "Every morning the small provision dealers received a 5-franc piece to buy the objects, which they resold with a profit of 3 or 4 francs. In the evening they repay the 5-franc piece, and give 25 centimes in addition. They make no complaint of interest, which is yet at the rate of 1,800 per cent." Nor had they any reason to do so, for by borrowing this 5-franc piece they made 3 francs of profit, out of which they only paid $\frac{1}{4}$ for interest. If therefore the rate of interest was 1,800 per cent. per annum, the rate of profit, assuming the gain to be, as stated, 3 francs per day, was at the rate of 21,600 per cent. per annum. And the interest, which is only one-twelfth part of the profit, is not unreasonable. And yet by the law of France it is still a crime to take more than 6 per cent.!*

* It may be stated that an Imperial Commission, before which the Author of this Work was examined as a witness, was some time ago appointed to inquire into the operation of the Usury Laws in France; their report is not yet published.

CHAPTER II.



THE THEORY OF VALUE.

“The Theory of Prices and their variations is the darkest part of our system.

“A Statist does nothing for philosophical economy, unless he ascertains and describes *changes*, and such relations among his details as are matter of fact.”—*Francis Horner*.

CHAPTER II.

THE THEORY OF VALUE.

DEFINITION OF VALUE—DEPRECIATION AND DIMINUTION IN VALUE—ERROR OF EXPRESSION INTRINSIC VALUE—ORIGIN, SOURCE, OR CAUSE OF VALUE—THE GENERAL LAW OF VALUE—IMPOSSIBILITY OF A STANDARD OF VALUE.

1. We have seen in the preceding chapter that there are three species of Exchangeable Quantities, the various interchanges of which give rise to *sic* different kinds of exchange, which constitute the pure Science of Economics, or Political Economy, in its most modern definition. It has also been said that the Value of any Economic Quantity is any other one for which it can be exchanged. To examine these six species of exchange with all their ramifications, would be a complete treatise on Economics. In the present work we have only to do with *two* out of the six species of exchange, viz., the exchange of money for debts, and of debts for debts, which constitutes the business of Banking. We must now examine the foundations of the Theory of Value, which must be equally applicable to all Economic Quantities, and to all the six species of exchange. It is the more necessary to do this, and to lay before the reader shortly the remarkable misconceptions and self-contradictions which are very prevalent among writers on the subject, as they have done so much to obscure the Theory of Credit in recent times.

The complete Theory of Value comprises the following:—

1. *The Definition of Value.*
2. *The Origin, Source, or Cause of Value.*
3. *The General Law of Value.*

We must now examine each of these separately, and lay a solid foundation for our subsequent investigations.

On the Definition of Value.

2. In § 8 of the preceding chapter we have shortly defined the Value of an Economic Quantity to be any other Economic Quantity it can be exchanged for. Thus, let A and B be any two

Economic Quantities which are exchanged at any moment, then,
 $A=B$.

Then B is the Value of A, and similarly A is the Value of B, whatever be the nature of A and B.

Now, suppose B is 10 guineas; A may be any of the three species of Economic Quantities; it may be a material product, as a watch; or may be an immaterial product, as so much instruction; or it may be a bill of exchange, *i. e.*, a debt, or public stock; or any other species of incorporeal property. This furnishes a complete answer to those Economists like Malthus, who oppose the admission of immaterial products into Economics, alleging that they cannot be measured. The answer is plain, if a man can sell so much instruction for 10 guineas, by the very definition its Value is as clearly defined as if it were a watch. So also if so much public stock can be sold for 10 guineas, its Value is as clearly defined as in the other cases. If a man owes me a debt, *i. e.*, if I have the right to demand 10 guineas from him, and I know that he can and will pay me that sum on demand, the Value of the debt is 10 guineas.

But B may be either of the three species of Economic Quantities as well as A. Therefore any Economic Quantity may have value in terms of the others. Thus A may be a debt, and B may be a debt as well. That is, debts may have value in terms of other debts. The business of Banking chiefly consists in buying debts by creating other debts. And the variable relations of debts are subject to precisely the same general law of Value as those of any material products.

Moreover, it is perfectly clear that the Value of A increases and diminishes as B increases or diminishes, and the Value of B increases or diminishes as A increases or diminishes. It is also clear that if the exchangeable relation between A and B changes, the Value of *both* must have changed; it is clearly absurd to suppose that the Value of one remains the same while that of the other changes.

Thus J. B. Say, whose doctrines of Credit we shall have to investigate in a subsequent chapter, says that things cannot be valued except by an exchange. That Value is always comparative; that the Value of a franc is the things which one can buy with this sum, and that gold and silver have no value except what they can buy.

Hence we see that by its very definition, Value requires two objects; the Value of a thing is always something external to itself. It is absolutely impossible to predicate that any quantity has Value, without at the same time implying that it can be exchanged for something, and of course everything it can be exchanged for will be its Value in that commodity. Moreover, it is as absurd to speak of a quantity changing its own Value, without stating the article in respect of which its Value has

changed, as it would be to say that an object had changed its own distance, without stating what other object it was distant from.

The Value of the goods in the merchants' and traders' warehouses is the money in the pockets of their customers. The Value of the money in the pockets of the public, is whatever things they can buy with it. The Value of the professor's lectures is the fees paid by his scholars. The Value of an abstract right, or property, to demand a thing is the thing promised. Thus the Value of a £5 bank note is the 5 sovereigns. The Value of a postage stamp is the carriage of a letter. The Value of a pledge, or promise, to cut a man's hair is the cutting of the hair.

Hence also it is quite clear that nothing can have a fixed or invariable Value, because however it may remain the same with regard to any one or more things, yet if it has changed its relation to any other things, its Value has changed.

All this seems plain enough, but yet, with scarcely an exception, while Economists admit that the Value of a thing is something external to it, they constantly consider Value to be some quality appertaining to the thing itself, and inherent in it, without, apparently, the least idea that these are two different conceptions.

The extraordinary confusion of ideas of Smith and Ricardo are more fully shewn under the next section, and that of a *Standard of Value*, but we must just quote here a sentence or two from a few writers. Thus Ricardo commences his work:—"The Value of a commodity, or the quantity of any other commodity, is that for which it will exchange." At p. 333 (3rd edit.) he says, "I cannot agree with Mr. Say in estimating the Value of a commodity by the abundance of other commodities for which it will exchange." A disciple of Ricardo, who is supposed to have carried his doctrines to an extreme, says, "There is no necessary connection at all, or of any kind, direct or inverse, between the quantity commanded, and the value commanding." And a little further on, "I presume that in your use, and in everybody's use of the word Value, a high value ought to purchase a high value, and that it will be very absurd if it should not. *But, as to purchasing a great quantity, that condition is surely not included in any man's idea of Value!!*"—(*The Templar's Dialogues by De Quinevy.*)

Thus, also, an able Economical writer, Mr. Senior, says, "We have already stated that we use the word VALUE in its popular acceptation, as signifying *that quality in anything which fits it to be given and received in exchange*, or, in other words, to be lent or sold, hired or purchased.

"So defined, Value denotes a *relation* reciprocally existing between two objects, &c.!!"

Now, the quality of a melon which fits it to be sold is its agreeable flavour; this, according to Mr. Senior, is its Value, and so defined, he says that means it costs 5s.! That is, he defines the quality of a thing to be its price.

On the Error of the Expression Intrinsic Value.

3. We have now to call attention to a phrase which has been the cause of an enormous amount of confusion in Economic Science. Say remarks on the difficulty of divesting the mind of the influence of common language in Economics. Nothing has been more mischievous than the influence of the phrase we are going to notice, and to exterminate it is the first step in the improvement of the science, and the proper comprehension of the subject of credit.

Many Economists having defined the value of a thing to be the things it would buy, began to confine their attention solely to things of value, the produce of labour, quite oblivious of the fact that there are multitudes of things of value, which are not the result of labour at all. Then they began to consider that things would exchange in the proportion of the labour employed in producing them. Thus the value of a thing was considered to depend on the quantity of labour employed in producing it. Hence the quantity of labour embodied, as it were, in the thing, came to be counted as its value, and thus Value came to be called *Intrinsic*. And in late times the constant idea is that Value is some inherent quality of a thing conferred by labour. This unhappy phrase meets us at every turn in Economics, and yet the slightest reflection will show that to define Value to be something *external*, and then to be constantly speaking of *Intrinsic* Value, are utterly self-contradictory and inconsistent ideas.

Thus over and over again it is repeated in Economical treatises that money has *Intrinsic Value*, but that a bill of exchange, or bank note, is only the *representative* of Value.

Money no doubt is the produce of labour, but, as Smith observed, if it would exchange for nothing it would have no value; so, Say says, that the value of gold and silver consists only in what they will buy. How then can its value be *Intrinsic*? How can anything have *Intrinsic* Value unless it has the things it will exchange for inside itself? Money has *Intrinsic* Value! Has a piece of money got the merchandize, and all the other things it will purchase inside itself? Money will exchange for anything—corn, houses, horses, carriages, books, &c., and each of these is the Value of the money with respect to that commodity. But which of these is its *Intrinsic* Value?

The incongruity of these ideas is so glaring that it is only necessary to call attention to it, for it to be perceived at once. Yet from the very beginning of the science this phrase has infested it. So long ago as 1696, an excellent writer, Barbon, remarked

on the confusion it introduced into the subject. He says, "There is nothing that troubles this controversy more than for want of distinguishing between *Value* and *Virtue*."

"Value is only the price of things; that can never be certain, because it must be then at all times, and in all places, of the same value, *therefore nothing can have an INTRINSIC VALUE.*"

"But things have an intrinsic virtue in themselves, which in all places have the same virtue; as the loadstone to attract iron, and the several qualities that belong to herbs and drugs, some purgative, some diuretic, &c. But these things, though they may have great *virtue*, may be of small *value*, or no price, according to the place where they are plentiful or scarce, as the red nettle, though it be of excellent virtue to stop bleeding, yet here it is a weed of no value from its plenty. And so are spices and drugs in their own native soil of no *virtue*, but as common shrubs and weeds; but with us of great value, and yet in both places of the same excellent intrinsic virtue." Again, "*For things have no value in themselves, it is opinion and fashion brings them into use, and gives them a value.*"

Barbon thus puts his finger on the very thing which is the curse and the bane of Economic Science to this very hour, and especially of the Theory of Credit.

It is quite clear that money has not *Intrinsic* but *General Value*, because it is *generally* exchangeable throughout the country. But take it to a foreign country, or among a race of savages, and where would its value be? What value would a bag of sovereigns have among the Red Indians?

We know that persons throughout a country will always be ready to give things in exchange for the money of the country, hence money has *General* and *Permanent Value*, but manifestly not *Intrinsic Value*.

A Bank Note, however, which is payable on demand, is admitted by all Economists to have the value of money. And why is this? Simply because it is exchangeable for money. A bill of exchange on a solvent merchant has value, simply because at a certain time it will be exchanged for money: hence it is clear that bank notes and bills of exchange have value for precisely the same reason that money has, and no other, *viz.*, that they are *exchangeable for something else*.

The notes of a great Bank may be exchangeable throughout the country as easily as money, and such notes will of course have the same value as money in such a case. The Value of a bill of exchange entirely depends upon the solvency of the merchants whose names it bears. These may not be generally known throughout the country, and they may fail: hence the value of such an instrument of credit is not *general*, and it is *precarious*, but it is, nevertheless, of the same nature as that of money.

Hence we see that the Value of Money and Credit of all kinds is essentially of the same nature, though there may be different degrees of it. A piece of credit is an article of merchandize and an exchangeable commodity just as much as money or any other goods.

Moreover, we see, on considering the term Value, that it is nonsense to speak of the *representative* of Value. Value is a ratio—an external relation? What can be the representative of a ratio, or of an external relation?

To say that money, because it is material and the produce of labour, has intrinsic value, and that a bank note is only the representative of value, is just as absurd as to say that a wooden yard measure is *intrinsic* distance, and that the space of 36 inches between two points is *representative* distance.

It is of the first importance to Economic Science to exterminate this unhappy phrase Intrinsic Value, which is clearly shewn to be a contradiction in terms, and the source of endless confusion, especially in the Theory of Credit. How many writers acknowledge that bank notes, &c., if exchangeable for money, are of the same value as money, and perform all the functions of money, and in the next breath ridicule the notion that credit is capital! How many laugh at the idea that bits of paper can be wealth! And, in fact, it is not exactly these bits of paper that have value. What is really of value is the Right, or Property, to demand money. These bits of paper only contain the evidence of this Right, or Property, as a matter of convenience, which would equally exist without them. This property, nevertheless, whose existence so many are unable to realize, is the most gigantic subject of commerce of any, and its creation, exchange, and extinction is the subject of this work.

On the distinction between Depreciation and Diminution in Value.

4. We must now observe the difference between two expressions, which, though often used indiscriminately, are essentially distinct, viz., *Diminution in Value* and *Depreciation*. An *alteration in value* of any commodity means that the quantity of it which was considered as an equivalent for a certain amount of some other commodity with which it is compared, has undergone a change. *Depreciation* means that it is not really of the value it professes to be. *Alteration in value* of a commodity is always used in reference to some other commodity, with which it is compared; *Depreciation*, in reference to itself. Thus, if at any given time an ounce of gold will exchange for fifteen ounces of silver, and owing to any great and sudden increase of the quantity of silver, while the quantity of gold remains the same, one ounce of gold becomes able to purchase twenty ounces of silver, then silver is said to have sustained a *Diminution of*

Value with respect to gold; or if, while silver remained the same, gold became very scarce, so that one ounce of gold would purchase twenty ounces of silver, then gold would be said to have *risen in value* with respect to silver. But if a bank note which professes to be of the value of five sovereigns, will only purchase four sovereigns, it is *depreciated*; or if a guinea, which professes to contain a certain amount or fixed weight of pure gold, does not contain that amount, it is *depreciated*. The expression *Diminution in Value* is applicable both to commodities and money; the word *Depreciation* is more properly restricted to currency; when an analogous change takes place in commodities, it is usually called *deterioration*.

These distinctions are very necessary to be observed in all discussions regarding the value of coins which retain the same names during a long series of ages. The pound of money in the days of William the Conqueror really meant a pound weight of silver bullion; and silver was the only money. Since then, silver has greatly increased in quantity, and other things are used as money, which have tended very greatly to diminish its value. It is said, though of course all such statements are extremely difficult to verify, that silver has fallen to a twelfth of its value in those times. Not only has the value of the metal greatly diminished, but the coinage is greatly deteriorated. By various diminutions effected by successive sovereigns, the shilling now is only the 66th part of a pound weight, whereas it was formerly the 20th part. Hence it is said that a shilling will only command the 36th part of what it formerly would. Though, as great changes have taken place in everything else as well, it would be difficult to prove this.

These causes affecting the value of coins which retain their names through long periods, may act in the same or opposite directions. It is quite easy to imagine that a coin, though greatly deteriorated, or diminished from its original weight, may, in consequence of the increased value of the material of which it is composed, be able to purchase as much as it would have done originally. It is alleged sometimes that this happened at Rome. The first coinage of Rome was copper, and this metal was found in great abundance for some time after the foundation of the city. The first measure of value was the *as*, which was a pound weight of copper. The *as* was subsequently reduced to the twelfth part of its weight, and some writers say, that in consequence of the great scarcity of the metal, it had increased so much in value, that the deteriorated coinage would purchase as much as the full pound would originally. This may be so, or not, but it in no way affects the argument. It might, very possibly, have been so.

These considerations greatly affect the public in the matter of public debts. The State agrees at a particular time to pay a fixed

quantity of bullion, either for ever, or for a long period, to the public creditors. Now, even supposing all other things to remain the same, the value of the money may vary very greatly during long periods, either from the increased scarcity or the increased abundance of the metal; and either the State or the creditors may be grievously affected by these changes.

In recent times, many able Economists have expected that the value of gold would be violently affected by the great discoveries in California and Australia. Some countries have taken such alarm at this as to abolish gold as the legal measure of value, and some writers have proposed that the weight of the sovereign should be increased in consequence. Even if the consequences expected did follow, which is extremely doubtful, it is not very likely that this would be done. However, this is not the place to discuss this important question.

On the Origin, Source, or Cause of Value.

5. We have seen that there are three species of Economic Quantities which may have value, and have decided that the definition of *the* value of a quantity is any other quantity it can be exchanged for. We now come to the second branch of our inquiry—What is the Cause, or Source, of Value, and whence does it originate?

Now, when we are to search for the Cause, or Source, of Value, it may be as well to understand what it is we are searching for. We see that there are several species of quantities which all have value; we must, therefore, manifestly search for some cause that is common to them all. We are not seeking for what may, in many cases, accompany Value, or what is the *accident* of Value, but we are to search for that general cause, which being present, Value is present, which being absent, Value is absent, which when it increases, Value increases, and which when it diminishes, Value diminishes.

6. The first and most popular doctrine was, that the *cause* of Value was LABOUR.

Adam Smith founded, or rather is supposed to have founded, all his notions of Value upon Labour. This is so well known that we shall not here make any quotations to justify the assertion, more especially as we shall have to quote from him subsequently.

Ricardo began his work by expressly limiting his doctrines to certain specific classes of articles; but he soon lost sight of this limitation, and lays down the broad principle, that labour is “really the foundation of the exchangeable value of all things, excepting those which cannot be increased by human industry.” Again he says, “In speaking, however, of labour as being the foundation of *all* value;” and he considers the quantity of labour employed in obtaining commodities as their *absolute* value.

Ricardo very soon lost sight of the limitation he had begun with, and, as is usual in such cases, his disciples pushed the doctrine to its utmost extravagance. Thus McCulloch says (*Introductory Discourse to Adam Smith*, p. xliii.), "In its natural state, matter is very rarely possessed of any immediate or direct utility, and *is always destitute of value*. It is only through the labour expended on its appropriation, and in fitting and preparing it for being used, that matter acquires exchangeable value, and becomes Wealth."

Again, at p. xxxii. of the same discourse, he says, "Nature is not niggard or parsimonious. Her rude products, powers, and capacities, are all offered gratuitously to man. She neither demands nor receives an equivalent for her favours. An object which may be appropriated or adapted to our use, without any voluntary labour on our part, may be of the highest utility, but, as it is the free gift of nature, *it is quite impossible it can have the smallest value*."

Mr. Carey, the American Economist, also maintains that Labour is the sole cause of Value, and this doctrine he repeats over and over again. He replies to the objection, that "it may be said that Labour is not invariably a cause of Value," thus: "Pearls may be found by those who do not seek them, and meteoric iron may be a gift to those who little anticipate its reception, while others may seek for pearls, or dig for iron, without profitable results. These are accidents which do not in the slightest degree militate against the assertion that *all Value is the result of Labour*. Nine hundred and ninety-nine out of every one thousand parts of those annually created are so, and the exceptions are too slight to be deserving of consideration! They are just sufficiently numerous to prove the rule!!"

We need not multiply quotations, as we think it is sufficiently well known that this school of Economists holds that Labour is the cause of all Value, and that there can be no Value without Labour.

Now we may lay down this proposition—That if Labour be the sole cause of Value, then whatever labour has been bestowed upon must have value. For if there be two things produced with the same amount of labour, and the one has value and the other not, then there must be some other cause of value besides Labour, which is contrary to the hypothesis.

Moreover, *all variations in Value must be due to variations in Labour*.

Now, this doctrine is contrary to all experience. Because there are many material things which have value upon which no labour was ever bestowed—

1. As, for example, take the space upon which a large town stands. Land in the heart of London has been sold at the rate of £2,000,000 an acre, perfectly exclusive of any buildings on it.

Where is the labour that has been bestowed upon it? Again, as we recede from the centre, the value of land rapidly diminishes. At Charing Cross it may be worth £100,000 an acre; by the time we reach Kensington it has fallen to £10,000 an acre. Now, how can these variations in value be due to different quantities of labour, when, as we have seen, these spaces of ground are not in any way whatever the result of labour at all?

The doctrine that no natural product has value unless labour has been bestowed upon it, is contrary to all experience. The proprietor of a coal mine, or a stone quarry, demands and receives a price for the coal, or the marble, or building stone, as it is placed in the mine, or the quarry, before a human being has touched it. Is any one so simple as to suppose that the owner of the marble quarries of Carrara would let any one take the marble without payment? Does the value of these things come from labour?

2. Take the case of timber trees. In the Midland Counties of England there are many oak trees which would sell on the ground for £60 or more. They were perhaps self-sown. No human being, perhaps, ever bestowed so much labour upon them as to plant the acorn from which they grew.

Hence, we see that there are abundance of material things which have value, and upon which no labour was ever bestowed.

Next, *If Labour be the sole cause of Value, then all things produced by the same amount of labour must be of equal value.*

But this doctrine is also contrary to the most manifest experience. For, if it were true, a diamond and the rubbish it is found in, ought to have the same value! So should a pearl and its shell. If a sportsman were to shoot a pheasant with one barrel and a crow with the other, would they have the same value? Now here are products obtained by exactly the same quantity of labour, which have very different values. It is clear then, that there is some other cause of value besides labour.

Again, *if Labour be the cause of Value, the value must be proportional to the labour.*

But this doctrine is also contrary to the most manifest experience. Suppose that by good luck a gold digger finds a nugget of gold lying on the surface of the ground. Another, perhaps, works hard for six months, and finds one exactly similar. Then according to this doctrine, the latter nugget ought to be immensely more valuable than the other. Or suppose some gold was brought from diggings near the market, and that exactly an equal amount were brought from diggings many hundred miles off. The latter is of course produced, *i. e.*, placed in the market, at much greater cost and labour than the other. But would it be more valuable? The least experience shews that it would not be so, but that things of exactly the same

quality would be of exactly the same value at the same time in the same market.

Again, if Labour be the sole cause of Value, *a thing once produced by labour must always have value, and the same value.*

But this is notoriously contrary to experience, for it is notorious that a thing may have value in one place and not in another; and also at one time and not at another.

Take a bag of sovereigns among the Red Indians, and where would their value be? A professor of Greek and Latin, or mathematics, may find his acquirements of great value to him at the Universities, but of what value would they be to him in the Hebrides? A great lawyer finds his knowledge and abilities of great value to him in London, but of what value would they be to him in Timbuctoo?

Moreover, the same things are of very different values in the same place at different times. Thus, pictures by some masters constantly rise in value, and pictures by others frequently diminish in value.

Labour itself has Value. Now if Labour be the sole cause of Value, what is the cause of the Value of Labour?

Some Economists are so *entété* of the doctrine that Labour is the sole cause of all Value, that when the plain case of increased value by the simple operation of nature is put before them, they declare it is labour! Thus, when beer or wine is increased in value by fermentation, McCulloch gravely maintains that is Labour!! Can the force of absurdity go further? Suppose the beer *works* a little more and turns sour? He also maintains that the growth of a tree is Labour. By the same rule, when a lamb grows up into a sheep, a calf into a cow, or when an egg develops into a chicken, that is Labour! If then a tree labours by growing, suppose it labours a little more and decays? Suppose the egg labours and turns rotten?

Ricardo maintains that natural agents, though they add greatly to value in use, never add anything to exchangeable value. But every merchant, every manufacturer, every agriculturist in the world would at once say that such a doctrine is contrary to the plainest experience; so plainly, indeed, that it is useless to give examples to shew its fallacy.

Now, when we see such doctrines as these maintained by writers who are reputed to be authorities, we can scarcely wonder at the low esteem in which the Science of Economics is too generally held.

Lastly, if Labour is the sole cause of Value, it is clear that whatever labour has been bestowed upon must have value. But this is clearly contrary to experience. If it were true, suppose we began to dig a well, the rubbish got from the surface would have little value; but as we went deeper and deeper, the rubbish

brought up ought to have a constantly increasing value. But this is evidently contrary to fact.

Hence we see that there are material products which have value, which are not in any way the product of labour—that labour may produce material products which have no value—that the same quantity of labour may produce products, one of which has value, and the other not—that quantities of things produced by varying quantities of labour have the same value—that things produced by labour may have value in some places and at some times, and not in other places or at other times—and that things produced by less labour may have greater value than things produced by more labour—from which the indisputable inference is, that Labour is in no way whatever the *cause* of, or even necessary to, Value; and, in fact, in this commercial country, the enormously greater proportion of valuable things are not the produce of labour at all.

It is thus seen that labour is only often associated with Value, or that it is the accident of Value; and we must entirely reject Labour as being the Cause, or Source of Value.

7. J. B. Say saw that the doctrine that Labour was the cause of Value was untenable, and he said that Value arose from UTILITY.

This doctrine is considerably more specious than the former one, and yet reflection will shew that it is liable to the same fatal objections as that of Labour; for it makes Value some quality of the thing itself, absolute and inherent, and therefore, of course, its value cannot vary so long as the quality remains the same. Many of the arguments which we applied to labour are also applicable to utility, and therefore we need not repeat them.

The doctrine that utility is the cause of value is more specious in this respect, that for a thing to be useful, it must be useful to some person. But then there is this defect, that the same thing may be useful at some times and not at others, and in some places and not in others, and to some persons and not to others. As for instance, some people smoke and some do not. A box of cigars would have value among a society of smokers, whereas a society of non-smokers would consider them a nuisance, and they would have no value there. A tureen full of train oil would be a great delicacy and highly prized by the Esquimaux, but it would probably not have the same value at the Lord Mayor's dinner.

It is notorious that merchants cannot sell their goods to savage nations until they have been refined and taught to feel the want of them. And, in short, it is clear, that however useful a thing may be, unless its qualities are known to, and wanted by, some one, it cannot have value. The qualities of the cigars are absolutely the same; but offered to those who want them, they have utility; offered to those who do not want them, they have none.

Not only is it evident that utility is so vague an expression that it cannot be made the basis of value, but there are also a great number of things which have value to which it would be a great debasement of the word utility to apply it to them. The depraved tastes and licentious appetites of too large a portion of mankind confer a value upon things of the most mischievous and noxious nature. In former times, there was, undoubtedly, a large sale for low and licentious literature and pictures. It was impossible to deny that such things had value, but would any one debase the word utility by applying it to them? And yet, while such masses of abomination met a ready and large sale, no Economist could refuse to class them as wealth.

8. Seeing, then, that labour and utility altogether fail to stand the test of being the cause of value, what remains? The only thing which Smith said long ago—EXCHANGEABILITY. And what does exchangeability depend upon? If I have something to offer for sale, what is necessary in order that it may be sold? There must be some one else to DEMAND it. Aristotle said long ago that it was *χρεία*, or *demand*, that bound society together. So Say speaks of the value which men attribute to things, that it is a moral quality. He also says that demand is the first cause of their value, and that they can have no value unless they are demanded.

Here it is quite clear that we have now got the true source and cause of value. It is DEMAND. Value is not a quality of an object, but an *affection of the mind*. The sole source and origin of value is *human desire*. When there is a demand for things they have value, when the demand ceases they cease to have value, and (the supply being the same) when the demand increases the value increases, and as demand diminishes value diminishes. It is demand which discriminates between the pearl and the shell, the diamond and the rubbish. It is because some people demand cigars that among them cigars have value, and because others do not demand them, that among them they would have no value. It is the intensity of demand that confers such enormous value on the space in the heart of London, and the gradually diminishing demand which makes land less valuable as the distance from the centre increases. What is it that gives value to the produce of the farmer? It is the demand of the people for food and clothing, and their readiness to give something in exchange for its products. These wants are permanent, and consequently, so long as they exist, the value of the land will be permanent. If it were possible to imagine that men would cease to require food or clothing, or should they change their tastes and require such food and clothing as could not be produced in England, then the value of the land would immediately die off.

The value of land, then, arises from the fact that it supplies something that is wanted by men. And men invest their money and their labour in cultivating land and rearing cattle, because they expect that they will continue to have a permanent value. So in the same way, it is the wants and desires of men that cause others to invest their money and labour in any pursuit whatever, and which gives value to that product. The continued desires and wants of men in law, medicine, engineering, literature, art, and science, cause other men to devote their money and their labour in becoming lawyers, physicians, engineers, authors, artists, &c., &c., and so on through the whole catalogue of trades and professions. It is the demand of the public, and that only, which confers value on them. And if the demand of the public were to cease, the whole value of the labour of those who had devoted themselves to their acquisition would be lost.

Hence we see how totally erroneous is the doctrine so common among writers that labour is the cause of, or even necessary to, Value. Archbishop Whately remarked this:—"In this as in many other points in Political Economy men are prone to confound *cause* and *effect*. It is not that pearls fetch a high price *because* men have dived for them; but, on the contrary, men dive for them because they fetch a high price."

The preceding observations seem to us to prove irrefragably that it is demand, or consumption, and not labour that gives value to production; and that it is *not labour which is the cause of Value*, but *Value which is the cause of, or inducement to, Labour*.

Value, therefore, in its true sense, signifies an affection of the mind. The usual phrase is, "I value so and so" It is the force of attraction between the mind and some external object. But an impotent desire of the mind, not manifested by any overt act, is not an economical phenomenon. In order to come into that science something must be done. But even then the desire of a single mind is not sufficient to produce an act. A man may have things he wants to sell, but if no one will buy them, they have no value. He may wish to possess things offered for sale by others, but if they do not want, and will not take in exchange what he offers, no exchange can take place. In order to constitute an exchange two persons must produce something, and what each produces must be wanted by the other. Hence the concurrence of two minds is essential to produce an exchange, or an economic phenomenon. Each one will try to give as little as he can of his own product to obtain as much as he can of the other's. Hence, when the exchange ultimately takes place, the quantity exchanged by each measures the intensity of his desire to obtain possession of the product of the other. And hence the quantity given by each is called *the Value of the other*.

Value, then, resides exclusively in the mind. It is not the

labour of the producer, but the desire, or the demand, of the consumer, or purchaser, that constitutes a thing wealth. The cessation of demand causes a destruction of capital and of wealth. The creation of a new desire causes the production of new wealth, and of new capital. Heavy taxes can only be borne by an industrious and wealthy people. And no people can be wealthy who are not inspired by strong and various desires. Hence we may see in a purely economical point of view the enormous importance of an educated and an enlightened people. The multiplication of wants multiplies industry, multiplies capital, multiplies incomes, multiplies the persons to bear the burden of taxation, and renders the nation capable of great achievements, and of taking a leading position among the nations of the world.

On the General Law of Value.

9. Having thus given the Definition of Value, and found that its source, or origin, lies exclusively in the human mind, the last branch of our inquiry is to determine the General Law of Value, that is, to discover the causes which produce changes in the exchangeable relations of quantities, whatever their nature be.

The commonest principles of science show us that there can be but one General Law of Value. There are six species of exchange, and the object before us is to discover a general law which shall govern them all. To develop the application of such a law in all the species of exchange would be a complete treatise on Economics. In the present work we are only dealing with two of the six species of exchange. But it is the fundamental condition of the truth of the general law that it shall be applicable to all the six species indifferently. The law which governs the exchangeable relations of material products must equally govern the exchangeable relations of debts.

It is on this point that the Economical system of Ricardo is contrary to all the fundamental principles of modern science. He begins his work by excluding from his inquiry all but a small class of objects, namely, material products which can be increased without limit by human exertion. He divides these into such things as manufactures, which can be indefinitely increased by equal quantities of labour, and such things as corn, minerals, &c., which can only be increased at a constantly increasing cost of production. Ricardo's system of Political Economy is nothing but a treatise on the price of manufactures, corn, minerals, and one or two other things. And for each of these he proposes a distinct law of value. Mr. Mill, who ardently admires Ricardo, has added other false distinctions of his own, thereby making the system still worse. Moreover these writers have altogether omitted the greater portion of things that have value, from their consideration. Such a system as

this is utterly repugnant to the established laws of modern science. The only way to attain scientific truth is to embrace all sorts of things which have value in one definition, and all changes of value of all the quantities in one general law.

Lord Lauderdale long ago observed, as is indeed quoted by Ricardo—that of two quantities which may each vary, if we suppose the variation to take place in one of them first, the other remaining the same, its value would be influenced by four causes:—

It would increase in value—

(1) *From a Diminution in Quantity.*

(2) *From an Increase in Demand.*

It would diminish in value—

(1) *From an Increase in Quantity.*

(2) *From a Diminution of Demand.*

Now as the variations of the other quantity will be influenced by the same *four* causes, it is quite clear that the variations of both quantities will be influenced by EIGHT independent causes. Experience also proves that none other than these causes produce changes in value, and hence it is manifestly the great general law of which we were in search.

Now Ricardo admits it to be true of all monopolized commodities, and for all others during a limited period. But, in fact, it is not only true during a limited period, but it is true in all cases and in all times.

It would be quite easy to reduce the separate cases treated by Ricardo and Mr. Mill to this general law, and to abolish the false distinctions created by them, but that would be beyond the purpose of this work.

Bacon truly says, “That which in Theory is the cause, in Practice is the rule.” The practical meaning of which is this: that all changes in value take place by or through changes in the *supply* or the *demand* of the quantities exchanged, and nothing else, and that if we wish to produce changes in value, the only way it can be done, is by causing some changes in the Supply or the Demand.

A Standard of Value is impossible.

10. The unfortunate confusion of ideas between the Value of a quantity being any other quantity a thing will exchange for, and the quantity of labour as embodied in obtaining the quantity itself, has led not only to the mischievous expression, Intrinsic Value, the source of endless confusion, but also to the search for something which reflection would have shown to be impossible, viz., an *Invariable Standard of Value*.

The great difficulty in dealing with Economical writers and their opinions is, that to collect their opinions, it is often necessary to place before the reader long passages, and to examine

closely the structure of nearly every sentence, to mark the changes and inconsistencies of thought which take place. This is insufferably wearisome to the reader, and therefore we must refer to the chapter in Smith on the subject, for a full consideration of his views. It is B. i., c. v. But we must shortly state his doctrine.

The first doctrine he lays down is that the value of any commodity is equal to the quantity of labour which it enables him to command or purchase. Hence, if l denote labour,

$$A=l, 2l, 3l, 4l \dots$$

He then says, in the next paragraph, that that is the same thing as saying that it is equal to the produce of labour, it enables him to purchase; or, denoting produce by p ,

$$A=p, 2p, 3p, 4p \dots$$

And then in the next paragraph he says that the value of anything is more frequently estimated in money than either in labour or commodities; or, denoting money by m ,

$$A=m, 2m, 3m, 4m \dots$$

Now, although it has justly been pointed out that these modes of estimating the value of a quantity are by no means identical, we observe that in this passage Smith defines the value of a thing to be something *external* to itself—it is the thing which any thing can be exchanged for. Hence it is manifest that the value of A must vary directly, as l , p , or m . The more of l , p , or m that can be got for A , the more valuable is A ; the less of l , p , or m that can be got for A , the less valuable is A . It is also perfectly clear, that if any change whatever takes place in the exchangeable relations between A and these quantities, the value of A has changed.

Hence Smith admits that Value, like distance, requires two objects. If any change takes place in the position of either of these, the distance between them has changed, no matter in which the change takes place. So if the exchangeable relation between two quantities changes, their Value has changed, no matter in which the change takes place. Hence it is clear that there can be no such thing as *Invariable Value*. Nothing whatever can by any possibility have an invariable value, unless its exchangeable relations with everything else were fixed. Hence we can at once see that, by the very nature of things, there can be no such thing as an invariable standard of value, by which to measure the variations in value of other things, because by the very nature of things the very condition of anything being invariable in value is that nothing else shall vary in value, and consequently the very condition of there being an invariable standard is, that there shall be no variations to measure.

Nevertheless a very large body of Economists have set out upon this wild goose chase—this search for an invariable

standard, which is utterly contrary to the nature of things should exist at all. Directly after the passages we have referred to, Smith commences the search for that single thing which is to be the invariable standard of value. He says that gold and silver will not do because they vary in their value, —sometimes they can purchase more and sometimes less of labour and other commodities. Then he says:—

“But as a measure of quantity, such as the natural foot, fathom, or handful, which is continually varying in its own quantity, can never be an accurate measure of the quantity of other things, so a commodity, *which is itself continually varying in its own value*, can never be an accurate measure of the value of other commodities. *Equal quantities of labour at all times and places may be said to be of equal value to the labourer.* In his ordinary state of health, strength, and spirits, in the ordinary degree of his skill and dexterity, he must always lay down the same portion of his ease, his liberty, and his happiness. *The price which he pays must always be the same, whatever may be the quantity of goods which he receives in return for it.* Of these, indeed, it may sometimes purchase a greater and sometimes a smaller quantity, *but it is their value which varies, not that of the labour which purchases them.* At all times and places, that is dear which it is difficult to come at, or which it costs much labour to acquire, and that cheap which is to be had easily, or with very little labour. *Labour alone, therefore, never varying in its own value, is alone the ultimate and real standard by which the value of all commodities can at all times and places be estimated and compared.* It is their real price; money is their nominal price only.

“*But though equal quantities of labour are always of equal value to the labourer, yet to the person who employs him they appear sometimes to be greater, and sometimes of smaller value.*

* * * * *

“*Labour, therefore, it appears evidently, is the only universal, as well as the only accurate measure of value, or the only standard by which we can compare the value of different commodities at all times and at all places.*”

Now the utter confusion of ideas in these passages is manifest. A foot, or a fathom, is an absolute quantity, and of course may increase or decrease by itself; but Value, by Smith's own definition, is a *ratio*, and therefore we might just as well say that, because a foot which is varying its own length cannot be an accurate measure of the length of other things, therefore a quantity which is always varying its own *ratio* cannot be an accurate measure of the *ratio* of other things. The utter confusion of ideas as to the whole nature of the thing is manifest. We may measure a tree with a yard, because they are each of them single quantities, but it is an impossibility that a *single*

quantity can measure a ratio. It is a manifest impossibility to say

$$a : b :: x$$

It is manifestly absurd to say 4 is to 5, as 8, without saying, as 8 is to what, just as it is absurd to say that a horse gallops at the rate of 20 miles, without saying in what time.

But Smith tells us that "equal quantities of labour are always of equal value to the labourer." What! if a man performs a certain quantity of labour and gets £1,000 for it, is his labour of the same value to him as if he gets five shillings?

The incongruity of ideas in this chapter of Smith are palpable. He first of all defines the Value of A to be the quantity of things it will purchase, and therefore of course varying directly as that quantity, and then he suddenly changes the conception of Value into the quantity of labour bestowed in producing A, and says that the Value of A is invariable, so long as it is produced by the same quantity of labour, and that its Value is the same whatever quantity of things it will purchase!

The term Value has been used with such diversity and inconsistency of meaning by writers, that it will aid much in shewing the confusion that runs through the whole of Smith's ideas to translate them into mechanical language, thus:—

"As a measure of quantity, such as a foot, which is always varying its own length, can never be an accurate measure of the length of other things, so an object which is always varying its own *distance* can never be an accurate measure of the *distance* of other objects. But the sun is always at the same distance. And though the earth is sometimes nearer to the sun, and sometimes farther off from it, the sun is always at the same distance. And though the earth is at different distances from the sun, it is the distance of the earth which has varied, and not that of the sun; and the sun alone, never varying its own distance, is the ultimate and real standard by which the distances of all things can at all times and places be estimated and compared."

Such is a fair translation into mechanical language, merely substituting "distance" for "value," of Smith's ideas. No wonder, says Francis Horner, "we have been under the necessity of suspending our progress in the perusal of the *Wealth of Nations*, on account of the insurmountable difficulties, obscurity, and embarrassment in which the reasonings of the fifth chapter are involved."

But after saying, in the last-mentioned passages, that a thing produced by the same quantity of labour is always of the same value, no matter what it may exchange for, he says, speaking of money, in the passage we have already quoted, if it could be exchanged for nothing, it would be of no more value than the most useless piece of paper. So that, after beginning with exchangeability, and then adopting quantity of labour, he comes

back again to exchangeability as the measure of Value, quite unconscious that these are different conceptions. And this confusion of idea runs through the whole of Smith's work: one half of it is based upon labour being the foundation of value, and the other half upon exchangeability.

Exactly the same confusion runs through the whole of Ricardo. He begins by defining the value of a thing to be something external to it, and then he afterwards says, that by Value he means the cost of production or the quantity of labour bestowed in obtaining a thing. The very first day that Bentham read the work, he wrote to tell him that it was all founded on a confusion between *Cost* and *Value*.

The whole of this search after an invariable standard of Value is founded upon this false conception, that the value of an article is the quantity of labour bestowed in obtaining it. Ricardo says, "The labour of a million of men in manufactures will always produce the same value." "That commodity is alone invariable, which at all times requires the same sacrifice of toil and labour to produce it." Also, "When commodities varied in relation to value, it would be desirable to have the means of ascertaining which of them fell and which rose in real value, and this could be effected only by comparing them, one after another, with some invariable standard of value, which should itself be subject to none of the fluctuations to which other commodities are exposed. Of such a measure it is impossible to be possessed, because there is no commodity which is not itself exposed to the same variations as the things the value of which is to be ascertained; that is, there is none which is not subject to require more or less labour for its production." "Of such a commodity we have no knowledge, but we may hypothetically argue and speak about it, as if we had."

In these passages Smith and Ricardo have both assumed that labour is an invariable standard of value. Other things, it is true, have been proposed, such as corn; but we need not encumber ourselves with their consideration, because our object is to shew that such a thing is, by the very nature of things, absolutely impossible.

One of the first writers to point out the impossibility of such a standard was Mr. Samuel Bailey, in his admirable "*Critical Dissertation on the Nature, Measures, and Causes of Value*," a work which has greatly contributed to found Economic Science.

If we had a British yard and any foreign measures before us, we could at once perceive the difference between them, and if we were told the measurements of any foreign buildings, however remote in age or country, we could by a very simple calculation, reduce them to the standard of British measurement, and compare them in size with our own buildings. So with our measures of weight; if we were told that in ancient days people

could carry a ton as easily as men can now carry a hundred-weight, we should at once have a standard by which we could judge of the relative strength of men of old and the men of the present day.

In a certain popular way money is termed the measure of value. And so it is in exchanges which are effected at the same time and place. If we were told that a quarter of corn was worth 60s., and that a sheep was also worth 60s., at a certain time and place, we should know that they were then and there equal in value. That is, they would both exchange for the same quantity of gold or silver.

But such matters are not the result of simple perception by the senses. If we had a quantity of gold or silver placed beside a number of other things, no human sense could tell us what their relative values were. And the most violent changes in value might take place without our being able to have the slightest perception of such a thing.

Moreover, it would be equally absurd to suppose that we could ascertain the different values of different quantities of gold obtained in different ages and countries. If a quantity of gold coins minted in the reign of Elizabeth, a similar quantity minted in China, and an equal quantity minted in the reign of Victoria were placed side by side, what human sense could discern the difference in value between them? And yet that is what those Economists require, who want an invariable standard of value. They want something by which they can at once decide whether gold is of more value in 1400, or in 1800, in England or in China, without any reference to anything else.

The least reflection will shew that this is an impossibility. The only test of value is an exchange, and unless we can effect an exchange there can be no value. How can we exchange an ounce of gold in the year 1566, for an ounce of gold in the year 1866? Mr. Bailey well says, p. 72, "Value is a relation between contemporary commodities, because such only admit of being exchanged for each other; and if we compare the value of a commodity at one time with its value at another, it is only a comparison of the relation in which it stood at these different times to some other commodity. It is not a comparison of some intrinsic independent quality at one period, with the same quality at another period, but a comparison of ratios, or a comparison of the relative quantities in which commodities exchanged for each other at two different epochs. If a commodity A in the year 100 was worth 2 B, and in 1800 was worth 4 B, we should say that A had doubled its value to B. But this, which is the only kind of comparison we could institute, would not give us any relation between A in 100 and A in 1800: it would be simply a comparison of the relation between A and B in each of these years.

“It is impossible for a direct relation of Value to exist between A in 100 and A in 1800, just as it is impossible for the relation of distance to exist between the sun at the former period and the sun at the latter.”

It is obvious that all we can do by a measure of Value is to ascertain in a convenient way the exchangeable relations existing between any quantities at any given time. And by a comparison of prices at different epochs we can observe the differences which have occurred in the exchangeable relations of these quantities between the different times. And this, though far from what is required by those writers, is all that we can have.

The fundamental objection then to there being a Standard of Value is simply this, that Value is always a ratio, and a single quantity cannot be the measure of a ratio. And yet it is by no means uncommon to hear able men rise up at learned associations and demand that the Government should institute an inquiry to ascertain and fix an invariable Standard of Value, in the same way as they have bestowed great care and pains to fix the standard of length, and capacity, and weight. All they can do is to maintain a fixed weight and purity in the current coin of the realm; but they can no more control its variations in Value than they can regulate the motions of the stars by Act of Parliament.

CHAPTER III.



THE THEORY OF CREDIT.

“Εἰ δὲ τοῦτο ἀγνοεῖς, ὅτι πίστις ἀφορμὴ τῶν πιασῶν ἐστὶ μέγιστη πρὸς χρηματισμὸν, πᾶν ἂν ἀγνοήσῃς.”—*Demosthenes.*

“If you were ignorant of this, that Credit is the greatest Capital of all towards the acquisition of Wealth, you would be utterly ignorant.”

“Credit is the vital air of the system of Modern Commerce. It has done more a thousand times to enrich nations than all the mines of all the world.

* * * * *

“Credit is to money what money is to articles of merchandize. * * *

“It is very true that Commercial Credit, and the system of Banking as a part of it, does furnish a substitute for Capital.”—*Speech of DANIEL WEBSTER, in the Senate of the United States.*

CHAPTER III.

THE THEORY OF CREDIT.

PRELIMINARY OBSERVATIONS.

SECTION I. INVESTIGATION OF THE NATURE OF CREDIT—
ON THE DISTINCTION BETWEEN A BAILMENT AND A DEBT—
AMBIGUOUS MEANING OF THE WORD LOAN.

SECTION II. UPON INSTRUMENTS OF CREDIT.

SECTION III. ON COMMERCIAL CREDIT.

SECTION IV. THE THEORY OF BANKING.

SECTION V. EXAMINATION OF THE OPINIONS OF MODERN
ECONOMISTS ON CREDIT AND CURRENCY.

PRELIMINARY OBSERVATIONS.

1. We have now arrived at the consideration of the great subject of Credit, the great marvel of modern commerce. What the steam engine is in manufactures, what the differential calculus is in mathematics, that is Credit in Commerce.

Credit in its simplest form, it is true, did exist in ancient times, and even then, when it was in its very infancy, Demosthenes, as we see in the motto prefixed to this chapter, says that he who is ignorant that Credit is the greatest capital of all is utterly ignorant.

But the Credit which was understood and practised in ancient times is no more to be compared to the system of Credit which exists now, than the steam-engine, as it was before the days of James Watt, is to be compared to what it is now. That apparently simple, though really surprising, discovery that a Debt is exchangeable property, or an article of merchandize, and that its effects in promoting the formation and exchange of products are identical with those of specie itself, is entirely, we believe, a discovery of modern times; and, like many other discoveries which have produced the most important consequences to mankind, the origin of the system is involved in much obscurity, and it grew up gradually and silently.

Nevertheless, at the present time, the commerce in Debts is beyond all comparison the most gigantic of any. Truly, says Daniel Webster, "Credit has done more a thousand times to enrich nations than all the mines of all the world." So also an able French writer, M. Gustave du Puyode says, "However fruitful have been the mines of Mexico and Peru, in which, for a long time after Columbus, seemed buried the fortune of the

world, there is yet a discovery more precious for humanity, and which has already produced more wealth than that of America: that is, the discovery of Credit—a world altogether imaginary, but vast as space, as inexhaustible as the resources of the mind." The merchants who trade in debts—namely Bankers—are now the Rulers and Regulators of commerce: they almost control the fortunes of States. Some of the most palatial structures of modern times are those devoted to the commerce in debts. The subject of debts is one of the most extensive and intricate branches of the Law of Property; and all over the country are established Courts of Law, whose exclusive province it is to deal with this species of property.

It was out of discussions on the nature of Credit that the modern science of Political Economy took its rise, and yet it is the subject which has been least understood by Economical writers. To understand it properly requires a thorough settlement of nearly all the fundamental conceptions in Economic Science, which hitherto has been almost entirely neglected. It requires a knowledge of some of the most abstruse branches of law; and, indeed, to explain some cases in Credit was too much for some of the most eminent judges on the bench. In one case, Lord Eldon said, "I think that I argued the case of *Ex parte Walker*, and I must say, that the speculations about paper certainly outrun the grasp of the wits of the Courts of Justice. This sort of circulating medium puzzled as able a man as ever sat here—Lord Thurlow. * * * What was to be done then? The court was puzzled and distressed. At last, however, we came to a sort of anchorage in that case—*Ex parte Walker*. I have no difficulty in saying that I never understood it. I am satisfied, that though no doubt the court understood that judgment, yet none of the counsel did." And it requires a thorough knowledge of some of the most abstruse branches of commerce. But even that is not sufficient to explain the whole of this beautiful subject. Mathematicians have for more than a hundred years called debts "negative" quantities, but not one has ever given any explanation of what was meant by calling a debt a "negative quantity" that could be received in Economic Science.

In a work of this kind, which must necessarily endeavour to be as simple as possible on subjects of the greatest abstruseness, it would be out of place to enter into a complete discussion of the question of how the negative sign, the complete theory of which has only been really understood by mathematicians themselves within the present century, is applicable to the Theory of Credit. In this work we only state results, expressed as simply as we can; but for the full development of this subject we must refer to our "*Dictionary of Political Economy*," Art. *Credit*, where the whole subject is explained, and it is seen what a

beautiful exemplification it is of the universally received mathematical doctrine.

In this chapter we have endeavoured to explain the fundamental conception of Credit, and to point out certain important distinctions between instruments of credit and other paper documents, and also some ambiguities of language, to which much of the confusion which is prevalent on the subject, is due. Credit is recorded and transferred by means of certain forms, which are then explained, and some peculiarities pointed out, which have been misunderstood by some writers of influence on the currency, and thus caused some important errors. There are two grand divisions of Credit, Commercial Credit and Banking Credit. The mechanism of each of these is fully exhibited in the following sections. Having thus given an exposition of the actual facts, we are led finally to examine the doctrines which have been put forth recently by Economical writers, and to point out their variance from each other, and from themselves.

SECTION I.

INVESTIGATION OF THE NATURE OF CREDIT—ON THE DISTINCTION BETWEEN A BAILMENT AND A DEBT—AMBIGUOUS MEANING OF THE WORD LOAN.

Investigation of the Nature of Credit.

2. In the first chapter we gave a short definition of credit, and showed that it is a species of independent exchangeable property of the same nature as, but inferior in degree to, money. We also showed that it has value for precisely the same reason that money has value, and no other, namely, because it is exchangeable for something else. We must now investigate its nature somewhat more minutely.

It has been observed that, as an Economic Quantity, a man exercising any profitable business bears a strong analogy to the land. The value of the land consists in the right to the past produce, together with the right to receive its future produce for ever: so the value of a man as above, consists in his right to the past produce of his industry, together with his right, or property, to receive the profits of his future industry as they arise.

Now he may trade with the produce of his past industry as represented in money, or he may trade with the expectation of making future profits; and when he does so, this is called his credit.

Hence his total purchasing power is his money, together with his credit; his property in the fruits of the past, together with his property in the fruits of the future. Hence we see that Credit may be called the *inverse* of money.

Now this latter property, though intangible, is yet a real property.

Suppose a man has a flock of sheep, or a field sown with corn. Although the increase of the flock, or the next harvest are not yet in existence, he has the right to receive them when they do come into existence. Knowing then that, at a certain period, the increase of the flock and the field will be in existence, and of a certain value, the owner may buy things with his promise to pay when they are produced, and if this promise does not exceed the value of the future produce, it will be a safe operation. We see also plainly that the limit of the promise transferred, or the credit, is the value realised by the produce.

Now it is clear that though the farmer is not bound to pay this promise until the produce is realised, yet if an estimate were made of what he was substantially worth, these debts would have to be subtracted from his possessions, and he would

only be worth the balance, but yet this debt, or promise, or obligation, might be transferred a hundred times before it was paid and extinguished.

Mathematicians have for many years been in the habit of calling debts *negative* quantities. They say that if a man's property may be called *positive*, his debts may be called *negative*. By which they mean that if we wish to estimate a man's fortune we must subtract his debts from his property, and the remainder will be his fortune.

This mode of statement is sufficiently correct in some respects. If a man were going to retire from business, he would call in, and discharge his debts, and what remained afterwards would be his fortune.

But such a mode of statement is quite unsuitable for Economic Science, because debts are a species of property of the most gigantic magnitude, which is a subject of commerce as much as any other merchandize, until they are extinguished, and Economic Science has only to do with them while they exist and are in commerce. When they are paid they cease to exist.

Moreover it is contrary to law and fact to say that a man is in debt, until the period of payment has arrived.

Suppose a man rents a house or a farm, he promises to pay a definite sum as rent, at certain fixed periods. But he does not owe the payment until the period arrives. A tenant is not in debt at the present moment for rent which will not be due for two months. Nevertheless the right to receive that rent when due is the property of the landlord, and he may sell and transfer it to any one else, and it may be sold or exchanged as distinct property, any number of times before it is due and is paid.

It is exactly the same with a merchant who buys goods and gives his promise to pay for them three months after date. Such a transaction is a complete sale or exchange, just as much as if he had paid cash. The goods become his absolute property, and the promise he has given is the absolute property of his creditor, which he may sell like any other merchandize. When the period of payment arrives the merchant is bound to effect another exchange, and buy the debt with money, but until that is done, it exists as a distinct property.

The fortune of the merchant might be stated thus—

PROPERTY—OBLIGATIONS;

And so far as he is concerned this would be substantially correct.

The real subtlety in the case consists in this, that while the merchant's property is his own, which he may do what he likes with, his debts, or obligations, are also exchangeable property which may circulate in commerce, and produce all the effects of money.

Moreover, if his creditors were to release him from any of his

obligations, it is evident that his fortune would be so much increased. Hence we see, that to him, the release of a debt is augmentation of capital.

The proper method of understanding the statement of this question is of such supreme importance in grasping the true Theory of Credit, that we must illustrate it a little more.

The celebrated mathematician, Euler, says, "The manner in which we generally calculate a person's property is an apt illustration of what has just been said. We denote what a man really possesses by positive numbers, using or understanding the sign +, whereas his debts are represented by negative numbers, or by using the sign —. Thus, when it is said of any one, that he has 100 crowns, but he owes 50, this means that his real possessions amount to $100-50$, or, which is the same thing, $+ 100-50$, that is to say, 50.

"As negative numbers may be considered as debts, because positive numbers represent real possessions, we may say that negative numbers are less than nothing. Thus, when a man has nothing in the world, and even owes 50 crowns, it is certain that he has 50 crowns less than nothing; for if any one were to make him a present of 50 crowns to pay his debts, he would still be only at the point nothing, though really richer than before."

It is quite easy to shew that the first paragraph is not a suitable mode of stating the question in Economic Science. For suppose that a man has 100 crowns, but is bound to pay 50 crowns one year hence; then his property would be correctly stated as $100-50$; but it would be quite inaccurate to say that his property was only 50 crowns; for this reason—he has the 100 crowns to trade with in the mean time to make a profit out of, and all he is bound to do is to have, on a certain day at the end of a year, 50 crowns to discharge his debt. And the owner of the debt may put it into circulation, and it may produce all the effects of money until it is paid. So that there are the 100 crowns, *and* the debt of 50 crowns as well, circulating simultaneously in commerce.

Again, in the second paragraph, when Euler says that he has less than nothing, when he has nothing and owes 50 crowns, this clearly means that he has not only spent the accumulation of his *past* industry, but also spent the anticipated proceeds of his *future* industry. Now, let us suppose that, having done so, some one makes him a present of 50 crowns to pay his debt, then, as Euler says, he is 50 crowns richer than before, but yet his property is now only=0.

That is to say, that if some one gives a man enough money to pay his debts, he is by so much the richer, although he is only worth nothing.

The same practical result may be attained in a different way.

Suppose that his creditor releases him from the debt, he is then exactly in the same position as if some one had given him money to pay it with,—he is by so much the richer, though he is now worth nothing.

Hence we have in all cases this doctrine, which is the fundamental one upon which the whole Theory of Credit is based—

A release from a debt is absolutely equivalent to a payment in money.

Also, a mutual release of debts is absolutely equivalent to a reciprocal payment of debts.

Suppose a banker has issued so many notes; these are circulating debts, and he is indebted to the holders of them.

Suppose that a merchant has bought goods with his bill at three months, and the banker has bought this debt, then, on the day of payment, the merchant is bound to pay his debt in money.

The banker may present it for payment to the merchant, who may pay it in money.

But suppose he has become possessed of an equal number of the notes issued by the banker, then, of course, the banker is equally indebted to him, and bound to pay him an equal amount of money.

Thus the two parties, the merchant and the banker, are equally indebted to each other, and when the merchant is called upon by the banker to pay his bill, he may, instead of money, give him an equal amount of his own notes, the banker at the same time giving the merchant back his bill. Each of the parties has thus paid his own debt by releasing the other from his debt, and this mutual release of debts has been absolutely equivalent to a payment in money. Of course if the two debts were not exactly equal, the difference would have to be paid in money.

This simple case is an example of the almost universal practice in this commercial country. The enormously greater proportion of modern commerce is carried on by means of credit, and not by cash, and the enormously greater proportion of debts are paid, not by cash, but by mutual releases of debts. We observed in the first chapter that the use of money was to preserve and record the debts that arose from the unequal exchanges. In modern commerce, credit is the merchandize with which operations are carried on, and money now only performs the very insignificant part of settling unequal credits.

The considerations in the preceding paragraphs will, we hope, be sufficient to explain that seeming paradox, which so many find it so hard to understand, that Credit is Wealth and Productive Capital. For we have defined wealth to be simply exchangeable property, and we have shewn that any exchangeable property whatever may be employed as productive capital; since purchase, as all Economists allow, is one species of production. In this country the immense majority of purchases are

effected by credit. Credit is productive capital in the same way that money is, and in no other. Smith, after saying that retailers are "productive" labourers, because they "produce" what is wanted in their shops, and that capital so employed is "productive," says that money "produces" nothing, for which McCulloch justly censures him—"It is a capital error to affirm that the gold and silver used as money, *produce* nothing; on the contrary, it is quite obvious that, by facilitating exchanges, and enabling the division of labour to be carried to a much greater extent than it could be under a system of barter, they are *in no ordinary degree productive*." Now, credit performs exactly the same function as money in this respect, and to a far greater extent, and hence it is far more productive than money.

Now, so far is it from being a paradox that debts, or credit, are wealth, that a little reflection will show that when a country employs credit, it is just so much the richer by an equal amount of the precious metals. Suppose a machine is required for a certain purpose, then if we can substitute a very cheap machine for a very expensive one, we are so much the richer by the difference between the cost of the two. Now, as credit and specie perform exactly the same duty, if there were no credit it would require an equal amount of specie, which could only be purchased by an equivalent amount of merchandize. Credit costs nothing, and hence the difference between that and an equal amount of specie has been saved to the country. Hence, not only is the total cost of the machine saved by the country, but exchanges are enormously accelerated and increased. Therefore the country has not only gained the difference in the cost of the machine, but also all the profits generated by these exchanges, and, of course, it is impossible to calculate these accurately.

On the Distinction between a BAILMENT and a DEBT.

3. The preceding remarks are sufficient to explain the fundamental nature of credit. Before, however, we proceed to the exposition of the mechanism of the system, we must observe upon some confusion on the subject that has arisen among modern writers. It is a point of the greatest importance, and, in fact, may be called the *pons asinorum* of Economic Science. It is, perhaps, somewhat of a subtle nature, and would not be perceived by any one not conversant with law and commerce. But it is one of those delicate subtleties which occur in all sciences, upon which the most important consequences turn, and it is, in fact, a confusion on this point, which is at the root of most of the false theories of currency and credit, which have produced such terrible catastrophes in the world.

There are two species of paper documents which are in general use in commerce, and which have some superficial resemblances—that is, they both convey rights to certain

things, and are similarly transferable, and are therefore considered by many to be of the same nature, but which are yet fundamentally distinct in their nature, and in this radical distinction is contained the basis of the Theory of Credit.

These species of paper documents are—

I. Bills of Lading, Dock Warrants, and all other titles to specific things.

II. Bank Notes, Bills of Exchange, and other forms of Credit.

In order to show clearly the fundamental distinction between these two classes of paper documents, we will explain how each arises.

When a man ships goods on board a vessel, he receives from the captain a paper document, acknowledging the receipt of the goods, and promising to deliver them to whomsoever shall be the owner of the paper. This document is called a *Bill of Lading*.

The shipper of the goods sends the Bill of Lading to the consignee, who directly he receives it may negotiate it, *i. e.*, transfer it by indorsement to whomsoever he pleases, in all respects like a Bill of Exchange, and it may pass through any number of hands, and whoever is the owner of it at any time may go and demand the goods from the captain.

Similarly, when goods are deposited in a dock warehouse, the dock master gives a paper document or a receipt for them of a similar nature to the Bill of Lading, which is called a Dock Warrant. This is transferable in all respects like a Bill of Lading, or Bill of Exchange, and whoever is the owner of the Dock Warrant is the owner of the goods described in it, and is entitled to demand and receive them from the dock master.

Now, it is especially to be observed in these two cases that, although the goods are delivered into the temporary custody of the captain, or dock master, they have no *property* in them. The *property* in the goods remains with the shipper or depositor, and is transferred by him along with the Bill of Lading, or Dock Warrant. The captain, or dock master, is the mere BAILEE, or TRUSTEE, of the goods, and *not* the OWNER. He has no right to convert them to his own use, and if he did so, it would be a *robbery*, and he would be liable to be punished as a *thief*. Thus the Bill of Lading and the Dock Warrant form *one* property with the goods, and cannot be separated from them. The goods travel *with* the paper document. Thus it may be said in this case that the paper document *represents* goods. In this case there is no *exchange*, and these documents have no *value*, *i. e.*, they are not exchangeable separately. They are not exchangeable for goods generally, but are titles to certain specific goods and no others. No one ever spoke of the *value* of a Bill of Lading, or a Dock Warrant. Such documents are *not credit*, because the owner of them does not simply *believe* that he can

obtain goods in exchange for them, but he *knows* that he has become the owner of certain specific goods. Such a transaction is not an exchange, but is what is called in law a BAILMENT.

So also a man may take a bag of money to his Banker, and may ask him to take care of that specific money, and give it back to him, or any one else he may name, on demand. In such a case, no *Property* in the money would pass to the Banker. He would have no right to use it for his own purposes, and if he did so, he would be guilty of theft. If he gave a receipt for it, promising to deliver it to whomsoever it might be transferred, that receipt and the money would be *one* property, as in the case of Bills of Lading and Dock Warrants. The money and the receipt could not be separated, and the property in that very money would always pass along with the receipt. The Banker in such a case would be merely the BAILEE, or TRUSTEE, of the money, and not its OWNER. In the cases of the captain, the dock master, and the banker above described, the relation of Debtor and Creditor does not arise between them and the owners of the paper documents.

But this is not the ordinary case of a Banker and his customer. When a customer pays in money to his account at his Banker's, the *Property in the money passes absolutely to the Banker*. He is not the *Trustee*, or *Bailee*, of the money, but he becomes the *Owner* of it, and is entitled to use it in any way he pleases, for his own purposes. In *exchange* for this money, he creates a *credit* in his customer's favour, promising to deliver an equal amount of money on demand. This transaction is, in fact, an *exchange*, or a sale. The Banker buys the money from his customer, by *selling* him the right to demand an equal quantity of money at any time he pleases. Here, therefore, a *New* property is created. The customer may transfer this property to whomsoever he pleases, and it has *value*, because the owner of it can *exchange* it for money, or anything else. It is called CREDIT, because the owner of it only believes he can obtain money in exchange for it, but it is not appropriated to any specific sum of money. The Banker is not the trustee of the money, but he becomes the *debtor* to his customer, and, if unfortunately he should happen to fail, his customers, or creditors, are only entitled to have his property divided among them, and they must take their chance of having their debts paid in full.

It is exactly the same in all cases of Credit. If a merchant sells goods on credit, it is absolutely essential to the nature of the transaction that he should part with the property in the goods to the buyer, and receive only the abstract right to demand payment. Without the cession of the Property there is no credit.

Hence we see the radical and fundamental distinction between Bills of Lading and Dock Warrants on the one hand, and instruments of credit of all sorts on the other.

Bills of Lading and Dock Warrants are absolutely bound down and fixed to certain specific goods, and cannot be separated from them, and therefore they form only ONE property with them. They always arise out of a BAILMENT, and never out of an EXCHANGE, and they may justly be said to represent goods. They in themselves are nothing, and are no addition to the mass of other exchangeable property.

On the other hand, it is the fundamental legal requisite of an instrument of credit, that it shall be absolutely severed from any specific sum of money. It is even forbidden to be made payable out of any particular fund. It is nothing but an abstract right against the PERSON, and that is the very circumstance from which it takes its name, because it must be received on the simple *belief* that it can be exchanged for money. If any specific money was appropriated to it, it would not be *credit*. An instrument of credit always arises out of an *Exchange*, and never out of a *Bailment*. Bills of Lading, &c., always go along with goods, &c.; Bank Notes, &c., are always exchanged for money, &c. Bills of Lading *represent* goods, but are not of the *value* of goods, because there is no exchange, and there can be no value without an exchange. Bank Notes, &c., do not represent money, but they are of the *value* of money, because in their case there is always an exchange. And credit, in all its forms, is an addition to the mass of other exchangeable property.

From this it clearly follows that Bills of Lading and Dock Warrants can never exceed in quantity the goods they represent; if any one were to negotiate such documents without any goods to which they were attached, it would be an indictable fraud. But instruments of credit, of all sorts, immensely exceed in quantity the money in the country—on the lowest calculation, tenfold. Credit is in itself a merchandize, and the subject of a gigantic commerce. It may be said that all commercial crises arise out of the excessive creation of that species of property called credit. What are the due limits of credit is a question of the most momentous consequence, and the considerations we have already presented throw a great light on it, but it will be more convenient to defer this until we have given the exposition of the mechanism of the system of credit.

It is of the most fundamental consequence to understand clearly the distinction between Instruments of Credit on the one hand, and Bills of Lading and Dock Warrants on the other. Many able Economical writers recently have fallen into the grievous error of classing them together as all being of the same nature, and as Credit. Some of the most terrible financial catastrophes have been caused by adopting systems of paper money founded on this error. It will suffice here to say that John Law's Theory of Paper Money, of which we have given an exposition in a subsequent chapter, was entirely founded on this misconception.

On the Ambiguity in the meaning of the word LOAN.

4. There is still one formidable ambiguity to be cleared away, which has in recent times created immense confusion in the Theory of Credit. All the older writers, who were chiefly men having a practical knowledge of business, seeing that credit causes exactly the same circulation as money, maintained the doctrine that credit is capital, without entering into any very nice definition of either credit or capital.

Since the time, however, of the French writer, J. B. Say, this has been the subject of much ridicule. It has been repeated by a multitude of writers, that those who say that credit is capital, maintain that the same thing can be in two places at once. They conceive credit to be the loan of some material substance to some one else, and they ask how can the same thing be used by two persons at once, the borrower and the lender.

In a subsequent section we shall point out the astonishing self-contradictions of Say on this subject. It will suffice here to say that the whole misconception is founded on an ambiguity in the meaning of the word LOAN. And the examination of this will show upon what subtle considerations some of the most important doctrines in science depend.

Suppose any one lends his friend some such an article as a book. Then it is clear that the borrower and the lender cannot both have the book at once. Suppose that this person, wanting his book back again, calls on his friend and finds him not at home. Seeing perhaps his book on his friend's table, he would have no scruple in taking it away; though he would probably have the courtesy to tell his friend he had done so.

But suppose the same person had lent his friend £5, and, as before, wanting it back, called on him and found him not at home. Suppose he saw his friend's purse on the table, would he feel himself justified in opening it and helping himself to five sovereigns? Every one would at once feel he would not. He would have no scruple in taking back his own book which he had *lent*; but he would never dream of opening his friend's purse, and taking out five pounds he had *lent*.

Thus, without giving any particular thought to the subject, every one would instinctively feel that there was an essential distinction between the cases of *lending* a book and *lending* money. Or if he was so obtuse on the subject, the law would tell him so. The law would tell him he might take away his own book if he pleased, but that if he opened his friend's purse and took out five sovereigns, he would be guilty of *theft*; and that he must request his friend to pay him, but that he had no right to help himself.

So if a man pays in money to his account at his banker's, *i. e.*, lends him money, and wants some, would he venture to take it

himself off the counter? Of course he would not. He would request his banker to pay him, and he must wait until his banker gives him the money of his own free will. If he ventured to take it himself he might be given in charge to a policeman.

The fact is, that though both these operations, lending a book and lending money, are both called a *loan*, they are of an essentially distinct nature. When a man lends a book, or any other chattel, to his friend, he never parts or dispossesses himself of the property in it. He is entitled to have that very book, or the very chattel, back again. There is no exchange, and no new property created. And only one party can have the use of the book, or the chattel.

But in all cases whatever of a *loan* of money, the lender absolutely cedes the property in the money to the borrower, and it becomes his absolute property. What the lender does acquire is the right, or property, to demand back an equivalent amount of money, but not the specific money. A loan of money, is therefore, always an exchange, and in all such cases, there must, by necessity, be a new property created; and this property may be sold and transferred like the money itself.

In the loan of a book, or a chattel, the right to it, or property, of the lender, is never severed from it; in a loan of money, the right, or property, of the lender in it is always severed from it, or rather, transferred to the borrower; and the new right, or property, created in the lender is termed a Debt, or Credit, and when the debt is paid, or, in common language, the loan returned, this new property is destroyed.

Hence we see that there are two distinct species of loan: the one where the lender has the right to have the very thing returned, the other where he has only the right to demand to have an equivalent amount returned. Now all commercial loans are of the latter species: they are all sales, or exchanges, and they are never of the former sort; and all the confusion on the subject has arisen from not observing this distinction.

The same ambiguity also affects the word *Borrow*.

The confusion arises, then, from the English language having but one word, *loan*, to denote two distinct operations. The French language is equally faulty. But in Latin there are two words corresponding to these two meanings. These are *commodum* and *mutuum*. A *commodum* is a loan where, as in the case of a book, the property in the thing remains with the lender, and the identical thing is returned. A *mutuum* is where, as in the case of money, the property in the thing passes to the borrower, and in exchange for it is given, or created, the right to demand an equivalent at some future time. Now, from the word used, it is clear that there is an exchange. All commercial loans are *mutua* and not *commoda*.

SECTION II.

UPON INSTRUMENTS OF CREDIT.

5. We have now at length laid a solid foundation for an exposition of the mechanism of the great subject of Credit. We have shown that Credit is a species of exchangeable property, and that it has value for the very same reason that everything else has value, and no other, because it is exchangeable for something else. We have also pointed out the fundamental distinction between instruments of credit of all sorts, and such paper documents as Bills of Lading and Dock Warrants, and also the ambiguity in the words *Loan* and *Borrow*, which has caused so much confusion in the subject.

A debt, or credit, though saleable property, is yet invisible and intangible, and it is frequently, for the sake of convenience, recorded on paper, and the paper document is termed an instrument of Credit.

It is, perhaps, scarcely necessary to observe that this paper contains nothing but the *evidence* of the debt, which consists in the right residing in the person of the creditor, and equally exists without the paper.

These instruments of credit are of two forms:—

I. *Orders* to pay money, including Bills of Exchange of all sorts, Cheques, Bankers' Drafts, Exchequer Bills, Navy Bills, &c.

II. *Promises* to pay money, including Bank Notes, Promissory Notes, Credits in Bankers' Books called Deposits.

Orders to pay money are usually called *Bills*; promises to pay money are usually called *Notes*.

6. Before entering more minutely into the varieties of credit, it will be as well to explain certain peculiarities of English Law, as a misapprehension on this point has led to some erroneous doctrines on the extent of the currency.

There are three distinct species of property known and recognised by the Common Law of England, the transfer of which is subject to different rules. Firstly, goods and chattels of all sorts; secondly, money; thirdly, claims or liabilities, such as a debt, called a *chose in action*.

With respect to the first species of property, if a thief steals any of my goods, the Common Law says that he cannot transfer a property in them to any buyer, however innocent, unless the sale be made in market overt. That is, if he sell the stolen goods privately to any one else, who buys them honestly, without knowing they have been stolen, and gave a full price for them, the real owner may recover them from the innocent buyer.

With respect to money, if the owner of it finds it in the hands of the thief he may recover it; but if the thief has purchased things in a shop with it, the shopkeeper who takes it honestly in the way of his trade, has a right to retain it against the original owner; that is, as Lord Mansfield said, money cannot be recovered after it has been paid away in currency.

With respect, however, to the third species of property, viz., debts, it is an inflexible rule of the Common Law that they cannot be transferred at all. Thus, the transfer of Bank Notes, Bills of Exchange, &c., which are debts, is in direct contravention of the Common Law of England. However, the custom of negotiating Bills of Exchange grew up and flourished among merchants for upwards of three centuries before any case arising out of them came before a Court of Law. In course of time the Common Law adopted the *Lex Mercatoria*, or custom of merchants, and by it Bills of Exchange were treated like money in so far as this, that the property in them passed like that of money. Thus, if they were stolen, though the true owner might recover them if he found them in the hands of the thief, yet if he had passed them away for value to an innocent holder in the course of business, that innocent holder acquired the property in them, and might retain them against the true owner, and enforce payment from all the parties liable. Thus Bills of Exchange were assimilated to money in this important respect, that, even though stolen, when they had once been passed away in currency, the property in them belonged to the person who had innocently purchased them.

But promissory notes, such as bank notes, were of much later introduction into this country, and for a long time they were not recognized by the law merchant, as is explained below, and there was no case to decide whether the property in a stolen note would pass to an innocent holder for value, like money and bills of exchange. At length this was determined by Lord Mansfield in 1756, in the celebrated case of *Miller v. Race*, which is one of the leading cases in English law. He decided that the same rule applied to bank notes as to bills of exchange, and that, when stolen, when they had once been paid away in currency, the property in them passed to an innocent holder for value, and they could not be recovered by the original owner.

Hence the same law holds good with regard to money, and all instruments of credit—that when they have been stolen and paid away, and taken honestly in the course of business, the original owner cannot recover them. And it must be observed that this rule was held to apply to bills of exchange for centuries before it was applied to bank notes. The reason why we draw attention to this latter fact so particularly will be apparent afterwards.

On Bills of Exchange.

7. In its most general form, a Bill of Exchange is a letter from one person to another, ORDERING him to pay—first, a certain sum of money; secondly, to a certain person; thirdly, at a certain event. The usual form is this:—

£287 : 15 : 8

London, May 4th, 1866.

Three months after date, pay to myself (or A. B.), or order, the sum of Two Hundred and eighty-seven pounds fifteen shillings and eight pence, value received.

To Mr. John Cox,
Linendroper,
Strand, London.

WILLIAM SMITH.

The person who addresses the letter is termed the *drawer*; the person to whom it is addressed is called the *drawee*; and the person to whom it is to be paid is called the *payee*.

It is the payee's business, on the first convenient opportunity after he has received the letter, to present it to the drawee, to know if he will pay it; if he consents to do so, it is usual for him to write his name, with the word "accepted" across the face of the bill; he is then called the *acceptor*.

The drawer may make the bill payable either to a third person, or to his order, or to himself, or to his own order. If it be made payable to a third person only, or to the drawer himself only, without inserting the words "or order," the bill can only be paid to the person named, and cannot be transferred to any one else, or cannot be *negotiated*, as it is termed.

If the words "or order" are inserted after the payee's name, he can transfer it to any one else. This is done by writing his name on the back of the bill; hence it is called an *Indorsement*: the person who does it is called the *Indorser*, and the person to whom it is delivered is called the *Indorsee*.

The indorsee may, if he pleases, indorse it again to some one else, and if he make it payable to that person only, it is called a *special* indorsement, and can only be paid to him; but if he delivers it over with his own name only written on the back, it is called a *general* indorsement, or an *indorsement in blank*. Its effect is that it makes the bill transferable by mere delivery, without any further indorsement, exactly like a bank note or money; and the bill is then *payable to bearer* like a bank note.

Formerly indorsement was in all cases *necessary* to transfer the property in a bill or note. But this has long ceased to be the case in English law. It became the custom of merchants in England, which has long acquired the force of law, that any instrument of credit indorsed in blank, may be transferred by simple delivery, without any further indorsement.

It is still, however, the custom to indorse them on a transfer; at least there are very few persons who would take them without indorsement. And the effect of the indorsement is this: that if the bill be not paid by the acceptor at maturity, and if the owner, or *holder*, of it gives *immediate* notice to any, or all, of the preceding parties to it, he has a right to enforce payment of it from them.

But this demand for payment must be made without delay, in almost all cases within twenty-four hours after the fact of non-payment is known to the holder. If delay be made in notifying the fact, and demanding payment from the parties liable, they are absolved, and the holder's remedy is gone.

Thus in modern practice the indorsement is merely a *limited warranty of soundness*. There is no other difference between buying goods or money with a bill, with or without an indorsement, than between buying any other article such as a horse, a watch, or a carriage, with or without a limited warranty. It is in all cases a sale. In the case of a bill taken without an indorsement, or a horse bought without a warranty, the sale is final and conclusive; in the case of a bill taken with an indorsement, or a horse bought with a warranty, the sale may be cancelled, if the defect be discovered, and the demand made within the time limited, otherwise it is also final and conclusive.

The general rule of English law is now, that if any instrument of Credit whatever, whether it be a Bank Note, or a Bill of Exchange, be taken in exchange for goods or money in any transaction without indorsement, or if the period allowed for making a claim be suffered to elapse, it is a final closing of that transaction, and the receiver has no remedy against the transferor, if the instrument be not paid. *The payment is, in fact, in all respects, as valid and final as if it were money.*

Except only in the case of fraud, where the payer knew that the banker or person whose note or bill he tendered, was bankrupt or insolvent.

It is usual, in English Bills, to insert the words "value received," but it is not necessary. In former times it was necessary to state what the debt arose from, whether money or goods. But this has long fallen into disuse in this country.

8. A CHEQUE is a Bill of Exchange drawn by a customer on his banker, ordering him to pay A. B., or order, or bearer, a certain sum on demand.

9. Bills of Exchange have played such an important part in modern commerce, that we may shortly state in what manner they originated, and whence they derived their name. Some writers have supposed that they were used by the ancients, but there is no ground for such an opinion. It was to a certain

extent customary for Roman bankers to give drafts on their foreign correspondents, but that was not the origin of the modern system of Bills of Exchange.

The power and the arrogance of the Popes had long been increasing, till, in the time of the crusades, they claimed the general power to tax all Christendom to support them, and in process of time they sent their own agents to collect the money. These agents were correspondents of the Italian Cambitores, who were originally money dealers, who kept tables in the cathedrals, for the exchange of money of foreigners who came to worship. In the middle of the 12th century, the Florentines took up the business of money dealing to a great extent, and their example was soon imitated by other Italian cities, such as Lucca, Siena, Milan, Placentia, and Asti. Wherever the Pope's taxes were to be collected, these bankers sent their agents to collect them, and as soon as this was done, they sent drafts on their principals to the Pope. These letters were called *littere Cambitorie*, or money dealers', or bankers' drafts. Thus, originally, a Bill of Exchange was a banker's draft, addressed from a person in one country to some one in another, whose business it was to exchange foreign money. From these persons it naturally extended to commerce, but at what time does not appear. The oldest Bill of Exchange known to exist, is dated 1380. Another is quoted by Capmany, dated 1404, which was drawn by a Lucchese merchant of Bruges on his correspondent at Barcelona, and negotiated by him in Bruges. In neither of these bills are there any words of negotiability, yet we find that one was negotiated, whence we may conclude that the practice of negotiating them sprung up long before it was recognized on their face.

For a long period Bills of Exchange were confined to what their name indicated, namely, bills drawn in one country to be paid in the money of another. The Common Law of England, which inflexibly forbade the assignment of a debt, was, of course, a bar to their introduction in this country. But the custom with respect to foreign bills was adopted by it, to facilitate foreign trade. It was long before the transfer of Inland debts was attempted. At last, it was adopted between London and York, and London and Bristol. Thus the custom of Inland Bills of Exchange began. But it was still confined to different towns, and for a long time it was essential that a bill should be drawn in one town upon another. At last, in consequence of the Common Law recognizing Bills of Exchange, as part of the *Lex Mercatoria*, they began to be drawn by persons in the same town upon their neighbours, as between wholesale and retail dealers. Thus, by striking off one limitation after another, they have come, after a lapse of several centuries, to be what they are now, simply an order from one person to another, to pay a

definite sum of money, and they have thus lost all trace of their etymological origin.

On Promissory Notes.

10. Thus, at last, the convenience of trade overpowered the narrow rigour of the Common Law, and it became legal to transfer a debt in the form of a Bill of Exchange. But, so absurd and pedantic was the law, that it was not legal to do so in any other form, such as that of a simple acknowledgement of the debt by the debtor.

About the end of the Sixteenth Century, the merchants of Amsterdam, Middleburgh, Hamburgh, and some other places, began to use instruments of credit among themselves, and as they came into personal contact, these documents naturally assumed the form of an acknowledgement of the debt by the debtor, with a promise to pay it to bearer on demand, at the time fixed. These documents were called bills obligatory, or of debt, or of credit, and were transferable by indorsement in all respects like Bills of Exchange.

These documents are now called PROMISSORY NOTES, and an English writer in the time of Charles I., Gerard Malynes, strongly advocated their introduction into England, but he saw that the Common Law prohibited it. They first began to be used by the goldsmiths, who, as shewn afterwards, originated the modern system of banking in England soon after 1640. They were then called *goldsmiths' notes*, but they were not recognised by law. The first promissory notes recognised by law were those of the Bank of England in 1694, which were, technically, bills obligatory, or of credit. By the Act founding the Bank, their notes were declared to be assignable by indorsement (Act, Statute 1694, c. 20, s. 29). But this did not extend to other promissory notes. In 1701 and 1703 it was decided that promissory notes were not assignable, or indorsable over, within the custom of merchants. In consequence of these decisions, the Act, Statute 1701, c. 8, was passed, by which it was enacted that promissory notes in writing, made and signed by any person or persons, body politic or corporate, or by the servant or agent of any corporation, banker, goldsmith, merchant, or trader, promising to pay any other person, any sum of money, should be assignable and indorsable over in the same manner as inland bills of exchange.

These promissory notes, of all sorts, including Bank of England notes, as well as the notes of private bankers and merchants, were all placed exactly on the same footing as inland bills of exchange, that is, they were all made transferable by indorsement on each separate transfer.

In the case however of bank notes (by which, in law, is always meant Bank of England notes), as these were always payable on

demand, and the payment was quite secure, the practice of indorsement soon fell into disuse, and they passed from hand to hand like money. In the case of private bankers of great name, the indorsement was often omitted. But, though the ceremony of indorsement was often dispensed with as superfluous, it must be observed that in no way altered the character of the instrument, and the receiver of the note took it entirely at his own peril, and ran exactly the same risks as if he took any other instrument of credit without indorsement.

A promissory note is usually expressed thus:—

£143 : 4 : 9.

London, May 4th, 1866.

Three months after date, I promise to pay John Stiles, or order, the sum of One hundred and forty-three pounds four shillings and nine pence, for value received.

TIMOTHY GIBBONS.

In this case, Timothy Gibbons is called the *Maker* of the note, and John Stiles the *Payee*.

11. The system of credit forms two great divisions. The first is *commercial credit*, in which traders of all sorts buy commodities by creating debts payable at some time after date. The second is *banking credit*, in which bankers buy money and debts by creating other debts, usually payable on demand.

Moreover the system of Credit may, in another way, be conveniently divided into two parts. Credit being exchangeable property may, like money, be used either to circulate existing products, or to call them into existence. That is, it may be based upon the simultaneous transfer of a commodity, or it may be created to produce one. It is by no means uncommonly supposed that the former is the only legitimate use of Credit, and that the latter is fraudulent. We shall see, however, that this doctrine is quite unfounded. Certain documents, however, of the second form having been very grossly misused for fraudulent purposes, it has brought the whole system into groundless obloquy. We shall endeavour, in explaining the system of this second form, to point out in what the abuse of it and the danger really consist.

SECTION III.

ON COMMERCIAL CREDIT.

ON CREDIT BASED UPON SIMULTANEOUS TRANSFERS OF COMMODITIES—CREDIT CREATED FOR THE PURPOSE OF FORMING A NEW PRODUCT.

On the System of Credit based upon Simultaneous Transfers of Commodities.

12. Goods, or commodities, in the ordinary course of business, pass through the following hands:—1st, the foreign importer; 2ndly, the wholesale dealer; 3rdly, the retail dealer; 4thly, the customer or consumer. To the first three of these persons these goods are *capital*; because they import, manufacture, or buy them, for the sake of selling them with a profit; the fourth buys them for the sake of use or enjoyment. The price the ultimate consumer must pay for them, must evidently be sufficient to reimburse the original expense of production, together with the profits of the three succeeding operations.

Now, leaving out of the question at present, how the importer of the goods gains possession of them, which concerns the foreign trade of the country, which we do not touch upon here,—if he sells the goods to the wholesale dealer for ready money, he can, of course, immediately import, or produce, a further supply of goods in the room of those he has disposed of. In a similar way the wholesale dealer sells to the retail dealer, and if he were paid in ready money, he might immediately effect further purchases from the merchant to supply the place of the goods he had sold. So also if the retail dealer were always paid in ready money by his customer, he might replace the part of his stock that was sold; and so if everybody had always ready money at command, the stream of circulation, or production, might go on uninterruptedly, as fast as consumption or demand might allow.

This, however, is not the case. Few, or no persons have always ready money at command for what they require. Very few traders can commence with enough ready money to pay for all their purchases; and if the stream of circulation, or production, were to stop until the customer had paid for the goods in money, it would be vastly diminished.

Now, let us suppose that the merchant, having confidence in the character of the wholesale dealer, agrees to sell the goods to him, but not to demand money for them till a certain period afterwards. He accordingly parts with the property of the goods to the wholesale dealer, exactly as if he had been paid in money, and receives in return the right to demand payment

some time after date. Now the very same circulation of goods has taken place as would have been caused by money. The only difference is, that the actual payment is postponed, and for this the merchant charges a certain price. This debt may be recorded in two ways: it may either be simply recorded in the merchant's books, or else in a Bill of Exchange. But it is quite clear that the property is absolutely the same in whichever form it is, though one form may have more conveniences than the other.

In a similar manner, the wholesale dealer may sell for Credit to the retail dealer, and this debt may be recorded in two forms, like the first, either as a book-debt or in a Bill of Exchange. As in the former case, the same circulation, or production, has been caused by Credit, as by money. Lastly, the retailer dealer may sell to his customer on Credit, and this debt may also be recorded in two forms, either a book debt or in a Bill of Exchange. In this latter case the debt is very seldom embodied in a Bill of Exchange, it most frequently rests as a book-debt. But in this case, as well as in the former ones, Credit has had precisely the same effect as money in circulating goods. Hence we see that Credit has had precisely the same effect as money in circulating the goods from the merchant to the consumer. Moreover, we see that the passage of the goods through these various hands has generated a debt at each transfer. Supposing the merchant sold the goods for a debt of £100 to the wholesale dealer, the wholesale dealer would probably sell them for a debt of £140 to the retail dealer, and the retail dealer would sell them to different customers for debts, not less probably in the whole than £200. Hence we see that the successive transfers of the same goods have generated debts to the amount of £440: thereby exemplifying the distinction we have already pointed out between Credit and Bills of Lading; because, if the goods had passed through twenty hands, the same Bill of Lading would always have accompanied them.

Now the debt for which the merchant sold the goods to the wholesale dealer is no doubt valuable property to him, because he knows it will be paid in time. It may, moreover, be exchanged for anything else, like any other property, if any one will take it. But it is of no immediate use for what the merchant or manufacturer probably wants at the time, namely, money to buy more goods, or to pay wages, &c. Moreover, though he may be quite satisfied as to the safety of the debt, from his knowledge of his customer, it does not follow that others who don't know him will. Consequently such a debt would not be well adapted for general circulation, and therefore it would be of no use towards further production. In a similar way, the debt for which the wholesale dealer sold the goods to the retail dealer, would not be well adapted for general circu-

lation, and therefore could not conduce further to production. The debts due by customers to retail dealers, seldom do conduce to further production, because they are most frequently merely in the form of book debts.

Now, the merchant would probably sell to a great number of wholesale dealers whose debts would fall due at different times, and therefore a certain stream of money would always be coming in to enable him to continue production. Similarly, the wholesale dealer would sell to a great variety of retail dealers, whose debts would fall due at different periods, and so a certain stream of money would always be coming in to enable him to continue production. Similarly, the retail dealer sells to a great variety of customers, a great many of whom pay him ready money at the time of the purchase, as casual buyers, and his customers too, pay him money, by which he can continue to make purchases and keep up the stream of production. And therefore, this would greatly facilitate circulation or production.

And this we believe is the extent to which Credit in ancient times went. It did not go beyond book debts, at least as far as we have been able to discover. But all such statements must be made with the greatest reserve, because it is most unsafe to assert anything on merely negative evidence.

Credit, so far even as this, would be of great assistance to production, and the vast amount of it generated in this manner would be valuable property to its owners. But it is manifest that it would be of no further immediate use to them. It might therefore be aptly compared to so much dead stock. The next grand improvement would be to make this dead stock negotiable, or exchangeable. And in this, we believe consists the great difference between modern and ancient Credit. The great modern discovery is to make the debts themselves saleable commodities; to sell them either for ready money, or for other debts of more convenient amount, and immediately exchangeable for money on demand, and therefore equivalent to money.

There are two classes of traders whose especial business is to buy these commercial debts, and so to give activity and circulation to this enormous mass of valuable property, and to convert it from dead stock into further productive power. The first class of these traders are called BILL DISCOUNTERS, *i. e.*, *buyers of debts*; they buy these debts with money. The second class are called BANKERS; and they buy these commercial debts, by creating other debts payable on demand.

Banks, then, as far as regards our present subject, are shops opened for the purpose of buying these commercial debts. The merchant draws a bill upon the wholesale dealer, who accepts it, and thus becomes the principal debtor on the bill. The merchant then takes the bill for sale, or discount, as it is technically termed, to his banker. It is usual to make bills payable to the

drawer, or his order, which is signified by writing his name on the back of the bill. The merchant, therefore, writes his name on the back of the bill, and sells it to the banker, and this operation is termed **INDORSING** the bill. But the indorsement has another effect besides merely assigning over the debt to the banker, for, unless specially guarded against, it makes him a surety for the payment of the bill, in case the acceptor does not pay it. The effect, therefore, of the indorsement, is a sale of the debt, and a warranty of its soundness. But this warranty is not an absolute one, but only a limited one, as has been explained above. The banker, therefore, buys this debt with a limited warranty of soundness, by creating another credit, either as in former times, by giving the merchant the amount, less the discount, which some banks are permitted to do now, or else by writing down a similar amount to the credit of his account, which Credit is called a **DEPOSIT**, and giving the merchant power to draw upon him at pleasure, and at demand. Thus we see that the Banker has bought one debt, which is valuable property, by creating another debt, which is also valuable property, and is equivalent to ready money to the merchant. And we must particularly observe that this is not a cancelment of debts, as many suppose, but an *exchange* of valuable property.

The merchant has, however, a great many other similar debts, because he has sold to a great many wholesale dealers, and he will probably want to sell these in a similar way to his banker. The merchant will, therefore, indorse each of them over to his banker, thereby making each of the acceptors the principal debtor to the banker, but at the same time becoming himself responsible if any of them fail to pay his debt. If, therefore, the banker discounts the bills of 20 acceptors, he will have 20 principal debtors, who are each of them bound, under the penalty of commercial ruin, to pay their debts when they are due. The merchant, however, is surety for each of them, and as it may happen that out of so many, some may make default, the banker usually stipulates that the merchant shall leave a certain amount of deposit on his account by way of additional security. If any acceptor then make default, the banker immediately debits the account of his customer with the amount, and gives him back the bill. Thus, to a certain extent, the banker always keeps the means of paying himself in his own hands, besides having his customer's name on the bill, which makes his whole estate liable, and, even should his customer fail, he retains the right to have his debt paid out of the estates of both the principal and surety.

The wholesale dealer has given his acceptance for the goods, and he sells them to the retail dealer, and takes his acceptance for them. In a similar manner he wishes to sell this debt to his banker, and so convert it into productive capital. A similar

transaction takes place as in the former case. The wholesale dealer sells the debt of the retail dealer, and becomes himself surety for its payment to his banker. The banker also buys this debt by creating another debt payable on demand, which is equivalent to ready money.

The retail dealer may also draw upon his customers, though this is comparatively rare, because customers are generally beyond the pale of commercial law.

By these means we see that the dead stock of commercial debts are converted into productive capital. The merchant and the wholesale dealer, have now the full command of ready money for any purposes they require, and can continue the stream of production without interruption, and, as their bills fall due, all they have to do is to give an order on their banker.

These are the fewest number of hands that goods in the ordinary course of business pass through, and it is clear that, in their passage from the manufacturer to the customer, they will give rise to at least two bills, and sometimes three. They are all regular business bills, they originate from real transactions, and they are what are called real, or value bills, and they are what arise out of the regular and legitimate course of business, and are the great staple of what bankers purchase. It is a very prevalent belief among commercial men, that business bills are essentially safe, because they are based upon real transactions, and always represent property. But the foregoing considerations will dispel at once a considerable amount of the security supposed to reside in commercial bills on that account, because we have seen that in the most legitimate course of business, there will generally be two bills afloat, originating out of the transfers of any given amount of property, so that in the ordinary way there will be at least twice as many bills afloat as there is property to which they refer.

We must refer to the next section, for an exposition of the mechanism of banking, shewing how the creation and exchange of debts is made in modern commerce to perform the part of money. We will only observe here, that the manufacturer, the wholesale dealer, and the retail dealer, may all be customers of the same bank, and if they all have their bills discounted by it, it will purchase a whole series of debts arising out of the transfers of the same property.

The above operations are only what arise in the ordinary course of business; it may sometimes happen that property may change hands much more frequently, and at every transfer a bill may be created. Hence, when the credits are very long, and the transfers numerous, it is easy to imagine any number of bills being created by repeated transfers of the same property. In times of speculation, this is particularly the case. Now, all these bills are technically commercial, or real bills, but it is

evidently a delusion to suppose there is any security in them on that account. The fact is, that the whole misconception arises from an error in the meaning of the word "represent." A bill of lading does, as we have said above, *represent* property, and whoever has the bill of lading, actually has so much property. But a Bill of Exchange does not *represent* goods at all. It represents nothing but *debt*, not even any specific money. It is created as a substitute for money, to transfer property, but it does not represent it any more than money represents it. This was long ago pointed out by Mr Thornton, in his *Essay on Paper Credit*:—"In order to justify the supposition that a real bill, as it is called, represents actual property, there ought to be some power in the bill-holder to prevent the property which the bill represents from being turned to other purposes than that of paying the bill in question. No such power exists; neither the man who holds the bill, nor the man who discounted it, has any property in the specific goods for which it was given." This is perfectly manifest. It is both contrary to the law and the nature of Bills that they should be tied down to any specific goods. And it shews that the real security of the bill consists in the general ability of the parties to it to meet their engagements, and not in any specific goods it is supposed to represent, the value of which is vague or illusory, and impossible to be ascertained by any one who holds or discounts it.

The distinction between Bills of Lading and Bills of Exchange is of so subtle a nature, but is of such momentous consequence, that we may illustrate it still further. The preceding sections shew that any given amount of property may, by repeated transfers, give rise to any amount of bills, which are all *bonâ fide*, just for the same reason that every transfer would require a quantity of money equal to the property itself to transfer it. Then, even supposing the price remained the same at each transfer, it would require twenty times £20 to circulate property to the value of £20 twenty times. But also £20 by twenty transfers may circulate property to the value of twenty times £20. So also a Bill of Exchange may represent the transfers of many times the amount of property expressed on the face of it. This is the case whenever the bill is indorsed, or passed away for value; and the bill represents as many additional values expressed on the face of it as there are indorsements. Thus, let us suppose a real transaction between A and B. A draws upon B. That shews the bill has effected *one* transfer of property. A then buys something from C. It is clear that C might draw upon A, in a similar way that A drew upon B. But instead of that, A may transfer the Bill on B, by indorsement. It has now effected *two* transfers of property. In a similar way, C may buy from D, and in payment of the property may indorse over the bill to D. The bill then represents *three* transfers of property. In a similar

way it may pass through an unlimited number of hands, and will denote as many transfers of property. When C indorsed over the bill to D, he merely sold to him the debt which A had previously sold to him. Now that might be done, either by drawing a fresh bill on B, cancelling the first, or simply indorsing over the bill he received from A. Hence we see that every indorsement is equivalent to a fresh drawing. But if he draws a fresh bill on B, it will represent nothing but B's debt to him; whereas, if he indorses over the bill he received, it will represent B's debt to A, A's debt to C, and C's debt to D, and, consequently, it will be much more desirable for D to receive a bill which represents the sum of so many previous transactions, and for the payment of which so many parties are bound to the whole extent of their estates. Some thirty years ago, almost the entire circulating medium of Lancashire consisted of Bills of Exchange, and they sometimes had as many as 150 indorsements upon them before they came to maturity. From this also we see that no true estimate can be formed of the effect of the bills of exchange in circulation, by the returns from the Stamp Office, as has sometimes been attempted to be done, as every fresh indorsement is in effect a new bill. So that the useful effect of a bill of exchange is indicated by the number of indorsements upon it, supposing that every transfer is accompanied by an indorsement, which is not always the case. We see here the fundamental difference between Bills of Lading and Bills of Exchange, because the indorsements on the former denote the number of transfers of the same property; the indorsements on the latter denote the number of transfers of *different* property. Ten indorsements on a Bill of Lading shew that the same property has been transferred ten times, but ten indorsements on a Bill of Exchange shew that ten times the amount of property has been transferred once.

We have shewn that the prices of all commodities are universally governed by the Law of Supply and Demand at all times. If the supply be excessive, nothing can prevent the price from falling to any state of depression, until it becomes absolutely unsaleable. The commodity, therefore, will not pay the cost of its production, and unless those concerned in producing it have independent capital to enable them to hold on until the excessive supply is taken off, and save them from selling when the price is ruinously depressed, or to stand the losses, they will all fail.

Almost all men in commerce are under obligations; that is, they accept Bills of Exchange which must be paid at a fixed time, under the penalty of commercial ruin. To meet these obligations due by them, they have property of two sorts—debts, or obligations, due to them; and, secondly, commodities. To meet their own obligations, they must sell one or other of these kinds of property. They must either sell their debts to their bankers, or

they must sell their commodities in the market. While credit is good—that is, while bankers buy debts freely—they can retain their commodities from the markets, and watch their own opportunity of selling at a favourable moment. As their own obligations fall due, they sell to their bankers some of the debts due to them. Thus, if credit were always good, they might go on for ever without the necessity of ever having a single piece of money paid into their account, or having any money at all beyond what is necessary for their petty daily transactions. But if credit receives a check, and the banker refuses to buy their debts, they must still meet their own obligations, under penalty of ruin. They are consequently obliged to throw their commodities on the market, and sell them at all hazards; the supply of them becomes excessive, and inevitably depresses the price. Traders who have capital enough of their own to meet their engagements without discounting, are able to keep their commodities back from the market, until, the extra supply being exhausted, prices rise again, from the natural operation of the demand. Bankers, we have shewn, always buy the debts of traders by creating debts of their own, which are called their “issues,” and when bankers refuse to buy the debts of traders, they are said to “contract their issues.” Consequently, a contraction of issues, or of discounts, is generally followed by a fall in prices. And this fall in prices happening coincidentally with a contraction of issues, is frequently supposed to be caused directly by the diminished amount of currency compared to commodities, which is to a great extent erroneous, because it is in reality caused by the extra quantity of commodities, which a refusal to discount debts causes to be thrown upon the market.

We see, then, how utterly impossible it is to ascertain the precise effect of the contraction of issues of banks upon prices, because the change is principally produced by the quantity of produce which traders are compelled to sell to meet their engagements, when the negotiability of their debts receives a check, and of course similar circumstances not only compel traders to sell, but prevent others from buying. Consequently, the supply is greatly increased, and the demand greatly diminished. If, however, the holders of one commodity are possessed of much independent capital, and are not compelled to realize to meet their engagements, a contraction of issues would not affect them much. On the other hand, if the holders of another commodity were in general men who depended chiefly on credit, and were compelled to sell at a sacrifice to meet their engagements, a sudden refusal to discount for them would cause an extraordinary quantity of their produce to be thrown upon the market, and cause a ruinous depression of price.

It is the sudden failure of confidence and extinction of credit, which produces what is called in commercial language a

“pressure on the money market,” and which causes money to be “tight.” When money is said to be scarce, it does not mean that there is a smaller quantity of money actually in existence than before; there may be more, or there may be less in the country, no one can tell what the amount of money in existence is; but a great amount of credit, which serves as a substitute, and was an equivalent for money, is either destroyed altogether, or is suddenly struck with paralysis, as it were, and deprived of its negotiable power, and, therefore, practically useless. A vast amount of property is expelled from circulation, and money is suddenly called on to fill the void. When a new field of commercial adventure is found by sagacious discoverers, or a new market is suddenly thrown open by a change in the commercial policy of foreign nations, the first adventurers usually reap enormous profits. As soon as this becomes known, a multitude of other speculators rush into the same field, excited by the profits reaped by the first. Numbers of merchants and traders purchase commodities on credit, that is, they incur obligations which they must discharge at a future day, in the hope that the returns will come in before the day of payment. But the immense quantity of goods poured in usually gluts the market in a short time, and, from the excess of supply, prices tumble down often to nothing, so that the goods become unsaleable, and either no returns at all come in, or such as are quite inadequate to meet the outlay. When this occurs, it is called *overtrading*, and when this has been extensively practised, it is necessarily and inevitably followed by a great destruction of credit, and a great demand for *cash*. Thus, credit is destroyed faster than operations can be reduced in proportion. Those traders who have not received the returns they counted upon to meet their engagements, must raise money on any terms, and perhaps sell what property they have, at any sacrifice, to save themselves from ruin. The effect of this will be that money, for which there is an intense demand, will rise greatly in value, that is, discount will rise very high. But as a necessary concomitant of such a state of things, a great quantity of goods will be thrown upon the market, and their price will be enormously depressed. These circumstances will, therefore, produce a very high rate of discount, and ruinously low prices, which must continue until the excessive supply of goods is exhausted, and confidence revived. In such cases as these, traders who have not sufficient capital of their own to meet their engagements, and hold on their goods until prices rise, will infallibly be ruined. Under such circumstances, the rate of discount bears no relation whatever to the rate of profit. The use of ready money to persons who have overtraded, is of infinitely more consequence than the price they have to pay for it. It may be well worth their while to pay 15, or 20, or even 50 per cent. for

the use of money for a temporary emergency, which may save them from ruin, and enable them to maintain their position.

It is, therefore, not the scarcity of money, but the extinction of confidence, which produces a pressure on the money market; and an examination of all the great commercial crises in this country, will show that they have always been preceded and produced by a destruction of this credit, which has usually been brought about by extravagant overtrading and wild speculation.

The principle that the relation between supply and demand is the sole regulator of value, combined with the action of the credit system, will explain all the phenomena witnessed during a pressure on the money market. The failure of credit in any one branch of business will produce its full effect on the general market rate of interest, because that is regulated by the intensity of the demand for money from whatever quarter it comes; but it will not necessarily follow that the market prices of all commodities will be depressed. The market price for each commodity will be governed entirely by its own peculiar circumstances. If the holders of one commodity have independent capital, and have prudently abstained from overtrading, the price of such a commodity will not suffer much, because the ratio of supply and demand will not be altered to any great extent, but it cannot help sympathising to a certain extent with other commodities. But if the holders of another species of commodity have overtraded, and depended too much on credit, without sufficient means, they will necessarily be obliged to throw a great quantity of their produce on the market to realize, and this excessive supply will depress the price. And this effect will be increased because such are the very times when persons who have ready money are particularly cautious in buying, partly because they always hope the market will fall still lower, and they hope to buy cheaper when prices have fallen to a minimum, and they will certainly not buy more of any commodity than they can help, which is diminishing in value; and partly because they must keep their ready money to maintain their own position. From these causes, not only is the supply increased, but the demand is diminished, so that the fall is doubly aggravated. Thus, we see at once, that a falling market will always be well supplied, because people who must sell hasten to do so before the price falls still lower, and buyers hold aloof, waiting as long as they can, to see the lowest. On the other hand, when markets are rising, the case is reversed. The sellers hold aloof, hoping the price will be still higher, and buyers crowd in, hastening to purchase before the price rises more. A market that is desponding and inactive will usually continue so until people are persuaded that things are at the lowest, and are at the turn. It is evident that these considerations and observations apply to home produce, or at least to produce which is already

in this country, and which can be thrown on the market immediately. In order to attract foreign produce, the market must rise high for a considerable time, with the appearance of continuing so.

Considering that any bill whatever which is drawn against *bonâ fide* produce is in commerce technically a real bill, it will be seen at once that their supposed security is greatly exaggerated, because any operation, however foolish and absurd, is a good basis for a real bill. In times of rapid changes in price, multitudes of bills will be generated by speculative purchasers, and when the price falls as rapidly as it rose, as it usually does, it is simply *occupat extremum scabies*. Hence, losses, and very severe ones, too, are sure to happen in such times. But there is always at least this certainty with real bills. When persons have speculated unluckily and lost their fortunes, they are brought to a standstill. When a man has ruined himself by speculation, no banker out of Bedlam would advance him more money to speculate with. Hence, ill-judged speculation must stop a man's mischievous career in a comparatively short space of time, that is, whenever he has lost the value of the goods he has been speculating with. We shall find in the next section, unfortunately, that traders have devised a method to extract funds from bankers to speculate with, by which they can go on long after they have lost all they ever had, many times over, and adding loss to loss, until, perhaps, they may bring down their bankers, whom they duped and defrauded, as well as themselves. We have shewn, in the next section, that there are symptoms which will often indicate a commercial crisis.

On Credit created for the purpose of being applied to the Formation of New Product.

13. The operations on Credit, which we have hitherto been considering, were all based on an anterior operation, or one in which an exchange of commodities was affected by the creation and sale of the Credit, which Credit was afterwards sold or exchanged for another Credit. Such Credit is, therefore, manifestly limited by operations which have been made, and by commercial exchanges. The number of bills created could by no possibility exceed the number of transfers of commodities, although they might be greatly less, because, as we have seen, a single bill might be used to effect many transfers of property. In all these cases, a debt has been created, which was expected to be paid out of the proceeds of the sale of existing property.

But since Credit is, as we have shown, exchangeable property, and a substitute for money, it is clear that it may be applied as well as money to bring new products into existence. The limits of it in this case will be exactly the same as those in the former

case, namely, the power of the proceeds of the work to redeem the Credit.

As an example of such a creation or formation of a product, we may take such a case as the following:—Suppose the corporation of a town wishes to build a market-hall, but has not the ready cash to buy the materials, and pay the builder's and workmen's wages. It may be a matter of certainty, that if the market were once built, the stalls in it would be taken up immediately, and the rents received from them would liquidate the debt incurred in erecting it. But, as the workmen cannot wait until that period, but require immediate cash to purchase necessaries, it is clear that, unless there is some method of providing ready payment, they cannot be employed. In such a case, they might borrow money upon their own bonds, repayable at a future period. Now here we observe that these bonds are the creation of property. They are the right to demand a future payment, and are valuable exchangeable property, which may be bought and sold like anything else. In this case, we observe there is an exchange. But the corporation need not borrow money. They might make their own obligations payable at a future date. And if these were made small enough, and were readily received by the dealers in the town, they might be used in the payment of the workmen's wages, and perform all the functions of a currency, and be equivalent to money. Each of them is a new right created, and valuable property which is exchangeable, and, therefore, wealth, by the definition. They would be quite as efficacious in *producing* or forming the market-hall as real capital. And the market-hall itself would be capital, because it produces a profit. As the stalls were let and rent received for them, the bonds might be redeemed, and the debt cleared off. It is said that many market-places have been built by adopting such a plan. This case shews the utter futility of the notion that credit cannot be applied to the formation of products, and here we see it was not based on any anterior operation.

This is an instance of the *creation* of a product by credit, and not merely the transfer of an existing product. The result to the corporation would be precisely the same, whether they accomplished their object by borrowing real capital and paying interest for it, or by issuing bonds, bearing interest, payable at fixed periods. In the one case, they would be liable to the full extent of their property to the persons from whom they had borrowed the money; in the other, to those who held their bonds. If the operation was successful, its profits would in the first case pay the persons who had lent the money; in the second, the profits would pay the persons who held the notes, and extinguish the liability of the corporation. If the operation were unsuccessful, the corporation would equally have to make good the loss out of their general effects, either to the lenders of

the money, or to the holders of the notes. It would, therefore, be a matter of no consequence whatever to the corporation which way they adopted to accomplish the work; but it would be a matter of importance to the town at large, because, if they borrowed real capital to do it, that would by so much diminish the fund of moving power applicable to other species of industry, and raise its price. It is clear, therefore, that the second method would be so much clear addition to the capital of the community, and would therefore be most advantageous for them.

This second method of utilizing credit, from not being based upon *real* capital, is an instance of what is usually called *fictitious* capital, a name of extreme inaccuracy, which too many persons are in the habit of using, from the hasty assumption that what is not real must necessarily be fictitious, and are more led away by a jingling antithesis of words than an accurate perception of ideas. If the bonds issued by the corporation were not redeemable, and represented nothing, the epithet *fictitious* would be accurate. But such is far from being the case. In both cases it resolves itself into the present value of a deferred payment. In the first instance, the obligation incurred by the corporation to the lenders of the money would not be limited to the specific capital they advanced, but would be a general charge on the whole property of the corporation. The bonds issued in the second case would be precisely the same; they would confer upon the holders of them a general charge upon all the property of the corporation. The security to the holders of the corporation's obligations would be absolutely identical in either case. If the corporation spend the money, it is absolutely gone away from them for ever, and is no more a security to the holders of their notes than if it had never existed. In either case, then, it is the permanent property of the corporation which is the real security of the holders of its notes; and they have the same general charge over it in both cases. It is, therefore, to the last degree inaccurate and untrue to distinguish one case by the term real capital, and to brand the other as fictitious. There is absolutely no distinction at all between the two cases, as far as regards the corporation and the holders of its obligations; the profits and the losses are identical in their effects in either case. The true difference is to the community at large, and the general fund of capital available for its use, and its only effect is to make capital somewhat cheaper than it would otherwise be; and a judicious and successful employment of it eminently conduces to the national prosperity.

The only advantage of the second method is that it makes capital more abundant, and sometimes might provide it when not otherwise obtainable. If it were scarce, or otherwise occupied, it might not always be possible to obtain it. If nobody had money to lend, the second method might supply the want, and

so long as it is practised by judicious persons, and used in promoting successful operations, it is a great blessing. But it is just on this very point that it is liable to the most dangerous abuse. If the corporation were limited to the use of real capital advanced by some independent person, he would probably take into consideration the purpose to which it was to be applied, as well as the solvency of the corporation, and if he thought it injudicious, he would probably not advance it. There would, therefore, be so far a check upon them; but if they were totally destitute of control, and could embark in any operation, by simply writing a few "promises to pay" upon bits of paper, they may be led away into wild and dangerous speculations, deceived by false expectations of profit, and involve themselves and all who trust them in ruinous losses. Because, though these promises to pay did not represent real advances, and are therefore inaccurately called fictitious capital, if they get into circulation, and people give value for them in commodities or services, a disastrous operation based upon them is just as much loss of capital as if they had been real advances.

We have thus shewn that in the production of commodities, which term must be held to include both the formation and the transfer of commodities, credit performs exactly the same functions as money; so far, therefore, as production goes, credit is in all respects equivalent to money. And so long as the operations are successful, everything goes well: money being, as we have laid down, the representative of the fruits of a man's past industry, and credit a pledge of his future industry. It is certain that "credit" exceeds "money" many times in this country, for whereas it is not supposed that the actual money exceeds £60,000,000, the credit in bills of exchange, and which is only one form of it, exceeds £400,000,000; that is, the people of this country have always pledged their future industry to the extent of four hundred millions. And this £400,000,000 is equally capital, it is equally a real value as the £60,000,000. No doubt it is of a different description; it is more perilous; a portion of it may perish. But it is an undeniable fact that it has performed the same functions, so far as regards production, as money. It is a distinct and separate value over and above commodities, totally different from bills of lading, which merely represent particular commodities. Bills of exchange are not a lien upon property, but upon industry, and any property a man possesses is only a kind of collateral security to make good his engagements in case his industry is unsuccessful.

In the case we examined of a bank discounting the bill of the manufacturer A, upon the dealer B, the transaction was already effected upon which it was founded. A had rendered the service to B for which he was to be paid at a future day, *before* he drew the bill upon him, and originally all bills of exchange represented

previously existing debts, and they bore on the face of them the words "for value received" to testify the fact. Consequently, when A discounts the bill, founded upon that transaction, with the bank, it must be carefully observed that he is *simply* selling a debt which is his existing property. And so long as Bills of Exchange are restricted to representing past transactions, their negotiation is not borrowing money, as is commonly understood. But the sharpness of traders discovered that they might be applied to future transactions.

In the case of a *past* transaction, the bill was given by B, who had got the goods, to A, who had given them, and A had got the money that would be payable to him at the maturity of the bill, advanced to him by the bank on the credit of B's reputation, as well as his own. If B, however, be a person of wealth and reputation, he may lend the use of his name to A without any real transaction having taken place between them. Thus, he may accept a bill of A's, and A, on the strength of his name, goes to his banker, and gets the money, with which he performs some operation, such as manufacturing goods, and, having done so, he may sell them to C, and take C's bill in payment of them, which latter is a real transaction. Now the whole of this operation is based upon the credit of B's name, it is not based upon anything real, or upon any service previously rendered; consequently it is in itself a completely new transaction. Such a bill between A and B is called an ACCOMMODATION BILL. This name is, however, not confined to cases where the acceptor lends his name for the accommodation of the drawer, though that is the most usual form, but wherever an acceptor, drawer, or endorser puts his name upon the bill, and therefore renders himself liable to a holder for value to discharge it, without, as the legal expression is, consideration moving to him, it is an accommodation bill, and the party for whose accommodation it is negotiated is bound by law to provide funds to discharge it at maturity, and also to indemnify the accommodation acceptor, drawer, or indorser, as the case may be, against the consequences of non-payment.

The practical effect of this transaction is simply that B stands security to the bank for the money advanced to A; and there is nothing in the nature of such a transaction worse than for one man to stand security for another in any other commercial transaction. In some respects it is much fairer to the person who runs the risk as security, because, in the ordinary course, when one person becomes security for another, he does not receive any pecuniary recompense for the risk he runs, to which he was certainly most fairly entitled; whereas, if it be done by way of accommodation bill, he generally receives some *quid pro quo*, and when a bank performs an operation of exactly the same nature, it always receives a high interest for the risk it runs.

and, when judiciously done, is a very profitable source of income. From the extravagant abuse, however, of such methods of raising capital, accommodation bills have acquired a most discreditable reputation, and there is nothing which requires more vigilance in a bank than to guard against being intrapped into making unwary purchases of such securities.

A great deal has been said and written about the difference between real and accommodation bills, and while no terms of admiration are too strong for the first, no terms of vituperation are too severe for the latter. Thus, Mr. Bell says: "The difference between a genuine commercial bill and an accommodation one, is something similar to the difference between a genuine coin and a counterfeit," as if the act of negotiating an accommodation bill were in itself one of moral turpitude. It is also generally assumed that real bills possess some sort of additional security, because it is supposed that there is property to represent them. We have already seen, however, the entire delusion of such an idea, and that it is a great mistake to suppose that commercial bills have any specific relation to the property from the transfer of which they originally sprung. In truth, both real and accommodation bills have precisely the same security—they constitute a general charge upon the whole estates of all the obligants upon them. The objections to accommodation bills, therefore, on that ground are perfectly futile.

The essential distinction between real and accommodation bills is, that one represents a *past* and the other a *future* transaction. But even this is no ground for any preference of one over the other. A transaction that *has been* done may be just as wild, foolish, and absurd as the one that *has to be* done. The intention of engaging in any mercantile transaction is, that the result of it should repay all the outlay, with profit. There is no other test but this of its propriety, in a mercantile sense. Such things have been heard of in the mercantile world, as consignments of skates to tropical countries. Now, a bill drawn against such a shipment as this would pass muster, in technical language, as a *real* bill, while one drawn to forward some other operation, however sound and judicious it might be, if it were not yet accomplished, would be an accommodation bill, and be branded as fictitious. Mr. Bell would call the former genuine coin, the latter counterfeit.

We see, therefore, that the common objections urged against accommodation bills are perfectly futile, and quite wide of the mark. Whether a bill be a good and safe bill, has no reference to whether it represents a past or future transaction, but whether it is a safe and judicious one itself, and the parties to it respectable and of sufficient means to meet their liabilities. The whole cash credit system of Scotland, which has conducted so eminently to the prosperity of that country, is a system of accommodation

paper, which is sufficient to disprove, in the mind of any dispassionate person, that the system is in itself necessarily dangerous and pernicious, but is proof enough that, if it is judiciously managed, it may be of great advantage.

The true objection to accommodation paper is of a different nature. When the credit system is carried on duly and properly, and within legitimate limits, it is the most ingenious method ever devised for promoting commerce, and where it has been cautiously used, has marvellously succeeded in so doing. But it is a very trite remark, that the best things when corrupted become the worst. This is eminently true of paper credit. Universal experience proves that there is nothing so dangerous and pernicious as for individuals to have an undue facility for obtaining credit. When capital is to be had on too easy terms, it fosters, to an extravagant extent, the fatal propensity for embarking in all sorts of wild speculations, and pushing trade far beyond the possibility of being remunerative.

The considerations we presented shewed the exaggerated ideas of the security of real bills. But there is at least this security in real bills, that as they only arise out of real transfers of property, their number must be limited, in the very nature of things. However bad or worthless they may be individually, they cannot be multiplied beyond a certain extent. There is, therefore, a limit to the calamities they cause. But with accommodation paper there is no limit. A beggar may write upon bits of paper a million of "promises to pay" as easily as a Rothschild; and it is far more probable that he will do so; a man without a farthing is proverbially the most reckless, because when the bubble bursts, it is a matter of no consequence to him, he has nothing to lose, the misery and the ruin fall upon his unfortunate dupes. A man of real capital will be cautious in his operations. A loss to him will be real, but a man who is not worth a sixpence is indifferent whether he loses a £1,000 or a £1,000,000,

This system of accommodation paper of different descriptions, is one of immense importance in modern commerce, and its abuse has led to some of the most terrible mercantile catastrophes on record. It is, however, so intimately interwoven with banking, that we shall defer any more mention of it till the next section, which treats of the operations of Banking.

We have observed that so far as regards production, which, in a scientific sense, includes the formation and transfer of products, credit, whenever it is applied, performs exactly the same function as money. As in this section we wish to avoid all controversy, and merely to state facts, we will only say that all commercial transactions on credit are SALES. The absolute property of the article passes from the vendor to the purchaser, just exactly as if the price had been paid in money. The only

difference to the purchaser is, that his profits are less, because the credit price is higher than the money price. So long as matters proceed smoothly, and transactions are profitable, the bills generated by commerce are equivalent to so much money. The difference arises when the sales are unprofitable, and losses ensue. If the wholesale dealer buys from the manufacturer for ready money, and the speculation is unfortunate, the whole loss falls upon the dealer, the manufacturer does not lose, he has got his money. But if the speculation is unfortunate, and a loss ensues, or if the wholesale dealer fails from other reasons, the loss may fall upon him. When he has sold on credit to the dealer, his power over the goods is absolutely gone; and if the bill is unpaid he cannot reclaim the goods, even if they are still in the possession of the purchaser, he has no more claim to them than any other creditor. Consequently, if the dealer has not sufficient funds to pay his debts, the loss falls upon the original manufacturer. In this, then, consists the whole difference between sales on credit and sales for money, that if losses ensue they may be differently distributed. No doubt the manufacturer finds that a bill of exchange is not so negotiable as a bank note or money, but it is of the same nature, and must be placed in the same category. The money is nothing but a bill on the whole community. Good bills of exchange do, to a certain extent, circulate in commerce like money; but the manufacturer generally finds it more convenient to sell the bill to his banker, and how the banker buys it will be explained in the next section.

Now, we have shewn, in the first chapter of this work, that capital, in its most general sense, is not any particular thing, but a particular method of employing an economic quantity, be it currency or anything else, in reproductive operations. In its general sense, it is the purchasing power of the merchant, or it is the moving power at his command to generate a circulation of commodities, out of which he reaps his profits; it is the power which draws the goods out of the possession of the manufacturer into the possession of the dealer, for him to make a profit. The money he has is the fruit of the services he has formerly done to the community. Credit is also the power he has of drawing the goods from the possession of the manufacturer, and is the pledge of his skill in rendering future services to the community, by discerning their wants and supplying them. The effect upon the markets and upon the prices is exactly the same, whether purchases, *i. e.*, circulation of commodities, be generated by credit or real capital, and the profits and losses are exactly the same to the community, whether the operation be effected by credit, or by real capital. Hence, we arrive at this conclusion, that **MERCANTILE CREDIT IS MERCANTILE CAPITAL.**

It has frequently been observed that all great inventions have an equalizing tendency; the invention of gunpowder equalized

the condition of the poorest foot soldier and the wealthiest knight, and it destroyed the supremacy of the knights; the invention of printing opened up the paths of knowledge to the poorest as well as to the rich, and destroyed the supremacy of wealth in the acquisition of science; the invention of steam and railroads has equalized the means of locomotion to the humble and the wealthy; so the invention of credit has destroyed the supremacy of capital or money, and has provided the means for the most humble to place his foot on the first step of the ladder of opulence. It is a matter of common observation that nothing is so difficult as the first step to wealth; that many men could get on if they had only a beginning. Now, credit supplies the means of attaining that first step to all. Credit is a mighty power, and no doubt like other great engines, is liable to be abused; but it is entitled to take rank with gunpowder, printing, and steam, among the marvels of human ingenuity, and which has been the chief cause of the magnitude of modern commerce.

SECTION IV.

THE THEORY OF BANKING.

ERRONEOUS NOTIONS PREVALENT ON THE NATURE OF BANKING—
DEFINITION OF A BANKER—ON THE MEANING OF THE
WORD BANK—THE CURRENCY PRINCIPLE—EXPOSITION
OF THE MECHANISM OF BANKING—CASH CREDITS—ACCOM-
MODATION BILLS—ON THE TRANSFORMATION OF TEMPORARY
CREDIT INTO PERMANENT CAPITAL—ON THE EXTINCTION
OF CREDIT—ON THE LIMITS OF CREDIT.

14. In the preceding section we have explained how Bills of Exchange came to be used in commerce. But for many ages there is no evidence to shew that these debts were saleable property. In the archives of Venice there are many Bills of Exchange of the 15th century, drawn by Venetian merchants on their correspondents in London, and sent back protested for non-payment, but in none of these are there any words of negotiability. It is a matter of some obscurity to determine to whom this most important invention is due. Many writers say that Cardinal Richelieu made bills of exchange negotiable. But this can hardly be quite correct, as in a bill dated in 1589 the bill is made payable to Thomas Mun, *or his assigns*. It is remarkable, however, that Gerard Malynes, writing in 1622, says:—"Neither can you make a Bill of Exchange payable to the bearer, or bringer thereof (as you make your bills obligatory beyond the seas), to avoid the inconvenience which might happen in derogation of the nobleness of the said Bill of Exchange, which every merchant is to maintain." How it could derogate from the nobleness of a Bill of Exchange to make it negotiable is somewhat hard to understand. And Bills very soon had to submit to this derogation from their nobility, for, in the forms of Bills given by Marius in 1654, the words "or assigns" and "or order" are introduced into the bill, and, as this was exactly the period when "banking" was introduced into England, it may, perhaps, be that this custom was enforced by the bankers to make the debts payable to them by express order.

However this may be, these Bills would not be very generally current in trade, because many would hesitate to take them without being well informed of the capacity of the parties liable on them. A new class of traders sprung up whose business it was to purchase these debts, and these were BANKERS.

The business of a merchant is to deal in commodities, the business of a banker is to deal in currency. A merchant buys and sells commodities, a banker borrows, and buys, and sells

currency—two species of business which are essentially distinct from one another, and which can seldom be undertaken on a large scale by the same person or company, and the attempt to do so has in many cases led to the most disastrous results.

*Erroneous notions prevalent as to the nature of Banking—
Definition of a Banker.*

15. The popular notion is that the word Bank is derived from the Italian word *banco*, a bench or table, because the early Italian money dealers, or money changers, displayed their specie on a bench or table. And it is said that the business of a banker is to borrow from one set of people to lend to others; or that a banker is an intermediary between those who want to lend and those who want to borrow.

Nevertheless, both these notions are utterly erroneous, and it is of the greatest importance towards understanding the subject to point out their error.

In the first place, the word "Bank" is not derived from the Italian word *banco*; on the contrary, the Italian word *banco* is derived from the old Scandinavian, or Teutonic, word *Banck*. In the next place it is an entire misconception of the nature of banking to say that a banker is merely an intermediary between those who want to lend and those who want to borrow.

In former times there were many persons who acted in that capacity, and they were called *money scriveners*. But nobody ever thought of calling a money scrivener a banker.

At the present day, a firm of Attorneys, or Solicitors, in large practice, may have some clients who wish to lend money on mortgage, and at the same time may have other clients who wish to borrow money on mortgage. The first set may entrust their money to the firm to lend to the second set. Thus the firm would act as intermediaries between those who want to lend and those who want to borrow. But no one would call them "bankers" because they did this. They would merely act as Trustees of the money. They do not acquire any property in the money, so as to be able to appropriate it to their own purposes. On the contrary, it is only entrusted to their custody for the express purpose of being applied in a certain way. The actual property in the money passes direct from the lender to the borrower, through the medium of the trustees, and if these latter appropriated it to their own purposes they would be liable to be punished for embezzlement.

Neither are persons who lend out their own money bankers. Those who have cash at command may invest it in the purchase of commercial bills, or in any other way. There are many who trade in this way, but they are called *Bill Discounters*, not Bankers.

The essential feature of a "Banker" is this, that when his

customers place money with him, it becomes his absolute property, to deal with as he pleases, and he is in no way accountable to them for the purpose he applies the money to. The customers of a banker cede to him absolutely the property in their money, and receive, in exchange for it, only a right to demand an equal sum at a future time.

Thus a "Banker" buys money with his *Credit*; and, moreover, when he buys commercial debts, he always does it by his credit also, and not by cash. And this is the essential distinction between a Bill Discounter and a Banker, that the former buys bills with cash, and the latter with his own credit. Hence, when a Bill Discounter has invested all the cash in his possession, either his own or what others have placed with him, in this way, he is at the end of his resources. But a *Banker* always buys commercial debts with his own credit, or with his "promise to pay," and experience shows that his credit may exceed several times the cash in his possession. Authorities differ as to how many times the quantity of his credit may safely exceed the quantity of his cash, and it may differ in different localities, and methods of doing business; but, at all events, it may do so *several* times. Thus, the business of banking is essentially to CREATE CREDIT. This credit, of course, is made payable in money, but in practice it is very rarely actually paid in money. We have shown above that *a mutual release of debts is absolutely equivalent to a reciprocal payment of debts*; and, by the great modern banking system, the enormously greater proportion of banking credit is extinguished by mutual releases of debts.

The following is the true definition of a "Banker":—

A BANKER is a trader who buys money, or money and debts, by creating other debts.

A banker may, it is true, add other species of money dealing to his business; but the above is the essential definition of "Banking." The first business of a banker is not to *lend* money to others, but to *collect* money *from* others.

On the meaning of the word BANK.

16. We shall find that it will greatly conduce to a clear understanding of the subject to ascertain the true meaning of the word BANK and BANKER.

As we have said above, it is popularly supposed that the word Bank comes from the Italian *banco*, a bench, or table, because the money dealers, or money changers, kept their money piled on benches or tables, whence they were called *banchieri*. It is also said that when they failed their bench was broken up (*banco rotto*), hence our bankrupt.

Nevertheless, there can be no possible doubt but that this derivation is a pure delusion. In the first place the money dealers, or money changers, as such, were never called *banchieri*

in the middle ages. They were called *Cambiatores*, *Speciarii*, *Campsores*, *Argentarii*, *Nummularii*, *Trapezito*, and those who lent money were also called *Danista*, *Collybista*, and *Mutatores*, but not *banchieri*, and their places of business were called *casane*, and not *banchi*.

We shall shew what the real meaning of "Bank" is, not only in Italian, but as it was understood in English when it was first used, as applied to money dealing.

Muratori himself says, that the Italian *banca*, or *banco*, is derived from the Gothic or Scandinavian *Banck*, a heap or mound. The true original meaning of Banco is a heap, or mound, and this word was metaphorically applied to a common fund, or joint-stock, formed by the contributions of a multitude of persons.

As is explained in a subsequent chapter, the State of Venice being hard pressed in war in 1171, levied a forced loan from its citizens, and promised them interest in perpetuity at 4 per cent.; and this loan, or public debt, was called a Banco, or MONTE. Certain commissioners were appointed to manage the loan, who were called the *Camera degli Imprestiti*, or Chamber of Loans, and their office, where the interest was paid and the stock was transferred, was also called Banco, or Monte. The "Bank" of Venice was, therefore, nothing but a public debt, managed by commissioners. Two subsequent loans were made, called *Monte Nuovo*, and *Monte Nuovissimo*, of the same nature, and it was not till 1587, that these commissioners were appointed to receive public cash on deposit, and became what we call a Bank. There is no doubt whatever that the words *Monte* and *Banco* are equivalent in Italian, and were first applied to a public debt, and then afterwards to the office in which it was managed.

Thus, a recent eminent Italian writer, Cibrario, says (*Della Economica Politica del medio evo*, p. 530): "Circa alla teoria del credito, che dissì invenzione di comuni Italiani, è noto che il primo BANCO, o debito pubblico, fu eretto a Venezia nel 1171. Nel secolo XIII v'ha memoria di carta monetata in Milano. Il credito fu rimborsato. Un MONTE, o debito pubblico, fu stabilito in Firenze nel 1336. * * * * *

"A Genova, durante le guerre del secolo XIV, fu stabilito il banco di St. Giorgio, composto di ereditori dello stato."

"Regarding the theory of credit, which I have said was invented by the Italian cities, it is known that the first BANK, or public debt, was erected at Venice in 1171. In the 13th century paper money is mentioned at Milan. The credit was paid off. A MONTE, or public debt, was established in Florence in 1336. * * * * *

"At Genoa, during the wars of the 14th century, the Bank of St. George was established, composed of the creditors of the state."

Now, was the public debt of Venice a *bench*, or were the State creditors of Genoa a *bench*?

Thus, also, Benbrigge, a writer in 1646, further quoted below, speaks of the "three BANKES at Venice," meaning the three public loans, or *Monti*, mentioned above.

We have said enough, we think, to shew that *banco*, in Italian, means a fund formed by several contributions; we shall now shew that such was its meaning when first used in English, as applied to money dealings.

Thus, Bacon says, "Let it be no *bank*, or common stock, but every man be master of his own money."

So Benbrigge, a writer in 1646, in his *Usura Accommodata, or a ready way to rectify usury*, says, "for their rescue may be collected *MONS Pietates sive Charitatis*, a *BANKE of Piety or Charity*, as they of Trent fitly call it." Again, "For borrowers in trade for their supply, as their occasion shall require, may be erected *MONS Negotiationis*, or *BANKE of Trade*." He also quotes from Tolet, another writer, who speaks of two kinds of banks, namely, "*MONS fidei*, or *BANKE of Trust*, which Clement XII. instituted at Rome—he that put his money into this *Banke* was never to take it out again"—for which the investor received 7 per cent. interest, like the original Bank of England stock. He also speaks of *MONS Recuperationis*, or *BANKE of Recovery*, of which the interest was 12 per cent. The difference between these two was, that between perpetual and terminable annuities, where the higher interest of the latter is, in fact, repayment of the capital by instalments.

In the time of the Protector, some proposals were made for erecting public banks. Samuel Lambe, a London merchant in 1658, recommending these, says:—"A bank is a certain number of sufficient men of estates and credit *joined together in JOINT STOCK*, being, as it were, the general cash-keepers, or treasurers, of that place where they are settled, letting out *imaginary money* at interest at £2½ or £3 per cent. to tradesmen, or others that agree with them for the same, and making payment thereof by assignation, and passing each man's account from one to another, with much facility and ease."

So also, in a little tract, entitled "*A Discourse concerning Banks*," 1697, and known to be by a Director of the Bank of England, it says, there are three kinds of Banks, the first for the mere deposit of money, the second for profit. "The banks of the second kind, called in Italy *Monti*, which are for the benefit of the income only, are the banks of Rome, Bologna, and Milan. These Banks were made up of a number of persons, who, in time of war, or other exigencies of state, advanced sums of money upon funds granted *in perpetuum*, but redeemable." "The third kind of banks, which are both for the convenience of the public, and the advantage of the undertakers, are the several banks of

Naples, the Bank of St. George, at Genoa, and one of the banks of Bologna. These banks, having advanced sums of money at their establishment, did not only agree for a fund of perpetual interest, but were allowed the privilege of keeping cash." The Bank of England was of this last sort.

So also Blackstone says:—"At Florence, in 1344, Government owed £60,000, and, being unable to pay it, formed the principal into an aggregate sum, called metaphorically a *Mount*, or *Bank*."

Banks in this country have almost always received deposits in cash, but there was one formed soon after the Bank of England, called the "Million Bank," which was merely an association of persons who advanced a million to Government, who never kept cash. This company, which resembled the original Bank of Venice, existed till nearly the end of the last century.

It was some time in the 12th or 13th century that the Florentine merchants, and probably there may have been many of the *Cambitores* among them, began to receive deposits from the general public, and then they were called *Banchieri*, and their houses called *Banchi*, because they received deposits, in exchange for which they gave their own credit.

We have now, we think, offered ample evidence to prove that the word "Bank" means a general contribution received from the public, in exchange for which credit is created, and that the business of a "Banker" is to create credit.

On the Currency Principle.

17. The express function of a Bank being to create credit, a doctrine of considerable importance has been maintained by several writers of influence in recent times, to which we must now advert, as most discussions on banking for several years have been full of it.

We have shown, in a subsequent chapter, that the Chinese were the inventors of paper money, and that when the Government had brought the country to a state of the deepest distress by their extravagant issues of paper money, a writer sighed for the days when no paper was issued except in exchange for specie,—“Then,” says he, “it was ordered that at the offices of the rich merchants who managed the enterprise, when the notes were paid in the money came out, when the bills came out the money went in. The money was the mother, the note was the son. The son and the mother were reciprocally exchanged for each other.”

This doctrine, put forth in the year 1309 by a Chinese writer, is the CURRENCY PRINCIPLE. It is this—that when a Bank is permitted to issue Notes, the Notes ought to be exactly equal to the specie paid in, and that the sole duty of the Bank in such a case is to exchange specie for paper, and paper for specie; and that the quantity of paper in circulation should always fluctuate

in quantity, exactly as specie would do if there were no paper. Those writers in recent times who maintain this doctrine aver that any paper issued in excess of this principle causes a depreciation of the currency. The next enunciation of it that we are aware of is in John Law's *Money and Trade Considered*, p. 73, edit. 1755, where he says:—"Some are against all banks where the money does not lie pledged equal to the credit."

It was upon this principle that the Banks of Venice, Amsterdam, and Hamburg were constructed. These places were the centres of a great foreign commerce, and, as a natural consequence, an immense quantity of coin of all sorts, of different countries and denominations, was brought by the foreigners who resorted to them. These coins, were, moreover, greatly clipped, worn, and diminished. This degraded state of the current coin produced intolerable inconvenience, disorder, and confusion among merchants, who, when they had to make or receive payment of their bills, had to offer or receive a bagful of all sorts of different coins. The settlement of these bills, therefore, involved perpetual disputes,—which coins were to be received, and which were not, and how much each was to count for. In order to remedy this, it became absolutely necessary that some fixed uniform standard of payment should be devised, to insure regularity and a just discharge of debts. In order to do this, the magistrates of these cities instituted a Bank of Deposit, in which every merchant placed all his coins of different weights and nations. These were all weighed, and the bank gave him credit, either in the form of notes, or an entry in their books, exactly corresponding to the real amount of the bullion deposited. The owner of this credit was entitled to have a certain quantity of coin of full weight on demand. These credits, therefore, always insured a uniform standard of payment; and it was enacted that all bills upon the respective cities, above a certain amount, should be paid in these credits, which were called bank money. The consequence was evident: as this bank money was always exchangeable for money of full weight on demand, it was always at a premium, or *agio*, as compared with the current money. The difference was usually from 5 to 9 per cent. in the different cities. The expression, *agio*, or premium, is likely to mislead, because it is evident that it was the bank money that was the true standard, and the current money that was at a discount. These banks professed to keep all this coin and bullion in their vaults. They made no use of them in the way of business, as by way of discounting bills. Thus the credit created was exactly equal to the specie deposited, and their sole business was to exchange specie for paper, and paper for specie.

They were examples of the CURRENCY PRINCIPLE, and they are the models to which many persons would wish to see all banks reduced, and we shall see that they maintain that paper

should fluctuate in quantity exactly as a metallic currency would do if there were no paper; and that if paper is substituted for specie, it can only maintain an equality of value with specie by being exactly equal in quantity to what the specie would have been if there were no paper.

These Banks were of no further use to commerce than that they served as a safe place to keep money, and they insured a uniform standard of payment. They made no profits by their business, but those who kept their accounts paid certain fees to maintain the establishment.

We shall not here discuss the soundness of this currency principle, our only object is to state to our readers clearly what it is. Many writers of the greatest influence, such as Colonel Torrens, Lord Overstone, and others, maintain that this principle ought to be applied to all Banks, and that they should not be permitted to create any notes in excess of their bullion.

Mr. Mill says:—"Further consideration shewed that the uses of money are in no respect promoted by increasing the quantity which exists and circulates in a country, the service which it performs being as well rendered by a small as by a large aggregate amount." The slightest experience will show that this dogma is utterly unfounded. Does it never happen that an increased supply of money can benefit a country? One of the acknowledged wants of Ireland at the present day is want of capital; every one admits that the introduction of fresh capital would be of the greatest service to Ireland.

In B. iii., c. 13, § 5, he says:—"Another of the fallacies from which the advocates of an inconvertible currency derive support, is the notion that an increase of the currency quickens industry. This idea was set afloat by Hume, in his Essay on Money, and has had many devoted adherents since." Not only is the doctrine which Mr. Mill here derides indubitably true, though it is not an argument in favour of an inconvertible paper money, but it had many devoted adherents long before Hume was born, as every one acquainted with Economical literature knows well enough.

He then says:—"The substitution of paper for metallic currency is a national gain, ANY FURTHER INCREASE OF PAPER BEYOND THIS IS BUT A FORM OF ROBBERY."

"An issue of notes is a manifest gain to the issuers, who, until the notes are returned for payment, obtain the use of them as if they were real capital; and so long as the notes are no permanent addition to the currency, but merely supersede gold or silver to the same amount, the gain of the issuer is a loss to no one; it is obtained by saving the community the expense of the more costly material. But if there is no gold or silver to be superseded—if the notes are added to the currency, instead of being substituted for the metallic part of it—all holders of cur-

rency lose by the depreciation of its value, the exact equivalent of what the issuer gains."

Again in B. iii., c. 22, § 3, he says:—"When metallic money had been entirely superseded and expelled from circulation, by the substitution of an equal amount of bank notes, any attempt to keep a still further quantity of paper in circulation must, if the notes are convertible, be a complete failure. The new issue would again set in motion the same train of consequences by which the gold coin had already been expelled. The metals would, as before, be required for exportation, and would be for that purpose demanded from the banks to the full extent of the superfluous notes, which thus could not possibly be retained in circulation."

We desire to call particular attention to these dogmatic assertions of Mr. Mill, and especially to the fact that he brands as robbery any creation of notes beyond the quantity substituted for specie. We shall now give an actual exposition of the practice of banking, and, perhaps, Mr. Mill may be surprised to find what he brands as robbery, and whom he brands as robbers.

On the Mechanism of Banking.

18. Banks of the nature of those of Venice, Amsterdam, and Hamburg, never existed in England, and we must now explain the mechanism of banking, as it has been carried on in this country.

During the civil war, the goldsmiths of London began to receive cash of the merchants and country gentlemen, in exchange for which they gave their promissory notes payable to bearer on demand. In consequence of this they were called "bankers," and their notes were called "goldsmiths' notes," or "bankers' notes." But the goldsmiths did not charge anything to their customers for keeping their cash; on the contrary, they agreed to pay six per cent. interest for the cash left with them. In order to pay this interest, they were obliged to trade with this money, and it is in regard to the method of this trading that so much misconception exists.

Let us, for the present, leave out of consideration any private property the goldsmiths might have, and let us deal with small figures. Suppose the banker had £10,000 deposited with him by his customers, then, as he created an equal amount of debt against himself in exchange for this money, his accounts would stand thus:—

LIABILITIES.	|	ASSETS.
£10,000.		£10,000.

We shall now see the extreme importance of accurately stating Economic questions.

According to the method of stating this, given by Euler, the banker possesses £10,000, and owes £10,000. Euler, as well as

all mathematicians, calls the money a *positive* quantity and the debt a *negative* quantity, because, if the banker's fortune were estimated, his debts would have to be subtracted from his money. In this case, the money and the debts are equal, and, therefore, according to this mode of statement, the banker would be no richer than before.

Now, so far as the banker himself only is concerned, this view is sufficiently accurate. But it is easily seen that so far as regards Economic Science it is quite inaccurate. For the banker has issued £10,000 in notes, and these circulate among the public and perform all the functions of money, until payment of them is demanded, and then, of course, they cease to exist. But the banker has the £10,000 in cash, which has become his property, and, reserving a certain portion of it to meet the usual demand for payment of his notes, he may trade with the remainder, and it is quite clear that, supposing the £10,000 of his notes to be in circulation, whatever portion of cash he also issues is by so much an addition to the previously existing currency.

Now experience would soon shew him that, if some of his customers drew out their money from day to day, others would probably pay in about an equal sum, so that, at the end of the day, there would probably be not very much difference. From practical observation, we may state that, in ordinary times, a banker's balance in cash will seldom differ by more than a 36th part from day to day. So that, if he retains a tenth part in cash to meet demands for payment of his notes, that is ample and sufficient in all ordinary times.

The goldsmiths, then, soon found that they had a large quantity of bullion on their hands, which was so much dead stock, and they were able to trade with it in order to make profits to pay the interest of the whole. The method of trading they adopted was to discount, or buy, commercial debts, in the form of Bills of Exchange. These bills being payable in two or three months, their money soon came back to them with a profit.

It is commonly supposed that they advanced *money* on these bills. If they had done that, they could not have brought more than £9,000, as they kept one-tenth in their tills in cash. This, however, is an error. They did not buy the bills with cash, but with their own *promissory notes*, or their *credit*. And, as above stated, they soon found that their credit might safely exceed their cash several times. Hence they found that they could extend their credit safely very far beyond the limit of £9,000. They found that keeping the £9,000 in their coffers, they could safely buy at least £40,000 in bills with their own notes. Now, supposing the rate of discount was 8 per cent., and the bills were at three months, the discount on this sum would be £800,

and, consequently, in exchange for bills to the amount of £40,000, he would issue £39,200 in his own notes, and his accounts would then stand thus:—

LIABILITIES.		ASSETS.	
£49,200		By Cash	£10,000
—		By Bills of Exchange. . .	£40,000
£49,200			—
			£50,000

Now, by this process, the Banker added £39,200 to the previously existing currency, and his profit is clear—he pays six per cent. on £10,000, and he gains eight per cent. on £39,200.

Now, this was the business of banking, and hence the correctness of the definition given above is manifest—a *banker is a trader who buys money and debts (bills of exchange), by creating other debts (his own notes)*.

Thus we see that the distinctive function of a bank, and a banker, was to issue notes, payable to bearer on demand, which were to circulate as money. *That is to create paper currency*, in some cases only equal to the amount of bullion they displaced, in others, greatly exceeding it. And the meaning of the word “to bank” was to buy money and bills of exchange with such notes, that is, to create instruments of credit. Towards the end of the 17th century contemporary writers tell us that some of the London bankers had upwards of a million of notes in circulation.

We further see that as the banker had given an equal amount of notes for the cash he received, for which he paid interest, his only method of making profits was by augmenting the amount of previously existing currency—that is, according to Mr. Mill, he was a *robber!*

The relation in which the banker and the merchant stand to each other, after the banker has discounted the bill for the merchant by issuing his notes, also shews how indispensably necessary an exact method of statement is required to appreciate the subject of credit correctly. Some writers, who deny that credit is capital, say this—that if a person holds a bill of exchange, that is his property, and to be added to his other property, but that it is to be *subtracted* from the property of some one else, therefore, upon the whole, it is nothing.

Thus, Mr. Thornton says:—“Paper constitutes, it is true, an article on the credit side of the books of some men, but it forms an exactly equal item on the debit side of the books of others. It constitutes, therefore, on the whole, neither a debit nor a credit. The banker who issues £20,000 in notes, and lends, in consequence, £20,000 to the merchant, on the security of bills accepted by them, states himself in his books, to be the debtor of the various holders of his notes to the extent of the sum in question; and states himself to be the creditor of the acceptors

of the bills in his possession to the same amount. His valuation, therefore, of his own property, is the same as if neither the bills nor the bank notes had any existence. Again, the merchants, in making their estimate of property, deduct the bills payable by themselves, which are in the drawer of the banker, and add to their estimate the notes of the banker, which are in their own drawer; so that the valuation likewise of the capital of the merchants is the same as if the paper had no existence. The use of paper does not, therefore, introduce any principal of delusion into that estimate of property which is made by individuals."

Now, in the above extract, Mr. Thornton has begun by making a most extraordinary error for a banker. He supposes that the banker issues an amount of notes *equal* to the bills he discounts. That would be as much as saying that the banker charged no discount. But this is manifestly wrong. The banker retains the discount at the time of the advance, and, consequently, his property and his debts are *not* equal, but his property exceeds his debts by the sum charged as discount.

Again, though in a certain way, as regards the individuals themselves, this way of stating it has some plausibility, it is clearly quite incorrect as a scientific statement. The merchant acquires the Bill of Exchange as property given in exchange for some goods. He sells that property to his banker in exchange for the property created by his banker, viz., his notes. Now, it is clear that the banker may put this bill into circulation, and it may perform the same functions as money until the time for its payment comes, and also the merchant may buy with the banker's notes as money, and, consequently, the bill and the notes are each of them exchangeable quantities, and may both be in circulation at the same time, and perform many exchanges before they are paid and extinguished. Hence each of them forms a part of the mighty mass of circulating credit.

Such, then, was the business of banking. We need not here speak of the foundation of the Bank of England in 1694, but it is quite clear that the Legislature understood "banking" to mean issuing notes payable to bearer on demand. In 1708 an attempt was made by some other companies to do banking business; and in 1709, on the renewal of the charter, Parliament meant to confer a monopoly of banking on the Bank of England. In order to do that, there being at that time no legal definition of banking, the Act did not directly prohibit any "bank" with more than six partners being formed, but it described what was well understood to be banking business, and it prohibited any partnership of more than six persons doing that. It forbade them "*to borrow, owe, or take up any sum or sums of money, on their bills or notes, payable at demand.*"

Thus, at this period, banking was understood to mean *borrowing, or owing, money on notes payable on demand, and to*

forbid persons to do that was to prevent them from "banking." This Act was effectual for some time, but, about 1740, some persons tried to evade the words of the Act, and, to put a stop to this, the Act of 1742 is more explicit. It says:—"And to prevent any doubt that may arise concerning the privilege, or power, given by former Acts of Parliament to the said Governor and Company of *exclusive banking*; and also in regard to erecting any other bank, or banks, by Parliament, or restraining other persons from *banking*." It thus forbade, as before, any partnership "to borrow, owe, or take up any sum or sums of money, on their bills or notes, payable at demand." So that the Bank of England might remain a corporation, "with the privilege of *exclusive banking*, as before recited."

Still, we observe that the intention of Parliament was to confer on the Bank of England the exclusive monopoly of Banking. And this privilege of banking consisted in "*borrowing, owing, or taking up any sum, or sums, of money on their bills or notes, payable at demand*." Hence, we see, that "Banking" meant the creation and issuing of "Currency;" and to prohibit persons from creating currency was, in fact, to prohibit them from doing banking business. These words were devised with the utmost care, so as to prevent any other rival, in the most comprehensive manner possible. It was supposed that no legal ingenuity could devise an expedient to evade so extensive a prohibition. The form of words adopted in this Act, was devised in reference to the methods of doing banking business at the time they were framed, and they were successful in preventing any rival bank being formed, so long as bankers adhered to that particular method of doing business. But about 30 years afterwards, bankers adopted a change in the method of doing their business, so simple, and apparently so unimportant, as scarcely to deserve attention. And it was this mere change in the form of doing their business, that is, of creating liabilities, or currency, in a form not provided for by the words of the Act, that cut away the ground from under the Act, and was the means whereby the present Joint Stock Banks in London were founded, and thus destroyed the monopoly of the Bank of England, because, when this mode of evading the Act was discovered, and the Bank, in dismay, applied to Parliament to put a stop to it, they were told that such monopolies were out of fashion, and their demand was refused.

Up till about the year 1772, bankers adhered to the original method of issuing promissory notes, payable to bearer on demand. But about this time, they changed the form of making the purchases of bills. When their customers brought them bills to discount, instead of giving them their promissory notes payable to bearer on demand, they *wrote down the value of the bill to the credit of their customers in their books*. They then

gave them books containing a number of printed forms. These forms were called *cheques*, and were bills of exchange, drawn upon the banker, payable to bearer on demand. But it is usual for the drawer of a cheque to fill in the name of some one to whom it is made first payable. And these cheques may be put into circulation, exactly like bank notes.

These cheques are nothing whatever but bills of exchange upon the banker, payable to bearer on demand. There is, however, one peculiarity about them that must be noticed. In ordinary cases no man can be compelled to accept a bill drawn upon him for a debt, without his own consent, which is signified by his writing his name upon it. But, in the case of cheques, if this rule was enforced, it would have destroyed their utility, and they could never have been substituted for bank notes. A bank note bears on the face of it the obligation of the banker to pay it; but an unaccepted cheque, if it followed the usual law of bills of exchange, would be no obligation to pay without acceptance. Consequently, no man would have been safe in taking a cheque before he knew whether the banker would accept it or not. To obviate this difficulty, and to make a cheque as like a bank note as possible, it was established as a custom among bankers, that the *possession of a customer's funds by a banker is equivalent to acceptance*. Consequently, if a banker has funds of his customer in his hands, he is bound to pay all that customer's cheques, to the amount of the funds in his hands, without notice and without acceptance, to the bearer on demand, exactly as if it was his own promissory note.

Hence, cheques are nothing but a substitute for bank notes. A bank note, in fact, is a double obligation, the one is an obligation to pay the customer, the original creditor, and the second is to pay the bearer, *i. e.*, any one to whom the original creditor may transfer the obligation. Now, the modern practice splits these obligations. The entry in the banker's books is the obligation to pay his customer, the permission to draw a cheque payable to bearer on demand is the obligation to pay any one the customer may transfer the debt to. And the entry in the banker's books, together with the cheque, make up the bank note.

Hence, we see, that although "Banking" originally consisted in issuing notes payable to bearer on demand, yet bankers devised a method of doing the very same thing under another form, and we must change the form of expression accordingly, to meet the altered form of doing business. Nor shall we have the least difficulty in finding an expression, which will include both forms. For though the business of banking consisted in discounting bills with their promissory notes payable to bearer on demand, we may express it thus:—That it consisted in buying debts with "promises to pay," and these "promises to pay"

may be of two forms; 1st. Promissory notes payable to bearer on demand; 2ndly. Figures written down to the credit of the customers, to be drawn against by cheques payable to bearer on demand. Up to the period when cheques were introduced the London bankers had very extensive issues of notes, but the method of doing business by cheques was found to have so many practical advantages over that by way of notes, that London bankers from that period universally discontinued the issue of notes, and adopted cheques: though they never were forbidden to issue notes until the Bank Act of 1844.

The modern system of banking, then, by means of cheques, is exactly the same in principle as the former method of Bank Notes, only it is somewhat varied in form. In each case banking consists in creating liabilities, and the modern name and form of stating these liabilities in banking accounts is a source of an enormous amount of erroneous opinion. In the former mode of stating these accounts, it is open and patent to all the world, that the banker has created liabilities against himself by the discount of bills. In the modern form all these liabilities are stated as so much credit in his books, and are called DEPOSITS, and these *deposits* are formed of the credit created in exchange for cash as well as bills, so that it is made to appear, and is almost universally believed, that what is classed under deposits in the published banking accounts are deposits in actual cash, whereas they are nothing but a creation of credit.

The name itself of *Deposit* is a source of much misconception. It is generally supposed that a "Deposit" in a bank means the thing deposited. But this is quite an error. The Deposit is the credit created in exchange for the thing deposited, and when a banker discounts a bill by creating a credit in his books, that credit is equally a "Deposit" with the credit created in exchange for cash. Hence, in banking language, it must always be remembered that *a Deposit is the credit created in a banker's books; the thing deposited is the Asset, or the Security.*

The only practical difference between bank notes and cheques is this, that the former were, on the face of them, direct obligations of the banker to pay the money stipulated; the latter were not direct obligations of the banker. The consequence is, that when cheques are transferred from hand to hand, it is usual to require the transferor to indorse them, so that if the banker refuses to pay them, the liability of the transferor may be preserved. In bank notes this is not usually done, because, as the holder may demand payment for them on the instant from the bank, few persons expect that the bank will fail before payment is demanded, and, consequently, bank notes usually pass from hand to hand by simple delivery, without indorsement.

In order to present the difference between the old and the

new system in the clearest manner, we will now contrast the two forms of stating the accounts, supposing that they denote the same operation—

Old form of Banking Accounts.

LIABILITIES.		ASSETS.	
To notes in circulation	£49,200	By Cash	£10,000
		By Bills of Exchange	40,000
	<hr/>		<hr/>
	£49,200		£50,000
	<hr/>		<hr/>

Modern form of Banking Accounts.

LIABILITIES.		ASSETS.	
Deposits	£49,200	By cash	£10,000
		By Bills of Exchange	40,000
	<hr/>		<hr/>
	£49,200		£50,000
	<hr/>		<hr/>

Now, in examining these two forms of accounts, though they are in reality two different methods of doing the same thing, a striking difference is apparent on the face of them. In the first it is manifest, on the face of it, that the banker thus created £49,200 of notes, or created that amount of liabilities against himself. In the second form this does not appear at all, but this sum of £49,200 appears as a “deposit,” or a “balance on drawing account,” and to any one who is not conversant with the subject, it seems to be a deposit of actual cash, and many persons are apt to believe that a banker has that amount of cash to trade with. Thus, when the accounts of the great Joint Stock Banks in London are published, and it appears that one has £20,000,000 of “deposits,” and so on, it is almost universally believed that it has twenty millions of actual money to trade with, or lend out, as it is erroneously called. And every half-year we see summaries in the newspapers shewing that all the Joint Stock Banks have, perhaps, an aggregate of £100,000,000 of “deposits,” and it is generally believed that they have that sum of money to trade with. But there never was a more complete and entire delusion. These £100,000,000 of “deposits” are not deposits in cash, but they represent the *old bank note circulation*. They are nothing but an enormous superstructure of CREDIT, built up on a comparatively small basis of bullion, exactly like the note circulation. These figures do not shew the quantity of cash at their command to trade with, but they shew the quantity of business they *have* done, and the liabilities they *have* created. These apparent “deposits” in cash, then, are nothing but credit created in exchange for the cash and bills which figure on the other side of the account as Assets.

These two forms of banking accounts, thus presented in contrast to each other, shew how the accounts would stand just *after* the banker has discounted his customers' bills, and *before* they have begun to operate upon their accounts, in the latter form by means of cheques. Every banker does business in exactly the same way, and, when their respective customers begin to operate by means of cheques, the following three different results may ensue:—

1. The actual money may be drawn out.

2. The credit may be transferred to the account of another customer of the same bank.

3. It may be an order to pay another bank. But in the last case, if the banker A is ordered to pay the banker B so much, the chances are that B will be ordered to pay A very much the same amount, and then an interchange of these respective orders may take place, and only the differences be paid in cash. And this is exactly the same in effect as an interchange of bank notes, and thus we see that mutual releases of debts are exactly equivalent to reciprocal payments in cash.

Thus we see that the modern system may be expressed in exactly the same language as the old one. Banking formerly consisted in the creation and exchange of instruments of credit. And so it does now. Banking equally now consists in the creation and exchange of instruments of credit, just as much as ever it did. The only difference is, that the *form of the instrument is changed*, and it was by this change in the form of the instrument that the London Joint Stock Banks were able to be founded, because the words of the monopoly clauses of the Acts of 1709 and 1742, only specified the former method of creating these instruments of credit.

Now, under the former system it was universally allowed that banks, by creating credit in the form of notes, created currency; under the modern system of entries, or "deposits," cheques perform exactly the same functions as notes, consequently, in a scientific sense, they are to be considered as currency now, just as much as they did before, and the supposition that the Legislature can prevent banks from dealing in credit, by prohibiting the issue of bank notes, is a mere delusion. But it must, at the same time, be fully admitted that bank notes may produce a greater inflation of credit than cheques, because there are many cases when bank notes would pass, in which cheques will not pass, and hence the latter system requires a broader basis of bullion, but yet, whenever they do pass, they are to be considered in all respects as the equivalents and substitutes for notes.

These considerations afford an explanation of some very well known phenomena, which are generally much misunderstood respecting Joint Stock Banks, which publish their accounts, and

give interest on "deposits," according to the rate of discount. When the rate of discount rises very high, it is universally observed that the apparent deposits in banks decline, and it is very commonly explained by saying that when interest rises very high, people take their money out of banks to invest it in other ways. But such an explanation is paradoxical on the face of it. Banks raise the rate of interest to attract money, and not to drive it away. Besides, if one asks contractors, builders, &c., at such periods, they will say that work is stopped, because people put their money into the banks for the sake of the high interest. Thus we meet with two diametrically contrary assertions, as to the flow of money at such periods, but, if we understand the real nature of these so-called "deposits," the reason of their diminution is plain; because, when the rate of discount is raised very high, it stops the discount of bills, it stops the creation of credit, in fact, *it is not a diminution of deposits in cash, BUT IT IS A CONTRACTION OF CREDIT.*

The very same phenomenon is usually witnessed after a great commercial crisis, such as that of 1857. In July, 1858, the aggregate of "deposits" in the Joint Stock Banks appeared to be considerably less than that in July, 1857, and this was, in fact, owing to the diminished number of bills discounted from the general contraction of mercantile operations, and by no means necessarily from a diminution in the actual cash deposited.

Now, it is generally admitted that issuing notes is coining credit; that it is, in fact, to all intents and purposes, creating capital, both as regards the issuers of the notes, and their effects to the public, a species of capital which is liable to be destroyed, and is capable of very serious abuse. But, it also necessarily follows, from the preceding details, that the modern system of banking is equally coining credit; and just as much as the "deposits," or the liabilities, created exceed the actual cash, they are equivalent to a creation of currency, and to an increase of capital.

Many persons say that Bills of Exchange are not currency, because they require to be discharged in money; and many more think that bills of exchange are analogous to bills of lading, because one *represents*, as they erroneously call it, money, and the other represents commodities. It is perfectly true that all bills of exchange must be expressed to be payable in money, but it is a most grievous error to suppose that they are all paid in money. The immense majority of commercial bills are not paid in money, but by credits in bankers' books. Most men in commerce draw bills and accept bills, that is, they have debts due to them, and debts due by them. These fall due at different dates, and when a trader's acceptances are falling due, he takes some of the debts due to him to his banker, and sells them to him. The banker buys them, as we have already explained, by

creating fresh liabilities of his own, and writing down so many figures to his customer's credit. When his own acceptance falls due, and is presented to him for payment, he draws a cheque upon his banker, and if the holder of the bill is a customer of the same banker, the matter is settled by a mere transfer of figures in the banker's books; if he is the customer of another bank, the two bankers have probably an exchange of debts, arising out of similar transactions on both their parts, and the debts are settled with the payment of no more coin than the difference; or if, as is more usually the case, the holder of the bill has deposited it with his banker, and the acceptor has made it payable at his bankers, who pays it, as a matter of course, as an ordinary cheque, the day it is due. Thus, we see, that the whole monetary business of the country is gradually reduced to the *creation and exchange of instruments of credit*, and the only use of the actual money is to pay the differences. Now, this is the regular practice of banking: this is the way in which the vast majority of bills of exchange in commerce are paid, and, consequently, the whole system may go on for an indefinite time and to an indefinite extent, without a single coin being required. Thus, a merchant may carry on a trade for any length of time, and pay bills to the amount of millions of money, and never touch a single coin. But these instruments of credit perform exactly the same functions as if they were coin, and in a scientific point of view they are to be considered in all respects as if they *were* coins. They are all a part of the currency.

Both bank notes and cheques are subject to the general rule of law, which affects all instruments of credit, that whoever takes one in payment of a debt *without indorsement*, does so at his own peril, and has no remedy against the person he receives it from, if it is not paid. And the indorsement only preserves the liability for a very short period; in almost all cases not more than 24 hours. The law intends that all bank notes and cheques should be presented for payment within 24 hours. If the receiver of a bank note requires the transferor to indorse it, which is by no means unfrequently done, and if, on presenting it within reasonable time, he finds the banker has failed, he has his remedy against the transferor, just exactly as if it was a cheque. On the other hand, if he delays presenting it beyond a reasonable time, and then finds the banker has failed, he has no remedy against the transferor, either in the case of an indorsed bank note or a cheque.

The erroneous notion of the real meaning and nature of "deposits," in banking language, may lead to great mistakes in estimating the stability of a bank. That depends upon a due proportion of cash being kept to meet them, and it might very well happen, that while the "deposits" were apparently mounting up, and might lead many persons to believe that the actual

quantity of cash was increased, it might be nothing, perhaps, but a dangerous extension of credit. And if this were carried to too great a length, the bank might be in the most dangerous position, just when it was apparently most flourishing. A private banker on a large scale often has an application to place £10,000, or more, to the credit of a customer; if he does this, it immediately counts as a "deposit" in banking accounts. Again, it is a very possible case, that a large railway company might request their banker to place £100,000 to their credit. Now, if the bank does this, such a transaction goes to swell up the figures of "deposits" in their published accounts, which may lead to very erroneous inferences by the public, who do not know the mode in which banking accounts are made up.

A consideration of this example also shows the very great misconception that is likely to be produced by an expression which is very often used regarding bankers, that they are merely agents between persons who want to lend, and those who want to borrow. This is not true in the ordinary sense of the words lending and borrowing, because, in ordinary cases of lending and borrowing, the lender deprives himself of the use of the capital he lends. But, in ordinary banking, both parties have the complete use of the capital. The customer lends his money to the banker, and yet has the free use of it—the banker employs that money in promoting trade; upon the strength of its being deposited with him, he buys debts with his "promises to pay," and the person who sells the debt has the free use of the very coin which the lender has the same right to demand.

The common notion of banking is, that it consists in lending money upon the security of bills of exchange. Such an idea, is profoundly erroneous, as it consists in buying debts with "promises to pay," or creating liabilities. And the contingency is, that he may be called upon to pay them; no doubt, theoretically speaking, he is liable to be called upon to pay all those liabilities at a moment's notice, just in the same way as it is theoretically possible that all the lives insured in a life insurance company may drop at the same moment; or, it is theoretically possible, that all the property insured in an office may be destroyed by fire at the same moment; but no one expects such a contingency to happen. Banking is like insurance, the sum in cash retained by the banker is what his experience tells him is sufficient to ensure his being able to meet any calls which are likely to be made upon him.

In order to add further proof, if possible, of the utter fallacy of the common notion that discounting bills is borrowing money, we may state, that when a customer has discounted a bill with his banker, he has parted with all property in it, just as with any other article of sale. The bill becomes the absolute property of the banker, which he may sell again, or pledge, or deal

with in any manner that suits his own interests best. Now, if it was a loan from the banker to his customer, it would manifestly be the duty of the customer to repay the loan in due time, and get back his bill, which would be merely deposited with the banker as security, and should be restored when the loan was paid, and which the banker would have no right to part with. But this is not the case. The banker does not receive payment from his customer, but from the acceptor of the bill, and he has a perfect right, if he pleases, to sell the debt to any one else. On the other hand, in some few instances, a customer does sometimes borrow money on the security of bills, and in these cases, the customer repays the loan and receives back his bills. But such cases are comparatively rare, and to be distinguished from the ordinary business of discounting bills.

From the foregoing considerations, we see that a merchant deals *with* credit, and a banker deals *in* credit. A merchant brings him debts, payable some time after date, for sale, and, by a flourish of his pen, the banker transmutes them into debts payable instantly, which have precisely the same effect in commerce as so many sovereigns. He reaps exactly the same profit by creating a credit in favor of his customer, as if he gave him the actual cash. And the cheques drawn against these credits, so created by the banker, circulate commodities exactly in the same manner as bank notes do, which circulate commodities exactly in the same manner that gold and silver money does. Consequently, these credits, so created by the banker, are CURRENCY, or CIRCULATING MEDIUM. From this it manifestly follows, that BANKING CREDIT IS BANKING CAPITAL.

Now, in the preceding section, we have proved that mercantile credit is mercantile capital, and, consequently, as all credit is either banking, or mercantile, we arrive at this general conclusion, that CREDIT IS CAPITAL.

The preceding details also show the prodigious error of those who think that banking does not add to capital, that it only distributes existing capital. It is unquestionably true that no mode of banking can create actual gold sovereigns. But if, by means of their credit, bankers can circulate their promises to pay, and if these be voluntarily received and accepted by the community at large, at exactly the same value as if they were actual sovereigns, then just by so much as they exceed in number the quantity of actual sovereigns in the banker's possession, they are, to all intents and purposes, an *addition* to existing capital. For, not only does he save the use of the actual coin in an immense multitude of instances where it would be required if banking did not exist, and liberates it, and enables it to be applied to promote commerce, which is in its practical effects identical with an addition of actual coin to that extent, but, by the extra multiplication of his promises to pay over and above

that, he is enabled to make what is, to all intents and purposes, a further addition to the moving power of commerce to an enormous extent.

Banking is, therefore, the most potent engine for the increase of the moving power of any given quantity of actual capital that it is possible to devise, consistently with keeping up the value of the currency at its level with bullion. John Law says, most justly:—"The introduction of credit by means of a bank, augments the quantity of money more in one year than a prosperous commerce could do in ten." And just as banking spreads more extensively, does it multiply the producing power of the community. Every one knows the great economising power of railroads in diminishing the quantity of capital required to supply any given demand for commodities. Now, an extension of banking acts precisely in an analogous manner, but to a much greater degree; for, not only does it economize the actual substance to a very great extent, but it makes the "promise to pay" of equivalent value with the actual payment. And it is just in this multiplying power of capital that the principal danger of too rapid an extension of banking consists. The rate of discount always depends upon the proportion between actual capital and the demand for it, or on the debts offered for sale. A sudden change in the proportion of these, causes the most violent fluctuations in the rate of discount. If an unusual quantity of capital is thrown too suddenly upon the market, the only result must be a rapid and extreme fall in the rate of discount. Now, a too rapid extension of banking has precisely the same effect as throwing a vast quantity of capital suddenly on the market. For, not only do the actual operations of banking have all the practical effects of adding to the existing capital, but to that will be added all the evil effects of over-competition, an unnaturally low rate of discount, thereby a depreciation of the currency; an export of bullion; a joint-stock bubble mania, with all its rogueries; then a collapse, and commercial ruin.

Great and inestimable, therefore, as are the blessings and advantages of banking, there is no department of trade which is likely to produce more fatal consequences to the public by too rapid an extension of it, than too rapid a multiplication of banks. There is no *mania* which should be looked to with a more jealous eye by the public, or more carefully guarded against by the Legislature, than a bank mania.

The preceding details also show the entire fallacy of the almost universal opinion, that the London banks, public and private, other than the Bank of England, are mere banks of deposit, and are not banks of issue. Thus, McCulloch says, (*Dictionary of Commerce*, Art. *Bank*):—"Banks are commonly divided into two great classes of *Banks of Deposit* and *Banks of Issue*. This, however, appears, at first sight, to be rather an

imperfect classification, inasmuch as almost all Banks of Deposit are at the same time Banks of Issue, and almost all Banks of Issue are also Banks of Deposit. But there is, in reality, no ambiguity; for, by Banks of Deposit, are meant banks for the custody and employment of the money deposited with them, or entrusted to their care by their customers, or by the public; while by Banks of Issue are meant banks which, besides employing or issuing the money entrusted by others, issue money of their own, or notes payable on demand. The Bank of England is our principal Bank of Issue, but it is, as well as the other banks in the different parts of the empire that issue notes, also a great Bank of Deposit. The private banking companies of London, and the various provincial banks that do not issue notes of their own, are strictly *Banks of Deposit*."

This view is manifestly erroneous. A Bank of Deposit is one which, like those of Venice, Amsterdam, and Hamburg, is for the sole purpose of keeping the custody of money, and the credit it creates is exactly equal to the cash deposited. A "Bank of Issue" is one that, besides that, purchases bills by means of creating credit, in addition to the cash deposited, and thus adds to the quantity of the currency. Now, all banks in England, whether they issue notes or not, add to the currency by creating credit, and, therefore, they are all to be considered, in a scientific sense, as *Banks of Issue*.

To show how completely at fault even the most eminent writers are on the nature and effects of banking, we shall quote an extract from Mr. Mill, B. iii., c. 24, § 3. In treating of the regulation of a currency, and the effects of the Bank Act of 1844, he says, in a note:—"It would not be to the purpose to say, by way of objection, that the obstacle may be evaded by granting the increased advance in book credits without the aid of bank notes. This is indeed possible, as Mr. Fullarton has remarked, and as I have myself said in a former chapter. BUT THIS SUBSTITUTE FOR BANK NOTE CURRENCY CERTAINLY HAS NOT YET BEEN ORGANIZED; and the law having clearly manifested its intention, that in the case supposed, increased credits should not be granted, it is yet a problem whether the law would not reach what might be regarded as an evasion of its prohibitions, or whether deference to the law would not produce (as it has hitherto done), on the part of banking establishments, conformity to its spirit and purpose, as well as to its mere letter."

We have seen, in the preceding exposition of the actual mechanism of banking, that what Mr. Mill says has never yet been organized, and which the law might possibly put down, is the very thing in which London banking has exclusively consisted for eighty years!!

Moreover, the Bank Act of 1844 was passed for the express purpose of preventing banks from creating credit, and the

almost universal opinion is, that it does so—that it makes the currency vary exactly as if it were so. The preceding details shew that the ordinary business of London bankers consists in the daily creation of *millions of promises to pay*. The popular belief, that the Bank Act of 1844 prevents bankers from creating credit, is probably, since the belief in the balance of trade, beyond comparison, the most profound delusion that has deceived the public mind.

It is just because *all* banking advances are creations of credit, that every one, who really understands the mechanism of banking, has declared that banking practically augments the capital of a country. Thus, for example, Mr. Hamilton, the celebrated financier of the United States, when called upon, as Secretary to the Treasury, to present a report on the expediency of establishing a national bank, says (*Gales and Seaton, Vol. ii., p. 2083*):—

“The following are among the principal advantages of a bank:—First, the AUGMENTATION of the active or productive capital of a country. * * * It is a well-established fact, that banks in good credit can circulate a far greater sum than the actual quantum of their capital in gold and silver. * * * This faculty is produced in various ways:—1st. A great portion of the notes which are issued, and pass current as cash, are indefinitely suspended in circulation, from the confidence which each holder has that he can at any moment turn them into gold and silver. 2ndly. *Every loan which a bank makes is, in its first shape, a CREDIT GIVEN to the borrower on its books*, the amount of which it stands ready to pay, either in its own notes, or gold, or silver, at his option. But, in a great number of cases, no actual payment is made in either. * * * The same circumstances illustrate the truth of the position, that it is *one of the properties of banks to increase the active capital of a country*. * * * This additional employment given to money, and the faculty of a bank to lend and circulate a greater sum than the amount in coin, *are, to all the purposes of trade and industry, AN ABSOLUTE INCREASE OF CAPITAL*. Purchases and undertakings in general can be carried on by any given sum of bank paper, or credit, as effectually as by an equal sum of gold and silver. And thus, by contributing to enlarge the mass of industrious and commercial enterprises, banks become nurseries of national wealth—a consequence as satisfactorily verified by experience, as it is clearly deducible in theory.”

Thus we see that this celebrated financier knew perfectly well what Mr. Mill does not know, that all banking advances are made by creating credit; and he does not consider this as robbery; nor does he at all countenance the doctrine that no increase of money can be of any service to a country; on the contrary, he pronounces that it may be extremely useful.

Now, as we have shewn that these debts may all be settled by

the mere payment of differences between the mutual claims, it might so happen that they might all be equal, and no coin at all pass. It is perfectly possible, therefore, that any amount of business might be settled without any coin at all. Consequently, we observe that this is a very strong confirmation of what we have already said, that the quantity of money necessary in any country depends very much on the method of doing business, and has no relation to the quantity of commodities. It is very common among some writers to say that the prices of commodities depend upon the quantity of money and the quantity of commodities; but such ideas are mere visionary chimeras.

There is in London an office for the express purpose of exchanging the mutual claims of those bankers upon each other who are members of it. This office is called the Clearing House, and we have given an account of it in a subsequent chapter, by which it will be seen that millions of debts, or credits, are daily extinguished by mutual releases.

Now, when we see that cheques are merely substitutes for bank notes, that in every case where a cheque now passes bank notes would be required if cheques did not exist: when we also see that a bill of exchange on the day it is payable becomes a cheque, which is equivalent to a bank note, it follows very clearly that all the obligations interchanged at the Clearing House form an integral part of the circulating medium. Their being exchanged at the Clearing House can make no difference to what they would be if they were presented and paid by each banker; for they have all done their duty *before* they arrive at the Clearing House—they have caused commodities to circulate, perhaps many more times than once before they come to be discharged.

We see, then, how utterly futile it is to attempt to form any estimate of the amount of paper currency in this country. Returns may be made of the stamps issued for bank notes, bills of exchange, and promissory notes; but how is it possible ever to discover the amount of cheques in circulation? If this cannot be done, it is useless to try to estimate the amount of the paper currency; and still more impossible is it to control the issue of paper, while the power of drawing cheques is unrestricted.

The great and important portion of the currency which consists of cheques has not been sufficiently appreciated. The attention of speakers, writers, and legislators, on the *paper currency*, has been almost exclusively directed to bank notes; whereas all the ideas involved in bank notes are, with a small change in the form of expression, applicable to cheques; and there is no operation whatever which a bank can promote by means of bank notes which it cannot with equal efficacy perform by means of cheques. If it wishes to advance a speculation, instead of giving its customer so many of its notes, it promises

to honor his cheques to an equal amount. In Scotland the system of bank notes chiefly prevails; and cheques are of more recent introduction, and more sparingly used than in England. In this country, cheques have very greatly superseded bank notes, and in many respects are far superior to them. Among other reasons, they are not such ready weapons against a bank in the hands of rivals and enemies. It has been by no means an unheard-of measure of hostility against a bank which issues notes, for its rivals to buy them up in all directions, and having accumulated a considerable amount of them, to present them for payment suddenly in a mass, in the hope that the bank may be unprepared to meet, on the instant, so great a demand for gold, and be ruined. With cheques this method of hostility is more difficult. It is not easy to conceive that any person could go round to all the customers of a bank, and accumulate such an amount of cheques as to render a demand for payment of them in gold formidable to the bank. At all events, it would require a much more elaborate and deep-laid plot to injure a bank by the method of cheques than of bank notes.

Seeing, then, that the nature of discounting bills of exchange is buying debts, which are to be considered just like any other article of commerce, it follows that the same laws govern their exchangeable relations as those of any other quantities. The first duty of a banker is to maintain his own position, which he can only do by maintaining certain proportions between his actual cash and his promises to pay, or his liabilities, and that proportion must vary from time to time, according to circumstances. In times of a general failure of credit, he must maintain a very much larger portion of cash compared to liabilities than in times of general confidence. Under such circumstances, his duty is to *contract* his liabilities, which he must do either by refusing to buy debts altogether, or else by giving a lower price for them, *i. e.*, raising the rate of discount. And a general rise of the rate of discount has a tendency to discourage the offering of debts for sale, just as low price of anything else discourages its being offered for sale, except by those who positively require the cash.

On the other hand, this lowering of the price of debts, *i. e.*, this increase in the value of money, or the raising of the rate of discount, has an inevitable tendency to attract bullion from where it is more abundant, *i. e.*, where the rate of discount is lower. Wherever debts are to be bought cheap, thither will bullion fly to buy them; wherever debts are sold dear, that is, wherever money is to be bought cheap, thither will debts fly to be sold, and there will competitors be to buy money. Consequently, it is an infallible law of nature, that whenever the price of debts differs in two markets by more than sufficient to defray the expense of sending bullion, it will cause an immediate flow

of bullion to that market where debts are to be bought cheapest, *i. e.*, where the rate of discount is highest. That is to say, if the rate of discount at Paris is greater than at London by more than sufficient to cover the expense of sending bullion, debts will fly from Paris to London to buy bullion, and bullion will fly from London to Paris to buy debts. The exchangeable relations of money and debts will obey exactly the same laws as the exchangeable relations of money and wheat. Consequently, if left free and uncontrolled, the prices of debts have a natural tendency towards equilibrium in different markets.

On Cash Credits.

19. The credit created by the Bankers, in the operations just described, was employed to purchase commercial bills, which arose out of the *transfer* of commodities, and we have seen that they could create credit to several times the amount of cash in their possession. And, according to the notions of some writers, this was the limit of legitimate credit. We have now to describe a species of credit of a totally different sort, invented in Scotland, and to which the marvellous progress and prosperity of that country is mainly due. The consideration of this, will sorely test the dogmatic assertions of literary dreamers.

As stated in the History of Banking in Scotland, the Bank of Scotland began the issue of £1 notes about the beginning of the last century. In 1727, a rival bank was founded, named the Royal Bank. In the very contracted sphere of Scotch commerce, at that period, there were not sufficient Commercial Bills to exhaust the credit of the Banks. They had, as it were, a superfluity of credit on hand, and the Royal Bank devised a new means of getting it into circulation.

It agreed, on receiving sufficient guarantees, to open, or create, credits in favour of respectable and trustworthy persons.

A Cash Credit is, therefore, simply a drawing account, created in favour of a customer, upon which he may operate in precisely the same manner, as on a common drawing account. The only difference being, that instead of receiving interest upon the daily balance at his credit, as is very commonly the custom in Scotland, he pays interest upon the daily balance at his debit. It is thus an *inverse* drawing account.

All these advances were made exclusively in the Bank's own notes, and they were not issued on the basis of any previous transaction.

Cash credits are applicable to a totally different class of transactions from those which give rise to Bills of Exchange, and we will now explain their nature more fully.

Every man in business, however humble, or however extensive, must necessarily keep a certain portion of ready money by him, to answer immediate demands for small daily expenses, wages,

and other things. This could, of course, be much more profitably employed in his business, where it might produce a profit of 15 to 20 per cent., instead of lying idle. But, unless the trader knew that he could command it at a moment's notice, he would always be obliged to keep a certain portion of ready money in his own till, or he must be able to command the use of some one else's till. Now, one object of a cash credit is to supply this convenience to the trader, to enable him to invest the whole of his capital in business, and, upon proper security being given, to furnish him with the accommodation of a till at a moment's notice, in such small sums as he may require, on his paying a moderate interest for the accommodation.

Almost every young man commencing business in Scotland, does it by means of a cash credit. Thus, for instance, lawyers, or writers to the signet, commencing business, have occasion for ready money from day to day, before they can get in payments from their clients. It is a great bar to any young man to commence the business of a solicitor without capital, which must be either his own, or furnished him by his friends. It is an immense advantage to him and to them to have it supplied by a bank, on a guarantee, a mere contingency, which they never would give if they thought there was any danger of its being enforced.

These credits are granted to all classes of society, to the poor as freely as to the rich. Every thing depends upon character. Young men in the humblest walks of life begin by making a trifle for themselves. This inspires their friends with confidence in their steadiness and judgment, and they become sureties for them on a cash credit. This is, in all respects, of equal value to them as money, and thus they have the means placed within their reach, of rising to any extent that their abilities and industry permit them. It is an undoubted fact, that multitudes of men who have raised themselves to enormous wealth, began life with nothing but a cash credit. As one example among thousands, Mr. Monteith, M.P., told the Committee of the House of Commons, in 1826, that he was a manufacturer, employing at that time 4,000 hands, and that, except with the merest trifle of capital, lent to him, and which he very soon paid off, he began the world with nothing but a cash credit!

The banks usually limit their advance to a certain moderate amount, varying from £100 to £1,000 in general, and they always take several sureties in each case, never less than two, and frequently many more, to cover any possible losses that might arise. These cautioners, as they are termed in Scotch law, keep a watchful eye on the proceedings of the customer, and have always the right of inspecting his accounts with the bank, and of stopping it at any time, if irregular. These credits are not meant to degenerate into dead loans, but they are

required to be constantly operated upon, by paying in and drawing out.

The enormous amount of transactions carried on by this kind of accounts may be judged of by the evidence given before the Committee of the Commons in 1826. It was then stated that, on a credit of £1,000, operations to the extent of £50,000 took place in a single week. Its effects, therefore, were exactly the same as if there had been 50,000 sovereigns. Others stated that, on a cash credit of £500, operations to the amount of £70,000 took place in a year. One witness stated that during twenty-one years in a very moderately-sized country bank, operations had taken place to the amount of nearly £90,000,000, and that there had never been but one loss of £200 on one account, and that the whole loss of the bank during that period did not exceed £1,200. Now, the whole of these gigantic operations were transacted by creations of pure credit. At that time it was conjectured that there were about 12,000 cash credits guaranteed to persons in Scotland, and that there were about 40,000 persons as sureties, who were interested in the integrity, prudence, and success of the others. The witnesses before the Lords declared that the effects of these were most remarkable on the morals of the people.

But the operations of these cash credits was immensely extended beyond mere commerce, and their advantages are more openly and strikingly displayed in the prodigious stimulus it gave to the agriculture of Scotland during the last century. They have, indeed, been the main cause of making it what it is. In the Scottish system of farming, leases almost universally prevail, and a farm is not entrusted to a man who is not educated to his business. He usually enjoys nineteen years security of tenure; or, where leases are granted for the purpose of reclaiming land, for much longer periods. Now, suppose a farmer is known to be active, skilful, and industrious, and obtains a farm upon lease, which is capable of great improvement, he goes to the bank, and, upon the security of his lease and some friends, who become bound for him, the bank grants him a cash credit. With this advance—pure credit—he reclaims the land, employs the people, reaps the harvest, and, when that is gathered, pays back the loan.

It was in this manner that that prodigious progress in agriculture was made in Scotland. There were immense quantities of reclaimable land, and abundance of unemployed people, but no capital, or money, to set their industry in motion. Seeing this state of matters, the Edinburgh banks opened branches in numerous parts of the country, and sent down boxes full of £1 notes, and granted cash credits to the farmers. These notes were universally received as readily as coin. The farmers made their purchases and paid wages with them; and the enormous

tracts of barren land were changed into fertile corn fields. Now, these £1 notes were not a substitute for any specie, they did not supersede or displace any previously-existing money, they were a pure addition to the existing money; and, seeing all this, what are we to say of the doctrines of those writers, who maintain that no increase of money can be of any use to a country, and that to issue paper in excess of specie is robbery?

Commerce and agriculture, therefore, received their prodigious stimulus from these cash credits. But they were of still greater use in a public point of view. Almost all the great public works of every description were created by means of Cash Credits. One witness stated that the Forth and Clyde Canal was executed by means of a Cash Credit of £40,000 granted by the Royal Bank. And, in a similar way, whenever any other great public works are to be done, such as roads, bridges, canals, &c., the invariable course is to obtain a large Cash Credit at one of the banks.

The advantage to the person who has a cash credit is, that he only pays interest from day to day on the sum he actually has at his debit, whereas, in discounting a bill of exchange, he pays interest on the whole amount of his credit, whether he uses it or not, and discount is a trifle more expensive than interest. The Bank would, therefore, naturally prefer to employ its resources by way of discount, if it could, rather than cash credit. There is also a further disadvantage attending them, that they cannot be called up on a sudden emergency, and if there be a run upon the bank, the security cannot be negotiated like a bill of exchange. It is, therefore, only where a bank has a superfluity of credit, which it cannot employ profitably, that it would resort to a cash credit, and also when there is but a slight chance of a run upon it.

For these reasons, cash credits have always been looked upon with a very unfavourable eye by London Bankers, and for very good reasons. In the first place their credit, until recently, was not so solid and well established as that of the principal Scotch banks. These originated cash credits in consequence of their issuing £1 notes, and London bankers do not issue circulating credit in the form of notes—they can always find employment for their cash—and they are more liable to runs.

All these marvellous results, which have raised Scotland from the lowest state of barbarism up to her present proud position, in the space of 150 years, are the children of pure CREDIT. It is no exaggeration whatever, but a melancholy truth, that at the period of the Revolution of 1688, and the establishment of the Bank of Scotland, that country, partly owing to such a series of disasters as cannot be paralleled in the history of any other independent nation, and partly owing to its position in the very outskirts of the civilized world, and far removed from the

humanizing influence of commerce, divided, in fact, into two nations, aliens in blood and language, was the most utterly barbarous, savage, and lawless kingdom in Europe. And it is equally undeniable that the two great causes of her rapid rise in civilization and wealth, have been her systems of national education and banking. Her system of banking has been of infinitely greater service to her than mines of gold and silver. Mines of the precious metals would probably have demoralized her people. But her banking system has tended immensely to call forth every manly virtue. In the character of her own people, in their steadiness, their integrity, their honour, Scotland has found wealth infinitely more beneficial to her than the mines of Mexico and Peru.

The express purpose of these banks was to create credit, incorporeal entities created out of *nothing*, for a transitory existence, and then, having performed their functions, vanishing again into the *nothing* from whence they came. And has not this *credit* been CAPITAL? Will any one, with these results staring the world in the face, believe that it is maintained by writers, who are still considered as Economists, that the effects of credit are purely imaginary!—That credit conduces nothing to the increase of wealth!—That credit conduces nothing to production!—That credit only transfers existing capital!—And that those who maintain that credit is productive capital, are such puzzle-headed dolts as to think that the same thing can be in two places at once!!

Now, we observe, that these Cash Credits, which have produced such marvellous results, are purely of the nature of what is called *accommodation paper* in England. They are not based upon any previous operations, nor upon the transfer of commodities already in existence. They are created for the express purpose of *creating or forming future* products, which would either have had no existence at all but for them, or, at all events, it would have been deferred for a very long period, until solid money could have been obtained to produce them. Thus we have an enormous mass of exchangeable property, created by the mere will of the bank and its customers, which produces all the solid effects of gold and silver, and when it has done its work, it vanishes again into nothing, at the will of the same persons who called it into existence. Hence we see that the mere will of man has *created* vast masses of wealth out of *nothing*, and then DECREASED them into NOTHING, which, having served their purpose, after a time were

“Melted into air, into thin air.”

But their solid results have by no means faded like the baseless fabric of a vision, leaving not a rack behind. On the contrary, their solid results have been her far-famed agriculture,

the manufactures of Glasgow and Paisley, the unrivalled steamships of the Clyde, great public works of all sorts, canals, roads, bridges, and poor young men converted into princely merchants.

What the Nile is to Egypt, that has been her banking system to Scotland; and it was fortunate for her that the foundations of her prosperity were laid broad and deep before the gigantic fallacy was dreamt of, that the issues of banks should be inexorably restricted to the amount of gold they displace, and before Mr. Mill had proclaimed to the world that those who created paper beyond that are robbers!

On Open Credits.

20. We have seen that Cash Credits are always created to forward a future operation, and are never founded on a past one. There is always, however, collateral security taken, so as to protect the Bank against loss. In the keen spirit of competition, however, a hazardous system has sprung up of granting these credits without collateral security. This system is a good deal practised abroad, we believe, and is called *Crédit à Decouvert*, and, in this country, *Open Credits*. It is manifestly far more hazardous than Cash Credits, or common discounting, because there are always two names at least in such cases. We believe that the Joint Stock Banks, which failed a few years ago, indulged to a great extent in this dangerous system.

On the Transformation of Temporary Credit into Permanent Capital.

21. We have already seen that, in commerce, the *release of a debt* is in all cases whatever equivalent to a *payment in money*. We shall now give an application of this doctrine, which may startle some of our readers.

We have observed that mathematicians denominate debts *negative* quantities, because, in estimating a man's fortune, they are to be *subtracted* from his property.

Now, let us suppose that a trader has a certain amount of property, or trading capital, and has also a certain amount of obligations, or debts, in circulation.

Then, if any one were to make him a present of some money, that, of course, would be an augmentation of his capital. And, as Algebraists call money a positive quantity, giving him money would be represented by $+ \times +$ which gives $+$.

Suppose, however, that his creditors were to *release him from his debts*, that would also be an augmentation of capital. And, as debts are negative quantities, to *take away a debt* is expressed by $- \times -$ which also gives $+$.

Thus, in Commercial Algebra, to pay money is absolutely equivalent to release from a debt, in strict accordance with the doctrine that $+ \times +$ is always equivalent to $- \times -$.

When it is published to the world that the Bank of England has a paid-up capital of £14,000,000, and that the various Joint Stock Banks of London have paid-up capitals of this magnitude:—

London and Westminster.	£1,000,000
Union Bank	800,000
Joint Stock Bank.....	800,000
London and County Bank	800,000

Does not the whole world, except those very few who are conversant with the mechanism of banking, believe that the Bank of England and the Joint Stock Banks have these sums of capital paid up in hard MONEY?

What will they say then, when they learn that this idea is pure *moonshine*? These Banks never had anything like that sum paid up in actual money at all. Of course, it is utterly impossible to tell how much was ever paid in money, but this we believe we are safe in saying, that not the half of these sums were ever paid up in money. At least half of these gigantic sums of so-called paid-up capital are nothing more than the *Banks' own CREDIT turned into CAPITAL!*

In order to see how this was done, we have only to refer to the history of banking in England, where the mode of increasing the capital of the bank in 1697 is described. The bank was founded by means of the payment in money of £1,200,000. It afterwards, in the course of business, issued notes to a considerable amount. These notes were debts, or *negative* quantities, and the bank was indebted to the holders of them. After it stopped payment, these notes fell to a heavy discount. In 1697 it was determined to increase the capital of the bank, and this was done by receiving £800,000 of Exchequer tallies, and £200,000 of its own *Depreciated Notes*. These depreciated notes were received at their full value as cash. And thus we see, at once, that at the first *augmentation of capital*, £200,000 of this *capital* consisted of its own *Depreciated Notes*—or CREDIT.

An exactly similar proceeding is described in the history of banking in Scotland. In 1727, the Bank of Scotland increased its capital. The subscription was paid up partly in the bank's own notes. An outcry was made against this, but the Directors justly answered, "But the objectors do not at all consider this point, for the payments are many of them made in specie, and *bank notes are justly reckoned the same as specie when paid in on a call of stock, because, when paid in, it LESSENS the DEMAND on the Bank.*"

Here we see that the Directors clearly understood, that the *Release of a Debt*, is in all respects equivalent to the *Payment of Money*. The Bank had issued its notes. For whatever reason they were issued, they were, as said, *negative* quantities,

and the Bank was debtor to the holders of them. When the call was made, the subscriber might either pay money, or release the bank from its debts. And we see that the two operations were absolutely equivalent. At every further increase of capital, the very same operation would be repeated, payment in money and in the Bank's own notes would always be treated as exactly equivalent; and hence we see that at every fresh increase of capital, a certain quantity of the Bank's own *Temporary Credit* would be turned into *Permanent Capital*.

Such are the methods by which the Capital of a Joint Stock Bank, which issues notes, may be increased. It might be thought, perhaps, that it is only banks which issue notes that can turn their own credit into Capital. But that is a complete error. We have seen, in this section, that the very essence of Banking consists in making advances by creating debts, either in the form of notes, or credits, in their books, called DEPOSITS. Thus, all the Joint Stock Banks in London, other than the Bank of England, do business exclusively by creating deposits. Now, suppose a customer of one of these Banks has a Balance, or Deposit, on his account. The Bank determines to increase its Capital, and the customer wishes to take part of the stock. He may either pay in money, or he may give the Bank a cheque on his account. This is exactly the same thing as paying the Bank in its own notes. It is the *Release of a Debt*. Supposing he has not enough on his account to pay for the stock he wishes to purchase, he may bring the Bank bills to discount. The Bank discounts these bills, or buys these debts, by creating another debt, in the form of a credit, or a deposit, on the customer's account, which is a *negative* quantity, exactly equivalent to a Bank note. The customer then gives the Bank a cheque on his account, that is, he releases it from the debt it has just created in his favour. *And that debt released then becomes augmentation of Capital*. Hence, we see that the Bank first created the credit, and it was then turned into Capital.

It is true that this method cannot be adopted to so great an extent by the public when the Bank does not issue notes; because the general public would not have any claims against the Bank, but only its own customers, and those who might happen to have cheques given to them by them. Still, as far as it goes, the principle is the same. And this is the way in which the capital of all Joint Stock Banks is increased, and it may go on to any extent without any payment in money.

In a precisely similar way, when great public loans are contracted for, a very large portion of them is always created by means of credit. The customers of a Bank wish to subscribe to a loan. They bring it a batch of bills to discount. They draw cheques against the deposits created on the discount of these bills. These cheques may be paid into the credit of the great

contractors, at their bankers, and transferred an indefinite number of times, without even being required to be discharged in money; they may, in fact, be discharged by being cancelled against other Credits.

On Accommodation Bills.

22. We now come to a species of Credit, which will demand great attention, because it is the curse and the plague spot of Commerce, and it has been the great cause of those frightful commercial crises, which seem periodically to recur; and yet, though there can be no doubt that it is in many cases essentially fraudulent, yet it is of so subtle a nature as to defy all powers of Legislation to cope with it—at least, according to the still unreversed doctrines of Westminster Hall.

We have shown, by the exposition of the system of Cash Credits, that there is nothing essentially dangerous or fraudulent in a Credit being created for the purpose of promoting future operations. On the contrary, such Credits have been one of the most powerful weapons ever devised by the ingenuity of man to promote the prosperity of the country. A certain species of this Credit, however, having been grossly misused for fraudulent purposes, and having produced great calamities, we must now examine wherein the danger and the fraud of this particular form of Credit lie.

When a Bill of Exchange is given in exchange for goods actually purchased at the time, it is called a Real Bill, and it is supposed by many writers, and even by many commercial men, that there is something essentially safe in it, because, as the goods have been received for it, it is supposed they are always there to provide for the payment of it; and that only so much Credit is created as there are goods to redeem it. Thus, in the article *Credit*, in the *Encyclopædia Britannica*, it is said:—"Every sum of Credit, therefore, must be founded on a transfer of a corresponding sum of Capital, and the whole amount of Credit existing, at any time, can never exceed that of the lent capital."

When we see such gross, dense, *crassa ignorantia* in a publication of the character and pretensions of the *Encyclopædia Britannica*, what are we to expect from the general public?

Leaving out of consideration at present the cases where Credit is created without the transfer of any capital at all, it is manifest, from the description of the system of Credit already given, that it is utterly erroneous to say that the quantity of Credit cannot exceed the quantity of Capital lent. A Bill of Exchange, it is true, only arises out of a transfer of goods, but then a fresh bill is created at *each* transfer. In the ordinary course of business, there will always be, in general, at least *twice* the amount of bills to what there are goods. But if twenty transfers took place, twenty bills would be created. If goods

to the amount of £100 were transferred twenty times, supposing even that the price of the goods did not change, which it most assuredly would, there would be Credit created to the amount of £2,000. And it would only be the last holder of the goods who would have them, and be enabled to devote the proceeds to the payment of the last bill only. The remaining nineteen bills must manifestly depend upon other sources for payment.

The security, therefore, which is supposed to reside in Real Bills, on account of their being founded on the transfer of goods, is shewn to be, to a great extent, imaginary. Let us suppose, however, that A sees that a profitable operation may be done. The Bank will not, as traders do, make him an advance on his own name alone. It must have at least *two* names. A therefore goes to B, and gets him to join him as security to the Bank, on engaging to find the funds to meet the bill when due. A then draws a Bill on B, who accepts it to *accommodate* A, as it is called, and such a Bill is called an *Accommodation Bill*.

The Bill thus created without any consideration, as it is termed in legal language, or, in common language, without any transfer of goods, may be taken to a Banker to be discounted like any other bill, an operation may be performed, and, if successful, the bill may be paid with the proceeds.

Stated, therefore, in this way, there is nothing more objectionable in such an accommodation bill than in any ordinary real bill. The security is just the same in one case as in the other. In the one case goods *have been* purchased, which will pay the bill: in the other case goods *are to be* purchased, whose proceeds are to pay the bill. In fact, we may say that all commercial credit is of this nature, because a credit is created to purchase the goods whose proceeds are to pay it.

There is, therefore, clearly nothing in the *nature* of this species of paper worse than in the other, and, when carefully used, nothing more dangerous. Cash credits, which have been one of the safest and most profitable parts of Scotch banking, and have done so much for the country, are all of this nature. They were created without any anterior operation, for the express purpose of stimulating future operations out of which the Credit was to be redeemed. There is, therefore, not anything more criminal, atrocious, and vicious in the one system rather than in the other. Or, if there be, the criminality and atrocity must lie in the difference between *have been* and *is to be*.

Nevertheless, as it is indubitably certain that most of those terrible commercial crises which have so frequently convulsed the nation have sprung out of this species of paper, it does merit a very considerable portion of the obloquy and vituperation heaped upon it. It is, therefore, now our duty to investigate the method in which it is applied, and to point out wherein its true danger lies.

The security supposed to reside in Real Bills, as such, is, as we have seen, exaggerated. But there is at least this in them, that as they only arise out of the real transfers of property, their number must be limited by the nature of things. However bad and worthless they may be individually, they cannot be multiplied beyond a certain extent. There is, therefore, a limit to the calamities they cause. But we shall show that, with *Accommodation Bills*, the limits of disaster are immensely and indefinitely extended, frequently involving in utter ruin all who are brought within their vortex.

We shall now endeavour to explain to our readers, wherein the difference between real and accommodation paper consists, and wherein the true danger lies.

Let us suppose that a manufacturer, or wholesale dealer, has sold goods to ten customers, and received ten *bonâ fide* trade bills for them. He then discounts these ten bills with his banker. The ten acceptors to the bills, having received value for them, they are the principal debtors to the Bank, and are bound to meet them at maturity, under the penalty of commercial ruin. The Bank, however, has not only their names on the bills, but also that of its own customer, as security. It, moreover, generally keeps a certain balance of its customer in its own hands, proportional to the amount of the limit of discount allowed. Now, even under the best circumstances, an acceptor may fail to meet his bill. The Bank then immediately debits its customer's account with the amount of the bill, and gives it him back. If there should not be enough, the customer is called upon to pay up the difference. If the worst comes to the worst, and its customer fails, the Bank can pursue its legal remedy against the estates of both the parties to the bill, without in any way affecting the position of the remaining nine acceptors, who, of course, are still bound to meet their own bills. Even supposing, however, it is only the acceptor who fails to meet his bill, the Bank would not probably take a second bill upon him, nor would a dealer sell his goods again to him, after giving him the annoyance of having to take up his bill.

In the case of accommodation paper, there are very material differences. To the eye of the banker, there is no visible difference between real and accommodation bills. They are, nevertheless, very different, and it is in these differences that the danger consists.

In accommodation paper, the person for whose accommodation the drawing, indorsing, or accepting, is done, is bound to provide the funds to meet the bill, or to indemnify the person who gives his name. In the most usual form of accommodation paper, that of an acceptance, the acceptor is a mere surety, the drawer is the real, principal debtor.

Now, suppose, as before, that A gets ten of his friends to

accommodate him with their names, and discounts these bills at his banker's, it is A's duty to provide funds to meet every one of these bills at maturity. There is, in fact, only one real principal debtor, and ten sureties. Now, these ten accommodation acceptors are probably ignorant of each other's proceedings. They only give their names on the express understanding that they are not to be called upon to meet the bill; and, accordingly, they make no provision to do so. If any one of them is called upon to meet his bill, he immediately has a legal remedy against the drawer. In the case of real bills, then, the bank would have ten persons, who would each take care to be in a position to meet his own engagement; in the case of accommodation paper, there is only one person to meet the engagements of ten. Furthermore, if one of ten real acceptors fails in his engagement, the bank can safely press the drawer; but if the drawer of the accommodation bill fails to meet one of the ten acceptances, and the bank suddenly discovers that it is an accommodation bill, and they are under large advances to the drawer, they dare not, for their own safety, press the acceptor, because he will, of course, have immediate recourse against his debtor, and the whole fabric will probably tumble down like a house of cards. Hence the chances of disaster are much greater when there is only one person to meet so many engagements than when there are so many, each bound to meet his own.

We see, then, that the real danger to a bank in being led into discounting accommodation paper is, that the position of principal and surety is reversed. They are deceived as to who the real debtor is, and who the real principal is, being precisely the reverse to what they appear to be, which makes a very great difference in the security to the holder of the bills. To advance money by way of cash credit, or by loan with security, is quite a different affair; because the bank then knows exactly what it is doing, and, as soon as anything occurs amiss, it knows the remedy to be adopted. Moreover, it never permits the advance to exceed a certain definite limit, but it never can tell to what length it may be inveigled into discounting accommodation paper, until some commercial reverse happens, when it may discover that its customer has been carrying on some great speculative operation, with capital borrowed from it alone.

Such appears to us to be the true explanation of the real danger of accommodation paper, and which was given in the first edition of this work, and we may say that its correctness has received the sanction of the high authority of Mr. Commissioner Holroyd, who quoted it in his judgment in the case of the great leather frauds, *Lawrence, Mortimer, and Schrader*, as appears in the *Standard*, March 7th, 1861.

To exhibit to our readers how this nefarious system is carried on, it will be advisable to give an outline of this celebrated case.

In the first place, in order to explain how such things are possible, we may, perhaps, call attention to a delusion which is very prevalent among uninformed writers, namely, that Bills of Exchange are paid in money. It is true that Bills of Exchange must always be expressed to be payable in money, but, as the reader may see in the preceding section, very few bills are really ever paid in money. When a customer has a banking account, the banker discounts his bills by writing down the amount to his credit, and this credit is called a DEPOSIT. The customer always pays his bills by drawing upon this credit, and when it gets low, the usual practice is for him to discount a fresh batch of bills. Thus, in ordinary times, the previous debts are always paid by creating new debts. No doubt, if the banker refuses to discount, the customer must meet his bills in money, but then no trader ever expects to do so. If his character be good, he counts upon discounts with his banker almost as a matter of right, and, therefore, to call upon him to meet his bills in money may oblige him to sell goods, &c., at a great sacrifice, or may cause his ruin.

However, it is always supposed that the bills discounted are good ones, that is, they could be paid in money if required. Thus, though in common practice very few bills are really paid in money, it is manifest that the whole stability of the Bank depends upon the last bills discounted being good ones.

Now, let us suppose that for some time a customer brings good bills to the Bank, and acquires a good character, and thus throws the banker off his guard: meeting some temporary embarrassment, perhaps, he is in difficulty to meet his bills. In order to get over this difficulty, perhaps he goes to some man of straw, and perhaps, for some trifling consideration, gets him to accept a bill, without having any property to meet it. He then takes this fraudulent bill to his banker. Thrown off his guard, perhaps, by his previous regularity, the unsuspecting banker buys this bill, and gives him a deposit for it. This deposit goes to pay the former bills. In the mean time, the rotten bill is falling due, and must be met. The acceptor has manifestly no means to meet it, and the only way to do so is to create some more of these rotten bills. Now, the drawer may be speculating in trade and losing money every day; but his bills must be met, and there is no other way of doing so but by constantly creating fresh rotten bills to meet the former ones. By this means, the customer may extract indefinite sums of money from his banker, and give him in return so many pieces of paper! Now, when times are prosperous and discounts are low, this system may go on for many years. But at last a commercial crisis comes. The money market becomes "tight." Bankers not only raise the rate of discount, but they refuse to discount so freely as formerly; they contract their issues. All these rotten bills are in the bank, and must be met. But, if the

bankers refuse to discount, they must be met with *money*. But all the property which the conspirators ever had may have been lost twenty times over, and, consequently, when the crisis comes, they have nothing to convert into money! Then comes the crash! Directly the banker refuses to pay his customer's bills by means of his own money, he wakes to the pleasant discovery that he has been dancing upon nothing! and finds that he has been paying all his customers' bills for many years with his own money!

This is the *rationale* of accommodation paper; and here we see how entirely it differs from real paper. Because, with real paper, and *bonâ fide* customers, though losses may come, still, directly the loss occurs, there is an end of it. But, with accommodation paper, the prospect of a loss is the very cause of a greater one being made, and so perpetually in an ever-widening circle, till at last the canker may eat into his assets to any amount almost. It is also clear that if a man, having got a good character, may sometimes do so much mischief to a single banker, the capacity for mischief is vastly increased if, from a high position and old standing, he is able to discount with several banks, for he is then able to diminish greatly the chances of detection.

In the case above mentioned, Laurence, Mortimer, and Co. were of very high position and of old standing in the commercial world. They were leather and hide factors, and the house was of above fifty years' standing. They bought hides on commission for tanners, and sold leather, and had leather consigned to them for sale. The hides were paid for by the tanners' acceptances of the factors' drafts at four months. In the course of business, they got connected with a considerable number of houses which were in a state of insolvency. To support these houses, and to extend their own operations, they entered into an enormous system of accommodation paper. They were in the habit of advancing money to their customers at five per cent., and then discounting these bills at their bankers at three per cent., thus making two per cent. by the transaction. When their customers often lost the money, their bills were renewed, or new ones created of arbitrary amounts, to conceal the loss. The house had an agency in Liverpool, which pursued exactly the same course. They set up people ostensibly in business for the purpose of drawing on them. And these "dummies" drew upon the house, and these cross acceptances were afloat to a large amount. This will be sufficient to give an idea of this complicated net-work of cross transactions between the house and its satellites. In the mean time, heavy losses were sustained in their trade transactions, which were, in fact, extracted out of the bankers by the fraudulent concoction of bills among the losers. The high standing of the house enabled

them to entangle no less than twenty-nine banks and discount houses in their meshes. At the time of the stoppage, the London houses had liabilities of £820,000, of which £620,000 consisted of these fraudulent bills. The Liverpool houses had liabilities of £158,750, out of which £130,000 were fraudulent. Such is one example of the mischief worked by this nefarious system.

A still more terrible example is the case of the Western Bank of Scotland, which is fully detailed in a subsequent chapter, which was in great part caused by the fraudulent proceedings of four houses. The cases there detailed shew to a what gigantic length these proceedings were carried. The Macdonalds had bills discounted to the amount of £408,716, drawn upon 124 acceptors, of whom at least 70 were men of straw, who made it a regular trade to accept bills for a small commission. In fact, they kept an agent in London for the express purpose of procuring accommodation acceptances.

From these accommodation bills to forged bills there is but one step. It is but a thin line of division between drawing upon a man who is notoriously utterly unable to pay, and drawing upon a person who does not exist at all, or forging an acceptance. In practical morality, and in its practical effects, there is none. Traders sometimes do not even take the trouble to get a beggar to write his name on their bills, but they invent one. The case of traders dealing with a number of small country connections affords facilities for such practices. They begin by establishing a good character for their bills. Their business gradually increases. Their connections gradually extend all over the Kingdom. The banker, satisfied with the regularity of the account, cannot take the trouble of sending down to inquire as to the acceptor of every bill. The circle gradually enlarges, until some fine morning the whole affair blows up. The ingenuity sometimes exercised by traders in carrying out such a system is absolutely marvellous.

It is in times of speculation in great commodities that accommodation paper is particularly rife. In a great failure of the harvest, when large importations are required, and it is expected that prices will rise very high, every corn merchant wants to be able to purchase as much as possible. But if no sales have taken place there can be no real trade bills. They, therefore, proceed to manufacture them in order to extract funds from bankers to speculate with. No banker in his senses would actually advance money for them to speculate with, with his eyes open. Nevertheless, they must have the funds from the bankers, and this they do by means of cross acceptances, which they go and discount with their bankers. They then, perhaps, buy a certain amount of corn, or any other goods, and many bankers will discount their bills, with the collateral security of

the bill of lading. And this they may repeat many times over, till the quantity of Credit created is something astonishing. In the Crimean war there was a great demand for shipping, and there was an enormous amount of accommodation bills manufactured by the Liverpool shipowners, and discounted all over the kingdom. The results were frightfully disastrous.

The insurmountable objection, therefore, to this species of paper, is the dangerous and boundless facility it affords for raising money for speculative purposes. And there is much reason to fear that this pernicious system prevails to a much greater extent than is generally supposed. The Legislature has imposed bounds upon the issue of notes by banks, but there is much greater reason that some attempt should be made to curb the extravagant magnitude to which this detestable practice has been developed. The Bank of England is strictly forbidden to issue a single £5 note of accommodation paper, and is it to be tolerated that any set of adventurers may set afloat many hundred thousand pounds worth of their accommodation paper?

To deal, however, legislatively with fictitious paper, is the most perplexing commercial problem of the day. The difficulty consists in determining what is really an accommodation bill. An accommodation bill is defined to be a bill to which the acceptor, drawer, or indorser, as the case may be, has put his name, *without consideration*, for the purpose of benefiting, or accommodating, some other party, who is to provide for the bill when due. But the whole difficulty turns upon the *consideration*. The consideration may be of many sorts, and does not by any means denote a sale of goods at the time. Moreover, a bill may be an accommodation bill at its creation, but, if any consideration be given during the period of its currency, it ceases to be an accommodation bill.

Moreover, the consideration may be of many sorts. If A draws a bill upon B, who accepts it for A's accommodation, for the express purpose of enabling him to go to a Bank and get money for it, that is a pure accommodation bill, and manifestly fraudulent. But if B draws an exactly similar bill at the same time on A, and A accepts it for the accommodation of B, then neither of the bills are accommodation bills.

To an unlearned reader, this may seem a monstrous doctrine. It is, nevertheless, firmly-established law. In the case of *Rolfe v. Custon* (2 H. Blackstone, p. 571), A and B being desirous to accommodate each other, each drew a bill upon the other, and accepted one in return, the two bills being precisely alike, in the date, sum of money, and times of payment—neither party having any effects of the other in his hand. The Court were clearly of opinion that the two bills were mutual engagements, constituting on each part a debt, the one being a consideration of the other. This doctrine was repeated and confirmed in the

case of *Cowley v. Dunlop* (7 T. R. 565), in which Grose, J., said, the instant the bills were exchanged each was indebted to the other in the sum which was the amount of their respective acceptances, for the counter acceptances were a good consideration to found a debt upon either side respectively. In the case of a single accommodation acceptance, said the learned judge, there is no debt to the acceptor; the debt accrues only by payment of the money. The acceptor, *quà acceptor*, can never be a creditor; his acceptance imports the admission of a debt from him to another, and when he has paid as acceptor, if he paid for any other person in consequence of any request from that other, he becomes a creditor, not on the face of the bill, but by a contract collateral to the bill. When two persons exchange acceptances, each becomes the debtor of the other upon his accepted bills. But when a man accepts without consideration, he is never a creditor of the person for whom he accepts till he pays; from that payment arises the debt; but when the acceptance was exchanged, the debt arises from these acceptances. This doctrine was repeated and confirmed in the cases of *Rose v. Sims* (1 B & Ad. 521), and *Buckler v. Bultivant* (3. East. 72), when it was adopted by the whole Court of King's Bench.

This doctrine shews how utterly hopeless it is to deal legislatively with accommodation paper. At least, they must be very poor rogues indeed who cannot manufacture any amount of real *bonâ fide* bills they please. Two ragsmuffins, who neither possess one sixpence in the world, have only to get a quire of paper—if they can pay for it. One engages to pay £1,000 to the order of the other. That would be an accommodation bill. But the second then engages to pay £1,000 to the order of the first. These are no longer accommodation bills! but given for a *consideration*. If two such bills are good, then two thousand, or any larger number, are equally good. We suspect that Bankers would look askance at such paper, but Westminster Hall declares them all to be good *bonâ fide* bills, given for a good *consideration*.

That such is the well-settled doctrine of Westminster Hall is beyond dispute. And perhaps it may ill become us to offer any suggestions on what has received the sanction of the Courts for so long a time. Nevertheless, at the hazard of being thought presumptuous, we may make a few remarks. When we search for the foundation of the doctrine, we find it to be this:—That by giving their cross acceptances the parties become *indebted* to each other. That by these cross acceptances mutual *debts* are created. But is this doctrine quite impeccable? It is admitted that when B accepts a pure accommodation bill for A, no debt is created. It is nothing whatever but a piece of waste paper between the parties. Of course, a similar bill upon A would be an absolute nothing as well. Now the question is this—It

being admitted that these two bills *separately* are absolute nothings, how can it be that when created *together* they spring into existence as Debts?—a debt being, as we know, valuable property. It is a doctrine very hard to understand.

In a real bill the drawer may, of course, sue the acceptor; but in an accommodation bill he cannot. Suppose A draws a pure accommodation bill on B for £100 at three months. Then, of course, he cannot sue him on it. But suppose, one month after the first bill, B draws a bill of £100 at six months on A, without any consideration whatever but his previous acceptance. Then, according to the doctrine stated above, the first bill, which we may suppose never to have quitted the drawer's possession, immediately becomes a real bill, and A may sue B if his acceptance be unpaid. Did such a case as this ever occur? And could A recover under such circumstances? And yet that is the consequence that must necessarily follow, if it be true that mutual accommodation acceptances constitute mutual debts between the parties.

We venture, with the greatest deference, to think that a fallacy lurks at the bottom of the doctrine. An accommodation acceptance, in the hands of the drawer, is simply *nil*. Directly he passes it away, it becomes, in effect, the joint promissory note of the two parties. The acceptor cannot incur a liability without the drawer at the same time incurring an equal one. To suppose that one joint promissory note of two parties should be a *consideration*, for a second promissory note of the same parties, seems a very strange idea. When a man is already a coöbligant as drawer on a bill, to suppose he can make that bill a good consideration for becoming coöbligant as acceptor on another bill with the same person, seems a most unaccountable doctrine. To suppose that a man can make a liability he has already incurred a *consideration* for incurring another seems most extraordinary.

A consideration in commerce means something *external*. It is a *security* for incurring a debt. If I buy another man's debt, that is a consideration, or *security*, for creating one of my own. If the Government has created a debt, as the public funds, or Exchequer bills, that may be a good consideration, or security, for the Bank of England to create notes in exchange. So a banker creates a debt, either by notes, or a deposit, in exchange for the bills of his customer. In these cases there is an exchange of independent securities. Neither party are coöbligants, or liable with the other. But how can a liability a man has already incurred be a *consideration*, or *security*, for incurring a second one? Suppose a bank issues £10,000 in notes. Is the previous issue to be a security for issuing a second amount? If this be a good consideration, or security, then, indeed, the philosopher's stone is, at last, discovered! There is no need to cross

half the globe in search of an El Dorado. All the treasures of California and Australia are dust in the balance compared to this. Only let two men provide themselves with a slip of paper and shut themselves up in a room, and, in the twinkling of an eye, they can make themselves richer than ever Solomon was.

If it were possible for each party to incur a liability on account of the other, separately, and without himself being also bound, it might alter the case. But, in accommodation paper, neither party incurs an obligation without the other being also equally liable. A second bill is, therefore, nothing more than a dilatation of the first bubble; and to suppose that it can be a consideration—a security for the first bubble—to swell it to twice its previous dimensions, is contrary to the usual experience of bubbles.

We have felt bound to lay these observations before our readers. As we have already warned them that they are contrary to the established doctrine of Westminster Hall, they must, of course, be held to be fallacious; at least, the probabilities of their being so are very great indeed. But it may, perhaps, exercise the ingenuity of our readers to point out their fallacy. At all events, what we have said, right or wrong, may serve to fix the attention of our readers upon the doctrine under discussion; because, however it may be regarded, it is one of the extremest subtlety. It is one which sanctions a practice which, without its sanction, would appear to any plain person to be a gross fraud; and it is this practice which has caused incalculable disasters in commerce, and, while it is held to be good, entirely precludes the possibility of dealing legislatively with so great a curse.

On the Extinction of Credit.

23. In the preceding sections we have examined the various operations out of which credit is generated, and the transcendent functions it performs in production—it being, in fact, the grand productive, or circulating power, of modern times. We have now to consider the various modes in which it is extinguished. Because it is by its very nature, and as appears by its very name, transitory, and is created always with the express purpose of being destroyed. It is when it cannot be destroyed that it produces such dire effects. It is UNEXTINGUISHED CREDIT which produces those terrible monetary cataclysms, which shake nations to their foundations, scattering ruin and misery among societies. The inability of credit-shops to extinguish the credit they have created, commonly called the failures of banks, are, perhaps, among the most terrible social calamities of modern times.

We have seen that, in commerce, bills are created by the transfer of commodities, a fresh one being created at each transfer. And this debt becomes itself a transferable com-

modity, and is capable of circulating an indefinite number of times, like money. This debt, or promise to pay, might be made payable in anything the parties pleased—coin, wine, oil, &c., &c.—and, in some countries, is so. But in this country instruments of credit are always expressed to be payable in *money*. But we have already seen that a debt is only a lower form of money, and hence there are four different ways in which credit may be extinguished—

1. *By Payment in Money.*
2. *By Exchanging one Debt for another.*
3. *By the Creation of fresh Debt to discharge the old.*
4. *Where parties are mutually indebted to each other, each being Creditor of, and each Debtor to, the other, they may make a Mutual Release of Debts.*

The different proportions in which these various methods are employed to extinguish credit, have very great effect in determining what quantity of specie is required to carry on the commerce of a country.

Before the establishment of banks, credit could only in general be extinguished by payment in money. But, of course, the same quantity of money would extinguish an infinite series of bills; in fact, it is always by the *circulation* of money that bills are extinguished. Bills are always generated by the circulation of commodities, and always extinguished by the circulation of money. Each manufacturer, or merchant, would sell to a number of wholesale dealers, who would each buy from a number of manufacturers, or merchants. They would then each sell to a number of customers, or consumers. Many of these customers would pay in ready money, or, at least, they must all do so ultimately, so that the retail dealers would always have a constant stream of ready money coming in to discharge their bills, as they fell due in succession.

Now, as each wholesale dealer sells to a number of retail dealers, who would always have a stream of ready money coming in to pay their bills, each wholesale dealer would always have a stream of ready money coming in from many sources to enable him to discharge his various bills to the merchants and manufacturers. In a similar manner, the merchants and manufacturers would always have a stream of money coming in from a multitude of sources to discharge their bills to foreigners and producers of raw materials. But, of course, each of them would spend a certain portion of their profits as revenue, that is, they would be customers of the retail dealers. And, consequently, by these means, the identical pieces of money would perform a perpetual circulation among the various classes of society. Each person collecting a multitude of little sums into one reservoir, as it were, and then discharging the aggregate so collected into a multitude of other channels. And so on *ad infinitum*.

Now, the least consideration will show that the quantity of money being exactly the same, its circulation may be extremely languid, moderately rapid, or extremely rapid. And as in commerce, assumed to be sound, profits arise out of exchanges, it is clear, that within certain limits, the greater the profits will be, according as the circulation of money is more rapid. Moreover, we see this, that the quantity of credit generated, does not depend simply on the quantity of money, but on its quantity multiplied into the velocity of its circulation.

We thus see how the fundamental distinction between bills of lading and bills of exchange is illustrated, which is at the root of the currency question. The bill of lading is not generated by the transfer of the *Property* of the goods, but only by a transfer of *Possession*; and, when the possession is given up, the bill of lading is cancelled. Thus, the bill of lading is only extinguished by the delivery of the very goods it represents. But bills of exchange are generated by the transfer of the *property* of goods, and are absolutely severed from them, and circulate independently in commerce, and are exchangeable for money at a given time. Bills of Lading can never exceed in quantity the goods they represent; instruments of Credit cannot exceed the quantity of the Circulation of Money. Be the circulation of goods fast or slow, the quantity of bills of lading cannot vary, but the quantity of credit varies with the circulation of money, so that if the circulation be increased tenfold, credit may always be, and is almost necessarily increased tenfold.

The preceding considerations shew that Credit is limited by the Circulation of money. It is clear, therefore, that if some substitute for money be invented, or, if by improved methods, a less quantity of Money can do the same duty as a greater quantity, the limits of Credit may be proportionably extended. And new methods of extinguishing credit would come into existence. This is done to an enormous extent by the institution of Banks. We have fully described in this section, and that on the CLEARING HOUSE, how debts are extinguished by the creation of new debts, and partly by the exchange, or cancellation, of debts by the Bankers *inter se*. The extension of business, by the means of erecting a vast superstructure of credit upon a basis of bullion, is something almost incredible. It is probably quite safe to say, that not over five per cent. of commercial transactions are ever settled in money. Such is the proportion of *Debts*, or *Negative Quantities*, to Money in Commerce.

On the Limits of Credit.

24. In the preceding sections we have endeavoured to lay before our readers an exposition of the actual mechanism of the system of Credit, and shew its powerful effects as a productive agent.

Credit, in fact, is to money what steam is to water. And, like that power, while its use within proper limits is one of the most beneficent inventions ever devised by the ingenuity of man, its misuse by unskilful hands leads to the most fearful calamities. It is chiefly the abuse of credit by which that *over-production* is brought about, which causes those terrible catastrophes called Commercial Crises. It is, therefore, essential to ascertain its limits.

The true limits of Credit may be seen from the etymology of the word. Because all Credit is a *promise to pay something in future*. And that "something," whatever it be, is the VALUE of the promise. That something need not necessarily be money. It is perfectly possible that it should be anything else. The practice of interest, or usury, was in force before the invention of money. It might be a promise to do something. As an example of this, we may take a postage stamp, which is a promise by the State to carry a letter. And this service is the value of the stamp. Now, it is quite clear, and, to shew it, we have only to appeal to every one's experience, that a postage stamp is a valuable thing. It passes currently as small change. Now, people take postage stamps as equivalent to pence, because they often wish to send letters by the post. The recent regulations that stamps shall be convertible into money at any post office, makes them in all respects part of the currency of the country. They are, in fact, 1d. notes.

Now, the only real difficulty in the case, is to observe that the naked "promise to pay" is independent exchangeable property, quite distinct from the thing itself, and it may circulate, in commerce, just the same as the thing itself. This may surprise some readers at first, but, to shew its truth, they need only appeal to their own daily experience, where they see bank notes, cheques, and bills of exchange, circulating to the extent of hundreds of millions, and performing all the functions of money. We shall see below, that J. B. Say, whose doctrines of credit we shall examine in the next section, fully acknowledges that an instrument of credit has an actual value, and may perform the duties of money.

But, of course, it is quite manifest that the VALUE of the promise is the THING *itself*, and, consequently, if the thing itself fails, the promise has lost its *value*. This, consideration, therefore, at once indicates the limit of credit. Assuming credit to be, what it is in its best known form in this country, the promise to pay money, it is quite clear that every future payment has a *present value*. Consequently, whenever the possession of money at any time is actually certain, the Right to receive it is an exchangeable Property, which may be bought and sold.

Commercial credit, however, does not rest upon so solid a basis as the *certainty* of being in possession of money, for then

it would be as safe as money itself, and losses would be unknown. It is based upon the expectation of receiving money at a certain time. A trader buys goods, and gives his promise to pay money, upon the reasonable expectation that he will be able to sell them for money before the bill becomes due; or, at least, that he will be in the possession of money before that time. That is, he *produces*, or brings and offers them for sale, in the hope that they will be *consumed*, or bought. If he brings forward for sale more of any species of goods than is suitable to the circumstances of the time, so that they cannot be sold at all, or if they are obliged to be sold at a lower price than they cost, that is *over-production*. He must then pay his bills out of any other funds at his disposal, or sell other property to meet them, and, if he cannot do so, he is ruined.

In times of great speculation and great fluctuations of prices, there is an exceeding danger of over-production by means of credit, especially by that abuse of it called Accommodation Paper, which we have described. A new channel of trade is opened, perhaps, and the first to take advantage of it, make great profits. Multitudes of others, hearing of these great profits, rush in, all dealing on credit. The market is overstocked, and prices tumble down, and the credit created to carry on these operations cannot be redeemed. Not only are the speculators in many cases ruined, but also frequently the banks which created credit by discounting these bills.

The institution of Banks and Bankers, who create currency by means of their Credit, either in the form of notes, or deposits, gives a great extension to the limits of Credit. But, nevertheless, the *principle* of the limit remains the same. The increased quantity of currency they can issue by means of their Credit, enables them to lower the rate of discount. These banking debts take the place of money, and serve the purposes of money for all internal transactions. When a banker has created these debts by buying commercial debts, those who are indebted to the banker must obtain a sufficiency of money, or of other bankers' notes, or of the banker's own notes, to discharge their debt. And if this be done the Credit has been sound; payment in all these forms, as we have seen already, being absolutely equivalent. Hence we see that Credit is never excessive, no matter what its absolute quantity be, so long as it always returns into itself.

It is a matter of considerable interest to discover what are the proportions which credit and money bear to each other in modern commerce. The difficulties, however, which prevent private inquirers arriving at any reliable information, are very great, and those opportunities which are presented by Parliamentary inquiries into Commercial Crises are very rarely made use of for any but their immediate purpose. In the

Report, however, of the Committee of the House of Commons on the Commercial Crisis of 1857, there occurs a very interesting statement made by Mr. Robert Slater, the managing partner of the great house of Morrison, Dillon, and Co. Having analysed the operations of the house for the year 1856, he gave in the following statement, as showing the proportions in which each million of payments and receipts were made in money, bank notes, and other instruments of credit:—

RECEIPTS.		
	£	£
In Bankers' Drafts and Mercantile Bills of Exchange, payable after date.....	533,596	
In Cheques on Bankers, &c., payable on demand	357,715	
In Country Bankers' Notes	9,627	
	—	900,938
In Bank of England Notes	68,554	
In Gold	28,089	
In Silver and Copper.....	1,486	
In Post Office Orders	933	
	—	99,062
		<u>£1,000,000</u>
PAYMENTS.		
	£	£
By Bills of Exchange, payable after date..	302,674	
By Cheques on London Bankers	663,672	
	—	966,346
By Bank of England Notes	22,743	
By Gold	9,427	
By Silver and Copper	1,484	
	—	33,654
		<u>£1,000,000</u>

Here we have it shewn, that in this great house, which there is no reason to suppose we may not consider a fair representative of commerce in general, it appears that in receipts, gold and silver only entered to the extent of 3 per cent., and Bank of England notes to the amount of less than 7 per cent., the remaining 90 per cent. being entirely in credit. Of the payments, gold and silver were only 1 per cent., and bank notes 2 per cent., the remaining 97 per cent. being effected by pure credit. In Scotland specie enters even in a far less degree into payments. This will give some idea of the stupendous power of Credit in this country.

A Banker, of course, can only maintain his credit by being always supposed to be able to cash any reasonable amount of his liabilities on demand. In order to do this, he must always maintain a certain proportion between his liabilities and his cash. If, therefore, an excessive number of debts be pressed on him for sale, the same result must follow as when an over-abundant supply of any other article is offered for sale in the market. They must fall in value, that is, the rate of discount must be raised. By this means, if done in due time, over-production may often be arrested, because the difference of 1 per cent. in the rate of discount is sufficient to curb a considerable amount of enterprise. If that is not sufficient, still more stringent measures must be adopted until it is effectual. But the method is infallible; by raising the rate of discount sufficiently, nearly all production might be brought to a standstill. It is the neglect of this precautionary measure during an excessive generation of Credit, which drives bullion out of the country, that has led to several Commercial Crises.

SUCH IS THE GRAND THEORY OF CREDIT.

SECTION V.

EXAMINATION OF THE OPINIONS OF MODERN ECONOMISTS ON CREDIT AND CURRENCY.

25. We have now given the exposition of the actual mechanism of the system of Credit, and shewn how it performs the function of money; and how it may be used as Capital, exactly in the same manner that money is.

Up to the beginning of the present century, we may say that there was no difference of opinion on the subject of Credit and Currency. All writers previously to that time, seeing and feeling that Credit performed the same function as money, classed Credit under the title of Capital, and no one ever doubted that all forms of Credit came under the category of Currency, or Circulating Medium.

Every one knows, however, that in recent times the most unsparing ridicule has been poured upon the doctrine that Credit is Capital, and about the same period strong differences of opinion began to be held as to what should be deemed Currency; and what not.

It is now absolutely incumbent upon us to examine these conflicting opinions, to lay them before our readers, and endeavour to arrive at a definite conclusion on the subject. Though the subject may be somewhat dry, it is one of the most important consequence, because legislation deeply affecting the whole commercial community of this country, and indeed of the whole world, is based upon a peculiar definition of Currency, and upon a peculiar theory of Currency. No time, therefore, really employed in arriving at an accurate decision on a subject of such overwhelming importance to such gigantic interests is wasted.

Our readers may take it for granted that, up to the time of the French writer, J. B. Say, the whole world believed that Credit was Capital, not to mention a crowd of others, Demosthenes, Daniel Webster, Hamilton, Adam Smith, Ricardo, all declared that credit was capital. At last J. B. Say made the wonderful discovery that this was all a delusion, and that all writers, from Demosthenes to Ricardo, were such dolts as to maintain that the same thing can be in two places at once, when they said that Credit was Capital.

26. Political Economy owed its origin as a Science in modern times to the terrible desolation and ruin, caused in France by the wars of Louis XIV., and the Mississippi Scheme of John Law.

Towards the close of the 17th century, a strong commercial spirit seized on the English nation. Wearied with politics and polemics, they began to turn their attention more to the practical business of this world, and commercial enterprise.

At this time several writers, seeing the immense benefit which the Dutch derived from their bills of debt, wished to introduce them into England, but the inflexible rule of the common law that *choses in action* could not be transferred, presented for a long time an insurmountable obstacle to such a plan. Soon after the Restoration, however, the extension of commerce attracted a great deal of attention to the subject of Credit, and multitudes of pamphlets were published advocating the institution of public banks. The notes which were issued by the private bankers of London shewed the utility and the convenience of the invention. At last, after several attempts, the Bank of England was founded in 1694, with the express intention, as was very clearly stated by its founders, of *increasing* the quantity of the currency.

All these projects, however, were for the purpose of augmenting *Credit*, that is, paper currency convertible into specie, and, therefore, of the value of specie. But many projectors, not satisfied with the increase of the currency caused by Credit, began to devise schemes for creating paper *money*, that is, paper notes not convertible into specie, a thing of a totally different nature, though often confounded with it. Among these were Chamberlain, Asgill, Briscoe, and others, who wished to found an *inconvertible* paper money, based upon land. The most famous, however, of the advocates of this plan was John Law, and as his name has acquired the greatest notoriety from his connection with the Mississippi Scheme, we may confine our attention chiefly to him.

Most persons have no other conception of John Law than as the deviser of a scheme which produced a great financial catastrophe, somewhat similar to the South Sea bubble. The latter was a pure swindle and a fraud; and, as both schemes produced a great catastrophe about the same period, most persons jumble up the two events, and class the projectors of both enterprises under a common name.

This, however, is a very grievous error indeed. Law was neither a swindler nor a rogue. Even his enemies, and those persons who were opposed to his system, bear ample testimony to his personal integrity and sincerity, and, even after the collapse of the system, the higher ranks of the country treated him with the greatest respect. The fact is, that his writings are divided into two distinct classes — those upon Banking and *Paper Credit*, and those upon *Paper Money*. His writings on Banking and Paper Credit, were originally written in French, and presented to the Regent Orléans, and were never, that we know of, trans-

lated into English. His treatise on *Paper Money* was originally published in English, at Edinburgh, in 1705.

Nothing can be better and sounder than his writings on Banking and Paper Credit. They were, by far, the best exposition of the subject that had then been published; in fact, they are some of the best that exist to the present day. But the theory of PAPER MONEY which he adopted is a totally distinct thing, and has no connection with his doctrines of CREDIT. It would be out of place to examine his theory of money here. That is fully done in a future chapter; but we may observe that his career was, like his writings, divided into two distinct operations. So long as he confined his operations to legitimate banking, nothing could be more successful. There was scarcely ever such a marvellous restoration of prosperity in so short a space of time as by the institution of Law's Bank. And well would it have been for him and the country if he had stopped there. It was only when he put into practice his theory of paper money that the mischief was produced. But this does not prove that he was a rogue; it only shews that his theory of money was erroneous. It is, nevertheless, one that has innumerable admirers at the present day, and to shew its fallacy requires a thorough knowledge of the most fundamental subtleties of Political Economy.

We have been obliged to say this much here as a preface to quoting anything from Law regarding Credit, which must be carefully distinguished, as we have said above, from his doctrines on Money. His writings on Banking and Credit are contained in ten *Mémoires sur les Banques*, fifteen *Lettres sur les Banques* addressed to the Regent Orléans, and some letters on the system, all in French, published in the first volume of Guillaumin's Collection of Modern Economists.

We shall now show that Law maintained that Credit was equivalent to an increase of money. In the first *Mémoire*, p. 521 of the volume just mentioned, Law says:—"Les Crédits sont nécessaires et utiles; ils font les mêmes effets et le même bien dans le commerce comme si la quantité de la monnaie était augmentée." He points out the advantage England derived from the institution of Credit during the war with France, and being in great difficulty from want of money—"s'est avisée d'introduire des Crédits, qui ont suppléé aux espèces, et soutenu ses manufactures, et son commerce qui, sans ce secours, auraient été ruinées par de si longues guerres qui ont causé un grand transport d'espèces, et sous lesquelles l'Angleterre aurait succombé sans les Crédits dont elle s'est bien servie. Les Crédits ont non seulement suppléé aux espèces qui étaient transportées mais ont servi au delà, et ont augmenté ses manufactures et son commerce, même pendant la guerre." He then says:—"La Banque est un espèce de Crédit," and, speaking of the Bank of England—"mais

le bien que la banque fait en augmentant le quantité de la monnaie." He shews, too, that its shares being negotiable, in many cases served the purpose of money. At p. 545, he says:—"La Banque d'Angleterre, outre ces commodités qu'elle donne aux négociants pour faciliter les payments, produit une plus forte circulation, et fait le même effet que si la monnaie d'Angleterre était considérablement augmentée, comme je l'ai déjà remarqué." And at p. 554:—"Done, l'introduction d'un Crédit, dans le commerce augmentait la quantité de la monnaie réellement, et faisant le même effet que si elle était augmentée, par une plus forte circulation que ce Crédit procure, doit diminuer le prix ou intérêt de l'argent." At p. 560:—"La circulation des billets de la banque dans les provinces ferait le même effet qui si la quantité des espèces était considérablement augmentée, et par là soutiendrait et augmenterait l'agriculture et les manufactures."

Law also saw, of course, that these notes, &c., were of the value of money, because they were exchangeable for money—"ces billets étant supposés au moins aussi bien que l'argent puisqu'on les peut convertir en espèces à volonté."

In the first *Lettre sur les Banques*, he says:—"Si l'Espagne avait cédé les Indes aux Anglais, cette nation n'aurait pas tant profité de ce commerce qu'elle a profité de son crédit."

"Avant le mort de Charles II, roi d'Espagne, le commerce des Indes a fourni aux Anglais environ 25 millions par année en matières d'argent; de cela une partie était consommée, une partie payait une balance due alors à la France, une partie était transportée par la Compagnie des Indes Orientales; il n'en restait qu'environ 8 millions; ainsi, pour augmenter la monnaie d'Angleterre de 400 millions, il aurait fallu 50 années d'un commerce bien réglé et sans interruption, en donnant le produit et manufactures du pays en échange de ces matières."

"Par l'introduction du crédit, l'Angleterre a augmenté sa monnaie au-delà de cette somme, sans avoir donné en échange aucune valeur en marchandise, car le crédit qui circule dans la ville de Londres seule, monte à plus que les espèces monnayées de la France et de l'Angleterre. Ainsi il ne doit pas paraître extraordinaire que la monnaie soit si abondante à Londres, les espèces ne faisant pas la cinquième partie de ce que le crédit fait."

"Le revenu de cette augmentation de la monnaie produit annuellement plus que double de ce que le commerce des Indes aurait produit, par une augmentation de l'industrie et des manufactures de ce royaume, qui ont été portées si loin qu'elles fournissent la plus grande partie de l'Europe."

These extracts are sufficient to show that Law knew and maintained that credit was separate and independent exchangeable property, which was cumulate property over and above specie and commodities. He never falls into that extraordinary confusion of idea of believing that Credit is the transfer of

Capital. He sees, as we have said above, that Credit is to be *added* to the mass of other exchangeable property (§ 3). So also Melon, a contemporary writer, in his *Essai Politique sur le Commerce*, in the same volume, already mentioned, p. 757, commenting on the political arithmetic of Sir W. Petty, says:—"Au calcul des hommes il faut ajouter le calcul de ce qu'ils valent par leur travail.

"Au calcul des valeurs numériques, il faut *ajouter* le crédit courant du négociant, et son crédit possible."

27. That astounding confusion of ideas which prevails through so many modern writers, that Credit is the *transfer* of something, began with Turgot. When he was at College, and only 22 years old, he began to reflect on Law's system, and addressed a letter on the subject to the Abbé de Cicé, *Sur le papier suppléé à la monnaie*. (*Œuvres de Turgot*. Vol. I., p. 94. Edit. Guillaumin.) This letter contains an expression which has been the key-note of a fallacy which has been sedulously propagated from that day to this, by a long series of writers both in France and in England. He says:—"En un mot tout Crédit est un emprunt, et a un rapport essentiel à son remboursement." Here we see the first statement of that gross confusion of ideas on the subject of Credit, which is so prevalent. Preceding writers had always seen that Credit was a species of exchangeable property, which served the purpose of money; but Turgot makes Credit to be an *operation*. To say that Credit is a *loan*, is as gross a misconception of the nature of the thing, as to say that a guinea is the *transfer* of a book! Moreover, the word loan is ambiguous. We have fully explained the nature of this ambiguity in § 4, where we have shewn that in English there is but one word for the two Latin ones *mutuum* and *commodum*, in the distinction between which lies one of the greatest subtleties in Political Economy. An operation on Credit is always an exchange, where the property of the thing "lent" always passes to the "borrower," and the "lender" receives in return the right, or property, to demand back an equivalent to the thing "lent" at a future time. Turgot, rightly enough, says that every Credit implies a future repayment. That is true; Credit means the Right to a future Payment. And it is precisely because this Right is exchangeable for something at a future period, that it has value. And it may be bought and sold like any other species of property. We shall see afterwards that J. B. Say, whose doctrines we shall have to examine, fully acknowledges this.

The Opinion of Adam Smith on the Nature of Credit and Currency.

28. The controversies about Credit, of which the germ is

contained in the extract from Turgot, which we have given above, did not commence till after Adam Smith's time. He, therefore, did not discuss them. Though his doctrines on the powers of Credit are self-contradictory, he is perfectly consistent with himself as to the *nature* of Credit. He uniformly considers Credit to be independent exchangeable property, and we shall now show that he classes it under CAPITAL.

In the first place, we have shewn in the first chapter, that Smith, in a passage which has been most unaccountably overlooked by nearly every writer, expressly enumerates the useful and acquired abilities of the inhabitants of a country as part of its Wealth, or fixed Capital. Now, as a man's Credit depends purely upon the belief in his character and abilities, it is manifestly, according to the very definition, Capital to him, by means of which he can make a profit. Thus Smith says, Book i., c. x. :—
 “In great towns trade can be extended as stock increases, and the CREDIT of a frugal and thriving man increases much faster than his stock. His trade is extended in proportion to the amount of BORN, and the sum or amount of his profits is in proportion to the extent of his trade, and his annual accumulation in proportion to the amount of his profits.” Hence we see that Smith places Credit on exactly the same footing as stock, and, as he makes a profit by it in the same way as by Stock, it is clearly capital to him as well as his Stock.

But we shall now shew that Smith expressly includes Credit under the term Capital, and says that it produces exactly the same effects as money.

Under the term fixed Capital he includes the abilities of the people upon which Credit depends. Under the term floating Capital he includes four sorts. The first of these, he says, is “The *money* by means of which all the other three are circulated and distributed to their proper consumers.”

In B. ii, c. ii., he says :—“Money, therefore, the great wheel of circulation, the great instrument of commerce, like all other instruments of trade, though it makes a part, and a very valuable part, of the *Capital*, &c.”

Thus we see that Smith expressly includes the wheel of circulation, or, according to a name it has received since his day, the “circulating medium,” as part of the Capital of the country.

He then says that every saving in the expense of collecting and supporting that part of the circulating capital, which consists of money, is an increase of the neat revenue of the country.

He says, then, “The substitution of paper in the room of gold and silver money, replaces a very expensive instrument of commerce with one very much less costly, and sometimes equally convenient. Circulation comes to be carried on by a new wheel, which it costs less both to erect and to maintain than the old one.

“There are several different sorts of paper money, but the

circulating notes of banks and bankers are the species which is best known, and which seem best adapted for this purpose."

Thus we see that Smith expressly includes all forms of paper credit under the term money, or circulating power, which he has already said is Capital.

After saying that if people have confidence in a banker, his notes come to have the same currency as gold and silver, because people believe that money can always be had for them, he says: "When a particular banker lends among his customers his own promissory notes to the extent, we shall suppose, of £100,000, as these notes serve all the purposes of money, his debtors pay him the same interest as if he had lent them so much money. This interest is the source of his gain. Though some of these notes are continually coming back on him for payment, part of them continue to circulate for months and years together. Though he has generally in circulation, therefore, notes to the extent of £100,000, twenty thousand in gold and silver may frequently be a sufficient provision for answering occasional demands. By this operation, therefore, £20,000 in gold and silver perform all the functions which £100,000 could otherwise have performed. The same exchanges may be made, the same quantity of consumable goods may be circulated and distributed to their proper consumers, by means of his promissory notes to the value of £100,000, as by an equal value of gold and silver money."

Thus we see that Smith says that a banker may derive exactly the same profit from the use of his credit that he would from actual money, and, therefore, it is capital to him. And he shews that it has exactly the same effects on the country as so much money, and, therefore, it is equally capital to the country.

He also supposes a case in which the circulating money of a country should be £1,000,000 at any time. Different banks and bankers issued paper to an equal amount, reserving £200,000 to meet the demand for specie. "There would remain, therefore, in circulation £800,000 in gold and silver, and £1,000,000 of bank notes, or £1,800,000 of paper and money together." Thus we see that Smith classes paper credit as independent exchangeable property, just on the same footing as gold and silver. He then says that such an emission of paper will release a quantity of the circulating money, and enable it to be exported to purchase foreign goods, and to be invested in foreign trade, and he says:—"Whatever profits they make will be an addition to the neat revenue of their own country. It is like a new fund created for carrying on a new trade, domestic business being now transacted with paper, and the gold and silver being converted into a fund for this new trade." He says, also, that it may be applied to purchase an additional stock of materials, tools, and provisions, in order to maintain and employ an additional number of

industrious people, who reproduce with a profit the value of their annual consumption. * * * *

“When paper is substituted in the room of gold and silver money, the quantity of the materials, tools, and maintenance which the whole circulating capital can supply, may be increased by the whole value of gold and silver, which used to be employed in purchasing them. * * * *

“When, therefore, by the substitution of paper the gold and silver, necessary for circulation, is reduced to, perhaps, a fifth part of the former quantity, if the value only of the greater part of the other four-fifths be added to the funds which are destined for the maintenance of industry, it must make a very considerable addition to the quantity of their industry, and, consequently, to the value of the annual produce of land and labour.

In speaking of bankers, he says:—“It is chiefly by discounting bills of exchange, that is, by advancing *money* upon them before they are due, that the great part of banks and bankers issue their *promissory notes*. * * * The banker who advances to the merchants, whose bill he discounts, not gold and silver, but his own promissory notes, has the advantage of being able to discount to a greater amount, by the whole value of his promissory notes, which he finds by experience are commonly in circulation, he is thereby enabled to make his clear gain of interest on so much a larger sum. * * *

“The banks, when their customers apply to them for *money*, generally advance it to them in their own *promissory notes*. These the merchants pay away to the manufacturers for goods, the manufacturers to the farmers for materials and provisions, the farmers to their landlords for rent, the landlords repay them to the merchants for the conveniences and luxuries with which they supply them, and the merchants again return them to the bank in order to balance their cash accounts, or to replace what they may have borrowed from them; and thus almost the whole money business of the country is transacted by means of them.”

Thus Smith clearly places Paper Credit on exactly the same footing as money. He shewed that traders made a profit by their credit, and in the last-mentioned passages he shews how bankers make a profit by their credit, and how, in process of time, the greater part of the circulation of the country is carried on by Credit. In B. ii., c. iv., he says:—“The stock which is lent at interest is always considered as a CAPITAL by the lender.” Then a little after—“Almost all loans at interest are made in money, either of paper or of gold and silver.” * * * “The quantity of *stock*, therefore, or, as it is commonly expressed, of *money*, which can be lent at interest in any country, is not regulated by the value of the *money*, whether *paper* or coin, &c.”

Thus Smith expressly classes Paper Credit under the term Capital, and, therefore, it must be *Productive*. It has puzzled

many persons, however, to conceive how Credit can be *Productive*. This, of course, manifestly turns on the meaning of *Productive*. We have fully shewn, in the first chapter, that Smith says that there are four ways in which Capital may be employed productively (B. ii., c. v.)—1st, in procuring rude produce; 2ndly, in manufacturing it; 3rdly, in transporting it from place to place; 4thly, in dividing it into small parcels to suit the convenience of customers. Hence we see that he says Capital may be *productively* employed in buying and selling. Now, of course, it will be at once seen that Credit is employed in buying and selling. Smith says that the labour of wholesale and retail dealers is productive because it adds to the value of the commodities they deal in. But persons can buy and sell with Credit equally well as with money. Hence their labour is just as much *productive* in the one case as in the other. And here we see at last the root of the difficulty which many persons have in conceiving that Credit is productive capital, because they evidently mean by production an increase of *quantity*. But the fact is that *circulation* is one species of production, and hence the circulating power is Capital. Now, the circulating medium, as every one knows, is Money and Credit. As Smith says (B. iii., c. i.):—"The great commerce of every civilized society is that carried on between the inhabitants of the town and those of the country. It consists in the exchange of rude for manufactured produce, either immediately, or by the intervention of money, or of *some sort of paper* which represents money."

The extracts which we have laid before our readers are quite sufficient to shew that Adam Smith never committed the extraordinary error of supposing that Credit is the transfer of Capital, as is so common at present. It is quite evident that he always knew that Credit is independent, exchangeable property, and that it is PRODUCTIVE CAPITAL.

Self-contradictions of Jean Baptiste Say, on the subject of Credit.

29. We now have to examine the opinions of J. B. Say respecting Credit, as it is he who, following on the erroneous notion of Turgot, invented the phrase which so many unthinking writers have echoed from that day to this, that those who consider Credit to be Capital, maintain that the same thing can be in two places at once!

Credit, as we have shewn in the preceding sections of this treatise, is a species of incorporeal property, and was always well understood to be so, until Turgot originated the erroneous notion that it was a loan, or the *transfer* of something. The question of Credit, therefore, involves that of the admission of incorporeal property into Political Economy.

We shall find that all this confusion arises from Say never

having carefully thought out the fundamental conceptions of the science, and his incredible self-contradictions on almost every one. Say's name stands so high in the subject, and his doctrine has been chorused by such a multitude of writers, and the matter is in itself of really such transcendent importance, that we must give some space to a thorough investigation of his views. We must, therefore, inquire into his notions of *Wealth*, *Value*, *Capital*, and *Credit*.

On Say's definition of Wealth.

It is very commonly supposed that Say was the first writer to introduce immaterial products into Political Economy. This, however, we have shewn to be an error, as Adam Smith expressly enumerates the "acquired and useful abilities of the inhabitants," as part of the Wealth of the society. We have also shewn that Smith admits paper currency, or Credit, to be exchangeable property. Thus recognizing the existence of *Three* species of Wealth. Say does exactly the same, and he also enumerates several other species of incorporeal property besides credit.

And in his *Cours Complet d'Economie Politique*, Part i., c. i., Vol. i., p. 67, he says:—"La possession exclusive qui, au milieu d'une nombreuse réunion d'hommes, distingue nettement la propriété d'une autre personne, fait que dans l'usage commun, cette sorte de biens est la seule à laquelle on donne le nom de RICHESSE. * * C'est là que viennent se ranger non-seulement les choses capables de satisfaire directement les besoins de l'homme, tel que l'ont fait la nature et la société, mais les choses que ne peuvent les satisfaire qu'indirectement en fournissant des moyens de se procurer ce qui sert immédiatement, comme l'argent, les TITRES DE CRÉANCES, les contrats de rente, &c."

Thus we see that Say expressly enumerates DEBTS, or CREDIT, as WEALTH.

Again, in B. i., c. i., of his *Traité*, after speaking of things of value, such as the earth, metals, money, corn, stuffs, &c., he says:—"Si l'on donne aussi le nom de richesses à des contrats de rentes, à des *effets de commerce*, il est évident que c'est parce qu'ils renferment un engagement pris de livrer des choses qui ont une valeur par elles mêmes."

Again, in his *Cours*, Part i., c. i., he says:—"Vous voyez que la *richesse* ne dépend pas de l'espèce des choses, ni de leur nature physique, mais d'une qualité morale que chacun nomme leur valeur. La valeur seule transforme une chose en richesse dans le sens où ce mot est synonyme de biens, de propriétés. La richesse qui réside en une chose quelconque, que ce soit une terre, un cheval ou une *lettre de change*, est proportionnée à sa valeur. Quand nous parlons des choses comme étant des

richesses, nous ne parlons point des autres qualités qu'elles peuvent avoir ; nous ne parlons que de leur valeur."

These extracts are quite sufficient to prove that J. B. Say amply admits instruments of credit to be wealth, which will be much more fully exemplified further on.

On Say's Definition of Value.

We shall now find exactly the same incongruity in Say's notions of value, as has been the ruin of so much of modern Economies. He over and over again says, that value is something external to an object, for which it can be exchanged, and then he repeatedly speaks of *Intrinsic* value, without the least idea that these are contradictory conceptions !

To shew this, we can only quote a few passages out of many. Thus, *Cours*, Part i., c. i., he says:—"La seconde circonstance à remarquer relativement à la valeur des choses, est l'impossibilité d'apprécier sa grandeur *absolue*. Elle n'est jamais que *comparative*. Quand je dis qu'une maison que je désigne, vaut 50 mille francs ; je n'affirme autre chose sinon que la valeur de cette maison est égale à celle somme de 50 mille francs ; mais qu'est ce que la valeur de cette somme ? Ce n'est point une valeur existante par elle même, et abstraction faite de toute comparaison. La valeur d'un franc, de 5 francs, de 50 mille francs, se compose de toutes les choses que l'on peut avoir pour ces différentes sommes. Si l'on peut, en les donnant en échange, avoir une *plus grande* quantité de blé, de sucre, &c., elles valent *plus* relativement à ces denrées ; si l'on peut en avoir moins, elles valent *moins* ; car la valeur d'une somme d'argent, comme toutes les autres valeurs, se mesure par la quantité des choses que l'on peut obtenir en échange.

"Il en est de l'idée de la valeur comme l'idée de la distance. Nous ne pouvons parler de la distance où est un objet, sans faire mention d'un autre objet, duquel le premier se trouve à un éloignement quelconque. Le même, l'idée de la valeur d'un objet suppose toujours un rapport quelconque avec la valeur d'un autre objet."

Again, in the same chapter:—"Ces même principes nous apprennent encore que l'or, l'argent, les monnaies, ne sont point recherchés pour eux-mêmes, et ne valent jamais que ce qu'ils peuvent acheter."

We need not overload our pages with more quotations. These are sufficient to shew that Say fully admits that *the value* of a thing is what it will exchange for: if it will exchange for more, it has greater value; if it will exchange for less, it has less value; and if it will exchange for nothing, it has *no* value.

Moreover, Say repeatedly acknowledges that value is a quality of the mind, and that it is the mind of man only that confers value.

Thus, he says (*Cours. Consider-Général.*):—“Cependant la valeur est une QUALITE PUREMENT MORALE, et qui paraît dépendre de la volonté fugitive et changeante des hommes.”

So also—“Pour qu’une valeur soit une richesse il faut que ce soit une valeur reconnue, non par le possesseur uniquement, mais par tout autre personne.”

Here Say admits that value does not depend upon a single mind, but upon several; he goes somewhat too far in saying every one, as two minds are sufficient to constitute value.

So also, he says, *Traité d’Economie Politique*, p. 57:—“La valeur que les hommes attachent aux choses. * * * Toujours est il vrai que si les hommes attachent de la valeur à une chose, &c. ;” and in a note to this passage he says:—“Ce n’est pas ici le lieu d’examiner si la valeur que les hommes attachent à une chose est proportionnée ou non à son utilité réelle. La juste appréciation des choses dépend du jugement, des lumières, des habitudes, des préjugés de ceux qui les apprécient. Une saine morale, des notions précises sur leurs véritables intérêts conduisent les hommes à une juste appréciation des vrais biens.” Now, what can be more self-contradictory than the notion that value is something inherent in the substances themselves, and then to say that it entirely depends on the judgment, the knowledge, the habits, and the prejudices of men?

These passages are sufficient to shew that Say admits that the source of Value lies in the human mind.

On Say’s definition of Capital.

We shall see how self-contradictory Say is on the subject of Value hereafter, but his self-contradictions on the subject of Capital are, if possible, still more astonishing.

They will appear more striking if we place them in parallel columns.

Say says that Immaterial and Incorporeal Capital is so part of National Wealth.

Say says that Immaterial and Incorporeal Capital is part of National Wealth.

Cours. Considerations Générales.

“Depuis qu’il a été prouvé que les propriétés immatérielles, tels que les talents et les facultés personnelles acquises forment une partie intégrante des richesses sociales.”

Cours. Part iv., c. v.

“Il faut comprendre parmi les capitaux plusieurs biens qui ont une valeur quoiqu’ils ne

soient pas matériels. Le cabinet d'un avocat, d'un notaire, la chalandise d'une boutique, la réputation d'une enseigne, le titre d'une ouvrage périodique, sont incontestablement des biens ; on peut les vendre, les acquérir, en faire l'objet d'un contrat, et ces sont des biens capitaux, parce que ces sont les fruits accumulés d'une industrie. Un avocat par la sagesse de ses avis, par son assiduité et ses autres qualités a fait concevoir au public une bonne opinion de son cabinet ; cette opinion favorable lui donne droit à de plus forts honoraires ; ce supplément de profit est le revenu d'un CAPITAL appelé *reputation* ; et ce capital est le fruit des soins et des peines que l'avocat a pris pendant plusieurs années.

Cours. Part i., c. x.

La nature des capitaux, la nature des fonctions, nous découvrent des vérités assez importantes. L'une d'elles est que les capitaux productifs ne consistent point en valeurs fictives et de convention, mais seulement en valeurs réelles et intrinsèques que leurs possesseurs jugent à propos de consacrer à la production. En effet, on ne peut acheter des services productifs, qu'avec des objets matériels ayant une valeur intrinsèque ; on ne peut amasser en capitaux et transmettre à une autre personne, que des valeurs incorporées dans des objets matériels.

In a note to this passage he says :—

Il y a des capitaux qui ne sont pas incorporés dans les choses matérielles, comme la clientèle d'un notaire, d'une entreprise commerciale ; mais cette portion de capital est une valeur très réelle, et non pas seulement un signe comme ceux qui selon certaines personnes peuvent remplacer les capitaux.

So also just afterwards—

Les seuls capitaux que je sache être immatériels, sont la clientèle, la chalandise d'un magasin, d'un cabinet, d'un journal. On peut aliéner, on peut vendre un capital de cette espèce.

Traité. B. i., c. xiii.

De la nature des produits immatériels, il résulte qu'on ne saurait les accumuler, et qu'ils ne servent point à augmenter le capital national. Une nation où il se trouvait une foule de musiciens, de prêtres d'employés pourrait être une nation fort divertie, bien endoctrinée, et admirablement bien administrée; mais voilà tout. Son capital ne recevrait de tout le travail de ces hommes industrieux aucun accroissement direct, parceque leurs produits seraient consommés à mesure qu'ils seraient créés.

Definitions at end of same.

Tout capital transmissible est composé des *produits matériels*; car rien ne peut passer d'une main dans une autre, si non des matières visibles.

Cours. Part iv., c. iii.

Sans une classification des choses possédées qui les embrasse toutes, en faisant une évaluation des biens d'une nation, d'une communauté, d'un particulier, nous ne serions jamais certains de la faire complète * * *

Nos propriétés composant de nos biens quels qu'ils soient, comprennent nos biens naturels, en même temps que nos richesses sociales."

And after going through several descriptions of personal talent, he says:—

"Ce que je vous ai dit suffit je pense pour vous convaincre, messieurs, que les facultés industrielles sont des propriétés du même genre que toutes les autres, et que ce n'est qu'en les respectant à l'égal de toutes les autres qu'on obtient tous les avantages sociaux attachés au droits de propriété. Par la même raison cette espèce de propriété, quoiqu'elle puisse difficilement se traduire en chiffres fait néanmoins partie des richesses générales d'une nation. Une nation où les capacités industrielles sont plus nombreuses plus éminentes qu'ailleurs, est une nation plus riche."

It is only requisite to read over these extracts, to see Say's self-contradictions on the subject of Capital.

On Say's Opinion on Instruments of Credit.

We shall now be able to shew how Say's doctrines on instruments of credit is in direct contradiction to some of these opinions on capital. We have already shewn that he expressly classes debts under the title of wealth.

Again, he says, *Traité*, B. i., c. 30 :—

“Une billet à ordre, une lettre de change, sont des obligations contractées de payer, ou de faire payer, une somme soit dans un autre temps, soit dans un autre lieu.

“Le droit attaché à ce mandat (quoique sa valeur ne soit pas exigible à l’instant et au lieu où l’on est), lui donne néanmoins une VALEUR ACTUELLE, plus ou moins forte. Ainsi un effet de commerce de cent francs, payable à Paris dans deux mois, se négociera, ou, si l’on veut, se vendra pour le prix de 99 francs ; une lettre de change de pareille somme, payable à Marseille au bout du même espace de temps, vaudra actuellement à Paris peut-être 98 francs.

“Dès-lors qu’une lettre de change ou un billet, en vertu de leur valeur future, ont une VALEUR ACTUELLE, ils peuvent être employés en guise de monnaie dans toute espèce d’achats, aussi la plupart des grandes transactions du commerce, se règlent-elles avec des lettres de change.”

Thus we see in this passage that Say maintains exactly the same doctrine as we have set forth in the preceding sections, that an instrument of Credit is a *present right to a future payment*, and that it is separate and independent exchangeable property. That is, that CREDIT, or DEBTS, are WEALTH.

We may also quote another passage from his *Cours* (Part iii., division iii., c. 27, p. 461, vol. i.) :—“ Il y a néanmoins une observation importante à faire relativement aux signes représentatifs des monnaies. C’est qu’ils sont capables de rendre un service exactement pareil au service que peuvent rendre les monnaies qu’ils représentent. Si quelqu’un souscrivait un engagement par lequel il s’obligerait à livrer, à une époque désignée, un manteau fait de telle ou telle façon, cette promesse, quoiqu’elle fût en quelque sorte un signe, un gage de la possession du manteau, ne saurait en tenir lieu ; car une feuille de papier ne garantit pas du froid, comme fait un manteau ; tandis que les signes qui représentent la monnaie, peuvent la remplacer complètement, et rendre tous les services que l’on peut attendre d’elle. En effet, les qualités qui font qu’un sac d’argent nous sert dans nos échanges, peuvent toutes se trouver dans une billet. Ces qualités, vous le rappelez, consistent :

“D’abord dans la VALUER qu’il a. *On peut donner à un billet exactement la même valeur qu’à une somme d’argent*, en donnant au porteur le droit de toucher la somme, de manière à lui ôter toute inquiétude sur ce remboursement ; c’est ainsi qu’un billet de banque peut circuler dix ans en conservant une valeur de mille francs sans qu’il soit remboursé, seulement parce qu’on est convaincu qu’il le sera du moment que le porteur le voudra.

* * * * *

“Vous voyez, Messieurs, que toutes les qualités utiles de la monnaie peuvent se retrouver dans un signe représentatif, qui n’a

aucune valeur par lui-même, et tire de la monnaie même, toute celle que l'on veut bien lui accorder."

Hence we see that these passages assert as clearly and explicitly as it is possible that language can do, that Credit may be in all respects equivalent to money, and, therefore, that it may be CAPITAL, just as money may.

Having thus laid before our readers these explicit declarations of Say, that Credit is Wealth, we will now place before them the passage which has been the foundation of such an immense amount of misconception. He says *Traité*, B. ii., c. 8:—"On s'imagine quelquefois que le Crédit multiplie les capitaux. Cette erreur qui se trouve fréquemment reproduite dans une foule d'ouvrages, dont quelques unes sont mêmes écrits *ex professo* sur l'économie politique, suppose une ignorance absolue de la nature et des fonctions des capitaux. *Un capital est toujours une valeur très-réelle, et fixée dans une matière; car les produits immatériels ne sont pas susceptibles d'accumulation. Or un produit matériel ne saurait être en deux endroits à la fois, et servir à deux personnes en même temps.* Les constructions, les machines, les provisions, les marchandises qui composent mon capital, peuvent en totalité être des valeurs que j'ai empruntées; dans ce cas, j'exerce une industrie avec un capital qui ne m'appartient pas, et que je loue; mais, à coup sûr, ce capital que j'emploie n'est pas employé par un autre. Celui qui me le prête s'est interdit le pouvoir de le faire travailler ailleurs. Cent personnes peuvent mériter la même confiance que moi; mais ce Crédit, cette confiance méritée ne multiplie pas la somme des capitaux disponibles; elle fait seulement qu'on garde moins de capitaux sans le faire valoir."

He also says in his *Cours* (Part i., c. 9):—"Le manufacturier qui achète à Crédit des matières premières, emprunte à son vendeur la valeur de ces marchandises pour tout le temps où ce dernier lui fait Crédit; et cette valeur qu'on lui prête, lui est fournie en marchandises qui sont des valeurs matérielles.

"Or, si l'on ne peut prêter et emprunter une portion de Capital qu'en objets effectifs et matériels, que devient cette maxime que le Crédit multiplie les capitaux? Mon Crédit peut bien faire que je dispose d'une valeur matérielle qu'un capitaliste a mise en réserve; mais s'il me la prête, il faut qu'il demeure privé; il ne peut pas en même temps la prêter à une autre personne; la même valeur ne saurait servir deux fois en même temps; l'entrepreneur qui emploie cette valeur, qui la consomme pour accomplir son opération productive, empêche qu'aucun autre entrepreneur puisse l'employer dans la sienne."

We have now to remark upon the extraordinary self-contradictions of Say. He tells us expressly that instruments of Credit have an actual value in respect of their future payment, and that they may be made to have precisely the same value as

money itself, and may be employed in purchases in all respects exactly in the same manner that money may. Now this, of course, by implication, admits that they may be Capital, because money is only used as Capital, by being employed in buying and selling.

Having laid this down as clearly as can be, we have now to see how Say proceeds to contradict himself. He says, in the passages last quoted, that Capital is always a very real value fixed in a matter! Why, he himself has told us that there is incorporeal Capital *not* fixed in any matter whatever, such as Copyright, the goodwill of a business, &c., &c. He then says that immaterial products are not capable of accumulation! What! Cannot a man be possessed of £100,000 of Funded Property? And of the Copyrights of Books, &c., and of a number of Bills of Exchange? He then says that a material product cannot be in two places at once. But who said it could—except Sir Boyle Roche, the famous Hibernian,—and even he limited this power to birds? Neither, however, can an immaterial product be in two places at once, that we are aware of; so that it makes not much difference as to its capacity of being in two places at once, whether the product is material or immaterial. He says that the material merchandise *lent* cannot serve two persons at once. No one says it could; but that has nothing to do with the question. Because it is not the merchandise which is the Credit, but the *Debt created in exchange for the merchandise*, which is a valuable property in itself, and may either be used to buy other articles, and, therefore, is productive capital, or else it may be discounted by a banker, and the proceeds used in the same manner.

But Say himself calls these instruments of Credit, Capital. In his *Cours* (*Part* iii., *c.* xviii.), he says:—"Tout particulier peut souscrire un billet ordinaire, et le donner en paiement d'une marchandise, pourvu que le vendeur consente à le recevoir comme si c'était de l'argent. Ce vendeur à son tour, s'il est acheteur d'une autre marchandise, peut donner le même billet en paiement. Le second acquéreur peut le passer à un troisième dans le même but. Voilà un engagement qui circule; il sert à qui veut vendre; il sert à qui veut acheter; il remplit l'office d'une somme de monnaie.

"La valeur d'une signe dépend de la valeur de la chose signifiée; mais pour que cette valeur soit précisément aussi grande que celle de la chose dont elle est la gage, il faut non-seulement que le paiement du billet soit indubitable, mais qu'il puisse être exigé à l'instant. * * * *

"Si les billets de confiance peuvent remplacer complètement la monnaie métallique, il est évident qu'une banque de circulation augmente véritablement la somme des richesses nationales; car dans ce cas la richesse métallique devenant superflue comme

agent de circulation, et conservant néanmoins une valeur propre, devient une valeur disponible, et peut servir à d'autres usages. Mais comment s'opère cette substitution? Quelles en font les bornes? Quelles classes de la société font leur profit de l'intérêt des *nouveaux fonds ajoutés aux capitaux* de la nation?

"A mesure qu'une banque met ses billets dans la circulation et que le public consent à les recevoir sur le même pied que la monnaie métallique, le nombre des unités monétaires augmente. * * Les personnes qui font la spéculation d'envoyer des monnaies métalliques dans l'étranger, après les y avoir vendues, ou les avoir employés à des achats de marchandises, ont soin de se faire adresser l'équivalent de leurs achats. Ce sont là des richesses réelles des valeurs *ajoutées* à nos capitaux, des valeurs sur lesquelles peut s'exercer notre industrie, et que notre industrie rétablit à mesure qu'elle les consomme, pour fournir des avances à une production nouvelle. *Nous avons des capitaux de plus*, et la valeur capitale qui servait auparavant aux besoins de notre circulation, n'est pas moindre, puisqu'elle est remplacée chez nous par un signe représentatif qui en tient lieu parfaitement.

"Il ne faut pas pourtant pas qu'on s'imagine que la valeur retirée de la somme des monnaies et ajoutée à la somme des capitaux-marchandises, égale la somme des billets en émission. Ceux-ci ne représentent la monnaie qu'autant qu'on est toujours en mesure de les payer à bureau ouvert; et pour cela, la banque est obligée de garder dans ses coffres, et par conséquent de retirer de la circulation une somme quelconque de numéraire. Si, par supposition, elle met dans la circulation pour cent millions de billets, elle retirera peut-être 40 millions d'espèces, qu'elle mettra en réserve pour faire face aux remboursements qui pourraient lui être éventuellement demandés. Or, si elle ajoute à la quantité de monnaie en circulation, 100 millions, et si elle en retire 40 de la circulation, c'est comme si elle en ajoutait seulement 60.

"Nous devons à présent désirer de savoir quelle classe de la société jouit de l'usage de ce NOUVEAU CAPITAL."

Say then goes on to explain how this *new capital* is employed, and who reaps the profit of it.

Thus, J. B. Say, who is supposed to be the Economist *par excellence*, who has proved that those writers who maintain that Credit is Capital, are such poor muddle-headed creatures as to think that the same thing can be in two places at once, himself expressly declares that CREDIT IS CAPITAL!!!

On the self-contradictions of Mr. J. S. Mill on the subject of Credit.

30. Turgot, we have seen above, was the writer who started the erroneous notion that Credit was the transfer of something, and J. B. Say extended this error by saying that credit could not

multiply capital, because the same thing could not be in two places at once. These two sentences have been repeated by a multitude of unthinking writers in France and England, from that day to this. The number of writers who have reiterated these absurdities is so great that we cannot afford room to examine them all. We have only room to examine what Mr. J. S. Mill has said, and to see whether he is more consistent with himself than Say.

We have already quoted in Chap. I., Mr. Mill's definition of wealth. At page 8, Vol. i., he says:—"Everything forms, therefore, a part of Wealth, which has a power of purchasing." And—"Money being the instrument of an important public and private purpose, is rightly regarded as Wealth; but everything else which serves any human purpose, and which nature does not afford gratuitously, is Wealth also." Here, therefore, are propositions of the widest generality, which assert that whatever can be bought and sold, no matter what its nature be, is Wealth. Consequently, if bank notes, bills of exchange, &c.—or Credit—can be bought and sold, they are Wealth, by the very force of the definition.

Let us now turn to Mr. Mill's definition of Capital. He tells us, B. i., c. iv., that money may be productive capital by being exchanged for other things, and that ANYTHING which is susceptible of being exchanged for other things is capable of contributing to production in the same degree. That is to say, without inquiring here what is meant by production, he says that money may be productive capital by being used in a certain way, and that anything which may be used in a similar way may be productive capital as much as money. Now, it is perfectly well known that bank notes, bills of exchange, &c.—or Credit—may be, and are exchanged for other things just as money is. Hence this sentence expressly implies that Credit may be productive Capital just as much as money.

Thus we see that Mr. Mill has already, by implication, admitted that credit may be capital. And this doctrine we shall find he still more explicitly states when he speaks of credit itself, B. iii., c. xi., is headed, "Of Credit, as a substitute for money." Now, we observe that if one thing is to be a substitute for another, it must be of the same general nature. Not so high, or excellent in degree, perhaps, but still it must be of the same kind. Things of totally different natures cannot be substituted for each other. Thus, for instance, if a man cannot get xxx ale, he may have to put up with swipes as a substitute. But a pair of shoes could never be a *substitute* for a glass of ale. If, therefore, credit is to be a substitute for money, it must be of the same general nature as money. Now money, as every one knows, is separate and independent exchangeable property, and, consequently, credit must be so also. Money, if used in a certain way, is capital; credit must

also be capable of being used as capital as well. If money, therefore, is capable of being productive capital, credit must be so likewise.

Passing over the beginning of this chapter, to which we shall revert, Mr. Mill says, in § 3:—"For Credit, though it is not *productive* power, is *purchasing* power." Now, here is a striking contradiction already to what he had said before. For, in B. i., as we have already shewn, he says that anything which has power of purchase is Wealth. Here he admits that credit is purchasing power, and, therefore, by his own shewing, if it is purchasing power, it is Wealth; and if it is Wealth, it may, by his own admission, be productive capital.

In § 5, he says, that a form "in which credit is employed as a substitute for eurrency is that of promissory notes." In § 6, he says, another mode "of making credit answer the purposes of money, by which, when carried far enough, money may be very completely superseded, consists in making payments by cheques." Here we see that he expressly calls the Promissory Note and the Cheque, the Credit.

In the next chapter, xii., we shall see that he expressly allows that these instruments of Credit are independent exchangeable property, and valuable things. He says, § 1:—"An *order, or note of hand, or bill payable at sight*, for an ounce of gold, while the credit is unimpaired, is worth neither more nor less than the gold itself;" and, "But we have now found that there are other things, such as bank notes, bills of exchange, and cheques, which circulate as money, and perform ALL the functions of it." Now here is an explicit declaration that Credit performs ALL the functions of money, and, therefore, as one of the functions of money is to be *productive Capital*, it follows that Credit may also be productive Capital.

In § 2 of the same chapter, he says, that a man "may make purchases with money which he only expects to have, or even only pretends to expect. He may obtain goods in return for his acceptance payable at a future time, or on his note of hand, or on a simply book credit, that is, on a mere promise to pay. All these purchases have exactly the same effect on price, as if they were made with ready money. The amount of purchasing power which a person can exercise, is composed of all the money in his possession, and due to him, AND OF ALL HIS CREDIT." "He creates a demand for the article to the full amount of his money AND CREDIT *taken together*, and raises the price proportionably to both." In § 3, he says:—"The inclination of the mercantile public to increase their demand for commodities by making use of all or much of their credit as a purchasing power." In § 4:—"The banker's credit with the public at large, coined into notes, as bullion is coined into pieces of money to make it portable and divisible, is *so much purchasing power* SUPER-

ADDED, in the hands of every successive holder, to that which he may derive from his own credit. * * Credit, in short, has exactly the same purchasing power with money; and, as money tells upon prices not simply in proportion to its amount, but to its amount multiplied by the number of times it changes hands, so also does credit; and credit, transferable from hand to hand, is in that proportion more potent than credit which only performs one purchase."

In § 5, he says:—"Since, then, credit in the form of bank notes is a more potent instrument for raising prices than book credits—* * If we consider the proportion which the utmost increase of bank notes in a period of speculation bears, I do not say to the whole mass of credit in the country, but to the bills of exchange alone, the average amount of bills in existence at any one time is supposed considerably to exceed a hundred millions sterling. The Bank Note circulation of Great Britain and Ireland is less than thirty-five millions, and the increase in speculative periods, at most, two or three." And, as a note to this passage, Mr. Mill gives a table of the bills supposed to be created in several years, the last of which is 1839, when the bills supposed to be created amounted to £528,493,842. In *c. xiii.*, he says:—"After experience had shewn that pieces of paper of no intrinsic value, by merely bearing upon them the written profession of being equivalent to a certain number of francs, dollars, or pounds, could be made to circulate as such, and to produce all the benefit to the issuers which could have been produced by the coins which they purported to represent—"

Now, from these extracts from Mr. Mill's work, our readers will clearly perceive that he expressly asserts, as positively as it is possible that language can do, that Credit is independent, exchangeable property, like any other. That it is cumulative property to money and commodities, and that it may be dealt with precisely in the same manner as money, and may produce all the effects of money. Now, as this Credit is nothing but circulating debts, it follows clearly from Mr. Mill's own admission, that DEBTS are WEALTH. All this is in exact accordance with the doctrines laid down in the preceding sections of this treatise.

In *B. iii., c. xxii.*, he is equally explicit:—"The same effects which would thus arise from the discovery of a treasure accompany the process by which bank notes, or any of the other substitutes for money, take the place of the precious metals."—"The value saved to the community by thus dispensing with metallic money is a clear gain to those who provide the substitute. They have the use of 20 millions of circulating medium, which have cost them only the expense of an engraver's plate. If they employ this accession to their fortunes as PRODUCTIVE CAPITAL, the produce of the country is increased and the community benefited as much as by any *other* CAPITAL of

equal amount. * * When paper currency is supplied, as in our own country, by bankers and banking companies, the amount is almost wholly turned into **PRODUCTIVE CAPITAL** * * A banker's profession being that of a money lender, his issue of **NOTES** is a simple extension of his ordinary occupation. He lends the amount to farmers, manufacturers, or dealers, who employ it in their several businesses. So employed, it yields, like any *other* **CAPITAL**, wages of labor, and profits of stock. The profit is shared between the banker, who receives interest, and a succession of borrowers, mostly for short periods, who, after paying the interest, gain a profit in addition, or a convenience equivalent to profit. The **CAPITAL** itself, in the long run, becomes entirely wages, and, when replaced by the sale of the produce, becomes wages again; thus affording a perpetual fund of the value of 20 millions for the maintenance of productive labour, and increasing the annual produce of the country by all that can be produced through means of a **CAPITAL** of that value."

Thus our readers will perceive, from the former extracts that we laid before them, that Mr. Mill expressly stated that Credit was independent, exchangeable property, whether embodied in the forms of Notes, Bills, Bank debts, or any other form, which was capable of performing all the functions of money, and therefore, by implication, capable of being employed as capital. But in the last preceding extracts he expressly calls bank notes—which are Credit—**PRODUCTIVE CAPITAL**.

We think we have shewn our readers as clearly as it can be done, that Mr. Mill asserts that Credit is Capital. And yet will they believe that he not only denies that Credit is Capital, but sneers at the imbecility of those who think it is!

In B. iii., c. xix., which we have already quoted from, the heading of the chapter is, as we said, "Of Credit, as a substitute for money," which clearly affirms that Credit is exchangeable property like money, he says:—"The functions of Credit have been a subject of as much misunderstanding, and as much confusion of ideas, as any single topic in Political Economy.

"As a specimen of the confused notions entertained respecting the nature of Credit, we may advert to the exaggerated language so often used respecting its national importance. Credit has a great, but not, as many people seem to suppose, a magical power; it cannot make something out of nothing. [Who said it could?] *How often is an extension of Credit talked of as equivalent to a creation of Capital, or as if Credit actually were capital!!!*] Why! Who has said more distinctly than Mr. Mill himself that Credit is Capital? The very object of the whole of the preceding extracts is to shew that Credit is Capital!] It seems strange that there should be any need to

point out that *credit being only the permission to use the capital of another person!!* the means of production cannot be increased by it, but only *transferred*. If the borrower's means of production, and of employing labour are *increased* by the credit given him, the lender's are as much *diminished*. The same sum cannot be used as capital, both by the owner and also by the person to whom it is lent, it cannot supply its full value as wages, tools, and materials, to two sets of labourers at once. It is true that the Capital which A has borrowed from B, and makes use of in his business, still forms part of the wealth of B, for other purposes; he can enter into engagements in reliance on it, and can even borrow, when needful, an equivalent sum on the security of it; so that, to a superficial eye, it might seem as if both B and A had the use of it at once. But the smallest consideration will shew that when B has parted with his capital to A, the use of it as capital rests with A alone, and that B has no other service from it than in so far as his ultimate claim upon it serves him to obtain another capital from a third person C. All capital (not his own) of which any person has really the use, is and must be, so much subtracted from some one else.

“But though Credit is never anything more than a TRANSFER of Capital from hand to hand?”

Our readers cannot fail to see the astonishing confusion of ideas, on the subject of Credit, in the above extracts. In the first set, Mr. Mill sees clearly Credit is the *Promise to pay*, which he over and over again says is independent, exchangeable property, of the value of money, which may be used in all respects like money, and perform all its functions. And, therefore, it may be Capital as well as money.

Mr. Mill says that the Capital (*i. e.*, the goods) which A has sold on credit to B, are so much subtracted from his property, and cannot be used by him as well as by B. But he wholly forgets that, in exchange for those goods, A receives B's “promise to pay,” which is a debt, and, in fact, is the credit. And this debt is exchangeable property, with which he can either purchase new goods to replace those he has sold to B, or he can sell it to his banker, and receive a bank credit, with which he can purchase fresh goods, just the same as he could with money.

In the second extract Mr. Mill has changed his conception of Credit from being a *Promise to pay*, or a Debt, to its being the *Transfer of Capital!!*

Now, we ask—Is a Bank Note the *transfer* of a commodity? Is a guinea the sale of a book? Is a piece of independent property the transfer of something else? Is a table the *transfer* of a chair? Is an independent quantity of any sort whatever an *operation*?

Mr. Mill informs us that Credit cannot make something out of nothing. Who said it could? Can a guinea make something

out of nothing? It is not Credit that makes something out of nothing; but it is Credit itself which is a valuable property, which is created out of nothing by the consent of the wills of persons, and which, by the reiterated acknowledgments of Say and Mill, is capable of performing all the functions of money. Now, money becomes Capital, by their own admission, by being exchanged for other things, or by circulating other things. Credit may be Capital in precisely the same way.

Moreover, we see how completely Mr. Mill is in error when he says that Credit is never anything more than the transfer of Capital. It is wholly untrue that Credit is always created in exchange for commodities. As we have shewn in the preceding section, all profitable banking business consists in buying debts by creating other debts. That is, Credit is created to purchase Credit.

After this exposition, our readers will, perhaps, think that Mr. Mill is not exactly the person to sneer at others for their confused notions about Credit, though his own work is a striking example of the misunderstanding and confusion of ideas which he says prevail upon the subject. And many may wonder, perhaps, at a logician who is unable to perceive the difference between an independent quantity and a sale of goods.

Opinions of some other Writers.

31. We have sufficiently shewn, we hope, the inconsistency of the doctrines of Say and Mr. Mill on credit. We may give a quotation from a few other well-known writers. Thus, Bastiat says (*Harmonies Economiques*, Art. *Capital*, Vol. vi., p. 219., edit. 1855):—"Ce qui est plus surprenant encore, c'est que nous pouvons faire l'opération INVERSE, quelque impossible qu'elle semble au premier coup d'œil. Nous pouvons convertir en instrument de travail, en chemin de fer, en maisons, un capital qui n'est pas encore né, utilisant ainsi des *services*, qui ne seront rendus qu'au xx^e siècle. Il y a des banquiers qui en font l'avance sur la foi que les travailleurs et les voyageurs de la troisième ou quatrième génération pourvoient au payment; et ces *titres sur l'avenir* (*i. e.*, instruments of Credit), se transmettent de main en main sans rester jamais IMPRODUCTIFS."

This is exactly the very doctrine we have been endeavouring to explain. In commerce, these *titres sur l'avenir*, or instruments of Credit, are not drawn upon the third and fourth *generation*, but they are drawn payable three or four months hence, and are exchangeable property, and made productive capital by circulating merchandize.

Mr. McCulloch says, in his *Dictionary of Commerce*, Art. *Banking*:—"Those who issue such notes, coin as it were their credit. They derive the same revenue from the loan of their

written promises to pay certain sums, that they would derive from the loan of the sums themselves; and, while they thus increase their own income, they at the same time contribute to increase the wealth of the society."

Therefore, Mr. McCulloch clearly asserts that Credit is productive capital.

Mr. Gilbart says (*Logic of Banking*, p. 46):—"Bankers also employ their own Credit as capital. They issue notes, promising to pay the bearer a certain sum on demand. As long as the public are willing to take these notes as gold, they produce the same effects. The banker who makes advances to the agriculturist, the manufacturer, or the merchant, in his notes, stimulates as much the productive powers of the country, and provides employment for as many labourers, as if, by means of the philosopher's stone, he had created an equal amount of solid gold. It is this feature of our banking system that has been most frequently assailed. It has been called a system of fictitious credit—a raising the wind—a system of bubbles. Call it what you please, we will not quarrel about names, but by whatever name you please to call it, it is a powerful instrument of *production*. If it be a fictitious system, its effects are not fictitious, for it leads to the feeding, the clothing, and the employing of a numerous population.

* * * * *

"Thus a banker, in three ways, increases the productive power of capital—1st. He economises the capital already in a state of employment. 2ndly. By the system of deposits he gives employment to capital that was previously unproductive. 3rdly. By the issue of his own notes he *virtually* CREATES CAPITAL by the substitution of CREDIT."

*On the common difficulty in understanding the subject of
Credit.*

32. We have, in the preceding remarks, pointed out that the writers who have so sneered at the notion that Credit is Capital, have themselves declared it to be so.

The real difficulty which impedes a true comprehension of the subject, is very similar to that which long obstructed the progress and reception of the Newtonian doctrine of gravity. It had been handed down as a dogma from the days of the Greek philosophers, that a body could not act where it was not. Instead of reflecting on the facts with unbiassed minds, the opponents of the Newtonian doctrines contended that his doctrines violated the fundamental dogma, that a body could not act where it was not, and treated them with ridicule.

A very much more specious dogma is, however, at the root of the common inability among uneducated writers to grasp the true conception of Credit. From the days of Anaxagoras and Epicurus, it has been handed down from age to age, by

succeeding generations of physicists, *That nothing can come out of Nothing*, and *That Nothing can go back into Nothing*. The fundamental dogma of Lucretius, the hierophant of the Atomic Philosophy, is that Nothing can come out of Nothing. I., 151, &c. :—

NULLAM REM E NIHILO GIGNI DIVINITUS UNQUAM.

* * * * *

NIL igitur fieri de NILO posse fatendum 'st.

Moreover, that Nothing can go back into Nothing. I. 216, &c. :—

Huc accedit, uti quæque in sua Corpora rursum
Dissolvat Natura, neque ad Nihilum interimat res.

* * * * *

Nullius exitium patitur Natura videri.

* * * * *

Immortali sunt naturâ prædita certe ;
Haud igitur possunt ad Nilum quæque reverti.

* * * * *

Haud igitur redit ad Nihilum res ulla, sed omnes
Descidio redeunt in corpora materiai.

* * * * *

Haud igitur penitus pereunt quæcunque videntur ;
Quando alia refecit Natura nec ullam
Rem gigni patitur, nisi morte adjutum alienâ.

And this is the constant *refrain* of the Lucretian philosophy, That nothing can be produced from nothing, and that nothing can go back into nothing. I., 266 :—

Nunc age, res quoniam docui non posse creari
De Nihilo, neque item genitum 'st ad Nil revocari,

* * * * *

At quoniam supra docui NIL, posse creari
De Nihilo, neque quod genitu 'st ad Nil revocari,
Esse immortalis Primordia corpore debent."

And this is the identical doctrine which physicists maintain to the present day. Chemists delight to expatiate to their audience on the indestructibility of all things. How seeming destruction is merely the dissolution of atoms under their present combinations, to reappear in new forms and new combinations in perpetual succession.

But Political Economy confounds the best settled doctrines of the sages of old. It is true that many Economists have declared that man can call nothing into existence, that all wealth comes from the earth. That wealth is but the particles of matter, and that all that man can do is to re-arrange them, and either place them in a new position, and let nature do the rest. But their own doctrines, their own books, their own definitions, confound all such notions. And lawyers know better than that. Economists, with scarcely an exception, are agreed that what-

ever can be exchanged, whatever can be bought and sold, is wealth; that everything by which profit can be made is capital. Twenty-two centuries ago Socrates expressly declared that KNOWLEDGE WAS WEALTH. Aristotle laid down as a definition that *everything* whose value could be measured in money was WEALTH. Adam Smith expressly enumerates the "acquired and useful abilities" of the people as part of the Wealth of a country. He also classes paper money—which is credit—as valuable property, and, therefore, Wealth, making exchangeability the test of Wealth. J. B. Say has done the same. So does Mr. Senior. He says:—"Health, strength, and KNOWLEDGE, and the other natural and acquired powers of MIND, appear to us to be articles of WEALTH. * * * * In the greater part of the world a man is as purchasable as a horse. In such countries the only difference in value between a slave and a brute consists in the degree in which they respectively possess the saleable qualities that we have been considering. *If the question whether personal qualities are articles of wealth had been proposed in classical times, it would have appeared too clear for discussion.* [We have shewn in the first chapter that this very question was proposed in classical times, and personal qualities were decided to be WEALTH.] In Athens every one would have replied that they, in fact, constituted the whole value of an ἔμψυχον ὄργανον. The only difference in this respect between a freeman and a slave are, first, that the freeman sells *himself*; and only for a period, and to a certain extent, the slave may be sold by others and absolutely; and, secondly, that the personal qualities of the slave are a portion of the wealth of his master; those of the freeman, so far as they can be made subjects of exchange, are a part of his own wealth. They perish, indeed, by his death, and may be impaired, or destroyed, by disease, or rendered valueless by any changes in the customs of the country, which shall destroy the demand for his services; *but, subject to these contingencies, they are wealth, and wealth of the most valuable kind.* The amount of revenue derived from their exercise in England far exceeds the rental of all the lands in Great Britain."

Again, at p. 145, Mr. Senior says:—"Even in our present state of civilization, which, high as it appears by comparison, is far short of what might easily be conceived, or even of what may confidently be expected, the INTELLECTUAL and MORAL CAPITAL of Great Britain far exceeds all her MATERIAL CAPITAL, not only in importance, but even in productiveness. The families that receive mere wages, probably do not form a fourth of the community; and the comparatively large amount of the wages even of these, is principally owing to the capital and skill with which their efforts are assisted and directed by the more educated members of the society. Those who receive mere rent, even

using that word in its largest sense, are still fewer; and the amount of rent, like that of wages, principally depends on the knowledge by which the gifts of nature are directed and employed. The bulk of the national revenue is profit, and of that profit, the portion of which is mere interest on material capital, probably does not amount to one third. The rest is the result of PERSONAL CAPITAL, or, in other words, of education.

“It is not in the accidents of soil, or climate, or on the existing accumulation of the material instruments of production, but on the quantity and the diffusion of this IMMATERIAL CAPITAL, that the WEALTH of a country depends. The climate, the soil, and the situation of Ireland have been described as superior, and certainly are not much inferior, to our own. Her poverty has been attributed to the want of *material capital*; but were Ireland now to exchange her native population for seven millions of our English North-Countrymen, they would quickly create the Capital that is wanted. And were England, north of Trent, to be peopled exclusively by a million of families from the west of Ireland, Lancashire and Yorkshire would still more rapidly resemble Connaught. Ireland is physically poor, because she is morally and intellectually poor. And while she continues uneducated, while the ignorance and violence of her population render persons and property insecure, and prevent the accumulation and prohibit the introduction of capital, Legislative measures, intended solely and directly to relieve her poverty, may not, indeed, be ineffectual, for they may aggravate the disease, the symptoms of which they were meant to palliate, but undoubtedly will be productive of no permanent benefit. KNOWLEDGE *has been called power—it is far more certainly WEALTH.* Asia Minor, Syria, Egypt, and the Northern Coast of Africa, were once among the richest, and are now among the most miserable countries in the world, simply because they have fallen into the hands of a people without a sufficiency of the *immaterial sources of wealth* to keep up the *material* ones.”

Knowledge, therefore, by the very generality of the definition, and the consent of nearly every Economist of note—is Wealth. And where does Knowledge come from? And what is it formed out of? Does it come from the earth? and is it formed out of the materials of the globe? We should fancy that few would maintain that. All that we know is that Knowledge originates *in* the mind. Knowledge is formed *in* the mind, but is it formed *out of* the materials of the mind? And if so, what is the composition of the mind? Does it come from the earth? Are we to have an Atomic theory of Knowledge, or of the Mind? Will some metaphysical Dalton tell us that knowledge, or the human mind, is composed of indestructible primordial Atoms?

Πολλά τὰ δευρά, καὶ δὲν ἀν-
θρώπου εἰσότερον πέλει

But this same knowledge—*Whence* cometh it? *What* is it? *Whither* goeth it?

We know not—Do our readers?

Nevertheless, it is WEALTH; and, therefore, it is within the domain of the Economist. It may be bought and sold; it may be valued; it may be accumulated; it may be handed down from age to age, like any material product whatever. The acquisition of knowledge is the acquisition of Wealth; and the loss of knowledge is the destruction of Wealth. And is the loss or destruction of knowledge the dissolution of indestructible primordial atoms? Here, then, are vast masses of Wealth, and the question is where it comes from, and what is it composed of? And there are but two solutions of the question. Either knowledge is composed of indestructible atoms, or it is not. If it be so, then, of course, the formation of knowledge is not the Creation of Wealth out of Nothing. But, unless we are prepared to admit that—and who is?—the formation of knowledge must be creation of Wealth out of Nothing. And the loss or destruction of Knowledge must be the Decreation, or the return, of Wealth into Nothing!

As one example of this out of thousands, we may take a case that was not very long ago before the Scotch Courts. In the beginning of the 17th century, a man named Anderson discovered a way of making pills, which soon became very popular. The secret of making these pills has been handed down from generation to generation, and has been a constant source of Wealth to the owner of it. Very recently, the possessor of it became bankrupt, and his creditors claimed the right of having it given up to them, as part of the bankrupt's property. The pills have been analysed in vain by chemists, and the secret of their composition has never been able to be discovered. Now, here is a manifest case of a trade secret—knowledge,—being Wealth,—and where did this Wealth come from? and what is it composed of? Did it come from the earth? and is it composed of the materials of the globe? And yet it has been handed down as an heirloom from age to age. Suppose the present possessor of the secret dies without divulging it, there is a manifest loss of Wealth. And what would become of it in such a case? And this is clearly only a particular example out of countless others.

Here, therefore, we have enormous masses of what every Economist, with scarcely an exception, admits to be wealth, which shakes the doctrines of the Physical Philosophers. But also, the doctrines of many Economists are equally overthrown, because they say that all wealth comes from the earth. But here we have great masses of wealth which do not come from the earth. Hence it is manifest that there is another source of wealth besides the Earth, namely, the HUMAN MIND.

But even this does not exhaust the list of Economic Quantities, though Economists have scarcely noticed any other. When we adopt the definition of Wealth as everything that can be exchanged, or whose value may be measured, we very soon find that there is yet another species of exchangeable quantities, which do not originate in the earth, nor yet in the mind. And here again we may observe that Lucretius is at fault. For he says that there is nothing, besides the void, which is separated from something corporeal. I. 420:—

Omnis, ut est, igitur, per se, Natura, duabus
Consistit rebus; nam CORPORA sunt, et INANF.

* * * * *

Præterea nihil est, quod possis dicere ab omni
Corpore sejunctum, secretumque esse ab INANI.

* * * * *

Et facere et fungi sine CORPORE nulla potest res.

* * * * *

Ergo præter INANE et CORPORA, tertia per se
Nulla potest rerum in numero natura relinqui.

From these lines it is clear that Lucretius did not live in the days of Public Debts, Bills of Exchange and Bank Notes, Bank Shares, Copyrights and other incorporeal property, or he would have modified this part of his Philosophy.

Modern ingenuity has reduced what Lucretius declared an impossibility into reality. There are enormous masses of exchangeable incorporeal property, for which there are express shops for creating, and there are special markets for trafficking in, namely, the Royal Exchange and the Stock Exchange.

Mr. Mill, we have seen, defines Wealth to be anything which has power of purchasing, and he says that productive labour is labour which is productive of Wealth. Hence manifestly labour which produces anything which is exchangeable is producing Wealth. In Book iii., c. xii., § 5, he gives a table shewing that the Bills created in a single year amounted to £528,493,842, and these, after all, were but a fractional part of the total quantity of credit. In B. iii., c. xx., § 2, he expressly calls Bank Notes "Productive Capital," and Smith enumerates paper credit enumeratively to gold and silver money.

Now, we observe, that every one allows Bank Notes, Bills of Exchange, &c., to be separate, independent, exchangeable property, and, therefore, *ex vi termini*—Wealth. And what are they? Simply Credit—DEBTS. Now, where do these debts come from? Do they come from the materials of the globe? Are they, too, formed of indestructible primordial atoms? When a debt is extinguished, is it a mere dissolution of certain material particles to reappear under another form? Are they even the products of Labour and the human mind?

How is a debt created? By the mutual *consent* of two minds.

By the mere fiat *of the HUMAN WILL*. And how is a debt extinguished? By the mere FIAT *of the HUMAN WILL*. Now, we again ask—we need scarcely repeat that a debt is property—Whence does it come? When two persons have WILLED to create a debt—whence does it come? From the materials of the globe? Does it come even from the mind? No! it is nothing but a valuable product, created out of Absolute NOTHING, by the mere Fiat of the Human Will. And when it is extinguished, it is a valuable product DECREASED into NOTHING by the mere Fiat of the Human Will.

But, besides debts, there is an enormous mass of valuable property of a similar nature created by the mere Will of the Legislature, such as Copyrights. It is true, that the Legislature cannot make a Copyright a valuable thing; but it can prevent it from being destroyed. Now, we ask—Are not the Copyrights held by a publisher part of his fixed Capital? Part of his Wealth? Just as much as so much land? Whence come they? From the materials of the Globe? or even from the Human Mind? It is quite clear that Copyrights are the pure creation of the Will of the Legislature.

Suppose that the Legislature were to abolish Copyrights, would not that be an actual *annihilation* of Wealth, and not merely the Dissolution of material atoms?

What, again, are the Funds? Nothing but valuable Rights created by the Will of the Legislature. Suppose Parliament were to abolish the Funds. Would not that be the *annihilation* of a vast amount of property?

Precisely the same considerations apply to vast amounts of property of a similar nature. Such as policies of insurance, leases, and annuities of all sorts. They are all property created by the mere Fiat of the Human Will. And who can form the most distant conception of the value of all the Incorporeal property of this nature in Great Britain? In the species of private credit alone, which is the subject of this chapter, it is probably not far short of the value of the land of the country.

The Opinions of various Writers on the Nature and Extent of the Currency.

33. Within the last thirty or forty years strong differences of opinion have manifested themselves among Economists as to the nature and extent of the currency. It may be said, we think, that these discordances have arisen from writers not well ascertaining the true philosophical import of the terms they use. We shall now place before our readers the opinions of various persons of eminence on the subject. Whenever we clearly understand that the true function of the *currency, or circulating medium*, is to circulate commodities, &c., *i. e.*, to obviate the necessity of barter, or exchange, by substituting a pledge of

future payment of some sort in place of an actual equivalent, there can be no reasonable doubt but that currency must include money and Credit in all its shapes and forms; and such was the opinion of speakers and writers until a comparatively recent period, when an influential sect sprung up, who restricted the term currency to money and bank notes payable to bearer on demand, and excluded all other forms of credit from it.

We shall first place before our readers the opinions of several writers who held the former opinion, and then examine the opinions of those who hold the latter view, and the reasons they allege in support of it.

The discussions on the nature of currency had not arisen in Smith's time. The name itself was new. What we call paper currency, he usually calls paper money, which is an error, the two being very different. But it is manifest that he includes all forms of credit under the title of money, or currency.

We have already shown that Adam Smith includes credit under the title of capital. He specifies money as one form of circulating capital, and under the title of money he includes all forms of paper credit. Thus he says, B. ii., c. ii. :—"Money, therefore, the great wheel of circulation, the great instrument of commerce, like all other instruments of trade, though it make a part, and a very valuable part of the capital." He then speaks of the substitution of paper for specie, and says:—"There are several different sorts of paper money [currency]; but the circulating notes of banks and bankers are the species which is best known, and which seem best adapted for this purpose." Now, what can the other species of paper currency be, except bills of exchange, &c.? Cheques had only just begun to be used in London a few years before the publication of the *Wealth of Nations*, and the probability is that Adam Smith had never seen a cheque when he wrote his work, but manifestly they are included under his designation. In B. iii., c. i., he says:—"The great commerce of every civilised society is that carried on between the inhabitants of the town and those of the country. It consists in the exchange of rude for manufactured produce, either immediately, or by the intervention of money, or of some sort of paper which represents money." Now, what sort of paper, besides bank-notes, does this mean, but bills of exchange and cheques?

The controversies about the meaning of currency, the circulating medium, seem to have begun about the time of the Bank Restriction Act, in 1797. In the debate on that measure (*Parl. Hist.*, vol. xxxiii., p. 340), Mr. Fox said that he wished "that gentlemen, instead of amusing themselves with new terms of *circulating medium* and the like." In his reply, Mr. Pitt said:—"As so much had been said on the nature of a circulating medium, he thought it necessary to notice that he did not, for

his own part, take it to be of that empirical kind which had been generally described. It appeared to him to consist in anything that answered the great purposes of trade and commerce, *whether in specie, paper, or any other term that might be used.*" Hence we see that Mr. Pitt expressly included all forms of Credit under the term Circulating Medium.

The next writer we may cite is Mr. Henry Thornton, one of the authors of the Bullion Report. In his *Inquiry into the Nature and Effects of the Paper Credit of Great Britain*, he says, p. 40:—"A multitude of bills pass between trader and trader in the country in the manner that has been described; and they evidently form, in the strictest sense, a part of the circulating medium of the country." And, in a note on this passage, he says:—"Mr. Boyd, in his publication addressed to Mr. Pitt on the subject of the Bank of England issues, propagates the same error into which many others have fallen, of considering bills as no part of the circulating medium of the country." After quoting a passage from Mr. Boyd, which is given below, he says:—"It will be seen, in the progress of this work, that it was necessary to clear away much confusion which has arisen from the want of a sufficiently full acquaintance with the several kinds of paper credit, and, in particular, to remove, by a considerable detail, the prevailing errors respecting the nature of bills, before it could be possible to reason properly upon the effects of paper credit."

We may next quote from a speech of the Marquis of Titchfield, in 1822, on Mr. Western's motion regarding the Act of 1819. He said:—"Economy of money was, by contrivances to spare the use of it, according to the description of his right honourable friend, by substitutions for the precious metals in the shape of voluntary credit. Every new contrivance of this kind, and every one improved, had that tendency. When it was considered to how great an extent these contrivances had been practised, *in the various modes of verbal, book, and circulating credits, it was easy to see that the country had received a great addition to its currency. This addition to the currency would, of course, have the same effect as if gold had been increased from the mines.*" Here, therefore, we see it explicitly stated that credit in all its shapes and forms was independent, exchangeable property, of the value of, and producing the same effects as, gold.

We may now consider the opinions of those writers who have taken a different view of the matter.

Mr. Walter Boyd is the first that we are aware of who confined the term currency to money and bank notes. He says (*Letter to Mr. Pitt*, p. 2):—"By the words 'means of circulation,' 'circulating medium,' and 'currency,' which are used almost as synonymous terms in this letter, I understand always ready money, whether consisting of bank notes or specie, in contra-

distinction to bills of exchange, Navy bills, Exchequer bills, or any other negotiable paper, which form no part of the circulating medium, as I have always understood the term. The latter is the *circulator*; the former are merely *objects of circulation*."

A few traces of this opinion may be discovered in certain writers after this period; but, as this view was most prominently brought forward before the Committee of 1840, we may pass at once to that.

Mr. J. B. Smith, President of the Chamber of Commerce of Manchester, said that he thought circulation and currency were the same (Q. 40); that deposits were currency, which was, in fact, another word for liabilities.

Q. 70. *Mr. O'Connell*—"There is another description of paper in circulation, namely, bills of exchange; do you include those also in your description of the currency?—I do not consider bills of exchange as currency.

Q. 71. "What is the difference between a bill of exchange which is passing from hand to hand and commanding property in return for it, and a bank note which is performing the same functions, supposing each to be for £100?—I consider a bill of exchange to be a debt.

Q. 72. "Is not a bank note a debt?—The difference between a bill of exchange and currency would be this, that currency would discharge the debt; the payment of a bill of exchange is not the discharge of a debt till it is due.

Q. 78. *Mr. Smith*—"Supposing this case to happen, that the same bill of exchange passed through a banker's hands six times in one day on the account of different persons having accounts with this bank, should you not say that that bill of exchange discharged the functions of currency?—It is a mere transfer, after all, from hand to hand, with, every time it is indorsed, an additional security.

Q. 79. "Supposing it not to be indorsed, can you point out the difference between that and a Bank of England note?—The difference between a Bill of Exchange and a Bank of England note in any transaction, is that a Bill of Exchange is a debt, and it continues a debt till it is discharged by a Bank of England note, or by some other currency, which is a full discharge of the debt.

Q. 80. *Sir R. Peel*—"What does a Bank of England note profess upon the face of it; is it not 'I promise to pay?'—Precisely so.

Q. 81. "Is not that evidence of a debt?—Certainly, but it is legal tender.

Q. 82. "Supposing a law were passed permitting a gold circulation to continue, and prohibiting the issue of notes by the Bank, do you not think the measure which traders would resort

to, would be to supply the deficiency by Bills of Exchange?—It is probable; it might be so.

Q. 83. “Would not they answer the purposes of Currency?—Bills of Exchange do not perform the functions of Currency, but they are instruments by which commodities are exchanged, equally with every other mode of Credit, but requiring money for their discharge.

Q. 84. “Though there is a difference in the nature of the transactions between the issue of a note, payable on demand, and passing of a bill of exchange, is there any substantial difference in their sensible effect on the currency of the country?—I do not think that Bills of Exchange affect the Currency, though the Currency has a very important influence on Bills of Exchange.

Q. 87. “Do not you recollect, that during the Bank restriction law, there did not remain a circulation of Bank of England notes in parts of Lancashire for the discharge of small payments, but that, in point of fact, the great commercial transactions of Lancashire were carried on by the intervention of Bills of Exchange, performing the ordinary functions of currency by means of promissory notes?—Unquestionably, and a very large amount of these payments are still in existence.

Q. 88. “When payments do take place by these means, do not bills of exchange answer, in a great measure, the functions of promissory notes, though there is a difference in the character of the transaction between a bill of exchange and a promissory note?—Yes, they are a medium for the exchange and distribution of commodities, no doubt.

Q. 89. “They are the representatives of commodities?—Yes; they are representatives of transactions in commodities.

Q. 90. “Then are they not currency?—No, I do not think that follows.

Q. 91. *Mr. O'Connell*—“What is currency but an instrument of exchange?—It is an instrument of exchange, but it is an equivalent also for commodities.

Q. 92. A bill of exchange performs that function, it assists to exchange commodities?—Yes, a bill of exchange assists in the exchange and distribution of commodities.

Q. 93. “Then it has that function of currency?—Yes, it has.

Q. 94. “Then, having that function of currency, which, perhaps, is the only function, can you distinguish that from currency? What is there in your mind to induce you to say that that is not currency which performs the functions of currency?—I have already explained that the difference between a bill of exchange and currency is this, that the one discharges a debt and the other does not.

Q. 95. *Mr. Warburton*—“If a party receiving a bill of exchange indorsed, were you to give a receipt in full for the pay-

ment of the debt, would not that bill of exchange perform precisely the same functions as a bank note does?—Yes, but it would be merely a party consenting to accept a debt due from another person in full discharge of the debt due to himself.

Q. 96. *Mr. Herries*—“Is not that a very common proceeding in trade?—I am not aware of that. If I am asked whether parties accept bills of exchange for debts, that is a fact, but whether they accept them in full discharge of a debt contracted, I am not aware.

Q. 97. *Mr. Gisborne*—“Do you consider a £10 note of a country bank, a joint stock bank, to rank under eurrency, or to rank under bills of exchange?—Under eurrency.

Q. 98. *Mr. Grote*—“Suppose there was a seven-day post bill issued by a banker, would you consider that a part of the eurrency?—No.

Q. 99. *Mr. Lubouchere*—“Suppose it was a seven-day post bill issued by the Bank of England?—No, not until discharged.

Q. 100. *Mr. O'Connell*—“A cheque on the Bank is eurrency in London, is it not?—It performs the function of eurrency; it is a transfer of eurrency from one to another.

Q. 118. *Mr. Wood*—“Will you define what you mean as constituting the entire eurrency of the country?—I should define eurrency to be gold and silver, or the promises of bankers to pay on demand, which either constitute a legal tender, or which the public are willing to accept in lieu of coin in discharge of debts. I consider the eurrency in this country to consist first of coin in circulation; secondly, of Bank of England notes issued against bullion, and of Bank of England notes issued against securities; thirdly, of deposits in the Bank of England, payable on demand, the same as bank notes; fourthly, of notes issued by the Country Banks; and fifthly, of deposits in country banks in their own notes, which are of the same character as deposits in the Bank of England.”

As to the meaning of deposits, and the general confusion as to the way in which they arise, we may refer to the exposition of the Mechanism of Banking given in the preceding section. The witness was further examined at immense length, but the above gives the substance of his opinions.

Mr. COBDEX was of opinion that no inflation of the eurrency would arise from bills of exchange, provided the money of the country were not previously inflated. There is a great distinction between a bill of exchange and a bank note. A bill of exchange follows the trading transaction, and is merely a voucher for the transaction, in the shape of a transfer of the debt, or an acknowledgment of the debt; but a bank note put into circulation either in the purchase of public securities or in a loan, or in any other way, goes to the artificial creation of com-

mercial transactions, and is not itself necessarily originated by the transaction. Bills of exchange can multiply only in proportion to commercial transactions, provided the currency be kept as a metallic currency.

Mr. Cobden said that, with a metallic currency, there would be no risk of any great extent of accommodation bills; an opinion which we think is scarcely warranted by the reality.

Q. 572. *Mr. Smith*—"Inasmuch as bills of exchange are used at Manchester as an instrument of exchange, do they not form part of the currency?—No; I have defined currency to be money. I cannot call a bill of exchange money. It is a promise to pay money at a certain time, and it is a security only for a certain time, after which all securities are forfeited."

Mr. W. R. WARD (Q. 674) considered currency to be coined gold, silver, and copper, and notes payable on demand, issued by the Bank of England and country banks.

Mr. RICHARD PAGE understood currency to mean the current money of a country, in which debts are discharged and commodities purchased and sold, and consisting of Bank of England notes and gold and silver. Country bank notes he considered only to be money by courtesy. He included deposits in the Bank of England; but, as he gave to the word "deposit" an inaccurate meaning, we do not know what he would have done if he had understood the real meaning.

Mr. GEORGE WARDE NORMAN, a Director of the Bank of England, was asked:—

Q. 1691. "Are there any grounds for considering the deposits of the Bank of England as currency?—No, I think not.

Q. 1692. "Do you consider that any deposits, merely in their character of deposits, can be considered as currency?—No, I do not.

Q. 1693. "Will you state what, in your opinion, forms the distinction between currency and deposits?—I consider that, looking broadly at deposits and currency they are quite distinct; they have little to do with each other. But I conceive that the use of deposits is one of the banking expedients, which is available for economising currency, along with a great many others. I do not consider them as currency or money. I ought to observe, perhaps, to the Committee, that I employ the words 'money' and 'currency' as synonymous. Deposits are used by means of transfers made in the books of bankers; and these afford the means of adjusting and settling transactions, and *pro tanto* dispense with a certain quantity of money; or they may be set off against each other, from one banker to another, to a certain extent, and thus produce the same effect. Still they possess the essential qualities of money in a very low degree.

Q. 1694. "Do you entertain a similar opinion as to bills of exchange?—Yes, exactly; I think they are also used to

economise currency. I look upon them as banking expedients for that purpose; but they do not possess fully the qualities which I consider money to possess.

Q. 1695. "Will you explain the difference between the functions which money will perform and those which bills of exchange or deposits will perform?—To answer that question fully, one must, I am afraid, take rather a wide view; but I look upon it that the three most essential qualities money should possess are, that it should be in universal demand by everybody, in all times and all places; that it should possess fixed value; and that it should be a perfect numerator. There are other qualities; but I think these are the most essential. Now, when I look at all banking expedients, I find they do not possess these qualities fully. They possess them in a very low degree; and, therefore, as we see took place in the Autumn of 1835, with a very large increase of the deposits of the Bank, the circulation diminished, and there was every appearance of the effects of contraction: there was an increased influx of treasure; and I conceive from that there were lower prices. By a numerator I mean that which measures the value of other commodities with the greatest possible facility. If we look at all these banking expedients, we see that they possess the three qualities which I have mentioned in a very much lower degree.

Q. 1696. "Will you state in what respect?—I can only take them one by one. A bill of exchange is an instrument commonly payable at some future time, at a certain place, and to some particular individual; it is of no use to any other individual, except it is indorsed to him. A man cannot go into a shop with a bill of exchange and buy what he wants; he could not pay his labourers with a bill of exchange. The same with a banker's deposit, he can do nothing of that sort with that; he can do with less money than he would otherwise employ, if he has bills of exchange, or bankers' deposits; but he cannot, with bills of exchange or bankers' deposits, do whatever he could with sovereigns and shillings. By a banker's deposit, I mean a credit in a banker's books; nothing more nor less than that."

MR. SAMUEL JONES LOYD, now LORD OVERSTONE, was asked:—

Q. 2655. "What is it that you include in the term circulation?—I include in the term circulation, metallic coin, and paper notes promising to pay the metallic coin to bearer on demand.

Q. 2661. "In your definition, then, of the word circulation, you do not include deposits?—No, I do not.

Q. 2662. "Do you include bills of exchange?—No, I do not.

Q. 2663. "Why do you not include deposits in your definition of circulation?—To answer that question, I believe I must be allowed to revert to first principles. The precious metals are distributed to the different countries of the world by the opera-

tion of particular laws, which have been investigated and are now well recognised. These laws allot to each country a certain portion of the precious metals, which, while other things remain unchanged, remains itself unchanged. The precious metals, converted into coin, constitute the money of each country. That coin circulates sometimes in kind; but, in highly advanced countries, it is represented to a certain extent by paper notes, promising to pay the coin to bearer on demand; these notes being of such a nature in principle that the increase of them supplants coin to an equal amount. Where those notes are in use, the metallic coin, together with those notes, constitute the money or currency of that country. Now, this money is marked by certain distinguishing characteristics; first of all, that its amount is determined by the laws which apportion the precious metals to the different countries of the world; secondly, that it is in every country the common measure of the value of all other commodities, the standard, by reference to which the value of every other commodity is ascertained, and every contract fulfilled; and, thirdly, it becomes the common medium of exchange for the adjustment of all transactions equally at all times, between all persons, and in all places. It has, further, the quality of discharging these functions in endless succession. Now, I conceive that neither deposits nor bills of exchange, in any way whatever, possess these qualities. In the first place, the amount of them is not determined by the laws which determine the amount of the precious metals in each country; in the second place, they will in no respect serve as a common measure of value, or a standard, by reference to which we can measure the relative value of all other commodities; and, in the next place, they do not possess that power of universal exchangeability which belongs to the money of the country. If the Committee will allow me to refer to it, there is a passage in the report of the French Chambers which has recently been appointed to inquire into a subject very similar to that which this Committee is now investigating, which seems to me to put the point of the universal exchangeability of money in a very striking way:—*‘Si l'on réfléchit en effet aux innombrables transactions commerciales qui s'opèrent chaque jour, depuis celles qui doivent fournir aux plus modestes consommations jusqu'à celles qui multiplient les spéculations, les plus entreprenantes du commerce international, on s'aperçoit aisément qu'elles ne s'accompliraient pas sans le secours d'une valeur intermédiaire qui puisse être mise successivement en rapport avec toutes les autres valeurs, et servir entre elles de moyen d'estimation et d'échange.'*

Q. 2664. "Why do you not include bills of exchange in circulation?—I exclude bills of exchange for precisely the same reasons that I have stated in my former answer for excluding deposits. There is another passage in the same report which

appears to me to shew very clearly that the French Chamber have fully appreciated the distinction between bills of exchange and money:—‘Tout engagement par écrit de payer une somme due a pu devenir ce signe du numéraire; le signe a acquis quelques-uns des avantages de la monnaie circulante, lorsque, comme le billet à ordre et la lettre de change, il a pu être transmis par la voie facile et prompte de l’endossement. Mais que d’entraves encore! Il ne représente pas à tout moments pour son détenteur la somme pour laquelle il a été souscrit, elle peut n’être payable qu’ à un terme éloigné, pour le réaliser immédiatement il serait nécessaire de la céder. Trouvera-t-on quelqu’un qui soit assez confiant pour l’accepter? On ne le transmettra qu’en le garantissant de sa signature; c’est une obligation éventuelle que l’on contracte soi-même, et sous le poids de laquelle jusqu’au jour de l’échéance, on sentira son crédit gêné. On n’est pas toujours disposé à révéler la nature de ses affaires par les signatures que l’on met en circulation ces inconvénients devaient conduire à trouver un signe de numéraire plus actif encore et plus commode, qui participât, comme la lettre de change et billet à ordre, des qualités de numéraire métallique, puisqu’il n’a d’autre mérite que de le représenter, mais qui permit de s’en procurer à tout moment; qui, comme la pièce de monnaie se transmet de main en main, sans avoir besoin d’être garanti, sans laisser de traces de son passage. Le billet au porteur et à vue, émis par des associations puissantes, formés sous l’autorisation et agissant sous la surveillance continue des gouvernements à paru présenter ces avantages. De là les banques de circulation.’

Q. 2665. “Under similar circumstances, will the aggregate amount credited to depositors in bankers’ books bear some relation to the quantity of money in the country?—During temporary fluctuations in the amount of circulation, all other things remaining unchanged, I conceive the amount of deposits will be affected by such fluctuations.

Q. 2666. “Is the amount of bills of exchange dependent in some degree on the quantity of money?—I apprehend that it is dependent in a very great degree. I consider the money of the country to be the foundation, and the bills of exchange to be the superstructure, raised upon it. I conceive that bills of exchange are an important form of banking operations, and the circulation of the country is the money in which these operations are to be adjusted; any contraction of the circulation of the country will, of course, act upon credit; bills of exchange, being an important form of credit, will feel the effect of that contraction in a very powerful degree; they will, in fact, be contracted in a much greater degree than the paper circulation.

Q. 2667. *Sir Robert Peel*—“What are the elements which constitute money in the sense in which you use the expression

'quantity of money?' What is the exact meaning you attach to the words 'quantity of money—quantity of metallic currency?'—When I use the words quantity of money, I mean the quantity of metallic coin and of paper notes, promising to pay the coin on demand, which are in circulation in this country.

Q. 2668. "Paper notes payable by coin?—Yes.

Q. 2669. "By whomsoever issued?—Yes.

Q. 2670. "By country banks as well as other banks?—Yes.

Q. 2671. *Chairman*—"Would this superstructure, consisting of sums credited to depositors in bankers' books and bills of exchange, equally exist, although no notes payable in coin on demand existed in the country?—Yes; I apprehend that every question with respect to deposits, and with respect to bills of exchange, is totally distinct from the question which has reference to the nature of the process of substituting promissory notes in lieu of coin, and of the laws by which that process ought to be governed. If the promissory notes be properly regulated, so as to be at all times of the amount which the coin would have been, deposits and bills of exchange, whatever changes they may undergo, would sustain those changes equally, either with a metallic currency, or with a paper currency properly regulated; consequently, every investigation respecting their character or amount, is a distinct question from that which has reference only to the substitution of the paper notes for coin.

Q. 2672. "There would be no reason why, if there were no notes payable in coin on demand, the amount of this superstructure should be less than it now is, with a mixed circulation of specie and of notes payable on demand?—None whatever. I apprehend that, upon the supposition that the paper notes are kept of the same amount as the metallic money, the question of the superstructure, whether of deposits or of bills of exchange, remains precisely the same.

Q. 2673. "That answer takes for granted that, in the first case, the metallic currency, and, in the second case, the metallic currency, plus the notes payable on demand, are the same in quantity?—Yes.

Q. 2674. *Sir Robert Peel*—"You suppose the notes payable on demand to displace an amount of coin precisely equal to those notes?—They ought to do so under a proper regulation of the paper money, otherwise they are not kept at the same value as coin.

Q. 2675. *Mr. Attwood*—"Would you consider that the superstructure of bills of exchange, founded entirely upon a metallic currency, might, at particular times, become unduly expanded?—The answer to that question depends entirely upon the precise meaning of the word 'unduly.' I apprehend, undoubtedly, that it is perfectly possible that credit, and the consequences which sometimes result from credit, viz., over-banking in all its forms,

and the over-issue of bills of exchange, which is one important form of over-banking, may arise with a purely metallic currency; and it may also arise with a currency consisting jointly of metallic money and paper notes promising to pay in coin; and I conceive, further, that if the notes be properly regulated, that is, if they be kept at the amount which the coin otherwise would be, whatever over-banking would have arisen with a metallic currency, would arise and to the same extent, neither more or less, with money consisting of metallic coin and paper notes jointly.

Q. 2676. "May not over-banking and over-issue of bills of exchange, forming a superstructure based upon money composed of metal and paper notes, derange the certainty of the notes being duly paid in gold?—I apprehend that if the paper notes be properly regulated, according to the sense which I have already attributed to that expression, and if a proper proportion of gold be held in reserve, the solidity of the basis cannot be disturbed; that is, that if there be a proper contraction of the paper notes as gold goes out, the convertibility of the paper system will be effectually preserved by the continually increasing value of the remaining quantity of the currency, as the contraction proceeds.

Mr. TOOKER was asked—"In using the term 'circulation' of the Bank of England, what do you include in that term?—I include in that term only the Bank notes in the hands of the public. In order to avoid confusion, perhaps the Committee would allow me to state the meaning which I attach to the different terms 'currency' and 'circulating medium.' The currency I consider to be, in strictness of language, according to the apparent derivation of the term, that part of the circulating medium, such as the coin of the realm, and Bank of England notes and country bank notes (although not a legal tender), which pass current from hand to hand, without individual signature, such as appears on drafts or indorsements. I am doubtful whether cheques on bankers might not be included, from their perfect similarity to Bank notes, in many of the purposes for which they are employed; at the same time, there is the feature of distinction which I have mentioned, viz., that cheques require the signature of the party passing the draft, and that they do not pass from hand to hand. Bills of exchange I consider as a part of the general means of distributing the productions and revenues of the country, and, therefore, as constituting a part of the circulating medium. I consider, also, that the simple credit by which goods are, in many instances, bought and sold, come likewise under the general description of the circulating medium, in as far as the prices of commodities are in question; because a simple contract of sale, whether any payment eventually passes or not, is commonly entered in the

price currents without distinctions from those for which any actual payment is made. I cannot consider that transferable debts constitute circulating medium, but only the actual transfers.

Q. 3279. "What do you mean by transferable debts?—The deposits in the hands of bankers, against which the depositors are entitled to pass their drafts.

Q. 3280. *Mr. Grote*—"You include, not simply transfers of deposits in the hands of the Bank of England, but also transfers of deposits in the hands of other bankers?—Yes; transfers of deposits generally.

Q. 3281. *Chairman*—"Do you then consider a deposit to be a transferable debt owing by the banker to the depositor?—Yes.

Q. 3282. "In the use of the term 'currency' in your future examination, do you propose, in addition to coin, Bank of England notes, and country bank notes, to include cheques upon bankers?—Yes; I think upon the whole the distinction I have mentioned is not sufficient to exclude them, and, therefore, I shall propose to consider them as included.

Q. 3283. *Mr. Warburton*—"By cheques, you mean cheques actually drawn, and passing from one person to another?—Yes; that which is current, in fact.

Q. 3284. "Will you be good enough to state what you propose to include in the word 'circulation' in the course of your future examination?—I propose to include in the term 'circulation' the notes of the Bank of England, and of country banks, payable on demand.

Q. 3285. "What do you mean by 'circulating medium'?—I mean all instruments of interchange by which the productions and the revenue of the country are distributed; everything which serves and is received as a mode of payment, or which constitutes nominal money-price which appears in price currents.

Q. 3286. *Mr. Grote*—"There is the currency, and there are also certain expedients for economizing the use of the currency; you would call both one and the other of those portions of the circulating medium?—Precisely.

Q. 3287. "Do you include, in the word 'currency,' bills of exchange?—No.

Q. 3288. "If you include, in the term 'currency,' a crossed cheque payable at a banker's, to be presented, therefore, at the Clearing House, and having, therefore, before presentation not more than seven or eight hours to run, why is it that you do not include in the term 'currency' a bill of exchange payable also at a banker's, falling due to-morrow, and having, probably, not more than about 24 hours to run?—It is only a question of the general acceptance of the term; there is no essential distinction in the particular case. I may, perhaps, be allowed to say, that the only question as to the employment of different descriptions

of circulating medium is referable to the combined considerations of economy, convenience, and security.

Q. 3289. "If the cheque, according to the supposition in the former question, be included in the term 'currency,' will not a bill of exchange, due to-day, payable at a banker's, be entitled also to be included in that term?—It is only a question of convenience in the classification; I am not aware that it is of any importance in practical operation.

Q. 3290. "Bills of Exchange having, previous to maturity, one, two, three, four, or more days to run, differ in character by insensible degrees from a crossed cheque, a crossed cheque being that bill which has the shortest time to run?—They differ in character by insensible degrees, and likewise in the trifling difference of convenience from their not being used till maturity, unless under a calculation of discount.

Mr. Tooke then started a theory which, like many others, is true in some cases, and which, we believe, he was the first to notice; but which he pushed to an extreme, which drew out some just strictures from Colonel Torrens.

Q. 3292. *Mr. Hume*—"Will you state what part of the currency, or circulating medium, affects prices, under the definitions which you have now given?—No one part of them affects the prices of commodities more than any of the other parts.

Q. 3293. *Mr. Grote*—"Do you mean not more in degree, or not in any different way?—Not more in degree.

Q. 3294. "You mean that every portion of that which you have described under the name 'circulating medium' is perfectly equal to every other portion in the effect which it produces upon prices?—Perfectly so.

Q. 3295. *Mr. Hume*—"Do you mean that every transaction of purchase or sale by any of the means which you have mentioned, as included in the circulating medium, equally affects prices?—Yes; and that was my reason for caring so little about making a distinction among them. I doubt whether they operate upon prices at all.

Q. 3296. *Mr. Grote*—"You mean that none of these items which you have enumerated under the general term 'circulating medium' have in your opinion any effect upon prices?—Yes; I mean that they are not operative causes of prices.

Q. 3297. *Mr. Hume*—"What is it, then, which does affect prices?—The cost of production limiting the supply on the one hand, and the pecuniary means of the consumer limiting the demand on the other.

Q. 3298. "Will not the variations in the quantity of the circulating medium affect prices?—No.

Q. 3299. "Will it not, if abundant, be more at the disposal of individuals for purchases than when it is scarce?—It will be more easily disposable, but it will not be necessarily so disposed

of. I believe that the amount of the circulating medium is the effect, and not the cause, of variations in prices.”

Such are the various opinions and arguments brought forward to draw a distinction between bills and notes as currency, and we may now examine them seriatim.

I. *That Bills of Exchange are only the Evidence of a Debt.*

This is equally true of Bank Notes, and we have seen that money itself, by the acknowledgement of a long series of writers, is itself nothing more than the evidence of debt. It is a general Bill of Exchange upon all the commercial community; and is only the highest and most general form of credit. The payment of a Bill in money is only the exchange of a particular and precarious instrument of credit for a general and permanent one.

II. *That Bills of Exchange do not discharge Debts, but they require to be paid in Currency.*

It is a very great error, indeed, to say that Bills of Exchange do not discharge debts. We have said something more below about the effect of taking Bills of Exchange for debts. But Bills of Exchange, the day they become payable, are payable on demand like cheques and bank notes, and they are set off against each other among bankers, and at the Clearing House in London, to the amount of several millions daily. They discharge each other by mutual set off, just in the same way that notes and cheques do. There are, besides, other ways in which Bills are paid, as is fully shewn in the preceding section, explaining the mechanism of banking. A trader, when his bills become due, discounts fresh bills with his banker, who creates fresh credit, and bills are paid by giving cheques on this credit.

Mr. NORMAN said that money, or currency, should possess fixed value, and be a perfect numerator. But how can money, or any thing, possess fixed value, when its value is changing from hour to hour?—An instrument of credit may preserve an equality of value with respect to money, but not with respect to anything else, unless it is expressed to be payable in it. He said that he meant by a numerator that which measured the value of other commodities with the greatest facility. Why does a promise to pay £50 measure the value of things with less facility than £50 itself?

It is not a little amusing to find the celebrated phrase of the Roman Catholic Church—*Quod semper, quod ubique, quod ab omnibus*, starting up and meeting us in a discussion on currency. In Lord Overstone's opinion money and currency are identical, and include the coined metallic money, and the paper notes promising to pay the bearer coin on demand; and, he says, that

the characteristic of their being money is, that they are received equally at "*all times, between all persons, and in all places.*" For the sake of shortness, let us designate this phrase by 3A, from the three alls in it. He excludes Bills of Exchange from the designation of currency, because "they do not possess that power of universal exchangeability which belongs to the money of the country." This definition is fatal to Lord Overstone's own view. In fact, if it be true, there is no such thing as money or currency at all. In the first place, it at once excludes the whole of bank notes. The notes of a bank in the remote district of Cumberland, would not be current in Cornwall, *therefore* they are not 3A, *therefore* they are not currency. Again, the notes of a bank in Cornwall would not be current in Cumberland, *therefore* they are not currency. Similarly there are no country bank notes which have a general currency throughout England, *therefore* no country bank notes are 3A, *therefore* no country bank notes are currency. Till within the last thirty years or so, Bank of England notes had scarcely any currency beyond London and Lancashire; in country districts a preference was universally given to local notes, *therefore* Bank of England notes were not 3A, they had not a power of "universal exchangeability," *therefore* they were not currency. Bank of England notes would, even now, not pass throughout the greater part of Scotland. If, therefore, the test of 3A and "universal exchangeability," be applied, the claims of all bank notes to be considered as currency are annihilated at once. The acceptance of a Baring, or a Rothschild, would be received in payment of a debt by a far larger circle of persons than the notes of an obscure and remote country bank.

But the universality of Lord Overstone's assertion is fatal to his argument in other ways. On the Continent, silver is the legal standard of value; in England, silver, like copper, is merely coined into small tokens, called shillings, &c., which are made to pass current above their natural value, and are only legal tender for a very trifling amount, hence it cannot be used in the adjustment of *all* transactions, *therefore* it is not 3A, *therefore* it is not currency. There are other countries where gold is not a legal tender, *therefore* it fails to satisfy Lord Overstone's test, *therefore* it is not currency. If, then, the test proposed by Lord Overstone be considered as correct, it is easy to see that there is no substance or material whatever that will not fail under it, and, *therefore*, *there is no such thing as currency.*

The fact is, that the only difference between a Bill of Exchange and a Bank Note is, that the former is a promise of a deferred payment, and the latter that of an immediate one, and there is less risk in taking the latter than the former. From these circumstances, a Bank Note possesses a greater *degree* of circulating power than a Bill of Exchange. But, in the Midland Counties

of England, it used to be quite common for the banks to issue the Bills of Exchange they had discounted with their own indorsement upon them. In which respect they were in every way equivalent to Bank Notes; moreover, there is not the same inducement to put a bill into circulation as a Bank Note, because the former increases in value as the day of payment approaches. But it is unprofitable to keep a note idle. But it is to the last degree unphilosophical to maintain that these two obligations are of different *natures*, because they are adapted in different *degrees*.

We may quote from Colonel Torrens, as he expresses a view that is by no means uncommon, but which is quite erroneous. He says (*The Principles and Practical Operation of Sir Robert Peel's Act of 1844 explained and defended*, p. 79):—"The term money and currency have hitherto been employed to denote those instruments of exchange which possess intrinsic or derivative value, and by which, from *law or custom*, debts are discharged and transactions finally closed. Bank Notes, payable in specie on demand, have been included under these terms as well as coin, because, by law and custom, the acceptance of the notes of a solvent bank, no less than the acceptance of coin, liquidates debts and closes transactions; while bills of exchange, bank credits, cheques, and other instruments by which the use of money is economised, have not been included under the terms money and currency, because the acceptance of such instruments does not liquidate debts and finally close transactions."

It is upon such views as these that the opinion of those rests who maintain that bills of exchange are not currency or circulating medium. They suppose that bank notes pass without indorsement, and that bills of exchange do not. Even if that were true, it would not be any valid ground for the distinction, because such a thing would in no way affect the nature of the instrument. It is wholly untrue to suppose that bank notes and money are the only things which close transactions. By the table given above, it is seen that upwards of 95 per cent. of commercial payments and receipts were made by Messrs. Morrison and Co. in instruments of credit, other than bank notes.

But it is a very great mistake to say that bank notes pass without indorsement and bills of exchange do not. At the time the Bank of England was founded, it was quite illegal for any such thing as promissory notes to pass by assignment. The negotiability of bank notes had to be provided for by the Act. It was enacted, that all the Bank's bills, obligatory and of credit, made or given to any person, might, *by indorsement of such person*, be freely assigned to any person who should voluntarily accept them, and so by such assignees *toties quoties* by indorsement thereon, and all such assignees might sue thereon in their own names.

The assignment of the Goldsmiths' notes, or the private banker's note, was held to be illegal much later than this. In 1703 it was decided that no promissory notes were assignable or indorsable over within the custom of merchants. In 1704, the Act was passed which allowed promissory notes to be assigned by indorsement like Bills of Exchange. It is true that the *custom* of indorsing Bank of England Notes, and, it is probable, country bank notes too, soon fell into disuse, but that makes no difference in the *law* of the subject.

The case of *Miller v. Race* has often been quoted in support of the doctrine, that Bank Notes are money or currency, to the exclusion of Bills of Exchange, but the true bearings of that case have been completely misunderstood. In that case, the whole point turned on how the property in a stolen note would pass, and it was held that it would pass like that of a stolen Bill of Exchange. It had long been held that, for the convenience of commerce, the innocent holder for value of a stolen Bill should be able to retain it against the former owner, just as if it were money, to which this principle had long been applied. By the case of *Miller v. Race*, this principle was *extended* to Bank Notes, and it has been confirmed by numerous cases since. The only effect of this case was, that the principle which Bills had in common with money was now held to extend to notes, so that, if there be any force whatever in it, it proves that Bills were held to be currency long before notes.

It is also an error to suppose that Bills of Exchange require an indorsement at each transfer. A Bill of Exchange may be made payable to bearer, and then it requires no indorsement at all. Bills, however, are generally drawn payable to order, and then they require that the payee should indorse them; but he may do that without making himself liable on them, as is done in many cases. After the first indorsement in blank, the Bill is payable to bearer, and may be passed by mere delivery, in all respects like a Bank Note. "And," says Mr. Justice Byles (*A Treatise on the Law of Bills of Exchange, &c.*, 8th Edit., p. 146), "a transfer by mere delivery, without indorsement, of a Bill of Exchange, or Promissory Note, made or become payable to bearer, does not render the transferor liable *on the instrument* to the transferee.

"And it is conceived to be the general rule of the English law, and the fair result of the English authorities, that the transferor is not even liable to refund the consideration, if the bill or note so transferred by delivery, without indorsement, turn out to be of no value by reason of the failure of the other parties to it. For the sending to market of a bill or note payable to bearer without indorsing it, is *primâ facie* a sale of the bill. And there is no implied guarantee for the solvency of the maker, or of any other party.

“If a bill, or note, made or became payable to bearer, be delivered without indorsement, not in payment of a pre-existing debt, but by way of exchange for goods, for other bills or notes, or for money transferred to the party delivering the bill at the same time, such a transaction has been repeatedly held to be a sale of the bill by the party transferring it, and a purchase of the instrument, with all risks, by the transferee. ‘It is extremely clear,’ says Lord Kenyon, ‘that if the holder of a bill send it to market without indorsing his name upon it, neither morality, nor the law of this country, will compel him to refund the money for which he sold it, if he did not know at the time that it was not a good bill.’ So, when A gave a bankrupt, before his bankruptcy, cash for a bill, but refused to allow the bankrupt to indorse it, thinking it better without his name, and afterwards, on dishonor of the bill, proved the amount under the commission, the Lord Chancellor ordered the debt to be expunged, observing, that this was a sale of the bill. So, if a party discounts bills with a banker, and receives, in part of the discount, other bills, but not indorsed by the banker, which bills turn out to be bad, the banker is not liable. ‘Having taken them without indorsement,’ says Lord Kenyon, ‘he has taken the risk on himself. The bankers were the holders of the bills, and, by not indorsing them, have refused to pledge their credit to their validity; and the transferee must be taken to have received them on their own credit only.’ So where, in the morning, A sold B a quantity of corn, and, at three o’clock in the afternoon of the same day, B delivered to A, in payment, certain promissory notes of the Bank of C, which had then stopped payment, but which circumstance was not at the time known to either party, Bayley, J., said, ‘If the notes had been given to A at the time when the corn was sold, he could have no remedy upon them against B. A might have insisted on payment in money, but, if he consented to receive the notes as money, they would have been taken by him at his peril.’ Such seems the general rule governing the transfer by delivery, not only of ordinary Bills of Exchange and Promissory Notes, but also of Bank Notes. Nor is there any hardship in such a rule, for the remedy against the transferor may always be preserved by indorsement, or by special contract.”

While it has always been acknowledged that the delivery of a bill without indorsement, in exchange for a valuable consideration, is a sale of it, it has frequently been said that, if the bill be indorsed, it is only a loan. We have pointed out the ambiguity of the word *loan* already under § 4. It is often said that a banker lends his customer money on the security of bills. But this is an inaccurate mode of statement. What the banker does is to buy a debt due to his customer, and, when he indorses the bill, his customer gives him a limited warranty of its sound-

ness. If the banker lent his customer the money, it would be his duty to repay it. But that is not so. It is the acceptor's business to pay the bill, and, if he do not do so, the banker may, by giving his customer immediate notice, and making a demand, make his customer take back the bill, and repay the money. But if the banker fail in giving immediate notice his remedy against his customer is gone.

But the *Law of Continuity* shews the fallacy of the doctrine that Bank Notes payable to bearer on demand alone are currency. Lord Overstone rigorously restricts the term to such notes. But would not notes payable one minute after demand be currency? or one hour? or two, or three, or four hours? Would not notes payable one day after demand be currency? or two or three days? Lord Overstone denied that Bank post bills, which are issued payable seven days after sight, are currency. According to this doctrine, if a man deposits money in the Bank and receives in exchange for it a bank note payable on demand—that is currency; but if he ask, for his own convenience, for a note payable seven days after sight—that is not currency! But the note becomes payable on demand on the seventh day after sight, and then, by their own definition, it is currency. What was it before? It used formerly to be the custom for banks in the country to issue notes payable 20 days after demand. These notes circulated and produced all the effects of money. What were they, if they were not currency? Cheques are payable on demand. How are they not currency as much as notes? How are Bills of Exchange not currency on the day they become payable? And, if they are so then, what were they before? It is quite plain that there can be but one answer. They are all species of currency, though differing in degree, and the distinction between them is untenable.

It would be too long to mention the host of writers who have expressly included all forms of paper credit under the title of currency. Mr. Mill truly says there is no generic distinction between bills and notes. We rejoice to say that M. Michel Chevalier is entirely of the same opinion as ourselves. In his treatise *La Monnaie*, sect. 3, c. v., after shewing the untenable nature of the distinction set up between Bank Notes and Bills of Exchange, he says:—"La langue Anglaise a un mot générique qui embrasse la monnaie, le billet de banque, le papier-monnaie ou assignat non convertible en espèces, et tout autre espèce de titre qu'on peut mettre dans la circulation et qu'accepte plus ou moins le commun des hommes; c'est le mot de *currency*. Notre langue n'en offre pas l'équivalent parfait. Cependant le terme de *numéraire* pourrait être pris dans le même sens, et je l'emploierai ainsi dans la suite de cet écrit." And in the number of the *Journal des Economistes*, for August, 1862, in which the same distinguished writer has published the substance of a Report to

the Imperial Institute of France on our *Elements* and *Dictionary*, he re-affirms the same opinion. After explaining the ideas contained in the former part of this work, he says:—"A ce même point de vue, et sous le bénéfice de ce commentaire, la relation intime qu'établit M. Macleod entre la notion de la *currency*, et l'idée d'une dette ou d'une obligation sérieuse et positive a un mérite incontestable."

But, while we contend that Lord Overstone's criterion of a currency is fatal to his own view, we are quite willing to accept it. For what is it that exists in all places, in all times, and among almost all persons? DEBT, or SERVICES DUE. And what is it that is universally required to measure, record, and transfer them? *Some material*. But we see that all currencies are more or less local, none are universal. The idea, or the want alone, is universal. The notes of a country banker, only circulating in his own neighbourhood, are like a country *patois*, each district has its own. A national currency rises to the dignity of a language. But even that is only local, on a larger scale. The ideas only expressed in the language are universal. We are, therefore, strengthened in our conviction, that the only true idea of a currency is, that it is the *Representative of Transferable Debt*, and that *whatever represents Transferable Debt is Currency*.



CHAPTER IV.

THE THEORY OF THE COINAGE.

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MEANING OF BULLION—COIN—MINT PRICE AND MARKET PRICE—WHAT IS A POUND?—ON A DOUBLE STANDARD.

1. Most nations, even the rudest, have felt the advantage of employing some substance to perform the functions of a currency. We have noticed, in the first chapter, most of the substances which have been used for this purpose by different nations. A metal, however, of some sort has been found to possess the greatest advantages, and of these, gold, silver, and copper, have been chiefly preferred.

Gold and silver, however, in a perfectly pure state are too soft to be used for this purpose, and it is necessary to mix some other metal with them to harden them, which is called alloy. By a chemical law, whenever two metals are mixed together, the compound is harder than either of them in a pure state.

When gold and silver are in the mass, they are called **BULLION**, which, of course, may be of different degrees of fineness. But as the laws of all countries in which bullion is coined into money define the quantity of alloy to be mixed with the pure metal, we shall use the word **Bullion** to mean gold, or silver, in the mass, mixed with such a proportion of alloy as is ordered by law, so as to be fit to be coined.

Some nations have used **Bullion** as a circulating medium; but the merchants of those nations were obliged to carry about with them scales and weights to weigh out the bullion on each occasion. This was usual among the Jews. In some countries it is necessary both to weigh and assay the bullion at each operation, which, of course, is a great impediment to commerce.

Other nations adopt a more convenient practice. They divide the bullion into pieces of a certain definite weight, and affix some public stamp upon it to certify to the public that these pieces are of a certain fixed weight and fineness, and they give them certain names, by which they are commonly known.

These pieces of bullion, with a public stamp upon them to certify their weight and fineness, and called by a publicly-recognized name, and intended to be used for the purposes of commerce without further examination, are called **Coins**.

It may almost appear superfluous to remark that this stamp,

or certificate, in no way affects the value of the metal, or the quantity of things it will exchange for. Its only object is to save the trouble of weighing and assaying the bullion in commercial transactions. Nor can the *name* of the coin in any way affect its *value*. Values, it is true, are estimated in the number of these pieces of bullion or coins, but it is perfectly clear that it is necessarily implied in the bargain that these coins contain a certain definite quantity of bullion.

Nevertheless, although this seems so perfectly clear, it is a confusion on this point which is at the root of all the extravagancies of the currency question, which have so long vexed the public ear. They almost all arise from confounding the *name*, or *denomination*, of a coin, with its *value*, its name with its purchasing power; and from supposing, that if the Legislature chose to call a *shilling* a *pound*, that therefore a shilling would have the value of a pound. Any one who will brand on his mind the simple principle, that although the stamp gives the coin currency, it is the weight of bullion alone which gives it value, will be able to steer his course safely through all the shoals and quicksands of monetary controversies.

We shall see, a little further on, that calling the reader's attention to these self-evident truths, is not so superfluous as it may appear at present.

It is also perfectly evident, that if this process of stamping bullion, and so turning it into coin, is done free of all expense, at the will of any one who chooses to present bullion and demand to have it stamped, and also without any delay, the value of the metal as bullion must be exactly the same as the value of the metal as coin.

If, however, a charge is made for the workmanship, or if any tax is levied on changing the metal from one form into the other, or if a delay takes place in doing so, there will be a difference between the value of the metal as bullion and as coin, and this difference will manifestly be the charge for the workmanship, the amount of the tax, and the quantity of interest accruing during the period of delay.

These, however, are all fixed, or constant quantities, which may be ascertained, and they form the limits of the variation of the metal in one form from its value in the other.

In the following remarks we shall assume that there is no charge for the workmanship of coining, no tax upon it, and no delay in doing it, no obstruction, in short, of any sort to changing the metal from one form to another.

If in any particular cases obstructions should occur, of course, the necessary corrections must be made throughout the course of the following reasonings.

Upon the assumptions, then, above stated, we have this fundamental principle of the coinage:—

Any quantity of metal in the form of Bullion must be exactly of the same value as the same quantity of metal in the form of coin.

On the meaning of the MINT PRICE and MARKET PRICE of Gold and Silver.

2. As the very purpose of coining is to certify that the pieces of bullion are of a certain definite weight and fineness, it is evident that any fixed quantity of bullion, as a pound weight, must always be divided into a fixed number of coins.

The number of coins into which a given quantity of bullion is divided, is called the MINT PRICE of that quantity of bullion.

It is perfectly clear, then, that the Mint Price of Bullion is a fixed quantity, it can by no possibility vary, until the same quantity of bullion is coined into a different number of coins.

To alter the Mint Price of Bullion is merely an expression which means an alteration in the standard weight of the Coinage.

To suppose that the Mint Price of Bullion could vary is manifestly as great an error as to suppose that a hundred-weight of sugar can be a different weight from 112 separate pounds weight of sugar, or that any quantity of wine in a hogshead could be different in quantity from the same quantity of wine in bottles, or that a loaf of bread could alter its weight by being cut up into slices.

Until recent times, when more attention has been paid to the state of the coinage, these coins might circulate for a considerable time in a country, and lose much of their weight, without losing their value. People were so accustomed to attach a certain value to the sight of a particular coin that, unless they were money dealers, they did not stop to inquire too curiously whether it was exactly of the proper weight or not. In fact, when a coinage has been some time in use, few people know what the legal weights of the coins are. Many, for instance, do not associate the idea of a pound with any particular weight of bullion, and thus, in exchange for commodities and services, coins may pass at their nominal value for a considerable time after they have lost much of their weight. Thus Shakespeare says (*Cymbeline*, Act v., Sc. iv.):—

“Tween man and man, they weigh not every stamp,
Though light, take pieces for the figure's sake.”

When coin has been some time in circulation, it must necessarily lose much of its weight from the wear and tear of circulation, even if it be not subjected to any bad practices, such as clipping, which used to proceed to a great extent in this country formerly, as will be shewn a little further on. So late as 1816, when the last great reformation of the coinage took place in England, the greater part of the metallic circulating medium

was nothing but a thin wafer of silver, from which all traces of an impression had long since vanished, and it was reduced to scarcely more than half its legal value.

Coins might circulate in a country for some time after they had lost some of their weight, without any perceptible change in their value with respect to ordinary commerce, but when they were given in exchange for bullion the case would be different. As the value of bullion is measured weight for weight with the coins, it is clear that if the coins have lost their weight, a greater number of them must be given to purchase any amount of bullion than if they are of full weight. Thus, if the Mint Price of silver bullion be 5s. 2d. per ounce, or if that be the quantity of coin into which an ounce of silver bullion is cut, then, if the coins have lost their proper weight from any cause, it is clear that more than 5s. 2d. must be given to purchase an ounce of bullion. It may perhaps require 6s., or even more, to buy an ounce of bullion.

Now, the quantity of coin at its full legal weight, which is equal to a given weight of bullion, is called its MINT PRICE, but the quantity of the current coin which is equal to it in weight is called the MARKET PRICE; and as, if the coins are diminished in weight, more of them must be given than if they are of full weight, the *Market Price* will apparently be higher than the *Mint Price*, and this is called *a rise of the Market Price above the Mint Price*.

This expression, however, has given rise to much error. The plain meaning of it clearly is, that six of the current coins are only equal to what 5s. 2d. ought to be, which merely means, that the current coinage is deficient by 1-6th of its legal weight. Thus, in reality, we see that it is perfectly clear that the rise of the Market Price is due to the DEPRECIATION of the coinage.

Hence we obtain this fundamental law of the coinage—*When the Market Price of Bullion rises above the Mint Price, the excess is the proof and the measure of the depreciation of the coinage.*

In fact, this apparent rise of the Market Price is due to just the same cause as has made the Mint Price of silver bullion apparently rise from £1 in the days of William the Conqueror, to £3 2s. in the present day. It is merely that the same quantity of bullion is cut into a greater number of pieces, and, consequently, each piece must be proportionally diminished in weight, or depreciated.

The Market Price of bullion could never fall below the Mint Price, unless there was more bullion in the coins than there ought to be, and, of course, in such a case, the difference in the Market price below the Mint Price would be the proof and the measure of the excess of the coins above their legal weight.

If the coinage of a country fall into a degraded state, from long

wear and tear, and a new coinage of full weight be issued, and allowed to circulate along with it, one of two effects must inevitably follow. Either those persons who have commodities to sell will make a difference in the nominal price of articles, according as they are paid in the full weighted or the degraded coin, that is, the degraded coin will be at a discount as compared to the heavy coin; or, if there be a law to prevent this, and to make both pass at the same value, bullion dealers will immediately collect all the full-weighted coins they can, and melt them down into bullion, or export them; so that the new coinage will quickly disappear from circulation.

If persons, in selling their goods, are paid in light coin, as they wish to secure a certain weight of bullion in exchange for them, they would, of course, require a larger number of the light pieces than of the heavy ones, so that prices would apparently rise if paid in light money. In such a state of things, the prices of goods are, in a certain sense, fictitious—a number of light pieces are presumed to have the same value as the same number of heavy ones. The weight of bullion given in exchange for commodities, is expressed in a greater number of figures than it ought to be, and, if the law prevents any difference being made between heavy and light pieces, the same number of heavy pieces will purchase no more. This is as great an anomaly in commerce, as it would be to say in arithmetic that three were equal to four. But the consequence is very plain. If four pieces of coin will only purchase as many commodities as three ought to do, no one will turn bullion into coin at so great a disadvantage. On the contrary, as bullion would diminish so much in value, it would be sent to other countries, where it would purchase a greater amount of commodities. During the degraded state of the coinage during the last century, the Market Price of silver always considerably exceeded the Mint Price. Adam Smith says that the Market price of silver ranged from 5s. 4d. to 5s. 8d. an ounce before the re-coinage. And we find it stated in the second Report of the Lords' Committee of Secrecy in 1797, p. 257 :—"But as the Mint Price of silver bullion has been, during nearly the whole of the present century, considerably less than the Market Price of this precious metal, the silver bullion imported could not be converted into coin, but, having left a quantity sufficient for the use of our manufacturers, must have again been exported, and did not contribute in the smallest degree to augment the coin of this kingdom." Moreover, as every one would try to pay his debts in the cheapest medium, or at the least expense to himself, it is evident that he would always try to pay them in the worst coins in circulation, and he would either hoard the good coins, or send them to foreign countries.

If, while the Bank of England were subject to their present law of being compellable to pay notes in exchange for bullion, at

their present rate, the Market Price of bullion were to rise above the Mint Price, it would, in a short time, be fatal to the Bank; for while their notes, which represent coin, would only buy a diminished quantity of bullion, they would be compellable to pay full weight for them, a process which would evidently exhaust their bullion, for nobody would be content to have bank notes in his possession which would only pass for 15s. in the open market, when he could compel the bank to give him 20s. for it. Such a state of things would, therefore, necessarily cause a run upon the Bank, which would not stop while any of its notes remained out, or until the value of the note was restored to par. It was such a state of things which, we shall see, compelled the Bank to stop payment in 1697, three years after it was founded. The Bank received all the worn and clipped coins at their full nominal value, and gave their notes in exchange for them; when the new coinage came out, they were called upon to pay these notes in the new coinage, which, of course, produced a great demand upon them, which compelled them to stop. And the same state of things was grievously felt about 1774, and is the true explanation of the difficulties mentioned by Adam Smith, which he attributes to over-issues by the Bank.

During Sir Robert Peel's administration, in 1844, the currency was beginning to exhibit symptoms of depreciation from its wear and tear. Owing to the effective measures taken by him, it is now almost universally of full weight, and the deficiency in most cases is so slight, that it is not observable in ordinary transactions. The Bank of England, however, warned by experience, weighs rigidly every single sovereign paid into by its customers, and does not credit them with more than its intrinsic value as bullion. Other banks in London find it impossible to maintain the same strictness with their customers, so that, if they pay the money they receive in the course of their business into their account with the Bank of England, they generally incur some loss.

These considerations lead us to a fundamental and universal law in Political Economy, which has been found to be true in all countries and ages—*That bad money drives out good money from circulation*; or, as it is expressed in an anonymous pamphlet, *A reply to the Defence of the Bank, setting forth the unreasonableness of their slow payments.* LONDON, 1696.

“*When two sorts of coin are current in the same nation of like value by denomination, but not intrinsically, that which has the least value will be current, and the other as much as possible will be hoarded,*” or exported, we may add.

The fact of the disappearance of good coin in the presence of bad, was noticed by Aristophanes; and was long the puzzle of financiers and statesmen, who continued to issue good coin from the Mint, and were greatly perplexed by its

immediate disappearance, till Sir Thomas Gresham explained the cause, whence we have called it Gresham's Law of the Currency.

This law is of such fundamental importance in Political Economy, viz., *That good and bad coin cannot circulate together, but the bad coin will drive out the good*, that it may be interesting to quote the passage which contains the earliest notice, that we are aware of, of the phenomenon. During the extreme distress caused by the Peloponnesian war, Athens had for the first time issued a debased gold coinage; the consequence was that the good coin immediately disappeared from circulation. Aristophanes, *Frogs*, 765, says:—"The State has very often appeared to us to be placed in the same position towards the good and noble citizens as it is with regard to the old currency and the new gold; for we make no use at all, either at home or abroad, of those which are not adulterated, but the most beautiful of all money, as it would seem, which are alone well coined and ring properly, but of this base copper, struck only yesterday, and recently of a most villainous stamp. And such of the citizens as we know to be well-born and prudent and honorable gentlemen, and educated in the palaestra, and chorus, and liberal knowledge, we insult. But the impudent and foreigners, and the base born, and the rascals, and the sons of rascals, and those most recently come, we employ." This law, thus first noticed by Aristophanes, has been found to be true in every age and country.

It is also from the same principle that a paper currency is invariably found to expel a metallic currency of the same denomination from circulation. And to show the generality of the principle, it was found in America that when a depreciated paper currency had driven coin out of circulation, and a still more depreciated paper currency was issued, the more depreciated drove out the less appreciated from circulation.

It may, perhaps, be worth while to advert to an error, which is by no means unfrequent. Some writers contend against *fixing* the price of gold, as it is called. It is now acknowledged by every one that it is a great Economical error to attempt to fix the price of any articles. Some writers contend that it is an equal error to *fix* the price of gold. But those who do so overlook a very important consideration. The word "price," except in the single instance "Mint Price," always denotes the quantity of one article which is used as a measure which is given for another article of a *different* nature. Thus we say that the price of a bushel of corn is 6s., when the silver, the substance of which shillings are composed, is of a different nature from coin. But, in the expression *Mint Price* of bullion, it always means the value of bullion expressed in coin of the same metal. Thus the Mint Price of gold bullion means its price expressed

in *gold* coin, and the Mint Price of silver bullion means its price expressed in *silver* coin.

These considerations shew that so long as the coins retain their full legal weight, the Market Price of bullion can by no possibility vary from its Mint Price. If the law requires an ounce of gold to be coined into £3 17s. 0½d., so long as the coins contain their proper weight, it can make no difference in the Market Price whether gold becomes as plentiful as iron, or as scarce as diamonds, for the money always continues of the same weight, whatever be the abundance or the scarcity of bullion. The value of gold may vary with respect to other things; it may purchase more or less bread, or meat, or clothes, or anything else at one time than another; but it is absolutely impossible that its value in bullion can differ from its value in coin. To suppose that it could, would be as irrational as to suppose that because bread became very abundant or very scarce, a loaf of bread could differ from itself in weight when cut up into slices, or a cask of wine differ from itself when drawn off into bottles.

As, however, gold and silver vary in value with respect to each other, and this variation may proceed, nominally at least, either from a diminution in value of one metal, or from a depreciation of the coinage, we are enabled to devise a test by which to decide to which of these circumstances it is due. Thus, in the reign of William III., guineas rose to 28s. and 30s., and silver bullion rose at the same time to 7s. an ounce; one party stoutly contended that this was due to the scarcity of silver. Now, this argument was absurd on the face of it, because, if silver had been extremely scarce as compared to gold, it is perfectly clear that silver would have risen as compared to gold, and not fallen. That is, guineas would have sold for less than 28s. and not more. From the figures given above, this argument was manifestly self-contradictory, because, as compared with gold, silver had apparently *fallen* in value, and, as compared with silver money, it had apparently *risen* in value.

Now, it is quite clear that a *diminution in value* of the coin cannot be followed by any difference between the Market and the Mint Price of bullion. By the meaning of the words "Mint Price," however plentiful, or however scarce, gold may be, an ounce of it in coin must always be equal in value to an ounce of it in bullion. On the other hand, a *depreciation* of the coinage must inevitably be attended by a rise in the Market Price above the Mint Price of bullion, because, however plentiful or scarce gold is, three-quarters of an ounce of it in coin can never be equal in value to one ounce of it in bullion. The case may be shortly stated thus:—Guineas may rise to 25s. in silver, either from a *depreciation* of the silver coinage, or from a *diminution in value* of silver. What is the test? It is to be found in the

Market Price of silver. If the silver coinage is debased, the Market Price of silver will rise above the Mint Price; if it is diminished in value, it will not.

The Mint Price of gold, therefore, in its modern meaning, is nothing more than a public declaration of the weight of metal the law requires to be in the coin, which accidental circumstances have caused to be considered as the legal measure of value in this country; and an alteration of the Mint Price of gold would be simply an alteration in the standard weight of the coin, and would be the same thing in principle as an alteration of the standard yard measure. Those persons who ridicule the idea of having the Mint Price of gold fixed, should, if they be consistent, also ridicule the idea of having the standard yard measure fixed. Those who wish to let the Mint Price of gold follow the Market Price, should also contend that every tradesman should have his yard measure of as many inches as he pleases, because when the Market Price of gold rises above the Mint Price, it is precisely analogous to curtailing so many inches of the yard. This fraudulent curtailment of the measure of value has never been done since Parliament has been the chief power in the Legislature. But it was constantly done in former times when the Crown was more despotic than it is now, so that the pound in the present day is curtailed of two-thirds of what it was in William I.'s time.

An alteration of the standard is a direct fraud upon debtors or creditors, according as it is raised or lowered; because the essence of every contract is, that the debtor is to pay a certain weight of gold, and not so many abstract ideas which are called pounds. Hence, if while any contract is incomplete, an alteration takes place in the weight of the coins, if, when it is fulfilled the debtor only looks to the number of pieces, neglecting their weight, it is evidently a fraud upon the creditor. Suppose a cloth manufacturer were under contract to deliver so many yards of cloth, and before the delivery took place, the law was to reduce the yard measure to 30 inches, surely the purchaser of the cloth would not be satisfied with receiving the same number of these diminished yards, simply because they were called "yards," as he bargained for. On the contrary, he bargained for a definite *length* of cloth, and if, when the law diminished the yard to 30 inches, it is also declared that the cloth manufacturer had fulfilled his contract when he had delivered so many yards of this curtailed measure, it would be clearly a fraud upon the purchaser.

It is clear, however, that this fraud and injustice would only extend to existing contracts. If the law were to reduce the yard in that manner, all contracts made subsequently to that law would adapt themselves to it, and the injustice would be just the more severe in proportion to the number and amounts of con-

tracts existing when the change took place. But suppose that, while the legal yard continued to be 36 inches, from the inattention of Government to send round proper inspectors of measures, tradesmen had become so fraudulent as to cut off gradually several inches from their yard measure, and suppose that this was done so openly and universally that numerous contracts were entered into, in these measures, which were known by both parties to be below their legal length, so that contracts were subsisting that were made both in the proper measure and in the diminished measure. Now, suppose that the Government being suddenly roused from its inattention, determined to enforce the legal length of the yard measure, it might become a question of some perplexity to decide whether equity would be more satisfied by enforcing a general return to the original legal standard, or by lowering the legal standard to the average length of the yard in use.

In concluding this part, we need only observe that its principles are, of course, subject to great modifications when obstacles are interposed to the conversion of bullion into coin. And that in several instances the value of bullion has differed immensely from the same quantity in coin. In the Eastern Archipelago, for instance, Spanish pillar dollars had long an almost exclusive currency. The people had such confidence in them, and were so accustomed to their use, that they would take nothing but them, and as, of course, they were only coined in Spain, when the supply of them was deficient in the East, bullion fell to an immense discount as compared with the dollars. The very same thing happened in the Australian Colonies soon after the gold discoveries, before mints were established there. Sovereigns could only be coined in England, and there were no means of converting the gold into currency without sending it to England to be coined. Gold, consequently, fell to an immense discount as compared with sovereigns. After some time, however, mints were erected in several of the colonies, and a plan was adopted of issuing notes in exchange for bullion, and this difference was immediately rectified.

What is a Pound ?

3. In the currency discussions during the great war, many curious notions were started as to what a "Pound" is. Sir Robert Peel asked the question—"What is a Pound?"—and he found many who could give him no answer. There are a good many, we suspect, who do not know how a certain weight of gold bullion came to be called a "Pound." We shall now explain this.

The original measure of value in France, England, and Scotland, was the pound weight of silver bullion. No coin, however, of this actual weight was ever struck. But the pound weight of

bullion was divided into 240 coins called pence. Twelve of these pence were called a shilling, or solidus, and, therefore, twenty shillings, or solidi, made a pound. These 240 pence actually weighed a pound of bullion.

Now, let us denote the pound weight of metal in the form of bullion by the symbol—lb., and the pound weight of metal in the form of coin by the symbol—£. Then we have:—

$$240 \text{ pence} = 20 \text{ shillings} = 1 \text{ £} = 1 \text{ lb.}$$

Now, it is perfectly clear that, if the pound weight of bullion were divided into a greater number of pieces than 240, that greater number would still be equal to the pound weight, and if we denoted by the symbol £, 240 pieces, or pence, irrespective of their weight, we should have the 1 lb. equal to 1 £, + the number of pieces above 240.

Now, this is what has been done in the coinage of all the three countries above-mentioned. The Sovereigns of these countries were frequently in want of money to pursue their various extravagancies, and, as they could not make more money, they adopted the fraudulent and surreptitious plan of cutting the pound weight of bullion into a greater number of pieces, but they still called them by the same name. By this means they gained an illusory augmentation of wealth. As they could not multiply the quantity of the metal, they at various periods *falsified the certificate*. While they still called their coins by the same name, they diminished the quantity of bullion in them, and so coined more than the original number of pence out of a pound weight of bullion.

The consequence of this was very manifest. As 240 pence were still called *a pound* or £, in money, whatever their weight was, and as more than 240 pence were coined out of a pound of bullion, the £, or pound of money, began to vary from the lb., or pound of bullion. This falsification of the certificate increased till the time of Elizabeth, when, instead of 240 pence, or 20 shillings, being coined out of the pound weight of bullion, no less than 62 shillings, or 744 pence, were coined out of it. Then we have manifestly

$$744 \text{ pence} = 62 \text{ shillings} = \text{£}3 \text{ 2s.} = 1 \text{ lb.}$$

Now, as there are 12 ounces in one pound weight of bullion, it is evident that each ounce of bullion was coined into 62 pence, and hence, as the value of bullion is measured by the ounce, the Mint Price of silver was said to be 5s. 2d. the ounce.

Afterwards gold was used as a measure of value concurrently with silver, and gold pieces were struck and made to pass current as nearly as could be done at the value corresponding to the market values of gold and silver. Thus there was for a considerable time a double standard.

The celebrated Locke, however, had pointed out that a double standard was improper, and that there ought to be only one

standard in a country. Sir Isaac Newton also pointed out in 1717 that the coins were then improperly rated according to the market value of gold and silver, and that the effect of this would necessarily be to drive silver out of circulation. In consequence of his representations, the value of the gold coin was reduced, but not to a sufficient extent, and the consequence which he predicted took place. In consequence of gold, in coin, being still overrated, in comparison with its relative market value to silver, merchants, during the course of the last century, adopted the universal custom of paying their bills in gold coin in preference to silver, and thus gold became gradually to be considered as *the* measure of value in England.

In 1816, this custom was adopted as the law, and gold was declared to be the only legal measure of value, and the pound, the legal tender or measure of value, became the equivalent in gold of 20s. in silver.

The pound weight of gold bullion was ordered to be cut into 46 pieces of the value of 20s. or £1 each, with a piece over, equal to 14-20ths and 6-12ths of 1-20th, or the Mint Price of 1lb of gold was fixed at £46 14s. 6d.

But, as the value of gold is estimated by the ounce, the Mint Price of gold is fixed at £3 17s. 10½d. per ounce, and, as long as the coins are ordered to be coined of the same weight, the Mint Price cannot vary.

On a Double Standard.

4. We have seen that a large number of eminent writers have observed that the fundamental idea of Currency is debt; and that specie is, in fact, only the most general form in which this is recorded and transferred. That portion of the Currency which a debtor can compel his creditor to receive as payment of the debt due from him, and as, in fact, a means of obtaining any services he may require from some else, is called MONEY, or LEGAL TENDER, and sometimes the *measure* or *standard* of value.

When coins are struck of two different metals, and each is made indiscriminately legal tender to an unlimited amount, there is said to be a double standard.

Silver money was, at the time of the conquest, the only legal tender. Afterwards, in the reign of Edward III., gold money was coined to be as nearly as possible equal in value, to a certain amount of silver money, and, for several centuries, they were each legal tender in discharge of any amount of debt.

It would seem apparently to be very convenient to have money of both metals. The gold for large payments, and the silver for smaller ones. Nevertheless, there are certain fundamental objections to having both metals as legal tender to any amount.

We have observed that it is a fundamental law of the coinage,

found to be absolutely true in all ages and countries, that good and bad coins cannot circulate together, but that the bad coin drives the good coin from circulation. That is to say, that the one which is *overrated*, expels the one which is *underrated*.

Exactly the same consequence follows if the coins be made of different metals.

Gold and silver have value with respect to each other, just as any other commodities have; and this value is constantly changing in the market of the world; though, no doubt, in a minute degree. Now, coins of gold and silver may be issued at a fixed relative value, which may be true at the time of issue; but the value of the metals is constantly changing in the open market, and hence, the Mint value of the coins never remains for any length of time in proper adjustment with their market value; and, consequently, the inevitable result happens, the coin that is overrated drives out the coin that is underrated; and the latter is melted down and exported to where it will fetch a better price in the market.

The reason is plain. Suppose that at any time a gold coin is issued from the Mint to represent twenty shillings in silver, and that it is either misrated, or the market value of the metals has so changed from the Mint value, that it ought in reality to exchange for twenty-one shillings, it is clear that merchants will then discharge their debts in silver. All the gold coin will be melted down, and exported to where it can buy twenty-one shillings in silver, and thus, in a very short space of time, it will disappear from circulation.

This is what has repeatedly happened in the coinage of this country, and, from the cause not being understood, it was for many ages a source of great perplexity to financiers. It would be too long to enumerate these instances here, to establish the truth of the doctrine, but they will be found in our *Dictionary of Political Economy*, Art. *Coinage of England*. And we will only confine our attention here to a late example. At the beginning of the last century, gold and silver were legal standards within England and France, and it was from the misrating of the value of the coins by the two Mints, that gold came to be considered as *the* legal standard of England, and silver *the* legal standard of France.

In 1663, Charles II. issued a splendid gold coinage of £5, £2, and 20s. pieces. The latter were called guineas, as they were made of gold brought home by the African Company. They were struck to be equivalent to twenty shillings in silver, and thus to represent the £, in gold. The pound weight of crown gold was ordered to be cut into $44\frac{1}{2}$ guineas, and continued to be so as long as they were coined.

From some fatality they seemed to be always incapable at the English Mint of ascertaining the true value of gold and silver

according to their market rates. The guinea was soon found to be underrated, and, accordingly, the old practices of clipping, melting, and exporting were soon in full operation, and the scarcity of money was complained of in Parliament.

In April, 1690, the great scarcity of silver coins occasioned great public inconvenience. The goldsmiths complained to the House of Commons, that they had ascertained that immense quantities of silver bullion and dollars had been exported. That many Jews and merchants had recently bought up vast quantities of silver to carry out of the kingdom, and had given three half-pence an ounce above its regulated value. That this had encouraged the melting down of much plate and milled money, whereby for six months past no bullion had been brought to the Mint to be coined. The House appointed a Committee, who verified these allegations. It was shewn that the profit of melting down the milled money for exportation was above £25 per £1,000, and that the Mint price of silver was 5s. 2d. per ounce, but it was generally sold for 5s. 3½d. The House, in consequence, passed one of their useless laws against exporting bullion.

The state of the currency now became every day more disgraceful. Quantities of base and counterfeit coin were thrown into circulation. The House of Commons addressed the King to abolish the right of private coinage of half-pence and farthings. The current coins had been for many years clipped and adulterated, which in 1694 reached such a height, that the silver coins current had lost nearly half their value, while a great part of the current money was only iron, brass, or copper plated.

As this state of matters gave rise to the first great currency debate of modern times, and brought about a great monetary crisis, we may dwell upon it rather fully.

During 1694, the silver coinage became worse daily, and by the end of the year, guineas, which had originally been coined to represent 20s., gradually rose, till they reached 30s. The exchange with Holland fell 25 per cent., and it would have fallen still lower, only it was shewn that the real exchange was in favor of England. The exchange with Ireland fell so much that £70 there was worth £100 in England.

The evils of clipping the coin reached so great a height at the end of 1694, that Mr. Fleetwood, the Chaplain-in-Ordinary to the King and Queen, being selected to preach before the Lord Mayor and Aldermen on the 16th December, 1694, made it the subject of his sermon on the text, Gen. xxiii., 16. In an admirable sermon, or rather politico-economical discourse, he denounced the fraud and wickedness of clipping and debasing the coinage. He said (p. 19), that the money was clipped down nearly one half. He shewed that he understood the subject a

great deal better than many men a century later. He shewed that, if the money generally were clipped, all the good and weighty money that remained must be exported. "The merchant that exports more goods from home than he imports from abroad, must unavoidably discharge the overbalance with good money; this he can never do with clipped, for it is not *Cæsar's face and titles*, but *weight and goodness* that procure credit. And, if a foreigner import more of his country's goods than he carries away of ours, the overbalance must be paid in weighty money, for the clipped will not go abroad. Now, if the exportation of our weighty money (which is only now the milled) be a mischief to the nation, we see it is occasioned chiefly by the clipping."

The disgraceful state of the coinage could no longer be overlooked by Parliament. On the 8th of January, 1695, a Committee was appointed to consider the subject. At this time, says the Parliamentary History, Vol. v., p. 955:—"The difficulty lay so heavy upon the Government, that a stop was almost put to trade and taxes. The current silver coin had for many years begun to be clipped and adulterated; and the mischief of late had been so secretly carried on by a combination of all people concerned in the receipt of money, and so industriously promoted by the enemies of the Government, that all pieces were so far diminished and debased, as that five pounds in silver specie was scarce worth 40s., according to the standard; besides an infinite deal of iron, brass, or copper washed over or plated." The Committee recommended that the money should be recoined into milled money. It estimated the expense at one million. That the new money should be of the same weight and fineness as the old. That the crown piece should be current at 5s. 6d. That various penalties should be imposed for offences against the coins. An Act was passed, statute 1695, c. 17, to prevent counterfeiting and clipping the coin of the kingdom. This statute averred that it was notorious that the current coin had been greatly diminished by clipping, rounding, filing, and melting, and that many false and counterfeit coins had been clipped, for the better disguising thereof, and that these practices had been much occasioned by those who drove a trade of exchanging broad money for clipped money, and other arts and devices. It, therefore, prohibited any person from exchanging, lending, selling, borrowing, buying, receiving, or paying any broad or unclipped silver money for more in tale, benefit, profit, or advantage than the same was coined for, and ought by law to pass for, under a penalty of 10s. for every 20s. so illegally trafficked with. It also enacted that whoever should buy or sell, or knowingly have in his possession, any clippings or filings of the coin should forfeit them, as well as a penalty of £500, and be branded on the right cheek with a hot iron. It forbade any one but a trading gold-

smith, or refiner of silver, to buy or sell bullion, under pain of imprisonment, and enacted numerous other vexatious penalties and regulations respecting the export of bullion. All these absurd cruelties were wholly ineffectual, and, while multitudes of miserable wretches were dangling on the gibbets, clipping and counterfeiting were as rife as ever. Guineas, which had originally been coined to be equal to 20s., had progressively risen as the silver got worse, till at this time they were current at 30s. of the base trash, which passed by the name of silver coin.

In February, 1696, several petitions were presented to the House of Commons (*Commons Journals*, Vol. xi., p. 445). The graziers, butchers, and others connected with Smithfield Market, said that £40,000 a week passed through their hands for cattle, which for almost twelve months past had been paid in guineas at 30s. a piece, for want of current silver. There are besides, abundance of pamphlets in existence which prove that guineas were commonly current for 30s. in the spring of 1695.

The frightful disorder of the currency may be judged of by the following facts. In the months of May, June, and July, 1695, 572 bags of silver coin, each of £100, were brought into the Exchequer, whose aggregate weight, according to the standard, ought to have been 18,451 lbs., 5 oz., 16 dwts., 8 grs. : their actual weight was 9,480 lbs., 11 oz., 5 dwts., making a deficiency of 8,970 lbs., 7 oz., 11 dwts., 8 grs., shewing a deficiency in the weight of the current coins in the ratio of 10 to 22. One writer says (*An Essay for regulating of the coin. By A. V., Sept. 2, 1695*):—"Upon trial, I have found that 5s. of milled money hath weighed 8s. of the present current money, and 3s. of the 8s. was not clipped, only worn. Again, I have found 10s. in milled money to weigh 21s. of the clipped money. Again, 20s. of milled money to weigh 43s. of our now current money.

"I have gone to several goldsmiths in London, and have got them to take out of their counters a bag of £100 as came to hand, which, upon trial, I have found at one place to weigh:—

	Oz.	Dwt.	Gr.
A bag of £100	230	13	6
Another place £100 Weighed	222	0	15
Another place	198	17	0
Another place	190	0	0
Another place	182	3	0
Another place	174	11	20
	1,198 5 17		

"The £600 weighing in all 1,198 oz., 5 dwts., 17 grs., and is no more than what £310 in milled money will weigh.

"I am informed the money paid into the Exchequer doth weigh from 15 (and seldom the £100 reacheth) to 20 lbs. weight,

so that the very best brought in there doth not weigh two-thirds of what it ought to do, and the money paid into the Exchequer is supposed, a great part of it, to come from the country.

“But, as it’s believed that the money in the country is generally not the one-half so bad as it’s in and near London, I have procured an account to be sent me from the following cities, from whence I am informed that £100 doth weigh on trial of *two* bags in each place, to be viz. :—

	Oz.	Dwt.	Gr.
In the City of Bristol, one bag of £100 weighed	240	0	0
Another weighed	227	15	0
In the City of Cambridge, a bag of £100 weighed	203	5	10
Another weighed	211	0	19
In the City of Exon, one bag of £100 weighed	180	7	0
Another weighed	192	3	0
In the City of Oxford, £100 in half-crowns weighed	216	10	0
£100 in shillings	198	0	15
	1,669	1	20

“The £800 weighing not more than £431 15s. of milled money will weigh, and but a very small difference between the weight of the money in London and the country.”

This disgraceful state of the money gave rise to the greatest public confusion and distress, and a warm controversy arose whether the new money which should be coined should be of the old standard in weight, fineness, and denomination, or whether it should be depreciated, or raised in value, as it was absurdly called. This controversy was keenly disputed then, and we may pay some considerable attention to it, because it was revived under another form 116 years later, when the notes of the Bank of England were depreciated, and a strong party maintained that the standard of the coin should be depreciated to the level of the depreciated notes.

Mr. William Lowndes, the Secretary to the Treasury, was ordered by them to make a Report on the subject of the coin. This he did in *A Report containing an Essay for the Amendment of the Silver Coins*. London, 1695. In this he enters into a long, and at that time, valuable investigation of the history of the coinage, and its successive depreciations in weight and fineness. After giving the details of every Mint indenture for four hundred years, he says, p. 56:—“By the careful observing of which deduction here made, from the indenture of the Mint for above 400 years past (many of which are yet extant, and have been seen and examined by me), it doth evidently appear that it has been a policy constantly practised in the Mints in England (the like having indeed been done in all Foreign Mints belonging

to other Governments), to raise the value of the coin in its extrinsic denomination from time to time, as any exigence or occasion required; and more especially to encourage the bringing in of bullion into the realm to be coined (though sometimes, when the desired end was obtained, the value has been suffered to fall again), so that, in the whole number of years from the 28th Edward I. until this time, the extrinsic value or denomination of the silver is raised in about a triple proportion." Here we cannot fail to observe the utter confusion of idea that Mr. Lowndes, and too many after his time, labour under. They manifestly suppose that, by raising the *name* of the coin they raise its *value*. The extrinsic value of the coin can by no possibility mean anything else but the quantity of things it will *exchange for*. And to call the quantity of things it will exchange for its *denomination* is a most pitiable confusion of ideas. Mr. Lowndes then says:—"The which being premised, and every project for debasing the money (by the reason before given) being rejected as dangerous, dishonourable, and heedless, it remains that our nation in its present exigence, may avail itself, by raising the value of its coins, and this may be effected either by making the respective pieces called crowns, half-crowns, shillings, and to be lesser in weight, or by continuing the same weight or bigness, which is at present, in the unclipped moneys, and ordaining at the same time that every such piece shall be current at a higher price in tale.

"But, before I proceed to give my opinion on this subject, it seems necessary for me to assert and prove an hypothesis, which is this, namely, *That making the pieces less, or ordaining the respective pieces (of the present weight) to be current at a higher rate, may equally raise the Value of Silver in our Coins.*"

Mr. Lowndes then enters into an argument to prove that sixty pence are equal to seventy-five pence—a wild goose chase in which we decline to follow him.

His proposal was, then, that all the existing unclipped silver money should be raised in denomination to 6s. 3d. the crown, and other coins in proportion, so that the shilling would pass for fifteen pence instead of twelve. That new coins should be struck at the increased denominations. These coins he proposed to christen by new names. The reasons he alleges for this proceeding are—"1. The value of the silver in the coin ought to be raised to the foot of 6s. 3d. in every crown, because the price of standard silver in bullion is risen (from divers necessary and unnecessary causes, producing at length a great scarcity thereof in England) to 6s. 5d. an ounce. This reason (which I humbly conceive will appear irrefragable) is grounded chiefly upon a truth so apparent, that it may well be compared to an axiom, even in mathematical reasoning, to wit,—That whensoever the extrinsic value of silver in the coin hath been, or shall be, less

than the price of silver in bullion, the coin hath been, and will be, melted down."

He then enters into some objections against this proposal, and says, p. 76 :—"That everything having any value or worth whatsoever, when it becomes scarce, grows dear, or (which is the same thing) it riseth in price, and, consequently, it will serve to pay more debts, or it will buy greater quantities of other goods of value, or in anything else it will go further than it did before. That silver in England being grown scarce as aforesaid, is consequently grown dearer. That it is risen in price from 5s. 2d. to 6s. 5d. an ounce; and, by daily experience, 19 3-10 dwts. in sterling silver (equal to the weight of a crown piece) in England, doth and will purchase more coined money than 5s. by tale (though the latter be delivered *bonâ fide* in unclipped shillings, or in a good bill), and, consequently, doth and will purchase and acquire more goods, or necessaries, or pay more debts in England, or (being delivered here) it fetches more money in any foreign parts by way of exchange, than 5s. by tale, or the sixth part of a guinea by tale, or goods to the value of 5s. in tale only, do or can fetch, purchase, or acquire. That this advanced price of the silver has been growing for some time, and is originally caused by the balance, excess, or difference above mentioned, which naturally and rationally produces such an effect * * * That the raising the value of the silver in our coins to make it equal to silver in mass, can in no sense be understood to be a cause of making silver scarce. That there can never be proposed any just or reasonable foot upon which the coin should be current, save only the very price of the silver thereof, in case it may be molten in the same place where the coins are made current, or an extrinsic denomination very near that price. It being most evident that if the value of the silver in the coins should (by any extrinsic denomination) be raised above the value or market price of the same silver reduced to bullion, the subject would be proportionably injured and defrauded, as they were formerly in the case of the base monies coined by public authority."

He then says the value of the silver in the coin ought to be raised, to encourage the bringing of bullion to the Mint to be coined. That this had been repeatedly done both in the English and Foreign Mints. That raising the value of silver in coin would increase the whole species in tale, and thereby make it more commensurate to the need for it for carrying on the common traffic and commerce of the nation, and to answer the payments on the numerous contracts, securities, and other daily occasions, requiring a large supply of money for that purpose.

He says that at that time guineas passed current for 30s.

He then gives some details of the state of the coinage, by

which he shewed that they were diminished by about half their usual weight.

We have said, that when coins were struck out of bullion, that the value, or purchasing power of the money depended upon the actual quantity of bullion in it, and not at all on the name of the coin. A most extraordinary delusion, however, began to prevail in early times, of which we have the first notice in Plutarch. It was this, that when coins were once called and recognized by a certain name, that their value depended upon the *name*, and did not depend on the quantity of metal in them. About the end of the 17th century this incredible heresy began to find adherents in this country, and this notion long infested the notions of many financiers, and, we shall see hereafter, was stoutly maintained by the Government party in the great currency debates in 1811, and was the cause of great mischief to this country.

The extraordinary doctrines of Lowndes called forth a worthy antagonist, and were the origin of some of his most admirable writings, and they are of so much importance that we shall make some extracts from them, as there is no doubt that the fallacies he combated are even yet not entirely eradicated.

Locke had in 1691 published a treatise, in which he shewed the utter futility of interfering with the rate of interest by law, and combated the idea that was then becoming prevalent, that the value (as it was called) of the coin should be raised in order to keep it in the country. He shewed that the persons who supported such a plan were confounding the *denomination* with the *value*, its name with the purchasing power, and that all such ideas proceeded from a confusion of terms, and would have no real effect. The arguments of Locke, though by no means absolutely novel, had never been put before so luminously and fully. The proposal of Lowndes, coming from a man holding his official position, demanded a prompt notice and exposure. This Locke did, in *Further Considerations concerning Raising the Value of Money*, in which he exposed the fallacy of Lowndes's arguments:—"Raising of coin is but a specious word to deceive the unwary. It only gives the usual denomination of a greater quantity of silver to a less (*v. g.*, calling four grains of silver a penny to-day, when five grains of silver made a penny yesterday), but adds no worth, or real value, to the silver coin, to make amends for its want of silver. That is impossible to be done, for it is only the quantity of silver in it, that is, and eternally will be, the measure of its value, and to convince any one of this, I ask whether he that is forced to receive but 320 ounces of silver under the denomination of £100 (for 400 ounces of silver which he lent under the like denomination of £100) will think these 320 ounces of silver, however denominated, worth those 400 ounces he lent? If any one can be supposed so silly,

he need but go to the next market, or shop, to be convinced that men value not money by the denomination, but by the quantity of the silver there is in it. One may as rationally hope to lengthen a foot, by dividing it into 15 parts, instead of 12, and calling them inches, as to increase the value of the silver that is in a shilling, by dividing it into 15 parts instead of 12, and calling them pence. This is all that is done when a shilling is raised from 12 to 15 pence.

“Clipping of money is raising without public authority, the same denomination remaining to the piece, that hath now less silver in it than it had before.

“Altering the standard, by coining pieces under the same denomination with less silver in them than they formerly had, is doing the same thing by public authority. The only odds is that, by clipping, the loss is not forced on any one (for nobody is obliged to receive clipped money); by altering the standard it is.

“Altering the standard by raising the money, will not get to the public, or bring to the Mint to be coined, one ounce of silver; but will defraud the king, the church, the universities and hospitals, and of so much of their settled revenue as the money is raised, *v. g.*, twenty per cent. of the money (as is proposed), be raised one-fifth. It will weaken, if not totally destroy, the public faith, when all that have trusted the public, and assisted our present necessities, upon Acts of Parliament, in the million lottery, Bank Act, and other loans, should be defrauded of twenty per cent. of what those Acts of Parliament were security for. And quantity of silver has a less value; and an equal quantity an equal value.

“4. That money differs from uncoined silver only in this, that the quantity of silver in each piece of money is ascertained by the stamp it bears; which is set there to be a public voucher of its weight and fineness.

“5. That gold is treasure, as well as silver, because it decays not in keeping, and never sinks much in value.

“6. That gold is fit to be coined, as well as silver; to ascertain its quantity to those who have a mind to traffic in it; but not to be joined with silver as a measure of commerce.”

Locke then examines Lowndes's doctrine, that the value (or denomination) of the silver coin should be raised to 6s. 3d. the ounce, because the price of standard silver had risen to 6s. 5d. the ounce—

“This reason seems to me to labour under several mistakes; as

“1. That standard silver can rise in respect of itself.

“2. That standard bullion is now, or ever was, worth or sold to the traders in it for 6s. 5d. the ounce, of lawful money of England. For, if that matter of fact holds not to be so, that an ounce of sterling bullion is worth 6s. 5d. of our milled weighty money, this reason ceases; and our weighty crown pieces ought

not to be raised to 6s. 3d., because our light clipped money will not purchase an ounce of standard bullion, under the rate of 6s. 5d. of that light money. And, let me add here, nor for that rate neither. If, therefore, the author means here, that an ounce of standard silver is risen to 6s. 5d. of our clipped money, I grant it him, and higher too. But, then, that has nothing to do with the raising our lawful coin, which remains unclipped; unless he will say, too, that standard bullion is so risen, as to be worth, and actually to sell for, 6s. 5d. the ounce of our weighty milled money. This I not only deny, but further add, that it is impossible to be so. For 6s. 5d. of milled money weighs an ounce and a quarter near. Can it, therefore, be possible that one ounce of any commodity should be worth an ounce and a quarter of the self-same commodity, and of exactly the same goodness? for so is standard silver to standard silver. Indeed, one has a mark upon it which the other has not; but it is a mark that makes it rather more than less valuable, or, if the mark, by hindering its exportation, makes it less valuable for that purpose, the melting pot can easily take it off. * * *

“Those who say bullion is risen, I desire to tell me what they mean by risen? Any commodity, I think, is properly said to be risen, when the same quantity will exchange for a greater quantity of another thing; but more particularly of that thing, which is the measure of commerce in the country. And thus corn is said to be risen among the English in Virginia, when a bushel of it will sell or exchange for more pounds of tobacco; among the Indians, when it will sell for more yards of wampompeak, which is their money; and among the English here, when it will exchange for a greater quantity of silver than it would before. Rising and falling of commodities are always between several commodities of distinct worths. But nobody can say that tobacco (of the same goodness) is risen in respect of itself. One pound of the same goodness will never exchange for a pound and a quarter of the same goodness. And so it is in silver: an ounce of silver will always be of equal value to an ounce of silver: nor can it ever rise or fall, in respect of itself: an ounce of standard silver can never be worth an ounce and a quarter of standard silver: nor one ounce of uncoined silver exchange for an ounce and a quarter of coined silver: the stamp cannot so much debase its value. Indeed, the stamp, hindering its free exportation, may make the goldsmith (who profits by the return of his money) give one 120th, or one 60th, or perhaps sometimes one 30th more, that is 5s. 2½d., 5s. 3d. or 5s. 4d. the ounce of coined silver for uncoined, when there is need of sending silver beyond seas; as there always is, when the balance of trade will not supply our wants, and pay our debts there. But much beyond this the goldsmith will never give for bullion, since he can make it out of coined money at a cheaper rate.

“It is said bullion is risen to 6s. 5d. the ounce, *i. e.*, that an ounce of uncoined silver will exchange for an ounce and a quarter of coined silver. If any one can believe this, I will put this short case to him. He has of bullion, or standard uncoined silver, two round plates, each of an exact size and weight of a crown piece: he has besides, of the same bullion, a round plate of the weight and size of a shilling, and another yet less, of an exact weight and size of a three-pence. The two great plates being of equal weight and fineness, I suppose he will allow to be of equal value, and that the two less, joined to either of them, make it one-fifth more worth than the other is by itself, they having all three together one-fifth more silver in them. Let us suppose, then, one of the greater and the two less plates to have received the next moment (by miracle, or by the mill, it matters not how) the mark, or stamp, of our crown, our shilling, and our three-pence: can anybody say, that now they have got the stamp of our Mint upon them, they are so fallen in value, or the other unstamped piece so risen, that that unstamped piece, which a moment before was worth only one of the other pieces, is now worth them all three? Which is to say, that an ounce of uncoined silver is worth an ounce and a quarter of coined. This is what men would persuade us, when they say that bullion is raised to 6s. 5d. (of lawful money) the ounce, which I say is utterly impossible. Let us consider this a little further, in another instance. The present milled crown pieces, say they, will not exchange for an ounce of bullion, without the addition of a shilling, and a three-pence of weighty coin added to it. Coin but that crown piece into 6s. 3d., and then they say it will buy an ounce of bullion, or else they give up their reason and measure of raising the money. Do that which is allowed to be equivalent to coining of a present milled crown-piece into 6s. 3d., *viz.*, call it 75 pence, and then also it must, by this rule of raising, buy an ounce of bullion. If this be so, this self-same milled crown-piece will, and will not, exchange for an ounce of bullion. Call it sixty pence, and it will not: the very next moment call it seventy-five pence, and it will. I am afraid nobody can think change of denomination has such power.”

Locke then goes through each of Lowndes's arguments and proposals one by one, and gives them such a refutation as would have delighted the heart of Chillingworth. Among other things, he says:—“It is true, what Mr. Lowndes observes here, the importation of gold, and the going of guineas at 30s., has been a great prejudice and loss to the Kingdom. But that has been wholly owing to our clipped money, and not at all to our money being coined at 5s. 2d. the ounce: nor is the coining of our money lighter the cure of it. The only remedy for that mischief, as well as a great many others, is the putting an end

to the passing of clipped money by tale, as if it were lawful coin."

To Lowndes's doctrine, that raising the coin by making it more in tale, would make it more abundant for general use, Locke says:—"Just as the boy cut his leather into five quarters (as he called them) to cover his ball, when cut into four quarters it fell short; but, after all his pains, as much of his ball lay bare as before; if the quantity of coined silver employed in England fall short, the arbitrary denomination of a greater number of pence given to it, or, which is all one, to the several coined pieces of it, will not make it commensurate to the size of our trade, or the greatness of our occasions. This is as certain, as that if the quantity of a board, which is to stop a leak of a ship fifteen inches square, be but twelve inches square, it will not be made to do it, by being measured by a foot which is divided into fifteen inches, instead of 12, and so having a larger tale, or number of inches in denomination, given to it.

"This, indeed, would be a convincing reason if sounds would give weight to silver, and the noise of a greater number of pence (less in quantity proportionably as they are more in number) were a large supply of money. * * *

"The necessity of trust and bartering is one of the many inconveniences springing from the want of money. This inconvenience the multiplying arbitrary denominations will no more supply, nor any ways make our scarcity of coin commensurate to the need there is of it, than if the cloth which was provided for clothing the army, falling short, one should hope to make it commensurate to that need there is of it, by measuring it by a yard one-fifth shorter than the standard, or changing the standard of the yard, and so getting the full denomination of yards necessary according to the present measure. For this is all that will be done by raising our coin, as is proposed. All it amounts to is no more but this, viz., That each piece, and, consequently, our whole stock of money, should be measured and denominated by a penny one-fifth less than the standard * *

"The increase of denomination does, or can do nothing in the case, for it is silver by its quantity and not denomination, that is the price of things and measure of commerce; and it is the weight of silver in it, and not the name of the pieces that men estimate commodities by, and exchange them for.

"If this be not so, when the necessity of our affairs abroad, or ill-husbandry at home, has carried away half our treasure, and a moiety of our money is gone out of England, it is but to issue a proclamation that a penny shall go for two-pence, sixpence for a shilling, half-a-crown for a crown, &c., and immediately, without any more ado, we are as rich as before. And, when half the remainder is gone, it is but doing the same thing again, and raising the denomination anew, and we are where we were, and

so on; whereby, supposing the denomination raised 15-16, every man will be as rich with an ounce of silver in his purse as he was before when he had 16 ounces there, and in as great plenty of money, able to carry on his trade without bartering, his silver, by this short way of raising, being changed into the value of gold; for, when silver will buy 16 times as much wine, oil, and bread, &c., to-day as it would yesterday (all other things remaining the same, but the denomination), it hath the real worth of gold.

“This, I guess, everybody sees cannot be so, and yet this must be so, if it be true that raising the denomination one-fifth can supply the want, or one jot raise the value of silver in respect of other commodities, *i. e.*, make a less quantity of it to-day, buy a greater quantity of corn, oil, and cloth, and all other commodities, than it would yesterday, and thereby remove the necessity of bartering. For, if raising the denomination can thus raise the value of coin in exchange for other commodities, one-fifth, by the same reason it can raise it two-fifths, and, afterwards, three-fifths, and again, if need be, four-fifths, and as much further as you please. So that, by this admirable continuance of raising our coin, we shall be rich, and as well able to support the charge of the Government, and carry on our trade without bartering, or any other inconvenience for want of money, with 60,000 ounces of coined silver in England, as if we had six, or 60 millions. If this be not so, I desire any one to show me why the same way of raising the denomination, which can raise the value of money in respect of other commodities, one-fifth, cannot, when you please, raise it another fifth, and so on? I beg to be told where it must stop, and why at such a degree, without being able to go further.

“It must be here taken notice of, that the raising I speak of here, is the raising of the value of our coin in respect of other commodities (as I call it all along) in contradistinction to raising the denomination. The confounding of these in discourses concerning money, is one great cause, I suspect, that this matter is so little understood, and so often talked of with so little information of the hearers.

“A penny is a denomination no more belonging to eight than to eighty, or to one single grain of silver: and so it is not necessary that there should be 60 such pence, no more nor less, in an ounce of silver, *i. e.*, twelve in a piece called a shilling, and sixty in a piece called a crown: such like divisions, being only extrinsical denominations, are everywhere perfectly arbitrary. For, here in England, there might as well have been twelve shillings in a penny, as twelve pence in a shilling, *i. e.*, the denomination of the less pence might have been a shilling, and of the bigger a penny. Again, the shilling might have been coined ten times as big as the penny, and the crown ten times as big as the shilling; whereby the shilling would have but tenpence in it, and the crown a hundred. But this, however

ordered, alters not one jot the value of the ounce of silver, in respect of other things, any more than it does its weight. This raising being but giving of names at pleasure to aliquot parts of any piece, viz., that now the 60th part of an ounce of silver shall be called a penny, and to-morrow that the 75th part of an ounce shall be called a penny, may be done with what increase you please. And thus it may be ordered by a proclamation, that a shilling shall go for twenty-four pence, and half-crown for sixty instead of thirty pence, and so of the rest. But that an half-crown should be worth or contain sixty such pence, as the pence were before the change of denomination was made, that no power on earth could do. Nor can any power but that which can make the plenty or scarcity of commodities, raise the value of our money their double in respect of other commodities, and make that same piece, or quantity, of silver, under a double denomination, shall purchase double the quantity of pepper, wine, or lead, an instant after such proclamation, to what it would do an instant before. If this could be, we might, as every one sees, raise silver to the value of gold, and make ourselves as rich as we pleased. But it is but going to market with an ounce of silver of one hundred and twenty pence, to be convinced that it will purchase no more than an ounce of silver of sixty pence; and the ringing of the piece will as soon purchase more commodities, as its change of denomination, and the multiplied name of pence, when it is called six score instead of sixty."

It may, perhaps, appear to some that the arguments put forward by Locke, are so simple and convincing, that it is almost a waste of ingenuity and labour to dwell on them at such length. But, unfortunately, this is not so. The confusion of idea between the *name* and the *value* of a coin, is one which is but too prevalent even at the present day. It seems almost incredible that an able man like Mr. Lowndes could perceive that debasing the standard of the coin, by putting less silver and more alloy, was a public fraud, and an injury to all creditors, and yet that he should be totally incapable of perceiving that raising the denomination of the coin, was exactly the same thing in principle as debasing the standard. In each case the quantity of pure silver in a crown or a shilling was diminished. Nevertheless, this fallacy is deeply seated even at the present day. It was, moreover, exactly the same fallacy, under another form, which blinded and deluded the Bank of England, the Government, and the House of Commons in 1811, into their insane vote on the doctrine of the Bullion Report, that the Bank Note was depreciated. But, alas! instead of a Montagne willing to learn wisdom from the counsels of a Locke, there was only a Vansittart, who refused to listen to Horner and Canning, and we are still smarting for his infatuation.

The Government, adopting the councils of Locke and Newton, restored the coinage according to its ancient weight, fineness, and denomination.

The political benefits which followed this great restoration of the coinage are beyond the purpose of this work. In 1707, the union of the kingdoms necessitated a new coinage. At the same time the relative value of the gold and silver coins began to differ from the market value of the two metals, and, as silver was underrated, it became very scarce. It is much to be lamented that the Government, having adopted Locke's arguments in favour of the maintenance of the standard, did not also adopt his argument with respect to the necessity of there being only one standard of value. It was perfectly conclusive, and the evils, which he had shewn must necessarily follow from this economic error of having two measures of value, manifestly displayed themselves. In 1708, the Government offered a premium of 2½d. per ounce to every one who brought foreign silver coin, or plate of any sort, of standard fineness, to the Mint to be coined. This, however, was quite ineffectual, and as matters grew worse every day, the Government referred the matter to Sir Isaac Newton, who had for many years been at the head of the Mint, to report upon.

Sir Isaac Newton said, in his Report (*Parl. Hist.*, vii., 526): "That a pound weight Troy of gold, 11 ozs. fine, and 1 oz. alloy, is cut into 44½ guineas; and a pound weight of silver, 11 ozs. 2 dwts. fine, and 18 dwts. alloy, is cut into 62 shillings; and, according to this rate, a pound weight of fine gold is worth 15 pounds weight 6 ozs. 17 dwts. and 5 grs. of fine silver, reckoning a guinea at £1 1s. 6d. in silver money. But silver in bullion, exportable, is usually worth 2d. or 3d. per ounce more than in coin; and if, as a medium, such bullion of standard alloy be valued at 5s. 4½d. per ounce, a pound weight of fine gold will be worth but 14 lbs. 11 ozs. 12 dwts. 9 grs. of fine silver in bullion; and, at this rate, a guinea is worth but so much silver as would make 20s. 8d. When ships are lading for the East Indies, the demand of silver for exportation raises the price to 5s. 6d. or 5s. 8d. per ounce, or above; but I consider not these extraordinary cases.

"A Spanish pistole was coined for thirty-two rials, or four pieces of eight rials, usually called pieces of eight, and is of equal alloy, and the sixteenth part of the weight thereof; and a Doppio Moeda of Portugal was coined for ten crusados of silver, and is of equal alloy, and the sixteenth part of the weight thereof. Gold is, therefore, in Spain and Portugal, of sixteen times more value than silver of equal weight and alloy, according to the standard of those kingdoms; at which rate a guinea is worth 22s. 1d. But this high price keeps their gold at home in good plenty, and carries away the Spanish silver

into all Europe; so that at home they make their payments in gold, and will not pay in silver without a premium; upon the coming in of a Plate fleet the premium ceases, or is but small; but, as their silver goes away and becomes scarce, the premium increases, and is most commonly about six per cent., which, being abated, a guinea becomes worth about 20s. 9d. in Spain or Portugal.

“In France a pound weight of fine gold is reckoned worth fifteen pounds weight of fine silver; in raising or falling their money, their Kings’ edicts have sometimes varied a little from this proportion, a little in excess or defect; but the variations have been so little, that I do not here consider them. By the edict of May, 1709, a new pistole was coined for four new Louises, and is of equal alloy, and the fifteenth part of the weight thereof, except the errors of their mints; and by the same edict, fine gold is valued at fifteen times its weight of fine silver; and at this rate a guinea is worth 20s. 8½d. * * *

“The ducats of Holland and Hungary, and the Empire, were lately current in Holland among the common people, in their markets and ordinary affairs, at five guilders in specie, and five stivers; and commonly changed for so much silver moneys in three-guilder pieces and guilder pieces, as guineas are with us for 21s. 6d. sterling; at which rate a guinea is worth 20s. 7½d.

“According to the rates of gold to silver in Italy, Germany, Poland, Denmark, and Sweden, a guinea is worth about 20s. and 7d., 6d., 5d., or 4d., for the proportion varies a little within the several Governments in these countries. In Sweden, gold is lowest in proportion to silver, and this hath made that kingdom, which formerly was content with copper money, abound of late with silver, sent thither (I suspect) for naval stores.

“In the end of King William’s reign, and the first year of the late Queen, when foreign coins abounded in England, I caused a great many of them to be assayed in the Mint, and found by the assays, that fine gold was to fine silver in Spain, Portugal, France, Holland, Italy, Germany, and the northern kingdoms, in the proportion above mentioned, errors of the Mint excepted.

“In China and Japan, one pound weight of fine gold is worth but 9 or 10 pounds weight of fine silver; and in East India it may be worth 12; and this low price of gold in proportion to silver carries away the silver from all Europe.

“So, then, by the course of trade and exchange between nation and nation in all Europe, fine gold is to fine silver as 14 4-5, or 15 to one; and a guinea at the same rate is worth between 20s. 5d. and 20s. 8½d.; except in extraordinary cases, as when a Plate fleet is just arrived in Spain, or ships are lading here for the East Indies, which cases I do not here consider. And it appears, by experience as well as by reason, that silver flows from those places where its value is lowest in proportion to gold, as from

Spain to all Europe, and from all Europe to the East Indies, China, and Japan; and that gold is most plentiful in those places in which its value is highest in proportion to silver, as in Spain and England.

“It is the demand for exportation which hath raised the price of exportable silver about 2d. or 3d. in the ounce above that of silver in coin, and hath thereby created a temptation to export, or melt down, the silver coin rather than give 2d. or 3d. more for foreign silver; and the demand for exportation arises from the higher price of silver in other places than in England, in proportion to gold; that is, from the higher price of gold in England than in other places in proportion to silver, and, therefore, may be diminished by lowering the value of gold in proportion to silver. If gold in England, or silver in East India, could be brought down so low as to bear the same proportion to one another in both places, there would be here no greater demand for silver than for gold to be exported to India. And, if gold were lowered only so as to have the same proportion to the silver money in England, which it hath to silver in the rest of Europe, there would be no temptation to export silver rather than gold to any other part of Europe. And to compass this last, there seems nothing more requisite than to take off about 10d. or 12d. from the guinea; so that gold may bear the same proportion to the silver money in England, which it ought to do by the course of trade and exchange in Europe. But if only 6d. were taken off at present, it would diminish the temptation to export or melt down the silver coin. And, by the effects, would shew hereafter better than can appear at present, what further reduction would be most convenient for the public.

“In the last year of King William, the dollars of Scotland, worth about 4s. 6½d., were put away in the North of England for 5s., and at this price began to flow in upon us. I gave notice thereof to the Lords Commissioners of the Treasury, and they ordered the collectors of taxes to forbear taking them, and thereby put a stop to the mischief.

“At the same time, the louis-d'ors of France, which were worth but 17s. ¾d. a piece, passed in England at 17s. 6d. I gave notice thereof to the Lords Commissioners of the Treasury; and his late Majesty put out a proclamation that they should go but at 17s.; and, thereupon, they came to the Mint, and £1,400,000 were coined out of them: and if the advantage of 5¼d. in a louis-d'or sufficed at that time to bring into England so great a quantity of French money, and the advantage of three farthings in a louis-d'or to bring it to the Mint, the advantage of 9½d. in a guinea, or above, may have been sufficient to bring the great quantity of gold which hath been coined in these last fifteen years, without any foreign silver.

“Some years ago, the Portugal moedors were received in the

West of England at 28s. a piece. Upon notice from the Mint, that they were worth only about 27s. 7d., the Lords Commissioners of the Treasury ordered their receivers of taxes to take them at no more than 27s. 6d. Afterwards, many gentlemen in the West sent up to the Treasury a petition, that the receivers might take them again at 28s., and promised to get returns for money at that rate; alleging, that when they went at 28s., their country was full of gold, which they wanted very much. But the Commissioners of the Treasury, considering that at 28s. the nation would lose 5d. a piece, rejected the petition. And if an advantage of 5d. in the 28s. did pour that money in upon us, much more hath an advantage to the merchant of 9¼d. in a guinea, or above, been able to bring into the Mint great quantities of gold, without any foreign silver, and may be able to do so still, till the cause be removed.

“If things be let alone till silver money be a little scarcer, the gold will fall of itself; for people are already backward to give silver for gold, and will in a little time refuse to make payments in silver without a premium, as they do in Spain; and this premium will be an abatement of the value of the gold; and so the question is, whether gold shall be lowered by the Government, or let alone till it falls of itself, by the want of silver money.

“It may be said, that there are great quantities of silver in plate, and if the plate were coined, there would be no want of silver money. But I reckon that silver is safer from exportation in the form of plate than in the form of money, because of the greater value of the silver and fashion together; and, therefore, I am not for coining the plate, till the temptation to export the silver money, which is a profit of 2d. or 3d. an ounce, be diminished; for, as often as men are necessitated to send away money for answering debts abroad, there will be a temptation to send away silver rather than gold, because of the profit, which is almost 4 per cent.; and for the same reason foreigners will choose to send hither their gold rather than their silver.”

Mr. Aislacie, the Chancellor of the Exchequer, brought the subject of the great scarcity of silver coin before the House on the 21st of December, 1717, and was seconded by Mr. Caswall, who gave details of the different relative values gold and silver coin had borne with respect to each other, according to the plenty or scarcity of each, and said that the over-valuation of gold in the current coins of great Britain, had caused the exportation of great quantities of silver specie. To prove this, he laid open a clandestine trade which had been carried on for many years by the Dutch, Hamburgers, and other foreigners, in concert with the Jews and other traders here, which consisted in exporting silver coins, and importing gold in lieu thereof, which being coined into guineas at the Tower, near 15d. was got by

every guinea, which amounted to about 5 per cent., and, as these returns might be got five or six times in the year, considerable profits were made by it. In his opinion, the only way of checking this was to lower the price of guineas and other gold specie.

Sir Isaac Newton had shewn that the true value of the guinea, according to the market values of gold and silver at that time, was 20s. 8d. The House, however, did not adopt his recommendation to its full extent, but they addressed the Crown to issue a proclamation to make guineas current at 21s. In accordance with this, the King issued a proclamation on the 22nd December, 1717, making guineas current at 21s., and reducing the other gold coins for 23s. 6d. and 25s. 6d. to 23s. and 25s. each.

This was the last alteration made in the relative values of gold and silver coin, and now, in the language of the Mint, the price of gold was fixed at £3 17s. 10½d. an ounce, which is so sore a puzzle to many persons. This alteration in the value of guineas created some alarm that it might be further reduced, and caused considerable confusion in trade, but, in January, 1718, both Houses of Parliament passed resolutions that they would not alter the standard of the gold and silver coins of the kingdom in fineness, weight, or denomination.

By the reduction of the price of the guinea, the value of gold to silver was fixed at $15\frac{14295}{68200}$ to 1; but, as in Holland and France the rate was $14\frac{1}{2}$ to 1, a profit still remained on exporting silver and importing gold. Thus gold became the cheapest medium in which to make payments; and, by this means, during the course of the last century, it became gradually an understood thing in commerce that gold was the standard of value. This custom was finally adopted as law in 1816.

We shall not here notice the great Currency Debates in 1811, as that is done in a subsequent chapter. We rejoice to see the great names of Locke and Newton establishing on incontrovertible foundations the great fundamental principles of the coinage, which are now at length happily adopted.

Immediately after the cessation of the war, the Government took in hand the great work of a complete re-coinage. The great principle, so earnestly enforced by Locke, of having only one metal as a standard measure of value, was at length adopted. During the course of the last century merchants had universally adopted the custom of paying their debts in gold, because, from the misrating of the Mint, it was the cheapest medium of payment. All contracts had consequently come to be considered as payable in gold, and this was now adopted as the sole legal tender. At the end of the 18th century the relative value of gold and silver had undergone a perceptible change in the markets of the world. Hence, the valuation that had been made of the two metals in 1717 no longer corresponded to the

market value of the two metals, and if a silver coinage had been issued of the former denomination and weight, the very same effects would have followed which had been so often experienced before. It would immediately have disappeared from circulation. In order to guard against this, the power of private persons to have silver coined was taken away, and the pound weight of silver was ordered to be cut into 66 shillings instead of 62. But of these four are kept back for expenses of coinage, and by way of seignorage, and only 62 are issued, but they are declared to be equal to £3 2s. in tale. The result of this is, that the present shillings pass current for rather more than 6 per cent. above their real value. In order to prevent any injustice to individuals from this depreciation of the coinage, it was enacted, that no tender of payment in silver above 40s. at any one time should be legal, either by tale or by weight. This arrangement of the English coinage has this great merit, that it allows a very considerable change to take place in the market value of gold and silver, without causing any disturbance in the currency. The amazing quantities of gold poured into Europe, greater than had ever before occurred in so short a time, created great apprehensions in many persons' minds that gold was going to undergo a rapid diminution in value, similar to what had happened in the 16th century. If this were the case, it would become necessary to consider what should be done with the British coinage. It is not likely that Parliament would ever sanction any alteration in the weight of the measure of value, or in other words, alter the Mint price of gold. If such a diminution in the value of gold should take place, of which there does not appear, as far as can be conjectured on so doubtful a point, any very great likelihood, the probable plan adopted would be to diminish the weight of the shilling to the 70th part of the pound.

CHAPTER V.



THE THEORY OF THE EXCHANGES.



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THE THEORY OF THE EXCHANGES.

DEFINITION OF THE "EXCHANGES"—DIFFERENCE BETWEEN MONEY-CHANGING AND BANKING—PAR OF EXCHANGE—EFFECT OF A DEPRECIATED COINAGE ON THE EXCHANGES—NOMINAL AND REAL EXCHANGE—NATURE OF AN EXCHANGE—ON FOREIGN EXCHANGE—LIMITS OF THE VARIATIONS OF THE EXCHANGES—EFFECTS OF AN INCONVERTIBLE PAPER CURRENCY ON THE EXCHANGES—ON EXCHANGE OPERATIONS—ON THE REAL OR COMMERCIAL EXCHANGE—CAUSES WHICH INFLUENCE THE MOVEMENTS OF BULLION—RATE OF DISCOUNT—FOREIGN LOANS—MONETARY AND POLITICAL CONVULSIONS—ON THE METHOD OF CORRECTING AN ADVERSE EXCHANGE.

1. We have said that when an interchange of like things takes place, such as commodities for commodities, or currency for currency, it is called an exchange. The "Exchanges" is that branch of Economics which treats of the exchange of the money of one country for the money of another, and of the remission of debts from one place to another by paper documents. They are merely an exemplification of the doctrines of Coinage and Credit which have been so fully explained in the preceding chapters.

2. Next to a universal language, it would be the greatest commercial blessing to all nations, if they could agree to use one uniform measure of value, and the same weights and coins. No small part, nay, we might almost say the chief part, of the intricacy and subtlety of the subject of exchanges, arises from different nations using different metals as the legal measure of value, and coins of all different denominations and values. If all nations could be brought to a uniformity on these subjects, there would be no more difficulty in understanding the Theory of the Exchanges between them than of those between England and Scotland. The artificial intricacy of the subject of exchanges gives rise to the employment of a considerable amount of labour, which is unprofitable to the community at large, exactly in the same way as a superfluous amount of technicality in a system of law gives rise to a large amount of unnecessary law business. Every one who has travelled abroad, knows how detrimental the different exchanges are to his purse, as he passes through the

different States. If any one were to take a quantity of money with him abroad, and pass through several different States, like those in Germany, it would soon dwindle away to almost nothing by the repeated operation of exchanging it for the current money of the country he happened to be in at the moment. The profits of the money-changers, as they do not arise out of natural operations, but out of the artificial distinctions in the different coinages, are wholly unprofitable to the community at large, because, in this case it is true, what many people think of real commerce, that the gains of one party are wholly made up of the losses of a number of others, whereas, the test of genuine commerce is, that both parties gain by the very nature of the transaction. It is clear, that the gains of the money-changers are no more additions to the wealth of the community, than the practice of sweating sovereigns in a bag, where the apparent profit is made up of the losses on each coin.

Banking first grew out of the operations of the money-changers, and was first practised by them, but yet banking and money-changing are wholly different in their nature. The latter produces no benefit to society, the necessity for it only arises out of the artificial and unnecessary defects of the commercial regulations of nations. If these were put on a better footing, the whole trade of money-changing would be swept away at a breath. As the want of proper sanitary arrangements often breeds the diseases which cause the necessity for medical men, so it is the imperfection of the monetary systems of the world that produces the necessity for money-changers. Banking, on the contrary, is wholly different in its nature; it is genuine commerce, and, like all genuine commerce, it promotes the interests of both parties, it blesses him that lends and him that borrows, and augments the prosperity and wealth of the community at large. The correction of the imperfect system which gives rise to the necessity of money-changers, would be an unmitigated blessing to every nation in the world; the abolition of banking would be the direst blow commerce could receive.

We have observed that, in former times, when there was comparatively little commerce between different countries, the coinage might circulate for a considerable time in a country without very much losing its value, after it had become considerably depreciated from loss of weight.

When these coins, however, are carried to a foreign country, they are of no value beyond their intrinsic weight as bullion. Though the natives of the country it belonged to, from long habit and association of ideas, see in it a certain denomination, and may receive it at its nominal value long after it has lost its legal weight, a foreigner sees in it nothing but so much bullion. When a person takes the coin of one country to another, and purchases the coin of that country with it, he is said to *exchange*

it. Now, suppose that the coinage of two countries is of the same metal, and that both of the coinages be of their full legal weight and fineness, then, if either of them be taken as a standard, which may be called A, then the number of units, or parts of a unit, of the coinage of the other, which may be called B, which contains precisely the same quantity of pure metal, is called the PAR OF EXCHANGE between the country A and the country B. Thus, if the legal standard of France and England were gold, and the pound be taken as the standard unit of England, the number of the standard units of the French coinage which contained precisely as much pure gold as the English pound, would be the par of exchange between England and France. The French standard is the franc, which is a silver coin. The gold Napoleon is also legal tender, which is twenty francs. Now, there is as nearly as possible one-fourth more pure gold in a sovereign than in a Napoleon, therefore, as the par of exchange is the ratio between these two coins, we might say that 1.25 is the par of exchange between England and France. But, as it is invariably expressed in *francs*, 1.25 Napoleons is equivalent to 25 francs, and hence we may, for the sake of argument, call 25 the par of exchange. Hence, if an English sovereign would exchange for 25 francs in Paris, we should say that the exchange was at par.

Though a worn and depreciated coinage might pass for its full nominal value in its own country, in a foreign country it will evidently only exchange for its actual weight in bullion; hence, if the English coinage of sovereigns became worn and clipped, or much diminished in weight, they would not exchange for so many francs as they would do if they were of full weight; hence, an English sovereign, if taken to Paris whilst the French coinage maintained its full weight, in such a depreciated state, might only exchange for 22 or 20 francs, and this would be called a *fall in the foreign exchanges*; or if an English merchant were bound to pay his creditor in Paris 2,500 francs, he would have to give more than £100 English to purchase them, and the exchange would be said to be *so much per cent. against England*, by the amount of that difference.

It is evident that this adverse state of the exchange would continue so long as the English coinage remained depreciated; but that if it were restored to its legal standard, that restoration would be itself sufficient to restore the exchange to its usual rate. Hence, we see that if any foreign country maintain its coinage of full weight and purity, that a *depreciation of the coinage of England necessarily produces an apparently adverse state of the exchanges, and that a reform of the English coinage is sufficient by itself to restore them to their proper state.*

It is also evident that a depreciation of the coinage, by a

debasement of its purity, will produce exactly the same effects. It is also clear, that if the coinages of both countries were equally degraded, the rate of exchange would not be altered between them; and that the rate would vary just in proportion as one was more or less degraded than the other.

Now, as when the coinage of a country has become depreciated either from wear and tear, or a debasement of the standard, the consequence is said sometimes to be a *fall* in the foreign exchanges, and sometimes a *rise* in the foreign exchanges, it is as well to fix clearly what these expressions mean, as it might be thought they are contradictory, when they are not so. They only refer to two different modes of estimating the coinage.

When a depreciated coinage is said to produce a FALL in the Foreign Exchanges, it means that a given amount of coinage will purchase a LESS amount of foreign coin.

When a depreciated coinage is said to produce a RISE in the Foreign Exchanges, it means that a GREATER quantity of coinage is required to purchase a given amount of foreign coin.

A clear understanding of these expressions will prevent any confusion arising when they are used indiscriminately, as they often are, in discussions on the Exchanges.

3. It is also evident that there can be no true par of exchange between two countries which do not employ the same metal as their legal standard. We have seen, in the preceding chapter, the insuperable objections to employing two metals as legal standards in the same country. Up to a comparatively recent period gold and silver were equally used, and their relative values were fixed by law. This was their legal par of exchange, but we also saw that their market values were constantly varying, and from causes quite beyond the reach of any law; and that it was no more possible to have a fixed price of one in terms of the other, than to have a fixed legal price for corn or other commodity. The very same rule must clearly apply to two countries, one of which uses gold and the other silver as the measure of value. Hence, in speaking of the par of exchange between England and France as 25:20, which it usually is, or that £100=2,520 francs, it is only on the assumption that the relative values of gold and silver are fixed, which we know can never occur between any two countries, any more than between the same metals in the same country. The only correct mode of expressing it is, therefore, to say that such is the *usual rate of exchange* between the two countries.

In the year 1797, when the Bank of England stopped payment, the House of Lords appointed a Committee to investigate the whole subject. The Committee, among other things, wished to ascertain the par of exchange between London and Hamburg, and they examined several merchants upon the subject, but they

were quite unable to agree among themselves what was the par of exchange between these two places; and the Committee reported that they were unable to come to any satisfactory conclusion on the subject, and in this they were correct. And the very same reasons apply to any other two countries which use different metals as measures of value, as there is not in the nature of things any permanently fixed relation between them. Hence, there cannot be, in the nature of things, any fixed par of exchange between England and any country that uses exclusively a silver standard. The most that can be said is, that there is a usual rate of exchange between them; hence, between such countries, it is often totally impossible to decide certainly which way the exchange is, unless the difference exceeds a certain limit. At the time of the foundation of the Bank of England, in 1694, the coinage of England was in such a disgraceful state from the wear and tear of many years, and extensive clipping, that the rate of exchange between London and Hamburg, owing to this circumstance alone, was 25 per cent. against England.

Although, when the currency is in a depreciated state, the exchange will be apparently adverse with those countries which maintain their currency in its standard state, it is quite clear the exchange, as founded upon the commercial operations of the two countries, may be above, below, or at par; and it is a very simple matter to discover its true state, that is, whether it is favorable or the contrary, and the amount of its difference either way. The rate of the exchange, which arises out of the state of the currency, is called the **NOMINAL EXCHANGE**; the rate which arises out of the commercial relations of the country, is called the **REAL EXCHANGE**. Thus, if we suppose that the exchange on Paris is 2,521 francs for £100 in gold at the Mint price, or when the currency is at its full legal weight, then, if we suppose that, in consequence of the depreciation of the currency, the market price of gold bullion to rise to £4 3s. per oz., then the market price of £100 is £106 11s. 7½d. Now, suppose that the exchange on Paris is 23·80, or £100 will purchase 2,380 francs in Paris, then £106 11s. 7½d. would be able to purchase 2,536·63 francs. But, as the real par at the Mint price is assumed to be 2,521, it is evident that the difference between these two sums is the extent to which the real exchange is in favour of London. We can also see the extent to which the exchange is depressed, because £100 at the above exchange will purchase 2,380 francs, whereas they ought to purchase 2,536·63, if they were of full weight; and the difference between these two sums shews the extent by which the nominal exchange is depressed. Hence, we have the following rule:—

Find the market price of the sum in London compared to the Mint or money price, multiply the market price so found by the

rate of exchange, then, if the result is equal to the par of exchange, the exchange is at par, and if there be a difference, the exchange is favourable, or adverse, according as the difference is above or below the par, and the depression of the exchange, caused by the depreciation of the currency, is the difference between the sum so expressed in the mint and market prices multiplied by the rate of exchange. In the excellent state in which our currency now is, the question of the nominal exchange is of little importance, but it is impossible to understand the history of the currency in former times without it: and it is essential now with regard to several foreign countries at present which use an inconvertible and depreciated paper currency.

On the Nature of an Exchange.

4. We will now explain the nature of an exchange. Suppose two cities, say London and Edinburgh. Suppose a trader A in London is debtor to a trader B in Edinburgh for a certain sum: suppose also that a trader B¹ in Edinburgh is debtor to A¹ in London for an equal sum. Then, in order to pay their debts, A would have to send the money to B, and B¹ would have to send an equal sum to A¹, thus causing two separate transmissions of bullion between London and Edinburgh, at some expense for freight and insurance.

Now, this settlement of debts may be greatly facilitated, if A in London goes and pays his debt to A¹, and buys from A¹ the debt due to him from B¹, and sends this debt by post to B in Edinburgh. B then goes to B¹ and demands payment from him of his debt due to A. Thus, it is clear that the whole business has been settled by the transmission of the debt, instead of by the transmission of twice the amount in bullion, and each debtor been paid the debt to the creditor in the same town.

The whole transaction is called an exchange, and it is clear that there must be a debtor and a creditor in each city. In the case given there are *four* parties; but an Exchange is possible with *three* parties. Thus, suppose that A in London owes B in Edinburgh a debt, and B¹ in Edinburgh owes A in London an equal debt. Then it is clear that A may pay B by transferring to him the debt due to himself from B¹. From this, it is seen that *three* parties are indispensable to an exchange.

We may observe that a consideration of this transaction is sufficient to disprove the popular account that Bills of Exchange and exchange operations were invented by the Jews. A crowd of writers have said that the Jews, having undergone a terrible persecution in France towards the end of the 12th century, invented Bills of Exchange in order to transmit their effects from France to foreign countries. This account, however widely received, is impossible, because it is clear that exchange operations can only arise out of reciprocal debts being due between

two places, as they cannot take place unless debtors and creditors of the one reside in the other. To suppose that people could simply remit their money by means of Bills of Exchange, is as absurd as to suppose that a man could send his luggage by the electric telegraph. All that he could do in either case would be to send an *order* to deliver his money, or his luggage, to some one else.

Now, when the debts between London and Edinburgh are equal, it is evident that they may all be discharged by means of such an exchange, without remitting any specie. The exchanges are then said to be at *PAR*.

Supposing, however, that the debts are unequal, and Edinburgh wishes to send more money to London than it has to receive, it is clear that the demand for bills is greater than the supply, and, as every one would rather send a bill than cash, as it is cheaper to do so, those who had money to send would bid against each other for the bills in the market as for any other merchandize, and the price of them would rise, or a premium would have to be paid for a bill on London.

Now, London is the great centre of commerce. It supplies the rest of the country with foreign merchandize: it is the seat of Government, to which the revenue is remitted from all parts of the country: the great families from all parts of the country go to reside there, and their incomes must be remitted to them there: hence there is almost always a much greater quantity of money seeking to flow from the country to London than the contrary: consequently, the demand for bills on London in the country is greater than the supply, and, therefore, inland bills upon London are always at a premium.

This premium is computed by time. Thus, if a person paid a sum of money into a bank in Edinburgh, in former times, he got a bill payable at 60 days' date in London; or, if he wanted it payable at sight, he had to pay 60 days' interest. This was afterwards reduced to 40 days, and was estimated at about $\frac{1}{2}$ per cent. As communications improved, this was reduced to 20 days, or 5s. per cent. But, in consequence of the still further facilities afforded by railways, the premium is now reduced to 1s. per cent.

Hence, if a person in Edinburgh wishes to have a bill at sight on London, he must pay 1s. per cent., or four days' interest, on it. And this time is also called the *Par of Exchange* between London and Edinburgh. There is a similar premium on bills, or par of exchange, between all other cities in the country on London. This is called *Inland Exchange*.

The Exchange of the country upon London is said to be against the country and in favour of London. But it must be observed that it is only unfavourable to the *buyers* of bills, or those who wish to *send* money. It is equally favourable to the *sellers* of bills, or those who have to *receive* money.

The exchange is called unfavourable, because, after the settlement of the whole debts between the two places, there remains a sum in cash to be remitted.

It appears from this, that when in any place the demand for bills is greater than the supply, the Exchanges are *adverse* to that place, because it has more money to pay than to receive: when the supply is greater than the demand, the Exchanges are *favourable* to it, because it has more money to receive than to pay.

On Foreign Exchange.

5. The principle of Foreign Exchange is exactly the same as that of Inland Exchange. But there is somewhat more complication in the detail, on account of the different moneys of different countries.

In Exchange between two foreign places and of different moneys, the money of one place is always taken as fixed, and the Exchange is reckoned in the variable quantities of the money of the other given for it. The former is called the *fixed* or *certain price*, and the latter the *variable* or *uncertain price*.

Thus, between London and Paris, the Exchange is always reckoned by the *variable* sum in francs and cents given for the *fixed* £.

On the contrary, between London and Spain, the Exchange is always reckoned by the *variable* sum in pence given for the fixed dollar of Exchange.

When a certain place is taken as a centre, if the fixed price is the money of that place, it is said to *receive* the variable price: on the contrary, when the money of that place is the variable price, it is said to *give* the variable price.

Thus, at any time, London *receives* from Paris so many francs and cents for the £1 sterling; and London *gives* Spain so many pence for the dollar.

In the quotations of the Rates of Exchange, it is usual to omit the fixed price and name only the variable price, and then that is called the *Rate* or *Course of Exchange*.

One source of perplexity in the Foreign Exchange arises from the circumstance that, in consequence of London *giving* the variable price to some places, and *receiving* it from others, the same state of the exchanges will have to be expressed in opposite language, as we have observed above, in speaking of the expressions used regarding the Foreign Exchanges *rising* or *falling* in consequence of a depreciated currency.

According to *Tate's Modern Cambist*, the following are the present Rates of Exchanges between London and the principal Foreign Cities:—

London receives from

Amsterdam	12 3	Florins and Stivers for	£1
Hamburg	13 12	Marks and Stivers	—
Paris	25 50	Francs and Cents	—
Frankfort	121	Z. V. Florins	10
Vienna	13 70	Florins and Kreuzers	1
Genoa	25 35	Lire and Centesimi	—
Berlin	6 25	Dollars and Silver Gros	—
Milan	25 40	Lire and Cent	—
Leghorn	25 50	Do.	—

London gives to

Lisbon	53 $\frac{1}{4}$	pence sterling for	1 Milreis
Madrid	50 $\frac{1}{4}$	”	1 Hard Dollar.
Gibraltar	48 $\frac{1}{2}$	”	1 do.
Naples	39 $\frac{5}{8}$	”	1 Ducat
Palermo	119 $\frac{1}{2}$	”	1 Onza
Venice	47	”	6 Lire Austriache
St. Petersburg.	38 $\frac{1}{4}$	”	1 Silver Ruble
Rio Janeiro	30	”	1 Milreis
New York	47 $\frac{1}{2}$	”	1 U. S. Dollar
Calcutta	23	”	1 Comp. Rupee.

Now, if the exchange of London on Paris is against London, or the demand in London for bills on Paris is greater than the supply, it is clear that the £ sterling will purchase *fewer* francs. Hence, between London and Paris, when the exchange is adverse to London, the rate or course of exchange will *fall below* par.

On the contrary, when the exchange is favourable to London, that is, the supply is greater than the demand, the rate of exchange will *rise above* par.

And the same is manifestly true with respect to all other places *from which* London *receives* the variable price.

But, suppose the Exchange between London and Madrid is against London, or the demand in London for Bills on Madrid is greater than the supply, then London will have to *give more* pence to purchase the Spanish dollar.

Hence, between London and Madrid, when the exchange is against London, the Rate, or Course of Exchange, will *rise above* par.

On the contrary, when the exchange is favourable to London, she will have to give *fewer* pence to purchase the Spanish dollar, and, consequently, the Rate of Exchange will *fall below* par.

And the same is manifestly true, with respect to all other places *to which* London *gives* the variable price.

Hence, when the Exchange between London and any other place, varies from par, we must always consider whether London gives the variable price to, or receives it from, that place.

The interests also, of the buyers and sellers of bills are always opposite. If the Rate of Exchange is favourable to the one, it is equally unfavourable to the other. The buyers of bills are also called *remitters*, and the sellers are also called *drawers*.

On the Limits of the Variations of the Exchanges.

6. Supposing that while the Exchange between any two places—say London and Paris—is in a state of equilibrium, that is, when the demand and supply of bills in each city is exactly equal, so that they would each have to receive and send the same sum, it should happen that from any cause whatever, no matter what, there should be a desire on any particular day to send more money from one side than it has to receive. Suppose more money has to be sent from London than it has to receive, then those merchants who want to remit money from London will strive to buy bills on Paris in the London market. But, as the demand is greater than the supply, a competition will spring up to buy the bills that are in the market, and hence the price of them will rise. It is their duty to place the bullion in Paris at their own expense and risk, and, consequently, they would rather give somewhat more for a bill than its par price, to save themselves that expense. But they will not give more than the cost of transmitting the bullion itself, because, if the price rose higher than that they would sooner send the money. Thus, when the Exchange in London rises against London, or, in the case of Paris, falls below par, it shows that London wishes to send to Paris more than it has to receive, and the exchange is said to be against London, but it is clear that it cannot continue at a greater rate against London than the cost of transmitting bullion. Hence this is manifestly a superior limit to the variation of the Real Exchange.

But the reverse case may also happen. The supply of bills in London on Paris may exceed the demand. The price of them will, therefore, manifestly fall. But for similar reasons the cost of transmitting bullion will be an inferior limit below which the price will not fall.

We thus see that the state of the exchanges arising out of the cross remittances of money is a simple example of the general law of supply and demand, with the exception that the variation in the rates of exchanges cannot exceed a certain definite sum, namely, twice the cost of sending bullion from one place to the other.

These limits of the Rate of Exchange are called *specie points*, because, when the Exchanges reach them, bullion may be expected to flow in, or out, as the case may be.

It is to be observed, however, that these limits of the variations of the Exchange, or specie points, only apply to bills payable at once, and to long periods. During short

periods, and for bills which have some time to run, temporary causes may produce fluctuations in the Exchanges greatly exceeding these limits. We shall consider these cases fully afterwards.

On the Effects of an Inconvertible Paper Currency on the Foreign Exchanges.

7. We must now consider what the effect of an inconvertible paper currency will be on the foreign exchanges, and the market price of bullion. So long as paper is convertible, that is, the holder of it has the power to demand payment in gold for it at sight, it is very clear that it cannot circulate at a discount, because, if it fell to a discount, every person who held it would immediately go and demand gold for it. But, if while it enjoys considerable circulation, the power of convertibility is suddenly taken away, then it becomes, in all respects, equivalent to a new standard, just as much as gold or silver, and its value will be affected by the same principles as these two, viz., by the sole question of the *quantity* of it in circulation, compared to the operations it represents.

Under the old system of making an attempt to fix the value of silver and gold relatively to each other, there was no power of convertibility of one into the other similar to the convertibility of the note. If silver fell to a discount, as compared with gold, no persons could demand, as a right, to have their silver exchanged for gold, consequently, the inevitable result of a considerable change in the quantity of either metal was a change in their market values. Thus, in 1794, gold rose to 84s. if purchased with *silver* bullion; now, if, speaking by analogy, the silver coin had been convertible into gold, the difference never could have arisen, any more than a bank note, convertible at the will of the holder of it, could circulate at a discount. Now, paper, when issued as a substantive standard of value, follows exactly the same rules; if only the usual quantity of it be issued, *i. e.*, no greater quantity than would have been issued if it were convertible into specie, it will continue to circulate at its par value; but, if these issues be continued, and if it be deprived of the natural corrector of an over-issue, viz., payment on demand, it is maintained in circulation, and exactly the same result follows as attends an excessive issue of silver,—it falls to a discount. Now, the silver coin may fall to a discount from two circumstances, either if silver be coined with too great profuseness, the excessive quantity of it will *diminish its value*, even though the coin be of full weight; or, if the silver coin be suffered to fall into a degraded state by clipping and wearing, so that it does not contain the full legal weight of bullion, it then becomes *depreciated*. The apparent result in figures will be just the same in either case, guineas will rise to 24s. or 30s. But, as silver has

general value, and is, from its qualities, a recognised measure of value, it is not correct to apply the term *depreciation* to it as long as the coin contains its full legal weight of bullion. But the case is different with paper; it is only received on account of bearing a promise to pay a certain quantity of bullion on the face of it, and if it is not able to fulfil that promise, it is *depreciated*.

Now if, for the public convenience, it be deemed advisable to issue an inconvertible paper currency, the only way of maintaining its currency at par is by limiting its quantity. We do not mean by this, limiting its quantity to an absolute fixed amount, but by devising some means whereby *a greater quantity of it shall not be issued than if it were convertible into gold*. If more than this be issued, it will be followed by the same result as attends an excessive issue of silver, it will fall to a discount, which, in this case, is *depreciation*, and the necessary consequences of a depreciated currency will follow, viz., the market price (or paper price) of bullion will rise above the mint price, and the foreign exchanges will fall.

Now, if such a state of things happens, the proper remedy is to *diminish* the quantity of the paper in circulation until the market price of bullion is reduced to the level of the mint price. If the direct power of demanding five sovereigns be taken away from the holder of a £5 note, still, if he can purchase bullion with it in the market to the amount of five sovereigns, it is an infallible proof that the note is current at par; and the limitation need not proceed beyond that. But, if this be not done, the next best thing is to allow all persons to receive the notes at whatever value they choose to put upon them, and let them make a difference, if they choose, between the prices of articles when paid in gold, or in paper. If this be allowed, no very great inconvenience will take place in the internal trade of the country beyond a certain loss of *prestige* which must happen to an institution whose paper circulates at a discount.

But suppose the law, with more zeal for the honor of the paper currency than discretion, declares it to be a crime to make a difference between paper and gold, and a punishable offence to give twenty sovereigns in gold for twenty-one pounds in paper—what will be the consequence? Exactly the same as we have seen happened when the silver and gold coins were improperly rated, *the one which was underrated disappeared from circulation*. We have seen this happen both in the case of the gold coin and the silver coin. Now, when the inconvertible paper currency is issued in too great abundance, and has a tendency to overflow the channels of circulation, its natural effect is to raise prices when paid in it. If people were free in their transactions, they would gradually make a difference in price between payments in paper and payments in bullion;

but if the owners of the coin are prevented by law from receiving more for it than the same nominal sum in paper, they will do exactly the same thing as is invariably done when, in a metallic currency, part is depreciated and part is of full weight, they will either hoard or export it. At all events, it will disappear from circulation. Now, as the gold gradually disappears, and paper issues multiply, people begin to estimate all prices by transferring their ideas from the gold to the paper, and the paper ends by finally displacing the entire gold coinage.

The stamp on the coin is similar to the banker's "promise to pay" on a note. The stamp is the guarantee of the State, that the coin does actually contain a given amount of bullion; the "promise to pay" is the banker's guarantee that he can pay so much coin if required. The convertibility of the coin into the legal amount of bullion, is the test of the depreciation of the metallic currency; so the convertibility of the note into coin is the test of the depreciation of the note. If the power of demanding coin be taken away by the *State*, the power of commanding a certain quantity of bullion in the market still equally remains as the only test of its value. The *Mint* price of bullion is the price paid in coins of the full legal weight, the market price means its price paid in the current coins, and a difference between the two is the proof and measure of the depreciation of the current coin. When paper became the standard currency the market price of bullion meant the price of it when paid in the paper currency, or the paper price of it; and, by a parity of reasoning, if the paper price of gold bullion rose above the *Mint* price, it was the *proof and the measure of the depreciation of the paper currency*.

Whenever the currency of a country becomes redundant, that is to say, that prices rise so much higher in one country than in its neighbours, that the value of money sensibly diminishes, the natural corrective for such a thing is to take a certain portion of it out of circulation, so that, by diminishing the quantity of it, its value may be raised. When people find that the same quantity of gold will not purchase an equal amount of commodities in this country, as they will in another, their own natural instincts will lead them to purchase commodities abroad where they are cheap, and bring them for sale here where they are dear. The natural instincts of trade will, therefore, produce an equilibrium in value, in the currency of neighbouring countries.

Now, when the currency of a country consists partly of paper and partly of gold and silver, it is quite clear that only the metallic portion of it can be exported in payment of foreign commodities. The paper portion of it, which has no value abroad, must remain at home. If the issues of the paper be continued, so as to prevent the currency from recovering its value, the process of the exportation of the metallic portion will

go on until it is entirely exhausted. If this be the case, the only method of restoring the currency to its former value is by diminishing the quantity of the paper, until the drain is stopped by the enhancement of the value of the whole currency. There is, however, a School of Doctrines that maintains that, as the gold goes out, paper should be issued to supply the vacuum until the gold comes back. But it requires little sagacity to see that if that be done, *the gold never will come back again*, and the drain will not cease until it is totally exhausted, and the only way to bring it back again, is to raise its value at home, which can be done only by removing the plethora of paper. When the currency is in its healthy state, the oscillations of the exchange may be compared to those of a tight, staunch ship, which has always a natural tendency to recover itself; but when there is an excessive quantity of paper, it is like the same ship waterlogged, when she once heels over she never can recover herself until the water is pumped out.

The doctrine that *the rise of the paper price of bullion above the Mint price, and a continuous state of the Foreign Exchanges below the limits of the real exchange, are the proof and the measure of the depreciation of an inconvertible paper currency*, may be called Lord King's law of the currency, because he bore the most conspicuous part in establishing it. The rise of the paper price of bullion attracted great attention soon after the beginning of this century, when Lord King and some others published pamphlets to demonstrate the above proposition. However, the price of bullion fell, and the subject slept till 1809, when the extraordinary rise of the paper price of bullion began again to be seriously felt. Ricardo then appeared as a writer for the first time, and a pamphlet he published to prove Lord King's doctrine, was the foundation of his fame as an Economist. This controversy gave rise to the famous Bullion Report, and the great currency debates in 1811, when the House of Commons solemnly repudiated the doctrine. These debates are narrated at great length in a subsequent chapter. This doctrine is now universally admitted, so that it is needless to say much more about it.

On Exchange Operations.

8. Exchange operations consist in buying, selling, importing and exporting bullion, called "Bullion Operations," and buying and selling Bills, called "Banking Operations."

The calculations necessary to ascertain the profit and loss on such operations, are given at length in various technical works on the subject. Our object only is to examine the general causes which produce these movements of bullion, which so sorely vex the banking and commercial world.

Exchange operations of both sorts may be either direct or

indirect, that is, they may take place directly between the two countries, or the final operations may be effected through the medium of one or more intermediate countries.

We have observed that for bills payable at sight the limits of the variations of the exchange cannot exceed the cost of the transmission of bullion, which are called the specie points, because, when they are reached, bullion may be expected to flow in or out.

When the bills, however, have a considerable time, such as three months, or more, to run, before they are payable, causes may operate which may produce *temporary* fluctuations of the exchange considerably beyond these limits. These are chiefly—

1. The necessity that the holders of these long-dated bills may have to realize them, even at a considerable sacrifice, to maintain their own position.

2. The doubtful position of the acceptors, or the general discredit of the place they are drawn upon.

3. The differing relative values of the precious metals which are the standards of payment at each place.

4. The respective rates of discount at each place.

Now, it may very often happen that, from these combined causes, it may be considerably more profitable to possess bullion at one place than another. Whenever this is the case, exchange operators export bullion from one place to another for the sake of this profit. They create bills upon such a place, they draw upon their correspondents, discount their bills, and remit the proceeds to meet their drafts when due.

It used to be the dogma of many commercial writers that bullion was only exported to discharge a previous state of indebtedness, and that consequently a drain of bullion came to a natural end, when the indebtedness was discharged. But this is a most grievous error. The sufficient difference of profit in possessing bullion at two places will cause a fabrication of bills for the purpose of exporting bullion, without any previous indebtedness, and, of course, this will continue so long as this possibility of profit exists. Consequently, unless this profit is destroyed, the drain of bullion will not cease. The effectual way of annihilating this profit is by raising the rate of discount.

It is manifest that in such operations, the difference of profit between the two places must exceed twice the cost of transmitting bullion, because, in such cases, the cost of transmitting the bullion both ways will fall on those who originate them.

Between countries in which there are no restraints upon trade, the exchanges will never vary much, except on some sudden emergency; but there are countries with which, owing to the prohibitive laws which still infest their commercial codes, the exchanges are permanently unfavourable, because they will take nothing but bullion for their commodities. Russia is one of

these countries, and hence, if not modified by other circumstances, bills upon Russia would always be at a premium; but here again the effect of trafficking steps in, which always has a tendency to equalise prices. The merchant (if we may call him so) who deals in bills, acts upon the same principles as the dealer in any other commodities, he buys them where they are cheapest, and sells them where they are dearest. Hence, he will try to buy up Russian bills cheap in other exchanges, or debt markets, and sell them in the London debt market. On the other hand, from the course of trade between England and Italy, the debt which Italy owes to England is usually greater than the contrary; hence, Italian bills will usually be at a discount, or cheap, in the London debt market. So the bill merchant buys them up cheap here, and sends them to some other market—Paris, for instance—where they may be at a premium. By these means, the price of bills is raised where they are cheapest, and depressed where they are dearest; and the general result will be to melt all the differences between separate countries into one general result, so that the exchanges will not be favourable with one country and adverse with another, but they will be generally adverse or favourable with all the rest of the world.

Supposing, however, a merchant has to remit money to Paris while the exchange with Paris is unfavourable to England, he may possibly discover a more advantageous way of remitting it than by buying a bill on Paris directly. Thus, for instance, while bills on Paris are at a premium in London, those on Hamburg may be at a discount, and bills on Paris may be at a discount in Hamburg. So, if the merchant buys a bill on Hamburg and sends it to his agent there, and directs him to purchase a bill on Paris with the proceeds, he may be able to discharge his debt in Paris at a less sum than he would have to pay for a Paris bill in London. This circuitous way of settling his debt involves additional charges for brokerage, commission, postage, &c., but the effect of it is still further to equalize the exchanges between London and all other countries. This circuitous method is called the *arbitration of exchanges*, and the sum which is given in London for the ultimate price it realizes in Paris is called its arbitrated price. When only three places are used in the operation as above, it is called *simple arbitration*. When more than three are employed, it is called *compound arbitration*. The practical rules for working out these results are very simple, and will be found in any technical book on the subject. But it is very evident, that the quicker, safer, and cheaper the communication between countries become, the less room will there be for such operations, because the limits of the variation of the real exchanges, which are the margin which renders such transactions possible, will constantly diminish.

The scale on which these indirect operations of exchange is carried on is immense, and peculiarly affects the London exchange. There is no exchange between places to and from which remittances have not constantly to be made. Consequently, when such places trade, their accounts must be settled by means of drafts upon some third recognised centre. Now, London is the banking centre of the world. From the enormous exports of England to all quarters of the globe, remittances have to be made to London from every part of the world. There is, therefore, a constant demand for bills upon London to discharge the debts incurred for these commodities. Hence, although the exporters may send their goods to different countries, yet if they can draw upon London their bills will be sure to find some purchasers somewhere to be remitted to England. Hence Bills upon London bear a higher price and meet with a readier sale than those upon other places.

One country A may import from another B less than she exports, and, consequently, a debt is due from A to B. Also, B exports to another country C more than she imports; and, consequently, a debt is due from C to B, and A may discharge its debt to B by transferring to it its claim against C.

As many countries trade with one another, between which there is no exchange, their claims are mutually adjusted by drafts upon London, the commercial centre. Hence, the London exchange is the most important in the world, and requires the greatest attention to be paid to it.

In the same way that there are arbitrated rates of exchange, there are arbitrated prices of bullion, but we need not enter into them here.

On the Real or Commercial Exchange.

9. We must now consider the causes that affect the Real Exchange, or the true Commercial one, which arises out of the transactions between this and other countries. As the British Islands do not produce the precious metals to any extent worth considering, they are only to be obtained in this country by importation, and we must now consider the various sources from which they come, and the different causes that produce an influx, or efflux, of them. They are to be treated in every other respect like any other foreign commodity, and are obtained by the same means as any other one that we require for domestic consumption which is not a native product.

The trade in bullion may be divided into two distinct branches: the one where it is carried on directly with the countries in which gold and silver are native products, and the other with those countries which do not produce it, but which, like our own, have no means of supplying themselves with it except by foreign commerce.

I. *With bullion-producing countries.* Before the late discoveries in California and Australia, the chief bullion-producing countries were Mexico and Peru. We need not specify others, because the same principle applies to them all, and to describe them all would rather belong to a work on commerce generally. British merchants have establishments, or correspondents, in these countries to whom they consign their goods, and their agents exchange them for the bullion brought down by the natives, and which is collected in large quantities, and usually brought home by men-of-war for the sake of security. Most of the men-of-war on the Pacific and West India stations make a voyage along the coast before they return home to collect bullion from the merchants, and the captain receives a commission on the freight. In these countries bullion is treated exactly like any other commodity, such as tea, or wool, or wine, and the British goods of all kinds are exported to them for the express purpose of being exchanged for bullion to be remitted home. The limits of this exportation are precisely similar to the limits of the exportation to any other country. It is clear, that by the time the bullion reaches this country, it ought to be sufficient to cover the original price of the goods, and all the charges on them on their way out, as well as the agent's commission there, the charges for freight, insurance, and commission for bringing it home, and a fair mercantile profit over and above all these expenses. Unless it does that, the commerce is not profitable. If too many goods are exported to these bullion-producing countries, their exchangeable value with bullion falls, and they will not purchase a sufficient quantity of bullion to afford this profit, and the further exportation of such goods to these markets must be discontinued until the goods first sent out are consumed and fresh ones required. The purchase of bullion, then, in these countries, is a very simple affair, and requires no further notice.

II. *With countries which do not produce bullion.* The causes which produce an inflow or outflow of bullion, between this and other countries like it, which do not produce bullion, are much more intricate, and have excited long and keen controversies. Taking this country as the centre, we may consider that the transmission of bullion to or from it, is influenced by the SEVEN following causes:—

1. The balance of payments to be made to or by it.
2. By the state of the foreign exchanges.
3. By the state of the currency.
4. By remittances made to this country, as the commercial centre of Europe, to meet payments due to other countries.
5. By the political security of this and neighbouring countries.
6. By the state of the money market, or the comparative rates of interest in this and neighbouring countries.

7. By the free or prohibitive commercial tariffs of this and foreign countries, as they permit or forbid our manufactures to be imported into them.

There are, then, seven different causes which act upon the movements of bullion, and, in any case, it is necessary to ascertain to which of these causes it is due. The inveterate error of mercantile opinion for a long time was, that there was only one cause which caused an export of bullion, namely, a balance of payments to be made.

We have already shewn that a degraded state of the currency has the inevitable effect of driving away bullion from here. As we may fairly hope that our currency will never again be allowed to fall into such a disgraceful condition as it was till 1816, we may consider that this cause is not likely to operate again on the bullion market; and we may now proceed to develop the system of the FOREIGN EXCHANGES.

According to the crude ideas that were generally received about a century ago, gold and silver were almost universally considered to be nearly the only species of wealth, and it was considered to be the true policy of every country to encourage by every means in its power, the influx of bullion, and to discourage its export; and most, if not all, of the European nations have gone so far, at one time or another, as to prohibit its export. The profit of foreign commerce was estimated solely by the quantity of gold and silver it brought into the country; and the Theory of Commerce seemed to be reduced to a general scramble among all nations, to see which could draw to itself most gold and silver from the others. According to this theory, the gain of one party was the loss of the other; every article produced in another country, and imported into this one, was considered to be a direct loss to the country. This was what was called the mercantile or commercial system. According to this theory, the leading maxim which governed the Legislature was, to make the exports to exceed the imports; and the conclusion drawn was, that the difference, or balance, must be paid for in cash by the debtor nation. When two nations traded with one another, the difference of debts between them was called the "balance of trade," and, when this was in favour of England, the exchange was said to be favourable, because bullion had to be paid to her; on the contrary, when, on the result of trade, payments had to be made to her, the balance of trade was said to be against her, and the exchange unfavourable, and then gold was sent out of the country. According to this theory, the prosperity, or the contrary, of the country, and the profit, or loss, of foreign commerce was exactly measured, according as gold had to be received or paid, or as the exchange was favourable or the reverse.

The admirable chapter of Adam Smith on the Principle of

Mercantile System, is a masterly exposition of the fallacy of this theory, and is certainly one of the soundest and best written in his whole work, from the more than usual consistency of its ideas, and the lucidity of its style. There are, however, some things relating to the subject which require further enforcement and illustration.

So far from the principle of the mercantile theory being true, that gold and silver are the most profitable and desirable objects of import, the direct reverse is unquestionably true, that gold and silver, are of all objects of commerce, the most unprofitable; and it is a certain axiom of commerce in a state of freedom, *that bullion will not be imported until it has become unprofitable to import any other article.* There are no class of traders who derive so little profit, in proportion to the capital invested in their business, as dealers in bullion and money of all sorts, whether they be bullion merchants or bankers. Although the opinions we have alluded to above were the prevalent ideas of the age, there were not wanting a few sagacious thinkers, who discovered the truth of what we have last said, and maintained the unprofitable nature of gold and silver; but, like others who are before their age, their voice was unheeded, and the general object of commercial ambition and legislation was to accumulate treasures of gold and silver.

There is no expression in commerce of more frequent occurrence than the "balance of trade," and it may be as well to give the interpretation of it generally received during the last century, and which is not yet wholly extinguished. Mr. Irving, Inspector-General of Imports and Exports in 1797, defined it thus:—"The common mode of considering that question has been to set off the value of the imports, as stated in the public accounts, against the value of the exports, and the difference between the one and the other has been considered the measure of the increase or decrease of the national profit." And Mr. Hoare, a banker of eminence for twenty-two years, said:—"I consider the only proper means of bringing gold and silver into this country to arise from the surplus of our exports over our imports, and that ratio or proportion which is not imported in goods must be paid for in bullion. In the year 1796, the imports of this country appear to be £19,788,923, and the exports appear to be £33,154,583, which ought to have brought to this country bullion to the amount of that difference, or £10,665,660."

We have made these extracts because they convey, in the fewest words possible, the whole ideas on the subject, and they are made by persons of great commercial eminence before the Committee of the House of Commons. It is true that Mr. Irving, who was Inspector-General of the Exports and Imports of Great Britain and the British Colonies, expressly states that the application of this principle to the whole of the British trade

would, in his judgment, be extremely erroneous. We, therefore, do not bring him forward as *approving* of the theory; but only as stating distinctly and authoritatively what it was. But Mr. Hoare, a banker of eminence and long experience, adopted it; and we believe that this theory of the balance of trade still retains a hold on the minds of great numbers of persons who do not give themselves the trouble to sift it thoroughly. Nevertheless, there never existed a more complete chimera and pernicious delusion than this said doctrine of the balance of trade, nor one which has exercised so disastrous an influence on commercial legislation.

It appears that the simplest way of arriving at an accurate conclusion on the subject is, to consider that the dealings between nation and nation are only made up of the aggregate of dealings between individuals of the nations, and we have only to consider the variety of methods in which an individual merchant may trade, to have an accurate and comprehensive idea of the commerce of the nation. Instead of dealing with figures of vast amount, which make no definite impression on the mind, and which are produced by a number of complex causes, we shall now proceed to consider in how many different ways an individual merchant may trade with foreign countries, and we shall shew, by considering the dealings of an individual, how utterly erroneous it is to suppose that an influx of bullion is, *ipso facto*, a proof that commerce is flourishing and profitable to the country, and that whether it is so or not depends very much as to where it comes from, as well as a number of other circumstances.

With respect to those countries in which bullion is a native product, and to which we trade for the express purpose of obtaining it, we have already shewn, that unless the quantity obtained in exchange for our goods exceeds a certain amount, the commerce is not a profitable one, and that the simple fact of bullion being remitted from them, and, therefore, though the exchanges with them must always be in our favour, it is no proof whatever of prosperity or profit.

Next, with respect to countries which do not produce bullion, it is easy to show the extreme fallacy of the opinion that our exports should exceed our imports, and that the *difference* will be the *profit* of the country; in many cases the precise reverse is true, that our imports should exceed our exports, and the profits are measured by the exact sum by which the imports exceed the exports, or the excess of what we receive over what we give.

To prove this, let us take a simple case. Suppose a merchant in London sends out £1,000 of goods to Bordeaux, by the time they arrive there, the mere addition of freight, insurance, and other charges, will probably have increased their cost of produc-

tion, or the expense of placing them where they are, to £1,050, supposing them to be sold without any profit at all. But, as the merchant would never have sent them to that market unless he expected to realize a good profit, we may assume that the market is favourable, and that they sell for £1,500, and he would probably draw against his agent for £1,200. His correspondent at Bordeaux, instead of remitting the money to England, would find it far more profitable to invest the proceeds of the goods in some native product, which would fetch a good price in England. The chief native product of that country is *wine*, so the agent would invest the proceeds of the goods, after deducting all charges for freight, commission, &c., in Bordeaux wine, and send it to England. This wine would probably be sold at a considerable profit in the English market, say it would fetch £2,000; and, after deducting all the charges of every description on the cargoes both ways, the difference would be the merchant's profit. In this case it is quite clear that no bullion would pass between the countries, and the merchant would apparently import more than he exported, and it is also clear that his profits are exactly estimated by the excess of the value of the inward cargo above that of the outward one, after deducting all the charges both ways, and just as this difference is the greater so his gain is greater. In this case, as no bullion would pass from either country to the other, there would be no question of exchanges.

It is clear that the London merchant's agent at Bordeaux would be governed by several considerations as to whether he would remit specie or wine to London, and he would be chiefly governed by the state of the wine markets, both at Bordeaux and London. For, supposing the goods to be sold at a good profit at Bordeaux, he must next consider the price of the wine at Bordeaux, and also what it might be expected to fetch in London. If some great disaster had happened to the vines so that there was a failure of the crops, the price of wine at Bordeaux might rule excessively high, but at the same time there might be a large stock of wine in London, and the price might not be unusually high; so that if he were to purchase wine at Bordeaux, and send it to London, it might be a loss. In such a case as this, if there were no other native product to send, he would find it most advantageous to remit specie, whatever he could sell the goods for, and then the exchange would be in favour of London; but, before the London merchant could reckon his profits, he would have to deduct the freight, insurance, &c., on the specie.

Whether the transaction was profitable or not to the London merchant would entirely depend on the amount of specie he received after deducting all charges; and if he had purchased the goods he sent out from England cheap, and there was a

scarcity of them at Bordeaux, he might realize high prices there, which might leave him a good profit. It would be very improbable that he could realize so much profit on that single operation, as in the double one of exporting goods and importing wine. So that the import of the specie would be less profitable to him, and the nation at large, than the import of the wine.

The reasons which caused the export of specie from Bordeaux, and the import of it into England, in this case, are very plain, they were the scarcity and dearness of the native products at Bordeaux, and the abundant supply of them already in the London market. Hence, we gather that the scarcity and dearness of native products is an infallible cause of the export of specie from a country; on the contrary, an already existing abundant supply of foreign products of all sorts, is a certain cause of its import into a country. On the contrary, when native products are cheap and abundant, it will cause an importation of bullion, and when foreign products are scarce and dear, it will cause an export of bullion.

We have before observed that the exchange being in favor of a country means nothing more than that bullion has to be remitted to it. In the case above described, the exchange at Bordeaux would be in favor of London; but this simple case is as good as a thousand to shew the extreme and dangerous fallacy of drawing any conclusion as to the advantage of the trade to England, from the simple fact of the exchange being favourable to her, and an inflow of bullion taking place.

The example given above is of the simplest description, and a merchant of eminence, who had correspondents in several different parts of the world, might easily multiply these operations, so as to visit many markets before the returns of his cargo were brought home. Thus, instead of having the wine sent home from Bordeaux, his correspondent might find it more profitable to send it to Buenos Ayres, and dispose of it there. The chief native product of that place is hides, and we may suppose that his correspondent there might invest the proceeds of the cargo of wine in hides, which there might be a favourable opportunity of selling in the West Indies. When the cargo arrived in the West Indies, instead of remitting the proceeds directly home, it might very well happen that, owing to a scarcity of corn at home, it might be very high there, and cheap in Canada, so he would invest the proceeds of the hides in sugar, and despatch that to Canada, where the merchant's correspondent there would dispose of it, and purchase corn, which he would send to England.

In the case just described, we observe that there are five distinct operations, and, as we may suppose that there is a profit upon each of them, by the time the returns for the goods, which

originally cost £1,000, are brought to England, it may very well be, that the corn, which forms the ultimate payment of them, may be several times as valuable as the original cargo; and, as we have supposed the charges on each operation to be deducted before investing the proceeds in other articles, it is clear that the merchant's profit upon the whole is exactly the difference in value in England between the articles last purchased and sent home and the original cargo; after deducting all the expenses of sending home the last cargo, and we also observe that no specie has been sent from one country to the other in the whole course of the extended operation.

This example is sufficient to demonstrate the utter fallacy of the old idea, which is even yet not extinguished, of the balance of trade. Nothing can be more clear, that unless the value of the cargo which comes into England, in payment of the cargo that was sent out, is sufficient, not only to defray the cost of the original cargo, as well as all charges upon it and the return cargo, and leave a profit besides, the commerce could not be carried on. No English merchant could export goods unless he receives in return others of much greater value; and the obvious consideration, that the more he gets for what he sends out, the more profitable it is to himself and the nation, is sufficient by itself to explode the old fallacy of the balance of trade. One obvious source of error is, that the value of the exports from this country is estimated at the time of their leaving the country, and before the charges for freight, &c., are incurred, which must necessarily raise their selling price in the foreign market, if they are not sold at a loss, and their value in that market is expected to be considerably higher than that. On the other hand, the value of the imports is estimated, not according to their value when they left the foreign country, but what it is upon their arrival here, including all their charges upon them.

If we suppose that Bordeaux had but one native product—wine, the chances of finding the markets, both at Bordeaux and London, in a favourable state for importing produce instead of specie, would be limited to that single article. But if it had other products, such as olive oil, the chances would be increased of finding articles to suit the market, and the chances would evidently be multiplied according to the number and variety of its products.

Let us take another example, and let New York be the starting place. The staple products of America are breadstuffs and provisions. A merchant of New York sends a cargo of corn to Liverpool, and his correspondent there will endeavour to invest the proceeds of that in British goods, if he finds the state of the markets in England and New York will make such an operation profitable. Suppose that the price of corn is very high here, and British goods are also very high here, and very

low in America, it is clear that nothing but specie will be sent. In cases where a great and unexpected dearth of corn occurs in England, and its price rises enormously high, the infallible result is to cause a great drain of specie for the time being, because our necessity for food is much more pressing and immediate than their necessity or capability of consuming our cotton or woollen goods. And the only way to arrest such a drain is to effect such a reduction in the prices of British goods as shall make it more profitable to export goods than specie.

In the cases we have been hitherto considering, we have described the operations as if merchants were left perfectly free to carry their goods whither they pleased, and were not met and obstructed by artificial obstacles purposely devised for interfering with their business, by the laws of different nations. But there are few nations, and our own among the rest, which have not habitually discouraged the importation of foreign goods, and imposed heavy duties for the specific purpose of excluding them, as they conceived the extraordinary idea that all foreign goods brought into the country were so much loss to it. Thus, the statute of William III. (1688, c. 24) says:—"It hath been found by long experience that the importing of French commodities of all sorts" (enumerating them) "hath much exhausted the treasure of this nation, lessened the value of the native commodities and manufactures thereof, and greatly *impoverished* the English artificers and handicrafts, and caused great *detriment* to the kingdom in general." If we consider the effect of these laws in one place, it will equally apply to every other; thus, in the first instance, suppose that there are very high protecting duties at Bordeaux against British goods, as the consumer must ultimately pay all the expenses and charges on the goods, it will have the effect of greatly raising the market price there, and diminishing the number of persons who can afford to buy them, and hence, as the market is so limited, a smaller quantity of goods will overstock it than if it were much extended. This will cause a much less quantity of goods to be sent from London, and it will cause a much larger proportion of specie to be remitted to pay for the productions of Bordeaux. This example shews that the inevitable effect of high protecting duties between country and country is to cause a much more frequent transmission of bullion from one to the other than would be the case in an unfettered state of commerce; unless, indeed, the smuggler steps in, who is the corrector provided by nature against this commercial insanity. The effect, then, of prohibitive duties is to cause an inflow of bullion; but we must carefully guard against supposing that this inflow is a favourable sign, as it is certainly the least profitable import a merchant can receive for his goods; and there is this very marked difference between an inflow of bullion under the Protectionist system and

under a Free Trade system, that the former is accompanied with a great dearth of foreign commodities, but the latter is an infallible sign of a great abundance of them, as bullion is never imported when men are allowed to follow their own interests, until our markets are already so overstocked that every other article has ceased to be profitable.

The foregoing cases comprehend the different varieties of commercial transactions between this and any other country, and we gather from them the following results respecting the inflow or outflow of bullion:—

I. The cause of bullion being imported is either when the price of goods is so *low* in England, and so *high* in the foreign market, as to tempt foreigners to send here to buy goods, or the price of goods is so high in the foreign market, and so low in England, that nothing but specie can be sent in payment of goods exported from England.

II. The cause of bullion being exported from England is that there is some great and pressing demand for some article in this country, and other commodities are so scarce and dear that they cannot be exported with a profit, or that the article is required in such great quantities that the foreigner cannot consume our goods which we should prefer to send in payment fast enough, and so specie must be sent, and the greater the difference in price the greater will be the drain of bullion; or that other markets are already overstocked with our productions, which are depressed below their usual market value there. This is what is meant by overtrading; and, from this circumstance, we see that overtrading is a sure precursor of a drain of bullion from the country. When there has been a great failure in the crops in this country, so as to cause a famine price, the demand for corn is so immediate and urgent that it necessarily causes a great drain of specie, and it is then of the greatest possible consequence that the prices of other commodities should be as low as possible, to enable them to be sent in payment of the necessary supplies of food, and prevent such a drain of bullion as may disturb the whole monetary system of the country.

Overtrading, and a failure of the cereal crops of this country, are each of them sure causes of a drain of bullion. The most disastrous event for the commerce of this country is when both these circumstances happen concurrently. It is like a spring tide of disaster. The most terribly disastrous commercial crisis this country ever experienced was preceded by some years of overtrading, followed by successive failures in the staple support of the people of England and Ireland. These two adverse events together produced the calamities of 1847. We shall see that the intended effect of the Bank Act of 1844 is to provide a remedy for such a state of things, by causing such a reduction in the price of home commodities, in the event of a drain of

specie taking place, as to render it more profitable to export them than bullion, and so stop the drain. Whether the Act is effective for this purpose is another question, which it is not the proper place to discuss here.

There are some countries from which we draw articles of great necessity, but to which, from different circumstances, we do not expect to remit goods in payment. Russia was the great source of our supply of hemp, flax, and flax, and we used to import these products to the value of £12,000,000 yearly, but, owing to the prohibitive character of her tariff, we were unable to send our own products in payment of these goods to anything like a similar amount in value. To such a country the difference must be remitted in cash, to the mutual loss of both parties, and, unless there were other means of equalizing the exchanges with different countries, the exchange with Russia would always be unfavourable to England. The chief export trade from Ireland to England was in articles of food—pigs, cattle, oats, butter. Great quantities of these came from Ireland, but the inhabitants of that country were much too poor to be able to consume an equivalent amount of English goods; in consequence of which the difference had to be remitted in specie, and so the exchanges between England and Ireland were almost uniformly favourable to Ireland. Now, if Ireland had been sufficiently wealthy to have consumed English goods instead of specie, it is evident that it would have been far more advantageous for both countries; for English industry would have been promoted, and Ireland would have gained a more valuable import. These two examples offer a further illustration of what we said before, that the frequent transmission of bullion between countries which do not produce it, is a system of a less profitable trade than it would be if goods were transmitted.

In the operation first described above, we have supposed it to originate with the English merchant who remits his goods to his correspondent abroad, and who reaps the profits, and the proceeds must be remitted to him after deducting the freight, charges, and commission, of the agent there. But it is also probable that there will be native merchants at Bordeaux, who will send wine to England on their own account, to their correspondents here, and then the whole transaction will be reversed. The English correspondent will endeavour to purchase English goods as low as he can, and if he can get them low enough to realise a profit in the Bordeaux market, he will send goods out; but if the English goods are too high for that purpose, he must send specie. It is also evident that, even if the goods be at no unusual height in England, still, if the market at Bordeaux be already overstocked with them, or, as it is called, "glutted," it would be useless to send more goods, to force the price down

still further, and the consequence must be that nothing but specie will go.

From this we see, that if specie be coming in from a country, it is a proof that we have already got so many of their goods, that it will not pay to import any more, and if specie be going out to a country, it shows that we have already sent out so many of our goods to that market that it is already overstocked. The different barbarous laws which every country has enacted under the erroneous appellation of protection, by aggravating the price, limit the markets in every country for the products of other countries, and cause much fewer commodities to pass between nations than otherwise would, and cause the markets of any country to be much sooner overstocked than they would otherwise be. By preventing this interchange of commodities which every nation would naturally prefer, it necessitates payments in specie to a much larger extent than would be the case if commerce were free, to the common impoverishment of all parties.

The foregoing considerations shew that it is possible to carry on any amount of foreign trade without the necessity of any remittances being made in specie. In the instance above taken, the English merchant purchases goods and sends them to his correspondent abroad, who realizes them and invests the proceeds in that market, and sends them to England, and the English merchant disposes of them in England, and gains the profits there, and no specie is sent from one country to the other. Similarly the foreign merchant sends his goods to his correspondent in England, who disposes of them there, and invests the proceeds of them in England in English commodities, and sends them to his foreign correspondent, who gains his profits, either by selling them in his own country, or by sending them to some other market where he may make a higher return, and, as in the former case, no specie passes between the two. Nor is the result in any way different, if the trade be conducted by the more circuitous method of three or more transactions. Hence, in a healthy state of the markets of different countries, scarcely any specie will pass between them, and the very fact of there being a necessity for making frequent and large remittances of specie from one country to another, is in itself a proof of there being something irregular and unhealthy in the state of commerce in general, and in the state of the markets of one country or the other, either that they are overstocked or understocked, or that there is some legislative interference with the natural course of trade between nation and nation. Nothing can be more certain than that bullion is the least profitable of any article of commerce, except from bullion-producing countries, and that when merchants have recourse to it, it is because some disturbance has taken place in the profitable relations between supply and demand of other commodities.

Now, supposing commerce to be in that desirable and healthy state in which no specie passes between non-bullion-producing countries, who could tell how what is called the balance of trade is inclined? Who can tell what the balance of trade is? Each country would shew a favourable balance, taking the values of the exports and the imports at their market prices in each country. Each country would shew that their imports exceeded their exports in value, that is, each would shew that they had gained by their commerce, for the very simple reason that the value of the article they received would be greater in their own market than the value of the one they gave; and, unless it was so, it is manifest that trade could not be carried on, because all the expenses and profits of trade are provided for, by the difference in value between what they give and what they receive. Hence, unless both parties gain by the transaction, commerce cannot be carried on. But this shews that the expression of the "balance of trade" is a gigantic delusion, and it is greatly to be wished that it should be for ever exploded and laid aside, as the fountain and origin of incalculable mischief to the world, in the suicidal efforts every nation has made to secure to itself that great chimera—a favourable balance.

The mistake of unreflecting writers, who think that the price of foreign goods sold in this country goes into the pocket of the foreigner, consists in this, that the probability is, that the English merchant who imports these goods has already purchased them with English goods, so that their money price goes into the pocket of the English merchant, and not that of the foreign one, and is, probably, re-invested in English goods, if there is a prospect of a favourable opening for them.

The fundamental fallacy about the balance of trade, which seems to have taken possession of the Legislature, was, that the interests of the State were different and opposite to the interests of individuals. They seem to have entertained the idea that every merchant had entered into a conspiracy to ruin the country, which he tried to carry into effect by becoming as prosperous himself as he could. It seems most unaccountable how long they missed the obvious truism, that the prosperity of the State was made up of the prosperity of the individuals composing it, and that every one was far keener in discerning what conduced to his own prosperity than the State could be, and that if private merchants found it to be to their individual advantage to import commodities rather than bullion, it could not be beneficial to the State to force trade into a contrary direction.

When our ships first traded with the South Sea Islanders, they took out with them axes, beads, and other trifles, which had very little value in this country, and bartered them for all sorts of curiosities, shells, &c., which were very valuable in England. A pair of fine shells from the South Seas in many

cases is worth ten guineas in England, which perhaps an English sailor obtained in exchange for an axe worth 2s. 6d. The English sailors thought the natives very simple to give away so many valuable curiosities for such common things. We cannot doubt that the natives had exactly the same opinion of the English sailors; they thought them great simpletons to give away such valuable things as axes, beads, &c., for so common things as a few shells. Each party, however, exchanged what was common and cheap in his own country for what was scarce and valuable. The axes were infinitely more valuable in Feejee than the shells: the shells were many times more valuable in London than the axes. Thus, an English sailor, by giving perhaps 2s. 6d., gained in Exchange what was worth ten guineas and the difference was his profit. Now, this was the genuine spirit of commerce. The coloured beads were just as valuable to the poor untutored savages, as diamonds to civilized Europeans. The commerce between all nations is exactly similar in principle to that between the sailors and the savages. But, according to the old doctrine of the balance of trade, this difference between the value of the axe and the shells in England, ought to have been paid in bullion. This simple case is quite sufficient to explode the whole fallacy.

Notwithstanding the prevalent idea that foreign trade was profitable just in proportion to the money it brought into the kingdom, and that this was indicated by the so-called balance of trade, there were a few enlightened persons who saw through the fallacy, and combated it. In reference to a certain "balance" which occurred in the trade between Holland and England, and which was a subject of much gratulation, Craik well observes that it would be as irrational to suppose that the English must necessarily be the chief gainers by this trade, as it would be to maintain that the productive labourer must always be a greater gainer on the article he produces than the capitalist who employs him. That the Dutch were in the position of the capitalist, and the English of the labourer, and that while the Dutch had the goods the English had the money; just as, while the master has the goods the workman has his wages. But that the excess of profit, or real advantage, should be with the labourer rather than with the capitalist, may fairly be presumed to be as unusual, and as little likely in the nature of things, in the case of nations as of individuals.

An attentive consideration of these various methods of trading will shew what a complete phantasy the old, and still too common, idea of the "balance of trade" is; and, as nothing more conduces to error and confusion in any science than a nomenclature and technical phrases which are founded upon misconceptions of the principles of that science, so nothing has exercised a more malignant influence upon legislation, and

popular ideas generally, than this phrase; and it would be very desirable if some means could be taken to discontinue its use altogether. But, as it does occur in the course of trade that transactions between nations have to be settled in specie, we must now consider the operations of the foreign exchanges.

The course of the foreign exchanges, then, entirely depends upon the fact of persons in one country having to make payments to persons in another country, from whatever causes these payments have to be made. And there are but two causes which influence their rates: first, the depreciation of one or both of the currencies which have to be exchanged; secondly, the relative amounts of money that have to be remitted from one country to the other.

On the Rate of Discount as influencing the Exchanges.

10. We have now to treat of a cause of the movement of bullion which has acquired an importance in modern times, far exceeding what it ever did before; in fact, it is now probably more important than any other, viz., a difference in the rate of interest or discount between two countries. In former times, when the communication between different places was slow and expensive, before the days of railroads and steamers, a considerable difference might exist in the rates of interest in two places, without causing a movement of bullion from one place to the other. But that is not possible now. The communication between places is so rapid now that directly the difference between the rates of interest in any two places is more than sufficient to pay for the expense of sending the bullion, an immediate flow of bullion commences from one place to the other. And this is in exact accordance with the usual mercantile principle that operates in every other case, that if the difference of price of the same article in any two markets is more than sufficient to repay the cost of sending it from one to the other, it will be sent; and this movement will continue as long as the difference in price continues. Now, if the rate of discount in London is 3 per cent. and that in Paris is 6 per cent., the simple meaning of that is that gold may be bought for 3 per cent. in London, and sold at 6 per cent. in Paris. But the expense of sending it from one to the other does not exceed $\frac{1}{2}$ per cent., consequently it leaves $2\frac{1}{4}$ or $2\frac{1}{2}$ per cent. profit on the operation. The natural consequence immediately follows, gold flies from London to Paris, and the drain will not cease until the rates of discount are brought within a certain degree of equality. It used to be the common delusion of mercantile men that gold was only sent to pay a balance arising from the sale of goods, and that, therefore, it must cease of itself whenever these payments were made. But this is a profound delusion. When the rates of discount differ so much as is supposed above between

London and Paris, persons in London fabricate bills upon their correspondents in Paris for the express purpose of selling them in London for cash, which they then remit to Paris, and which they can sell again for 6 per cent. And it is quite evident that this drain will not cease so long as the difference in the rates of discount is maintained. Moreover, merchants in Paris immediately send over their bills to be discounted in London, and, of course, have the cash remitted them. Now, the only way of arresting such a drain is to equalize the rates of discount of the two places. These simple facts are a perfectly conclusive answer to those writers, and they are many, who complain of the variations of the rate of discount by the Bank of England, and suppose that it is possible to maintain a uniform rate. Consequently, at the present day it is the imperative duty of the Bank of England to keep a steady watch upon the rates of discount of neighbouring countries, and to follow these variations so as to prevent its being profitable to export bullion from this country.

On Foreign Loans, Securities, and Remittances, as affecting the Exchanges.

11. Besides the state of national indebtedness, arising out of commercial operations, there are other causes which seriously affect the Exchanges. In former times, England being more abundant in money and material resources than men, used to subsidize foreign powers to a great extent; and the method of transmitting such a loan to the best advantage to the remitting country, is an operation of considerable nicety and delicacy. If the sums to be remitted were very large, the expense and danger of the transit of the coin would have been very considerable in former times; but since the introduction of railroads, and greater internal security, such considerations would have little influence at the present day. But an actual and sudden withdrawal of a very large amount of bullion from a commercial country would cause the most disastrous consequences when so many engagements had to be met at a fixed time. When such necessities, therefore, did arise during the last war, the operation was effected by means of bills of exchange, and the object to be obtained was, to prevent a sudden vacuum being caused in the currency of one country; but, by operating on all the different centres of payment of Europe, to cause a gradual and equable flow from all of them to the place of payment. We may give, as an instance, the following, as narrated by Mr. Boyd, who had the management of the operation. In the year 1794 the English Government agreed to make a considerable loan to the Emperor of Germany, and the money was required to be sent from London to Vienna, causing as little disturbance as possible in the English money market:—

“The remittance of so large a sum as £4,600,000, I considered

as a matter of infinite difficulty and delicacy, so as to prevent its producing any remarkable effects upon the course of Exchange. It was necessary to vary the modes of remitting, and to make use of the various means for that purpose presented by all the different exchanges of Europe. It was not necessary to remit bills upon Hamburg only, because it frequently happened that it answered better to remit to Hamburg upon other places, such as Madrid, Cadiz, Leghorn, Lisbon, Genoa, &c., than to remit direct upon Hamburg; and, having constantly orders from Vienna with regard to the rates of the different remittances to be made, our attention was directed to the accomplishment of these orders, on the best possible terms. In fine, it was necessary to take bullion, bills direct upon Hamburg, and bills upon other places, all into our means of remittance, and to make the most of these modes of remittance without giving the decided preference to that mode which was the most favourable, because any one mode invariably adhered to would soon have exhausted and destroyed that mode; whereas, by turning occasionally to all the modes, and not sticking too long to any one particular mode, we had the good fortune to make upon the whole very favourable remittances."

We may mention another instance of a similar operation quoted by Mr. McCulloch:—

"In 1804, Spain was bound to pay to France a large subsidy, and, in order to do this, three distinct methods presented themselves. First, to send dollars to Paris by land; second, to remit bills of exchange directly to Paris; thirdly, to authorize Paris to draw directly on Spain. The first of these methods was tried, but was found too slow and expensive; and the second and third plans were considered likely to turn the exchange against Spain. The following method, by the indirect, or circular, exchange was therefore adopted:—A merchant, or *banquier*, at Paris, was appointed to manage the operation, which he thus conducted. He chose London, Amsterdam, Hamburg, Cadiz, Madrid, and Paris, as the principal hinges on which the operation was to turn; and he engaged correspondents in each of these cities to support the circulation. Madrid and Cadiz were the places in Spain from whence remittances were to be made, and dollars were, of course, to be sent where they bore the highest price, for which bills were to be procured on Paris, or any other place that might be deemed more advantageous. The principle being thus established, it only remained to regulate the extent of the operation, so as not to issue too much paper on Spain, and to give the circulation as much support as possible from real business. With this view, London was chosen as a place to which the operation might be chiefly directed, as the price of dollars was then high in England, a circumstance which rendered the proportional exchange advantageous to Spain.

“The business commenced at Paris, where the negotiation of drafts issued on Hamburg and Amsterdam, served to answer the immediate demands of the State; and orders were transmitted to these places, to draw for the reimbursements on London, Madrid, or Cadiz, according as the course of exchange was most favourable. The proceedings were all conducted with judgment, and attended with complete success.”

The preceding are examples of loans raised in this country with the consent of the Government, and, consequently, every care was taken to have them transmitted in such a way as to produce as little disturbance of the exchanges as possible. But it has become very common for foreign Governments to raise loans in England, without any sanction of the Government at all. During the late unhappy war in America, both the belligerent Governments sent over enormous quantities of their securities or stock, to be disposed of for specie in the European markets for what they would fetch, and the proceeds were remitted either in cash or bills. So, also, vast numbers of foreign companies of all sorts seek to raise capital in England.

There is, lastly, to be considered, the sums required by residents abroad for their expenditure. The drafts of the great English and Russian families, on their bankers, at home, affect the exchanges exactly in the same manner as any other drafts.

On Monetary and Political Convulsions as influencing the Exchanges.

12. As an immediate consequence of the preceding principles, it follows that a political or monetary convulsion in any country will immediately turn the foreign exchanges in favour of that country, if such an event is not prevented by the issue of an inconvertible paper currency. The reason is plain, any political or monetary convulsion is attended by a great destruction of *credit*. Now, that credit, while it existed, performed the functions of money, but as soon as it is destroyed, there is an intense demand for money to fill the void. Money rises enormously in value. Multitudes of persons are obliged to sell their goods at a sacrifice. The consequence is that money, having risen greatly in value, both with respect to goods and debts, an immense quantity will flow in from neighbouring countries. Thus, in 1801-2 there was a great commercial crisis at Hamburg. The rate of discount rose to 15 per cent. That immediately drained the bullion from the Bank of England. In 1825 there was a great commercial crisis in England. For a considerable period the bank, by making extravagant issues at a low rate of discount, had turned the foreign exchanges against the country. But, no sooner did the crisis occur in December, than the foreign exchanges immediately turned in favor of it. Exactly the same thing happened in 1847. No sooner had the crisis in that year

fairly set in, than the exchanges turned in favor of the country. In the French revolution in 1793, and subsequent years, immense quantities of inconvertible paper were issued, that kept all the French exchanges in a very depressed state. In 1796 this paper currency was annihilated, and the exchanges immediately turned in favor of France. The same thing was observed in 1848. Things were to be had so cheap then that multitudes of persons went over to buy.

On the Means of Correcting an adverse Exchange.

13. The preceding paragraphs shew upon what complicated causes these great movements of bullion depend, which produce such important consequences. There are three great Economic Quantities—PRODUCTS—BULLION—and DEBTS—all seeking to be exchanged, all flowing from where they are cheaper to where they are dearer.

But all this vast superstructure of credit—this mighty mass of exchangeable property—is based upon GOLD BULLION. Different methods of doing business require different quantities of bullion; but, however perfect and refined the system may be, we must come at last to a basis of bullion, as its moderator and regulator. If, therefore, the bullion be suffered to ebb away too rapidly the whole superstructure is endangered, and then ensues one of those dreadful calamities—a monetary crisis.

We have endeavoured to explain the different causes which produce an adverse exchange, so that if one takes place the proper corrective may be applied. If it be caused by a depreciated currency, there is no cure but a restoration of the currency to its proper state.

When, however, it arises from a balance of indebtedness from commercial transactions, there are but two methods of correcting it—an export of produce, and A RISE IN THE RATE OF DISCOUNT.

It used to be a favorite doctrine that an adverse exchange was in itself an inducement to export, on account of the premium at which bills could be sold. What truth there was in this doctrine can only be known to those actually engaged in such operations. But a very much more certain means of producing an export of goods is a *lowering of their price*.

This was one of the fundamental objects of the framers of the Bank Act of 1844. They truly observed that the prices of goods had often been unduly inflated by the excessive creation of credit, while gold was rapidly flowing out of the country. Thus, when prices were kept too high here, nothing but gold would go. One object of that Act was, therefore, by causing a gradual and compulsory contraction of credit as bullion ebbed away, to lower the prices of goods and encourage an export of them.

The reasoning of the framers of the Act was undoubtedly

correct in that respect. But the only thing is, whether the same object might not be attained another way. This is not the place to discuss fully the policy of that Act, because there are several other conflicting theories involved in it, which we cannot fully discuss until we come to the consideration of a commercial crisis.

It is sufficient to say here, that all the objects of that Act are obtained by paying proper attention to raise the rate of discount rapidly as bullion flows out. If the Directors of the Bank had understood and acted upon that principle, there never would have been any necessity for the Act. It is true, we cannot blame them too much, as before 1833 they were prohibited by law from raising it above 5 per cent., a rate wholly inadequate to check a great outflow; and for many years there was a great prejudice against doing so.

We have observed that a difference in the rate of discount between any two countries more than sufficient to pay for the transmission of bullion, causes a flow of bullion from one to the other. But it must be remembered that, as all the cost of the transmission both ways falls upon the operator, the difference will be more considerable than might appear at first sight. And, if they be three months' bills, of course, the profit reaped will be only one-fourth of the apparent difference. Thus, Mr. Goschen says, there must be a difference of 2 per cent. between London and Paris before the operation of sending gold over from France for the sake only of the higher interest will pay. And between other continental cities, of course, the difference may be much greater.

But whatever the difference may be, the *method* is absolutely certain. Directly the rates of discount rises here, people cease to export bullion from here, and the continental bankers and brokers increase their demand for English bills. And as the rate rises the demand will increase, until at last the price reaches the specie point, and gold begins to flow in, and as the rate rises more, more powerful will be the attraction, until at last the necessary equilibrium is restored between bullion and credit.

The state of indebtedness, however, may be so great as to deepen an adverse exchange into a monetary crisis, but what may become advisable to be done in such an emergency, we must defer discussing until a future chapter, when the policy of the Bank Act of 1844 is examined.

CHAPTER VI.

ON THE RISE AND PROGRESS
OF BANKING.



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BANKING PROBABLY INVENTED BY THE ROMANS—GREEK BANKERS—CHINESE INVENTED BANK NOTES—BANK OF VENICE—BANK OF ST. GEORGE—BANK OF STOCKHOLM—BANK OF AMSTERDAM—HISTORY OF BANKING IN SCOTLAND.

1. In the preceding chapters we have endeavoured to investigate the fundamental principles of the Theory of Credit and Banking, and to set forth its mechanism as it actually exists. We must now trace the history of this most important invention. On many points of its practical application there have been, and still continue to be, several conflicting theories. The best way to form a judgment of the correctness and merits of these various theories is to give an authentic account of the history of Banking in various countries, which we now proceed to do.

AT ROME.

2. The business which is technically called BANKING seems, as far as we can ascertain, to have been invented by the Romans. It is true that there were abundance of money dealers and money lenders at Athens, and other places, but their business seems, as far as we can discover, to have been more analogous to that of those persons we call *money scriveners*, and *bill discounters*, than of those whom we call bankers. For we have seen that the business of banking technically consists in creating credits in favor of the persons who deposit money with the banker, and in paying debts by transferring sums from one account to another, as well as by making all advances in the first instance by creating a credit. This mode of doing business essentially distinguishes a banker from a *money scrivener*, or *bill discounter*, who actually advances the money itself. This seems to have been the business of the Athenian *τραπέζίται*, and, if so, they were technically bill discounters, and not bankers.

The Romans, on the contrary, practised the business, which is technically called banking, exactly as we do, nor do we know when it was invented. The earliest notice we have of these banks, or *argentariæ*, is in Livy ix., 40., B.C. 308, where they are spoken of as being already placed in the forum, where they always continued. But he gives no account of the method in which the bankers transacted their business. The comedies of Plautus are full of allusions to bankers and their business. He

calls them *trapezitæ*, *argentarii*, and *danistæ*. We have Latin words corresponding to the method of keeping banking books. Thus, *scribere* was to give credit in the books, *rescribere*, or *prescribere*, was to transfer a sum from one account to another by means of a cheque, which was called *perscriptio*, or *attributio*. Thus, in the *Asinaria* ii., 4, 34, Leonida says:—

“Abducit domum ultro, et scribit numos.”

“Of his own accord he brings him home, and places the money to his account.” So *acceptum ferre* was to credit a customer's account with money received, *expensum ferre* to debit it for money paid. Thus, in the *Mostellaria* i., 3, 146:—

“Ratio accepti et expensi inter nos convenit.”

“The accounts between us balance.” Plautus only uses the word *mensa* to mean a bank, in two places. *Curculio* iv., 3, 4:—

“Velut decem minas dum hic solvit omnis mensas transit.”

“As before this fellow paid me the ten minae, he had to go to every banker's;” and in the *Pseudolus* i., 3, 62:—

“Postquam isti a mensa surgunt.”

“After these bankers broke.” But he never uses *mensarius* for a banker. These persons are mentioned numberless times in his plays. So, also in Terence. *Phormio* v., 7, 29:—

“Sed transi, sodes, ad forum, atque illud mihi
Argentum rursum jube rescribi, Phormio,

PHORM. Quodne ego perscripsi porro illis, quibus debui?”

“But, Phormio, be good enough to go over to the forum, and order that money to be put to my account.

“PHORM. What! that for which I have already given cheques to my creditors?”

So Cicero (*Epist. ad Atticum* xvi., 2): “Qui de cccc. His ce presentia solverimus, reliqua rescribamus.” “Of the remaining four hundred sestertia, I have paid two hundred in cash, and I shall send a cheque for the rest.” So *Orat. pro Caccinâ* vi. “Se autem habere argentarii tabulas, in quibus sibi expensa pecunia lata est, acceptaque relata.” “But he himself has the banker's books, in which are the accounts of the money paid and received.”

Although we have seen above that Plautus uses *mensa* as the counting-house of a private banker, they were never called *mensarii*. The latter were public officers of high rank, who were appointed by the State only in times of great public distress, when the plebeians were weighed down with the accumulation of compound interest, to effect a compromise between debtors and creditors, and to advance money from the treasury to citizens in distress, on the security of goods, or land, or cattle. The first appointment was made 348 B.C. (Livy vii., 21.) They were then five in number. On other occasions (Livy

XXIII., 21; XXVI., 36) they were only three in number. They seem to have been instituted for very much the same purpose as the *monti di pietà*, in the middle ages in Italy, and which are still very common on the Continent under the name of *monts-de-piété*.

Although there is no evidence to prove that the ancients used bills of exchange in commerce, as many writers have asserted, in Cicero we find several passages which speak of remitting drafts. Thus, *Epist. ad famil. to Cavinus Salustius*:—"Se ait curasse, ut eum questu populi pecunia permutaretur." "He says that he has taken care that a draft for the money should be sent (to Rome) along with the people's share of the profit." So when his son is going to Athens, he writes to Atticus, XII., 24:—"Sed quero, quod illi opus erit Athenis, permutarine possit, an ipsi ferendum sit." "But I wish to know whether the money which he will require at Athens can be sent by a draft, or whether he must carry it with him." So also, xv., 15:—"Quare velim cures, ut permutetur Athenas, quod sit in annum sump-tum ei." "Wherefore I wish you to take care to send him a draft at Athens for his yearly expenses." So also, v., 15:—"Ut vereor, ne illud quod tecum permutavi, versurâ mihi solvendum sit." "So that I fear that I must borrow money to pay the draft you changed for me." So also: "Scripseras ut II. S. xii. permutaret." "You had written that he was to send me a draft, or bill, for 12 sestertia."

IN GREECE.

3. We are not very well acquainted with the customs of the Athenian bankers, but, as far as we can understand, they seem more to have corresponded to what we call "Bill Discounters" than "Bankers." They not only made a profit by exchanging foreign money, but also received deposits at interest. The father of Demosthenes kept part of his capital at a banker's. Though they were generally of low origin, such as freedmen, aliens, or persons who had been admitted as citizens, they gradually rose into great credit, which, in the case of the principal ones, extended throughout Greece. They obtained so much confidence that business was transacted with them without witnesses: money and contracts of debt were deposited with them, and agreements were concluded and cancelled in their presence. They obtained 36 per cent. for loans.

The Athenian bankers were the first that we are aware of who invented the method of *discount*, that is, of retaining the profits at the time of the advance, as we learn from Plutarch, was their practice. In his violent tirade against money-lending, he is particularly severe against the invention of discounting:—"It is said that hares bring forth and nourish their young at the same time that they conceive again, but the debts of these scoundrels

and savages bring forth *before* they conceive! For they give and immediately demand back, and take away their money at the time they place it out, and they place out at interest what they receive as interest. The Messenians have a proverb—

“There is a Pylos before Pylos, and yet another Pylos still.”

But it may be said to the usurers:—

“There is a profit before profit, and yet another profit still, and then, forsooth, they laugh at philosophers, who say that nothing can come out of nothing!”

So, what between Plutarch, who raves against discount, and Mr. Mill, who declares it to be robbery to create credit, our poor modern bankers have a hard time of it.

It is often said that the Temples in Greece, especially those of Delos and Delphi, acted as great Banks of Deposit. It is true that they received sums of money for safe custody, but we do not think that there is any evidence to shew that either they or the Greek money dealers, settled claims by transferring credit from one account to another, which is the essential feature of “Banking.”

IN CHINA.

4. We have seen that the Romans first invented the business of “banking,” namely, making instruments of credit perform the functions of money. But they did not invent bank notes. The invention of bank notes is due to the Chinese. About the year 807, A.D., there was a great scarcity in the country. The Emperor ordered all the merchants and rich persons to bring their money into the public treasury, and, in exchange for it, he gave them notes, called *flying money*. In three years, however, this money was suspended in the capital, and only current in the provinces. In 960, A.D., another Emperor revived this practice. Merchants were allowed to deposit their cash in the public treasury, and received notes in return. The convenience of this was so great, that the custom quickly spread, and in 997, A.D., there was paper in circulation to the amount of 1,700,000 ounces of silver, and in 1021 it had increased to 2,830,000 ounces. At this period a company of 16 of the richest merchants were allowed to issue notes, payable in three years. But, at that time the company was bankrupt, which gave rise to much distress and litigation. The Emperor abolished the notes of this company, and forbade any other joint stock banks to be formed. Henceforth the power of issuing notes was in the hands of the Government. They were of the value of an ounce of silver. In 1032 there were notes of the value of 5,256,340 ounces in circulation. Subsequently, banks of this nature were set up in every province, and the notes issued in one province had no currency in any other. These Chinese notes were the first on record. They were notes issued in exchange for money, and convertible into money.

The transition, however, from paper credit to paper money was too easy and convenient to be long overlooked, and for many centuries China was afflicted with all the evils of an inconvertible paper money. The details are too long to be inserted here, but they will be found in our *Dictionary*, Art. *Currency*. In 1367, a Chinese writer, groaning over the miseries caused by paper money, recalled the happy times when paper was only issued in exchange for specie. "When the notes were paid in the money came out: when the bills came out the money went in." This is exactly the CURRENCY PRINCIPLE, of which we have heard so much of recent years in England. At last in 1644, the miseries produced by paper money were so intolerable, that the Tartar dynasty ordered paper currency to be for ever abolished in China, and issued nothing but specie. How long this continued we cannot say, but it is quite certain that there are abundance of Banks in China issuing notes at the present day.

Historical sketch of the Rise and Progress of Banking
IN ITALY.

5. A crowd of writers, including among them many of the greatest names in literature, have assigned the date of 1171, or even 1153, to the Bank of Venice, and that of 1407, to the Bank of St. George, at Genoa. But we shall shew that these dates are both extremely erroneous. The *Bank* of Venice dates only from 1587, and the *Bank* of St. George only from 1675. To say that they were founded in the years 1171 and 1407 respectively, is exactly as erroneous as it would be to say that the Dukedom of Wellington was created in the year 1769, because the illustrious person on whom that title was conferred was born in that year. No doubt the bodies of persons, or corporations, who managed these banks, were formed in the years 1173 and 1407, but the *Banks* were only founded in the years we have mentioned, namely, that of Venice in 1587, and that of Genoa in 1675.

Money dealers established themselves in Italy at a very early period of the middle ages, both as money changers and money lenders. But neither of these constitute Banking. As far as we can ascertain, the business of *banking*, or dealing in credit, was revived at Florence in the early part of the 12th century. It was intimately connected with the invention of bills of exchange, which was practised by the Lombards, especially those of Asti, and the people of Cahors, in the Department of the Lot, in France, very early in the 13th, if not in the 12th century. The business of *bankers*, however, chiefly flourished at Florence, and was one of the principal causes of raising it to so great a pitch of commercial eminence. The names of the Bardi, Acciajuoli, Peruzzi, Pitti, and Medici, were famous throughout Europe. In 1345, the Bardi, and the Peruzzi, the

two greatest mercantile houses in Italy, failed. Edward III. owed the Bardi 900,000 gold florins, which his war with France prevented him paying, and the King of Sicily owed them 100,000 gold florins. The deposits of citizens and strangers, with the Bardi, were 550,000 gold florins. The Peruzzi were owed 600,000 gold florins by Edward III., and 100,000 by the King of Sicily, and the deposits they owed their customers were 350,000 gold florins. The fall of these two great pillars of credit involved that of multitudes of other smaller establishments, and, says Villani (*Istor. Fiorent.*: xii., 55), the community of Florence had never been thrown into such ruin and disorder before, and thereupon he breaks out against the folly of his fellow-citizens entrusting their money to the care of others for the love of gain. The city, however, recovered from this terrible disaster, and we find that between 1430 and 1433, 76 bankers at Florence lent the State 4,865,000 gold florins. At one time Florence is said to have had 80 bankers, but not any public bank.

In the 16th century there were 40 great bankers at Naples. They were obliged to deposit 40,000 ducats with the Government, as security, and they were bound not to go beyond the limits of the kingdom. But these precautions were in vain. They frequently failed, causing, of course, great distress; and, in 1575, the Government determined to institute a public bank. This was the earliest public bank in Italy, being 12 years before that of Venice, and exactly 100 years before that of Genoa, both of which are erroneously placed before it. This was called the *Banco di A. G. P. et di Pietà*. Several other joint stock public banks were founded shortly afterwards, viz., the *Banco del Popolo*, in 1589; the *Banco dello Santo Spirito*, in 1591; the *Banco di S. Eligio*, in 1596; the *Banco di S. Giacomo*, in 1597; the *Banco delle Povere*, in 1600; and the *Banco de' SS. Salvatore*, in 1604. Private bankers were not abolished, but they could not stand the competition of the public banks, and ceased to exist after 1604. Whether any of these banks survived the Revolution we are not aware.

AT VENICE.

6. It is one of the great current delusions of historians and economists, that the Bank of Venice was founded in 1171. But, in the technical sense of *banking*, this is a complete error. We have seen above that the Bank of Venice was not even the first public Bank in Italy. The fact is that, in the year 1171, the Venetian Republic was oppressed with great financial disorder, in consequence of wars carried on simultaneously with the empires of the east and the west. In order to extricate herself from these financial difficulties, the State levied a forced loan from its citizens, and promised them interest at the rate of 4 per

cent. The stock was made transferable, and a body of commissioners was erected in 1173 to manage the transfer of the stock, and the payment of the interest. These commissioners were called the *Camera degli Imprestiti*. Such a loan has several names in Italian, such as *compera*, *mutuo*, but the most common is *monte*, a joint stock fund. This loan, in 1173, was called the *monte vecchio*, and, in course of time, several others were contracted, and two especially were called the *monte nuovo*, and the *monte nuovissimo*. Now, we have shewn, in a previous chapter, that the English word *bank* is the equivalent of *monte*, and that a writer of the 17th century repeatedly translates the word *mons* by *bank*, and especially calls these *monti* at Venice by the name of the three "*bankes of Venice*." It is thus the confusion has arisen. The word "*bank*" is the translation of *monte*, but it has no relation whatever to the business of *banking*. These banks at Venice were nothing but commissioners of public debts. The very same error, as we have shewn below, prevails with regard to the Bank of St. George, at Genoa.

The first "*bankers*" at Venice were two Jews, who obtained leave from the Senate, in 1400, to set up banking, and this business was afterwards taken up by many of the nobility, but, towards the middle of the latter half of the 16th century many of them failed, and caused great public distress. Moreover, the coinage was in a great state of confusion, from the number of clipped and worn foreign coins in circulation, which disorganised all dealings in credit. In consequence of some political changes which took place in the constitution, the Senate prohibited the nobility from engaging in commerce, and organised the Bank of Venice in 1587.

Dr. Lewis, writing in 1678, says (*A large Model of a Bank*, p. 40):—"As to the bank at Venice, it is not of any very long standing—it had its first rise from the dishonesty of the bankers. The bankers at Venice did just as our bankers have done here,—they got men's money into their hands at interest, and used it (as was necessary) to their best advantage; that they might make a better profit of their money than the interest they paid, they lent it out to insolvent persons, or laid it out in desperate cases, as our bankers did. Hence, when they were disappointed, they did unavoidably break, the creditor lost his money, the commonwealth their trade: for the banker got what he could, and fled out of their territories, as ours do into the *King's Bench*."

"The States, finding such an intolerable inconvenience, as we do, if men lent out their money, many times they lose it; if it lay dead by them, trade dwindles away by this stagnation. Just in such a time as this is, the States set up their bank, and their officers became cashiers (as at Amsterdam), for about two millions of ducats, a bank sufficient for their trade, which was

kept in specie to be taken in, or paid out, as the merchants desired it, until the necessity of their affairs in the late Turkish war, forced them to expend all the money in specie, which was lodged in the bank. Now there is no money at all, neither is any money in specie ever paid out; but their bank is a perfect credit bank, and the fund is a mere imaginary thing; yet, because the fund being, as I said, four millions of ducats, which Venice is able to raise, and the States are obliged to pay (though they are never like to pay a farthing of it to the end of the world), all men accept this credit as money; nay, since it hath been in this condition, the very credit hath been 20 per cent. more than cash in specie; all merchants trading thither can tell you credit in the bank is much better than cash in the chest; the reason is what I have first mentioned. Credit in bank is more safe, more portable, and more transférable than money in specie, and so of greater value, as gold is better than silver.

“Not many years since credit in Bank at Venice (as our merchants can remember), was better than cash in specie, by more than twenty in the hundred, which the States found inconvenient for their trade: the States could not by any law suppress this excessive exchange, though they made it capital to take 20 per cent., till at last they were advised by a sagacious merchant to bring money in specie into the Bank to answer their credit, this presently brought down the exchange: hence, some merchants here thought the credit of the bank was impaired, because the exchange fell, when it was quite contrary, the bank paid money in specie instead of writing off credit from one to another; this made the exchange less.” This passage is repeated, with a few verbal alterations, in a pamphlet called *England's Glory by a Royal Bank*, published in 1694.

This organization of the BANK of Venice took place in 1587. The merchants were invited to deposit their money in an office managed by the Commissioners of the Public Debts. They received a credit in the bank's books equal to the actual weight of the bullion deposited, for which they could always demand an equal quantity of bullion at any time, or transfer it to any one else. Thus a uniform standard of payment was insured. It was enacted that all bills on Venice should be paid in bank money. By this means the bank money bore always a premium, compared with the current money, of about 9 per cent., called an *agio*. This bank did no business on its own account, and, as it professed always to keep the bullion in its vaults, it is clear that the credit it created was exactly equal to the bullion displaced. This is an example of what is called the “currency principle.”

Although the bank transacted no commercial business of its own, the temptation of using the money deposited in its vaults was too strong to be resisted, and on certainly two, if not three

occasions, it suspended payments. Besides the suspension alluded to in Dr. Lewis's tract above quoted, in 1678, it suspended payment again in 1691, and again from 1717 to 1739, when the State applied the money in its vaults to the purposes of war. Mr. Cantillon also says that on one occasion it tried to raise a loan by creating credits in the Bank's books, but this was done to such an extent that the credits fell to a discount of 20 per cent., as compared with specie. To remedy this, the State was obliged to mortgage a part of its revenue to raise a fund of real current specie, to purchase these transfer credits, which had the desired effect of bringing the credits to par. The author does not give the date of this transaction. (*Analysis of Trade, &c.*, 1759, p. 185). The Bank was destroyed by the French in 1797, the same year with that of Genoa.

THE BANK OF ST. GEORGE, AT GENOA.

7. The origin of public debts at Genoa is even earlier than those of Venice. In 1148, the Ligurian Republic conquered Almeria and Tortosa, in Spain, and found themselves greatly encumbered with debt. Public loans were created by means of terminable annuities, which were secured on the taxes and customs duties. In process of time these loans, or *mutui*, greatly increased, and in the 14th century it was thought that something must be done to reduce them to greater order. In 1346 it was proposed to consolidate them, but the plan was not carried out then. Towards the end of the century the Republic was torn with internal dissensions, and in 1396 Antoniotto Adorno, then Doge for the fourth time, thought it would be advisable to apply to a foreign power for protection. Application was accordingly made to Charles VI. of France, who sent Jean Le Maingre, Marshal of France, as Governor. At this time there were a great number of different offices for the management of these loans, which were also called *comperc*, and for the management of the revenue, called by a variety of different names. The names of the public creditors were entered in a book called *cartulario*, the credit was called *colonna*, and the Creditor *colonnante*. The debts were divided into shares of 100 lire each, and made transferable at will. At length, in 1407, these loans fell into great disorder from the political disturbances. The Governor called a council of the Ancients, together with the *Uffizj di Provisioni e della Moneta*. By their advice, eight of the most highly esteemed citizens were appointed a committee to devise a plan to extricate the Republic from its difficulties. All the public debts were consolidated, and all the public offices were formed into one Company, which took the name of the *Ufficio di San Giorgio*. The old loans at 7 and 8 per cent. were paid off, and a new single stock at 6 per cent. was created. The Company gradually acquired great privileges and power, they were entrusted with the collection of the revenue,

and were endowed with civil and criminal powers in all matters relating to the taxes.

In 1453, Pietro Fregoso was Doge. The Republic was distracted with internal dissensions and the expense of the war with Mahomet II., who was besieging Constantinople, and the Genoese settlement of Pera. The Government ceded to the Company of St. Giorgio, Pera, and its other colonies in the Black Sea, in full property. In the same year it was unable to maintain its authority over Corsica, and it also ceded it to the Company, with full power to equip all forces necessary to preserve these possessions. The Company was so embarrassed by the expenses of these acquisitions, that it was unable to pay any dividend on its shares in 1456, and it obtained the Pope's leave to suspend their payment for three years. In 1479 it was further released from paying any stated dividend in future, and allowed to divide whatever profits there might be for the year. In the same year a distinguished citizen, named Lodovico Fregoso, took Sarzana by stratagem from the Florentines, and the State being too weak to defend it, ceded it to the Company. In a short time it also obtained Serravalle, Castlenovo, Ortonovo, and S. Stefano. In 1512, Pieve del Picco, with the territory attached to it, was also given over to it. In 1514 it acquired Ventimiglia and its territory, and in 1515 Levanto and its territory. "In short," says Machiavelli (*Istorie Fiorentine, lib. viii.*), "the Company, being always wealthy and well managed, was able to make constant advances to the city, which was always in difficulties. The city first conceded the customs to the Company, as security for the loans, then she assigned towns, castles, and territories, so that the Company had at that time under its administration the greater part of the lands and cities of the Genoese dominions. Every year it sent its deputies, selected by vote, without the interference of the State. And the citizens greatly preferred the rule of the Company to that of the State, on account of the tyranny of the latter, and the excellent regulations of the former. The Company did not interfere in the political contests itself, but it was powerful enough to compel the successful party to respect its laws. Thus, this Company exhibited an extraordinary spectacle, which no philosopher had ever imagined, namely, within the same State, and among the same citizens, there was liberty and tyranny, justice and licence, and order and disorder, for the Company alone maintained in the city many ancient and venerable customs,—and if it should happen, as was extremely probable, that the Company should obtain possession of the whole city, Machiavelli expected that Genoa would become even more illustrious than Venice. Notwithstanding this, the Company found that the administration of these territories was ruining its finances, and in 1562 it returned them to the State. In 1539 the debts which had been redeemable were changed into per-

petual annuities, the operation was called *magno contratto di consolidazione*, and the Company was put in full possession of 76 kinds of taxes and customs duties.

All this time the Company was in no sense whatever a bank, nor ever called by that name. It was called the *Casa*, or *Ufficio di S. Giorgio*, or the *Amministratori delle Compagnie di S. Giorgio*, and its financial business was to collect the taxes, and pay the dividends upon their shares. In 1674 they presented a petition to the Government, to be allowed to set up a bank, which was granted in 1675. And this is the true date of the formation of the BANK of St. George. It was decreed, that by means of the Bank, or its credit, or by means of the books of S. Giorgio and their notes, all bills of exchange, and mercantile obligations, however small, and all payments due in the city from all parts of the world, should be paid. The Bank's notes were made the only legal tender in the city for all payments above 100 lire, and they were to be received in payment of all taxes at the treasury. This Bank, in a very short time, acquired great credit, and its business increased so rapidly that it was obliged to open four additional offices.

This Bank was at the height of its power and reputation when Law visited Genoa, and there is every reason to believe was what furnished him with the model of what he afterwards attempted to carry out on a much greater scale in Paris, and which ended in so great a catastrophe. The Bank continued to flourish till Genoa was captured by the Austrians in 1746. It had advanced 15 millions of lire to sustain the war, and it had spent not only its own money, but also 1,333,088 lire of its depositors. The Austrians plundered it, and it was obliged to suspend payments. In 1750, the Senate ordered all the note-holders to inscribe their names in a register, called *Monte di Conservazione*, the debts were capitalised in shares of 200 lire, which were to be gradually redeemed by lot. Other of its obligations, called *paghe*, were also due to the amount of 64,000 lire. These were also capitalised, as a *Monte Pagine*, on the same terms as the others, and the shares were made transferable like stock. In 1777 there were only 2,251 shares, and 7,663 *paghe* unpaid, and they were then converted into public stock.

In 1794, Genoa was involved in the war of the Revolution, and it was taken by the French in 1797, who immediately abolished the Company of St. George. The public debts were placed under the protection of the honor of the State, and the circulation of its notes prohibited. In 1799 the sale of all its effects was ordered, in order to discharge its obligations, but commerce was so utterly prostrated that its property was sold at a very low value, and the proceeds were insufficient to satisfy all its creditors. Thus ended this extraordinary corporation. Attempts were made in 1804, and in 1814, to resuscitate it, but they failed.

IN SWEDEN.

8. The Bank of Stockholm, founded 1668, is remarkable as being the first, which, according to the testimony of Law (*Mémoires sur les Banques*, p. 523. *Edit. Guillaumin*. 1851). Voltaire, (*Histoire de Charles XII.*, p. 33. *Edit.* 1785), and Hume, (*Life*, by *J. H. Burton*, Vol. II., p. 459), invented bank notes in Europe. The money of Sweden was of copper, and very inconvenient to make large payments with. A cart was required to carry a moderate amount of it. To remedy this inconvenience, a public bank was established, in which the merchants deposited their copper money, and received bank notes in return for it, which were used in payments all through the country. Payments were also made by transfers in its book. In 1726 an edict enacted that the notes should be taken in payment of bills of exchange. This bank, although first instituted as one of deposit only, seems afterwards to have done commercial business; "För," says M. Gustave du Puynode (*De la Monnaie, &c.*, p. 136), "it lent, not only on bullion and other merchandise, not subject to deterioration, but also on real property, to the amount of three-fourths of its value." In 1752 this had gone on to such an extent, that it gave rise to great alarm; the bank's funds were deeply engaged in such loans, and the owners of the property were unable to redeem them. In 1754 the debtors were allowed to pay their obligations by annual instalments of five per cent. We have read somewhere, but lost the reference, that when the exchanges were against the country, this bank used to suspend payments to prevent the drain. We much regret that so little is known in this country of the Political Economy of Sweden, where the third chair of the science was founded, and where it is said to have been cultivated with considerable diligence.

IN HOLLAND.

9. In Cisalpine countries the business of BANKING seems to have been first practised by the Dutch. And it was from them that several English writers, in the beginning of the 17th century, acquired their knowledge, and wished to introduce the business into England. Malynes, in his *Consuetudo, vel Lex Mercatoria*, published in 1622, explains their method of doing business. They did not issue notes, nor had they invented cheques. When a merchant had sold any of his credit in the banker's books, it was his custom to go and tell him to whom the credit was to be transferred. The inconvenience of this was obvious, and they subsequently either invented cheques, or adopted them from the Italians. John Law, writing in 1715, says that cheques were not then used in England, and describes the superiority of the Dutch method of doing business. At the end of the 16th

century, it was contemplated to establish a bank of deposit at Amsterdam, but the intention was not carried out till 1609, when a considerable number of bankruptcies took place. An account of the Bank of Amsterdam is given by Adam Smith, Book iv., c. 3. It received all coins, foreign and domestic, at their actual weight in bullion, and gave the depositors credit in its books to that amount. A small deduction was made for the expense of management. This credit was called bank money, and, as it always represented the real weight of bullion, it was usually at an agio of about 9 per cent. above the current worn, clipped, and degraded coins. It was enacted that all bills upon Amsterdam, above the value of 600 guilders, should be paid in bank money. The bank also received gold and silver bullion at a discount of 5 per cent., and gave the depositor a transferable receipt enabling the bearer to demand the bullion at any time within six months, upon re-transferring to the bank an amount of bank money equal to the credit originally given for the bullion, and paying one-fourth per cent. for silver, and one-half per cent. for gold bullion. If the term expired without payment of this premium, the bullion belonged to the bank at the price of the credit given.

So far all is clear. But Adam Smith then goes on to make a statement which seems to us to be perfectly unintelligible. He says:—"The person who, by making a deposit of bullion, obtains *both a bank credit and a receipt, pays his bills of exchange as they become due with his bank credit, and either sells or keeps his receipt*, according as he judges that the price of bullion is likely to fall or rise. The receipt and the bank credit seldom keep long together, and there is no occasion they should." Surely there is some extraordinary error here. How can a man, upon a deposit of £100, receive *both* a transferable receipt and also a bank credit for an equal amount? That is as much as to say that, for every deposit, a man received credit to *twice* the amount. This part of Adam Smith's account of the bank's transactions seems to us to be wholly unintelligible.

The Bank of Amsterdam professed to be a pure Bank of Deposit, that is, to make no use of its funds, but to keep in its vaults an equal amount of coin or bullion to all its obligations. Its stability was severely tested in 1672, in the French invasion, when every one rushed to demand his deposit. They were found perfectly intact, and, of course, this greatly raised the credit of the Bank. It became the great warehouse for bullion for foreigners, as well as natives. Notwithstanding its professions, and the solemnities with which each successive magistracy at Amsterdam swore to keep the treasure intact in the Bank's vaults, John Law shrewdly suspected that they did lend it out, and this was fully proved in 1794. They had for a very long series of years, notwithstanding all their oaths, been advancing

large sums to the Government, and to the Dutch East India Company, as well as to different municipalities in Holland. The first shock was given to its credit in 1790. In that year (*Davies, Hist. of Holland*, Vol. iii., p. 557. Edit. 1851) the East India Company found themselves in great difficulties. For many years they had been suffering a heavy annual loss, and had only been supported by clandestine loans from the Bank, contrary to the oaths of its Directors. In December, 1790, the Bank found itself in imminent peril from these perpetual advances, and it suddenly announced that it would in future fix the price at which it would pay out the silver held in deposit. The first price fixed inflicted on its holders a loss of 10 per cent., and it refused to pay any deposits of less than 2,500 florins. This, which was nothing less than an open bankruptcy, excited the utmost astonishment and alarm. Its receipts immediately fell from 5 per cent. above par to one-half discount. This, of course, brought a run upon it, and after a short time the order was rescinded. The public, who at that time had no knowledge of its illegal proceedings, and had no ostensible cause of distrust, was pacified for the time. In 1794, the French entered Amsterdam, and, upon investigating the affairs of the Bank, found that it had advanced nearly 11 millions of florins to the East India Company, and various cities. This, of course, was fatal to the Bank, and its notes immediately fell to a discount of 16 per cent.

We need not enter into any further details of the origin or history of banking in other countries, as what we have already given, sufficiently illustrates the different principles adopted, which is our main object. While we have shewn the extreme erroneousness of the current opinions regarding the early origin of some of the most celebrated banks, we may say that the Bank of Barcelona was in reality the oldest in Europe. It was founded, Capmany tells us, in 1401, by the municipality, for the use of the merchants. It was a bank both of deposit and discount, and the property of the city was pledged for the security of the depositors. It was thus founded 186 years before that of Venice, and 274 years before that of St. George. The Bank of Hamburg was founded in 1619, on the model of that of Amsterdam. The only peculiarity in it was that it gave credit on the deposit of jewels, as well as bullion. It is said to be nearly the only one of the old banks in Europe which still survives.

Historical Sketch of the Rise and Progress of Banking
IN SCOTLAND.

10. The Bank of Scotland is the first instance in the world of a private joint stock bank, formed by private persons, for the express purpose of making a trade of banking, dependent on their own private capital, and wholly unconnected with the

State. It differed in kind from any of the other banks existing at that time. The successful institution of the Bank of England led to a project being formed to establish a Bank in Scotland. A merchant of London, Mr. John Holland, was the author of the scheme, and he got eleven Scotch Merchants to join him. They obtained an Act of the Scotch Parliament on the 17th July, 1695, authorizing the Crown to grant them a Charter of Incorporation. The principal provisions of this Act are as follows (*Acts of the Parliament of Scotland*, vol. ix., p. 494):—

I. The joint stock was to be £1,200,000 Scots, or £100,000 sterling, and authorises certain persons to receive subscriptions for not less than £1,000 Scots (£83 6s. 8d.), nor more than £20,000 Scots (£6,666 13s. 4d.) for each person, with a deposit of 10 per cent.

II. They were allowed to lend on real or personal security, at not more than 6 per cent.; and, on failure of payment, to sell or dispose of the security publicly.

III. They were allowed to transfer their stock freely, or by will.

IV. No dividend to be made, but by consent of general meeting.

V. The joint stock to be free from all taxes affecting money for 21 years from that date.

VI. It was declared to be illegal for any other Company to set up banking for 21 years.

VII. Various legal privileges were granted for the more speedy and effectual recovery of debts due to the bank.

VIII. Prohibits any sum to be withdrawn from the joint stock.

IX. Prohibits the Company, directly or indirectly, from using or employing the joint stock of the Bank, or any of its profits, in any other trade or commerce, except the trade of lending and borrowing money upon interest, and negotiating bills of exchange.

X. Prohibits the Company from purchasing land, or heritages, or advancing money to the Government, upon the anticipation of any sums to be granted by Parliament, except only those particular ones upon which a credit of loan should be authorized by Parliament, under the penalty of forfeiting triple the amount, of which one-fifth to the informer.

XI. All foreigners who subscribed to the joint stock, were *ipso facto* naturalized to all intents and purposes. It was also provided that two-thirds of the stock must always belong to persons residing in Scotland. The Scotch subscription of £800,000 Scots (£66,666) was begun in November, and filled up at the end of December, 1695. The English subscription of £400,000 Scots (£33,333) was taken up in one day in London, a great part by Scotchmen. As the Scotch at that time were

supposed to know nothing about banking, it was also provided that for a certain number of years the Governor and twelve Directors should be English, and the Deputy-Governor and twelve Directors should be Scotch. However, it was soon found that the Scotch were such good managers, that this arrangement was changed, and all the Directors were Scotch, and thirteen trustees were chosen to manage the English business and affairs in London.

No sooner was the Bank fairly established, than, in 1696, the African Company attempted to set up the trade of banking in defiance of the Bank's privilege. This was the celebrated Darien Company, which was organized by William Paterson, who was one of the founders of the Bank of England. Mr. Holland was Governor of the Bank, but so little was it thought of, that it did not venture to vindicate its privileges against the African Company, for which there was a national phrenzy, and which afterwards ended so sadly. The Bank was obliged to content itself by strengthening its position by calling up two-tenths of its capital.

The African Company soon, however, burnt its fingers with banking, as, in order to rival the Bank, they advanced their notes with great imprudence to several of their own shareholders and others, and sustained great losses, which made them stop. The Bank then began the business of exchanges, but, finding that they could not compete with private merchants, gave it up. In 1696 they opened branches at Glasgow, Aberdeen, Dundee, and Montrose; but not finding them to pay, withdrew them. In May, 1698, the rivalry of the African Company being at an end, the directors repaid the two-tenths of capital last called up, as being more than necessary for their business.

The Bank at first received no deposits from the public; its business consisted in circulating its own notes upon the credit of the subscription that was paid in. These notes were for £100, £50, £20, £10, and £5. It is disputed when they began to issue £1 notes, for, while a pamphlet, published in 1728 on their behalf, says that they began to issue them in January, 1699-1700, Mr. Kinnear, a director of the Bank, stated to the Committee of the House of Commons that, though many proposals were made to them to circulate "tickets" or "tokens" of £1, they had always hesitated to adopt so novel an experiment till 1704. Which authority is right we have no means of deciding. In 1701 a great fire destroyed the Parliament Close, in which the bank was, but the cash and all the effects were safely removed into the Castle by the Earl of Leven, who was Governor of both.

In December, 1704, soon after, as it would appear by one account, that they had issued £1 notes, a rumour was spread all over the kingdom that the Privy Council were going to raise the value of the coin, which caused a run upon the Bank, and at

last it was obliged to stop payment. A meeting of the proprietors was held, who declared that all their notes should bear interest until they were paid. The directors also requested the Privy Council to appoint a Committee to examine their books. They reported that the Bank was in the most sound and flourishing condition, and their notes then passed without depreciation. The directors made a call of one-tenth, and in less than five months paid off all their notes with interest.

By the Act of Union between England and Scotland, it was stipulated that the coinage of Scotland should be reduced to uniformity with that of England, and the loss or deficiency to private individuals made good out of the Equivalent fund. (Art. xv.) The Bank assisted this operation by receiving all the old money and giving their own notes, or new money in return, receiving a commission of half per cent. This was successfully accomplished without any disturbance.

In September, 1715, the rebellion broke out, which immediately caused a run upon the Bank, the directors themselves urging it on, that the money might not fall into the hands of the insurgents. They then stopped, retaining all the money belonging to the Crown, which was about £30,000, which they lodged in the Castle. They then gave notice that all their notes should bear interest, as had been done in 1704. In May, June, and July, 1716, they were all called in and paid. In this year the monopoly of banking granted by their charter expired, and no steps were taken to renew it.

It appears that up to this time the profits of the Bank were enormous. A rival pamphlet states that the dividend was 35, 40, and 50 per cent., and, accordingly, as we may well suppose, these profits attracted rivals. A cry was got up against them, that they were too niggardly in advancing loans, that they exacted too high interest, and that the concern was altogether too small.

In December, 1719, proposals were made to them to unite with the proprietors of the Equivalent fund, to the amount of £250,000, so as to increase the capital to £350,000, and share the annual grant of £10,000 (being four per cent. on the amount) in the proportion of two-sevenths and five-sevenths. But, as the Bank had only one-tenth paid up, the proprietors of the Equivalent fund were to draw out of the Bank, as might be agreed upon, nine-tenths, or £225,000, in notes, so that there might then be a capital of £35,000 to bank upon.

The Bank replied that :—1st, They had no power by their Act to amalgamate with the Equivalent, as they were limited to £100,000 sterling; 2ndly, That they would not unite at par with the Equivalent at four per cent., while their own stock was worth at least ten per cent.; 3rdly, That the stock of the Bank was large enough for the country; and, if they wanted it en-

larged, they could do it themselves by calls on their proprietors. They also gave other calculations, shewing the absurd nature of the proposals.

No sooner were the advances of the Equivalent proprietors repulsed, than another set of persons began another rough wooing, to thrust themselves into a union with them. The *Edinburgh Society*, formed on a pretended plan of insuring against fire, tried to force a junction with them, and, being defeated in this, they tried to get up a run upon them. They got together £8,400 of their notes, and spread a report of a run. This, however failed; and shortly after the Bubble Act passed, by which the society found that they were an illegal company, and were obliged to dissolve themselves. The London Assurance Company then "proposed" to them, but met with a similar refusal.

At the time of the Union, a considerable number of persons, both civil and military, were creditors of the State, and the Equivalent sum stipulated in the Act of Union was not sufficient to discharge their claims. In 1714, they obtained an Act of Parliament, constituting their debts, but no Parliamentary provision was made to pay it till 1719, when £10,000 was set apart for that purpose, to be paid annually, in preference to all other claims. The Act of 1719 empowered His Majesty, by letters patent, to incorporate the proprietors of this debt into a body politic and corporate—a *Moxre*—with powers to do and perform all matters appertaining to them to do, touching or concerning the said capital sum; and the yearly fund, payable in respect thereof, as His Majesty, by the said letters patent, should think fit to grant. In pursuance of this Act, the proprietors, who included persons in all ranks of the State, were incorporated in 1724; and, by the same letters patent, the King agreed and covenanted with the corporation that he would, from time to time, grant them such other powers, privileges, and authorities, as he lawfully might.

This was the body of persons whom we have seen attempt to force themselves upon the Bank of Scotland. When they were repulsed by that body, they determined to apply to the King to grant them powers of Banking in Scotland, in pursuance of his agreement to grant them any powers that he lawfully might. They accordingly petitioned him to grant them powers to bank in Scotland, limited to such of the company as should on or before Michaelmas, 1727, subject their stock to the trade of banking. This petition came to the knowledge of the Bank in 1726, and, of course, they did everything they could to oppose it. A cry was got up against them that they were hostile to the House of Hanover—that they charged too high interest for their loans—that they were too particular in the securities they required—that they would not lend on their own stock, and other things. To all these various charges, they, or a friend for them, elabo-

rately replied, and they said that such a thing as two banks in one country was never heard of—that if Scotland had two England should have ten. By this time they had called up 3-10ths of their stock, or £30,000, and they alleged that that was sufficient to circulate all the credit that could be required in Scotland. They had some sound views on the subject: “For the quota of credit in a banking company must be *proportioned to the stock of specie in the nation*, learned and understood by long experience, and not extended to a capital stock subscribed for, which cannot in the least help to support the company’s credit if the specie of the nation decay.”

The call that had been made was partly paid up in the Bank’s own notes, just as we shall see that the subscription to the new stock of the Bank of England was partly paid in its own depreciated notes. An outcry was made about this, but it was well answered: “But the objectors do not at all consider this point. For the payments are many of them made in specie, and bank notes are justly reckoned the same as specie when paid in on a call of stock, *because, when paid in, it lessens the demand on the Bank.*” He also says: “A certain stock of specie circulating in the country is needful for currency of payments in markets, and amongst the meaner sort of people, bearing a due proportion to what is running on paper credit upon the faith of the Banking Company.” Excellent doctrines, in strict accordance with the principles which made the Parliament of Scotland reject the plausible and delusive schemes of Dr. Chamberlen and John Law, for issuing paper based upon land.

Notwithstanding the opposition of the Bank of Scotland, the charter, with powers of banking, was granted to the Equivalent Company on the 31st May, 1727. The King’s death on the 11th June following delayed it for a short time, but it was sealed on the 8th July. The Company took the name of the ROYAL BANK, and commenced business on the 8th December, 1727, with a capital stock of £151,000.

Granting that all the charges against the old bank were futile and groundless, we may well rejoice that the monopoly of the Bank of Scotland was not permitted to subsist. A writer, who professes to be independent of either bank, touched the right point in reply to the statement put forth on behalf of the old bank: “The power of monopolies is, I believe, an exploded doctrine. * * * Did ever any nation make an exclusive bank perpetual, or for longer than twenty-one years? Or, if such an instance can be given, was the measure right? * * * If the old bank should reply—We are in possession, what have we done to deserve to have our possession disturbed? The answer upon that abstract question is plain by another question—*What have we, the other subjects, done to be secluded? or by what law are we secluded from the advantages you enjoy?*” The

writer then says, after comparing the rival companies: "The obvious reflection which arises from comparing these two is, that these candid and fair dealers have also dealt profitably for themselves (as it is but reasonable that they should), they have taken very good payment for all the services they have done to the nation, *and what title they, or any other set of men, have to an hereditary or indefensible monopoly of banking is hard to understand.* * * * As ready as our Parliament was at the Union to accommodate petitioners, *a perpetual monopoly of banking was a thing so manifestly pernicious, that no private men could have the assurance to aim at it, far less could any Parliament be so unthinking as to grant it.*" On the south of the Tweed there was found a Parliament so unthinking as to grant a monopoly of banking to a single company for upwards of 130 years, and the consequences fully justified the opinions of the sagacious Scot.

The directors of the company were authorized to make calls upon the proprietors, to the amount of one-half of their stock, but there were no means given of enforcing the calls beyond retaining the accruing dividends until the call was satisfied. They got, however, great assistance by having £20,000 deposited with them by the Crown. This was sent down by the Government to be placed out at interest, to assist the fisheries and manufactures, and several of the directors of the Royal Bank, being among the trustees for managing the fund, voted that it should be placed in their own bank. Their charter also granted them unlimited powers of issue. The alarm and jealousy created by the establishment of the new bank happily soon wore off, as it was discovered that, so far from injuring it, the inevitable consequence followed that enlarged experience in commerce would enable us to predict; it increased the prosperity of both of them, so that the stock of the Bank of Scotland rose to 400 per cent., and that of the Royal Bank also very high.

The Royal Bank had only been in existence two years, when it invented a further development of the system of banking, which, by the unanimous testimony of all persons who know that country, has done more to develop its resources, and promote its agricultural and commercial prosperity, than any other cause whatever. This is the system of *cash credits, or cash accounts*. This system deserves the most attentive consideration, because it is entirely of the nature of *accommodation paper*, which has fallen into such disrepute in England, from the enormous abuse of it that has taken place. We shall not interrupt our present narrative by describing the system here, but refer to it elsewhere. In 1731, the Bank of Scotland tried again to establish branches at Glasgow, Aberdeen, and Dundee, but, after a trial of two years, was obliged to discontinue them, and the plan was not tried again till 1771.

The unlimited power of issuing "promises to pay," placed in the hands of two hostile parties, must naturally have led to great over-issues, before they acquired sufficient experience. To protect themselves from the consequences of these over-issues, as well as from the attacks of each other, the Bank of Scotland in 1730 introduced a clause into their notes making them payable, at the option of the directors of the Bank, at the end of six months, with a sum equal to the legal interest from the time of demand to that time. This practice was adopted by all the other banking companies, for the manifest advantages of banking were so strikingly displayed, that after the expiry of the monopoly of the Bank of Scotland, banking companies started up in all directions, and inundated the country with notes. When the holders of the notes demanded payment for them, the directors of the companies threatened that they would take advantage of the optional clause, unless the demanders would content themselves with a part of what they wanted. Moreover, as there was no restraint upon the amount of their notes, many of the companies issued notes for 10s., 5s., and even lower than that. In Perthshire there were notes for 1s., and even for 1d., and the Perth Banking Company was founded partly to put an end to this nuisance. The inevitable consequence followed; these paper notes drove all the gold and silver out of the country, and the exchange with London fell. Adam Smith says: "While the exchange between London and Carlisle was at par, that between London and Dumfries would sometimes be 4 per cent. against Dumfries, though this town is not thirty miles distance from Carlisle. But at Carlisle bills were paid in gold and silver, whereas at Dumfries they were paid in Scotch bank notes, and the uncertainty of getting those bank notes exchanged for gold and silver coin had thus degraded them 4 per cent. below the value of that coin." And this was at the time when, owing to the degraded state of the English coin, the foreign exchanges were adverse to England, and the market price of gold was £4 per ounce, so that the whole depreciation of the note was about 6½ per cent. Thus we see at this time, when the Scotch bank notes were at a discount, they were, in fact, *inconvertible*, or only payable six months after demand, a circumstance of great importance, and one which must be especially observed, as this was one of the instances alluded to by Sir Robert Peel in introducing his Bank Act of 1844.

The manifest consequence followed. All the gold left the country, as it always does from the excessive paper issues, and the banks were all obliged to employ agents in London constantly collecting money for them, at an expense of seldom less than one-and-a-half to two per cent. Adam Smith says: "This money was sent down by the waggons, and insured by the carriers at an additional expense of three quarters per cent.,

or 15s. on the £100. Those agents were not always able to replenish the coffers of their employers so fast as they were emptied. In this case the resource of the banks was, to draw upon their correspondents in London bills of exchange to the extent of the sum they wanted. When those correspondents afterwards drew upon them for the payment of this sum, together with the interest and commission, some of those banks, from the distress into which their excessive circulation had thrown them, had sometimes no other means of satisfying this draught but by drawing a second set of bills, either upon the same or upon some other correspondents in London, and the same sum, or rather bills for the same sum, would in this manner make more than two or three journeys, the debtor bank always paying the interest and commission upon the whole accumulated sum. Even those Scotch banks which never distinguished themselves by their extreme imprudence, were sometimes obliged to employ this ruinous resource.

“The gold coin which was paid out either by the Bank of England or by the Scotch banks, in exchange for that part of their paper which was over and above what could be employed in the circulation of the country, being likewise over and above what could be employed in that circulation, was sometimes sent abroad in the shape of coin, sometimes melted down and sent abroad in the shape of bullion, and sometimes melted down, and sold to the Bank of England, at the high price of £4 an ounce. It was the newest, the heaviest, and the best pieces only, which were carefully picked out of the old coin, and either sent abroad or melted down at home, and while they remained in the shape of coin, those heavy pieces were of no more value than the light, but they were of more value abroad, or when melted down into bullion at home.” This passage well illustrates the quotation we have given from Aristophanes, and is admirably illustrated by what took place in France during the existence of the Assignats, and in England during the suspension of cash payments.

At this period the Scotch Banks had got themselves into a very alarming position, from their ignorance of the true principles of regulating a paper currency, as well as of the effect of an excessive issue of paper in depressing the exchanges, and causing an export of gold, and not perceiving that, while in this state, bringing gold into the country was like pouring water into a sieve, or like the toil of the Danaides. They had been far too prodigal in granting cash credits, and allowing them to be converted into dead loans, without observing the rules that were specially applicable to them. And everything seemed to show that matters would get worse, as the annihilation of the last Jacobite rebellion in 1746 had freed the country for ever from the fear of internal disturbances, and numerous other companies

were forming to add to the currency, which was already superabundant.

United in a common danger, the two principal banks agreed to combine their influence, and obtain an Act to remedy this, and the Statute 1765, c. 49, was passed, suppressing all notes under 20s., and prohibiting those to be issued with the optional clause, and enacting that all such notes should be payable to the bearer on demand. The banks also curtailed their cash credits very extensively, and called up fresh capital. Owing to these combined measures, silver immediately returned into circulation, the value of the Scotch currency was restored to par, and from that time to the present, although the issue of bank notes was absolutely free until 1845, the Scotch currency HAS NEVER VARIED FROM PAR.

The Bank of Scotland and the Royal Bank continued to be the only chartered banks till 1746, when the British Linen Company was incorporated, for the purpose of carrying on the linen manufacture, and banking in connection with it. This Company soon found it expedient to discontinue the linen part of their business and confine themselves to banking, and it has since become one of the most powerful and wealthy of the Scotch banks, but it did not introduce any new feature into Scotch banking.

This is the first occasion, that we are aware of, on which that abominable system of accommodation paper, which is the sure precursor of mercantile convulsion, was fully manifested. The Scotch banks seem to have learnt a very wholesome lesson, and contracted their issues more within the bounds of prudence. This was a source of prodigious annoyance to a vast number of speculators and adventurers. The prudence which the banks exercised in discounting, not only alarmed, but enraged these projectors to the highest degree. "Their own distress," says Adam Smith, "of which this prudent and necessary reserve of the banks was no doubt the immediate occasion, they called the distress of the country; and this distress of the country they said was altogether owing to the ignorance, pusillanimity, and bad conduct of the banks, which did not give a sufficiently liberal aid to the spirited undertakings of those who exerted themselves in order to beautify, improve, and enrich the country. It was the duty of the banks, they seemed to think, to lend for so long a time, and to as great an extent, as they might wish to borrow. The banks, however, by refusing in this manner to give more credit to those to whom they had already given a great deal too much, took the only method by which it was now possible either to save their own credit, or the public credit of the country.

"In the midst of this clamour and distress, a new bank was established in Scotland, for the express purpose of relieving the

distress of the country. The design was generous, but the execution was imprudent; and the nature and causes of the distress which it meant to relieve, were not, perhaps, well understood. This bank was more liberal than any had ever been, both in granting cash accounts, and in discounting bills of exchange. With regard to the latter, it seems to have made scarce any distinction between real and circulating bills, but to have discounted all equally. It was the avowed principle of this bank to advance, upon any reasonable security, the whole capital which was to be employed in those improvements of which the returns are the most slow and distant, such as the improvements of land. To promote such improvements was even said to be the chief of the public-spirited purposes for which it was instituted. By its liberality in granting cash accounts, and in discounting bills of exchange, it no doubt issued great quantities of its bank notes. But those bank notes being, the greater part of them, over and above what the circulation of the country could easily absorb and employ, returned upon it, in order to be exchanged for gold and silver, as fast as they were issued. Its coffers were never well filled. The capital, which had been subscribed to this bank at two different subscriptions, amounted to £160,000, of which 80 per cent. only were paid up. This sum ought to have been paid in at several different instalments. A great part of the proprietors, when they paid in their first instalment, opened a cash account with the bank; and the directors, thinking themselves obliged to treat their own proprietors with the same liberality with which they treated all other men, allowed many of them to borrow upon this cash account, what they paid in upon all their subsequent instalments. Such payments, therefore, only put into one coffer what had the moment before been taken out of another. But, had the coffers of this bank been filled ever so well, its excessive circulation must have emptied them faster than they could have been replenished by any other expedient but the ruinous one of drawing upon London, and, when the bill became due, paying it, together with interest and commission, by another draught upon the same place. Its coffers having been filled so very ill, it is said to have been driven to this resource within a very few months after it began to do business. The estates of the proprietors of this bank were worth several millions, and by their subscription to the original bond, or contract of the bank, were really pledged for answering all its engagements. By means of the great credit which so great a pledge necessarily gave it, it was notwithstanding its too liberal conduct, enabled to carry on business for more than two years. When it was obliged to stop, it had in circulation about £200,000 in bank notes. In order to support the circulation of those notes, which were continually returning upon it, as fast as they were issued, it had been constantly in the practice

of drawing bills of exchange upon London, of which the number and value were continually increasing, and, when it stopped, amounted upwards of £600,000. This bank, therefore, had, in little more than the course of two years, advanced to different people upwards of £800,000 at 5 per cent. Upon the £200,000 which it circulated in bank notes, this 5 per cent. might perhaps be considered as clear gain, without any other deduction besides the expense of management. But upon upwards of £600,000, for which it was continually drawing bills of exchange upon London, it was paying, in the way of interest and commission, upwards of 8 per cent., and was, consequently, losing more than 3 per cent. upon more than three-fourths of all its dealings.

“The operations of this bank seem to have produced effects quite opposite to those which were intended by the particular persons who planned and directed it. They seem to have intended to support the spirited undertakings, for as such they considered them, which were at that time carrying on in different parts of the country, and at the same time, by drawing the whole banking business to themselves, to supplant all the other Scotch banks, particularly those established at Edinburgh, whose backwardness in discounting bills of exchange had given some offence. This bank, no doubt, gave some temporary relief to those projectors, and enabled them to carry on their projects for about two years longer than they could otherwise have done. But it thereby only enabled them to get so much deeper into debt, so that, when ruin came, it fell so much heavier both upon them and upon their creditors. The operations of this bank, therefore, instead of relieving, in reality aggravated, in the long run, the distress, which those projectors had brought both upon themselves and upon their country. It would have been much better for themselves, their creditors, and their country, had the greater part of them been obliged to stop two years sooner than they actually did. The temporary relief, however, which this bank afforded to those projectors, proved a real and permanent relief to the other Scotch banks. All the dealers in circulating bills of exchange, which those other banks had become so backward in discounting, had recourse to this new bank, where they were received with open arms. Those other banks were enabled to get very easily out of that fatal circle, from which they could not otherwise have disengaged themselves, without incurring a considerable loss, and perhaps, too, even some degree of discredit.

“In the long run, therefore, the operations of this Bank increased the real distress of the country, which it meant to relieve; and effectually relieved from a very great distress those rivals whom it meant to supplant.

“At the first setting out of this Bank, it was the opinion of some people that how fast soever its coffers might be emptied,

it might easily replenish them, by raising money upon the securities of those to whom it had advanced its paper. Experience, I believe, soon convinced them that this method of raising money was much too slow to answer their purpose; and that coffers, which were originally so ill-filled, and which emptied themselves so very fast, could be replenished by no other expedient but the ruinous one of drawing bills upon London, and, when they became due, paying them by other draughts upon the same place, with accumulated interest and commission. But though they had been able by this method to raise money as fast as they wanted it, yet, instead of making a profit, they must have suffered a loss by every such operation; so that, in the long run, they must have ruined themselves as a mercantile company, though perhaps not so soon as by the more expensive practice of drawing and re-drawing. They could still have made nothing by the interest of the paper, which, being over and above the circulation of the country could absorb and employ, returned upon them, in order to be exchanged for gold and silver, as fast as they issued it; and for the payment of which they were themselves continually obliged to borrow money. On the contrary, the whole expense of this borrowing, of employing agents to look out for the people who had money to lend, of negotiating with those people, and of drawing the proper bond or assignment, must have fallen upon them, and have been so much clear loss upon the balance of their accounts. The project of replenishing their coffers in this manner, may be compared to that of a man who had a water pond, from which a stream was continually running out, and into which no stream was continually running, but who proposed to keep it always full by employing a number of people to go continually with buckets to a well, at some miles' distance, in order to bring water to replenish it.

“But, though this operation had proved not only practicable, but profitable to the bank, as a mercantile company, yet the country could have derived no benefit from it; but, on the contrary, must have suffered a very considerable loss by it. This operation could not augment in the smallest degree the quantity of money to be lent. It could only have erected this bank into a sort of general loan office for the whole country. Those who wanted to borrow, must have applied to this bank, instead of applying to the private persons who had lent it their money. But a bank which lends money, perhaps, to 500 different people, the greater part of whom its directors can know very little about, is not likely to be more judicious in the choice of its debtors, than a private person who lends out his money among a few people, whom he knows, and in whose sober and frugal conduct, he thinks he has good reason to confide. The debtors of such a bank as that, whose conduct I have been giving some

account of, were likely, the greater part of them, to be chimerical projectors, the drawers and re-drawers of circulating bills of exchange, who would employ the money in extravagant undertakings, which, with all the assistance that could be given them, they would probably never be able to complete, and which, if they should be completed, would never repay the expense which they had really cost, would never afford a fund capable of maintaining a quantity of labor equal to that which had been employed about them. The sober and frugal debtors of private persons, on the contrary, would be more likely to employ the money borrowed in sober undertakings, which were proportioned to their capitals, and which, though they might have less of the grand and the marvellous, would have more of the solid and the profitable, which would repay with a large profit whatever had been laid out upon them, and which would thus afford a fund capable of maintaining a much greater quantity of labor than that which had been employed about them. The success of this operation, therefore, without increasing in the smallest degree the capital of the country, would only have transferred a great part of it from prudent and profitable to imprudent and unprofitable undertakings."

This bank, to which this long extract refers, was the celebrated Ayr Bank, which was founded to remedy the alleged distress caused by the niggardly conduct of the existing banks. It was started by a company which comprised the Duke of Hamilton and many other landed proprietors of immense wealth, and it was based on the fatal delusion that, because the capital and property of its proprietors was undoubted, it might therefore issue notes to any amount without depreciation. This was exactly John Law's theory of money, and this bank is a pregnant instance of its fallacy. The pamphlet we have already quoted from, relating to the bank of Scotland, had already seen and denounced this fallacy, for it said, with perfect truth and wisdom, *that no matter what the capital of a banking company is, the paper credit, in the shape of notes, which it can circulate, bears a certain proportion to the existing specie in the country,* and this can only be ascertained by experience. Now, this strikes at the root of John Law's whole theory, because that is based upon the fallacy that bank notes only *represent* property, and, therefore, may be multiplied to the extent of any existing property without depreciation—a theory whose results may be seen in the history of the Assignats, whereas the real truth and fact is, that bank notes do not *represent* any property whatever, but are themselves independent entities, and can only maintain their value, like any other independent entities, by bearing a certain proportion to the specie. Nor is Adam Smith correct in what he says, that the operations of banking do not increase the capital of the country; there is no more delusive fallacy than this in Political Economy; it is just because

banking *does* increase capital so rapidly that it is so dangerous. It is just for the very reason that bank credits, whether in the form of promissory notes, or entries and cheques, perform exactly the same functions, and are in all respects equivalent to the creation of so much additional capital, that they so fatally depreciate the value of the existing specie, if they are multiplied too rapidly. The fatal error of the Ayr Bank, and of Law's theory is this, *not* that capital might be increased by banking, but in not perceiving the *true natural limits to the increase*—in not seeing that the true limits were to be found in its maintaining an equality of value with gold and silver. This unfortunate concern was supposed to have been insolvent within a fortnight after it commenced business. Its mistaken course inflated speculation; the accommodation bill system, which has been the cause of every commercial crisis from that time to this, promoted by this bank and other speculators, formed the exact antetype of the proceedings of the Western Bank, and its herd of adventurers in 1857. The exports in 1771 and 1772 rose to a height they had never done before, and which they did not again equal till 1787. While commerce was in this apparently prosperous, but in reality bloated and diseased condition, the puncture of a pin was sufficient to make it collapse. On the 10th June 1772, a partner in one of the greatest banking firms in London, Neale & Co., decamped with £300,000, having been deeply engaged in speculation in funds. This man, named Fordyce, was a Scotchman, and had a large Scotch connection; these were blown upon by the failure of their London agent, and a complete commercial panic began. The Ayr Bank had branches in Edinburgh and Dumfries, and a run began upon it on the 17th June, 1772, in Edinburgh, and it stopped payment on 25th, along with a crowd of speculators. The whole of Scotland was shaken to its foundation. The paper of the Ayr Bank in circulation amounted to £800,000. There had been no disaster similar to it since the Darien scheme, and there has been none since like it, until the failure of the Western Bank. The credit even of the other banks was almost gone. Besides the three Public Banks, only three of the private ones survived. The person who was the immediate cause of the collapse of the rotten bubble of credit being a Scotchman, the London papers teemed with tirades of abuse of everything Scotch.

A writer in one of the papers says that the accommodation bill system first sprung up then. In the *Public Advertiser*, July 8, 1772, it says in a letter: "Banking Companies have appeared in almost every corner of the kingdom, and bills of exchange have been multiplied by a new method called *Swivelling*, without any solid transactions." Adam Smith, however, places it earlier. Speaking of the refusal of the banks to discount to

the extent the speculators wished, he says: "Some of those traders had recourse to an expedient, which for a time served their purpose, though at a much greater expense, yet as effectually as the utmost extension of bank credits could have done. This expedient was no other than the well-known shift of drawing and redrawing; the shift to which unfortunate traders have sometimes recourse when they are upon the brink of bankruptcy. *The practice of raising money in this manner had long been known in England*, and, during the course of the late war, when the high profits of trade afforded a great temptation to over-trading, is said to have been carried on to a very great extent. From England it was brought to Scotland, where in proportion to the very limited commerce and to the very moderate capital of the country, it was soon carried on to a much greater extent than it ever had been in England. The practice of drawing and redrawing is so well known to all men of business, that it may perhaps be thought unnecessary to give an account of it." And yet a respectable witness, Mr. Latouche, deputed by the private bankers of Dublin to give evidence before the Committee of the House of Commons in 1858, says that the accommodation bill system "arose from a new element, which, when the Act of 1844 was made, did not exist at all, and that was the immense amount of deposits in the hands of Joint Stock Banks paying interest!"

We may also notice a fact that was asserted at this time, especially as it has been brought up again in the recent crisis in Scotland. It was generally, if not universally supposed in Scotland that three of the chartered banks, the Bank of Scotland, the Royal Bank, and the British Linen Company, were banks with limited liability. It is even positively stated so in the Reports of both Houses of Parliament, in 1826. Recently, however, this has been called in question with regard to the two latter banks. Mr. Hodgson, a Director of the Bank of England, in giving evidence before the late Committee, says, Q. 3,575: "The only bank existing in Scotland with limited liability is, I believe, the Bank of Scotland; there is, I believe, a very great doubt about the Royal Bank of Scotland, and the British Linen Company, having a limited liability; I believe that the Bank of Scotland has a perfect charter, as perfect as that of the Bank of England; I believe that, though the other two banks, which I have named, have charters conferring certain privileges, it is very much doubted whether in those privileges limited liability is included. *Mr. Cayley*: Is there not a general impression in Scotland that they are banks of limited liability?—There has been that impression not only in Scotland, but in England, and amongst their own customers; but of late that opinion has been very much shaken, and I believe that the opinion of the Lords of Session now is, that those banks have not limited liability." However, there is, in the *Public Advertiser* of the 22nd June, 1772, a

letter from an apparently well-informed person, *stating that the proprietors of the Bank of Scotland are fully liable for all its debts, and that their property is worth several millions, and urging that as a strong reason why the Bank of England should come forward to their assistance.* Now, if this be so, it will certainly be a great surprise to common opinion. May it be long before the question in respect to either bank has any practical importance.

In 1774, by the Statute of that year, c. 32, the Bank of Scotland was authorized to double its capital stock, and the limit which any shareholder might hold was raised to forty shares. In this year the bank began successfully to establish branches, which has since become so marked a feature in Scotch banking. In 1784, by the Statute of that year, c. 12, the capital of the bank was raised to £300,000, and all restrictions as to the amount of stock any proprietor might hold, taken off. In 1792, by the Statute of that year, c. 25, the capital was raised to £600,000, and by Statute, 1794, c. 19, to £1,000,000, and by Statute, 1804, c. 23, to £1,500,000, of which £1,000,000 has been called up, and at which it still remains.

The next great commercial crisis was in 1793. This also extended to Scotland. This was attributed by the best contemporary writers to the inordinate multiplication of the country bankers, and the commencement of the revolutionary war. This crisis was most severely felt at Glasgow. Numbers of the most wealthy firms, both commercial and manufacturing, failed. The Glasgow Arms Bank, one of the three oldest in the city, stopped on the 14th March. Three-fourths of the country bankers in England were greatly shaken. The Bank of England refused all assistance, in spite of all solicitations made to it, for which it is severely blamed by Sir Francis Baring and the Bullion Report. When the Bank adopted this perverse course, universal failure seemed imminent. Sir John Sinclair remembered the precedent of 1697, when Montague had sustained public credit by an issue of Exchequer bills, and thought that a similar plan might be followed in this crisis. Mr. Pitt desired him to propose a scheme for the purpose, which he presented on the 16th April. A Committee of the House of Commons was immediately appointed. In the meantime a director of the Royal Bank of Scotland came up, with the most alarming news from Scotland. The public banks were wholly unable, with due regard to their own safety, to furnish the accommodation necessary to support commercial houses, and the country bankers. That, unless they received immediate assistance from Government, general failure would ensue. Numerous houses, who were perfectly solvent, must fall, unless they could obtain temporary relief. Mr. Macdowall, M.P. for Glasgow, stated that the commercial houses and manufactories

there were in the greatest distress, from the total destruction of credit. That the distress arose from the refusal of the Glasgow, Paisley, and Greenock Banks to discount, as their notes were poured in upon them for gold. This panic was allayed by the Government consenting to issue small Exchequer bills, and by the activity of Sir John Sinclair in getting money sent down to Glasgow in anticipation of these exchequer bills.

An idea of the great severity of this crisis may be formed from the interesting memoirs of Sir William Forbes, of the history of that house. He says, p. 80, speaking of deposit receipts:—

“In ordinary times, the number paid and granted are pretty much the same.

“Amount paid above, granted in December, 1792,	£10,670
” ” ” January, 1793,	16,916
” ” ” February, ”	11,561
” ” ” March, ”	52,961
” ” ” April, ”	105,075
” ” ” to 23rd May, ”	66,541
	£263,724

“The diminution on current accounts balances was in proportion, that is, nearly as much more.”

The news of the suspension of cash payments by the Bank of England reached Edinburgh by express on the 1st of March. An immediate run on the banks took place. The managers of the public banks waived all etiquette, and met at Sir William Forbes's to consider what was to be done. It was agreed to follow the example of the Bank of England, and suspend all payments in specie. A meeting of the principal inhabitants was called by the Lord Provost, and attended by the Lord President of the Court of Session, the Lord Chief Baron of the Exchequer, the Lord Advocate, and the Sheriff of Edinburgh. The meeting came to a unanimous resolution to support the credit of the banks, and to receive their notes as specie. This resolution was advertised in the papers, and expresses sent off to the principal towns in the kingdom to inform them of it.

The suspension of cash payments gave rise to terrible scenes of confusion and uproar. The doors of the banks were besieged by crowds, clamouring for gold and silver in exchange for notes. The demand for small change by the lower classes was most urgent. They adopted the plan of dividing the £1 notes into halves and quarters. Spanish dollars, stamped by the Mint, were issued at 4s. 6d., and quarter guineas were coined. An Act was speedily passed, to allow those banks which had been in the habit of issuing notes, to issue 5s. notes for a limited period. The panic was allayed, and confidence quickly returned. The

notes were received as readily as ever, though the banks refused to cash them; and, what was somewhat remarkable, no attempt was ever made by the people to compel them to pay specie, and not a single action was brought against them, although they were entirely unprotected by any Act of Parliament, and in a short time business proceeded more prosperously than ever.

The next occurrence that we may mention, as it was regarded as a political event, was the foundation of the Commercial Bank in 1810. This was at the time when the high Tory *régime* was in its highest and palmiest state, and the banks were alleged to carry their politics into their business. The Liberal party then determined to found an opposition bank, which was named the Commercial, which has attained as great an eminence as any of the older ones in public estimation. Its capital, as yet paid up, is £600,000, which, its directors very recently gave the satisfactory assurance to its shareholders, is perfectly intact, and in addition to that, it has £400,000 of accumulated profits as a reserve fund. This bank subsequently obtained a charter, but the liability of its shareholders is specially declared unlimited.

In 1818, it being found that many foreigners availed themselves of the privilege of naturalization, by purchasing stock in the Bank of Scotland, this clause in their original Act was repealed.

The long and dreadful catalogue of banking failures in England, chiefly owing to the monopoly of the Bank of England, and which were attributed to the issues of the £1 notes of the country bankers, made the Ministry of 1826 desirous to abolish them in Scotland and Ireland, at the same time as they did those of England. But this raised such a ferment in the country, that the Government consented that Committees of both Houses should be appointed to inquire into the matter. The result was so eminently favourable to the Scotch banking system, that no further interference was attempted. "With respect to Scotland," says the report of the Lords, "it is to be remarked that during the period from 1766 to 1797, when no small notes were by law issuable in England, the portion of the currency of Scotland in which payments under £5 were made, continued to consist almost entirely of notes of £1 and £1 1s., and that no inconvenience is known to have resulted from this difference in the currency of the two countries. This circumstance, among others, tends to prove that uniformity, however desirable, is not indispensably necessary. It is also proved, by the evidence, and by the documents, that the banks of Scotland, whether chartered or joint stock companies, or private establishments, have for more than a century exhibited a stability which the Committee believe to be unexampled in the history of banking; that they supported themselves from 1797 to 1812, without any protection from the restriction by which

the Bank of England, and that of Ireland, were relieved from cash payments; that there was little demand for gold during the late embarrassments in the circulation; and that in the whole period of their establishment there are not more than two or three instances of bankruptcy. As during the whole of this period a large portion of their issues consisted almost entirely of notes not exceeding £1, or £1 1s., there is the strongest reason for concluding that, as far as respects the Banks of Scotland, the issue of paper of that description has been found compatible with the highest degree of solidity; and that there is not, therefore, while they are conducted upon their present system, sufficient ground for proposing any alteration, with the view of adding to a solidity which has so long been sufficiently established." The report of the Commons was also adverse to any legislative interference with Scotch banking.

No interference with Scotch banking took place till 1845, when Sir Robert Peel, having carried his Bank of England Charter Act and Joint Stock Banking Act with scarcely a breath of opposition, determined to regulate those of Scotland and Ireland as well. The principal provisions of this Act, Statute 1845, c. 38, are as follows:—

I. All persons had been prohibited by the Statute 1844, c. 32, from commencing to issue notes after the 6th May, 1844, in the United Kingdom, and all such persons in Scotland as were lawfully issuing their notes between the 6th May, 1844, and the 1st May, 1845, were to certify to the Commissioners of Stamps and Taxes, the name of the firm and the places where they issued such notes.

II. The Commissioners were to ascertain the average number of such bankers' notes in circulation during the year preceding the 1st May, 1845.

III. Such bankers were authorized to have in circulation an amount of notes, whose average for four weeks was not to exceed the amount thus certified by the Commissioners, together with an amount equal to the average amount of coin held by the banker during the same four weeks. Of the coin three-fourths must be gold, and one-fourth silver.

IV. In case the bank exceeds the legal amount, it is to forfeit the excess.

V. If two or more banks unite, they are authorized to have an issue of paper to the aggregate amount of issues of the separate banks, as well as the amount of the coin held by the united bank.

VI. Notes of the Bank of England not to be legal tender in Scotland.

The reader will see that there are some striking points of difference between the restraints laid upon the English and Scotch banks, for, while the former are bound down to an abso-

lute fixed limit of issue, the latter are permitted to issue to any amount, provided they hold an equal amount of coin above their authorized amount. Moreover, if any number of banks unite, they may have an aggregate authorized issue, equal to that of the separate banks; but in England, if the number of partners of the united bank exceeds six, they forfeit their power of issuing notes altogether. This absurd restriction as to the number of partners in a bank never having had any force in Scotland.

The year 1857 was remarkable for a calamity, to which there had been no precedent except the Ayr Bank, namely, the suspension of two very large joint stock banks, the Western Bank and the City of Glasgow Bank. The latter, indeed, has resumed business, and, on an investigation of its affairs, it appeared that, out of a capital of above £800,000, it had lost about £70,000; having thus a very large paid-up capital intact, it resumed business, and, we may hope that after having received this severe lesson, its business will be conducted on better principles in future. But the Western Bank was found to have lost not only the whole of its paid-up capital, £1,500,000, but nearly as much more besides. This bank was founded in 1832, so that, in the course of twenty-four years, it lost £3,000,000 of money. The Ayr Bank, in two years and a half, lost £400,000, so that, of the two, the latter is proportionably the more severe calamity. The failure of the Western Bank, however, has called forth the most bitter attacks upon the general system of Scotch banking, which we shall find to be totally unmerited, because it is clearly proved, in the evidence taken before the Committee of the House of Commons in 1858, *that during the whole course of its career, it pursued a system which was diametrically opposed to the usual course of the other Scotch banks.*

The Western Bank began business in 1832, and in the next year had a paid up capital of £209,170, which was increased year by year, till, in 1849, it amounted to £1,792,850, at which it continued till 1852, when a number of shares having fallen into the bank's hands by bankruptcy and insolvency, they were written off against the capital, which was thus reduced to £1,500,000, at which it continued till the closing of the bank. The mode of business adopted by this bank, from the beginning, was not according to the usual plan of Scotch banking, for while, as explained by the witnesses before the Committee of 1858, one very important feature of it is to keep very large reserves in London, either at their bankers, or in Government securities, the Western Bank invested its means chiefly in local accommodation, and kept very insufficient reserves in London, so much so that, in 1834, its London agents, Messrs. Loyd & Co., dishonored its drafts. It appears that upon this, the other Scotch banks refused its notes, and remonstrated with it for its mismanage-

ment. On the 30th October, 1833, the directors, in answer to these remonstrances, notified to the other banks that they had resolved to invest, in marketable securities, a sum amply sufficient to prevent such a thing happening again. They promised to commence the necessary operations in the following January, and complete them in April, if not earlier. They also engaged to lessen their discounts, and to continue to do so, in order to have sufficient funds at its command. Upon this promise of better conduct in future, the three chartered banks advanced the Western Bank £100,000 to enable them to purchase these securities forthwith. But the Western directors very soon broke their engagement, and reverted to their former mode of business. In 1838 they applied to the Board of Trade for a grant of letters patent, when a number of the other Scotch banks presented a joint memorial against it. They said that they should be wanting in their duty to the public, as well as their own constituents, if they sanctioned, by their silence, such an application:—"The fact is well known to you, that while there have occurred, during the past fifty years, periodical convulsions among the banks in England, which have led to the failure of several hundreds, Scotland has, for the most part, maintained a state of general tranquillity, and there have, in the same time, occurred only three or four failures, and those of a very minor character. The cause of this is notoriously owing, first, to the large capital employed in the Scotch banks, and second, to the system of administration adopted. Capital alone, as has been recently experienced in England, by extending the scale of operations, may only increase the mischief. In the like manner, a numerous proprietary, constituting a protection to the public against eventual loss, may, by adding to the credit, add to the power of such an institution for evil. The safeguard of the Scotch system has been the uniform practice adopted of retaining a large portion of the capital and deposits invested in Government securities, capable of being converted into money, at all times, and under all circumstances. This requires a sacrifice, because the rate of interest is small, and, in times of difficulty, the sale involves a loss, but it has given the Scotch banks absolute security, and enabled them to pass unhurt through periods of great discredit.

"It is not then unreasonable that the managers of the Scotch banks should look with favour on a system which, notwithstanding their close connection with England, has exempted them from these calamities, and, in the doubt that exists on banking theories elsewhere, it is at this moment sufficient to say that the system established in Scotland has worked well, and ought not to be disturbed there.

"The Western Bank was established in the year 1832, and the principle on which it has avowedly acted has been to employ as much as possible of its capital and assets in discounts and

loans, retaining only the cash necessary to meet its current engagements.

“As this is a more profitable investment than Government securities, there is always a strong temptation to speculative or inexperienced persons to adopt this course, and if the consequences were to affect themselves alone, it would be of small moment, but, unfortunately, in banking, this cannot be. The whole system depends upon credit, and the failure of an ill-regulated establishment, affects those differently constituted. Such a body, in prosperous times, boldly extends its business, and, from seeing the readiness with which in such seasons commercial paper is discounted, comes to the conclusion, that it is the best and most convertible description of investment that could be found.

“Prudent banks, knowing the delusive nature of this expectation, are compelled to increase their own reserve to meet the consequences of this unwise expansion; and, when the difficulty comes, they must either assist their rival to prevent an explosion, or must make a heavy sacrifice by selling their securities at a loss.

“The Western Bank, acting on this principle, allowed their London transactions to assume such an irregular shape, that their London agents, the respectable house of Jones, Loyd, and Co., took alarm, and in 1834 dishonored their drafts. The Bank of Scotland, Royal Bank, and British Linen Company were compelled to come to their assistance, and made them considerable advances. These circumstances occurring in a time when the Money Market was perfectly tranquil, shewed the extreme danger of the practice. The Edinburgh banks insisted on a better system of management being adopted, and that the Western Bank should have invested in Government securities a sum amply sufficient to meet emergencies. The Directors, after much discussion, at length, by a resolution dated 30th October, 1834, distinctly assented to the requisition, but, as they had so engaged the assets of the Bank, as to render it impossible immediately to procure the funds, the Edinburgh banks lent them £100,000 for the purpose. *For some time the Western Bank may have acted on this agreement, but the temptation of profit appears to have got the better of their prudence, and they now repudiate their engagement.*

“It will be quite apparent that a bank that can employ its whole funds in this manner, is enabled either to divide a larger share of profits than its competitors, or to do business on more favourable terms: and we repeat, that if the only consequence of this was to increase or diminish the dividends of the rival establishments, it would be of comparatively small importance, but in its result it endangers the existence of every bank in the country, and the fortunes of a large portion of the community. We feel

that, if letters patent shall be granted to this bank, after what has passed, *it will be a public sanction and countenance of a new and mischievous principle, opposed to the Banking system of Scotland.*

“The question is not, in this instance, whether Government will interpose new restraints on banking companies, but whether they will encourage a violation of the old system, by granting distinction and privileges to a company which, having pledged itself to their observance, now disowns them in its practice, and under these circumstances applies for a charter.” This memorial was signed by the Bank of Scotland, the British Linen Company, the Commercial and National Banks; and the Charter, if applied for, never was granted.

This system of keeping such small reserves in London produced the consequence foreseen in the preceding memorial. In 1847 the Western Bank was in difficulties, and received assistance from the Bank of England to the amount of £300,000 in November and December, 1847, which it repaid in March, 1848. From this time forward till 1852, when a change in the management took place, a rather more cautious course was pursued, but they did what we believe to be totally contrary to the usual practice of the other Scotch banks—they rediscounted. The following figures shew the amounts of discounts and rediscounts from 1847 to 1852:—

	Discounts.		Rediscounts.
In 1847	£15,711,438	.....	£656,077
„ 1848	12,088,643	.....	374,707
„ 1849	10,522,022	.....	249,957
„ 1850	12,048,669	.....	290,813
„ 1851	13,322,753	.....	588,247
„ 1852	13,525,332	.....	407,143

At this time the Bank had £356,000 of overdue bills, besides other very heavy locks-up of capital, in one case amounting to £120,000, which was covered with insurances on the lives of the obligants, on which it had paid £33,512 as premiums when it stopped. “But even at this time,” says Mr. Fleming, “it had a cluster of those people who had manufactured accommodation bills, doing business with them.” So that in this year, he says, the Bank was not in a satisfactory state.

In 1852 a new management commenced, and to shew how the practice of rediscounting increased, we give the following figures:

	Discounted.		Rediscounted.
In 1853	£14,987,740	.....	£1,682,320
„ 1854	18,596,704	.....	3,856,292
„ 1855	19,835,781	.....	4,969,669
„ 1856	20,410,884	.....	5,407,363
„ 1857 till Nov. 9	20,691,415	.....	4,881,221

Thus we see the enormous increase of this most perilous practice during these years, a practice which places the existence of any institution that depends upon it to any great extent, at any moment at the mercy of the will, the caprice, or any accident that may happen to the purchasers of its bills.

But this was by no means the only instance of reckless management. Over and above all the other embarrassments, there were four accounts particularly to which the subsequent calamity was due; we will shew the state of these accounts in 1852 and 1857—

1852.	Discounts. £	Overdrawn Account. £
Macdonald & Co.	107,116 —
Menteith & Co.	83,779	.... 3,523
Wallace & Co.	18,144 —
Pattison & Co.	89,678	. 1,154
	<hr/>	<hr/>
	£188,717	£4,677
	<hr/>	<hr/>

Shewing that these four firms were under obligations to the Bank in 1852 to the amount of £193,394. The following was the state of the same accounts in 1857:—

	Discounts. £	Overdrawn Account. £	Overdue. Bills. £
Macdonald	408,716	5,636	8,526
Menteith	376,799	67,635	93,129
Wallace	227,464	—	—
Pattison	336,996	67,253	11,571
	<hr/>	<hr/>	<hr/>
	£1,349,975	£135,524	£113,226
	<hr/>	<hr/>	<hr/>

Being a sum total of £1,603,725 to these four houses alone, when they failed. And, to shew the character of the bills discounted for these firms, of £402,716 bills of Macdonald's current at the time of their failure, £398,349 were dishonoured at maturity; of Menteith's, £376,699 current at their failure, £269,726 were dishonoured at maturity; of Wallace's, of £226,741 current there were dishonoured £209,534; and of Pattison's, of £336,996 current, there were dishonoured £150,749.

Soon after the general meeting of June, 1857, the directors requested another person to examine the Bank's books, who, after doing so, and allowing all the current business of the bank to be good, including the above four firms, found that bad debts to the amount of £573,000 were kept on the books as good, which, after deducting the rest and guarantee fund, amounting to £246,000, made a loss of £327,000 in the capital of the bank, and the advances to the shareholders, holding 7,626

shares in the bank, amounted to £988,487. In the month of September, 1857, Mr. Fleming, the person whom the directors had requested to assume the temporary management of the Bank, began seriously to inquire into the nature of these immense accounts, and on the 7th, the Wallaces acknowledged that they were dealing in accommodation bills, and he saw that the Macdonalds must be doing the same thing, as the two houses were drawing on the same names. It was found that the Macdonalds drew upon the 124 acceptors, only 37 of whom had been inquired about, and of these, reports on 21 were extremely bad. But there were 60 or 70 persons whom they drew upon, who made it a regular trade to accept bills for small commission; in fact, it appeared that they engaged a man in London to procure them accommodation acceptances. As soon as the true nature of these accounts was ascertained, there was no resource but to stop them. The failures of Menteith and Macdonalds, which were the first that became notorious, created a panic on the Stock Exchange on the 10th October, and the price of stock rapidly fell, it being commonly reported that the whole capital of the bank had been engaged in enabling these parties to carry on their business for a series of years. These rumours created a run on the bank, to a slight extent, on the following Tuesday, which continued for two or three days, and during that week, ending the 17th of October, the bank paid away about £36,000 in coin, but this was the only run for gold of any amount on the bank, for during the following week it only paid away £4,000, and in the week after that about £2,000, and the whole paid away in coin, between the 10th of October and the 7th November, the Saturday before it stopped, was only £44,000. But, during this period, the total *deposits* demanded were £1,280,000, and, except the sum above mentioned as paid in coin, *the whole of these deposits were paid in the bank's own notes, which were immediately taken and lodged in the other banks.*

This dreadful catastrophe deserves to be minutely detailed, because it is strenuously asserted by a very influential party, that the small note circulation of Scotland tends to increase a panic among its holders. But in this case, the bank's notes in circulation did not in any way increase the panic. Mr. Fleming says: "I may say that there was no run for the payment of notes all through. There may have been a few notes presented, but I should certainly limit the demand for gold in exchange for notes to £5,000 or £6,000. I do not think it would exceed that. *Mr. Wilson:* In point of fact, the whole pressure upon the bank at any time was in respect to its deposits, and not in respect to its circulation?—*Decidedly, there was no pressure in respect to its circulation;* so much so, that during the last two days for which the bank was in operation, I do not think £1,000 was paid away in gold at the head office. The whole

money withdrawn was taken away in notes, and the consequence was that on the afternoon of the 9th of November, when the bank stopped, there was a very large amount of notes in circulation, something about £720,000. Then the depositors became uneasy about the security of their deposits, went to the bank, and took the bank's notes?—Yes. Did they pay them immediately into other banks?—Yes. * * * * Was there much drain in the provinces upon the balances?—Not a very large amount, certainly; a wonderfully small amount, in proportion to the total deposits, was withdrawn from the country.—I think you said that at the branches there was very little demand for gold; almost none?—*Almost none.*”

At the same time, a very heavy blow fell upon them from another quarter. The bank, instead of keeping its funds well in hand in London, engaged in exchange operations with America. They had an agent in New York, though, perhaps, not openly and avowedly in that character, who granted letters of credit upon them, in favour of persons who wished to raise money, such parties arranging with the agent, the securities to be lodged to meet the bank's acceptances. These credits were not by any means always paid at maturity, but were renewed to a large extent. By this operation, a very considerable portion of the bank's funds was locked up in America, instead of being in London as they ought to have been. At the time of its suspension, its acceptances current, and its obligations to accept, amounted to £317,000, in two months' bills, which, multiplied by six, gives the amount of the year's transactions. The amount of funds locked up in America by their agent there, appears to have been £376,520, against which he held railway bonds and current bills. Mr. Fleming said, *Q.* 5510:—“It appears to me in many cases, the credits established by Lee upon the Western Bank, have been modes of raising money for the purpose of constructing American Railways, and for speculation in stocks, in New York.” “The two banks, *i. e.*, the Western and the City of Glasgow,” said Mr. Robertson, the cashier of the Royal Bank, “were in the habit of accepting four months' inland bills drawn from London, Liverpool, and Glasgow, in respect of these credits, *which was quite condemned by the Bank of England, and all the other banks in Scotland.*”

The general stoppage and failure of American credit at this time, rendered the expectations of any remittances hopeless from there. And Mr. Fleming, who undertook the duty of manager on the 15th October, told the directors it was absolutely essential to make provision for a contingent drain upon the deposit money, and also for the American acceptances becoming due. On the 17th October, the directors resolved to apply to the Bank of Scotland. On the 21st, a written application was made to that bank for assistance, and on the 23rd a meeting having been held

of all the Edinburgh banks, they declined to assist, until application had been made to the Bank of England. This application was refused. This refusal being telegraphed down to Edinburgh, a meeting of the banks was held the same evening, and they agreed to advance £500,000, on condition that the directors should dissolve and wind up the concern. After some days' negotiation, the Edinburgh banks agreed to forego the compulsory winding up, as the directors of the Western said that they had no power to do so, and advanced the money without this condition. This sum was accordingly advanced on the 29th October, on the promissory notes of the Western Bank, at six months' date, for £510,000, the terms being that the Western Bank should be bound to replace the Edinburgh banks in Consols, at the price of the day. In addition to the loan so obtained from the Edinburgh banks, the Clydesdale Bank advanced £100,000 on a note of the bank's at six months, with the individual guarantee of the directors, which was discounted at the current rate of 8 per cent.

The withdrawal of the deposits from the bank, which was almost entirely among the small depositors, had greatly abated, and, whatever might have been the ultimate result, which might have been necessitated in consequence of the examination of the bank's affairs that was then in progress, there was no *immediate* danger of a catastrophe; when, on the 29th October, the City article of the *Times* announced that the Edinburgh banks had resolved to carry the Western Bank through their difficulties, on condition that they should wind up. The *Times* reached Scotland on the morning of the 30th, and immediately a fresh pressure commenced on the bank. But this time it was of a different character from the previous one. The first pressure had been among the small depositors, the second consisted of the traders who kept large accounts, who, seeing that the Western Bank was going to close, made haste to transfer their balances to the other banks and open accounts with them, and it was this pressure which continued and made the Bank close its doors on the 9th November, *not from a demand for gold, but because the balances of these accounts being withdrawn in the bank's notes, and paid into other banks, the Western Bank was unable to provide for the purchase of Exchequer bills from the other banks, to rectify this balance by a draft on London.*

To shew how mischievous this publication of the terms proposed was, we quote from Mr. Fleming's letter to the Bank of Scotland of 31st October, 1857:—"The application made a fortnight ago by the Directors of this Bank to the other Scotch banks, for a credit to the extent of £500,000, was based on my calculation that £350,000 or £400,000 would keep our London finance in perfect order, and that the remainder would be a sufficient reserve to meet any probable withdrawal of deposits.

This calculation, I still believe, would have proved correct, *had the assistance required been given promptly, quietly, and free from any condition as to winding up.*

“But the demands made upon us have considerably exceeded my calculation, from two causes; first, the notoriety of our financial embarrassment, created by the delay in acceding to our application, and the course which the negotiations took from our having been referred to the Bank of England; and second, the condition as to winding up, which the other banks sought to impose, and the publicity given by the *Times* to this condition.

“It is not easy to say in figures to what extent these causes have respectively operated in inducing withdrawals, or to estimate to what extent they may still operate. But as to the past, my own observation here, and the reports from our branch agents, all convince me that the second has been immeasurably more mischievous than the first. *Deposits on receipts have been withdrawn to a very limited extent indeed, but balances on current accounts kept by the trading community have been removed to other banks to a considerable extent.* The reason is natural and obvious. If this Bank is to wind up, traders know that we cannot give them accommodation, and they take the earliest opportunity of arranging for that accommodation elsewhere, and withdraw their balances.

“I am hopeful that the mischief already done is not irreparable. That we retain still a measure of public confidence, is proved by the fact *that no fixed deposits of any large amount have been withdrawn, and nothing like a run has taken place, and gold has scarcely ever been demanded.*

“I have already said that there has been no demand made upon us for gold, *all sums withdrawn having been taken in our own notes, and, consequently, the other banks have got the deposits.*”

The Western Bank then asked a further loan from the Edinburgh banks, which, having been discussed for some days, was unanimously refused.

On Saturday, the 7th November, there was, from the heavy withdrawals of deposits in the Bank's notes, and their lodgment with the other banks, a heavy adverse balance on the exchange of that day. The Edinburgh banks were immediately informed that the Western Bank was unable to provide for this adverse balance on the following Monday. On the Sunday they resolved as soon as this inability to pay the balance should be declared, to instruct their agents to refuse the Western's notes. *And it was beyond all question shown that it was this injudicious line of conduct that chiefly brought on the subsequent run for gold.*

The Exchange being heavily against the Western on Saturday, it made a final proposal to the Edinburgh banks, and sent a scheme of an amalgamation with the Clydesdale Bank, to be

discussed by them on Monday morning, the 9th, and kept its doors open till 2 o'clock, to learn their final decision. This being a decided refusal to entertain the terms proposed, the Western Bank shut its doors at 2 p.m., on Monday, the 9th November. Another Bank, the City of Glasgow, it was also known, had been engaged in transactions of the same nature as the Western, in America, and had also been equally negligent in keeping due reserves in London. This bank, too, required the assistance of the Edinburgh banks, though it had been stated how much they received. On the evening of the 9th a run commenced on the saving's bank branches of this bank. "On the Tuesday morning," says Mr. J. Robertson, the manager of the Union Bank, "when the doors of the banks were opened, a great number of parties appeared with deposit receipts demanding gold; in fact, the office of our own establishment was quite filled with parties within a quarter of an hour of the opening of the doors. I think at half-past 9. The *Chairman*: You are now speaking of the Union Bank?—I am speaking of most of the banks; I speak of the Union Bank particularly. Were the Western Bank notes at that time current, or were they refused?—*They were not current, unfortunately.* Was there any deputation from Glasgow to Edinburgh on the subject of the other banks agreeing to take the Western Bank's notes?—This run, as you may call it, or panic, increased so much, that *the continued refusal of the notes of the Western Bank added very much to the excitement.* Those people who came for money would not take the notes of any bank, it did not matter what bank it was; they refused everything but gold. We thought that it would allay the excitement, if we were to take the Western Bank's notes; there being no danger of ultimate payment. We were so much impressed with that feeling, that two of the banks sent a deputation of their directors to Edinburgh to confer with the managers of the Edinburgh banks on the subject, and to induce them to rescind their order. They failed in that; the notes of the Western Bank were refused the whole day on the Tuesday."

The run of Tuesday exhausted the City of Glasgow Bank, and it did not open on the Wednesday, the 11th. The state of Glasgow was so alarming that the magistrates sent for troops, and did all in their power to allay the excitement; they issued a proclamation advising the people not to press the banks for payment, and to take the notes of all the banks. They issued an order to all the rate collectors in the city to take all notes presented to them, including those of the two suspended banks. *But the demand for gold was almost entirely confined to the depositors, very few noteholders came forward.* On Wednesday and Thursday large remittances of gold from London arrived about 10 o'clock in the morning, and were taken in

waggons to the banks, escorted by strong bodies of police. But the run entirely ceased about 2 o'clock on Wednesday. At half-past two, says the same witness, there were not half-a-dozen people in the establishment. The panic, as this witness said, only lasted one whole day and part of the next.

In fact, the refusal to take the Western Bank's notes was one of the chief causes of the run for gold; and, as soon as the other banks agreed to take them, the panic ceased. Mr. Lawrence Robertson was asked, "What was it which first caused the panic to cease?—When the stoppage of these banks took place, the other banks were not precisely informed of their position, and hesitated a little in taking their notes; after further consideration, the other banks resolved to take all the notes as they came forward, *and when that was done the thing subsided*. As soon as it became known that the notes of the Western Bank would be received by the general body of banks in Scotland, the panic, with regard to the notes of the Western Bank, came to an end?—*Entirely.*"

The same witness also said, that there was no run upon any of the Glasgow banks before the stoppage of the Western Bank. "Were those parties who drew out gold over the counter in exchange for notes, or by cheques on their deposits?—It was chiefly in the case of small deposit receipts. And not for any considerable amount?—No. Do you think that it exceeded £1,000?—It is difficult to fix upon a sum; I never looked at that. It was not of sufficient importance to call your attention to it?—No." The City of Glasgow Bank resumed payment in about a month, but the Western Bank had lost not only its whole paid up capital of £1,500,000, but as much more again.

The details of this great catastrophe well deserve our closest attention, because it is the first instance of a *banking* panic in Scotland, and even that was confined to one town. The commercial failures were confined exclusively to the herd of adventurers who had been fostered and supported by the mismanagement of the Western Bank. There was but one house of any magnitude connected with Glasgow which suspended payment during this period, Dennistoun & Co., who were more a Liverpool and London house than a Glasgow one, and whose temporary stoppage was brought about by other causes. But this calamity has been seized hold of by persons who are hostile to the Scotch system of banking in general, and also to the £1 note currency of Scotland, to condemn them. But, when we come to investigate the true facts, we shall find that they lend no support to these charges. For, with respect to the first, it is distinctly proved by the most unanswerable evidence, that from the commencement to the close of its career, the Western Bank pursued a system of business that was totally opposed to the well-recognized system of Scotch banking, and unanimously con-

demned by all the well-conducted banks. That, during its whole course, it was a subject of terror and alarm to the other banks. That its locking up its funds in America was totally condemned by the Bank of England, and all the other Scotch banks. And the Directors themselves, when, however, it was too late, acknowledged their own misconduct, for, in their first application for assistance to the Bank of Scotland, on the 21st October, 1857, the Directors say: "On the part of the board of direction, it is right that *we should frankly say, that they are fully alive to the recklessness of the past management of the Bank*; that its credit has been strained to the extreme point; and that, in the attempt to make large profits for the proprietary, unwise and undue risks have been run. Feeling all this, the Directors have entered on a course of management, which (although the present commercial crisis renders curtailment difficult of speedy accomplishment) will eventuate in the establishment, on a secure basis, of a business of a safer and a more legitimate, though certainly of a more limited description, than has for many years been conducted by the Western Bank of Scotland." *Habemus ipsos confitentes reos.* The Directors themselves acknowledged that their course of business was *not* in accordance with the usual Scotch banking system. What possible reflection, then, can it be on the recognised system that a bank, which went right in the teeth of it, failed? The very same remarks apply, only, of course, in a lesser degree, to the City of Glasgow Bank. This bank, too, was guilty of speculating in America, instead of keeping its reserves in London; and it, too, paid the penalty by a temporary suspension.

The second charge, too, is equally groundless against the small note circulation. For it is said that these small notes aggravate a panic, and that a panic is most likely to commence amongst their holders. But, in this case, the evidence most decisively negatives the supposition that any part of the panic was due to the small notes, and not only that, *but it decisively proves that the demand for gold was greatly lessened on account of the notes.* Mr. Fleming says, Q. 5532: "I may say there was no run for payments of notes all through. There may have been a few notes presented, but I should certainly limit the demand for gold in exchange for notes to £5,000 or £6,000. I do not think it would exceed that. *Mr. Wilson:* In point of fact, the whole pressure on the Bank at any time was in respect to its deposits, and not in respect to its circulation?—Decidedly; *there was no pressure in respect to its circulation*; so much so, that during the last two days for which the bank was in operation, I do not think £1,000 was paid away in gold at the head office. The whole money withdrawn was taken away in notes, and the consequence was, that on the afternoon of the 9th November, when the Bank stopped, there was a very large amount of notes in

circulation, something about £720,000. *Mr. Wilson:* Then the depositors became uneasy about the security of their deposits, went to the Bank, and took the Bank's notes?—Yes. *Mr. Wilson:* Did they pay them immediately into other banks?—Yes. *Mr. Wilson:* They thereby indirectly obtained payment through the other banks?—Precisely so; they transferred their deposits from one bank to the other. *Mr. Wilson:* Did many of the depositors demand gold?—Almost none; during the week, after the 10th October, there was a slight demand for gold, and in the country, I believe, there was a very slight demand for gold." Mr. Fleming then gave the figures, shewing that the total demand for gold during the whole month, from the 10th October to the 9th November, was only £44,000, of which more than £6,000 was in exchange for notes, but the total demand for deposits and balances on account was £1,280,000; from which it follows, of course, that the total pressure on the bank was this:—

For gold in exchange for notes	£6,000
For deposits taken in gold	38,000
For deposits and balances taken in Bank's notes	1,236,000
	£1,280,000

Now, if the Bank had not issued notes, how would this last item have been demanded? *Of course, in gold.* So that it is quite clear that the power of the Bank to issue notes saved and lessened the demand for gold to that extent. And we have already shewn that it was not any run for gold which made the Bank stop, but its inability to provide for payment of the adverse balance of exchange. But it may be said—See what followed the next morning. There was undoubtedly a run for gold next morning on some of the other banks. *But then there would have been the very same run if there had been no notes at all.* And that very run was greatly aggravated, if, indeed, it was not chiefly due to the most unfortunate decision of the other banks to refuse the Western Bank's notes. *As soon as the other banks agreed to take the Western's notes, the panic immediately subsided, even though a second bank stopped the same morning.* Now, what is the effect we might naturally have expected from a second bank's stopping in the midst of a panic? Clearly that that panic would have been greatly intensified. But in this case it was not so. The City Bank did not open on the Wednesday morning, and yet the whole panic was over by two o'clock that day. The whole demand on the Royal Bank for gold did not exceed £1,000.

Now, without prejudging the question in any way, whether

the Scotch £1 notes should be suppressed, there is no dispassionate man who can, after reading the details of this crisis, come to the conclusion that they had anything whatever to do with this panic. The great wonder is, that after the unprecedented circumstance of two great banks stopping payment, the panic was so short, and so slight as it was. Does any man who knows London think that, if a similar case had happened there, the consequences would have been so comparatively trifling? The two London banks of most nearly equal magnitude with the Glasgow ones that stopped, are the Union and the London and County. Let us imagine that the Union Bank of London was to stop payment, and two days after the London and County. Does any man who knows London suppose that in such a case the panic would be limited to one day and a half? No man in his senses would think so.

Nor can there, we think, be any reasonable doubt that the refusal of the Edinburgh banks to take the notes of the Western Bank was a most unfortunate one. When the Ayr Bank failed, all the other banks immediately gave notice that they would take its notes at par, because they knew very well that its proprietors were perfectly well able to discharge all the claims upon them. It was perfectly well known that the proprietors of the Western Bank were worth many millions of money, and that there was no possible danger of any ultimate loss. Yet the banks on this occasion decided to refuse their notes, which decision they were afterwards obliged to rescind. And this is a very good proof that it was wrong from the first; and immediately that the notes were taken the panic ceased.

In the years of the great speculations in railways, numbers of persons wished to carry on the game of speculation by buying shares, and then raising money upon them from bankers. The old banks prudently declined this sort of business, and a number of banks were got up, principally for this business—if, indeed, it can be called business at all—as it was, in fact, pure gambling. After a short time, the railway shares went down as fast as they had risen, and all these banks, which were called Exchange Banks, were ruined, some of them under the most disastrous circumstances.

We have said that one of the principal features of the Scotch banking system is to have a small number of very large banks, with a great number of branches to each. To shew how the system has a natural tendency to become concentrated among a few great establishments, we may compare the existing number of separate institutions, at different periods. In 1826, there were 32 independent banks, of which 13 had less than 10 partners, 10 had less than 100, and the remaining 9 had more than 100. Fourteen of these had no branches, 17 had not more branches than 5, and the highest number that any bank had was 30, which

was the Commercial Bank. The total number of offices was 159. In 1848, there were 391 branches; in 1855, there were 462 branches, and 17 principal offices; in 1857, there were the same number of head offices, with 666 branches; and in 1859, there are 14 separate banks—one, the Union, having 4 head offices—and 597 branches, making, altogether, 615 offices.

The following table exhibits the banks at present existing in Scotland:—

Year.	Name.	Paid-up Capital.	Authorized Circulation.	Average Circulation, 1864-5.	Coin, 1864-5.	No. of Branches.
		£	£	£	£	
1695	Bank of Scotland - -	1,000,000	300,485	493,078	286,174	60
1727	Royal Bank - - -	2,000,000	183,000	534,717	397,555	74
1746	British Linen Company -	1,000,000	438,024	489,625	251,185	52
1810	Commercial Bank - -	1,000,000	374,880	555,227	286,973	76
1825	National Bank - - -	1,000,000	297,024	472,094	259,500	72
1830	Union Bank - - -	1,000,000	454,346	582,421	235,745	103
1825	Aberdeen T. & C. Bank -	156,000	70,133	143,350	87,218	31
1836	North of Scotland Bank -	280,000	154,319	217,914	88,228	34
1838	Clydesdale Bank - - -	900,000	274,321	373,026	151,395	60
1839	City of Glasgow Bank -	870,000	72,921	364,249	330,360	94
1838	Caledonian Bank - - -	125,000	53,434	74,112	33,300	16
1834	Central Bank - - -	100,000	42,933	61,443	29,949	9



CHAPTER VII.



RISE AND PROGRESS OF BANKING
IN ENGLAND.



CHAPTER VII.

ON THE RISE AND PROGRESS OF BANKING IN ENGLAND UNTIL THE RENEWAL OF THE BANK CHARTER IN 1800.

ORIGIN OF BANKING IN ENGLAND—SEIZURE OF THE MERCHANTS' MONEY IN THE TOWER BY CHARLES I.—SHUTTING UP OF THE EXCHEQUER BY CHARLES II.—FOUNDATION OF THE BANK OF ENGLAND BY WILLIAM III.—GREAT MONETARY CRISIS IN 1696-7—PROGRESS OF THE BANK—GREAT MONETARY CRISIS IN 1793—SUSPENSION OF CASH PAYMENTS IN 1797—RENEWAL OF THE CHARTER IN 1800.

1. Banking, in the modern sense of the word, had no existence in England before the year 1640. Up to that period merchants had been, for a considerable time, in the habit of depositing their bullion and cash in the Mint in the Tower, for convenience and security, under the guardianship of the Crown. Eleven years had elapsed since Charles I. had dissolved his third Parliament,—eleven years crowded with incidents of the deepest interest in the history of the human race. The King and the Parliament parted with feelings of mutual exasperation, and the Monarch gave very plain intimation that henceforth he meant to have no more of them. From that time he and the great apostate, Strafford, were engaged in a deliberate and systematic attempt to establish an absolute despotism on the overthrow of the ancient constitution of England. For a little while the King was triumphant—wicked judges decided against Hampden. Laud established an Anglican popedom on the banks of the Thames. Everything seemed to favor the design, and, humanly speaking, there is every probability that the eminent ability of Strafford would have been ultimately successful, when an incident occurred which destroyed the labors of so many years, and was the moving cause of a train of consequences which ended in the destruction of the monarchy and the church. The republican constitution of the Scottish church was an object of hereditary antipathy to the King; and his advisers, with that suicidal intemperance which is the invariable characteristic of ecclesiastical despots, thought that the time had now come to force a prelatie liturgy upon the nation. The Scotch, with fierce determination rushed to arms in defence of their ecclesiastical liberty, and the King did not hesitate to accept the alternative of civil war.

2. After some indecisive skirmishing, a treaty was at length agreed upon, probably with little sincerity on either side. But

an accommodation of some sort was then an absolute necessity to the King. His first army had exhausted his scanty and ill-managed exchequer. It had cost him £300,000; not only all the money that had been laid up was wasted, but the revenue had been anticipated. The enemy were proud and insolent, the army corrupt and disheartened, the country mutinous and inclined to the rebels, and the Court, according to Clarendon, were all three. The speculation that went on would be something incredible if it was not said on such excellent authority. The King thought he might rob every one else, so the officers of the revenue thought they had an unlimited licence of robbing him; of the sum of £200,000 raised from the people only £1,600 reached the Exchequer. The King was in despair, when he happened to intercept a treasonable correspondence between the Scotch and the King of France. At length, he thought, he might venture to call a Parliament. The English nation would surely be roused to indignation at such flagrant treachery.

3. The writs were issued in December, 1639, for the Parliament to meet on the 13th April, 1640. Notwithstanding the national exasperation at the proceedings of the King during the preceding twelve years—notwithstanding, that by way of bravado, and to induce people to believe that the Parliament was called entirely through the King's grace and good will, and not through necessity, ship money was levied with the same severity, and the ecclesiastical courts maintained their usual cruelty—the nation were sincerely anxious for peace and moderation. Under the influence of these feelings they returned a House of Commons, wishful to reform abuses, but composed of persons free from party engagements, afraid of all violence, secret combinations, or doing anything to hazard the peace of the country. Clarendon bears testimony that there was not the least approach to any irreverence to the Crown, that it managed all its debates and behaviour with wonderful order and sobriety, that it was exceedingly well-disposed to please the King, and to do him service. In a debate on a case where the Lords had undoubtedly committed a gross breach of the privileges of the House, there was not an angry or offensive word spoken, and when an obscure member made a sneering remark upon the bishops, he met with no encouragement.

4. But the evil genius of the King prevailed. The unhappy Monarch, utterly unconscious of the momentous nature of the problem which was in course of solution, quarrelled with the Parliament which was his last hope of salvation. In a fit of indignation that it did not instantly submit to his haughty demands, and vote an enormous supply with the readiness of eastern slaves, he dissolved it within three weeks of its meeting,

without having passed a single Act; to the profound grief and despondency of all who were anxious for peace—to the gloomy delight of those sterner spirits whose souls thirsted for vengeance for the tyranny of years. No sooner was the deed done, than he was seized with alarm and regret, and endeavoured to recall it, but it was too late. No supplies had been voted, but an invasion was imminent, and he was driven to devise expedients for raising money. He opened a voluntary loan, and in less than three weeks £300,000 were paid into the Exchequer, chiefly by the Catholics. But this was quite inadequate to his necessities, and he resorted to other more discreditable means of raising money. He bought up an immense quantity of pepper from the merchants on credit, and immediately sold it at a heavy loss for ready money. It was debated for several days at his council to coin £300,000 of base money, with 3d. of silver in the shilling, but the plan was finally rejected owing to the speech of Sir Thomas Rowe, a noble argument, which might have been studied with advantage nearly two centuries later. Besides this, the King seized the merchants' bullion and cash in the Tower, to the amount of £120,000.

5. The merchants were in consternation, as this cash was the provision they had made to meet their bills. They immediately met, and drew up and presented the strongest remonstrance to the Council. They pointed out the flagrant iniquity and impolicy of such a proceeding, and after the matter had been debated a whole day at the Council, they finally agreed to let the King have £40,000, upon receiving adequate security for its repayment with interest. The security was given, and the whole of the principal and interest was ultimately repaid to them. But, although they had succeeded in this instance in saving their property, the prestige of the Royal honor was gone, they were too wise to trust their money again to such precarious custody, and they were obliged to keep it at home under the care of their own clerks and apprentices.

6. But their treasures were no safer than before. The plebeian cashiers were more dishonest than the King. In process of time, as the war went on, these gentlemen of the quill were seized with a martial ardour; they deserted their desks in multitudes to join the army, and carried off with them their masters' cash. Others lent out their masters' money clandestinely to the goldsmiths at interest at 4d. per cent. per diem, which they kept to themselves. The goldsmiths, as might be expected from their business, had acuter perceptions with respect to the value of the bullion in the coin than the public generally. The money coined during the commotions was of very unequal weight, sometimes as much as 3d. difference in the ounce, and most of it heavier

than it ought to have been, according to the relative value of the metals abroad. The goldsmiths did, what always will be done under such circumstances, they bought up all the heaviest coins, and melted them for exportation. Moreover, they began to lend out at interest the money that thus came into their hands. They advanced great quantities of money to merchants, and others, weekly or monthly, at high interest, and began to discount their bills. Finding this to be very profitable, they began to attract deposits to themselves, by offering interest for them, and allowing the depositors to have repayment whenever they pleased. People found it much more convenient to leave their money with the goldsmiths, where they could have it whenever they pleased, as well as their interest, than to lend it out on real or personal security. They soon received the rents of all the gentlemen's estates, which were transmitted to town. Five or six stood pre-eminent above their brethren, and Clarendon says that they were men known to be so rich and of so good reputation, that all the money of the kingdom would be trusted or deposited in their hands. *And they then first came to be called BANKERS.*

7. Their command of ready money soon brought them a much higher customer than the merchants. Notwithstanding the fame and the strength of the Protector's Government, and his unquestionable sincerity in wishing to govern with free parliaments, he and they were unable to agree any better than his Royal predecessor had done with them. They were jealous of his power, and kept him in a constant state of financial embarrassment. He then applied to the "Bankers" and they advanced him money in anticipation of the supplies. They thus became almost necessary to the Government.

8. The position the bankers had gained under the frugal government of Cromwell was not lost under that of his dissolute successor. The first care of the restored Monarch was to disband the terrible Republican armies. But they required to be paid off, and some hundreds of thousands of pounds were required to be got together in a few days. The slow receipts of the taxes were quite inadequate to effect this, and the Ministers were compelled to have recourse to the bankers, and they were so well satisfied at their proceedings that they declared the King's affairs could not be carried on without their assistance.

9. Their method of doing business with the Crown was as follows. As soon as the supplies were granted, they were sent for to attend the King. He, having consulted his Ministers as to what immediate sums were required, desired them to be called in, and they were then informed what ready money would require to be provided by such a day. They were then asked

how much they could lend, and what security they would require. Each answered according to his several ability, for there was no joint stock among them, one perhaps £100,000, another more, another less. They were desirous of having 8 per cent. for their money, which the King and his Ministers were quite ready to give, as a reasonable remuneration; but, upon further consideration, they determined to leave it to the King's own bounty, lest it might afterwards be turned to their disadvantage, mentioning, at the same time, that they themselves paid 6 per cent. for it to their customers, which was known to be true.

10. They then received an assignment for the payment of the first money that came in under the Act of Parliament, or tallies upon such other branches of the revenue as were least charged. But even this was no security, as the King and treasurer might divert these payments to other purposes. "Therefore," says Clarendon, "there was nothing surer than that it was nothing but the unquestionable confidence in the King's justice and the treasurer's honor and integrity, which was the true foundation of that credit which supplied the necessities of the Government. The King always treated them very graciously as his very good servants, and all his ministers looked upon them as very honest men." We shall soon see how their confidence in the King's honour was repaid.

11. It belongs to the general historian to relate the terrible downfall of England's greatness in eight years from the death of Cromwell. The year 1667 may be considered as the nadir of the national humiliation. For the first, and, we may devoutly trust with Macaulay, for the last time, the citizens of London heard the sound of hostile cannon. With extraordinary infatuation the Government rushed into a war with Holland, whose capital had illuminated when the news arrived of the death of their terrible antagonist, Cromwell, and little boys ran about the streets, crying that the devil was dead. Notwithstanding the unexampled magnitude of the supplies voted by Parliament, they were all embezzled by the courtiers, who made fortunes while the sailors mutinied for want of pay, and the ships were unseaworthy. The Dutch destroyed Sheerness and Chatham, burned the ships lying there, and insulted Tilbury.

12. Nothing could be more disgraceful and humiliating than the misconduct which led to this disaster, but the wild despair, and ridiculous consternation, that took possession of the people of London when they heard of it. The King alone, who never wanted personal courage, and the Duke of York, kept their composure, and put to shame the cowardice of a general officer, who thought himself one of the greatest soldiers in Europe,

who declared the Tower not to be tenable, and refused to defend it. Every one, in consternation, rushed to demand his money from the bankers. It was known that they had lent it to the King, and the people believed that the regular payments out of the Exchequer could not be made. To quiet the public alarm, the King, on the 18th June, issued a proclamation to say that the payments of the Exchequer would continue as usual, and stating that it was his steadfast resolution to preserve inviolable to all his creditors all the securities and assignments made for repayment of their advances; that he would not upon any occasion whatever permit any alteration or interruption of these securities. He moreover said that he held this resolution firm and sacred in all future assignments and securities to be granted by him upon any other advance of money for his service, by any persons on any future occasion.

13. The insults and ravages of the Dutch were annoying and disagreeable, but they were inflicted by a brave enemy. Charles II., and his Ministers, plunged the nation into depths of disgrace a thousand times more humiliating. He sold himself, his country, her honour and greatness to the King of France, and for 29 years England suffered an eclipse in European politics. The public indignation at the ravages of the Dutch, demanded a scapegoat, and it was appeased by the ruin of Clarendon. Soon afterwards the King astonished and delighted the nation by entering into the Triple Alliance with the very people he had so lately been at war with, and Sweden. It was ostensibly to curb the overweening ascendancy of France, and to maintain the Protestant religion. While thus reaping popularity at home and respect abroad for this unwonted display of firmness and magnanimity, which revived the memory of Cromwell, the infamous traitor signed a secret treaty with Louis binding himself to re-establish the Roman Catholic religion in England, to unite with him, and destroy the very people with whom he was so ostentatiously in alliance. Bad as the Cabal Ministry were, the indelible infamy of this transaction was peculiarly personal to the King. He himself went to Dover to negotiate it; it was he who suggested the most disgraceful articles, and, abandoned as the Ministry were, he thought only two of them sufficiently wicked to be entrusted with their knowledge. The treaty was signed in May, 1670.

14. It was impossible to prevent some hints of what was going on reaching Holland. De Witt and the States took alarm at the recall of Temple, whose character for honour and integrity stood so high that his presence was considered a sufficient guarantee of the fidelity of England. The King ordered him to leave his family at the Hague, and promised his speedy return. Parlia-

ment met in October. The King left the Lord Keeper to explain his views to them. The Keeper expatiated upon the King's pleasure in meeting his Parliament, the immense growth of the power and navy of the King of France, the King's alliance with the Dutch, the neglected and feeble state of the navy, and the necessity of putting it in a position to cope with that of France. He ended by demanding a supply of £800,000 to fit out 50 ships of the line, to make him a match for his neighbours. The House eagerly voted him the supply asked for, and added to it a long homily upon the growth of Popery, and earnestly petitioned the King to take measures to suppress it. The King took the subsidy, instantly prorogued the Parliament, and, with the treaty of Dover in his pocket, published a severe proclamation against Papists, boasting that he had always adhered to the true religion as established against all temptation whatever.

15. No sooner were the credulous Commons duped out of their money and dismissed, than the King set to work to pick a quarrel with the Dutch. They were wantonly provoked by a most outrageous insult. A small yacht, not even a man-of-war, was ordered to sail through their whole fleet on their own coasts, and fire upon them if they did not strike their flag to it. The Dutch, who tendered any explanation that the English Government chose to dictate, were studiously insulted. Parliament was prevented from meeting lest they should declare against such atrocious proceedings; but the money of which they had been duped was soon exhausted by debts and expenses. France had promised to pay £200,000 a-year during the war, a sum, however, quite inadequate to maintain the navy. The axe of Charles I. inspired the King and his Ministry with too wholesome a respect for the English nation to venture again upon ship money. In this dilemma the King declared that the staff of the treasurer should reward the ingenuity of the man who should discover an expedient for "raising the wind." Shaftesbury is said to have the merit of originating the idea, but Clifford reaped the profit and the honour. The expedient hit upon was to shut up the Exchequer.

16. Charles seemed to be most at home in the lowest depth of iniquity. With the treaty of Dover in one pocket, he professed a warm zeal for the Protestant religion; with his proclamation of 1667 in the other, he seized upon the bankers' money in the Exchequer. When he had performed the splendid feat of duping his Parliament out of £800,000, for the purpose of cutting the throats of the very people to whom they were most attached, it was but sorry game to plunder a few bankers. Nevertheless, the King was so delighted with the peculiar perfidy of the transaction, that, to the promised reward of the

treasurer's staff, he superadded an ignominious peerage. On the 2nd of January, 1672, appeared a proclamation, stating that the payments out of the Exchequer should be suspended for one year; but interest at the rate of 6 per cent. was promised. The King seized £1,328,526; of this sum £416,725 belonged to Sir Robert Vyner alone.

17. The bankers, it is true, were not many, but the money they had belonged in great part to their customers, and these were 10,000. The *coup de finance* was so cleverly done that no one, except one or two of the most intimate friends of the conspirators, had the slightest warning. The consternation was dreadful in the City. Numberless merchants were ruined. The distress was felt through all ranks of society. Widows and orphans, who had no other means of investment, had lent their all to the bankers. Many persons went mad; many died of a broken heart; many destroyed themselves. It was at first promised that the suspension should only be for a year; but year after year passed away, and neither the principal nor the interest was paid. But the intensity of the public suffering was too great, and the public indignation was too fierce to be neglected. What seems to be a most extraordinary circumstance is, that although so many persons of influence must have been injured by the transaction, there was no notice of it taken in Parliament. At length, in April, 1676, the King was obliged to order the accounts of the creditors to be examined by the Chancellor of the Exchequer. This having been done, in April, 1677, the King issued letters patent, granting to each of the goldsmiths, their heirs and assigns, and for the benefit of their creditors, in lieu and satisfaction of their debts, a yearly rent, part of the hereditary excise, equal to 6 per cent. upon the debt, with a clause of redemption, upon the King paying the principal and arrears of interest. These letters were printed and made public on the 23rd of May, 1677, and a bill to ratify them was passed by the House of Lords, on the 10th July, 1678, but, unfortunately, was not presented to the Commons before the end of the Session, and never became law.

18. The interest continued to be paid till Lady-day, 1683, when it ceased. Those were times of fiery trial. The recoil of the crimes and cruelty of the Popish plot had struck down the fomentors of that horrible delusion. The blood of the hostile parties alternately flowed like water from the sea-flood. The Royalists had obtained the undisputed ascendancy, and payment of the interest due to the bankers immediately ceased. None was paid during the reign of James II. At length, in 1689, when the creditors were worn out with despair, some of them determined to petition the Court of Exchequer to make an order

for payment of their claims. The Crown determined to resist payment, and the case was argued at great length; two years were occupied in the arguments and the deliberations of the judges. At length, in 1691, the Court gave judgment in favor of the petitioners, and made an order on the Exchequer for payment. The Court appealed to the Exchequer Chamber. At that time the Lord Chancellor, or the Keeper of the Great Seal, sat in the Exchequer Chamber, and was accustomed to receive the assistance of all the Common Law Judges. Lord Somers was Keeper of the Great Seal. In 1697, the case was argued before the whole of the Judges. There were two points to be decided. 1. Whether the letters patent were good and valid to bind the Crown. 2. Whether the remedy taken by the petitioners was the proper one, and if it was in the power of the Court of Exchequer to order payment from the Treasury of the sums due to the claimants. On the first point the Common Law Judges unanimously held that the letters patent were good and valid to bind the Crown. On the second point they all, with one exception, held that the petitioners had adopted the proper course in petitioning the Exchequer, and that that Court had power to order payment. The Chief Justice of the Common Pleas alone held that they had not adopted the right remedy; that the Court of Exchequer had no power to order payments out of the treasury; and that the claimants ought to have petitioned the King himself. The assistant Judges having thus all delivered their opinions, the case remained for the final judgment of Lord Somers. It is one of the most famous cases in Westminster Hall. The Lord Keeper is said to have expended several hundred pounds in collecting books and pamphlets for his judgment. He carefully abstained from pronouncing any opinion as to whether the grant was good, and bound the Crown; but, after going over all the precedents with extraordinary care and minuteness, and reviewing the history and powers of the Court of Exchequer, he held that the petitioners had adopted a wrong remedy, and that the Court had no power to order payment as it had done. It was doubtful whether the Keeper of the Great Seal had power to give the judgment of the Court against the opinion of the majority of the assisting Judges. Three Judges held that he had not this power, but seven held that he had; he accordingly reversed the judgment of the Court of Exchequer.

19. Under such circumstances, it was scandalous and disgraceful in the Crown to contest the matter any longer. Every one affirmed the case; the objection was purely technical. The claimants appealed to the House of Lords; the Crown persisted in a strenuous and disgraceful opposition, but, on the 23rd January, 1700, the Lords finally gave judgment in favour of the

bankers, and reversed the judgment of Lord Somers. One would have thought, that after such aggravated wrong and injustice, the Parliament would have hastened to repair the injury done to these unfortunate men. But the strangest part of the case is yet to come. The judgment of the Court clearly established their right to all arrears of interest; but they were not paid one farthing of it. An Act was passed in 1700, that after the 26th December, 1701, the hereditary excise should be charged with interest at the rate of 3 per cent. on the principal, until payment was made of one-half of the debt. Thus ended this monstrous iniquity. The principal never was repaid, but was afterwards consolidated with the South Sea Annuities, and still forms part of the National Debt. It has been calculated that the loss to the bankers and their creditors, from arrears of interest and retention of the principal, was nearly three millions, to say nothing of the frightful expenses of such protracted litigation.

20. Notwithstanding the political agitation of the period, and the vice and extravagance of the Court, the nation, from the sheer force of its energy, continued to thrive and progress as soon as it attained a tolerably settled condition, but the want of an adequate supply of circulating medium was felt severely to cramp the operations of trade, and many persons who understood the great benefits which foreign countries derived from the establishment of banks, attempted to induce the Government to erect similar institutions. A great number of projects were started in print, some of particularly magnificent dimensions, but, as none of them came to anything, we need not be delayed by them any further.

21. The troubled, but glorious era of 1688, not only destroyed public credit, but, as was natural, diminished the productiveness of the taxes, and the new Government were obliged to purchase popularity by abolishing the hearth tax. The tonnage and poundage, which in the reign of James II. produced £600,000, fell in 1693, to £286,687, and, notwithstanding some additional taxes were laid on, the whole revenue in 1693, was £1,510,318. Such an income was wholly inadequate to sustain the feeble and unsettled Government, and the most extensive frauds and robberies prevailed among the public officers. Some of these frauds were brought to light, and the offenders punished; but, though commissioners were appointed for the purpose of discovering the defaulters, the Commons resolved, in 1701: "That it was notorious that many millions of money had been given to his Majesty for the service of the public, which remain yet unaccounted for." It was alleged, that in five years, the almost incredible sum of nearly eleven millions was thus embezzled.

22. The chief object which tempted William's ambition to obtain the Crown of England, was to head the great European alliance against the overwhelming power of France. No sooner was the King pretty firm on his throne than he persuaded the Parliament to agree to a war with their ancient enemies. The Parliament was eager for the war, and readily voted supplies, but they were scarce and difficult to be got. The Government, at first, attempted to persevere in the old plan of mortgaging the grants to be voted by Parliament. Their attempts, however, were not very successful; and, in 1690, Parliament began the system of allowing money to be raised on short annuities, which was attended with good success. The increasing expenses of the war, however, rendered this plan too burdensome, and in 1692 a plan was brought forward for raising duties for the space of 99 years, to pay the interest of an intended loan of £1,000,000 upon a tontine scheme. The subscribers were to receive 10 per cent. till 1700, and after that, £7,000 per annum was to be divided among the survivors till their number was reduced to seven, when, upon the death of each, his annuity was to lapse to the Crown. So low was the credit of the Government that only £108,100 was obtained on these tempting terms, and a clause was introduced by which the subscribers might obtain 14 per cent. upon any life they chose to nominate. But even these two schemes produced only £881,493.

23. All these devices, however, failed in producing an adequate supply of money to support the war, which languished in consequence. The fatal proceedings of Charles II. seem to have ruined the bankers, or, at least, to have deterred them from making advances to Government in their former style. The Government were obliged to revert to the humiliating plan of borrowing from every one in the city they could. They were obliged to solicit the Common Council of London for so small a sum as £100,000, and if they granted it, the Councilmen had to make humble suit to the inhabitants of their respective wards, going from house to house for contributions, and for these advances they had to pay, in premiums, discount, and commission, from 30 to 40 per cent.

24. The unhappy bankers, and their assigns, had, in despair of having their rights acknowledged by the Crown voluntarily, been driven into a court of law. Some of them, however, endeavoured to come to an agreement with the Crown. When it tried to raise money by way of perpetual annuities in 1691, they thought that they might make terms for themselves. On the 18th January, 1692, their proposal was submitted to the House. They said that whereas the debt due to the bankers, and their assigns, was above £1,340,000 principal, with 8 $\frac{1}{4}$ years'

arrears of interest, at 6 per cent. at Christmas, 1691, they proposed to forego all arrears of interest, and to advance a sum equal to their principal, on condition that interest at the rate of 6 per cent. should be secured to them by Act of Parliament. This proposal was subscribed by six or seven gentlemen whose principal money amounted to £29,378; several members of the House, whose principal was £5,400, immediately declared their willingness to accept the same proposals. They believed that most of the others interested would come into the same arrangement. After a few days' delay, persons whose principal amounted to £39,775 came into the proposal. Those who agreed to these proposals were chiefly the assigns of the bankers and their creditors. The bankers themselves declined to join in the arrangement, for fear it might prejudice their case in the Exchequer. When the Committee who brought up this report to the House first met, a proposal was made to them, that certain parties were ready to subscribe a million, on condition of receiving £65,000 a year, of which £5,000 was to be for management, and the rest for interest, and that their bills of property or stock should have a forced currency, or be made legal tender, in which case they offered to advance £200,000 in cash, to be ready as a bank to exchange such current bills as should be demanded of them, to give them credit, and support their circulation, and that they should receive 5 per cent. on that sum. This scheme was devised by Mr. William Paterson, and supported by several wealthy merchants in the city. The Committee declined to receive the proposal for giving a forced currency to this stock, but they were quite willing to receive such a plan, and make the stock transferable at pleasure. The proposal broke off upon this difference. Paterson and some of his friends were willing to waive the forced currency of the stock, but nothing came of it. Such was the first effort of Paterson to found a National Bank. After this failure, no further proposal was made till the beginning of 1694, when the increasing public necessities made the Ministry attempt to start another such project. They sent for Paterson, and requested him to organize another plan. His second project was to raise a capital of £2,000,000 at 7 per cent. interest. His influence obtained forty men to subscribe £5,000 each, as a fund to circulate £1,000,000 at 8 per cent. The Lords of the Treasury, however, who were accustomed to allow 40 per cent. discount on tallies at 8 per cent. interest, which had but four or five years to run, could not be persuaded that persons would subscribe at par to a fund which had no positive determination. This plan underwent several modifications, but they all failed, and a lottery was started to supply the deficiency, which was equally abortive. Not discouraged by the failure of all these attempts, he persevered, and formed another project, which was to raise and circulate £1,200,000 upon a fund of

£100,000 a-year. Some party jealousy came at the opportune moment to assist Paterson. Mr. Michael Godfrey, brother to Sir Edmundbury Godfrey, and some persons who were nettled with some transactions with the East India Company, now took Paterson up, and in effect supplanted him; for, though he continued to advise and assist in the direction of the measure, Godfrey stood foremost in it, and was considered both by the ministers and the Parliament as the efficient man, on whom all depended, and to whom all acknowledgments were to be paid.

25. This scheme at last succeeded; after the details had been settled in concert with the Ministers, it was brought before the Privy Council, and long and anxiously discussed in the presence of the Queen, and at last the Statute 1694, c. 20, was passed, by which the Bank of England was established.

26. Few things can be more surprising than that a system which had been in operation for centuries in Italy, and which had conducted so much to the stability, nay, almost to the existence of several of the Italian Governments, had not been thought of in England before this time. Such, however, was the case. Before the Bank of England there is no instance of any but a commercial State having adopted such a measure. Perhaps it was, that in no State but a commercial one was there to be found such a degree of monetary honour, as to induce people to lend their funds upon perpetual annuities upon the security of the Royal word. The debt created by the establishment of the Bank of England was the first attempt in England to raise money by way of perpetual annuities, and it did not take place until the chief power in the State had finally passed away from the Crown to the Parliament. Only thirteen years after the revolution the King, in his speech to Parliament 30th December, 1701, presses the House of Commons to take care of the public credit, "which," he says, "cannot be preserved but by keeping sacred that maxim, that they shall never be losers who trust to a parliamentary security." How different from the sentiments of preceding monarchs!

27. The Act, Statute 1694, c. 20, incorporating the Bank of England, received the Royal assent on the 25th April, 1694, and its chief provisions are as follows:—

1. After providing for raising certain taxes mentioned in the Act, it directed that the sum of £100,000 a year should be appropriated to the encouragement of persons making a voluntary loan of £1,200,000 for the purpose of carrying on the war with France, in the following manner:—

2. The Crown might appoint commissioners, to receive subscriptions for the sum of £1,200,000, before the 1st August, 1694,

from any person, native or foreign, bodies politic or corporate, to be paid into the Exchequer, and the said sum of £100,000 per annum was set apart to be paid to the use of the subscribers, their heirs, successors, or assigns.

3. The Crown was empowered to authorize, by letters patent, the subscribers to the loan to assign and transfer their stock and interest, and to prescribe the manner of doing so, and to erect them into a corporation, to be called the Governor and Company of the Bank of England, with all the usual privileges of a corporation, together with the power to acquire and hold lands, rents, tenements, and hereditaments of all descriptions, in as full a manner as any private individual, subject to a proviso of redemption.

4. That in case the whole sum of £1,200,000 should not be paid into the Exchequer by the 1st January, 1695, then the payment to the subscribers should only be at the rate of 8 per cent. on the sum advanced; and that at any time after the 1st August, 1705, upon Parliament giving twelve months' notice, and repaying the whole of the debt due, the Corporation should cease and determine.

5. No single person was to subscribe more than £20,000, and one-fourth was to be paid down at the time of subscription, and the remainder before the 1st January, 1695; in case of non-payment of the remainder, the first instalment to be forfeited to the Crown.

6. Unless at least one-half the capital was subscribed before the 1st of August, the subscribers were not to be made a corporation, but those who had subscribed might transfer their stock annuities as individual creditors of the Crown.

7. The corporation was strictly forbidden to borrow or give security by bill, bond, covenant, or agreement under their common seal, for any sums exceeding £1,200,000, except they were allowed to do so by Act of Parliament. In case they exceeded this limit, the proprietors were to be liable in their private capacities.

8. The corporation were allowed to deal in bills of exchange, to buy or sell bullion, gold, and silver, to lend money on the security of goods and wares, and merchandize, and if the loan was not repaid within three months of the time agreed upon, to sell such goods; and to sell goods, the produce of their own lands.

9. But they were strictly forbidden, either directly or indirectly, to deal or trade, or to permit any one on their behalf to deal or trade with any of the money, stock, or effects of the corporation, in buying or selling any goods, wares, or merchandize, under the penalty of forfeiting treble the value of the goods to any common informer.

10. All the bills obligatory, and of credit, under the seal of

the corporation made or given to any person, might, by indorsement of such person, be freely assigned to any person who should voluntarily accept them, and so by such assignees *toties quoties*, by indorsement thereon, and all such assignees might sue therein in their own names.

11. That if the corporation should purchase any Crown lands, or advance any money to the Crown whatever, except by the special permission of Parliament, they should forfeit treble the value of all such advances, one-fifth to any common informer, and the remainder to the public.

12. All fines, amerciaments, and judgments received against the corporation might be paid by the officers of the revenue, out of the annuity of £100,000.

In pursuance of this Act, a commission to receive subscriptions was nominated on the 15th of June, the whole stock was subscribed for in 10 days, and the Charter of Incorporation was issued on the 27th July.

28. This great experiment was regarded with some doubt and misgiving even by its zealous supporters; they feared it could hardly be successful with so moderate an interest as 8 per cent. But several very numerous classes of people regarded it with the utmost detestation. The usurers, whose inordinate gains were checked, were filled with rage. Some said that it would become a gigantic monopoly, engross all the money in the kingdom to itself, and combine with the King to set up a despotism. Some inveighed against its granting interest, which they said would draw money away from trade, not perceiving, in the blindness of their passion, that if the Bank allowed interest to its customers, it must advance money to traders to make it. Some became extremely zealous for the morals of the nation, which were to be placed in imminent peril by the new bank. Some pretended to dislike it for fear it should disappoint the King in the expected supplies. The domestic enemies of the Government were furious against it, because they saw how enormously it would strengthen the new dynasty.

29. The immense benefit which accrued to the State by the establishment of the Bank, was shewn by the increased vigor with which the war was carried on. The army assumed the offensive, and in July, 1695, the King undertook the siege of Namur. At this time Mr. Michael Godfrey, the Deputy-Governor of the Bank, went over to Namur to arrange with the King as to the manner in which the money for the use of the army should be remitted. In the last days of July he ventured too near the town to speak to the King during a heavy cannonade, and was killed at his side. Previously to this he had published

a pamphlet on the subject of the Bank, which is of great historical importance with regard to the currency. It is written in a strain of the warmest congratulation upon the great success of the experiment, which he had taken so leading a part in forwarding. He states that, whereas in the beginning of 1694, the Government tallies were at a discount of £25 to £30 per cent., in addition to the public interest, the Bank took them at par, and from the former heavy discount they had risen to a premium, so that they were then better than money, because there was 7 or 8 per cent. per annum benefit while they were kept, which never could have been done without the Bank. He said that those who lodged their money at the Bank had it as much at their disposal as if it were in the hands of the goldsmiths, or in their cash chest, and he certainly countenances an accusation which is constantly brought against the goldsmiths in contemporary pamphlets; for he says, that if the money which had been lodged with them for four or five years past had been deposited in the Bank, it would have prevented it from being so scandalously clipped, which he predicts would cost the nation some day a million and a half or two millions to repair. He notes it as very surprising and quite unexampled, that after the nation had been at war for six years, and had spent £30,000,000, besides great quantities of bullion being exported and captured by the enemy, that there had been so great a fall in the rate of interest instead of a rise, as in all previous wars, which was entirely due to the Bank, and he predicted that it would, in the course of a few years, reduce it permanently to 3 per cent. He says that, within 30 years of that time, the public had lost between two and three millions by the goldsmiths and scriveners breaking, which would not have happened if the Bank had been established. He says that there were some who were for having a forced currency of bills or tallies, thinking that they might pass as well as bank bills, *but they do not consider that it is nothing makes bank bills current, but only because all those who desire it can go when they will and fetch their money for them*; and to force anything to pass in payment but money would soon end in confusion. He then enters into numerous arguments to shew that any attempt at a forced currency would only end in damaging the public credit. He says that the chief reason of the indignation of the goldsmiths at the Bank was that they allowed 2d. per cent. per diem on their bank bills, which drew away customers from them. He says that the interest allowed to the holders of their bills amounted to £36,000 per annum.

30. The year 1694 is remarkable as the one in which the first of those speculative manias occurred, which have, on different subsequent occasions, seized upon the nation. All the tricks, all the rogueries, which have been so familiar in the joint stock

bubbles of later years, were rife at that time, but it is remarkable that while, in later times, these things have always sprung up when there was a greater abundance of capital than usual, in time of peace, this was at a time when a costly war had been raging for several years, and there was a great dearth of specie.

31. We have already, in the chapter on Coinage, noticed the extremely degraded state of the coinage at this period. It kept continually getting worse during 1694, and it is said, that at the end of that year, the difficulty lay so heavy upon the Government, that a stop was almost put to trade and taxes, and the cure of it could no longer be delayed, without apparent and inevitable ruin to the public, and an obstruction to all private commerce. A Committee of the House of Commons was appointed, and, having made a report, an Act (Statute 1695, c. 17), was passed, and received the Royal assent on the 3rd May, 1695, to prevent counterfeiting and clipping the coin of the kingdom. This Statute averred that it was notorious that the current coin had been greatly diminished by clipping, rounding, filing, and melting, and that many false and counterfeit coins had been clipped, for the better disguising thereof, and that these practices had been much occasioned by those who drove a trade of exchanging broad money for clipped money, and other arts and devices. It, therefore, prohibited any person from exchanging, lending, selling, borrowing, buying, receiving, or paying any broad or unclipped silver money for more in tale, benefit, profit, or advantage than the same was coined for, and ought by law to pass for, under a penalty of 10s. for every 20s. so illegally trafficked with. It also enacted, that whoever should buy, or sell, or knowingly have in his possession, any clippings or filings of the coin, should forfeit them, as well as a penalty of £500, and be branded on the right cheek with a hot iron. It forbade any one but a trading goldsmith or refiner of silver, to buy or sell bullion, under pain of imprisonment, and enacted numerous other vexatious penalties and regulations respecting the export of bullion. All these absurd cruelties were wholly ineffectual, and at this time, guineas, which had originally been coined to represent 20s. and had progressively risen, as the silver coin became worse, were current at 30s. of the base trash which passed by the name of silver coin.

32. We shall find that it is of very great importance to fix the exact period when the silver coin was so depreciated, as that guineas passed at 30s. We shall, therefore, make some extracts from contemporary pamphlets. It says, in one published in 1695 (Some Remarks on a Report containing an Essay for the Amendment of the Silver Coins by Mr. W. Lowndes.

London, 1695. Page 6), after speaking of the gradual deterioration of the coinage:—

“And so, by degrees, as the silver coin was diminished and debased in itself, so it fell in the estimation of the people, and in proportion gold advanced, and also bullion (that is not in itself, but in proportion to the bad money), not that bullion became worth 6s. 5d. an ounce, or GOLD 30s. A GUINEA in good money, that is, in weighty standard money, but in clipped and counterfeit money, whereof 6s. 5d. was not of the true nor esteemed value of 5s. 2d. And, as we ourselves grew sensible of the want of value in money that passed, so did foreigners likewise, AND THE FOREIGN EXCHANGES SOON ALTERED ACCORDINGLY, so that it cannot properly be said that bullion is advanced much, or that gold is advanced much, or commodities are advanced much, *but that the money that is exchanged for them is of much less value than it was*, and the new coining of our money will not, as I apprehend, alter the value of bullion, gold, &c., but it will bring silver in coin to its due value.”

After enforcing and illustrating these views at considerable length, he observes that Mr. Lowndes hoped that the exchange with Holland, which was then 25 per cent. against England, might be prevented falling lower, and says, page 16:—

“If guineas CONTINUE CURRENT AT 30s. A PIECE, the exchange will continue about the rate it does, except the common and ordinary variation, which many sudden drafts and remittances occasion; *and if guineas fall, the exchange will rise in proportion;* AND IF THE SILVER COIN IS REDRESSED, GUINEAS WILL FALL, and there are no other designs whatsoever can effect any considerable alteration, for English standard silver and standard gold will always be of the same value in Holland, as the same standard silver and gold in England, within 2, 3, 4, and 6 per cent., or thereabouts, and that difference happens according to present occasions, and the charge of sending it from one place to another, and the exchange to Holland and other places always govern accordingly.”

Again, page 19:—

“It is not the exportation of the silver which occasioned the fall in the exchange between Holland and here, but the reason of that *is the badness of our silver coin.*”

Again, page 20:—

“THE BALANCE OF TRADE IS NOT THE CAUSE OF THE GREAT FALL OF THE EXCHANGE FOR HOLLAND, BUT THE DEBASING OF OUR COIN.”

And he repeatedly declares, that the only way to set matters right was to reform the coinage. He also says that it was his opinion that it was not to the advantage of the kingdom to restrain the exportation of bullion, or indeed of money itself, to any certain quantity, but to let it be entirely free.

33. We have already seen from the pamphlet of Mr. Godfrey that, in the spring of 1695, the bank was in high credit. His pamphlet is nothing but a strain of congratulation on the great success that had attended the experiment. Burnet also tells us that a party in the country, who were moved with great jealousy, formed a design to ruin it on account of its flourishing credit. They tried what could be done to shake its credit, but this attempt was rejected with indignation by both Houses. He also tells us, at the same period, that there were two sets of coin, one milled, which could not be practised upon, the other not so, which was clipped, and so much so that at last it was diminished to less than half its proper weight. When this had gone on for some time, the King was advised to issue a proclamation to make it current by weight and not by tale, but it was strongly opposed in the Council. The badness of the money then was very visible. Guineas, which were in value to 21s. 6d. in silver, rose to 30s., that is to say, 30s. sank to 21s. 6d. The deterioration became still worse, and later in the summer Lord Somers again proposed in the Council that a proclamation should be issued to make coin current by weight and not by tale. The King was also of that opinion, but the rest of the Council were unanimously against it; "and so," says Burnet, "this proposition was unanimously laid aside, which would have saved the nation above a million of money. For now all people believed that the Parliament would receive the clipped money in its tale, clipping went on and became more visibly scandalous than ever it had been."

34. And so it went on till Parliament met in November, 1695. The urgency of the evil caused the subject to be taken up the very first thing by Parliament, and the Commons addressed the Crown to issue a proclamation to name a day when the currency of the clipped money should absolutely cease. A proclamation to that effect was accordingly issued on the 19th December, but the time named in it was so short, that it threw all trade into the utmost confusion. People refused to receive the old money, for fear it should be left on their hands. Evelyn has the following entries in his diary:—"12th Jan., 1695-6.—Great confusion and distraction by reason of the clipped money, and the difficulty found in reforming it. 23rd Jan.—They now began to coin new money."

35. The subject, then, of reducing guineas to their original value, was taken into consideration. A Committee was appointed to take into consideration the price of guineas on the 13th February, 1696. Several petitions were presented on the subject. The graziers, butchers, and others connected with Smithfield Market, said that £40,000 a week passed through

their hands for cattle, which for twelve months past had been paid in guineas at 30s. a piece, for want of current silver, a great part of which they had still, and were obliged to keep by them to trade with, and they said that a sudden fall would ruin them. The merchants, woollen drapers, and other traders stated, in their position, that commerce was brought to a stand by reason of the uncertain value of gold. They thought that a gradual lowering of guineas from time to time would be the only effectual means to remedy the evil, and prevent the loss from being more severe if they were lowered at once. A third petition, from divers merchants and others, said:—

“That by reason of the badness of our silver coin, some men have taken occasion to raise guineas to 30s. a piece, which being about 40 per cent. value here, above the proportion of gold to silver in any other part of Europe, hath caused the bringing over to us vast quantities of gold, causing the exchange to fall, and, consequently, the carrying out of our silver in that disadvantageous proportion, to the impoverishing of the kingdom. That, notwithstanding the care taken to reform the silver coin, yet certain persons continue buying and selling guineas, being employed therein, as they believe, by persons promoting their private gain, whereby they are still kept up to 29s. and 30s.; at which rate the petitioners are forced to receive them for debts, but cannot pay them so to the King’s receipts, or upon bills of exchange, so that they are necessitated to buy silver money with their guineas, at 3, 4, and 5 per cent. loss, and thereby contribute to the gain of those persons who kept up that trade. That at this time great quantities of gold are bought up and imported hither from Holland, where four of our milled crowns and two weighty shillings will purchase a guinea, the profit whereby is so great, that if some speedy stop be not put to this pernicious trade, our milled money will be melted down and carried away as fast as it can be coined.”

Other petitions to the same effect, and corroborating these facts, were also presented.

36. It was then carried by a majority of 164 to 129, on the 15th February, 1696, that guineas should be lowered to 28s.; on the 28th it was resolved, by a majority of 194 to 140, that after the 25th March, they should be reduced to 26s., and on the 10th April to 22s.; and heavy penalties were enacted against all who should deal in them at any other rate, after that date. It was further ordered that the clipped money should be received in payment of taxes till the 4th May, in advances to Government till the 1st July, and after the 1st February, 1697, should absolutely cease to be current. At this time, although both gold and silver were legal tender, yet the silver coin was considered as the standard currency, and gold only subsidiary. Debts were

considered to be contracted in silver, and, when this great disarrangement of the relative value of gold and silver took place, it was considered as a great public grievance. All the heavier pieces were called out, and sent to Holland, where guineas and bullion might be bought for 22s. which passed for 30s. in England, the consequence was a steady drain of silver from England, and a continued influx of gold. The Act of Charles II. gave every one the right to have his bullion coined at the Mint free of expense, and many persons had availed themselves of this privilege. By a return presented to the Commons, it appeared that since Lady-day, 1695, up to February, 1696, guineas to the amount of £721,280 had been coined for 149 persons. An Act, Statute 1696, c. 13, was passed to take off this privilege, and to prohibit the importation of guineas and half guineas.

37. All this time the Bank of England had received the degraded coin at its nominal value. Its notes were payable to bearer on demand. As soon as the new coin came out they were bound to pay them in full-weighted coin, that is, for every 7 ounces they had received, they were bound to give 12. Such a state of things could have but one result,—an immediate run upon them took place. Its success had enraged the private bankers and money dealers, whose profits it diminished. All its enemies now made a combined effort to destroy it. They collected its notes in all directions, and, on the 5th May, 1696, they suddenly presented for payment £30,000 in notes. The directors, after a solemn deliberation, knowing the purpose for which these notes were presented, refused payment of them, but continued their payments to their ordinary customers. Their enemies ran about crying that the Bank was destroyed. But the public, who understood the transaction, received their notes at first at their full value. But the extreme scarcity of silver continuing, they were obliged to make a general suspension. They gave notice that they could only pay 10 per cent on their notes once a fortnight, and, as the demand continued, they were unable to preserve even that payment, and a short time later they were obliged to make a still further suspension, by paying 3 per cent. every three months.

38. The following extracts from Evelyn's Diary are interesting and important:—

“13th May, 1696.—Money still continuing exceedingly scarce, so that none was paid or received, but all was on trust, the Mint not supplying for common necessities.

“11th June.—Want of current money to carry on the smallest concerns, even for daily provisions in the markets. Guineas lowered to 22s. and great sums daily transported to Holland,

where it yields more, and other treasure sent to pay the armies, and nothing considerable coined of the new, and now only current stamp, cause such a scarcity that tumults are every day feared, nobody paying or receiving money. Banks and lotteries every day set up.

“26th July.—So little money in the nation that Exchequer tallies on the best fund in England, the Post Office, nobody would take at 30 per cent. discount.

“3rd August.—The Bank lending the £200,000 to pay the army in Flanders, that done, nothing against the enemy had so exhausted the treasure of the nation, that one could not have borrowed money under 14 or 15 per cent. on Bills (*i. e.*, Bank of England Bills), or on Exchequer tallies under 30 per cent.”

39. We have in our possession a rare pamphlet, which has the unusual and fortunate circumstance of bearing on it the day of its publication. It is entitled “An Essay on the Coin and Credit of England, as they stand with respect to its Trade; by John Cary, Merchant, in Bristol. Bristol, printed by Will. Benny, and sold by the Booksellers of London and Bristol. October the 22nd, 1696.” It would have been fortunate if other pamphleteers had displayed equal forethought for the benefit of posterity, when exact dates are of such importance. This pamphlet contains statements of fact of the first importance in the Theory of the Currency. It says, p. 13:—

“When our coin was corrupt and base, all Exchange rose upon us, but now it is returned to its ancient standard, EXCHANGE RETURNS TO ITS OLD COURSE; not that the standard of our money is always the exact rule of our exchange, the balance of our trade often causes it to alter, either to our advantage, or to our loss, besides the charge of management, but this is little in comparison with the other. A familiar instance we have in the case of Ireland, *where, whilst our coin was base*, seventy pounds was worth one hundred pounds here, which was in some measure proportionable with the value of pieces of eight, which they took in Ireland by weight, to our clipped money, and also to our guineas at 30s. a piece, and how far this carried the trade of England into that Kingdom, the traders to the West Indies have been too sensible, *but, since the error of our coin hath been corrected, that very Exchange is so much varied* that one hundred pounds here is worth one hundred and fifteen pounds there.

“And since I have mentioned guineas, I cannot let them pass without some observations. How eager was the contest for keeping them up to that exorbitant value! and how unwillingly did the money changers, and those whom they had deceived, yield to the alteration! *Whereas, it was well known that the reason why guineas were so high was the badness of our coin.*”

This is a conspicuous and decisive instance of the truth of the principles in the chapter on Exchanges, that a restoration of the coinage is alone sufficient to bring the exchanges nearly to par. We then observe that, although at that time, the coin was very scarce, yet the mere fact of the restoration of its *quality* had brought the exchanges to par in October 1696. We must now inquire what the state of *Credit* was at that time, or the price of Bank notes and Exchequer tallies.

40. The Bank of England was a Whig project, and had been eminently successful in supporting the Government in the prosecution of the war. It had excited the warmest feelings of joy and congratulations among its friends, and the bitterest feelings of rage and indignation among its enemies, and the enemies of the Government. It was not endowed with any monopoly in its favour at that time. The Government of William was composed of a mixture of Whigs and Tories. The Tories determined to get up a rival bank on a much larger scale. The capital was to be £2,564,000 advanced to Government, on the same principle as that of the Bank of England, but its trading capital, notes, &c., were to be advanced solely to landowners for the cultivation of the land at three per cent. It was therefore called a Land Bank. It was warmly patronized by the Tory party. The origin of it is variously ascribed to a Mr. Brisco and to Dr. Hugh Chamberlain. The Bank of England and all its friends, of course, opposed it with all the power they could, but the temptation was too great, and it was sanctioned by Act of Parliament in April, 1696. The time for taking subscriptions was limited, in the like manner as had been done in the case of the Bank of England. When the subscriptions opened, the Lords of the Treasury subscribed £5,000 on behalf of the King, but the other subscriptions amounted only to £2,100 when the time came for its closing. It was, therefore, a total and complete failure. The finances of the State were in the utmost disorder, great arrears were due to every branch of the public service, some funds were wholly deficient, others produced much less than was calculated. In the next Session of Parliament the amount of arrears was ordered to be laid before them, and it amounted to the frightful sum of £6,000,459—more than all the current coin in the kingdom was supposed to be. Under these circumstances, when Parliament met in October 1696, Bank notes were at a discount of 20 per cent. and Exchequer tallies at 40, 50, and 60 per cent., at the same time that the exchanges were restored to par. Every one foreboded the total ruin of public credit. The enemies of England rejoiced, and believed that it was utterly irretrievable, and that the great European alliance against France would be dissolved.

41. Under these depressing circumstances, Parliament met on the 20th October, 1696. The King congratulated the House on the year having passed away without any disorder, considering the great disappointment in the funds voted at their last meeting, and the difficulties which had arisen from the re-coining of the money; he begged them to find out some expedient for the recovery of credit, which was absolutely necessary, not only with respect to the war, but for carrying on trade. The Commons responded with noble alacrity to the desires of the King; they immediately passed a vote, that they would not alter the standard of the gold and silver, in fineness, weight, or denomination, and that they would make good all the deficiencies on the funds. They also repealed the Bill for preventing the coining and importation of guineas, as it had only aggravated the public disorders.

42. When the Bank of England was subjected to the mortification of declaring a partial suspension of payments, it endeavoured to retrieve its credit by making two calls of 20 per cent. each upon its proprietors, the second of which was payable on the 20th November. These measures, however, did not effect their purpose, and the Parliament had to take in hand the great business of restoring the credit of the Bank notes, and the Exchequer tallies. On the 3rd February, 1697, Parliament agreed to increase the capital stock of the Bank, by receiving new subscriptions, which were to be made good in tallies and Bank notes. It passed an Act for this purpose, Statute 1697, c. 20. The chief provisions were as follows:—

1. All persons, natives or foreigners, bodies politic or corporate, might subscribe to the new stock, and the subscriptions might be paid, four-fifths in Exchequer tallies and one-fifth in Bank notes, upon which the Crown would allow 8 per cent.

2. Before the 24th July, 1697, the capital stock of the Bank was to be estimated, and made up to 100 per cent.; any deficiency was to be made up rateably by the proprietors, and any overplus to be rateably paid back to them.

3. All such subscribers were to be incorporated with the proprietors of the old stock.

4. The time when the Crown might put an end to the corporation was prolonged to twelve months after the 1st August, 1710, and repayment of all parliamentary debts.

5. It was enacted, that during the continuance of the Corporation of the Governor and Company of the Bank of England, no other Bank, or any other corporation, society, fellowship, company, or constitution, in the nature of a bank, shall be erected, or established, permitted, suffered, countenanced, or allowed by Act of Parliament, within this kingdom.

6. The Bank were allowed to extend their issues of notes

beyond the original capital of £1,200,000, to the amount of new capital which should be subscribed, provided that they were made payable to bearer on demand; and in case they made default in such payment, they might be paid on presentment at the Exchequer, out of the annuity due to the Bank. All notes above the sum of £1,200,000, were to bear a distinguishing mark.

7. All the property of the Bank was exempted from taxes.

8. Bank Stock was to be personal property, and not real.

9. It was made felony to forge or counterfeit any Bank note, or obligation under the Common Seal, or altering or erasing any indorsement on such a note or bill.

10. Bank Stock exempted from any foreign attachment.

11. The debts of the Corporation forbidden to exceed their capital stock; if they did so, the Members were liable in their private capacity.

12. All persons were forbidden to buy or sell tallies at more than the legal rate of interest, under the penalty of forfeiting treble the value of the money.

43. Such were the measures taken to restore the credit of the Bank, and we observe that their own depreciated notes, were taken in payment as specie at their full amount. The public, however, were still grievously suffering for want of a circulating medium during the slow progress of the re-coinage. The Bank of England did not issue notes below £20, which were of little use for the general purposes of business. The Chancellor of the Exchequer Montague, hit upon the plan of issuing bills upon the Exchequer for £5 and £10. These bills, at first, passed at a small discount, but, upon the second issue of them, £7 12s. interest per cent. was allowed, and they were received in payment of taxes at par. They soon rose to par. The Treasury was authorized to contract with any persons to cash these Exchequer bills on presentment, allowing them a moderate premium. They were allowed 10 per cent. at first, but the Exchequer bills soon rose above par, and then the interest was reduced to 4 per cent. Under this Act, upwards of £2,000,000 of Exchequer bills were issued.

44. The new subscriptions to the Bank, under this Act, amounted to £1,001,171 10s.; two hundred thousand pounds worth of Bank notes and eight hundred thousand of Exchequer tallies being taken out of circulation, and received at par in the subscription, raised the value of the remainder, and, in the course of the year, Bank notes which bore no interest were at par, and the bills which bore interest were at a premium.

45. When we consider the unquestionable services the Bank had rendered the Government, which contributed so greatly to the success of the war, and the pacification of Ryswick, and

when we consider the terrific state of public credit, owing very much to the total failure of the Land Bank, we need not be surprised that the Bank of England employed those circumstances for the purposes of securing a monopoly to themselves. Nor, considering the ideas of that age, can we be surprised that they received it. But, nevertheless, making allowances for all these circumstances, it is one of the most deplorable acts that have come down to our time. The founders and contemporaries of the Bank felt the benefit of its eminent services, but the consequences of this original sin fell with terrific force on their descendants of the third and fourth generation. The frightful convulsions and collapses of public credit which have taken place during the last three quarters of a century, are chiefly due to this great wrong, and violation of the true principles of trade. English banking has never recovered its fatal effects to this day, and many years must elapse before it will arrive at the form to which it is gradually tending, and which it would naturally have assumed, if its development had been left free to the skill and experience of men of business.

46. We have felt it necessary to be thus minute and circumstantial in the account of this great monetary crisis, because it is of very great importance in the Theory of the Currency, and because it has been very prominently noticed in the Bullion Report, and we must now examine the account of it given there.

But we must first of all give a statement of the Discount on Bank Notes and the Rates of Exchanges during 1696 and 1697.

Statement of the Discount per cent. on Bank Notes.

1696.	£ s.	1697.	£ s.	1697.	£ s.
July 9.....	16 0	Jan. 30	19 0	Aug. 3	7 0
„ 16.....	8 0	Feb. 18	21 0	„ 26	3 10
„ 28.....	10 0	„ 20	24 0	„ 28	2 0
Aug. 25	15 0	Mar. 23	23 10	Sep. 18	1 0
Sept. 12	17 0	April 3	18 0	Oct.	par.
Oct. 10.....	12 0	May 20	18 0		
„ 22.....	18 0	June 5	13 0		
„ 27.....	14 0	„ 17	13 0		
Dec. 26.....	17 0	„ 24	10 0		

*Statement of the Rates on the London Exchange
during 1695-1696.*

	Amster- dam.	Rotter- dam.	Genoa.	Ant- werp.	Ham- burg.	Cadiz.	Madrid.	Venice.
1695.								
April 23.....	31·2	31·4	59·29	30·11	29·11	56·2	56·1	59·
1696.								
January 21.....	31·0	31·2	60·	31·	29·9	60·0	60·	63·
May 2	30·1	30·2	61·	30·	28·8	60·	61·	61·2
July 19.....	29·3	30·6	65·	29·		60·		
July 28.....	38·7	33·9	58·	33·	32·4	53·	58·	54·
September 29	36·5	36·7	54·	36·	35·	48·	49·	51·
October 6	36·8	36·10	53·2	35·7	35·8	48·	49·	
November 6	37·4	37·6	52·2	37·2	36·4	47·	48·	49·
December 16.....	37·8	37·10	51·	37·8	36·8	46·2	47·	49·

In interpreting this table, we perceive that a great change in the figures took place at the end of July, 1696. Some *rise* very much, others *fall*. The fact was, that it was at this period that the new coinage came out in great abundance. This rectified the exchanges, and those *from* which London *received* the variable price would of course *rise*; those *to* which London *gave* the variable price would, of course, *fall*: as explained in the Chapter on Exchanges, § 5. These figures denote the Rates of Exchange as paid in coin. But we have a statement of the difference between the Rates of Exchange as they were paid in coin, or Bank Notes, during the winter of 1696-97, given in *A Collection for the Improvement of Husbandry and Trade*, thus:—

	Dec. 16, 1696.		Feb. 23, 1697.		Mar. 2, 1697.	
	Money.	Bk. Note.	Money.	Bk. Note.	Money.	Bk. Note.
Amsterdam	37·8	... 31·19	36·3	... 29·	36·5	... 29·2
Rotterdam.....	37·10	... 31·10	36·5	... 29·2	36·7	... 29·4
Antwerp.....	37·8	... 31·9	36·4	... 29·2	36·6	... 29·4
Hamburg	36·8	... 30·9	35·5	... 28·2	35·9	... 28·2
Cadiz.....	46·2	... 55·	47·1	... 58·	46·3	... 58·2
Madrid	47·2	... 67·	48·	... 58·	47·3	... 59·2
Leghorn.....	51·2	... 61·1	52·	... 64·	52·	... 63·
Venice.....	49·	... 58·	49·	... 60·	49·	... 61·
Discount on Bank Notes	16·		21·		22·	

Having given these tables, which are of the utmost importance in the Theory of the Currency, and to which we shall hereafter refer, we may now see what the Bullion Report states.

It says, p. 17 :

“The experience of the Bank of England itself, within a very short period of its first establishment, furnishes a very instructive illustration of all the foregoing principles and reasonings. In this instance, the effects of a depreciation of the coin by wear and clipping *were coupled with the effect of an excessive issue of paper*. The directors of the Bank of England did not at once attain a very accurate knowledge of all the principles by which such an institution must be conducted. They lent money, not only by discount, but upon real securities, mortgages, and even pledges of commodities not perishable; at the same time, the Bank contributed most materially to the service of Government for the support of the army on the continent. By the liberality of those loans to private individuals, as well as by the large advances to Government, the quantity of the notes became excessive, their relative value was depreciated, and they fell to a discount of 17 per cent. At this time there appears to have been no failure of the public confidence in the funds of the Bank, for its stock sold for £110 per cent., though only 60 per cent. upon the subscriptions had been paid in. By the conjoint effect of this depreciation of the paper of the Bank from excess, and of the depreciation of the silver coin from wear and clipping, the price of *gold bullion was so much raised that guineas were as high as 30s.*, all that remained of good silver gradually disappeared from circulation, and the exchange with Holland, which had been before a little affected by the remittances for the army, sunk as low as 25 per cent. under par, when the Bank notes were at a discount of 17 per cent. Several expedients were tried, both by Parliament and the Bank, to force a better silver coin into circulation, and to reduce the price of guineas, but without effect. At length the true remedies were resorted to; first, by a new coinage of silver, which restored that part of the currency to its standard value, though the scarcity of money occasioned by calling in the old coin, brought the Bank into straits, and even for a time affected its credit. [Surely, if Bank notes were at a discount of 17 per cent. *before this*, its credit was affected.] Secondly, by taking out of the circulation the excess of Bank notes. In proportion to the amount of notes sunk in this manner, the value of those that remained in circulation began presently to rise; in a short time the notes were at par, and the foreign exchanges nearly so. These details are all very fully mentioned in authentic tracts, published at the time, and the case appears to your Committee to afford much instruction upon the subject of their present inquiry.”

The Report refers, in a marginal note, to *A Short Account of*

the Bank, by Mr. Godfrey, and A Short History of the last Parliament, 1699, by Dr. Drake.

47. On examining this paragraph, it may be said to contain the following allegations:—

1. That, very soon after the foundation of the Bank, it made excessive issues of paper.

2. That in consequence of these excessive issues, *and while they continued to pay their notes in specie on demand*, their notes fell to 17 per cent. discount.

3. That, in *consequence* of these excessive issues of paper by the Bank, and the depreciation of the silver coin from wear and clipping, guineas rose to 30s. from 21s. 6d., and that the remaining good silver disappeared from circulation.

4. That in consequence of the two preceding causes, exchange with Holland rose to 25 per cent. against England.

5. That many attempts were made by the Bank and Parliament to reduce the price of guineas, and force a better silver coinage into circulation, which all failed.

6. That measures were at length resorted to of calling in the old silver coinage, and re-issuing it at full weight, and taking the excessive issues of the Bank out of circulation, which were finally successful, restored the Bank notes to par, and restored the exchanges.

The Committee ground their allegations upon Mr. Godfrey's pamphlet on the Bank, and Dr. Drake's History of the last Parliament, 1699, as well as a number of anonymous pamphlets, to which they give us no clue to discover their names.

48. We must now examine each of these propositions separately.

With respect to the first, what is, or what is not an excessive issue, is a matter of so much speculation that it is quite impossible to affirm or deny it.

With respect to the second allegation, there is not only no evidence in its favour in the pamphlets quoted, but the most overwhelming evidence against it. Mr Godfrey's pamphlet was written in 1695, when the credit of the Bank was in the most flourishing condition, when he makes this credit a matter of great boast, and he says that the only reason why the credit of the Bank notes was so good, was that their holders knew that they could get their *money instantly on demand* for them. Mr. Godfrey was killed at Namur, in July, 1695, and Bank notes were not at a discount till May, 1696.

With respect to the third allegation, we have the most positive and overwhelming evidence that guineas were at 30s. in the Spring of 1695, when the credit of the Bank was unimpeached, and its notes were all paid instantly on demand.

With respect to the fourth allegation, we have already seen that the exchange on Holland was at 25 per cent. against England in 1695, nearly one year before Bank notes were at a discount.

The fifth allegation is entirely erroneous. Parliament made no attempt to reduce guineas till February, 1696, when the silver coin had been already called in.

The commencement of the sixth allegation is quite wrong in point of time. It is an unquestionable fact, testified by the most conclusive evidence, that it was the scarcity of money while the old was called in, and before the new was fully in circulation, that caused Bank notes to fall to a discount, and their receiving the old coin at its nominal value, and binding themselves to pay in the new. We have read a considerable number of pamphlets of that period, and they all with one voice attribute the price of guineas, and the adverse state of the exchanges, to the *badness of the coin and to that only*. This Report, then, is not borne out in any of these statements by the authorities they have cited. The only one in which they are correct, is, that the new subscriptions in Bank notes and tallies raised their credit, by reducing their quantity, but they have been misled by Dr. Drake in saying that the exchanges began to recover at the same time. Dr. Drake, being a clergyman, and writing some years after the event, probably did not have his attention directed to so minute a point as the exact date when the exchanges rose to par, but we have in the pamphlet already quoted, written by a merchant, and dated on the 22nd of October, 1696, the express fact stated *that at that time the exchanges were at par*, in consequence of the good coin which had been issued, whereas bank notes were still at a heavy discount in June, 1697.

49. We have been thus minute in examining the circumstances of this great monetary crisis because we shall see hereafter that it is of great importance in establishing the true Theory of the Currency. We have, we think, shewn by the most conclusive evidence, that this paragraph in the Bullion Report is full of the gravest chronological errors, in a matter in which minute accuracy of dates is all important.

50. There was one circumstance which we have not seen noticed by any writer, which we may probably suppose contributed greatly to increase the discount at which the notes were. There were none at that time under £20, and notes of that amount must have been obviously unfit for the ordinary purposes of trade. The great want was small change, but that had almost entirely disappeared, consequently, when the holder of one of these notes wanted change, he must have made a much greater sacrifice than was warranted by any want of confidence

in the Bank. Under these circumstances we may be somewhat surprised that no one hit upon a plan which would certainly have been successful, namely, an issue of £1 notes, to have supplied the deficiency until a sufficient quantity of guineas had been coined for circulation.

51. The issue of small Exchequer bills was entirely successful, although they had not a forced currency. The great cause of the mischief to the Bank was, that the old and the new coin were allowed to circulate together, which all experience shewed would inevitably drive all the new coin out of circulation. And this is exactly what did happen.

“While the hammered money, and pieces not clipped within the ring, were permitted to pass, for the present necessity of trade, nobody was willing to make payments in new money, which so much exceeded the old in its intrinsic worth. And, therefore, the new silver money as fast as it issued from the mints and Exchequer, was in a great measure stopped in the hands of its first receivers, for none were disposed to make payments in the new silver coin at the old standard, when they could do it in clipped pieces so much below it. And those who had no payments to make, kept their new money as medals and curiosities in their chests, and there is reason to believe that at first a great quantity of new money, by the help of the melting pot, went abroad in ingots to purchase gold, which at this juncture was a very profitable commodity in England.”

52. In this great discussion, all the fallacies which are so specious and plausible, and which were maintained with so much earnestness 116 years later, were put forward—except one. The invariable language of all writers at that period was that the bank notes were depreciated. They always speak of the notes *being at a discount*, it was reserved to modern ingenuity to discover the crowning absurdity—that it was not notes that had fallen, but gold that had risen!

53. The Bank was instituted for the purpose of assisting the Government in the war with France, and did very materially do so in 1695, when its credit was high. In the next year, however, it continued to do the same, when its credit was greatly shaken. This no doubt was of great assistance to the army, and its conduct is highly lauded by Dr. Drake, but some of its own proprietors thought very differently of its management. In a pamphlet, entitled *A Second Part of a Discourse Concerning Banks*, which was published by one of them, which bears no date, but which was most probably written in 1697, which contains a series of excellent rules for the conduct of a bank, the direction is severely censured for dealing in exchanges, for

running into remittances, and launching too deeply into loans to which causes the author attributes the loss of their credit. This would seem to allude to the loan mentioned by Evelyn.

54. The political troubles at the commencement of the next century placed the Bank in difficulties again in 1704 and 1707. In the latter year the revived hopes of the Jacobite faction, roused by the preparations of Louis XIV., threw the country into a panic. The public stocks sunk 14 to 15 per cent. The enemies of the dynasty, and the enemies of the Bank, combined to make a run upon it. The private bankers tried to swamp their great rival, and Sir Francis Child pretended to refuse its notes. These malicious proceedings, however, called forth an equal amount of ardour from the Government and its friends. Several of the highest nobility came forward to lend money to the corporation, and the Queen lent it her warmest support. The directors made a call of 20 per cent. on their proprietors, and, by these means, surmounted their difficulties and restored their credit.

55. In 1709 the Government were again in a state of great pecuniary embarrassment. The produce of the taxes scarcely covered one half of the expenses. In this extremity the Ministry turned to the Bank of England, and, by mutual arrangement, the following terms were proposed and accepted by Parliament:—

1. That the interest upon their original stock of £1,200,000 be reduced to 6 per cent., with an allowance of £4,000 for managing the debt.

2. That they were to advance a further sum of £400,000 at 6 per cent. interest.

3. That they should be allowed to double their present capital of £2,261,171 10s. at the price of 115 per cent. for the new stock. Upon which they agreed to circulate £2,500,000 of Exchequer bills, and receive an allowance of 6 per cent., one half for interest, and the other for repayment of the principal, and that no more Exchequer bills should be issued without the consent of the Bank.

4. That their privileges as a corporation should be continued for 21 years from 1st August, 1711.

56. The subscription lists for the new stock were opened on the 22nd February, 1709, at nine in the morning, and by one o'clock the whole sum was subscribed at the premium. And a million more might have been subscribed before evening if there had been room.

57. The Act of 1697 had only provided that no other bank should be sanctioned by Act of Parliament; it did not prohibit

any private Joint Stock Bank from being formed, nor any other corporation, or company setting up banking business. A company, called the Mine Adventurers of England, at the head of whom was Sir Humphry Mackworth, who turned out to be a great rogue, commenced doing all kinds of banking business, issuing notes, &c. To put a stop to this it was enacted:—

“That during the continuance of the said Corporation of the Governor and Company of the Bank of England, it shall not be lawful for any body politic or corporate whatsoever, erected or to be erected (other than the said Governor and Company of the Bank of England), or for any other persons whatsoever united, or to be united, in covenants, or partnership, exceeding the number of six persons, in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes payable at demand, or at any less time than six months from the borrowing thereof.”

And the Bank was strictly forbidden to issue notes to a larger amount than their capital stock. That is, each loan to Government was attended with an *augmentation* of currency to an equal amount. Now, to a certain extent this plan might be attended with no evil consequences, but it is perfectly clear that its *principle* is utterly vicious. There is nothing so wild or absurd in John Law's Theory of Money than this. His scheme of basing a paper currency upon land is sober sense compared to it. If for every debt the Government incurs, an equal amount of money is to be created, why here we have the philosopher's stone at once. What is the long sought El Dorado compared to this? Even there the gold required to be picked up, and fashioned into coin. Besides, people in this country would have to go round the globe in search of it. But let us coolly consider the principle involved in this plan of issuing notes upon the security of the public debt. Stated in simple language, it is this—*That the way to create money is for the Government to borrow money.* That is to say, A lends B money on mortgage, and, on *the security of the mortgage*, A is allowed to create an equal amount of money to what he has already lent!! Granting that to a small extent this may be done without any practical mischief, yet, as a general principle, what can be more palpably absurd? The ravings of Chamberlen himself are not more wild.

58. At that time the practice of issuing notes was considered so essentially the main feature of banking, that a prohibition of that was considered an effectual bar against banking. The clause quoted above was intended to prevent any bank being formed with more than six partners, so as to prevent any private company being formed of sufficient power and influence to rival the Bank. It was so understood at the time, and it did have the effect of preventing any other Joint Stock Bank being formed.

59. The financial difficulties of the Government in the year 1713, at the Peace of Utrecht, made it necessary to have recourse to the Bank again. They agreed to lend the Government £100,000, secured upon Exchequer bills, at 3 per cent., upon receiving an extension of their charter, which had still twenty years to run. By the Statute I. 1713, c. 11, its existence as a corporation was prolonged to twelve months' notice, to be given after 1st August, 1742, and the payment of £1,600,000. By a second Statute that year, they were authorized to lend money upon South Sea Stock.

60. In 1716, an Act, Statute 1716, c. 8, was passed to redeem and modify several of the public debts due to the Bank, but not altering their privileges in any way, and to make further advances at 5 per cent. They were also authorized to make such calls as they pleased upon their proprietors. The excessive absurdity and inconvenience of the usury laws in commerce were even then felt, and the Bank was exempted from their operation. They were authorized, in the quaint phraseology of the Act, "at their own good liking," to borrow or take up money at any rate of interest they pleased, above the legal rate, upon their bills, bonds, or any obligation under their Common Seal, or upon credit of their capital stock for any time, or to be paid on demand. What portentous folly it was that any one else might not observe his "own good liking" in the rate he paid for borrowed money. In this Act, the clause prohibiting any banking partnership to consist of more than six members was repeated. There were at that time three annuities of £88,751, £100,000, and £76,830, besides other debts, upon which an annual interest at 5 per cent. was paid; the Bank's existence was prolonged indefinitely, until all these annuities and debts were discharged.

61. Up to the year 1711 all the permanent debt contracted by the Government consisted of Bank of England Stock. In order to replace the capital thus withdrawn from circulation, the Bank had always been allowed to issue notes to an equal extent; but it was quite evident that this could not go on indefinitely. At this period the party antagonistic to that which founded the Bank of England were in power. The dismissal of the Whigs had shaken public credit. The unfunded debt of the State was enormous—it amounted to nine millions and a half. Mr. Harley (afterwards Earl of Oxford), the Chancellor of the Exchequer, revived the idea which we have before noticed, as first suggested by Dr. Chamberlain. He persuaded a number of merchants to undertake this debt, upon receiving interest at 6 per cent., and being incorporated as a company for 32 years, with the exclusive privilege of trading to the South Seas. This was hailed by his

party at the time with great approbation, as a masterpiece of financial wisdom. Such was the origin of the South Sea Company. We cannot, of course, enter into any of the details of this famous scheme, beyond what strictly concerns our present subject. Ample details will be found elsewhere. Though especially forbidden by Act of Parliament to carry on banking business, this great monetary corporation overshadowed the Bank of England. In 1717, the Government determined to make a strong effort to reduce the national debts. Proposals were invited from each of these great companies. The South Sea Company proposed that their then capital of £10,000,000 should be augmented to £12,000,000; that the additional £2,000,000 should be employed in redeeming several public debts, and among these the bankers' debt; that the interest on their original capital should remain at 6 per cent., and interest at 5 per cent. should be given on the new capital till the 24th June, 1718. After that date interest at 6 per cent. should be allowed on the whole capital. That the duties upon which such interest was chargeable should be continued, and any surplus, after paying them, should be applied to redeem other public debts. That all sums of principal and interest might be redeemed upon a year's notice, after 24th June, 1725. That their capital and stock in trade should be exempted from all taxes whatever.

62. The Bank of England proposed that their privileges should remain untouched till 1742, as by the last Act. That an annuity of £106,500 due to them should be reduced to £88,175 after the 25th March, 1718. They offered to advance £2,000,000 at 5 per cent. interest, on Exchequer bills redeemable at one year's notice after 1720, and to circulate some others at 3 per cent. That the interest on the Exchequer bills they held, should be reduced to 1d. per cent. per diem, but that no more should be issued without their consent. They were further willing to advance £2,500,000 for the public service at the rate of 5 per cent. per annum. They demanded that all their privileges should continue until these sums were redeemed. After a warm debate, the proposals of the South Sea Company were accepted. The Bank of England, however, remonstrated strongly, and petitioned Parliament, reminding them of their eminent public services, and requested that all the public stocks might be made transferable and payable at the Bank, which duty they undertook to perform without any profit to themselves, on condition that no further taxes be laid on their capital, or upon their bills and notes. Upon further debate, the proposals of the Bank of England were accepted, as well as those of the South Sea Company, and three Acts were passed to carry them into effect. At this time the South Sea Company appeared to have got so com-

pletely the better of the Bank, that they invited the King to become their Governor, and, on the 1st of February, 1711, an Act was brought in to remove any difficulties in the way. It was read and passed through both Houses on the same day, and on the next, received the Royal Assent.

63. The skirmish between these two great corporations in 1717, was but the prelude to a much more gigantic contest in 1720. On the 23rd November, 1719, the King recommended the state of the public debts to the attention of Parliament. This was preliminary to the introducing a plan to Parliament which the Ministry and the South Sea Directors had secretly projected, and determined to bring before Parliament, before any opposition could be organized against it. It was brought before the House on the 22nd January, 1720. The details are given in the Parliamentary History, and are much too long to be inserted here. But the outline was as follows:—They estimated the whole of the public debts at £30,981,712; they proposed to buy up the whole of these, and consolidate them into one fund, which was to be added to their capital at 5 per cent. interest. For these privileges they offered a *bonus* of £3,500,000 to the State, payable in four instalments, to commence at Lady-day, 1721. This astounding proposal was brought before the House by surprise, but its terms were not so favourably received as was expected, and gave the friends of the Bank time to rally. They reminded the House of the great and eminent services it had done the public, and obtained five days' delay.

64. The Bank determined not to be outdone in audacity. They also undertook to consolidate these debts, and add them to their capital. Upon the whole, it was calculated that their proposal was more advantageous to the nation by about £2,000,000, and was payable in less time. The South Sea Company obtained three days' delay to amend their offer. They increased the bonus to the public to £7,567,500, besides other minor points. The Bank, in a fit of wild desperation, amended their offer. The chief points were, that for every £100 annuity for 96 and 99 years, they offered £1,700 Bank Stock, and that after the 24th June, 1727, the interest on the whole consolidated funds should be reduced to 4 per cent. absolutely, and thenceforth be redeemable by Parliament.

65. The contest between these gigantic rivals, was simply which was to devour the other. The debate was long and fierce; Mr. Robert Walpole was the champion of the Bank, Mr. Aislacie, Chancellor of the Exchequer, was patron of the South Sea Company. At length, on the 2nd April, the South Sea Bill was read a third time, and passed by a majority of 172 to 55.

Then it was carried up to the Lords. The debate was equally animated, but, as usual, less garrulous; it was ended in a single day, and the South Sea carried the day by a majority of 83 to 17. The King closed the Session on the 11th June, and congratulated Parliament on the good foundation they had prepared for the payment of the national debts, without violation of the public faith.

66. The price of the South Sea Stock on the 7th April, when the Bill passed, was 310, next day it fell to 290. On the 12th, the directors opened their first subscription of £1,000,000 at £300 for every £100, having first propagated the most enormous falsehoods of alleged trading advantages they had secured in the South Seas. Twice the sum was subscribed, and in a few days the subscriptions were sold at double the price of the first payment. Then began the wild delirium—by successive stages, the stock stood at £500 on the 23rd May; on the 2nd June, at £890; next day it fell to £640. After some fluctuations the Company opened their books for a third subscription at £1,000; £4,000,000 were taken at that price, and, before the end of June, the stock was at £2,000. The price of Bank Stock, at the same time, was £260. The great outbreak of the bubble mania had begun before the prorogation of Parliament, and on that day the King had published a proclamation to put them down, but with little effect. By the middle of July the projects before the public required a capital of £300,000,000. One was “For carrying on an undertaking of great advantage, but nobody to know what it is.” The witty rogue promised, on a deposit of £2 2s., that each subscriber should receive an income of 100 per cent. In a single morning he received £2,000, and, of course, immediately decamped. Permissions to subscribe to a future scheme were selling at sixty guineas.

67. Then came the fearful collapse; on the 2nd September the stock was at £700. The directors made many vain efforts to retrieve its credit. On the 13th it was at £400. Then the directors were compelled to make humble suit to their vanquished rivals. At the intercession of Walpole, the Bank of England agreed to a draft of a contract for providing means to sustain the credit of a number of their bonds. After protracted negotiations, the terms were agreed upon between the two companies, and brought before the proprietors of the Bank of England, and approved of by them. Before, however, it could be embodied in a legal form, affairs took a very different turn. A great many of the goldsmiths and private bankers had advanced great sums upon the South Sea Stock; when this fell, it brought a run upon them. Many of them stopped payment, and absconded. The Sword Blade Company, who were the cashiers

to the South Sea Company, stopped payment. This portended universal bankruptcy. The Bank had been assailed with every species of public resentment because it had hesitated to lend its aid in supporting the South Sea Bonds. Every one looked upon it as the sole pillar of credit, but even the credit of the Bank was now shaken. The general failure of the bankers immediately caused a great run upon it. The Bank, in these straits, devised a trick to prolong the payments. It employed a number of clerks to tell out the money which was demanded, as well as what was brought in. Payments were made in light sixpences and shillings, and large sums were paid to particular friends, who went out with their bags of money at one door, to deliver them to people placed at another, who were let in to pay the same money to tellers, who took time to count it over. These persons were, of course, always served first. By this means time was gained, the friends of the Bank rallied round it, and made large subscriptions to support the company; the festival of Michaelmas, at which it was usual at that time to shut up the Bank, came, and, when it was opened again, the public alarm had passed off.

68. But something was required to be done to restore public credit. The South Sea Company were permitted to sell annuities to the value of £200,000 a year. The Bank bought them at 20 years' purchase, and was allowed to add the £4,000,000 to its capital; it then stood at £8,959,995 14s. 8d.

69. Up to the year 1722, the Bank had divided the whole of its profits among the Shareholders, and had made no reserve for any contingencies. The dividend, therefore, had been extremely variable. It had fluctuated from 18½ per cent. in 1706, to 6 per cent. in 1722. The inconvenience of this was strongly felt, as well as having no fund to fall back upon in cases of emergency. These had hitherto been met by making calls upon the proprietors. In this year the Directors established a reserve fund, which is called the Rest.

70. Several financial transactions took place between the Government and the Bank, which need not be detailed here. Upon most of the previous occasions of the renewal of the charter, there had been much public discussion as to the expediency of continuing this monopoly. The Bank, however, had always been able to relieve the continually embarrassed state of the finances, and had thus purchased its privileges. As the time was drawing near for the expiry of the monopoly in 1742, these discussions became more frequent and animated, and several attempts were made to set up banks in such a manner that they should not violate the clause in the Act of 1709. When the

time for the renewal came, the Government were, as usual, in difficulties, and the Bank agreed to lend them £1,600,000, without interest. To raise this sum, they made a call upon their proprietors, which raised their capital stock to £9,800,000. In consideration of this, their exclusive privileges were continued till twelve months' notice after 1st August 1764. Moreover, it was determined to stop up all the loopholes in the Act of 1709, and the following clause was inserted in the Act, Statute 1742, c. 13, s. 5:—

“And to prevent any doubts that may arise concerning the privilege or power given by former Acts of Parliament, to the said Governor and Company of *exclusive banking*, and also in regard to the erecting any other Bank or Banks by Parliament, or restraining other persons from banking during the continuance of the said privilege granted to the Governor and Company of the Bank of England, as before recited, it is hereby further enacted and declared, by the authority aforesaid, that it is the true intent and meaning of the Act that no other bank shall be erected, established, or allowed by Parliament, and that it shall not be lawful for any body politic or corporate whatsoever, erected, or to be erected, or for any other persons whatsoever, united, or to be united, in covenants or partnership, exceeding the number of six persons, in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money, on their bills or notes payable at demand, or at any less time than six months from the borrowing thereof, during the continuance of such said privilege to the said Governor and Company, who are hereby declared to be and remain a corporation with the privilege of exclusive banking, as before recited.”

These words were devised with the utmost care, so as to prevent any other rival, in the most comprehensive manner possible. It was supposed that no legal ingenuity could devise an expedient to evade so extensive a prohibition. But, alas! for the wit of lawyers! We shall see afterwards that a change in the method of doing banking business, so simple, and apparently so unimportant, as scarcely to deserve attention, cut away the ground from under this Act, and destroyed the monopoly of the Bank. But we have many years to look forward to before that event.

71. In September, 1745, the rebellion in Scotland seemed to be assuming formidable proportions. The Chevalier captured Edinburgh, and this news produced a run upon the Bank, partly caused, it is said, by the friends of the Prince, both to get money to assist him, as well as to embarrass the Government. Bank notes fell to a discount of 10 per cent. A meeting of merchants immediately took place, and 1,600 of the most eminent came to a resolution, on the 26th, pledging themselves to support the

credit of the Bank notes. It also said that the Directors adopted the same expedient on this occasion, which had been so successful in 1720, of paying in sixpences.

72. In 1746 the Ministry were again in difficulties, from the political disturbances of the preceding year, and they were obliged to apply for assistance to the Bank. The proprietors authorized the directors to cancel £986,000 of Exchequer bills, upon receiving an annuity of 4 per cent., and to create new stock for that purpose. This increased the paid-up capital to £10,780,000, which was not further augmented till 1782. In 1750 the interest upon £8,486,000 of the debt due to them from Government was reduced to 3 per cent.

73. In 1759, the Bank began to issue notes for £15 and £10.

74. The practice of giving notes or receipts for deposits payable on demand, originated with the goldsmiths, and was continued by the bankers, and was universally followed by bankers at this period. Thus, we have it said by Cantillon:—

“The cash for bankers’ notes of undoubted capital and credit, such as a Child, a Hoare, and a Colebrook, is but rarely called for; but if these notes fall into people’s hands who are not their customers, then payment is immediately demanded. The prudent banker regulates his conduct by such as make use of his shop. If his notes fall into his brethren’s, or into the hand of a bank such as that of England, nothing will be more pressing than they will be for their cash.”

75. It is a favorite doctrine with some persons, that it is impossible to have an undue extension of credit with a purely metallic basis, and that an improper issue of bank notes is the sole cause of too great an expansion of credit. Just as if the currency being made of metal could prevent people from giving their “promise to pay,” and buying up goods on speculation. The year 1763 is remarkable as among the first of those great eras of commercial distress and prostration, caused by too great an expansion of credit. And these disasters took place where there was no currency at all but what represented bullion,—Hamburg and Amsterdam. The progress of the seven years’ war had probably encouraged great speculation among the continental merchants, which involved those connected with them in ruin when peace came. Two brothers at Amsterdam, named Neufville, were among the principal merchants and speculators who had connections all over the continent. At length their embarrassments became so great that the bankers at Amsterdam could no longer support them, and they failed for upwards of 330,000 guineas, on the 29th July, 1763. Before the

news of their actual stoppage reached Hamburg, the bankers at that town were thrown into the greatest consternation by hearing that it was intended at Amsterdam to allow the Neufvilles to fail. On the 4th August, 1763, the bankers at Hamburg met to consider how the tottering state of credit in that town was to be supported, when they say:—

“We received a fatal express with the terrible news that you, the gentlemen of Amsterdam, would leave the Neufvilles to sink, by which we were all thunderstruck; never dreaming that so many men in their senses in your city could take such a step—a step which will infallibly plunge all Europe into an abyss of distress, if not remedied by you whilst it is time. We, therefore, send this circular and general letter to you by an express, to exhort and conjure you, as soon as you receive this, to undertake still to support the Neufvilles by furnishing what money they want, and giving them two or three persons of unquestionable probity and skill for curators, that their affairs and their engagements may be concluded and terminated, without causing a general ruin, which will otherwise infallibly happen. If you do not, gentlemen, we hereby declare to you, that our resolution is taken, that is to say, that, although were present a very respectable body of rich and respectable men, we have unanimously resolved to suspend our own payments, as long as we shall judge it proper and necessary, and that we shall not acquit them, or the counter-protests that shall come from you, or any whatever.

“This is the resolution we have unanimously taken, and from which we will not depart, happen what will. The fate of the general commerce of all Europe is at present absolutely in your hands; determine, gentlemen, whether you should crush it totally, or support it.”

The letter, however, came too late to exercise any influence, as the Neufvilles had been allowed to fail six days before. A general failure took place, eighteen houses immediately stopped payment. A much greater number in Hamburg immediately followed, and no business was for some time transacted but for ready money. The failures were equally general in many others of the chief cities of Germany. A conspicuous example that credit may be just as easily abused under a metallic currency, as under a paper one. This crisis extended to England, and Smith says that the Bank made advances to merchants to the amount of a million.

76. In 1764 the Bank's Charter expired. The terms of renewal were an absolute gift of £110,000 to the nation, and a loan of £1,000,000 on Exchequer bills for two years, at 3 per cent. interest. The charter was then renewed on these terms till twelve months' notice after 1st August, 1786, and the repayment of the Government debt.

77. In 1772 the first of those great commercial panics took place, in which the Bank was called upon to take a prominent part in supporting commercial credit. The preceding two years had been distinguished by the most extravagant overtrading. On the 10th June, 1772, Heale and Co., Bankers in Threadneedle Street, stopped payment, involving several others. The Bank of England and some merchants came forward to support credit, which had the appearance for a few days, of being successful; but in ten days' time a general crash ensued. The whole city was in consternation, there had not been such a prospect of a general bankruptcy since the South Sea scheme. By the measures taken, the panic was at length allayed, but the bankruptcies of that year amounted to the unprecedented number of 525. These speculations had been general throughout Europe, and in 1773 the crash extended to Holland. About the beginning of the year, the failures of that country were of so alarming a nature, and so extensive in their influence, as to threaten a mortal blow to all public and private credit throughout Europe. They were caused by great speculative dealings in trade, as well as in the public funds of different countries, and the losses were estimated at £10,000,000.

78. We have, in a previous chapter, remarked that during the course of this century, the coinage was progressively deteriorating, and that a Committee of the House of Commons reported, that on a considerable amount of the gold coinage, the deficiency was about 9 per cent.; in the year 1774, the great re-coinage was ordered. The market price of gold well illustrates this deterioration:—

Before the re-coinage.

	Market Price of Gold.
July, 1718	£3 19 10
Jan. 1721	3 18 6
„ 1730	3 18 11
„ 1754	3 18 5
„ 1761	3 18 10
„ 1772	4 1 0

After the re-coinage.

Jan. 1782	3 17 6
„ 1790	3 17 6

And it continued at this rate till September, 1797.

79. The next renewal of the charter was in 1781, when, upon the Bank's advancing £2,000,000 at 3 per cent. interest for three years, the charter was renewed till twelve months' notice after the 1st August, 1812, and the payment of the public debt. In

the next year a call of £8 per cent. on the capital produced £862,000, and the paid-up capital of the Bank was £11,612,400. The renewal of the charter five years before its expiry excited very keen discussion. The Ministry, however, eulogized the eminent public services the Bank had rendered for ninety years, and warmly deprecated any attempt to interfere with its privileges. They carried their plan by a majority of 109 to 30. Considering that the 3 per cents. were then at 58, the offer of the Bank was a very great accommodation to the State.

80. It was about this period, though the exact date is difficult to ascertain, nor is it very material, that the London bankers introduced a change in the method of doing their business. Instead of giving their customers notes or deposit receipts for the sums left with them, they gave them *cheque* books, or books with a number of blank drafts upon themselves. The customer kept these books at his own house, and, whenever he had occasion to make a payment, he filled up one of these blank drafts in the payee's favor, and the banker undertook to pay such a draft on demand, provided he had funds of his customer's in his hands to meet them, just as he was in the habit of paying his own notes on demand. This method of doing business had so many advantages over that of bank notes, that it universally superseded them in London. From that period London bankers ceased entirely to issue notes, though they never were forbidden to do so until the Act of 1844. This change, simple as it may appear, is of great historical interest, for we shall see hereafter that it was this circumstance that destroyed the monopoly of the Bank of England. Bank notes, we have seen, are nothing but promissory notes, payable to bearer on demand. So these cheques are simply unaccepted bills of exchange payable to bearer on demand. By a fortunate accident, the opportunity that this method afforded of circumventing the monopoly of the Bank, was not discovered till many years afterwards. If it had been, there cannot be a doubt but that Parliament would have put it down very quickly; when it was discovered, the age of such monopolies had passed away, and the demand of the Bank to have it provided against was refused.

81. The termination of the seven years' war took place in 1763, when it is usually said that this nation finally took that rank in the scale of nations which she at present holds. After long and doubtful contests, in which victory often trembled in the balance, the star of England triumphed over that of France, both in the East and in the West. Coincidentally with this, the industrial energies and mechanical genius of the nation burst forth with unparalleled splendour. Previously to this time, Great Britain was probably more backward in great public

works than any State in Europe. She could show nothing that could be compared with the great French and Spanish engineering works. The first canal in France preceded the first canal in England by 150 years. The great canal of Languedoc was completed upwards of half a century before the smallest canal was begun in England. And Spain had preceded France by three quarters of a century. She owes the canal of the Ebro to the genius of Charles V. In Italy, Gerbert, the morning star of modern literature and science, was famous for his hydraulic works in 999. And those of Lombardy, executed in the eleventh century, are still the admiration of modern engineers. The first Act for a work of this nature, however small, in England, was passed in 1755. Facility, quickness, and cheapness of transit are the very foundations of commercial greatness. Brindley, the father of the modern commercial greatness of England, completed the canal from Worsley to Manchester in 1762. This was as prodigious a stride in advance of the age as the opening of the railway from Manchester to Liverpool was in its day. The success of this was triumphant. Then commenced the great era of canal making. Within 25 years the country was covered with a network of canals such as no other country in Europe, but Holland, can boast. Taking into consideration the comparative wealth of the country at the two periods, the period from 1770 to 1795 was fully as wonderful an effort in canal-making, as the period from 1830 to 1855 was in railway making. Concurrently with this prodigious extension of the facilities of transport, an equal extension of the powers of production took place. It would almost seem like a dispensation of Providence, that at this particular period such an extraordinary outburst of mechanical genius took place. It would almost seem that these three men, Brindley, Arkwright, and Watt, were specially raised up by Providence to elaborate those miraculous resources, which it is impossible to doubt, carried this country triumphantly through that terrific contest which was then just about to burst upon the world.

82. It was just at this period that the original sin of the monopoly of the Bank of England began to tell with full force upon the country. Now were the seeds of future ruin, misery, and desolation, sown broadcast throughout the land. The prodigious development of all these industrial works demanded a great extension of the currency to carry them on. What was required was to have banks of undoubted wealth and solidity to issue such a currency. Bank of England notes had no circulation beyond London. Its monopoly prevented any other great banks being formed, either in London or the country, and it would not extend its branches into the country. Scotland at this time possessed three great and powerful Joint Stock Banks,

and it was just at this period that they began successfully to extend their branches into the country. England required to have a currency, and, as it could not have a good one, it had a bad. Multitudes of miserable shopkeepers in the country, grocers, tailors, drapers, started up like mushrooms and turned bankers, and issued their notes, inundating the country with their miserable rags. Burke says, that when he came to England in 1750, there were not twelve bankers out of London; in 1793 there were nearly 400. In 1775 an Act was passed to prohibit bankers issuing notes of less than 20s., and two years afterwards of less than £5. It is no doubt true, that many of the most respectable banking firms of the present day, also took their rise at this time, but they were, comparatively speaking, few. The great majority were such as we have described above.

83. The state of the foreign exchanges, and the condition of coinage about this period, offer many instructive examples of the truth of the principles laid down in the chapter on Exchanges, but we shall reserve them till we come to the consideration of the Bullion Report, when they will be fully discussed.

84. In 1782 the unhappy war with America was fortunately terminated, and immediately a prodigious extension of the foreign commerce, which had been previously unusually restricted, took place. The enormous markets thrown open to the merchants, led to the most extravagant overtrading, which was greatly fostered by the most incautious issues from the Bank, and a very alarming drain of specie from the Bank, which produced a crisis, threatening to compel them to stop payment. The directors, however, considered that if they could only restrain their issues for a short period, the returns in specie in payment of the exports would soon set in in a more rapid manner than they went out. They determined, therefore, to make no communication to the Government, *but for the present to contract their issues UNTIL THE EXCHANGES TURNED IN THEIR FAVOR.* The alarm felt by the Bank was greatest in the month of May, 1783. They then refused to make any advances to Government on the loan of that year, but they did not make any demand for payment of the other advances to Government, which were then between nine and ten millions. They continued this policy up to October, when at length the drain had ceased from the country, and money had begun to flow in from abroad. At length, in the autumn, when the favourable signs began to appear, they advanced freely to Government on the loan, although at that time the cash in the bank was actually lower than at the time when they felt the greatest apprehensions. It was then reduced to £473,000.

85. The doctrine then stated by Mr. Bosanquet, that guided the directors, was this:—That while a drain of specie is going on, their issues should be contracted as much as possible, but that as soon as the tide had given signs of ceasing, and turning the other way, it was then safe to extend their issues freely. This was the policy they acted upon, and it was entirely successful, and the credit of the Bank was saved.

86. The period succeeding the American war was one of great apparent prosperity throughout Europe. People firmly believed that all wars were come to an end, and the reign of perpetual peace had begun. The fierce enthusiasm which had distracted Germany for so many years with religious wars, had abated, and the despotic sovereigns of that country, with no apparent object of terror, had become sensibly milder in their administration. The Press had attained unwonted freedom. To the unobserving eye, nothing betokened any symptoms of disturbance; and the writings of philosophers propagated the belief that the indefinite progress of human perfectibility was at hand. Europe was at last roused from its dream of security by the terrific progress of the French Revolution.

87. Mr. Tooke states, from his own personal recollection, that there had been an enormous and undue extension of commercial speculation, not only in the internal trade and banking of this country, but also throughout Europe and the United States, for some years previous to 1792. The amount of bank notes in circulation, which was under six millions in 1784, had increased to nearly eleven millions and a half in 1792. At length, in the autumn of 1792, commercial failures began both here and abroad, as well as in America. The average of bankruptcies during the first ten months had been 50, in November they suddenly rose to 105. This unusual number created much uneasiness, but they diminished greatly in December. In January, 1793, they rose again. The French Revolution was now advancing with rapid strides; the King had been a prisoner ever since the 10th August. In November the Convention published what was tantamount to a declaration of war against every established Government in Europe. Great Britain thought it time to arm. The militia were called out, and on the 13th December Parliament met, and the King called the attention of the Houses to the increasing political ferment in the country, which had shown itself in acts of riot and insurrection. He said that the agitators were evidently acting in concert with persons abroad, and that it was impossible to see, without the most serious uneasiness, the evident intention of the French to excite disturbances in foreign countries, wholly contrary to the law of nations. Under these circumstances it became necessary to augment the military and naval forces

of the country. An angry correspondence between the Governments inflamed the passions of both nations, and, on the execution of the King, the British Government expelled the French Ambassador, and the Convention instantly declared war. The declaration of war, though it must evidently have been foreseen, gave a shock to credit, which was already staggering. On the 15th February a house of considerable magnitude, deep in corn speculations, failed, and on the 19th, the Bank refused the paper of Lane, Son, and Fraser, who stopped next morning to the amount of nearly one million, involving a great number of other respectable houses. In the meantime, the panic spread to the bankers. It began at Newcastle. The partners in the Banks at Newcastle were opulent, but their private fortunes were locked up. They issued notes which allowed interest to commence at some months after date, and then they were payable on demand, when the run came they were unable to realise, and stopped payment. The panic immediately spread throughout the country. It was computed that there were nearly 400 country Banks at that time, of these 300 were much shaken, and upwards of 100 stopped payment. The Banks of Exeter and the West of England almost alone stood their ground. They issued notes payable at 20 days' sight, with interest commencing from the date of the note, and ceasing on the day of acceptance. The best contemporary authorities are unanimous in attributing this terrible disaster to the inordinate multiplication and reckless operations of these country "bankers," which had been established in almost every town and even villages in the country.

88. This great pressure extended to the London bankers as well as the country ones. One of them says that the extraordinary state of credit had obliged every person connected with trade and money transactions, to gather in and husband every resource to meet all demands. That for six weeks back every man of money and resources had been straining every nerve to support himself and immediate friends, and could not give that support to others which they would have been disposed to do. All these circumstances naturally produced a demand on the Bank of England for support and discounts. But the Bank, being thoroughly alarmed, resolved to contract its issues: bankruptcies multiplied with frightful rapidity. The Government urged the Bank to come forward and support credit, but they resolutely declined.

89. Sir Francis Baring (*Observations on the Establishment of the Bank of England*) greatly blames the directors for their conduct on this occasion. He says that they at first accommodated themselves to the crisis, but their nerves could not support the daily demand for guineas, and, for the purpose of

checking that demand, they curtailed their discounts to a point never before experienced; and that if they determined to reduce their issues, it should have been gradual. Their determination, and the extent to which it was carried, came like an electric shock.

90. He says that there are three different causes for a great demand for guineas:—

1. For export.

2. For the purpose of hoarding, from want of confidence in the Government, and in the circulating paper.

3. To enable country Banks to discharge their demands, whilst confidence in the Government and in the bank remained entire.

That every measure ought to be taken to prevent and mitigate the first cause, except prohibition or bankruptcy. We may reserve the second till we come to 1797. That the third ought to be viewed, not with indifference, but with a disposition to spend almost their last guinea. He shews, from the state of the exchanges, that it was quite impossible the guineas could have left the country, as the loss on exporting them to Amsterdam was £3 6s. 3d., and to Hamburg £4 2s. 6d. per cent., and it was notorious that large quantities of gold and silver were coming in from France. The cause of this was the continued depreciation of the Assignats. Under these circumstances, he says that the directors acted quite wrongly, they ought to have seen that the guineas would have very soon come back to them, and that they ought, in fact, to have followed the precedent of 1783, which had been so successful.

91. When the Bank adopted this perverse course, universal failure seemed imminent. Sir John Sinclair remembered the precedent of 1697, when Montague had sustained public credit by an issue of Exchequer bills, and thought that a similar plan might be followed in this crisis. The Minister desired him to propose a scheme for the purpose, which he presented on the 16th April. A Committee of the House of Commons was immediately appointed. In the mean time a director of the Royal Bank of Scotland came up with the most alarming news from Scotland. The public banks were wholly unable, with due regard to their own safety, to furnish the accommodation necessary to support commercial houses, and the country bankers. That unless they received immediate assistance from Government, general failure would ensue. Numerous houses, who were perfectly solvent, must fall, unless they could obtain temporary relief. Mr. Macdowall, M P. for Glasgow, stated that the commercial houses and manufactories there were in the greatest distress from the total destruction of credit. That this distress arose from the refusal of the Glasgow, Paisley, and Greenock

banks to discount, as their notes were poured in upon them for gold.

92. The Committee reported that the general embarrassment of commercial credit was so notorious as to call for an immediate remedy, without much examination. That the failures which had taken place had begun with a run on those houses that issued circulating paper without sufficient capital, but had extended so as to affect many houses of great solidity, and possessed of funds ultimately much more than sufficient to answer all demands upon them, but which could not convert those funds into money in time to meet the pressure. That the sudden discredit of so large amount of bankers' notes had produced a most inconvenient deficiency of the circulating medium. These circumstances had caused bankers to hoard to a great extent. That unless a circulating medium was provided, a general stoppage must take place. That they had requested a number of the most eminent merchants to meet and consider a plan of issuing Exchequer bills to a certain amount, under proper regulations, who had unanimously agreed in the propriety of such a course, as the best remedy that could be devised.

93. The Committee recommended that Exchequer bills to the amount of £5,000,000 should be issued under the directions of a board of commissioners appointed for that purpose, in sums of £100, £50, and £20, and under proper regulations. After considerable doubts were expressed by Mr. Fox and Mr. Grey, as to the policy of this extraordinary measure, which was unknown to the constitution and might subvert our liberties, the bill passed.

94. No sooner was the Act passed than the Committee set to work. A large sum of money, £70,000, was sent down to Manchester and Glasgow on the strength of the Exchequer bills, which were not yet issued. This unexpected supply, coming so much earlier than was expected, operated like magic, and had a greater effect in restoring credit than ten times the sum could have had at a later period.

95. When the whole business was concluded, a report was presented to the Treasury. It stated the knowledge that the loans might be had operated, in many instances, to prevent them being required. The whole number of applications was 338, and the sum applied for £3,855,624, of which 238 were granted, amounting to £2,202,000; 45 for sums to the amount of £1,215,100 were withdrawn, and 49 rejected. The whole sum advanced was repaid; two only of the parties assisted, became bankrupt, all the others were ultimately solvent, and in many instances possessed of great property. A considerable part of

the sum was repaid before it was due, and all the rest with the utmost punctuality. So much scrupulous care was taken to preserve secrecy as to the names of the applicants, that they were not known to that hour except to the Commissioners and their own sureties. After all expenses were paid, the transaction left a clear profit to the Government of £4,348.

96. Whatever were the prognostications of its futility and danger before it was done, its success was perfect and complete. The contemporary writers all bear witness to the extraordinary effects produced. Macpherson says, that the very intimation of the intention of the Legislature to support the merchants, operated like a charm all over the country, and in a great degree superseded the necessity of the relief by an almost instantaneous restoration of confidence. Sir Francis Baring concurs in this view, and adduces the remarkable success of the measure as an argument to shew the mistaken policy of the Bank. The panic was at length happily staid. The failures up to July had been 932, in the remaining five months they were reduced to 372. The gold continued to flow in, and in the last six months of 1793, and during the two following years, money became as plentiful as in time of peace, and 4 per cent. interest could scarcely be got.

97. All contemporary writers bear witness to the wonderful success of this expedient. After careful deliberation the Bullion Report warmly approved of it, censured the proceedings of the Bank of England, and especially cite it as an illustration of a principle which they laid down, that an enlarged accommodation is the true remedy for that occasional failure of confidence in the country districts to which our system of paper credit is unavoidably exposed.

98. Notwithstanding all this weight of testimony in favor of the happy effects of this measure, some rigid doctrinaires afterwards condemned the proceedings as a violation of the true principles of Political Economy. Even some who helped to devise it, changed their opinion afterwards upon the subject. Thus, Lord Sidmouth, in 1811, observed that he was, upon consideration, inclined to doubt of its wisdom and policy. Lord Grenville also said, that from experience and reflection he was convinced the measure was founded on wrong policy; as one of those who were concerned in the measure, he was perfectly ready to avow his error, for he was perfectly satisfied in his own mind that it was unwise and impolitic.

99. It appears to us that the reply to these objections is short and simple. In the first place, if it were a violation of the true

principles of Political Economy, it immediately resolves itself into a question of loss of capital. It is quite easy to shew that all great errors in Political Economy are destructive of capital. They may be estimated in money. Was this measure a pecuniary loss to the country? But what would have been the loss to the country if it had not been adopted? Who can estimate the destruction of capital that would have ensued in the general wreck of public credit? It might have endangered the safety of the State. But there are other arguments which appear to us to be conclusive as to its propriety. The general loss of credit was chiefly caused by a thorough want of confidence in the *cûrrency* of the country. The miserable notes of the majority of bankers were utterly blown upon. The great desideratum was a sound currency. Now, what was it that caused such an unsafe currency to be in circulation? It was nothing but the unjustifiable monopoly of the Bank of England. It was this monopoly, which was itself the most flagrant violation of the true principles of Political Economy, which caused the bad character of the currency. Consequently the measure of the Government, in providing a currency in which people would have confidence, was merely a correction of the error which had produced these deplorable results. An undesirable one, it may be, but yet no better one was possible under the circumstances.

100. Sir Francis Baring and Mr. Tooke both agree in saying that nothing could be more satisfactory than the financial condition of the country during 1794 and part of 1795. Both agree that the circumstances of the embarrassments, which led to the catastrophe of 1797, began in the latter part of the year 1795. Mr. Tooke places the commencement rather earlier than Sir F. Baring. He states that the winter of 1794-5, was one of the severest on record, and that, in the spring or summer of 1795, apprehensions began to be felt for the growing crops. The prices of all sorts of corn advanced rapidly. The spring of 1795 was very cold and backward, the summer wet and stormy, and the harvest unusually late. Under these circumstances, wheat, which was at 55s. in January, reached 108s. in August. The same scarcity was general throughout Europe and America. France was in a still worse position than England, and the Government, still further to embarrass her and afford relief to this country, seized all neutral vessels laden with corn bound for France; it also employed agents to buy corn in the Baltic ports, where its price had already been raised greatly, in consequence of large purchases on account of the French Government.

101. Sir Francis Baring also states (p. 46) that the method in which the Government contracted the loan that year tended much to aggravate the evil. He says that, in former wars, it

had been usual for the Government to contract with none but the most respectable monied men, who had the undoubted power to fulfil their engagements. On this occasion, the Minister contracted with men who did not possess those powers, and in order to make good their payments, they were obliged to have recourse to operations on foreign places, which deranged the exchanges, and had a still greater effect on raising the rate of interest in this country.

102. These causes alone were sufficient to create a monetary pressure, but, though they would have been inconvenient, there would have been nothing to create alarm in them. They were, however, aggravated and intensified by other circumstances, which we must now relate.

103. The enormous abuses which might be perpetrated by an unscrupulous Government, and the dangerous power which so potent an engine as the Bank of England would confer upon them, had been clearly foreseen by its antagonists, at the time of its foundation, and had inspired them with a well-grounded jealousy. We have seen that stringent precautions were taken in the first Act of 1694, to prevent the Bank making any advances to Government, without the express permission of Parliament. It had been the custom, however, time out of mind, to advance for the amount of such Treasury bills of exchange, as were made payable at the Bank, to the amount of £20,000 or £30,000, when it was usual for the Treasury to send down orders to set off such advances against the accounts to which they properly belonged. If ever these advances reached £50,000 it was a subject of complaint. In the American war these limits had been much exceeded, and sometimes reached £150,000. Mr. Bosanquet was Governor of the Bank in 1793, and the legality of such proceedings excited grave doubts in his mind, and, after consulting with his brother directors, they agreed that it was a serious question whether the penalties provided in the the Act did not extend to such transactions. They, therefore, thought it would be expedient to apply to the Government, to obtain an Act of indemnity, to relieve them from any penalties they might have incurred, and to permit such transactions to a limited amount. Mr. Bosanquet, who conducted the negotiation with Mr. Pitt, expressly says, that Mr. Pitt proposed to bring in a clause which should indemnify the directors to advance *to a limited amount*. He says, that it was originally intended that the penalty should be taken off only in case the advance on Treasury bills should be restrained within a limited sum. This limited amount was intended to be fixed at £50,000 or £100,000. Mr. Bosanquet, however, then went out of office, and was unable further to attend to the negotiation. Mr. Pitt was much too

keen not to see at once the enormous facilities Government would obtain if this Act were passed. Accordingly, he pressed it quickly through Parliament, but he took care to omit any clause of limitation (Statute 1793, c. 32). Never had such a formidable engine been placed in the hands of a Minister. He was now armed with an unbounded power of drawing upon the Bank, with nothing to restrain him, unless the directors should take the audacious step of dishonoring his bills. The Bank, henceforth, was almost entirely at his mercy, and then he plunged headlong into that reckless career of scattering English gold broadcast over Europe.

104. No sooner had Mr. Pitt surreptitiously obtained this power over the Bank, than he set all bounds of moderation at defiance, and, sure of being able to command unlimited supplies at home, he proceeded to send over enormous amounts of specie to foreign powers. In 1793 the subsidy and sums paid to foreign emigrants amounted to £701,475. In 1794 the foreign subsidies were £2,641,953; in 1795 they amounted to £6,253,140. Thus, in three years, the sums sent abroad amounted to upwards of nine millions and a half. These, however, were not the totals of the specie sent abroad on other accounts. In 1793 it was £2,715,232; in 1794 £8,335,592; in 1795 £11,010,236. These great remittances had the inevitable effect of making the foreign exchanges adverse, and excited the greatest alarm in the Bank parlour. At the same time that this great drain of specie was going on, the Treasury bills increased to an unprecedented amount, and the demands for accommodation from the commercial world were equally pressing. Nothing could be more unpleasant than the situation of the Directors, placed between these powerful parties contending for accommodation, which it was daily becoming less in their power to give. So early as the 11th December, 1794, the directors foresaw the ensuing pressure, and made representations to Mr. Pitt. In January, 1795, it became necessary to adopt a firmer attitude, and on the 15th they passed a resolution, that with a foreign loan of six millions, and a home one of eighteen millions about to be raised, the Chancellor of the Exchequer must be requested to make his financial arrangements for the year, without requiring further assistance from them; and more particularly, that they could not allow the advances on Treasury bills at any one time to exceed £500,000. Mr. Pitt promised to reduce them to that amount by payments out of the first loan.

105. He, however, paid little regard to these remonstrances; and, on the 16th April, they were compelled to remind him that he had not kept his promise that the sum should be reduced. They told him that they had come to a resolution that they

would not, in future, permit the advances to exceed the stipulated sum. Mr. Pitt pretended he had forgotten the circumstance in the multiplicity of business, and promised that the sum should be immediately paid. Nevertheless, no reduction took place in the amount; another remonstrance was equally ineffectual, and on the 30th July the Directors informed him that they intended, after a certain day, to give orders to their cashiers to refuse payment of all bills, when the amount exceeded £500,000. Mr. Pitt was not prepared to comply with the request, and on the 6th August he applied to them for another advance of two millions and a half, but they refused to take his letter into consideration, until he had made satisfactory arrangements with them for the repayment of the other advances. After some further communications, they agreed to the loan for £2,000,000.

106. The Act of Mr. Pitt had, in fact, deprived the directors of all control over the Bank. The foreign exchanges began to fall rapidly towards the end of 1794, and in May, 1795, had reached such a depression as to make it profitable to export bullion, and this circumstance, as well as the knowledge that several foreign loans were in progress, should have warned the directors of the necessity of contracting their issues; such was the course laid down by the directors in 1783. Instead of that, their issues were greatly extended. In the quarter from January to March, 1795, they stood higher than they had ever done before, though we must, in common fairness, acquit the directors of the whole blame. The amount of their issues in August, 1794, was little more than ten millions; in February, 1795, it had increased to fourteen millions, but this was chiefly caused by the bills which were drawn on the Treasury on behalf of foreign Governments, which were made payable at the Bank. The directors had then to choose between endangering their own safety, or declaring the Government bankrupt.

107. All these concurrent causes which we have detailed, began to produce their full effects in the autumn of 1795. The drain commenced in September, and proceeded with alarming rapidity. On the 8th October, the Bank made a formal communication to Government, that it excited such serious apprehensions in their minds, that they felt it an absolute necessity that the advances to the Government must be diminished. They reminded him of the warning they had given in the beginning of the year as to the danger of the foreign loans, which had been fully verified, and that numerous other payments must shortly be provided for. That the market price of gold was then £4 4s. per ounce. Under these circumstances, the Bank could lend no further assistance to the Government. On the 23rd of the same month, the directors having heard rumours of

a new loan, waited on Mr. Pitt, who professed that he had not, at present, the most distant idea of one. On the 18th November, the Governor informed Mr. Pitt that the drain continued with unabated severity, and that the market price of gold was £1 2s. per ounce, and said that rumours were in circulation that another loan was intended, notwithstanding Mr. Pitt's denial of it so lately. Mr. Pitt said that since their last interview the successes of the Austrians had been so great against the French, that he was of opinion that it would highly conduce to the common cause to aid them with another loan, not exceeding £2,000,000, but he added that if such a course would be hazardous to the Bank, every other consideration should be overlooked, and the loan abandoned.

108. Parliament met on the 29th October, in the midst of great public excitement and dissatisfaction. The King was saluted with loud hootings and groanings, and volleys of stones were flung at his carriage, as he went to open the Session. The Speech said that he had observed for some time past, with the greatest anxiety, the very high price of grain, and that this anxiety was much increased by the deficiency of the harvest that year. A Committee of the House of Commons was immediately afterwards appointed to consider the high price of corn. In December, the House came to strong resolutions as to the necessity of diminishing the consumption of wheat, as much as possible, and the members of both Houses signed an engagement to diminish the quantity by at least one-third, and to use their influence to persuade others to do the same; and an Act was passed offering heavy bounties for the importation of corn.

109. This project of a loan going on, and being now proposed to be £3,000,000, the Court of Directors, after a very solemn deliberation, on the 3rd December, came to the unanimous resolution that, if the loan proceeded, they had the most cogent reasons to apprehend very momentous and alarming consequences from the actual effects of the last loan, and the continued drain of specie and bullion. In answer to this representation, Mr. Pitt solemnly promised them that he should lay aside all thought of it, unless the situation of the Bank should so alter as to render such a loan of no importance to them.

110. The directors at last found that it was absolutely necessary to choose between making the Government bankrupt, and taking stringent measures to restrict their accommodation to the merchants. They resolved to fix beforehand the amount of advances they could make day by day, and gave notice that, if the application on any day exceeded the sum so resolved to be

advanced, *pro rata* proportion of each applicant's bills should be returned without regard to the respectability of the party or the solidity of the bills.

111. As matters continued to get worse, the directors had several communications with Mr. Pitt, in January and February, 1796, but the project of the foreign loan being much dwelt upon with much earnestness by Mr. Pitt, on the 11th February they came to a resolution which was communicated to him the same day:—

“That it is the opinion of this Court, founded upon its experience of the effects of the late Imperial loan, that if any further loan or advance of money to the Emperor, or other foreign State, should, in the present state of affairs, take place, it will in all probability prove fatal to the Bank of England.

“The Court of Directors do therefore most earnestly deprecate the adoption of any such measure, and they solemnly protest against any responsibility for the calamitous consequences that may follow thereupon.”

Mr. Pitt replied, that after the repeated promises he had made that no further loan should be made without communication with the Bank, and a consideration of their circumstances, he saw no occasion for these resolutions, and that he should regard them as having been made in a moment of needless alarm.

112. We have already seen, from Mr. Pitt's conduct in the affair of the clause relating to the advances on Treasury bills, that he was not bound by any very scrupulous notions of honour. On this occasion he departed still further from the right path, for, notwithstanding all his solemn promises, so frequently and emphatically made, the Directors discovered that remittances were still continuing to be clandestinely made. In several interviews with him, the Governor of the Bank stated that he apprehended these remittances were being made, but Mr. Pitt did not offer any explanation, and it was afterwards ascertained that they were going on.

113. Under the influence of all these combined drains of specie, the exchanges with Hamburg were in a state of extreme depression, during the first three months of 1796. Sir F. Baring shews that during January the profit was £7 10s. per cent.; during February £6 10s.; and during March £8 7s. 6d. in transmitting gold to that place. At length the several drains began to diminish. An abundant supply of corn was obtained. The continued contraction of the bank issues, and the cessation of the transmission of specie, caused the exchanges to assume a favourable aspect in the beginning of April, and it continued steadily to increase till February, 1797.

114. The stringent measures adopted by the Bank to contract its issues, caused much complaint amongst mercantile men, and a meeting of bankers and merchants was held at the London Tavern, on the 2nd April, who resolved, that an alarming scarcity of money existed in the City of London, which was caused chiefly, if not entirely, by an increase in the commerce of the country, and the great diminution of mercantile discounts by the Bank. They resolved that if means could be found to augment the circulating medium, without infringing the privileges of the Bank of England, so as to restore the amount to what it was before the contraction of discounts, it was the duty of every friend to trade to give such a plan the most earnest support. The meeting appointed a Committee to prepare a plan for such a purpose. Mr. Boyd drew up a long report on behalf of the Committee, which proposed that a Board of twenty-five members should be appointed by Parliament, who should be authorized to issue promissory notes, payable at six months after date, bearing interest at 1½d. per £100 per day, upon receiving the value in gold and silver, Bank of England notes, or in Bills of Exchange having not more than three months to run. The Committee had an interview with the Chancellor of the Exchequer on the subject, and he informed them that the directors of the Bank had proposed, as a remedy, that the floating debt should be funded, which plan he determined to try before adopting their plan. This was accordingly done, but it produced no relief.

115. Mr. Pitt had never fulfilled his promise, so often repeated to the directors, that the advances on Treasury bills should be reduced to £500,000; on the 14th June, 1796, they stood at £1,232,649. At the end of July, he sent an earnest request to have £800,000 at once, and a similar sum in August. They were induced to consent to the first, but refused the second advance. Mr. Pitt said that the first advance without the second would be of no use to him, and begged them to reconsider their decision. The directors, thus pressed, were driven to assent to it, but they accompanied it with a most serious and solemn remonstrance, which they desired should be laid before the Cabinet. They said that nothing under present circumstances could induce them to comply with the demand, except the dread of a worse evil following the refusal, and they said that this advance would incapacitate them from granting any further assistance during the year. They closed their remonstrance by saying:—

“They likewise consent to this measure in a firm reliance that the repeated promises so frequently made to them, that the advances on the Treasury bills should be completely done away, may be actually fulfilled at the next meeting of Parliament, and the necessary arrangements taken to prevent the same from ever

happening again, as they conceive it to be an unconstitutional mode of raising money, what they are not warranted by their charter to consent to, and an advance always extremely inconvenient to themselves."

However, in November, Mr. Pitt made a fresh demand on them for £2,750,000 on the security of the Land and Malt Taxes of 1797, which was granted on condition that the advances on Treasury bills amounting to £1,513,345 were paid out of it.

116. Mr. Pitt took the money, but never paid off the bills. The Directors again sent on the 1st February 1797, to demand payment of them, as they then amounted to £1,554,635 and would in a few days be increased by nearly £300,000 more. Mr. Pitt made many excuses for the non-payment, and promised to make an endeavour do so, but he dropped a hint that another large sum of bills had come in from St. Domingo. Upon being pressed as to the amount, he said that it was about £700,000. The Governor expressed the greatest apprehensions, and begged him to delay the acceptance as long as he could. Mr. Pitt then hinted that he should want a large sum for Ireland, which he said would be about £200,000. The Governor assured him that the drain of cash had been continuous and severe of late, and that such a demand would be very dangerous.

117. The enormous failures of the country bankers in 1793, had been followed by a permanent diminution of the issues of country banks to a prodigious extent. Mr. Henry Thornton, after instituting extensive enquiries in different parts of the country, stated, as the result, that the country bank notes were reduced by at least one half, and that the wants of commerce had caused a very large quantity of guineas to be drawn into the country, to supply their place. Meantime, as we have already observed, although the foreign exchanges had become favourable, the Bank still continued to adhere, with the utmost severity, to its policy of restriction throughout the autumn of 1796, and during the last three months they were no higher than they had been in 1782, with an amount of commerce many times larger than in that year. Commercial payments required to be made in some medium in which the public had confidence. As the public could not get notes, they made a steady and continuous demand for guineas. The bullion in the Bank in March, 1796, was £2,972,000; in September, £2,532,004; and in December, £2,508,000. When a drain set in more severely than ever.

118. At this period the political situation of the country was in the most gloomy condition. The war-like combinations of Mr. Pitt had totally failed, and all Europe was now smarting under the consequences of their suicidal folly in meddling with the

French Republic. Mr. Burke had pronounced, in 1790, that France was, in a political light, expunged from the system of Europe; that it was doubtful whether she would ever appear in it again. That *Gallos quoque in bellis floruisse audicimus* would possibly be the language of the next generation. So much for political prophecy! That country, which had been supposed to offer so easy a prey to surrounding nations, and whose epitaph Mr. Burke had suggested, was now the most powerful State in Europe. She had quelled internal dissensions in torrents of blood, and poured forth her armies in a resistless torrent to avenge herself upon the haughty States which had presumed to meddle with her domestic condition. Great Britain, which had commenced the war with every other State in Europe as her ally, was now left alone. The Directory had subdued Spain by artifice and negotiation, and concluded a treaty with her, offensive and defensive, at St. Ildefonso, on the 19th August. The campaign of Napoleon, in 1796, in the north of Italy, is generally allowed to be equal, if not superior, in brilliancy, to any subsequent one. By a series of marvellous victories, he drove the Austrians out of Italy, and, in the beginning of 1797, Rome was only saved from conquest by absolute submission at Tolentino; and, within a month, Venice was annihilated, and Austria sued for peace at Leoben. This great reverse of circumstances had strengthened the party who had always been advocates for peace in England, and Mr. Pitt was compelled to make overtures for peace in October, 1796. A British envoy was sent to treat with the Directory, and he staid in Paris for two months; but, as neither party was sincere, the treaty came to nothing. The fact was, that peace was the furthest thing possible from the thoughts of the Directory. After the conquest of La Vendee, they had an army of 100,000 men set free, under a general who is usually acknowledged to have been the equal of Napoleon in military talent, and who was burning to emulate his exploits in Italy. While the pretended negotiations for peace were going on, the Directory were organizing an immense expedition for the invasion of Ireland. The orders to sail were transmitted to it several weeks before the British envoy was expelled from Paris, and it actually sailed two days before he left. Fortunately this great armada was dispersed by a tempest, a few straggling vessels reached Ireland in the last week of December, but the rest were obliged to put back to France.

119. This terrible menace which had been so long hanging over the country, and whose destination it was vain to conceal, inspired the utmost alarm, and there was a continual demand for guineas in Ireland. The year 1797 commenced with the most gloomy apprehensions and depression; the country bankers

discerned that the first burst of the storm would fall upon them, and determined to provide for it, by obtaining as much specie as they could from London, and, accordingly, the drain continued with increased rapidity after the beginning of the year.

120. Mr. Pitt had hinted in his interview with the Governor of the Bank on the 1st February, that a loan for Ireland would probably be required, which would probably not exceed £200,000, but soon afterwards the directors was struck with dismay on hearing that the amount required was £1,500,000. On the 10th February the directors came to a resolution that before they could entertain any proposal for the Irish loan, the Government must pay off debts to them amounting to £7,186,445, of which they handed him in the details.

121. At this time the banks at Newcastle had a more than ordinary demand upon them for cash. In addition to the manufactories and collieries, the number of troops stationed in that part of the country had been considerably augmented. The banks had imported an extra supply of cash to meet their purposes, and were negotiating for more when an event happened which brought on the crisis. A French frigate went into one of the Welch harbours and landed 1,200 men. At the same time an order came down from Government to take an inventory of the stock of the farmers all along the coast, and to drive it into the interior if necessary. These circumstances created a perfect panic among the farmers: on Saturday the 18th February, being market day, the farmers, who at that time of year had the principal parts of their rents in their hands, actuated by the terror of an immediate invasion, hurried into Newcastle the produce of their farms, which they sold at very low prices, and immediately rushed to the different banks to demand specie. Seeing this universal panic, the banks came to an agreement to stop payment on the Monday, if the panic did not subside, which they accordingly did.

122. On the 21st February the state of the Bank became so alarming, that the directors resolved that the time had come when they must make a communication to the Government. The quantity of bullion had been rapidly diminishing, and the constant calls of the bankers from all parts of the town for cash, shewed them that there must be some extraordinary reason for it. Mr. Pitt was aware that this proceeded from the general alarm of invasion, which he thought was magnified much beyond anything to warrant it. It was agreed that a frigate should be sent over to Hamburg to purchase specie. On the 24th of February, the drain became worse than ever, and inspired them with such alarm for the safety of the House that they sent a

deputation to Mr. Pitt to ask him how long he considered the Bank should continue to pay cash, and when he should think it necessary to interfere. Mr. Pitt said it would be necessary to prepare a proclamation to put a stop to cash payments, and to give parliamentary security for the notes. But in that case it would be necessary to appoint a Secret Committee of the House to look into the affairs of the Bank. The deputation assured him that the Bank would readily agree to this; and it was resolved to call a meeting of chief bankers and merchants of London, to come to some resolution for the support of public credit in this alarming crisis.

123. The news of the stoppage of the Newcastle banks spread like wildfire throughout the country, and soon reached the metropolis. The drain upon the bankers' coffers now became a run; the first serious apprehensions that danger was imminent, were felt on the 21st of February, but the drain then became unexampled, till on Saturday, the 25th, the cash was reduced to £1,272,000. Before this, the directors, in a state of utter bewilderment at the state of the country, had used the most violent efforts to contract their issues. In five weeks they had reduced them by nearly £2,000,000. On the 21st January they were £10,550,830; on the 25th of February they were £8,640,250. But even this gave no true idea of the curtailment of mercantile accommodation, for the private bankers were obliged, for their own security, to follow the example of the Bank. In order to meet their payments persons were obliged to sell their stock of all descriptions, at an enormous sacrifice. The 3 per cents. fell to 51, and other stock in proportion.

124. On Saturday, the 25th, the Court felt that the fatal hour was at last come, when they must for the first time since its institution, come to a total suspension of payments. A meeting of the Cabinet was held on Sunday, at Whitehall, and an order in Council was issued, requiring the directors of the Bank of England to suspend all payments in cash, until the sense of Parliament could be taken on the subject.

125. The King, the next day, sent a message to Parliament, to inform them of the step that had been taken, and recommended the subject to their most serious and immediate attention. Mr. Pitt moved that the message should be taken into consideration the next day, and that he should propose that a Select Committee be appointed to investigate the state of the Bank's affairs, which he believed were in the most solid condition.

126. The directors of the Bank had the order in Council printed and widely circulated, and issued a notice of their own,

to say that the general concerns of the Bank were in the most affluent and prosperous condition, and such as to preclude every doubt as to the security of its notes. At this time the cash in the Bank was reduced to £1,086,170.

127. The relief produced at the instant, by the definite determination to suspend cash payments and extend their issues of paper, was very great. Within one week it increased its accommodation by nearly two millions. On the same day a resolution was entered into by 4,000 of the merchants, in the city, to combine to support the credit of the notes.

128. Both Houses of Parliament appointed Committees to examine into the affairs of the Bank. The Committee of the House of Commons reported the outstanding obligations of the Bank, on the 25th February, were £13,770,390, and the total amount of their assets, £17,597,280, leaving a surplus of £3,126,890 over and above the debt of the Government, amounting to £11,686,800, which paid them 3 per cent.

129. Both Houses reported that it was advisable for the public interest that the suspension of payments should be continued for a limited time, and a bill for that purpose was accordingly brought in. After some debates, which threw very little light on the subject, the Act (Statute 1797, c. 45), was passed. Its chief provisions were:—

1. A clause of indemnity to the Bank and all connected with it, for anything done in pursuance of the order in Council.

2. The Bank forbidden to make any payments in cash to any creditors, except in certain cases, and protected from all law proceedings.

3. The Bank might issue cash in payments for the Army, Navy, or Ordnance, in pursuance of an order from the Privy Council.

4. The Bank was to make no advance above £600,000 for the public service, in cash or notes, during the restriction.

5. If any person deposited any sum, not less than £500, in gold, in exchange for notes in the Bank, it might repay three-fourths of the amount.

6. It might advance £100,000 in cash to the bankers of London, Westminster, and Southwark, and to the Bank of Scotland, and the Royal Bank of Scotland, £25,000 each.

7. Payment of debts in bank notes to be deemed as payments in cash, if offered and accepted as such.

8. No debtor was to be held to special bail, unless the affidavit stated that payment in bank notes had not been offered.

9. Bank notes would be received at par, in payment of taxes.

10. Bank might issue any cash it received since 26th February,

upon giving notice to the Speaker of the House of Commons, and advertising in the "London Gazette," and on the Royal Exchange.

11. The Act to continue till the 24th June.

130. An Act was also passed to enable the Bank to issue notes under £5 (Statute 1797, c. 28), and by c. 32 this power was extended to the country banks, but they were to continue liable to pay money on demand for them, and, in failure of doing so within three days after demand, any justice of the peace might cause the amount and costs to be levied by distress.

131. All banking companies and bankers in Scotland were allowed to issue notes payable to bearer on demand for any sum under 20s.

132. We cannot refrain from noticing that, in the debate on this measure, Mr. Pitt expressed the identical views on the subject of the circulating medium that are the leading principles of this work. He said: "As so much has been said on the matter of a circulating medium, he thought it necessary to notice that he did not for his own part take it to be of that empirical kind which had been generally described. IT APPEARED TO HIM TO CONSIST IN ANYTHING THAT ANSWERED THE GREAT PURPOSES OF TRADE AND COMMERCE, WHETHER IN SPECIE, PAPER, OR ANY OTHER TERMS THAT MIGHT BE USED."

133. An event of such portentous magnitude as the suspension of cash payments by the Bank of England, of whose effects there had been no previous experience, could not fail to give rise to the most conflicting opinions as to the necessity of the measure, of the course of conduct of the directors which led to it, and as to the policy which ought to have been adopted under the drain which occurred in the last week of February, 1797. Many men of great eminence and ability changed their opinions in after times, when they came to look back upon the subsequent events. In examining this question, so as to form a just estimate of the conduct of the directors, we must remember that they were not masters of their own policy. They were distracted by two antagonistic claims, both of which they conceived it impossible to satisfy, at the same time, namely, that of the Chancellor of the Exchequer and the demands of commerce. They considered that if they advanced to the Government they must contract their issues to merchants, and, as the Minister was the more powerful and imperious party of the two, they were obliged to yield to his power.

134. Several of the directors being examined before the committees, unanimously attributed the necessity of stopping pay-

ment to the enormous amount of their advances to Government, and gave it as their decided opinion, that if the Government had repaid these advances, as they ought to have done, that this great catastrophe would have been avoided. We may take it, therefore, as admitted on all hands, that if they had been repaid by Government, they would have very greatly extended their advances to merchants. The real question, then, is, considering that they were under such advances to Government, would it have been prudent to have been more liberal in their accommodations to merchants?

135. Mr. Henry Thornton was very strongly of opinion that the excessive contraction of the Bank notes had produced the most injurious effects in shaking public credit of all descriptions. That the excessive reduction of notes had caused an unusually severe demand for guineas, that the great public distrust was directed against country bank notes, and that the Bank of England ought to have extended their issues, to supply the place of the country notes.

136. Mr. Walter Boyd, an eminent merchant, was very clearly of opinion that the restrictions upon the issue of notes by the Bank was the chief cause of the forced sale and depreciation of the public securities, and, if the Bank had only maintained its issues at the same height as they were in December, 1795, the drain of specie from the Bank, as well as the embarrassments in the mercantile world, would have been avoided, and a great portion of the fall which public securities had experienced, would have been prevented.

137. Mr. George Ellison, who was secretary to an association of a great part of the country banks, considered that the quantity of the coin in the country was greater than it was in 1793, though a very considerable part was hoarded away owing to the public alarms that were abroad. He attributed the great public distrust to the remembrance of the conduct of the Bank in 1793, when it suddenly contracted its discounts, just at the period when they were most wanted.

138. The Committee of the Lords called the attention of the House very strongly to these opinions, but they did not venture themselves to pronounce an opinion on their justness. The Committee of the Commons went considerably nearer towards approving of them. In the year 1810, the Governor of the Bank being examined before the Bullion Committee, stated, that after the experience of their policy of restriction, many of the directors repented of the measure, and the Bullion Committee explicitly condemned the policy of the Bank both in 1793 and 1797.

139. The Directors of the Bank, acting in the midst of such unprecedented circumstances, and so tremendous an emergency, are entitled to have their conduct examined with all forbearance. But, taking all these circumstances into consideration, we cannot fail to acquiesce in the opinion expressed by so many eminent bankers and merchants at the time, by the subsequent avowal that experience had led many of the directors to repent of the policy they then pursued, and by the decided opinion of the Bullion Committee, that the policy pursued by the Bank in this momentous crisis was erroneous, and that the severe restrictions they attempted to place upon commerce, very greatly contributed to bring on the calamity by which they were subsequently overwhelmed. Nothing, in short, could be more unhappy than their regulations of the amount of their issues. When the exchanges were violently adverse, so that it was enormously profitable to export gold, they enlarged them to an extravagant extent, and when the exchanges were extremely favourable, so that gold was sure to flow in, they restricted them with merciless severity. The issues, which were £11,000,000 when the exchange was against the country, were reduced to £8,640,250, when they had been for several months eminently favourable. It appears, from the entire evidence in the reports, that it was this excessive restriction of notes which drained their vaults during the autumn of 1796, and that if they had been more liberal in their issues, their vaults would have been much better replenished with cash.

140. This disaster was the second notable penalty which the country paid within four years for the unjustifiable monopoly of the Bank. Never was there a more unfortunate example of monopolizing selfishness; it would neither establish branches of its own in the country, nor would it permit any other private company, of power and solidity, to do so, whose credit might have interposed, and aided in sustaining its own. Moreover, when a failure of confidence was felt in the country notes, it refused to supply notes of its own to supply their place. The power of issuing what plays so important a part in commerce, was absolutely forbidden to wealthy companies, and left in unbounded freedom to private persons, many of whom had no capital or property to support their issues, and whose credit vanished like a puff of smoke, in any public danger. The Bank, consequently, was left to bear the whole brunt of the crisis, solitary and unsupported, and finally succumbed.

141. From the foregoing considerations, as well as the weight of authority on the subject, we can scarcely have any room to doubt that the suspension of cash payments was brought about at that particular time, by the erroneous policy of the directors.

We must, in candour, state that it appears open to much doubt whether any management, however skilful, could ultimately have saved them from such a disaster, during some period of the war. Several of those who concurred in the measure at the time, after their judgment had been corrected by experience, expressed their regret at having done so. Sir Robert Peel, in 1844, said it was a "fatal" measure. Notwithstanding, however, the concurrence of so many weighty authorities,—and this is peculiarly a case where great authorities carry much weight,—we cannot help thinking that it was fortunate that it occurred at this early period. The alarm and dangers which preceded its stoppage were comparatively slight, compared with those which menaced the country after that event. The mutinies in the fleet, the rebellion in Ireland, the enormous accumulation of troops on the heights of Boulogne, flushed with victory, and led by a more fortunate, though probably not a greater soldier than Hoche, and burning with zeal for the invasion of England, were dangers of such portentous magnitude, as to render it, to the last degree improbable, that any paper currency, convertible into gold could have survived them. That Montague was a greater and more successful financier than Pitt can, we think, scarcely be doubted, and the carrying through the re-coinage of the silver, in the midst of so much public distress, was a financial operation, of which the audacity, skill, and success, must ever be regarded with admiration. But it must be remembered that the crisis in that reign lasted a much shorter time than the revolutionary war, and was never fraught with so much real danger to the independence of the country. At that period there was no paper credit, except the notes of the Bank of England, and William was at the head of a great European confederacy against one overgrown power, so that the circumstances of the two periods were in no way parallel, but rather, we may say, reversed. The confederacy against England at the latter period, was far more menacing and formidable than the alliance against France. The fortunes of the British Empire were apparently at their lowest ebb in 1798, and there seemed to be but one thing wanting to complete the destruction of the country—the loss of public credit. However great and invaluable are the blessings of a paper currency in time of peace, there does not appear to be any instance of its having successfully withstood the danger of an invasion by a foreign enemy. Even in Scotland, were it had been confessedly conducted upon a better system, and obtained the confidence of the country to a much greater degree, it could not have withstood the dread of invasion, if it had not been for the timely assistance of the Bank of England. And if it could not do so in that country, where the danger was remote, it is not probable that it could do so in England, where not only it was of much inferior stability, but was the very part of the

empire aimed at, and first exposed to danger. The constant power of producing public embarrassment by demands for gold would have been a powerful weapon in the hands of the enemy, in which they would have found many to support them in this country from political sympathy. This measure, therefore, removed one perpetual source of terror and alarm from the Ministry. We shall shew, in the next chapter, that the great depreciation of the currency which took place some years later, was not by any means a necessary consequence from such a measure, but was produced by the infatuated perversity, both of the Government and of the Bank of England, who, with fatal obstinacy, persisted in a system combining almost every false principle that could be thought of. As the suspension, then, must, we think, have taken place sooner or later, it was probably advantageous for the country that it did occur so early in the struggle.

142. The presumed scarcity of guineas, which led to the supposed necessity of issuing the order in Council, also rendered a more abundant supply of the circulating medium necessary, and an Act was immediately passed suspending, till the 1st May, the Act (Statute 1775, c. 51) restraining the negotiation of small promissory notes. In a few days the Bank caused to be prepared and issued £1 and £2 notes, and, to supply still further the demand for a small currency, they issued a notice that they had imported a large number of Spanish dollars, which were to be current at 4s. 6d. However, it was discovered that the dollars were undervalued by 2d. each, so their current value was enhanced by 3d. These dollars were stamped with a small king's head. The Bank, having put the dollars into circulation at 1d. each above their intrinsic value, the bullion merchants were not slow in seizing the advantage, and imported an immense quantity of similar dollars, which they had stamped in a similar manner. They were all called in on the 31st October, 1797, by which time the Bank had put 2,325,099 into circulation. It at first attempted to refuse payment of the forged ones, but they were executed in so close imitation of the real ones that it was impossible to detect them, and they were obliged to pay them all.

143. When the actual suspension took place, the foreign exchanges were highly favorable, so much so as to make it profitable to import gold, which began to flow in in great abundance. On the 30th May, Mr. Manning stated in the House, that vast quantities of gold had flowed into the Bank, both from the country and from abroad. The Government, however, and the directors of the Bank concurred in thinking that it would be imprudent to resume payments in cash at the period when the

restriction Act expired, and it was prolonged to one month after the meeting of the next Session of Parliament.

144. Parliament met again on the 2nd November, and on the 15th the House of Commons appointed a Secret Committee to inquire whether it was expedient to continue the restriction. On the 17th they reported that, on the 11th of that month, the total liabilities of the Bank were £17,578,910, and their assets £21,418,460, leaving a balance in their favor of £3,839,550, exclusive of the Government debt of £11,686,800. That the advances to Government had been reduced to £4,258,140, while the cash and bullion were five times the sum they stood at on the 25th February last, and much above what they had been at any time since September, 1795. That the exchange with Hamburg was unusually favorable, and had every appearance of continuing so, unless political circumstances should affect it. That no inconvenience seemed to be felt by the bankers and traders of London, for, whereas by law they were entitled to demand three-fourths of any deposit in cash they might make, they had only actually demanded one-sixteenth. They presented a resolution of the Directors, stating that the condition of the Bank's affairs was such that it could with safety resume its usual functions. The Committee, however, recommended that in consequence of the state of public affairs, it was advisable that the restriction should be continued for a further period. After a short debate, an Act was passed to continue the restriction until one month after the conclusion of a definite treaty of peace.

145. The opposition in Parliament and in the country to the policy of the Ministry was very powerful, and the transactions between the Bank and the Government were severely commented upon by the leaders of that party in Parliament. They, however, did not venture to divide against the bill. In the course of the discussion, however, Sir William Pulteney spoke with very great ability against the national evils and inconveniences of the monopoly of banking by one company, and moved for leave to bring in a bill to establish another bank in case the Bank of England did not resume cash payments on the 24th June. His speeches on this and a subsequent occasion were full of admirable argument, but the interests arrayed against him were so strong that leave was refused to bring in the bill by a majority of 50 to 15.

146. The exchange with Hamburg at the time of the suspension of cash payments was 35:10; it continued to improve throughout the whole of that year, and in December stood at 38:5, which was about £13 per cent. above par; the issues of the Bank were about 11½ millions during the year. This extra-

ordinary state of the exchanges continued during the whole of 1798 when they began gradually to fall, and in March, 1799, they were at 37·7, which was still £11 6s. above par. This was, of course, followed by a very great influx of gold, and at the end of 1798, the Bank had upwards of £7,000,000 in its vaults, and the directors expressed their readiness to the Government to resume payments in cash. The Ministry, however, thought it inexpedient in the state of the country.

147. The harvests of the two preceding years had been unusually abundant, and in January, 1799, the prices of all sorts of corn were extremely low, wheat being 49s. per quarter, and other kinds in proportion; but the winter of 1798-9, was extremely rigorous and unfavorable for farming operations. The spring was equally unfavorable, and in May, wheat was at 61s. 8d. This was followed by an extremely wet summer and autumn, so that at the end of the year wheat was at 94s. 2d. In February, 1800, the subject of the scarcity was taken up in both Houses, Lord Auckland said that it was estimated that the produce of last year's crop was little more than half average. Under the influence of this unparalleled deficiency the price of wheat rose in June, to 134s. 5d., and remained at the end of the year at 133s., after having fallen for a short period to 96s. 2d. in consequence of large importation introduced by the temptation of heavy bounties.

148. Under the influence of the enormous importation of wheat, the exchange with Hamburg continued to decline all through the summer of 1799, till in the last week of August, it had fallen to par. It continued steadily to decline after that until, in December, 1800, it reached 30s. In the mean time the price of foreign gold in coin, which had been at £3 17s. 6d. in May, 1797, rose to £4 in December, and continued at that price till September, 1799. In June, 1800, it rose to £4 5s., and in December to £4 6s.

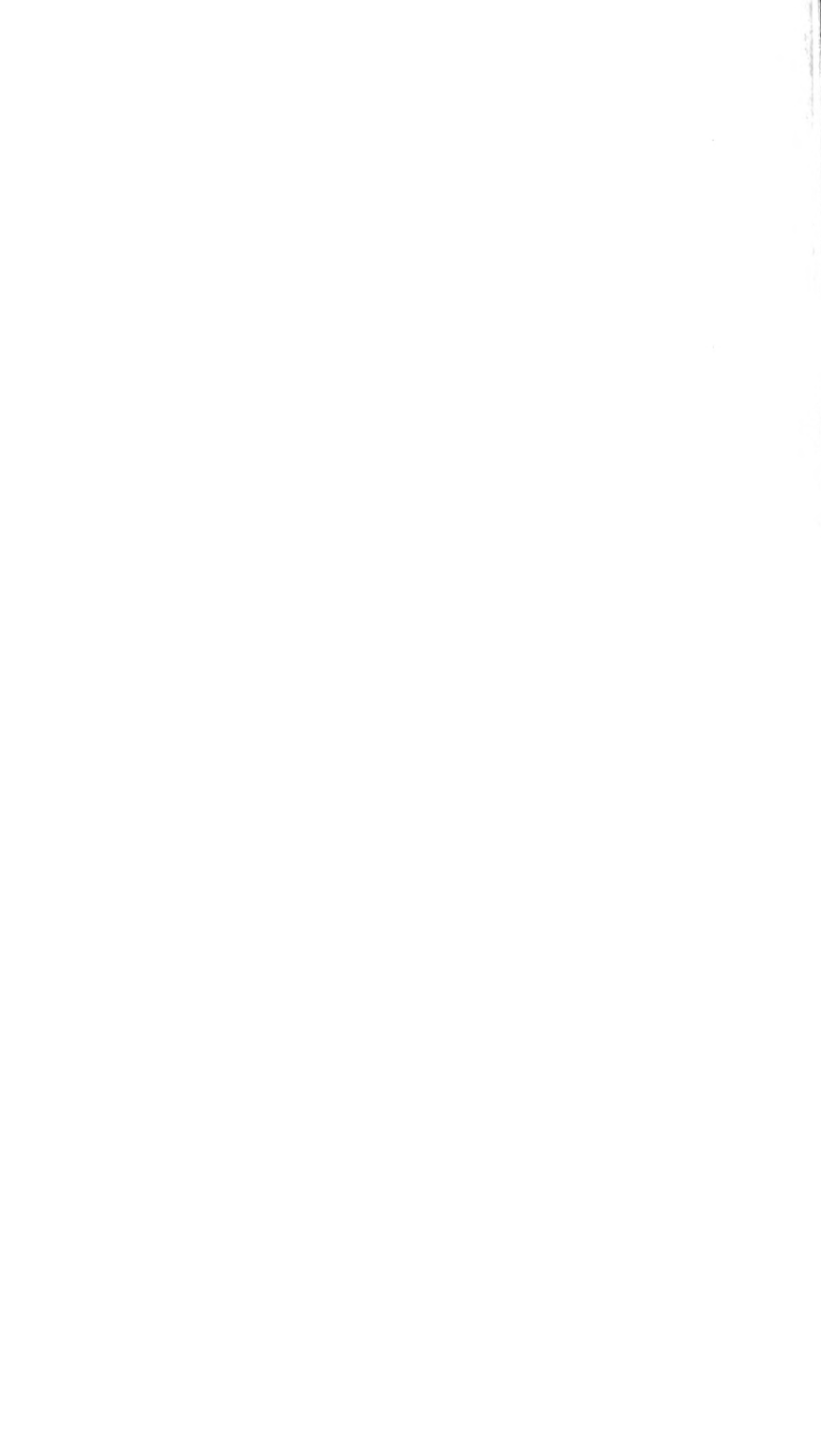
149. The arguments and ability of Sir William Pulteney in advocating the foundation of another Bank, produced great effect, and, during 1799, it excited great public interest. Meetings were held for the purpose of promoting it, and numerous pamphlets were published on the subject. The Bank Directors took alarm and, as the Minister was in want of a supply, they took advantage of his necessities to obtain a prolongation of their monopoly. The charter had still twelve years to run, but upon advancing £3,000,000, without interest for six years, Mr. Pitt agreed to renew it for twenty-one years from 1812. Very soon after the opening of the Session in 1800 a bill for this purpose was brought forward and passed.

We now see the results of two conflicting theories. For a considerable period there have been two opposite doctrines as to the true policy of the Bank during a great commercial crisis. The one is that the Bank should rigorously restrict its issues, and think of itself alone, and stand unmoved amid the universal ruin of the commercial world. The second is that due care should be taken to continue a restrictive policy while the exchange is adverse, but that, when the exchange becomes favourable, the Bank should enlarge its accommodation to support houses which are really solvent, but which may be brought down in the general discredit. Each of these theories have been tried, but the supporters of the first, a *restrictive* theory, have quite overlooked one fact. Every banker of experience would tell them that *an excessive restriction of credit causes a run for gold*. Thus Sir William Forbes, speaking of the crisis of 1793, says: "These proceedings, which obviously foreboded a risk of hostilities, were the signal for a check on mercantile credit all over the kingdom; and that check led by consequence to a demand on bankers for the money deposited with them, in order to supply the wants of mercantile men." The restrictive theory was likewise explicitly condemned by Sir Francis Baring, Mr. Thornton, the Bullion Committee, and all the most eminent authorities of the times, as we shall abundantly shew; and they expressly condemned an absolute limitation of the bank's issues, because, in certain states of credit, it would cause certain ruin, and a run for gold. They expressly recommended the *expansive* theory, and we see the results of the two.

In 1783, during a great commercial crisis, the Bank restricted its issues until the exchange became favourable, and then it freely expanded them, and passed safely through the crisis.

In 1797, the Directors having for some years previously prodigiously *extended* their issues, while the exchanges were adverse; and, being at last sensible of their imprudence, and having contracted them so that for a considerable period the exchanges had become favourable, continued their policy of merciless restriction long after gold was flowing into the country, AND THE RESULT WAS THE STOPPAGE OF THE BANK.

END OF VOLUME I.



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