

REAL WEALTH
AND
FINANCIAL POVERTY

A STUDY OF THE PRESENT FINANCIAL SYSTEM
AS A MONOPOLY OF MONEY, AND ITS RELATION
TO PRODUCTIVE INDUSTRY, SOCIAL POVERTY,
AND ECONOMIC WAR, FROM THE POINT OF VIEW
OF THE DOUGLAS CREDIT ANALYSIS

BY

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TO
EDWARD SALTHOUSE
ACKNOWLEDGING
WISE COUNSEL AND GREAT ENCOURAGEMENT
AND
AN EXAMPLE OF SINCERITY

PREFACE

To those who experienced and survived the tests and emotions of the "War to end War," and who returned to a disrupted civilian life looking, perhaps, for more than their deserts, certain questionings have been prompted by the happenings of post-war years. The loud promises of peace, prosperity, and progress, have been found to be impossible of fulfilment, and, after a short period of apparent plenty, marred by the evidences of inflation, a prolonged trade depression has plunged the nation into a state of despair; the industrialists are mortgaged or bankrupt, and the workers to the number of millions exist miserably on the "dole" or on wages just above subsistence-level. As a final tragedy, War itself is already back in its old place in the esteem of Governments; it is no longer considered "an impossible treachery to the memory of our million Dead," but practical politics. The number of armed men in Europe is at least as great as in 1914; the trade depression is world-wide.

What then are the causes of this poverty within nations, and this possibility of international war? In England the most earnest efforts of different political parties have failed to remedy the ills of unemployment and poverty, and the pious hopes of the business men for a return of commercial prosperity have seemed to be based on a superstitious regard for unknown and unknowable causes.

It would seem that in these circumstances the writings of an original thinker would be listened to with respect, and his suggestions examined with the dawning of a new hope. But though a man has arisen to diagnose the disease that afflicts the social organism, and to indicate the remedy, and though his writings are an essential contribution to social philosophy,—of a status and originality achieved, perhaps, only once in a generation,—unexpected difficulties have been met by those who have examined and understood his proposals, when endeavouring to propagate the “New Economics” founded upon them.

The remarkable books written by Major C. H. Douglas, the first produced in 1920, have supplied the answer to the questions asked regarding poverty and economic war. “Economic Democracy” and “Credit Power and Democracy” undertake a new and fundamental analysis of the economic system, and in particular of the relations between Present Financial Policy and the Industrial Organisation.

The analysis of Major Douglas is so new and startling in its implications, that the possibility of eliminating poverty and the economic causes of war is opposed by those to whom the present financial system is “instinctively” placed above criticism, and this opposition in many cases arises from a lack of knowledge of the actual operations of the present Money Market.

The following chapters, therefore, seek to give within one volume a concise outline of those divisions of the Money Market usually considered separately. These chapters are an actual study-course adopted by a student of the “New Economics,” with a view

to comparing the old ideas of money in the light of the new criticism; it is hoped therefore that the book will be helpful to those in particular who are handicapped, when considering the Douglas analysis, by indefinite opinions as to what the present Money Market is.

It is submitted that an examination of the present financial system as explained by the accepted authorities thereof, from the point of view of the new analysis, will show the conclusions arrived at by Major Douglas to be inevitable; they cannot be controverted, and the remedy suggested is a scientific regulation to replace an archaic and unregulated system. Poverty and war are the needless penalties imposed by an unsuspected monopoly of money, that renders the equitable distribution of natural wealth impossible.

These chapters suffer from the defects that cannot be avoided by one engaged strenuously in business; they have been written in the interval of work, and over an extended period. For that reason, perhaps, they will appeal to those similarly situated, and the reading of them will, it may be hoped, lead to the study of the works of Major Douglas on which they are based, and thereby to the clear understanding of the only practical alternative to Chaos and the ultimate disruption of the present state.

W.A.

Belfast.

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REAL WEALTH AND FINANCIAL POVERTY

CHAPTER I

CONDITIONS AND CHAOS; THE ENQUIRY JUSTIFIED

ARMAGEDDON

A GENERATION of men has died within the clouded plains of war, and the dying embers of the funeral pyre yet smoulder in the memories of survivors of the strife. Like broken gladiators the nations rise from the dust of battle, and through the mists of suffering grope their staggering way to seek an exit from the arena of their agony.

But they find it not.

The rushing flight of countless souls scarce has ceased to beat the anthem of their anguish, when Pity's tears are frozen in the stare of fear, and new sounds of discord thunder in the startled senses of the world. The Wars of the Nations are ended, and straightway they prepare for Armageddon.

Unless indeed there be some grim Goddess of Hate who wields unseen an inevitable power over the actions of humanity, there is now an imposition upon men to study the systems by which they seek to order

their lives, because, if the destiny of never-ending destruction, poverty, and misery, be not the relentless operation of a law of Nature, then assuredly the Chaos of this year of grace 1924 is caused by the flaws of those things that men, poor feeble artisans, have built by many labours to be the habitation of their dreams.

Therefore, it is proposed to examine the structure of the temple of Mammon, and, approaching the teaching of this thing that is protected by convention and honoured in proverb, it is hoped that the dread sounds that have been heard of war will be remembered amid the clinking of precious metals and the rustling of mystical papers.

For if these be not remembered, and if diligent search be not made in this, the most potent of the material powers of Man, for the causes of war (if they should lie herein), there is no doubt that soon again the flames will arise in the cities of luxurious poverty, and the edifice of this mighty civilization will crumble into the ashes of despair.

POWER AND POVERTY; THE TRAGIC PARADOX

A civilization exists to-day before which the grandeurs of the past seem but the laborious playthings of a child. At the dawn of history there was a civilization already old; it was engulfed by the tides of time, and succeeded again and again by the great achievements of later eras that were in turn destroyed.

But to-day progress has climbed without pause and without fear heights unknown to the older pioneers of hope. The treasure-house of Nature has been opened, and riches beyond the peak of dreams are within the reach of man. Science has scaled the ever-

receding ladders of the stars and scanned the secrets of immortal suns, and returned to the earthen stage to probe through diminished grandeurs into the ultimate recesses of matter, where now he hesitates at last before the chamber, mayhap, of the fundamental Truth.

And to-day, as never before, the triumphs of man over the forces of Nature are made available for use in comfort and in culture, by an engine of applied science called, in extenso, the Productive system. This is formed of the collective labours of men in the industrial community, whereby the products of the earth are converted by manifold processes to the necessities of life.

Yet to-day poverty and want are seemingly the inevitable price to be paid for progress, and the labour of men is bought and sold as a commodity, and subject to the chances of an economic law that is as undefined as it is terrible in its incidence.

Therefore, the scope of the enquiry will be to examine the means whereby the products of Nature, made available by scientific progress and converted to the needs of life by scientific industry, are ultimately controlled in their availability to the actual consumer, and with this information to enquire into the method of using the engine of production, and finally present an interpretation of the probable interaction of the means and methods considered.

PRACTICAL DETAIL OF THE SUBMISSION

The fundamental conception is of Money as the measure of value of material wealth. But it is desired to consider not a commodity, but a system;—the Financial System, which is a wider term and includes various conceptions quite foreign to the original idea of money. The system is usually

treated under several distinct headings, but the procedure herein will be as follows :—

- (A) To isolate the conception of Finance as a concrete system from the various inter-related ideas, trace and demonstrate its connection and duties within the various branches of economic studies, and create an inclusive and concise definition of it;
- (B) To examine by concise notes the components of the system under their proper headings as Money, in the abstract; Banking; Currency Systems and the Gold Standard; Public Funds; the Stock Exchange and Company Finance; this examination to treat of an internal organisation within a nation, and to be based upon the monetary system of Britain, and to proceed to the question of International Currency.
- (C) To describe and demonstrate the operations of the modern conception of the Money Market, and analyse the basis upon which it works and the extent of its powers.
- (D) To present a modern interpretation of the Financial System as embodied in the Money Market, explain its reaction upon productive industry and show the relative position of the two systems.
- (E) To summarise the discussion and present concisely the deductions drawn therefrom.

Under these various headings the discussion will be descriptive of the actual present position of Finance as understood by the accepted economic theories, and will be based upon the proper authorities. But at all times the position thus granted will be interpreted from the new standpoint made imperative by modern conditions, and the item of

ultimate importance—the effects of the system upon productive industry—examined thereby. The results having been summarised, the reorganisation or remedy that may be required will be indicated, with a short explanation of the implications and reaction of such a remedy.

METHOD OF TREATMENT

In dealing with a subject that involves the consideration of various departments of knowledge and several distinct and highly-complicated organisms, it is impossible within the compass of a concise discussion to "detail" the various propositions put forward. Therefore, no definitions of particular terms will be given excepting those that are essential to the discussion, knowledge being assumed of all terms used in their accepted economic sense. The conception of Finance ultimately to be considered is modern and post-war; it is to be regarded in the immediate present as a function of the world market, and, while historical notes are necessary to aid perspective in the general view, the tendency will be to look forward rather than to the past.

CHAPTER II

THE ECONOMIC FUNCTION OF A SYSTEM
OF FINANCE

THE SCIENCE OF WEALTH

THE advance of human knowledge has not been constant; there have been periods of varying progress. Periods extending to centuries have passed, during which the accretions to science have been relatively small; then, suddenly, a discovery that was entirely new, or one that reduced a theory to the practical plane, created a new interpretation of apparently hopeless problems, and being used as a new foundation and a new jumping-off place, sent forward the spearhead of knowledge with an immense momentum that was continued in a series of minor advances till all the possibilities were exhausted, and the time was ripe for another epoch-making pioneer to act his part.

In the opinion of Professor Soddy, man has made more progress in scientific achievement during the past hundred years than in the whole previous span of his unhappy history. And in many directions, particularly in the application of science to productive industry, probably more progress was made under the stimulus of the world war than during this whole century of vast achievement.

Departments of science have been demolished and rebuilt, but Economics, the science of wealth, has been born into its modern conception and reared

amidst an overwhelming torrent of new discoveries and new advances. In the words of Professor Soddy, the industrial revolution was not a mere step forward in the economic development of nations; it was the definite opening of a new era, and made possible by harnessing the energy—capital of the earth, in coal, the whole enormous edifice of the capitalistic civilization; truly "capitalistic" since it is founded upon the products of sunlight that have been hoarded during geological epochs.

Moreover, the rate of progress in the mechanistic creation of wealth shows no signs of diminishing, and it is astounding to realize clearly that the economic system of to-day is the mushroom product of one century at the end of countless ages that were lived under the impositions of penury, at the mercy of Nature's seasonal whims.

Now, what is Economics? The older term of "Political Economy" is purposely avoided. It is "the study of man in his efforts to earn a living," or the "study of man in relation to Wealth." Therefore, it is fundamentally a social science; perhaps *the* fundamental social science. It seeks to interpret the reactions of the community to wealth, to evolve rules, but not, obviously, to lay down laws. It is founded on physical sciences; that is to say, the physical sciences supply the materials that are primarily the subject-matter of its study, in material wealth, but it is not a physical science.

Rather does Economics deal with the evolution of man-made systems to utilize the materials supplied by the physical sciences, and in this connection it cannot state laws; it can deduce and pronounce generalisations only.

The point is elaborated to this extent because it is desired to emphasize the fact that, if Economics is a study of human conduct in its reaction upon wealth,

and if the studies are made during a century of unprecedented gains in power and knowledge, obviously it would be madness to impose a system or lay down a rule, and declare that this system or that rule is the expression of an economic "Law," which will be unaffected by future advances, and into which the mighty limbs of the ever-growing giant, Progress, must be fitted as into an inevitable yoke, prescribed for him by an inscrutable Fate.

Yet this is precisely what has happened within the domain of Economics, as will be seen.

Primarily, Finance is a branch of specialized study in the science of Economics; therefore, it has been shown that it is a study that cannot state laws and that is affected by the avalanche of riches poured by physical science at the feet of its bewildered practitioners.

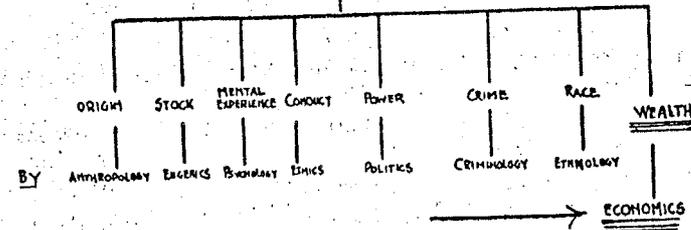
For clarity of thought it is desired to isolate the conception of Finance from the inter-related ideas; therefore it is advisable to show the position of Economics in relation to other sciences, and thereafter state definitely the relative position of Finance, as a system, within the economic sphere. The first can most concisely be displayed in diagram form;

ECONOMICS AS A SOCIAL SCIENCE
WITHIN THE DOMAIN OF MORAL PHILOSOPHY IS A GROUP OF STUDIES
CALLED

THE SOCIAL SCIENCES

COLLECTIVELY TERMED
SOCIOLOGY

BEING THE STUDY OF MAN IN SOCIETY
STUDIED AS TO —



(Diagram by STEPHENSON
"Principals & Practice of Commerce")

Diagram No. 1.

THE FINANCIAL SYSTEM AS A FUNCTION OF ECONOMICS

The outstanding feature of the age is specialization. It is symptomatic of the limited stature of Man intellectually, by comparison with the problems confronting him, and it is apparent in every sphere of learning both in pure and applied knowledge.

Sociology contains many different departments of study, and those departments are further sub-divided, Economics probably more than any other.

But unfortunately the science of Wealth is in many ways merely a battle-ground of conflicting theories and opposing schools of thought, and its methods in many respects are not scientific at all. Yet the

studies under the present accepted system are generally conducted under well-defined headings, and its leading conceptions, both subjective and objective, are contained within the four departments of Production, Distribution, Exchange and Consumption.

These conceptions are now required to consider the whole habitable world as one unit; the "market" for goods and services is the world. The production of wealth, its apportionment between the individuals of a community, the balancing of its surpluses and deficiencies (both geographical and otherwise), and its ultimate utility, in the economic sense, are therefore complicated by the desires and prejudices of many races of men and many new elements of conflicting interests.

In any such consideration the first essential is a universal measure of value, either actual or attainable by calculation. A measure of value is connected with the economic definition of Utility. Wealth may be desirable in itself, yet be incapable of transference from one to another, or it may be both desirable and transferable; that is to say, it may possess either value in use, or value in exchange.

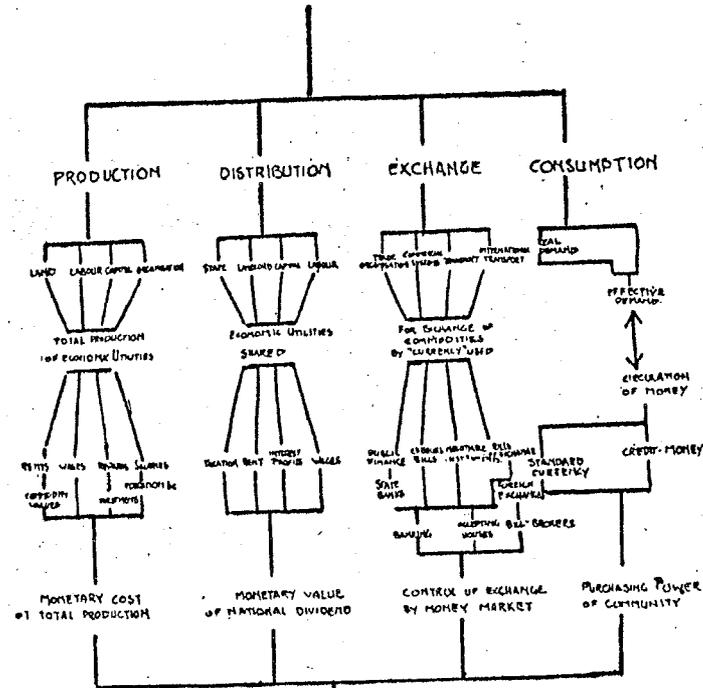
In the modern (objective) conception of economics, all material values are accordingly reduced to a common measure, and only their exchange values dealt with. The common measure used is called Money, and the adoption of money to the varying necessities of nations and of international trading, and the fluctuating demands of a productive system that is looking ever forward, has created the organisation that is collectively termed, for present purposes, the Financial System.

Let it be emphasized that this fundamental conception of Finance shows it to be a convenience; merely the particular method employed to render intelligible the conclusions drawn by economics

regarding wealth, so far as they can be expressed as "value in exchange."

The position of Finance relative to the four departments of economics is shown by means of diagram set out hereunder:—

THE PLACE OF FINANCE IN ECONOMICS
ECONOMICS.



THE COMMON "MEASURE OF VALUE
By
THE FINANCIAL SYSTEM
Diagram No. 2.

At the opposite extremes are the two conceptions of Production and Consumption, which in their interrelation contain the basis of what is usually called the Law of Supply and Demand. But note the distinction. The upper half of the diagram deals with the economic utilities themselves, and here the Agents of Production convert the bounty of nature into the form most necessary or most desired, and for these there is the natural desire of the community for the satisfaction of its wants, that desire being, in theory, practically insatiable. But transfer the economic conception downwards into the plane of practical industry, and here the economic utilities made available by Production are measured in terms of their money-costs, while the "satisfaction of wants" by the community is measured by its purchasing power, or the amount of money it can spend in exchange for goods.

Again, the amount of purchasing power at the disposal of particular sections of the community is examined in the theories of Distribution, and in practical life reduced also to monetary values, that represent in effect a claim upon the stream of production.

Here is the common measure of value, properly employed. But in the Exchange of commodities and utilities within a market embracing the whole world, the common measure of value became the basis of the system of which we treat, to be identified hereunder.

OUTLINE OF THE GROWTH OF THE "SYSTEM"

- (1) In the first place, as will be shown later, Barter within the local market was supplanted by the use of Money of various kinds, which evolved into the common measure of value of modern commerce.

- (2) But the original use of money, directly replacing barter, became unsuitable for the multitudinous operations of the national market evolved by increased production and improved communications, and therefore a monetary organisation evolved concurrently that is embodied in the present Banking system.
- (3) The continued improvement of applied sciences, of processes, communications, and transport, created the World Market in the strictest commercial sense, and therein grew up the theory of the foreign exchanges, with Bills of Exchange and certain negotiable instruments as "international currencies" creating the specific financial vocation of bill-brokers, bill-discounters and acceptors, who are apart from and in addition to the Bankers.
- (4) Incidentally the application of science to industry, and the desire for increased and "mass" production, favoured the growth of the co-operative use of money by the joint stock system, and ultimately created the present market for "securities" or documents embodying legal rights, called the Stock Exchange.
- (5) But the outstanding fact to be observed is that of the use of Credit as money, a use imposed upon the community, not only by the extent of the "market" but by the impositions of currency systems and the function attributed to Finance, and also by the magnitude and rapidity of industrial operations. This creation of financial credit is an actual creation of money, (Banker's or Token Money), and by custom, (be it noted, by custom or convention), the creation and control of such money has

become the monopoly of the Financial System as embodied in the Money Market. In Britain, the essentially modern conception of the Money Market consists of the Bank of England, the Joint Stock Banks, and certain international "accepting" houses, with the lesser assistance of discount houses, bill-brokers, and the Stock Exchange dealers in securities.

A DEFINITION OF FINANCE

It can now be stated that in the abstract there is a conception in the science of economics whereby the mercantile operations of the world are reduced to a common measure of value (in exchange) by means of money, and that the economic conception is put into practical operation through the financial system.

Therefore the Financial System may be described concisely as;—that organisation of Commerce whereby the economic movements within the whole community of Man, in relation to his material wealth, are translated into terms that are universally intelligible, and capable of convenient application to all the transactions, individual or collective, national or international, whereby Man seeks to satisfy the craving for all those utilities included in the term "economic wants."

RESUME

With a preliminary reflection upon the serious nature of economic studies as emphasized by modern conditions and the magnitude of the catastrophe of war, the plan has been drawn with wide general outlines that would be a proper guide to the gradual examination of the whole financial edifice.

For clarity of thought, the conception of Finance has been isolated, and its function within the

economic sphere demonstrated in its completeness, while the derivation and growth of the system as a whole has been indicated. By this means, while a wide general idea has been obtained of the financial structure actually in operation, and a definition framed therefor, there has been shown the necessity of avoiding the generalisations currently accepted as discussion upon financial problems, and of substituting in place thereof a close examination of those fundamental conceptions upon which Finance is founded, and by which it seeks to justify the exercise of a universal authority.

Therefore some time will be spent in examining the different departments that compose its structure, and the first study will be an examination of the abstract conception of Money.

But let one thought be ever present with the student. Of certain theories in the science of economics it is said that they have the force of a "law," as though to them might be attributed the truth of a Law of Nature. Such reasoning is false. Does not a natural law operate within a system that is the Universe, created by God? If it be identified correctly, it may indeed be examined and interpreted; but assuredly it will continue in the truth of its operation whether we study it or not. But an economic "law" must operate within a system created with little forethought by man himself; and though it may be a logical sequence of the system, it cannot be taken as a proof that the system itself is sound. Therefore, if the Financial System should be defective, how tragic may be the consequences of its "laws" when imposed by man between himself and his natural necessities.

CHAPTER III

THE ABSTRACT CONCEPTION OF MONEY

EVOLUTION FROM BARTER TO MONEY

It is more interesting than profitable to begin the study of the abstract conception of Money, by an imaginative effort to visualize our remote ancestors who lived, like the beasts, at war with Nature, and won their precarious livelihood in face of overwhelming menace. Their lives were cataclysmic; they lived within the cycle of a day, and the communal spirit was no more developed, perhaps, than it is to-day in the greater apes. They moved, maybe, in families, and ate what their force or cunning enabled them to obtain of flesh or wild fruits, but of other necessities of life as it is lived to-day they had none.

But too much attention has been given to the evolution of money, in order it may be to obtain for it historic sanction in a particular function. The pre-historic man, moving amid forces and in a world utterly beyond his comprehension, had no light within him to lay down even the rudiments of a system that would be applicable to the proud needs of his mighty descendants, who have harnessed those very forces that were the objects of his fear-inspired worship.

But the communal association of Man was an early development, and with the growth of a community, however primitive, arises the first possibility of a system for the conduct of life. In one sense all com-

munities are based on mutual trust between individual members, and it is by the expansion of such a sentiment that the national and international civilizations have been created.

Indeed, the community is an organism, and its growth and control is organic. The whole tendency is towards the division and specialization of work that is instinctive in all organisms. It was this division of labour that created the first "Surplus" of a commodity in the hands of one man with a corresponding deficiency of another commodity, and impelled him to seek for another individual similarly situated, to whom the surplus would supply a deficiency and by whom the deficiency would be remedied.

They bartered their commodities, but no elaboration is necessary to display the inherent difficulty of the exchange of commodities by this method. There is no barter to-day, in this sense, but there is a certain perfected system that amounts to the bartering of Credit, that will be described in a later chapter.

But here we have noticed that the first results of a human society were to cause division of labour according to skill and aptitude or special ability, and accordingly to create a desire for the exchange of commodities between individuals engaged in different occupations. The obvious tendency encouraged thereby to the increase and multiplication of desires need not be laboured. Therefore the first economic generalization would have stated "the desire for the exchange of commodities between individuals." But the operation of exchange was hindered by the method of barter, the chief difficulties of which may be stated as:—

- (1) The difficulty of each person having to find someone who not only desired what he wished to dispose of, but was also willing

to give him what he, in his turn, required in return for it; that is to say, the difficulty of balancing particular surpluses and deficiencies;

- (2) The great probability of disagreement regarding the respective values of the commodities to be exchanged.

In these circumstances the possibility of greater ease in exchange came to be recognised, by means of "A third commodity, chosen by common consent to be a means of exchange and a measure of value between every other two commodities." A surplus of one commodity might be disposed of for a proportionate value of the "medium of exchange," and with the latter could be purchased any other commodity desired. Thus the direct contact of persons having corresponding "surpluses" and "deficiencies" of commodities as in barter was avoided, and the generic term "money" is applied to anything that is "by common consent" used as the medium of exchange and measure of value of the definition.

EVOLUTION OF THE FORMS OF MONEY

Be it noted that, though Money has been described as "a third commodity," in effect the specific significance of the term lies in the expression "by common consent." Granted the common consent, anything might become by custom and acceptance the medium of exchange.

But on consideration it is noticed that the four great stages through which the race of man has laboured upward towards the light, have each evolved their particular forms of money. In this examination, however, it should be remembered that progress has been affected by racial and geographical and other

complex causes; the era of barter and primitive money ended many ages ago, yet it survives among primitive peoples even to-day. Therefore broad and general divisions only will be given, dates being unnecessary and misleading.

A concise and illuminating summary of the four stages in monetary development is given by Stephenson in his "Principles and Practice of Commerce," which may with advantage be quoted for the present purpose;

"The Hunting Stage. In this stage, the skins of wild animals were used as money. Reference is made to this stage of economy in the following passage, which occurs in the Book of Job, (Chap. 2, v. 4) 'Skin for skin; yea all that a man hath will he give for his life.' At this period, skins were the recognised medium of exchange, and a man was willing to give up his last skin rather than lose his life.

"Pastoral Stage. In this stage, man roams over land which is still ownerless. On it he feeds his cattle and then drives them to fresh pastures. His main possessions are, therefore, his flocks and herds; these constitute his wealth, and cattle are his money. Among the Anglo-Saxons, slaves and cattle are spoken of as living money. When metal money was first introduced, some of the earlier coins had cattle stamped upon them. Thus 'pecus' (cattle) is the origin of the Latin 'pecunia' (money) and of our English word 'pecuniary,' and the word 'cattle' itself is derived from 'capital,' the origin of which is the Latin word 'caput' (head), beasts having from the earliest times constituted the chief parts of a man's property.

"The Agricultural Stage. This stage evolved when the people settled down to cultivate the land, and thus abandoned their roaming habits. In this stage, people discovered that it was easier to dig with

a metal spade than a wooden one. Hence, bronze and iron became general commodities, and these were soon adopted as money. The money of the Spartans, for instance, was made of iron.

"The Commercial Stage. During this stage the precious metals emerged as the chief forms of money. 'By a tacit concurrence,' says J. S. Mill, 'almost all nations, at a very early period, fixed upon certain metals, and especially gold and silver, to serve this purpose. No other substances unite the necessary qualities in so great a degree, with so many subordinate advantages. . . . These were the things which it most pleased everyone to possess, and which there was most certainty of finding others willing to receive in exchange for any kind of produce.' Thus, the evolution of gold and silver as the principal form of money is an illustration of the law of the 'survival of the fittest,' since these metals possess qualities which have enabled them to survive."

In considering the earlier forms of money, it is important to remember that exchanges took place originally between groups, rather than individuals. As each group produced as much as possible of its own necessities, the slow growth of exchanges may thus be explained. This actually is the case amongst savage tribes in modern times, and by examining their customs also it is possible to verify the astonishing variety of articles, from shells to heavy metals, that have in different circumstances been used as money.

THE FUNCTIONS OF MONEY

Thus early in the consideration of Money appears the importance which custom has attached to the actual commodity used as a medium of exchange and a measure of value; an importance that is entirely

unjustified by the light of modern commercial practise, where the actual coinage or metallic money has become merely the "small change" of commerce, in deference to a more scientific and convenient conception.

Consider the actual functions that are required to be performed by Money:—

(1) *A Measure of Value.* The fundamental conception as a universal "measure of Value" has been isolated and demonstrated in the consideration of Finance in relation to the science of economics. Be it noted, therefore, that fundamentally Money need not be a commodity at all. It is a measure of value, an arithmetical method of expressing the "value in exchange" or "economic utility" of any commodity in a particular form that is universally recognised.

This disregarded fact is self-evident. The standard weights and measures of quantity, area, and capacity are merely scientifically-tested objects, like the "yard-stick" preserved by the State for the purpose of control in the operations of commerce. And in its fundamental conception as a measure of value, Money need not exist in any manner different from the other measures. It does not, in fact, exist in any of the major operations of commerce, as will be seen when currency systems and Credit are under examination.

(2) *A Medium of Exchange.* The growth of economic life must naturally precede the study of the problems connected therewith. Man has not, unfortunately, yet attained the degree of intellectual strength that would enable him to stand apart from the enveloping pressure of his immediate environment, and, in freedom, look behind and before his time and deliberately plan his systems for the future. The economic system has been a more or less fortuitous growth. Therefore the first practical function

of money was as a "medium of exchange";—in the terms of the definition already given, money was the "third commodity" by which the difficulties of Barter were overcome, and, in the Commercial era, undoubtedly the "medium of exchange," universally accepted, is an essential condition of the division of industry into specialized branches; in modern industry, it is an essential foundation to the "wages" system of reward for labour.

Accordingly, the function of money as a "medium of exchange" is usually stated first, as its fundamental and most important characteristic, in this way emphasizing the importance of the actual commodity used; but it is time that the study of Money became modern and in accordance with the facts of present-day Commerce.

Ninety-nine per cent. of all commercial operations are completed by using money as a Measure of Value only; nothing passes between the operators concerned, excepting a signed authority (a cheque or bill) from one to the other, whereby their respective bankers are authorised to make a book-keeping transfer of arithmetical figures only.

Let the conception of money thus be clarified from its foundation, even at the risk of anticipating the discussion of Banking, and be it noted that in 1924, when less than £150 millions of metallic money was "in circulation" in Britain, the circulation of cheques was in excess of £37,000 millions. This will be referred to at the end of the chapter.

(3) *A Standard of Deferred Payments.* One of the fundamental characteristics of advancing civilization is the tendency of people to trust one another. By a consideration of the development of any legal system, a continuous increase in relations arising from Contract may be observed, and this signifies the increasing tendency to undertake something to be

done in the future. Such a contract obviously necessitates some standard for expressing the present value of the future act, and also all potential values of rewards or creation connected therewith, and accordingly the function of Money as "the common measure of value," is used again as "the standard of deferred payments."

But apparently this important characteristic is but an extension of the function stated above to be fundamental,—that of the common "measure of value" whereby all operations in the economic community are reduced to terms universally intelligible.

(4) *A Store of Value.* The fourth function attributed to Money recognised that large bodies of Wealth cannot be concentrated excepting in the form of Money. It is obviously correct, as for instance, in the transport of values from place to place, or, practically, the reserve or transport of purchasing-power (that is of a demand upon the community's wealth). But this function must also be considered later, when the modern "system" of finance has been fully mastered.

CHARACTERISTICS OF "GOOD" MONEY

The present financial system, it must be observed, in its abstract conception of Money emphasizes the function of "exchange," the actual commodity used. Therefore the present interpretation of the characteristics of "good" money is primarily relative to the conception of a medium of exchange.

The commodities which most accurately perform this function fulfill the requisites of "good" money. It is for this reason that the employment of metals as money material can be traced far back in the history of civilization, and it may be said that as a medium of exchange among progressive communities,

the metals have tended to supercede all other commodities, and secondly, that the more valuable metals have tended to displace the less valuable ones.

There has undoubtedly been a long process of selection and elimination in monetary history, but the pre-eminence of gold as *metallic* money is now beyond dispute. And in this conception of the attributes of money its position is justified; the attributes of "good" money are stated as follows;—(Jevons).

(1) *Divisibility*. Gold (and silver) are eminently divisible, and when pure, are always of the same quality. Unlike diamonds, they are capable of reconstruction without loss.

(2) *Indestructibility*. Gold (and silver) do not deteriorate through exposure to the air, nor do they corrode. They are among the most imperishable of substances.

(3) *Stability of Value*. Gold is the least variable of all commodities in its intrinsic value.

(4) *Homogeneity*. Since all gold (and silver) coins bearing the same denomination are of equal value, there is no inducement to choose one unit in preference to another.

(5) *Cognisibility*. Gold may be distinguished easily from coins made from any other metal.

(6) *Utility*. As a substance, gold is itself the object of desire for purposes of ornament and adornment.

(7) *Portability*. Gold contains great value in small bulk.

Obviously, these qualities relate to the actual exchange of "the third commodity" that obviates barter. And it must equally be obvious that these qualities to-day refer only to the small individual transactions of commerce, and that they have no reference to the major operations, that are, as is

known, carried through by means of credit instruments based upon the "measure of value," but themselves having none of the attributes of "good" money in the conventional sense. This fact may with advantage be considered further by a short statement of the current theory of the Value of Money.

THE VALUE OF MONEY; THE QUANTITY THEORY

"Value," it must be remembered, is in economic study really value in exchange, that is to say, the worth of one commodity measured on terms of another commodity.

Therefore the economic definition of the Value of Money is concerned with money as a commodity, and not in the usual commercial sense (that is, the value measured by the rate of interest that can be obtained for loans).

But Money, let it be remembered, is a commodity only in theory; it is a commodity in its function as a medium of exchange. In this sense, its value is determined according to the "law" of supply and demand. The "supply" of a commodity is the quantity of it that is offered for sale. Money is offered for sale in exchange for goods. A person sells goods (i.e. exchanges them) for money, so that he can transport the money to another place and exchange (i.e. sell) it for other goods that he himself requires.

It is a feature of increasing culture that money is sought less and less for its own sake; it is not hoarded excepting as a demand upon the community's real wealth. It is merely a convenience.

Therefore the Quantity Theory states that the Value of Money, other things being equal, varies inversely with its quantity—if an expansion occur in the quantity of money put into circulation its value

will fall; if a contraction in the amount put into circulation take place, its value per unit will rise.

That is to say, the total number of units of Money, in the abstract conception, are divided into the total available units of material wealth, and the monetary unit-value determined by the number of wealth-units each will purchase.

Upon this assumption has been built a great edifice of theory, and in many text-books the Quantity Theory is declared to be more correctly termed the "Quantity Law," "the term 'law' being used in the scientific sense, viz., that it expresses a general principle deduced by observation or experiment from particular facts." (Stephenson.)

It is sought to justify this law after reducing various qualifying circumstances to terms amenable to its incidence. These circumstances are; the variable quantity and different nature of goods, or material wealth, produced by the industrial machine and offered for sale; the "velocity of circulation" or the "efficiency of money," one unit of money used three times successively being obviously the equivalent of three units of money, used once each; and lastly, the question of the use of Credit as money, by means of negotiable instruments that are now called "representative money."

But in the purely abstract conception of Money under the present financial system the Quantity "Law" is theoretically correct.

The question of importance, however, is the fact that a "Law" that is stated to be scientific, in order to justify itself is forced to consider a certain thing (credit) as Money, which is not in fact Money at all according to the very definition of money under which the "Law" has been created. The Quantity Theory is essentially based on the function of money

as "a medium of exchange"; it therefore ignores the actual circumstances of modern industry.

This statement may be more clearly justified by a brief restatement of the discussion up to this point.

RESUME

The discussion undertaken is that of a system existing in the immediate present, and the broad outlines and general definitions of this organisation were indicated in the previous chapter.

But since then the fundamental conception has been examined in the abstract, and difficulties have arisen. The generic term "Money" has been examined, and to understand it recourse has been made to history. But there seems to be herein an inherent difficulty, because the form and the functions and the value of money seem to have been evolved in conditions utterly different from those under which the "economic man" exists to-day.

An understanding of Money has been made by reference to the functions attributed to it; as a common measure of value; a medium of exchange; a standard of deferred payments; and a store of value. It was noticed that the first and third of these functions conform to the precise function allotted to the financial system when considered as an interpretation of economic life; also that the second and fourth functions are those upon which the idea of money first grew. Upon these latter two, also, the attributes of "good" money were observed to be based, and ultimately the Quantity Theory of the Value of Money, in its pure form, could deal only with them, as representing Money as an actual commodity.

Herein may be the difficulty that may be briefly stated, to be given at a later stage the detailed examination due to its importance.

The Financial System was assumed to be a very humble servitor of the Science of Economics, and the latter deals with real wealth, not with money as such, and the wealth considered is the economic utilities won from Nature by the physical sciences. Neither Economics nor Finance was to state laws, since the problems to be considered were not their own, but must be changed in accordance with the advances made by science as applied to the production of wealth.

But already certain economic statements have become too rigid, and the facts appear that (1) historically "money" was used actually as a medium of exchange, in an era wherein the productive capacity of man, of material wealth, in keeping with his limited knowledge of the utilization of Energy, was relatively insignificant, the available amount of commodity-money being therefore adequate for his needs, but (2), the present economic era is based upon the utilization of the energy of coal, and the productive capacity of scientific industry has therefore been so greatly expanded that an entirely new condition of things has been created, and Money as a medium of exchange, comparatively speaking, has ceased to exist and survives only as a "common measure of value."

The supply of commodities noted in the Quantity Theory has entirely overwhelmed the supply of "commodity" money, and the deficiency has been supplied by the creation of a form of representative money bearing none of the attributes of good money, stated to be essential in the medium of exchange.

The Quantity Theory is still imposed. It has become rigid; the law (or the weapon) of the operators of Finance. But it is imposed by the creation of "artificial" money, and, in order to justify its imposition, the artificial money must be reconciled to

the real money of its implication. This is done in practice by the elaborate contrivances embodied in the Gold Standard.

Again it must be pointed out that general statements regarding finance are useless; in the foregoing summary, the two conceptions of "representative money" and "the gold standard" require individual and detailed analysis, before accurate conclusions can be arrived at.

The derivation, growth, and meaning of representative money can most concisely be made when considering "Currency," hereunder, while the method of its application in practice is explained in the following description of Banking. This, again, leads logically to the larger questions of credit-money and the "reconciliation" thereof to our present subject, the Quantity Theory, by means of the gold standard.

Thus the labyrinth of study in financial matters becomes a circle; a circle, in fact, of gold; a circle, in modern times, of bondage. So comes the immediate necessity of understanding, firstly, Currency.

And thus we see already that the economic "law" of supply and demand is controlled by a minor "law" of the quantity of money. But the minor "law" is itself subject to the major law; truly a most unscientific tangle. Let the student elaborate his previous thought on this question of law, (p. 15). For man himself there is the natural—and inevitable—"demand" of his own necessity, and the potential "supply" lying dormant in the Real Wealth of Nature. If the Financial System impedes this natural contact it has a tragic responsibility. Shall the law of gravity operate only if an artificial "system" is interposed between the earth that attracts and the falling body?

CHAPTER IV

CURRENCY

DEFINITION

CURRENCY may be termed the means whereby commodities are exchanged by purchase and sale, without recourse to barter. The commodities are measured by the units of the currency, and the expression of their value in the terms of such units is called the "price." Therefore currency is in theory the "medium of exchange" which circulates in a country for the settlement of indebtedness between the individuals therein.

It has already been noted in examining the attributes of "good" money, that the elimination of the baser metals has left gold and silver as the generally-accepted "medium of exchange," while in more recent times the tendency has been to adopt gold alone as the sole monetary standard, using silver for subsidiary coinage only.

GROWTH OF METALLIC CURRENCY

Gold indeed has been used as money from the earliest times, and the cubes of gold used by the Chinese may have been the earliest form of coinage. Modern authorities accept the view that gold and silver coins were first used by the Lydians. But since that time the practical detail of the actual coinage

used in the exchange of commodities has been perfected by experiment and public opinion acting upon traditional growth. The shape has ultimately been evolved; all modern coins and most ancient ones are round; this being adopted after the earliest stage, when metallic currencies passed by weight,—which were in fact commodities, though used in a particular manner. Then the limit of size in coinage has been decided upon in practice, and the higher and lower limits of value; in this connection the comparative "wear" of different coins has been considered. At still later stages, the protection of the coinage from counterfeiting has received great attention, and, concurrently, the necessity of inserting an appropriate proportion of alloy for hardening the soft metals, gold and silver.

CONTROL

But the considerations enumerated above are details only. They relate to the "small change" of commerce. A question of much greater importance both politically and economically is that of the issue of money, and the power of the State concerning it.

"In the ruder societies, where money was not sharply divided from commodities, no difficulty presented itself. Skins, shells, or cattle were money—so to speak—by the force of things; and the same condition persisted as long as crude metals were employed. But with the introduction of coinage the idea of a regulating authority came into being. The necessity of enforcing contracts and the parallel system of penalties, made it incumbent upon the ruler and judges to provide due standards of payment. The combined effect of these influences was reinforced by the establishment of the rudimentary forms of state revenue, which made it a matter of interest to the

ruler to provide a good medium of payment. Accordingly with the origin of the organised state, we find the coinage as a special prerogative of the king.

One reason for the close connection of Money with the State is the fact that there is one attribute of currency which comes within the area of work specially allotted to the public authority. Money ought to have the power finally to close a transaction, i.e., to say it should be 'legal tender.' This 'liberating power' as the French call it, might be regarded as one of the money functions." (Bastable.)

Bastable further says that a currency system is never an arbitrary creation; it must grow slowly out of the habits and customs of the community, and must subserve its economic needs.

THE PRESENT POSITION

The opinion of Bastable is that generally held by the economic and financial writers of to-day. And the creation of currency is to-day the prerogative of the state. The "formal" problems connected with it are dealt with by the state; the relative values of coins, or denominations of value and the "series" employed for convenience; the "standard" or unit of value, and the expense of minting; seigniorage, depreciation, and the legal aspects of the attributes of currency as "legal tender." In theory, also, the State as the controlling authority should deal with questions of principle that are much more complicated than formal or practical details, and, if the State is the issuing or creating power, then particularly it should be interested fundamentally in the amount of currency actually in use in the community.

In theory, the governing authority is the only creator of money in the modern state. In practice, Governments no longer control the creation of the

money used in commerce; they regulate merely the "formal" details of coinage and legal tender.

Yet be it noted, from the typical economic quotation given above, that currency "must grow slowly out of the habits and customs of the community." Currency systems must not be reviewed; they are but the servitors of commerce, the hand maidens of the sciences that provide for the economic needs of man—yet, even when those sciences change the face of the earth itself and conquer the realms of air, the mysterious "evolutionary" power of growth attributed to currencies must protect them from revision or alteration to meet new conditions and new needs. Even the grim business of warfare advances from the bloody ecstasy of personal combat, to the chilling fear of a universal cataclysm caused by a poison-gas or a super-electrical ray of death; but the habiliments of currencies must remain upon the old set fashions of ancient histories.

The fact remains, that looking at the currencies of the world to-day it is seen that, while all countries possess an organised currency controlled by the governing power, the exigencies of modern commerce have removed the burden of trade, or the exchange of commodities, from the theoretical "medium of exchange" and placed it upon the new interpretation of Representative Money, in which the medium of exchange is referred to only as a "Measure" of value.

REPRESENTATIVE MONEY

Reference to the accepted definition of Currency shows that the term must include every means whereby the transfers of commodities or economic values are effected. "Let me define," says Mr. Reginald McKenna, "the sense in which I shall use the word money. I understand by it all currency in

circulation among the public and all bank deposits drawable by cheque." Currency includes everything used as money in the economic sense, and the great majority of commercial transactions to-day are completed by using credit instruments as money. "Representative" money is the use of paper or documents to represent the amount of "standard" money referred to thereon; it is in effect the use of the standard money as a "measure of value." The acceptability of representative money is based on credit and secured by various contrivances, the chief of which has been the "gold standard" theory, implying that all representative money could, on demand, be exchanged for its face value in gold or standard coin.

Therefore if the credit instrument is accepted and goods transferred against it, it is seen that, when later the credit instrument is used as the basis of other transactions, no commodity has been used at all as a medium of exchange, and the transaction is resolved into a *perfected system of barter*, between three or more persons instead of two, based upon credit, and made possible by the perfect organisation and world-wide scope of the economic system.

"The origination of paper money by state direction is the easiest to consider and explain. It does not follow that it is the most important or the earliest kind of representative money. . . . In truth representative money seems to have grown up out of the elementary contrivances of early credit. A claim could be expressed and transferred by a document, which might be used for facilitating exchanges. The rigid formalism of early law hindered the extensive use of this convenient machinery. It was not till the institution of Banking that the coining of Credit was made easy. Thus the banknote came into use, resting not on the fiat of the state, but on the repute of the

issuer. At this stage, the history of the two distinct forms of representative money became mixed, owing to the control exercised over banks by Government and to the fact that banking companies were in many cases the agents by which what was virtually State money was issued. There is, however, the fundamental difference that bank money finds its way into use through the ordinary system of granting credit, while Government money is used in the purchase of commodities and the hire of services. The former, therefore, returns in a short time; the latter remains in circulation and displaces metallic currency. In the long controversy over the Bank Charter Act, 1844, this distinction was brought into prominence. Since that date the extraordinary development of deposit banking in both Great Britain and the United States has furnished these countries with by far the most flexible form of currency yet known, in cheques that transfer claims on the capital held by the banking institutions. The confusion so often shown regarding the relation of credit to money is connected with this latest progress. When it is remembered that in its origin money is only an instrument to facilitate exchange—we might say to render it possible—it follows that from its earliest to its latest form the ruling influence is the need of society for the best Medium of Exchange." (Bastable.)

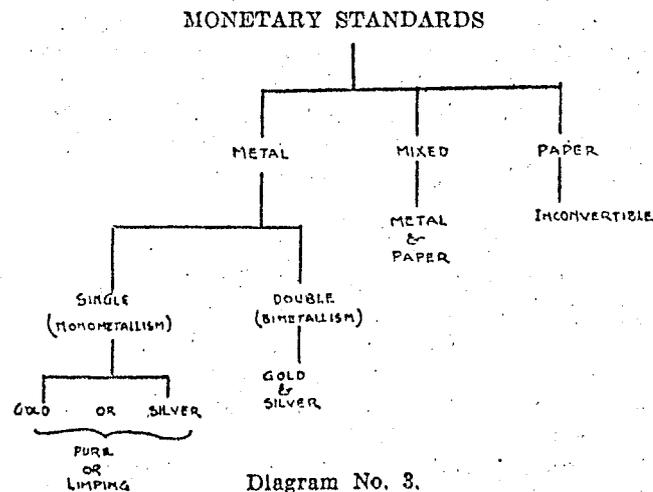
SUMMARY OF CURRENCY

To summarize, it can be said that the currency of a country consists of anything which is used as a medium of exchange in effecting purchases and sales, and in discharging debts or monetary obligations. It includes Standard money and anything used to represent standard money.

A Currency under present conditions is said to be normal when—

- (1) The current coins are struck from metal, the exchange value of which is practically equivalent to that stamped on the face of them.
- (2) The payer is obliged to give and the payee is entitled to receive current money.
- (3) Banks having the power to issue "representative" money in the shape of notes are under the obligation to meet their notes by the payment of current money, without any charge being imposed for so doing.
- (4) The "Token" coins or coins containing metal of less than face value correspond in amount to the requirements of the community.
- (5) The coinage of current coins can be effected (under the Government control) freely and without hindrance for public or private purposes.

Stephenson's diagram concisely states the different monetary standards :—



In actual practice, the methods of payments used in Britain are :—

Through the Post-office :	Postal Orders. Money Orders.
Through the Banks :	Notes. Cheques. Bills of Exchange. Telegraphic Transfers.
Through the Treasury :	Treasury Notes.
Through the Mint :	Bullion. Gold Coin. Token Coin.

RESUME

After the Financial System had been shown to be an expression in terms that are universally intelligible of the values dealt with by the science of economics, an examination was made of the fundamental conception of money upon which the System has been built. The functions of money, and the attributes of "good" money were examined, and therein was found the idea of "a measure of value" coinciding with the conception of Finance as a means of measuring all economic terms and transactions. But the idea of money as a "medium of exchange" was observed to be a growth in circumstances differing from those of the present, owing to recent advances in applied sciences. Further, the "Quantity Theory," called a "Law," was seen to be based upon the commodity idea of money as a medium of exchange, and similarly the attributes of "good" money were found to apply primarily to gold.

Therefore the abstract conception of money was left with the proposition that monetary policy has

developed the quantity theory of money on the commodity idea, and gold has been evolved over long periods as the standard of value.

The organisation of money into currency systems has now been examined, and the gradual development of State control. It is seen that the basis of currency to-day is still metallic, with gold as the standard, while the regulation of currency, and the "creation" of money are still in theory the prerogative of the State.

But later it has been found that modern conditions have created a new form of money called representative money, that is based on credit and has an indirect connection only with "good" money. This representative money is now used in most of the operations of commerce and metallic currency has become merely the "small change" of every-day life.

Finally, in quoting from a leading authority on economics, the control of the banks over representative money is disclosed, and, at the same time, it is admitted that the new form of currency based on banking, that has been described as *a system of perfected barter*, constitutes the most flexible and convenient form of currency yet evolved in the world.

Therefore when it is remembered that the deposit and cheque system is the growth of a period coinciding with the full development of the "age of coal," the facts have so far emerged :

That economic development demands and creates new means of exchange.

That all monetary theories are entangled in olden ideas and the "Quantity" theory.

That the "Quantity" of economic utilities potentially available has overwhelmed the "Quantity" of money.

Therefore that the most important and satis-

factory currency is now credit, controlled by the banks,—

and

Finally, Credit is used as Money and Gold is a measure of value only.

The importance of representative money, or to use a more modern term, "credit-money," is thus emphasized, and when it is observed that the practical application of credit-money to the needs of commerce is under the practice of Bankers, and its control vested in them, again the necessity appears for careful examination of the meaning of general statements. Thus to the Banking system and its implications.

But the natural necessities of man are to him the dominant economic fact, of an importance more vital and personal than systems or theories, be they called "laws" or any other name. Let the student therefore renew his thoughts upon the meaning of economic laws, (pp. 15 and 29). For if the satisfaction of natural necessities should be made to depend upon a "money" that is not natural; and if that "money" should be identified as an artificial thing controlled by the Financial System, that is itself artificial, then indeed the power of a natural law or necessity has become vested in the Financial System. Money has become a licence to live; and if its control is vested in a particular system, there is formed a monopoly not only of "money," but of human necessities, of the Real Wealth that might satisfy them, and of those things of comfort and of happiness that are greater than life itself.

CHAPTER V

BANKING

DEFINITION

WHEN starting a consideration of the banking organisation, it is necessary to isolate the conception that is current regarding it, and base the examination on this plan.

The history of money has been traced from early times; it is shown to be the continual search for a medium whereby the exchange of economic utilities could be effected with the greatest convenience and expedition. Therefore, proportionate to the specialization of labour and occupations, it has become more and more a necessity to man.

On the larger view of its history, it is further to be noted that the early exchanges were made between the individuals of a (comparatively) sparse and static population. The element of the transport of economic values was almost absent. Therefore the actual commodity accepted as money was invariably used, and was an essential to the completion of the transaction.

But when it is remembered that the financial system is, fundamentally, merely the method adopted to measure the values of economic utilities produced by the industrial system, it is understandable that proportionate to the rapidity and multiplicity of

transport in the commercial organism, the attribute of money as a "measure of value," accepted over ever-widening areas, becomes more and more important. The transport of economic values would have been retarded, if the "medium of exchange" had also continually to be transported. Thus representative money was invented. And in this aspect the modern banking system is a logical development of commercial organisation, to serve the economic needs of the community.

The banking system, as its proper function, expedites the exchange of goods, or of economic utilities, without the necessity of an equivalent transport of gold, the "standard" money of to-day. This is accomplished by the system of "perfected barter" explained hereunder.

Yet apart from this function by which banking is shown to be the legitimate progeny of the economic system, the word "Bank," in the economic sense, covers various meanings which all express one object, a contribution of money for a common purpose. The first meaning of the word "bank" in the commercial sense was a subscribed or piled-up loan. It was formed in the middle ages, when the Italian Republics were the great financial powers; and when Venice, about 1150, under the pressure of her enemies started a subscribed loan, which in Italian was called "monte," and in German, "bank." Since Austro-German was spoken widely in Italy in that time, the loan was known by the two names: "Monte" and "Banc."

HISTORICAL DEVELOPMENT

For the purpose of the present examination, it is desirable to divide the historic development of Banking into two distinct periods, and in a similar manner

to show that banks, whatever their proper place in the economic structure may be, now perform two definite and separate functions.

(1) Firstly, the general history of modern banking may be said to start in the 16th century. Therefore the period of banking activity is much shorter than general monetary history, and coincides with the greater efficiency of transport and the increasing volumes of trade between organised states.

Banks in Europe from the 16th century onwards may be divided into two classes, the one described as "Exchange banks" and the other as "banks of deposit."

The exchange banks were a definite effort to overcome the "transport" difficulty. They were established to avoid the trouble caused to merchants by uncertainty in the value of the currencies of foreign countries, compared to that of the city where the bank was domiciled.

In 1873 was written in "Notes on Banking"; "The Bank of Hamburg is now the last survivor of those banks, whose business lay in the assistance of commerce, not by loans, but by the local manufacture, so to speak, of an international coinage. In a city of the highest rank of commercial activity, but greatly circumscribed in territory, continually receiving payments for merchandise in the coin of other countries, a common standard of value was a matter of primary necessity. The invention of bank money, that is of a money of account which could be transferred at pleasure from one holder to another, enabled the trade of the place to be carried on without any of those hindrances to business which must have followed on the delay and expense attendant on the verification of various coins differing from each other in weight, intrinsic value, standard of purity of metal, in every

point in fact in which coins can differ from each other."

In other words, the evolution of the economic system towards the unification of the world into one market had created new needs, and the function of money as a "measure of value" was adopted inevitably as the most efficient method of meeting the need. But the volume of trade was not great, and all monetary systems were then metallic, so that each note unit issued by such banks "represented" an equivalent value of metal.

As in the case of the Exchange bank noted in the foregoing paragraphs, the earliest example of the "bank of deposit" was founded in a great commercial city of the middle ages. Even so, it has grown up in a period much shorter than the history of money and currencies. The dealers in foreign monies in Venice began to accept monies on deposit. They were becoming bankers in the more modern sense between 1270 and 1318, as proven by an Act passed, in the latter year, by the City's government for the better protection of depositors.

Having started the acceptance of deposits as a regular practice of their business, it is easy to appreciate the development of the usage of loaning such deposits again, under safeguard, for the assistance of industry, or of making them the foundation of a more extensive "international currency" as in the case of the exchange banks.

Thus in effect money is being used twice, and by this means has developed the second function of banking noted hereunder, which is the creation of money, or the equivalent of money, to meet the requirements of an expanding producing system and the necessity for an increased facility for rendering effective the clamorous demand of growing communities for the necessities of existence.

Following on the Venetian practice, in the 16th century a similar practice was developed and extended in Amsterdam, also by the money-changers. A further connecting link with the modern system was forged in the 17th century, by the goldsmiths of England. They, being the only people who could keep valuable property safe, accepted the property of their customers consisting of plate, gold, silver, or coins, granting them in return,—

- (1) The right to payment in cash.
- (2) The direct payment to a third person by what was called a cash loan, now called a cheque.
- (3) The right to receive from the goldsmith a goldsmith's note, (similar to a modern bank-note), with the assurance that the goldsmith would pay, on demand, any person whatsoever who presented the note.

Finally, the banking system came into direct line for the present-day organisation by the establishment of the Bank of England in 1694. It was a "bank" in the original sense of the word, being based on a subscribed or piled up loan of £1,200,000 made to the Government at 8%, and it was granted incorporation by Royal Charter. By the linking-up of districts and the growth of international trading, the economic demand for financial organisation continued to become more insistent, and banks sprang up in all parts of the country, most of them on the "bank of deposit" principle issuing their own notes.

Thus the increasing volume of economic utilities was evidenced by a demand for more of the medium by which exchanges were effected, and also by the Bank Restriction Act, 1797-1819, forbidding the Bank to make its payments in cash and making the notes legal tender,—in other words, equivalent to the gold

or standard money. Therefore, though the English system was complicated by the expense of wars and other national charges, thus early is evident the tendency to be examined later (that has already been briefly mentioned) whereby the balance of the "Quantity Theory" is upset by an over-weighing of the available currency by the volume of production. The above Act gives official recognition to the necessity for an expansion of currency, and it is but the first of many artificial and disastrous attempts to balance an increasing potential "supply" of goods, with a limited "effective demand" for them, without abandoning the edifice of the Quantity theory that has been founded upon gold as the universal standard.

(2) The Nineteenth Century Period.

Thus opens the second period of historical development. It has already been noted that, in the science of economics, every theory or belief founded upon historical data prior to the industrial revolution should be scrapped, and that even in more recent conceptions the startling advances of the opening years of the twentieth century create a demand for further revision of every aspect of the relationship of man to the material wealth at his disposal.

In this light it is obvious that any tendency to a shortage of currency compared with the potential production of industry that was in evidence at the beginning of last century, should become cumulatively more pronounced with the passing of each succeeding year. This indeed has happened.

The opening of the new period may be dated from the Bank Charter Act of 1844, and this date also may be regarded as the commencement of our present industry, because then the principle of Joint Stock

enterprises, or the coöperative use of money, began to develop.

Yet a significant fact must be noticed immediately; one of the chief purposes of the Bank Charter Act was the mitigation of financial crises by preventing inflation of the currency; that is to say by an increase of the available "quantity" of money. At the moment when the industrial organisation began that series of astounding developments ending in its practically unlimited power of production to-day, a step was taken that empowered the Bank of England to regulate the "quantity" of money that should be made available to buy the wealth thus released for the use of the nation. That Act was based on the Quantity "Law," and was passed at a period when the gigantic activities of the applied sciences were just shaking off the old chains and the penuries of pre-coal ages.

Yet that Act still controls the banking organisation of to-day, as shown below on considering the Creative Function of the banks. Economic needs tend to become inevitable, and, in the absence of other means of supply, money has been created by the extension of the loan principle of the old banks of deposit. This amounts to a creation of money; it is the use of Credit as money, and is exercised chiefly by the joint-stock banks, which, starting about the date of the Bank Charter Act, now control an almost perfect commercial machine, in one sense, and in another have abrogated the function of governments in the creation of money, and thereby gained the power of command over every other economic function.

The two ideas are enumerated hereunder, and lead to the conception of the lesser swallowing the greater; Finance, defined as a humble servitor of the economic state, ascending to the kingship thereof.

THE SYSTEM OF PERFECTED BARTER

The first function of Banking referred to above can be detailed very concisely, and its efficiency illustrated.

To-day the "market" for goods is the world. Even without the promises of wireless telephony between individuals, the instantaneous transmission of happenings by photograph and sound, and also of writing; and the world-circling vehicles that will ride the whirlwinds of the upper stratas of the atmosphere; without these, the world to-day is one market, within almost instantaneous communication by telegraph and cable, and comparatively short periods of time for the transport of goods. Therefore the idea of a medium of exchange has faded out of the individual transactions of commerce, and they are completed, with the assistance of the banks, on the basis of the universal "measure" of value, gold.

Within one country, the process may be described as follows:—

- (1) The general measure of value is the currency of the country, which, theoretically, is fixed by the State upon the value of gold contained in the gold standard coin.
- (2) The exchange value of all economic utilities, and the amount of all monetary indebtedness, is expressed in terms of the currency; say, in gold sovereigns and smaller token coins passing as legal tender in Britain. All such values are included in the generic term "price."
- (3) Under the principle of a "medium of exchange," each individual exchange of goods must be closed by "the liberating power of money"; that is by the gold. But since transactions take place over great distances

and extended periods, and with great rapidity and enormous volume, to wait for the receipt of gold, the theoretical "medium of exchange," would greatly hinder the commercial organisation.

- (4) Therefore each trader is supposed to deposit his money (in theory his gold) with the banking system, and the system is supposed to have its branches made available to every trader, and, as it were, a stream of gold running within the system to be tapped at any point or any moment.
- (5) Then when the exchange of goods between two traders has to be settled by an equivalent exchange of gold, the purchaser writes a cheque. The cheque, be it assumed, is for £1,000, and, legally, is termed "a bill of exchange drawn on a banker and payable on demand."

The purport of the cheque may then be read as an intimation to the vendor that the debtor has deposited with a particular unit of the banking system £1,000 in gold, which will be paid to the vendor on demand. The vendor then goes to his own unit of the banking system and asks it to collect the amount of the cheque, handing in the latter.

But in effect the vendor's banking unit says *that all units are within the system*, and it knows that, if the cheque is not fraudulent, the gold is really held by the other unit, then it will regard the cheque as money, and earmark some of its own gold for the vendor's use.

- (6) In practice, however, the vendor may be supposed to lodge his cheque, and draw another against it, for the same amount. This cheque he sends to the original pur-

chaser, for some other kind of goods which the latter has sent him. The purchaser, now being vendor in a new transaction, lodges his cheque for collection of the necessary gold.

- (7) But, in effect, the two traders have exchanged at different times various commodities value £1,000, merely by the issue of a cheque or authority to their respective bankers to collect the gold, or medium of exchange, in each transaction.

ALL is based on "credit," because the banker does not transfer gold against each cheque or order to do so. He makes a book-keeping entry recording each transaction as it affects the trader, and by means of the Bankers' Clearing House (see Chapter VIII) all similar transactions are summarized into a further book-keeping entry representing the "balance" of transactions between the two units. This, again, is not completed in summary by a transfer of gold, but by a final book-keeping entry in the respective accounts of the units in the "centre" of the banking system, which, in practice, is the Bank of England.

Thus it is seen that the medium of exchange has been eliminated by the operation of the Banking system, and, applying the illustration to all the variations and intricacies of commercial operations, that the economic activities of a community to-day are in fact carried on by a *system of perfected barter*. (The practical operation is shown by diagrams on pp. 106-107).

THE SECOND FUNCTION OF BANKING

So far, it is seen that Banking is a valuable and efficient commercial organisation. It is to commerce

in extenso what the counting-house is to the individual firm. It records the exchange of commodities, and removes the burden of record, or of the actual transfer of currency, from the practical operator and places it in the hands of men devoted exclusively to this duty and specially skilled in the work.

Obviously, on such a severely practical interpretation of banking as the servant of commerce, the assumption is made that the money-theory or Quantity Law has actually been carried into practise. Gold, being the accepted medium of exchange, should be there; the banks should have the duty of holding it, while avoiding the necessity of actual transference for each transaction. Like the old bank of issue, gold should in theory be held for each note issued or each cheque accepted, even while one side of each exchange of commodities is completed merely by the book-keeping entry affecting a cheque or bill.

But already the tendency has been noted towards the shortage of money used as a medium of exchange, and attending the increasing potential supply of goods as compared with the money available for purchase.

The cheque system has grown to its present dimensions during the nineteenth century. The nineteenth century witnessed the growth of a new industrial era, the age of coal. Using a new and almost limitless energy, industry began to create economic utilities in volume and rapidity previously unknown. But the currency in use was suited only to the penurious output antecedent to the industrial revolution, therefore expansion was necessary, and in their wisdom the originators of modern finance began the use of credit as money, but, by the contrivance of the "gold standard," harnessed it to the metallic currency.

The new industry could not be bound within the narrow limits of the old financial state, and the medium of exchange, gold, was not capable of an

equivalent expansion. Therefore, credit was to be used, but it was to be severely circumscribed and made the slave, not of the industrial system which it was designed to serve, but of gold, the centre of the older currency and monetary policy.

This fundamental fact has been commented upon, in passing, when the Bank Charter Act was mentioned. It is reiterated, because it founded the system of the gold-control of industry that is now prevalent.

CREDIT-CURRENCY

Therefore the second function of Banking is the use of Credit as money. A bank, wrote David Ricardo, would never be established if it obtained no other profits but those derived from the use of its own capital. The real advantage of a bank to the community it serves commences only when it employs the capital of others. The money which a bank controls in the form of the deposits which it receives and sometimes of the notes which it issues, is loaned out by it again to those who desire to borrow and can show that they may be trusted. It only holds the funds with which it is entrusted until it can use them and the use is found in the advances that it makes. These advances are made to men who wish to employ them on reproductive industry; that is to say, in work which rewards the controller with a return of the capital employed and an added profit, while at the same time founding and carrying on an enterprise beneficial to the community. (The creation of NEW money by such advances will be explained in Chapter VIII.)

Be it noted, that it is only by reproductive industry that the capital advanced by the banker can be replaced. To this extent, the bank is still dependent

upon the producing system it was designed to serve. It advances money to those who desire it, in the belief that there is a certainty of its return owing to the work they wish to engage upon.

Therein lies the element of Credit, which is plainly the belief or confidence which is reposed in anyone. So the banking system reposed confidence in the industrial system, and on the one hand, receiving money on the deposit principle embodied in the first function already described, promptly advances those deposits to other people in the belief that the depositors will work by cheque, and will not ask for "Standard" money.

The credit circle is complete, a circle of belief or confidence.

(1) The producers or industrialists working within extensive markets, wish to avail themselves of "the system of perfected barter" that is to them the primary function of banking. They therefore deposit their money in the belief that it will be held for them to form the "stream of gold" within the system. They then proceed to deal over wide distances by cheque.

(2) The banks, having established absolute confidence in their stability, and believing that depositors will work by cheque in that confidence, proceed to advance the money received to other producers, in the belief that it will be returned by reproductive work.

(3) The persons receiving the advances proceed to draw cheques upon them, which are paid away to other people and in due course are re-lodged with the banking system as deposits in the belief that gold will be collected, and credited, against them.

(4) The goods produced are in due course sold, cheques being accepted, and the original loan is repaid.

(5) Thus on analysis the credit system is a demand by an expanding industrial system for currency in the

belief that there is a necessity to produce certain goods which the community needs. In effect, there is a demand for goods, but sufficient currency does not exist to render it effective, and more must be created by the use of credit. *Each loan creates a deposit, and has an effect precisely similar to the use of new money*; it is used to bring into being new economic utilities.

USURPATION OF STATE FUNCTION

The economic structure of society is the very skeleton upon which the life of the society is built. Before any cultural environment may be created or enjoyed the animal necessities must be satisfied. That satisfaction is by the production of economic utilities by specialized industry, their exchange between the various departments thereof, and ultimate consumption. Wealth yet consists ultimately in the stream of production of necessities, and the exchange is made possible, as has been stated, by the currency system. So the currency is really the life-blood of a society that is considered, properly, as an organism.

Therefore it has been rightly admitted that all questions concerning the creation of money and the control of currency should be decided by the State, acting on behalf of the community as a whole. Such questions are vital; they are questions indeed of life or death to those who, in the modern state, cannot obtain the currency that is the only accepted evidence of a claim upon the "Stream of production." These questions are above all considerations of profit or loss; of personal gain or individual power; from all such things the central power alone can be supposed to be removed.

Yet the creation of credit-money is not controlled

by the State, and the necessity of the community, as such, is never considered in its issue. Credit-money is created by the banks and controlled by the money-market, and the consideration of its issue is the imposition of the shortest possible period of return. It is used for personal gain by the operators of the money-market, and it is created upon their individual judgment of the producing capacity of the borrower, and the potential demand for his product.

Therefore, in a condition of affairs when the demand for, and potential supply of, economic utilities has advanced infinitely more quickly than the old metallic currency; when a new currency in the shape of cheques and bills has been created to meet the new conditions; and when that new currency is controlled entirely by the operators of the money-market, it is accurate to say that the financial system has usurped the functions of the State, and, by the power of its veto upon new production, has brought the industrial producing system under its domination and, through this means, the whole condition of the "economic man."

THE PRESENT POSITION

The outstanding features of the financial system may be shortly summarised:—

- (1) An overwhelming preponderance of Credit-money as the currency of commerce.
- (2) The consequently insignificant proportions of the metallic currency and gold.
- (3) The complete insolvency of the banking system, if regarded as a structure founded upon and carrying out the principles of a metallic currency based upon gold.
- (4) The attempt made to reconcile the credit-

currency with the fundamental idea of a gold "medium of exchange" by means of the check created by the Gold Standard.

But these considerations are so important that they will require more detailed consideration.

Meantime, it is observed that to-day the banking system is universally adopted in the operations of commerce, and in England one branch exists for approximately each 4,000 of the population.

All the major operations of commerce are completed without the use of money other than a cheque; the whole commercial system therefore operates upon a *system of perfected barter*.

In 1920, the turnover of cheques that passed through the banking system, and were dealt with by the Clearing Houses,

	was - - -	£89,000,000,000
In the same year	bank-notes circulated	190,000,000
do.	Treasury Notes "	868,000,000
	Total - - -	£89,558,000,000

Therefore the trade of Great Britain employed a currency to the extent of almost forty thousand millions of pounds sterling during 1920, consisting entirely of representative money based upon credit. Against this, the gold and other metallic currency did not exceed two hundred millions sterling; the whole of the gold reserve of about £150,000,000 was concentrated in the Bank of England.

INSOLVENCY OF THE BANKING SYSTEM

The banking system is the machine built by the modern necessities of commerce to work the currency whereby commodities are exchanged. The currency,

in theory, is gold, and for each note issued or deposit received the banks are supposed to hold an equivalent value of gold.

But the banking system has abrogated the function of the State in the creation of money, by the use of credit-money, and, by the operation of the credit-cycle, it is obvious that if each deposit received by a bank is immediately re-loaned by it, and if the deposit is already based upon a loan received elsewhere within the system, then the element of gold is entirely absent from the transaction, and the banks are trading upon commercial usage and credit alone. An examination of the figures hereunder establishes the fact.

AGGREGATE BALANCE SHEET

of the Banks of the United Kingdom
(excluding the Bank of England)
at the end of the year 1920

Liabilities.		Assets.	
Capital, Reserves and Undivided		Cash and Money at Call	- 580,868,000
Profits - -	170,945,000	Investments -	558,848,000
Deposits - -	2492,061,000	Advances -	1561,887,000
Acceptances, Notes, Drafts, etc. - -	171,881,000	Cover for Acceptances, etc. - -	184,889,000
	<u>£2884,887,000</u>		<u>£2884,887,000</u>

Of the Liabilities shown, Acceptances, etc., are covered by the contra entry of the security deposited, while the Capital is the contribution of the bank proprietors, principally on the joint-stock method.

Therefore the outstanding fact disclosed is that on the basis of the "bank of deposit" the banking system has accepted deposits amounting to

£2,492,061,000. On the principle of a metallic currency, an equivalent amount of gold should be disclosed to "convert the deposits into standard money on demand."

But, on examining the Assets, the only item bearing the word "Cash" amounts to £580,363,000. And this, as will be explained when examining the Money Market, (Chapter VIII), is not gold or standard money, but contains no gold or practically none; merely claims upon others, notes, and a claim against the Gold Reserve held by the Bank of England.

Investments represent claims upon the property of governments or companies to whom the banks have advanced money in return for shares, under the joint-stock system, and include the value of land, buildings, or real property.

Advances represent the loans made from deposits to other producers, which are secured either by claims on real property, or the banker's belief in the borrower's capacity to produce goods for sale, and so reduce the loans by deposits.

It is now found that with the gold held by the Bank of England the actual metallic currency available at this date could be reckoned, on the most generous estimate, at no more than £200,000,000. Therefore, on the basis of a gold standard currency, the banking system is entirely insolvent.

Moreover, by no method could it be made solvent on such a basis.

Assuming the availability of the small quantity of gold, if faced with a demand for refund of deposits, in gold, and under the most favourable conditions, it could not be done.

First, the banks would call upon all debtors for the return of loans and advances. The debtors would then, having no "real" money, require to dispose of

their properties, or, if permitted, continue to produce goods for sale. But, (since the available metallic currency is included in the figure £200,000,000), their goods would be sold in return for cheques which they would lodge to reduce their loans. As the cheques must be drawn upon deposits, the latter would be reduced proportionately.

Therefore the fact emerges that, in order to honour the "gold standard" theory, the depositors with the banking system would first of all be required to purchase the whole of the real property or rights represented by the "advances," which is unthinkable. Even then, they would not receive gold for the balance of their claim, but shares in other corporations or government securities. (If more gold were suddenly produced, it would belong to an individual, and if lodged with the banks would increase deposits proportionately.)

The balance is ultimately exact, but it is not a gold balance. Currency is based on real property, not on gold. On a gold basis the position is absurd; the banking system is hopelessly insolvent. The real operator is the genius of Credit, and its monetisation by the banks.

ATTEMPTED RECONCILIATION OF CREDIT-MONEY AND GOLD

Under the stress of war conditions, the theoretical solvency of the banking system collapsed in 1914 like a house of cards. And, in proof of the submission that the real problem is the balancing of available currency with potential production (The Quantity Theory), during the war years when consumption, by the sabotage of war, was limitless, the available currency in the form of credit-money and shown by bank deposits increased two hundred and fifty per cent. to the figure quoted for 1920. The implications

thereof, and the evident evils of the Quantity Theory, have unfortunately been ignored by financial authorities.

In August, 1923, in "Bankers and Credit," Hartley Withers writes; "Before the war our monetary system was based on gold, and the pieces of paper,—notes and cheques,—by which most of our large transactions were paid for were claims to so much gold which the holder could turn into gold if he wanted to do so."

It has been proved by two methods,—the yearly turnover of currency, and the static figures of the banking system at a specific date,—that this convertibility of paper into gold is a fallacy, and is in fact impossible.

The real operation of the gold standard does not lie in the holding of an adequate reserve of gold, while the banks carry out the wonderfully efficient "system of perfected barter." The gold standard resolves itself into the actual control of industry by the Money Market. Under that heading its actual working may more adequately be examined. It is here sufficient to note its failure to disprove the actual preponderance of credit as money.

But the student continues to think upon the meaning of those laws that he obeys, and he asks; is this credit-currency indeed controlled by a system that is false to his necessities? For if this be so, it would seem that his economic freedom has passed away from him, and his existence is not bounded by the universal laws of Nature, but by a "system" the operation of which is recorded by figures in a ledger.