Select Statutes Documents and Reports Relating to British Banking 1832–1928

Volume I
1832–1844

T. E. Gregory

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SELECT STATUTES
DOCUMENTS & REPORTS
RELATING TO BRITISH
BANKING 1832–1928

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VOLUME 1 1832–1844

Selected and with an introduction by

T. E. GREGORY

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INTRODUCTION

§ I

THE student who turns from the literature of the Heroic Age of British monetary controversy in order to attempt a study of the original sources relating to the antecedents of our modern banking situation will find himself confronted with a jungle of blue books and Parliamentary discussions, pamphlets and tracts and leading articles: a jungle at first sight so impenetrable that he may well despair. For it is characteristic of the period of middle-class ascendancy after 1832 that it produced much heat and little light; many massive volumes of evidence and statistics, but no classic reports; much legislation but, for a long time at least, no final solution of the various problems to be faced. These volumes are an attempt to bring together some of the material by which the growth of British banking policy and of British banking institutions, in the Victorian era particularly, can be illustrated and illuminated. The original intention was to cover the period 1832–1925 in a single volume, and to accompany it by a volume covering the rise of British banking and the vexed era of the Restriction and the Resumption of Cash Payments. It very soon became apparent that, unless the book was to be nothing but a collection of mere snippets, restriction of scope and extension of space were indispensable. Thus very little will be found in these pages of the detail of banking practice: the development of Colonial Banking and contemporaneous events in Scotland and Ireland have had to be excluded, and the development of the capital market neglected. These are defects of which the present writer is fully aware, and he can only plead that even within the field so restricted, the material from which he was forced to choose was so overwhelming that but a small fragment can be presented here.

The value of original material lies only in part in the evidence it presents of the tendencies of thought or of the movements of events. A secondary but still not immaterial consideration is that it is only by the study of original materials that the tone of economic life, the temper of an age, can be fully appreciated. Mere antiquarianism is a taste for which the present generation least of all has any profound respect; but still, the language in which economic concepts are clothed has varied more, perhaps, than the concepts themselves, and there is some instruction to be derived from studying the words in which the leaders of the banking world in successive generations have dressed their arguments and convictions. Conflicts in the sphere of banking policy have revolved round a relatively restricted number of central ideas, but it is only by becoming familiar, through the study of documentary material, with the diversity of phrase that one comes to realize the real identity of content.

§ II

By 1832, when the series of documents included in this collection begins, British banking had already advanced some stages in the process of adaptation to a more complex economic environment. The question of the currency standard had been settled in 1819, though for a decade there were violent debates inside and outside the House of Commons on the wisdom of the steps taken. The Bank itself was hostile to the theories of the Ricardian economists which had inspired the Resumption Reports of 1819, and had expressed its dissent in a Minute which was published with the evidence submitted to the Secret Committees. On this point, time and experience gradually produced a change in the attitude of the Bank Directors, and in 1827, on the motion of William Ward, the hostile Resolution was expunged. This implied an acknowledgement on the part of the Bank that in the management of its note issues it was bound to have regard to the state of the foreign exchanges, so that a declining gold reserve ought to be accompanied by a declining note circulation. Now the Bank itself did not export gold when the exchanges were unfavourable: this was done by the public, and as the note issues naturally declined as they were exchanged for gold for export, the rule of having regard to the state of the foreign exchanges was interpreted to mean that, at a time when the public was taking gold, the Bank should not reissue the notes by means of additional loans. As was explained to the 1832 Committee, the aim was to keep the securities steady, so that fluctuations in the note circulation were to be caused by ' the action of the Public ', gold inflows causing an expansion of the note circulation, gold outflows a decline.

One difficulty at once presented itself. The securities of the Bank of England consisted of two portions, then as now, that is, Government Securities—largely Exchequer Bills—and commercial bills of exchange. If the demand for discounts increased, the Bank could compensate this additional demand by allowing Government Securities to run off or could sell them in the open market. But the amount of discounts offered to the Bank depended on the relation between Bank rate and open-market rates; and the question arose, what was the Bank to do if the demand for discount accommodation went on increasing so that the *Total Securities held* rose? Under the Usury Law the Bank could not charge more than 5 per cent. discount. It had either to go on discounting or to adopt some alternative device for limiting the offer of bills to it. It chose, as a matter of fact, to go on discounting, thus virtually abandoning its principle of keeping the securities steady, but also implicitly realizing that a Central Bank at critical periods *must* be prepared to accommodate the market. In 1825, after a period of hesitation, the Bank, with practically no reserve left, still went on discounting freely and saved the country from a second suspension. It was with these aspects of Bank policy, the reconciliation of the diverse elements of which it was composed, that the Committee of 1832 was largely concerned. In another respect the money market and the Central Bank were coming into closer touch. From 1829 onwards the Bank began to advance on securities in anticipation of the Quarterly Dividends Payments, thus evening out the flow of funds into and out of the market; though originally the advances were made not at or over Bank rate but below it.

Joint-stock banking was in its infancy, but had already given rise to much correspondence between the Bank and the Government, and was a cause of great heart-burning and dismay to the country bankers, who, in the period between 1826 and 1832, were in violent opposition to the Government, the Bank of England, and the Joint Stock Banks. The issue over joint-stock banking had been joined in 1822, when the Government offered to prolong the Bank Charter until 1st August 1843, in place of 1st August 1833, provided the Bank were willing to waive its monopoly of joint-stock note-issue outside a sixty-five-mile radius from London. These terms were accepted both by the Court and by the Proprietors, but the matter seems not to have been pursued. After the crisis of 1825 the Government again approached the Bank, and this time adopted a thoroughly hectoring tone. After the expiration of its Charter, the Bank could not expect to see its exclusive privileges prolonged—'such privileges are out of fashion: and what expectation can the Bank, under present circumstances, entertain that theirs will be extended?' After a period of hesitation, the Bank gave in and consented to allow the formation of joint-stock banks of issue outside a sixty-five-mile radius, subject to it itself being allowed to open branches. Thus the country bankers found themselves at one and the same moment confronted with two types of competition: that of the Bank and that of the new joint-stock banks.

The note-issuing privileges of the country bankers were also affected by fresh legislation passed as a consequence of the crisis of 1825. Originally, the £1 and £2 note issues which had been sanctioned by the emergency legislation passed at the outbreak of the war were to have been withdrawn 'Two Years after the Expiration of the Restriction upon Payments in Cash by the Bank of England' (56 Geo. 3, c. 21). In 1822 this period was extended till 5th January 1833, by 3 Geo. 4, c. 70. Acting on the assumption that these small notes were a form of currency peculiarly liable to abuse, the Government, after the crisis, decided to put an end to them. In its assault upon the same type of note in Scotland and Ireland the Government was unsuccessful; but by 7 Geo. 4, c. 6, small notes were to be retired in England and Wales after 5th April 1829. The small notes of the Bank of England had already been withdrawn in 1821, when, anticipating the date fixed by the Resumption Act, the Bank reverted to full cash payments. The position of the country bankers was not made easier by the fact that the Bank of England gave special rediscount facilities to country joint-stock banks prepared to substitute its notes for their own.

The result of these steps was a movement towards co-operation among the country bankers. In October 1827 a few country bankers came into touch with the Committee of London Bankers, at which meeting it appears to have been agreed that the new policy inaugurated by the Bank was ' unjust and dangerous ' and that it was desirable to organize an ' effectual opposition to their recently adopted principles and practices '. In May 1828 the country bankers claimed a right to be regarded ' as parties in the intended application for the renewal of the Bank Charter and that no special privilege or monopoly be granted or continued to the Governor and Company of the Bank of England: but that they may be placed on a perfect equality with the country bankers in the competition which, by means of their branches, they are now carrying on with your memorialists '. To this demand the Government replied that it would not lose sight of the interests of the country bankers in any negotiations with the Bank of England. The battle between the various sections of the banking structure was thus fairly begun.[1]

§ III

The appointment of a Secret Committee to inquire into the expediency of renewing the Bank Charter was moved by Lord Althorp in the House of Commons on 22nd May 1832,[2] who said that opportunity would be taken to inquire, not only into the Charter of the Bank, but into the banking situation as a whole. Subsequent discussion turned mainly on the point of whether or not it was desirable to include within the scope of the inquiry the question of the £1 note, but no attempt was made to guide the House into surveying the problems of British banking as a whole with a view really to instruct the Committee. Since the members of the Secret Committee had been specially selected with the idea of representing all points of view,[3] it is not surprising that their Report is a somewhat disappointing document. Nearly the whole value of the proceedings lay in the enormous

[1] For the expression of the views of the country bankers, *v. Memorials of Country Bankers to Government*, 1828–1833, P. P., 1833, vol. xxiii.

[2] *House of Commons Debates*, 3rd Series, vol. xii, col. 1356 *et seq.*

[3] *V. loc. cit.*, col. 1358.

mass of evidence collected, not only as to the policy and practice of the Bank of England, but also as to British banking practice generally. But by stating in detail ' the principal points to which they have directed their attention ', although on no single one did the Committee consider the information obtained ' so complete as to justify the Committee in giving a decided opinion ', the Report does throw some light upon what, by the men of the day, were considered to be the vital points at issue. The vital points the Report states thus:

> ' Whether the paper circulation of the metropolis should be confined, as at present, to the issues of one bank, and that a commercial company? or, whether a competition of different banks of issue, each consisting of an unlimited number of partners, should be permitted?
>
> ' If it should be deemed expedient that the paper circulation of the metropolis should be confined, as at present, to the issues of one bank, how far the whole of the exclusive privileges possessed by the Bank of England are necessary to effect this object?
>
> ' What checks can be provided to secure for the public a proper management of banks of issue, and especially whether it would be expedient and safe to compel them periodically to publish their accounts? '

These are significant statements. The centralization of note issues and the publication of accounts are undoubtedly two of the pillars of modern Central Banking practice, and it is not surprising, therefore, that information and guidance respecting them should have been sought by the Committee. But it would hardly occur to the modern mind to regard them as the most important matters into which a Committee of Inquiry into an established Central Bank would look. The Reserve, the Method of Control, the Government of the Institution, the Relations of the Central Bank to the Money Market, as determined both by the structure of banking and the methods of control used and available, *these* are the types of question which spring to mind as primarily involved in an examination of a Central Bank. The difference between 1832 and 1928 lies in the fact that the men of the period did not, as we are inclined to do, take a Central Bank for granted; whilst the paradoxical aspect of the situation of 1832 lay in the fact that, in spite of indecision on the main point of principle, a Central Bank in the true sense did actually exist, and the labours of the Committee were largely devoted to elucidating the principles upon which the Bank of England worked and the difficulties which a detailed examination of those principles revealed. That the practice was much in advance of the theory is clear from the evidence given by the Governor and one of the most distinguished of his colleagues on the Board: the general line of the argument is directed to showing that the Bank of England is *not* in the same position as other banks; therefore it ought not to compete with the other banks in discounting commercial bills in normal times,[1] nor ought its utility as an institution of last resort in times of difficulty to be hampered by altering its form of government,[2] nor is it deemed desirable that the rate of interest should be lowered ' by competition, on the part of a body like the Bank ' [3]; *because* at those times ' when a scarcity of money or discredit exists in the London commercial money market . . . the Bank becomes the main support of the commerce of the country '; it is undesirable that the discount-rate policy of the Bank should be hampered by the existence of Usury Laws, limiting the rate of discount and thus compelling the Bank ' to limit the quantity or description of bills to be tendered for discount; either of which last measures would be equally detrimental to the commerce of the country '.[4]

The Secret Committee not having recommended any positive policy at all, the Government was in a position to negotiate [5] with the Bank without having its hands tied in any way. It finally offered the Bank an extension of the Charter for a further twenty-one years, subject to a break at the end of ten years, if the then existing Government should see fit; and, further, proposed to make Bank of England notes a legal tender and to modify the application of the Usury Laws to bills of exchange having not more than ninety days to run before due date. These concessions

[1] *V. infra*, vol. i, pp. 13 *et seq.* [2] *V. infra*, vol. i, p. 16.
[3] *V. infra*, vol. i, p. 18. [4] *V. infra*, vol. i, p. 16.
[5] The negotiations can be followed in detail from the Parliamentary Returns, viz. (1) *Correspondence and Minutes of Conferences . . . on the subject of the Renewal of the Bank Charter*, and (2) *Communications . . . between the Government and the Bank of England bearing date subsequent to 3rd June, 1833*, in P. P., 1833, vol. xxiii.

were made conditional on the Bank agreeing to a modification of the rights of banking companies outside the sixty-five-mile radius to draw bills on London without restriction as to amount and to issue notes payable in London; and to the rendering of a confidential return, to be published only in an averaged form. Government further notified the Bank that it proposed to legislate on the subject of ' country banks. The provisions of the measure will be such as to hold out an inducement to the establishment of joint-stock banks who will not issue their own notes.' On 31st May 1833 Lord Althorp introduced his measures to the House of Commons.[1] The Government proposals with regard to the establishment of Chartered Joint Stock Banks did not win assent; and the Bank Charter Act of 1833, beyond providing explicitly for a recognition of the right of non-issuing Joint Stock Banks to open within the sixty-five-mile radius, left the *general* banking situation mainly unchanged, though embodying the modifications set up above.[2] The direct cost to the Bank was a reduction of £120,000 in the amount paid for the management of the Public Debt.

§ IV

For a period of eight years the Bank of England—but not the Joint Stock Banks—was relieved of further inquiry. But on 10th March 1840 the Chancellor of the Exchequer moved the appointment of a new Select (and Secret) Committee on Banks of Issue. The practical reason given was that, as the Bank Act of 1833 provided for a break in the Charter (on due notice being given) in 1844, it was desirable that ample time should be available for conducting preliminary inquiries into the policy of the Bank. That such inquiries should assume an ample scope was rendered particularly necessary by the division of opinion among the experts and by the absence of any agreed first principles; indeed, ' the question to which their attention ought to be specially called was as to the existence of a bank having any particular privileges—whether the existence of that bank was right or proper—whether

[1] *House of Commons Debates*, vol. xviii (3rd series), col. 169.

[2] For the protest of the country bankers against the general tendency of the 1833 legislation, proposed and actual, *v. Copies of Memorials, &c.*

it would not be more advisable to introduce the system called free banking; whether, if they conceded that a bank ought to exist, sufficient powers had been given to it to perform those functions which they expected a bank to perform. And then again there was the question, whether it were advisable at the present moment to reconstruct the whole system and have but one bank of issue.' Apart from an admirable speech by Grote, the rest of the debate upon the motion turned upon non-essentials, though the motion was, of course, agreed to, but not without further difficulties arising out of repeated attempts to alter the composition of the Committee.

The Chancellor of the Exchequer had not in the least exaggerated the prevailing state of intellectual confusion on the subject of Central Banking and of note-issue in general. The Bank of England was exceedingly unpopular, and the direct cause of that unpopularity is to be found in the dissatisfaction aroused by the conduct of the Bank since the last revision of the Bank Act: a dissatisfaction voiced almost as strongly by Tooke, who was later to be the leader of the opposition to Peel's measure of 1844, as by Lord Overstone and Colonel Torrens and G. W. Norman, who may claim to be the main protagonists on the other side. But the legislation of 1844 was an attempted solution of certain definite difficulties, and not a mere application of an *a priori* currency theory. If in the last resort the plan of 1844 springs from Ricardo's posthumous tract of 1824, the *Plan for the Establishment of a National Bank*, it was the conduct of affairs by the Bank which enabled the reformers to base their case on the existence of definite and pressing evils.

Since 1832, as the voluminous evidence collected by the Committee of 1840 (which was reappointed in 1841) showed, the rules by which the Bank of England professed to be guided were not observed in practice. The Bank did not maintain the securities even; it did not maintain a normal cash-ratio of one-third of its liabilities to the public; more important still, the action of the public, to which the Bank professed to look, did not result in decreasing the note-circulation as the reserve or ' Treasure ' fell off. The truth is that the circulation varied a great deal less than the reserve, the twofold explanation being that the deposits varied more than the note circulation did, and that the mechanism of the money market made it inevitable that, if a decline in the cash reserve resulted in a simultaneous reduction in the resources of the money market, outside money rates would rise towards the level of the Bank rate, and that bills would consequently be taken to the Bank in large quantities for discount. *Unless* the Bank managed to offset increased discounts by sales of securities, the liabilities would remain steadier than either the securities or the reserve, or, what is the same thing, notes issued against securities would replace notes against cash. The result was (as it was put to the House of Commons by the Chairman of the 1840 Committee) that, taking average quarterly figures between 1832 and 1840, 'in that period the difference between the highest and lowest amount of deposits was £12,384,000; securities £10,804,000; bullion £8,178,000; whilst the difference between the highest and lowest amount of circulation is only £3,334,000; the securities, which were to have been kept even, varied to the extent of nearly £11,000,000, and the circulation, which ought to have varied with the influx or efflux of bullion, varied only to the extent of rather more than £3,000,000. The result of the action of the Bank was to keep their circulation even and to let their deposits, securities, and bullion vary.'[1]

This general failure to implement the policy of 1832 culminated in the 'crisis' of 1839, itself not distantly connected with the minor 'pressure' of 1835–6. In the last resort the difficulties of the Bank sprang from the movements of the trade-cycle in Great Britain and the United States, the boom culminating in both countries in 1836–7 and being followed by the inevitable depression.[2] But the immediate point at issue was the degree to which the Bank contributed to its own difficulties in 1839 by pursuing too lax a credit policy previously. The straits to which, in that

[1] *House of Commons Debates*, vol. lxxiv (series 3), 20th May 1844, col. 1361. Wood added, 'I repeat that I do not mean, or wish to blame, the conduct of the Bank Directors. On the contrary, they were perfectly right in departing from their rule; but the consequence is, that there has been, and is, no rule at all for the regulation of their issues.'

[2] Cf. Silberling, *British Prices and Business Cycles*, p. 242; and Thorp, *Business Annals*, p. 76. Silberling's curves show a revival in 1838–9; Thorp describes these years as years of 'depression'.

year, the institution was reduced can be gathered from the fact that, had it not been made possible for it to borrow in Paris, the entire cash reserve of the Bank would have disappeared. What made the responsibility of the Bank still greater, in the eyes of its critics, was that it had had exceptional opportunities for controlling the market situation in 1834–7, owing to its command over certain special deposits, an opportunity which it was charged with neglecting. And, whilst not utilizing the resources at its command, it endangered its own future by coming to the assistance, in too liberal a manner, of the Anglo-American finance houses and certain Irish and British banks which found themselves in difficulties.[1]

It must not be forgotten that the Bank was not the sole source of note issue. Some progress had already been made in the study of the relative movements of country note issues and Bank note issues, especially by Tooke and, somewhat later, by Gilbart, whose important evidence on these matters is printed below.[2] But the fact that there were many independent sources of issue enabled the apologists for the Bank to argue that it was useless for the Bank to contract its issues if, simultaneously, the country bankers increased theirs, and it also enabled critics of the existing situation to argue that that being so, the only solution of this opposition of interests was to unify the note issues, either in the hands of the Bank or some other single and central authority.

§ V

Behind the wrangle on points of detail which preceded and followed the passage of the Bank Act of 1844 lay an important issue of principle. Given a metallic standard, with convertible notes circulating side by side with coin, was it true that the self-interest of *issuers* of notes and the self-interest of *holders* of notes would form such a system of checks and counter-checks as automatically to adjust the amount of notes issued to the volume which *ought* to be issued? That amount was given by the neces-

[1] The details of Bank policy during this period can best be studied by following the evidence given by J. Horsley Palmer before the Committee of 1840.

[2] *Infra*, vol. i, pp. 70–81.

sity, first, of maintaining parity between paper and coin inside the country; and, since the metallic standard was an international one, secondly, of maintaining parity between the money of the issuing state and that of the other states with the same metallic standard. In other words, the question at issue was the validity of enlightened self-interest as a guide to right note-issuing policy. The advocates of the Bank Act denied that equilibrium was necessarily maintained at all times by leaving the management of the note issues absolutely free: the opponents of the Bank Act affirmed that—subject to one important condition—self-interest would maintain equilibrium. True, if there were more than one issuer, it was to the interest of each issuer to push as many notes into circulation as he could; but then, the self-interest of all the other issuers was to return his notes to him in order to leave more room for theirs. And all the issuers of notes together were at the mercy of all the holders of notes. *Given convertibility*, there could be no divergence between notes and coin. For if there were, notes would at once be presented for conversion. The upper limit of note issue was fixed by the unwillingness of the holder to hold a note if it paid him better to hold coin; the lower limit of note issue was given by the unwillingness of an issuer to leave a single would-be holder of notes unaccommodated. Competition between note issuers would see that the demand for notes was satisfied; the self-interest of note holders would see to it that not too many notes were issued as a consequence.

Granted this chain of argument, *both* monopoly of issue and control over the monopolized issue by law was unnecessary; for, if in the end the holder and not the issuer of notes controlled the situation, why interfere with existing rights in any way? On the other hand, to deny this optimistic chain of argument was still not equivalent to proving the necessity *both* of monopoly of issue *and* of controlling the issue by law, apart from uniting the issue in a single authority. The advocates of the Banking legislation of 1844 affirmed *both* that competition made for over-issue—' competition is to place a great public trust, for such the issue of paper money really is, in the hands of a body, when, by its own statement, it appears that it is in the interest of each separate individual of that body to violate the rule upon which the public interest requires they should act, and even if interest does not lead them to violate it, they state that it is impossible for them to attend to that rule '[1]—*and* that not even a single issuer will manage his issues properly in the absence of adequate safeguards, since ' a close investigation of the events . . . has led observant and reflective minds to perceive that the constant right of converting your paper into gold does not secure with sufficient efficiency those which are really the ultimate ends and objects for which that convertibility was established '.[2] If the will and right of the holder of notes is not a safeguard against over-issue, temporary though that over-issue may be, the self-interest of the issuer certainly cannot be regarded as an effective safeguard, since it is obviously always to the immediate self-interest of the issuer to issue as many notes as he can. If he is to be restrained from increasing his issues too much, that restraint must come either from his knowledge of the ulterior consequences, which he may shrink from, or from the enactments of law. The problem cannot be left to be solved by the operations of ' demand '. But it is a far step from considerations of this sort to the detailed provisions of the Bank Act of 1844.

What the Currency School *wanted* was ' a regulation that depended upon principle, instead of a regulation that depended upon panic '; for a panic could only be met by ' paying out gold till the drain ceases ', whereas the desirable policy was ' contraction applied in the early stages when it could be borne without inconvenience to the community . . . and would necessarily tend to counteract and check in their early growth those tendencies, viz. to speculation, overtrading, excessive rise of prices, which, by their undue expansion under our present system and the consequent violence of the subsequent collapse, produce the extreme intensity which characterizes the commercial crisis of this country '.[3] The practical embodiment of this wholly admirable ideal was the Separation of the Departments, by which the volume of notes issued was expanded and contracted (over and above a fixed fiduciary amount) in strict accordance with the

[1] S. J. Loyd (Lord Overstone) before the 1840 Committee; *v. infra*, vol. i, p. 50.

[2] *Infra*, vol i, p. 53.

[3] *Infra*, vol. i, p. 36.

inflow and outflow of bullion. This division *could* have been simply defended on the twofold plea that, as in a panic notes would be returned and ' there is no method of meeting it but by paying out gold till the drain ceases ', the notes ought to be specially protected, and that the Bank of England would be forced to govern itself in the Banking Department as the Bank Act forced it to govern itself in the Issue Department: that is, the Bank would always contract and expand credit in the Banking Department in strict accordance with the Banking Department's reserve. It could have been argued that the operations of the Bank as a whole would thus be governed in accordance with a ' principle ', and that that principle conformed to the ideal postulated by the Currency School. But this was *not* what the Currency School said: on the contrary, Overstone urged that ' the management of a paper currency and the management of banking deposits cannot be blended together in one system, and treated as subject to the same laws and to be governed upon the same principles '.[1] What was wanted was contraction; but the Bank was forced to *expand* credit in a period of strain and did, in fact, extend increased accommodation in such periods.[2]

Unable to see their way through this seeming contradiction, the Currency School fell back upon the thesis that deposits were not ' money ' and that it was the contraction of the monetary supply which was the vital matter. This distinction between what was or what was not money was, however, quite beside the point: because, even if deposits were not money, it was impossible, as Tooke urged, for the Issue Department to remain nominally solvent if the Banking Department was threatened with insolvency

[1] Overstone's *Tracts*, p. 63; cf. *loc. cit.*: ' The principles upon which these two branches of business ought to be conducted are perfectly distinct, and never can be reduced to one and the same rule.'

[2] *Op. cit.*, p. 83: ' The abstract possibility of contracting issues by an absolute refusal to discount cannot be doubted; the real practicability of such a step as a measure of business is, however, much more questionable.' p. 181: ' The Bank seems thus called upon to act in a circle; a decrease of bullion requires a decrease of issues; decreased issues produce commercial pressure; in consequence of which, public and private credit is shaken; and there arises the obligation of the Bank to interfere for its support . . . hence a second class of securities which in a period of pressure, instead of being diminished, must be increased.'

through the approaching exhaustion of its reserves.[1] And since, on the line of argument laid down by Overstone himself, contraction involved 'pressure' and 'pressure' an increase in the accommodation demanded at the Bank, any mismanagement of its loan policy by the Bank increased the danger of such insolvency of the Banking Department.

There is something to be said for the view that just because the Bank Act of 1844 involved a division of the business of banking from the business of note issue, it ultimately enabled the problem of 'credit control' to be visualized more clearly than would otherwise have been the case: the Bank was prevented from managing the note issue at its discretion and yet the problem of controlling the credit situation remained. But the immediate effect of the Bank Act of 1844 was rather to accentuate these practical difficulties, by inclining the Bank Direction to regard the Bank as less peculiarly situated than was actually the case.

As for the intellectual difficulties involved, experience gradually showed that the 'contraction' upon which the Currency School rigidly laid stress could not be, and need not be, defined in the purely quantitative and rigid form employed in the controversies of 1840–4. The process of clarification began with the inquiry which followed the crisis of 1847,[2] and comprehends the whole course of theoretical discussion from that day to this. Two points are of especial importance. The first is the realization that an expansion of banking accommodation at the moment of panic represents a nominal rather than a real expansion of purchasing power, and that the power to expand often prevents the actual necessity for expansion at such times. The second point is less

[1] 'A most absurd, however disastrous a state of things. But it would be too disastrous and too absurd to be allowed to take its course. If such a crisis were to happen, . . . the Government would be imperatively called upon to interfere and prevent so ridiculous, however lamentable a catastrophe. And the only interference that could meet the emergency would be to authorize a temporary transfer of coin from the issuing to the banking department.' *Inquiry into the Currency Principle*, p. 110.

[2] *V.* Section III of the Report of the Secret Committee (House of Lords) on the Commercial Distress, 1848: 'The Act appears to assume that one fixed Amount of Notes out of the Custody of the Bank, and in the Hands of the Public, will at all Times produce the same Effect and will be governed by the same Laws. Unless this Proposition be true the uniform and fixed Rules of the Act of 1844 can hardly be justified. . . .'

amenable to summary statement. The Currency School, thinking out the problem of ' restriction ' and ' contraction ' in terms of what would have happened under a ' purely metallic circulation ', fell almost inevitably into the assumptions that restriction and contraction must involve a quantitative reduction of the volume of purchasing power below its initial level, and that such a reduction could only take place by an abstraction of purchasing power from out of the hands of the public.[1] It is an almost inevitable consequence, further, of this way of approaching the problem that the influence of the gold exports upon the price-level in the recipient countries should be neglected and that the degree of contraction necessary should therefore be exaggerated. The real terms of comparison, however, are not these at all, but are the volume of purchasing power which would have been in existence if the Central Bank had not pursued a restrictive policy and the volume actually in existence under restrictive conditions. ' Raising the Bank Rate ' is intended to prevent engagements from materializing which would have resulted in an increase of purchasing power. The test of whether restriction has been successful, therefore, is not the extent to which the volume of purchasing power falls below the pre-existing amount, but the degree to which expansive tendencies are held in check. In sum, whilst the Currency School realized the general nature of the problem to be solved, and of the general principles involved, the analysis by the School of means and technique to attain the end desired was in no sense final.

[1] Very soon after the passage of the Act, Lord Overstone was forced to substitute an abstraction of notes from the Banking Department of the Bank for a reduction of notes in circulation as the *measure* of successful contraction. ' By the Act of 1844 . . . a new source of useful information and admonition was opened to the public; they were taught to direct their attention to that portion of the circulation which consists of notes in the banking till; and the means of watching the fluctuation of this part of the circulation were provided. We are now reaping the fruits of this simple, but wise precaution. A continuous decrease of that portion of our circulation which is to be found in the Bank till has occurred; and this fact, not, as formerly, mystified and obscured by a vicious state of the law, but rendered clear and notorious to the whole public, *has produced all the effects of contracted issues*.' *Letters on the Bank Charter Act, &c.*, in *Tracts*, p. 330.

§ VI

For thirty years after its passage, the merits and demerits of the Bank Act of 1844 dominated the field of discussion, until towards the end of the 'seventies of last century the Bimetallic agitation took pride of place. It is this unsettled state of public opinion which lent to the ' crises ', or ' panics ', of 1847, 1857, and 1866 much of the importance which they have acquired in the literature of British banking. For the ' panics ' of those years were accompanied by, and led to, a ' suspension ' of the Bank Act, and it was inevitable that this should have called into question the wisdom of legislation which appeared to break down at the moment of greatest strain. Any rational treatment of the period requires, however, a preliminary recognition of the fact that these years marked the stage of transition from the upward to the downward phase of trade activity in the apparently endless but fairly definite rhythm of economic life. The trade cycle was not the product of the Bank Act of 1844: there had been panics before ever the Departments of the Bank were separated. The most that can be urged is that the hope of the Currency School that the amplitude of the Trade Cycle would be moderated and Panic prevented had not been realized, and that the Bank Act of 1844 was a factor *accentuating* both the amplitude of the Cycle and the extravagances of the Panic.

Encouraged by Sir Robert Peel to think that the business of the Banking Department ' should be governed on precisely the same principles as would any other Body dealing with Bank of England notes ',[1] and that ' the banking business, as distinguished from Issue, is a matter in respect to which there cannot be too unlimited and unrestricted competition ',[2] there was every reason, urged the critics of the Bank Act, for the Bank Directors to do as they actually did as soon as the Act came into force: namely, lower the Bank rate to a competitive level, and thus increase very

[1] *House of Commons Debates*, vol. lxxiv (series 3), 6 May 1844, col. 742.

[2] *Loc. cit.*, col. 743: ' The principle of competition, though unsafe in our opinion when applied to Issue, ought, we think, to govern the business of banking. After the issue of paper currency has once taken place, it is then important that the public should be enabled to obtain the use of that issue on as favourable terms as possible.'

considerably the holding of Bills of Exchange.[1] For any expansive influence which this may have had on the credit cycle,[2] the Act, and not the Directors, was to blame. That the Act added to the extravagances of the Panic was simply due to the fact that, so long as the money market did not know whether facilities for further borrowing would be available or not, every one would try to cover his needs whilst there was yet time, and then the reserve would be exhausted because people were afraid it would be exhausted. That the suspension of the Act mitigated the Panic of 1847 was admitted by the Governor of the Bank in cross-examination in 1848;[3] whilst in 1857, it is clear from the examination of the Governor and Deputy Governor, the fact that the crisis was less severe than it had been in 1847 was due, in their opinion, to the Bank lending freely in anticipation of the issue of a Treasury Letter, and to the public believing that such a letter would be issued.[4]

Logically, however, there is no necessary connexion between

[1] Tooke, *History of Prices*, iv, p. 294.

[2] If the operations of the Bank are summed up, it will be found that up to the period culminating in 1857, bank rate is both relatively low and relatively stable, whilst after that date down to the period ending in 1878, Bank rate tends to be both higher and much more unstable. Taking Palgrave's Tables (*Bank Rate and Money Market*, pp. 82, 97, 196) as basis, the average rate of discount and the number of changes in the Bank rate during the following ten-year periods were:

	Bank rate of discount.	*Number of changes in Bank rate.*	*Proportion of Reserve to Liabilities.*
1845–54	£3·46%	27	52%
1855–64	£4·64%	89	42%
1865–74	£3·80%	113	43%
1875–84	£3·19%	66	44%

Averages throw no light upon degrees of variation. In the period 1844–7 the variation in the reserve ratio was between 59% and 33%; in 1848–57, between 63% and 30%; in 1858–66, between 58% and 30%; and in 1867–78, between 52% and 37%. The average yearly ratios improve, the range of fluctuations declines: the changes indicate the changing tendency of Bank policy. And in this connexion it must not be overlooked that the earlier decades of the Bank Act coincide with the Australian and Californian gold discoveries, when the maintenance of a relatively high level of reserves was therefore easier.

[3] *V. infra*, QQ. 3155, 3171.

[4] *Select Committee on the Bank Acts*, P. P. 1857–8, v, especially QQ. 87, 92, 93, 99, 247, 569–73, &c.

the Separation of the Departments and the policy actually pursued by the Bank. It does not in the least follow, because the notes ought to be specially protected, that therefore the Banking Department should be free to pursue the same policy as any other bank. Nor does it follow from the fact that the Act of 1844 exaggerated the violence of panics, when they did occur, that therefore the Act was useless: if the Act did in general force a sounder policy on the Bank than it would otherwise have pursued, it might reduce the chances of panics occurring; and it is no answer to this contention to say that if the panic did occur, the Act became the reverse of useful. The difficulties of the Bank between 1847 and 1866 arose from the circumstance that only gradually was it realized that the Act of 1844 did not provide an automatic protection against unsound banking policy: in other words, that the Bank was not placed in the position of any other bank, merely because its control over the note issue was more restricted than it had been.

§ VII

Controversy was not confined, however, to the general principles of the Act, and by 1858 a whole series of detailed issues, involving the fundamentals of the modern theory of Central Banking, had quite clearly emerged. The fame of Bagehot has resulted in somewhat less than justice being done to Bagehot's predecessors, for the whole significance of Bagehot's great plea for the recognition of the special position of the Bank of England is lost unless it is put into its proper place in the chain of contemporary thought. Bagehot lent a pen of great genius to the view that was already in the ascendant, but which lacked wholehearted acceptance. He did not kindle a controversy, but extinguished one, and Thompson Hankey's querulous protest was already out of date at the time when *Lombard Street* was issued.[1]

Of these detailed issues six are of permanent importance.

(1) The ' relaxing power ', that is, the question of whether the

[1] Nor must it be overlooked that if Bagehot accepted the facts, he did so with misgiving. The ' natural ' system was one of decentralized, not of centralized reserves, and the one-reserve system would never have been evolved ' if Government had let banking alone '. A more question-begging statement by a man of genius can hardly be imagined.

machinery by which the Bank Act could be suspended should be regularized or not, had been discussed even before the Bank Act was passed. Thus even Overstone had agreed that the Bank of England must be given ' a discretionary power of suspending her obedience to principle ' *unless* a ' direct control . . . over the country issues ' were established.[1] Peel had written to W. Cotton, Governor in 1844, that though his ' Confidence is unshaken, that we are taking all the Precautions which Legislation can prudently take against the Recurrence of a pecuniary Crisis ', yet ' it may occur in spite of our Precautions; and if it does, and if it be necessary, to assume a grave Responsibility for the Purpose of meeting it, I dare say Men will be found willing to assume such a Responsibility '.[2] The matter had been discussed in the House of Commons by Wood, the Chairman of the 1840–1 Committees, who objected to any discretionary power being given to Government, on the ground that this would subject it to intolerable pressure.[3]

The matter naturally assumed still greater importance after the suspension of the Act in 1847: the important section of the Report of the House of Lords recommending such a discretionary power is printed below.[4] Overstone, though opposed to any general power of relaxation, admitted that the intervention of the Government in October 1847 was necessary, and that, though no discredit attached to the Act of 1844, ' circumstances may occur in mercantile affairs, and in the confidence on which mercantile affairs are based, of such a peculiar character that some interference may be desirable for the purpose of alleviating the intensity of pressure arising from the destruction of confidence '.[5] By 1857, as we have seen, the Bank was already assuming that such a letter would be issued, and the Committee of 1857–8, although approving of the absence of a general relaxing clause in the original Act, were in favour of amending the Act in this direction in future, though ' it scarcely . . . constitutes, of itself, a sufficient ground for bringing this important and difficult sub-

[1] *V. infra*, vol. 1, p. 52.
[2] *Lords Report of* 1848, Q. 3284; cf. *infra*, vol. ii, p. 38.
[3] *House of Commons Debates*, vol lxxiv (series 3), 20th May 1844, col. 1371.
[4] *Infra*, vol. ii, pp. 36–46.
[5] *Commons Committee*, 1848, Q. 5157.

ject under the review of Parliament, and may safely await the decision of the Legislature when the other branches of the subject shall again be dealt with '.[1] By 1857, opinion was, however, already moving forward to a tentative discussion of the possibility of combining a fluctuating fiduciary issue with a sliding scale of interest charges—the basis upon which modern Central Banking Constitutions are so largely built up.[2]

(2) The question of the Relaxing Power raised in an acute form the question of the Government of the Bank of England, for the expediency of vesting the Relaxing Power in the hands of Government or the Bank turned in part upon the fitness of the Bank Court to exercise such a grave responsibility. The same issue was involved in the discussion of the Discount Rate. Could a Court composed of merchants be expected to act with sufficient promptitude and in a sense, perhaps, opposed to their own immediate pecuniary interests? Doubt upon this point was one of the factors making, not only for the Separation of the Departments, but for a Government Note Issue. If the Court could not be expected, in view of its composition, to be really impartial, would it not be best to entrust the control of the note issue, on the lines suggested originally by Ricardo, to a separate body of Commissioners and leave the Court to manage the business of banking as it thought best? Deprived of the power of note issue, there would be less danger of a policy being pursued by the Bank which was antagonistic to the true interests of the nation.[3]

Some information had already been collected by the Committees of 1832 and 1840; and by 1848 dissatisfaction with the existing situation had gone far enough to warrant the Lords' Committee to express itself warmly on the subject[4]: the Commons' Committee, emphasizing the deep interest felt by the 'Public' and the 'Proprietors of Bank Stock' in 'every measure calculated

[1] *Report*, para. 72.

[2] *V. infra*, vol. ii, p. 52; also Mr. Gladstone's cross-examination of D.B. Chapman, 1857 Committee, QQ. 5000 *et seq.* The conception ultimately goes back to Tooke. *V. infra*, Newmarch's evidence.

[3] On the contemporary official point of view, *v.* the elaborate memorandum (written by G. Arbuthnot of the Treasury), presented to the 1857 Committee by Sir G. C. Lewis, P. P. 1857–8, v, pp. 414 *et seq.*: *Memorandum on the Question of establishing a National or State Bank.*

[4] *V. infra*, vol. ii, pp. 41 *et seq.*

to ensure an enlightened administration of the affairs of the Bank ', refer ' with satisfaction ' to recent changes announced by the Court ' as to the selection of the Governor and Deputy Governor, calculated, in the opinion of Your Committee, to improve the constitution of the governing body of the Bank '.[1] Opinion was still very divided on the issue of appointing a Permanent Governor, as it still was in Bagehot's time, and indeed still is; but in 1857 the Bank Court itself voted in favour of altering the law relating to the number of Directors retiring each year—a minor issue which was not finally settled until the Bank Act of 1892, which left the proportion to the Court itself.

(3) Before the passage of the Bank Act, the Discount Rate had mainly been discussed in relation to the Usury Laws. Up to 1844 the Bank rate had been practically a fixed rate of 4 per cent., though in the pressure of 1836–7 the rate had gone up to 5 per cent., and in the second half of 1839 had gone up to 6 per cent. The Bank held that it ought not to compete with the market; bills of exchange were not regarded as desirable objects of cover for the note issue in normal times, and the control over the total volume of interest-earning assets was to be accomplished by selling Government securities as the volume of bills presented rose, thus keeping the total of all securities steady.[2] After 1844 all this was to alter; and the problem of the discount rate and its relation to the market rate of discount became subjects of acute controversy. It is not going too far to say that the problems then raised have not yet received their definite answer.

There are in all inquiries relating to the discount rate two problems. The first is the effectiveness of the discount rate as a *means of control*; the second is the degree of discretion which the nature of the economic system allows to the system of interest rates *as a whole*. The latter question is one involving the relation of the money rate of interest to the real rate of interest on capital, and has nothing to do with the issue, also largely discussed after 1844, whether the Bank rate should be above or below the market

[1] Commons' Report, 1848, p. v. The change consisted in the abolition of the rule of strict seniority. *Evidence*, QQ. 2697–8 (and *Lords' Report*, *infra*, p. 190).

[2] *V.* evidence of Governor and Deputy Governor before the Commons' Committee of 1848, *infra*, vol. ii, pp. 13 *et seq.*

rate in normal times. The state of opinion at the Bank of England in the middle of the nineteenth century with regard to the efficacy of the Bank rate, compared with other possible devices, as a means of control over the Reserve, is very clearly depicted in the evidence before the Select Committee of 1857–8 reprinted below.[1] By 1857, the Usury Laws had been completely swept away, the Act of 17 & 18 Vict. c. 90 abolishing all the restrictions still remaining; and no obstacle stood in the way of any rise in the Bank rate considered necessary. Ten per cent. had been charged during the crisis of 1857.[2]

A Central Bank which desires to stabilize its discount rate will find its discounts falling off sharply at periods when the market rate is falling fast below its own fixed level, and rising sharply when the market rate is rising above the fixed level. A fixed rate of discount at the Central Bank is, therefore, accompanied by considerable variations in the volume of bills held by it. A Central Bank which desires to stabilize the volume of its bills can do so by keeping its rate near the market rate when the latter is rising, and lowering it *less* rapidly than the market rate when the latter is falling. A Central Bank which desires to stabilize its reserve must sometimes raise its rate faster, and sometimes lower it faster, than the market rate. The difficulty in pursuing any one of these ends is that the change in Central Bank rates may (and probably will) affect the market rate; so that in periods of falling rates a reduction in the Central Bank rate will cause market rates to fall still more (because the Bank has not to pay interest on deposits and the market largely pays interest), and a rise in Bank rate forces more than proportionate rises in market rate upon the outside market.

In practice, of course, no Central Bank can afford to follow any *one* of these aims exclusively. It must pay some regard to the susceptibility of the outside market, which resents continual changes in the Bank rate; it must have some regard to its own earning capacity, which exercises some, if only a subordinate, influence (as the Bank has the alternative of holding fixed interest-bearing securities) upon its policy; it must necessarily, and in all

[1] *V. infra*, vol. ii, pp. 50 *et seq.*
[2] *V. infra*, vol. ii, pp. 46 *et seq.*

cases, pay great attention to the reserve position. The significance of the discussion between 1844 and 1858 lies in the fact that each of the various groups tended to stress *one* of these ideas: the Banking School the stability of the discount rate,[1] the representatives of the Bank, at first, the right of the Bank to regard earning capacity,[2] and only later the necessity to regard the status of the Reserve; the Currency School, paradoxically enough, in view of the previous line of argument, to stress the importance of the discount rate as a means of control.[3]

(4) The position of the Bank as an ultimate reservoir of credit led to one development of great interest: the attempt to force the bill brokers into a position of greater independence in normal times. In 1857–8 a great deal of attention was devoted to the position of the bill brokers, who had by that time long ceased to be merely intermediaries earning a commission and had become dealers in bills, borrowing at call and investing the proceeds in bills. In view of the fact that banks were still largely local in character, the function of the bill broker was almost indispensable, since he linked up banks with surplus deposits and banks with less deposits than they could use. To some extent the broker competed with the banker by taking bills direct,[4] and the bill-broking system was not free from defects. It encouraged banks to discount bills too freely, and was thus in part responsible for that abuse of bill-credit which was a marked feature of the banking world;[5] and since the dealer paid interest on all money at call, he held no reserve of cash, relying on the Bank of England to

[1] *V. infra*, vol. ii, pp. 60 *et seq.*; and vol. ii, pp. 66 *et seq.*

[2] Cf. *infra*, vol. ii, p. 32, Q. 3008: 'When the rate of interest out of doors was $1\frac{1}{2}$ to $1\frac{3}{4}$ per cent. to 2 per cent., *if the Bank pretended to act as discounters* it was absurd to attempt to keep their rate of discount at 4 per cent.' (*Commons Committee*, 1848). Cf. QQ. 2654, 2845, 2883.

[3] *V.* James Wilson's amusing comments on Lord Overstone's epistles to *The Times* (under the pseudonym of *Mercator*: *Tracts, &c.*, pp. 309–[373], so paged in original), in a letter to Sir G. C. Lewis: 'how charmingly he persists in a high rate of interest as the only security, which is just what he never dreamt of before when the fluctuation in the circulation of notes was to do everything, and when those opposed to the mere currency theory insisted that it was the rate of interest only that could regulate the money market.' *V.* Mrs. E. I. Barrington's *The Servant of All*, 1927, vol. ii, p. 21.

[4] *V. infra*, vol. ii, p. 79.

[5] P. P. 1857–8, v, QQ. 4217, 1962–1996.

save him if his money were called. Early in 1858 the Bank decided to refuse discount accounts to the brokers and ' to make the transactions of the Bank confined entirely to advances. These advances will be the usual quarterly advances, and if they apply for advances at any other time, they will be considered special and dealt with accordingly '.[1]

Cross-examination speedily revealed that it would be impossible for the Bank to refuse accommodation at ' moments of extreme difficulty ', but the step was undertaken primarily to free the Bank in more normal times, and it was at first approved of by the financial press. ' As the bill brokers are the rivals of the Bank,' argued the *Economist*, ' they cannot reasonably expect that the Bank should act towards them with special and peculiar favour . . . there is no reason why an eminent bill broker should depend on the Bank of England any more than the London Joint Stock Bank or the London and Westminster Bank.' Since the Bank keeps the ultimate reserve, ' so far, therefore, from its being its duty to make advances which other banks would not think it wise to make under similar circumstances, its duty is of an opposite kind—is a duty of caution and prudence '.[2] By 1860, however, the paper was changing its tone: the action of the Bank was making the status of the broker less eligible than it had been, and a compromise was suggested. ' Why should not the bill brokers become regular customers of the Bank? The bill brokers, it is evident, must now keep some reserve: unless they do so, now that they have no access to the Discount Office of the Bank, their position is not safe for a day. . . . But why should they not keep it at the Bank of England? If the bill brokers habitually kept a large balance to their credit at the Bank of England, they would be good customers of the Bank, and would have a right to be treated as other good customers are.'[3]

So long as the Bank kept its rate low enough to be certain at all times of obtaining some of the floating supply of bills, it could afford to cut off the bill brokers from facilities at the Bank in normal times. The market rate tended to be somewhat higher

[1] *V. infra*, vol. ii, pp. 76 *et seq.*
[2] *Economist*, 1858, p. 305.
[3] *Economist*, 7th April 1860.

than Bank rate in the years 1865 to 1871 (though the trend was a falling one), but after 1872 there was an equally marked tendency in the other direction.[1] In 1878, as part of its policy of no longer feeling bound to adhere to its published minimum when discounting for its own customers, the Bank reverted to the practice obtaining before 1858,[2] but, while giving advances, refused to discount for brokers. In 1883, however, it again reversed its rules, and intimated to the brokers that it proposed to restrict advances: again with the approval of the *Economist*.[3]

After 1886 it will be found that the margin between Bank rate and open-market rate tended to be nearly twice as large as it had been in the earlier years of the decade; the inevitable consequences were that the Bank lost discounts and that the financial press should be insistent upon the desirability of the Bank intervening to control market rate and increasing its volume of bills, a demand which continued after the Baring Crisis.[4] In the second half of 1890 the Bank again altered its policy, and admitted the bill brokers to *discount* facilities, at first on short bills and subsequently on longer-dated paper.[5]

(5) Closely connected with the question of call money to the

[1] *V.* Table 4 in Palgrave, *op. cit.*, p. 33.

[2] Palgrave, *op. cit.*, p. 51.

[3] 'What has been spoken of as a new departure, but which is really only a return to former practice, has been made by the Bank Directors this week. They have given the bill brokers to understand . . . that in future their facilities for obtaining advances may be somewhat curtailed. While the Bank will . . . be ready as before to lend during the period at the close of each quarter . . . it may at other times, it has been intimated, leave the brokers to rely more upon their own, or at least, upon outside resources than they have done. And in this it certainly is acting rightly . . . there can be no doubt that of late brokers have come to rely far too much upon the Bank. They have reckoned upon getting advances there almost as a matter of course whenever they have applied for them, and in this belief they have entered into engagements which if they had not thought the Bank was behind them they possibly would not have risked. The belief, too, that the resources of the Bank would always be available at ordinary rates if necessary has enabled the brokers to borrow more freely than they would otherwise have been able to do, because the outside lender had, or thought he had, the assurance that if he called in his money the broker would be able to fall back upon the Bank.' (1883, p. 485.)

[4] *Statist*, 29th November 1890, p. 613: 'It is very desirable that the Bank should discount bills much more largely and much more freely than it does at present.'

[5] Palgrave, *op. cit.*, pp. 51–2.

bill brokers is the question of the rate of interest paid upon deposits. The tendency of opponents of the Joint Stock Banks before the 1857 Committee was to argue that they were tempted into dangerous courses by the high rate they paid upon deposits. From the evidence given by two leading Joint Stock Bankers in London,[1] it is clear that the general rule was to pay 1 per cent. under Bank rate, but that the more cautious bankers tried to prevent the rate from rising indefinitely as Bank rate rose, though it was impossible to get united action upon the point. In the seventies the problem was much canvassed; and for a time, in November 1877, the banks and brokers emancipated themselves from the rule, but failed early in 1878 to get a meeting at the Clearing House to agree upon a continuous policy. The danger was that, after the change in the Bank's practice in 1878, Bank rate was no longer a safe guide to the amount that banks could safely pay upon deposits, but the difficulty had already been recognized before that change took place. Arthur Ellis, writing in 1876, was already pointing out that ' the custom worked well enough while the Bank of England was the supreme power in the money market, when its rate of discount was the real gauge of the value of money, and when any one lending money at a rate differing much from it would be instantly suspected of doing unsound business; but times have changed, and the Bank rate no longer gauges the value of money with precision, and the Bank itself is a minority, no doubt a very respectable one, but only a part of the forces determining the value of money. . . . The Bank rate in fact has ceased to be a proper guide to the rate of interest which the banks may allow for the deposits left with them, for the anomaly sometimes occurs that the rate so allowed by the banks has exceeded the rate which they can *with safety* obtain for the money entrusted to them.'[2] The altered situation in the eighties led to a change of tone on the part of the financial press: the banks were now accused of paying too low a rate of

[1] *Infra*, vol. ii, pp. 86 *et seq.*

[2] *Rationale of Market Fluctuations*, p. 39. Cf. *Economist*, 9th February 1878, p. 150; and ' *Economist* ' *Commercial History* for 1878, p. 39. If these and other articles are compared with Palgrave's *Bank Rate and Money Market* on these subjects, it will appear clear that they were written by Palgrave.

interest upon their deposits and thus of helping to keep market rate too much below Bank rate.[1] During the Great War, having for many years paid $1\frac{1}{2}$ per cent. below Bank rate on deposits subject to seven days' notice, the banks resorted to a margin of 2 per cent., which they still maintain.

(6) After 1844 the growing importance of the Bank rate as a means of control thrust discussion of alternative methods into the background. This seems to be the explanation of why nothing more is heard of the proposal put forward by Gilbart that the Bank should hold foreign securities and foreign bills: should contract the circulation when it sold the foreign holdings and build them up again by increasing its circulation.[2] This is, of course, the 'Gold Exchange Standard', and it is interesting to notice that even Lord Overstone thought that 'the plan is certainly unobjectionable upon principle'; but he also thought that it had the disadvantage that the Central Bank would be so great a factor in the exchange market as to upset the 'ordinary action of the exchange dealers and to prevent their taking that course which, under ordinary circumstances, they would take'.[3]

§ VIII

Only twice since 1857–8 has the curtain which veils the operations of the Bank of England from vulgar scrutiny been even partially lifted. In 1875, when the opening of London offices by the Scottish banks outraged the feelings of English bankers, a Bill introduced by Mr. Goschen led to the appointment of a Select Committee on 17th March 1875 'to consider and report upon the restrictions imposed and privileges conferred by Law on Bankers authorized to make and issue Notes in England, Scotland, and Ireland respectively'. The evidence taken before that Committee very largely turned upon the 'monopoly' possessed by Scottish banks in Scotland owing to the right to issue £1 notes, and on the unfairness, therefore, of allowing 'subsidized' competition with English bankers hampered by the provisions of the Act of 1844. A good deal of evidence was presented showing the value of small local circulations, though the statistical evidence

[1] *V. Statist*, July–December 1889, pp. 350, 379, &c.
[2] *V. infra*, vol. i, pp. 97 *et seq.*
[3] *V. infra*, vol. i, p. 48.

also showed clearly the tendency for the note to lose in importance[1] and for the Bank of England circulation to take the place of local issues. Among the witnesses was Walter Bagehot, in his capacity of Director of Stuckey's Bank, and his very characteristic evidence is printed below.[2]

The two representatives of the Bank of England who gave evidence—Kirkman Hodgson and the Deputy Governor, E. H. Palmer—were still, on the whole, partisans of the characteristic ideas of 1844: Unification of Issues and the Separation of Departments. In the public interest, they thought it desirable that the Scottish and Irish issues, as well as the remaining English country issues, should be taken over by the Government or the Bank ('That is a matter of arrangement which the Government of the day would determine'[3]), but they were absolutely against £1 notes in England ('Anything more inexpedient or unnecessary than to reissue £1 notes in England I cannot well imagine')[4]; the risk of forgery and the cost would be very great, and an increase in the issue of fiduciary notes would 'impair the convertibility of the note'[5]—an amazing argument based on the view that if more fiduciary notes were issued 'it would reduce your stock of gold in the country'![6] The view that the Bank of England was the *de facto* holder of the entire reserve of the country was not accepted without scruples as regards Scotland; the Scottish banks had not the same moral claims 'as banks in other portions of the Empire', for, 'as regards banking, the Bill of 1845, which gave you great privileges, made you a foreign country'.[7]

[1] There is, however, a tendency among writers on banking to overlook the fact that if, on the one hand, the cheque took the place of the note after 1844 (and as a consequence of the Act of 1844), the Act, of course, also encouraged a large gold circulation.

[2] *V. infra*, vol. ii, pp. 266 *et seq.*

[3] Q. 7444.

[4] Q. 7489.

[5] Q. 7594.

[6] Q. 7596.

[7] Q. 7954. The next question and answer shows how hopelessly 'academic' this dispute was:

'Supposing that we have securities in England which we dispose of, and come to you in a legitimate way to get gold for them?—The only legitimate way in which you can come to us in a crisis is with bank notes in your hand, and then we will give you as much gold as you have in bank notes; but in this case you could not dispose of those securities and you came to the Bank of England, especially in 1857, and you brought masses of bills to discount. Those bills were discounted, the notes were taken out of our till, you went to our issue department, you cancelled

The possibility of introducing the £1 note was relatively soon, however, to spring into great prominence. The Baring Crisis of 1890[1] resembles the crisis of 1866 in this respect, that it originated, not in mismanagement of affairs by the Bank of England or by the short-loan market, but in the lock-up of funds by merchant bankers. The house of Overend, Gurney & Co., by the time of their failure, had ceased to be purely a bill-broking house and had branched out into ventures which had brought it great losses. The panic of 1866 arose from the fact that the firm owed enormous sums to the money market at call, and therefore its failure imperilled the whole banking system. The position of the Barings was very similar: 'they were not satisfied with the safe and magnificent profits which their splendid merchant banking business yielded', and they became illiquid because they were unable to dispose to the public of the mass of South American securities which they were carrying. The danger to the banking system came from the fact that they were the leading accepting house of the day, and any failure to meet their acceptances would have struck a vital blow at the whole money market. The two epochs differed because the failure of Overend's led to a panic and the failure of the Barings did not: the liabilities of the Barings were guaranteed by a syndicate headed by the Bank of England, and their affairs were successfully liquidated, without a suspension of the Bank Act and without any inordinate rise in Bank rate.

The Baring crisis raised two series of questions. The Bank was criticized,[2] on the one hand, for putting itself into a position in which it assumed obligations on behalf of a single firm so great that if the crisis had not been immediately overcome it would have been impossible for the Bank further to assist the market; on the other hand, it was something of a puzzle to the men of the time that there was no full-blown panic. These were the immediate reactions to the crisis. The ultimate ones were con-

the notes, and you took our sovereigns away to Scotland, and we were compelled to suspend the Act of 1844. We could have refused you, but supposing we had refused you!'

[1] *V. infra*, vol. ii, p. 187.

[2] At one moment the Bank had advanced as much as £7½ millions to the Barings; *v.* the Governor of the Bank, reported in *Economist Banking Number*, 1891, p. 8.

cerned with the whole drift of the money market situation, and particularly with the Reserve question. This in itself comprehended two aspects: the Reserve of the Bank, and that of the outside market, kept for the greater part in the shape of Other Deposits at the Bank of England. Both were inadequate, but the inadequacy of the Reserve of the Bank was illustrated by the fact that (through the good offices of the Rothschilds) the Bank of England borrowed £3,000,000 from the Bank of France, whilst £1,500,000 was obtained from Russia by the sale of Treasury Bills.

Goschen attempted to solve these problems by falling back upon the issue of £1 notes and the creation in connexion therewith of a ' second Reserve '. After the Issue department held a certain amount of gold, the £1 note might be issued on a fiduciary basis in the proportion of £4 against gold and £1 against securities; and the whole scheme culminated in a proposal to regularize the use of the gold in the Issue department for the purposes of the Banking department, that is, to sanction the possibility of an increase in the fiduciary issue without the necessity of a 'Treasury Letter'.[1] These proposals failed to mature; and, until the outbreak of the European War, the Bank Act remained what it had always been. Thereafter, indeed, the situation was to undergo great changes.

If, in spite of an almost continuous undercurrent of agitation and discussion upon the inadequacy of the gold reserves of the country and of the dangers incurred in "spinning a top on a needlepoint", nothing was done,[2] the reason lies in the fact that by the end of the nineteenth century the conditions of banking had

[1] For the evolution of Goschen's theory, *v.* his *Essays and Addresses on Economic Questions*, pp. 102–30. Cf. H. S. Foxwell, ' Mr. Goschen's Currency Proposals ', in *Economic Journal*, vol. ii, pp. 139 *et seq.*

[2] *V.* Prof. H. S. Foxwell's summary in his Introduction to G. H. Pownall's *English Banking*, p. xiii: ' The appeals made in the last twenty years by such men as our author, the late Viscount Goschen, Sir Inglis Palgrave, Sir Felix Schuster, Sir Edward Holden, the late Mr. Spencer Phillips, Mr. Crammond, and others had been made in vain. Received in some quarters with cynical indifference, they never obtained more than a lukewarm, platonic assent. So far as published figures go, no appreciable result is traceable. Other nations, on the average, roughly doubled their reserves; we were content to talk about it.'

largely changed. The private note issues had almost disappeared, and the chances of an internal panic were declining, partly because the technique of banking generally had greatly improved, mainly because the banks were individually growing in size and were therefore likely to be better administered. On the other hand, the Bank of England had learnt the art of adapting its reserve policy to the exigencies of the Bank Act, not by the accumulation of vast reserves, but by a manipulation of its securities[1] so as to make Bank rate effective. The various elements in the money market were in close touch; and, above all, the problem was eased by the growing sensitiveness of the International Money Market to movements in the British Rate.[2] The American crisis of 1907 and the crisis which accompanied the outbreak of war in 1914 both illustrated the enormous strength of the credit position of London. The policy of economy in gold reserves was based upon an instinctive recognition of the principle that it is not the absolute size of the reserve, so much as the power to keep the reserve actually possessed at the normal level considered desirable, which is the true test of the capacity of a Central Bank to control the situation. It does not in the least follow that the *actual* reserve held was arrived at as the result of scientific reflection: there is, indeed, every reason to suppose the contrary. It may have been true, therefore, that with a larger reserve the normal level of the discount rate might have been somewhat lower and that some fluctuations in that rate might have been avoided. To that extent the critics of the pre-war situation were no doubt justified. On the other hand, so long as London remained the financial centre of the world, the stability of the London rate was bound to be less than that, say, of the French rate, because France was not a free market for gold.

[1] As early as 1849 the Bank borrowed on Consols to strengthen the reserve; *v. infra*, p. 163. In December 1905, if the late Mr. J. Spencer Phillips's account to Lloyd's Bank shareholders is correct, the Bank asked the co-operation of the Clearing Banks 'to take the surplus money off the market and place it on deposit with the Bank at a low rate of interest. The Bank then charged 5 per cent. on their advances, and the effect was electrical. . . . This precedent has been followed again during the present month (January 1906) by the Bank.' Cited, E. T. Powell, *Evolution of the Money Market*, p. 650.

[2] *V. infra*, vol. ii, p. 191.

We owe to the initiative of the National Monetary Commission of the United States, appointed as a direct result of the crisis of 1907, the only glimpse into the mind of the Bank of England which has been vouchsafed to the world since 1875.[1] After 1877, certain statistical information, formerly made available, no longer appeared.[2]

§ IX

On 12th May 1836, Mr. William Clay moved in the House of Commons[3] that ' a Select Committee be appointed to inquire into the operation of the Act of the 7th Geo. 4, cap. 46, permitting the establishment of Joint Stock Banks, and whether it be expedient to make any and what alterations in the provisions of that Act '. The grounds for the motion cannot be better put than they were by the speaker himself. Under the Act of 1826, he said, ' a system of Joint Stock Banking has grown up already of great magnitude, which is daily extending its ramifications, and which promises very shortly to comprehend every portion of the Kingdom, and every class of the population within the sphere of its operation '; and this growing movement suffered from a lack of due legal regulation: ' I cannot but think that the circumstances I have now stated to the House—the vast and growing system of Joint Stock Banking on the one hand, the absence of all legal control over the working of that system on the other—constitute a state of affairs very far from satisfactory, and especially if looked at in combination with certain others, or at least, without considerable anxiety. We have called into existence, we have introduced into our monetary system, an element of tremendous power. We have taken no precaution to limit or control its operations.'

These statements are the more remarkable if it is borne in mind how relatively little developed the Joint Stock Banking movement still was. *An Account of the Number of Private and Joint Stock Banks registered in each Year, from* 1820 *to* 1842

[1] *V. infra*, vol. ii, pp. 307 *et seq.*
[2] H. W. Macrosty, ' Submerged Information—Banking ', in *Journal of the Royal Statistical Society*, 1927, pp. 365 *et seq.* Cf. Palgrave, *op. cit.* chap. I.
[3] *House of Commons Debates*, 3rd Series, vol. xxxiii, col. 840 *et seq.*

inclusive[1] (which does not, however, appear to include the London Joint Stock Banks which did not benefit from the Act of 1826) shows that between 1826–7 and 1835–6 the number of registered joint-stock banks had risen from six to fifty-five. During the same period the number of private banks registered had fallen from 465 to 407, the great mortality having taken place in the crisis year 1826, for the number registered previously had risen from 521 in 1820–1 to 554 in 1825–6. The tendency is, however, unmistakable; and in 1836–7 the number of registered joint-stock banks had jumped to 100, the number of private banks had fallen to 351. By 1841–2 the numbers were respectively 118 and 311. The movement towards 'banking amalgamation' had already begun; and so had the necessary concomitant—branch-banking. According to Clay's statement, in March 1836 the 61 joint-stock banks then registered were established at 472 places and had 15,670 'partners', that is, shareholders. Between 1836 and 1862 the question of Joint Stock Banking—in particular the issue of whether or not these banks were to enjoy the benefits of limited liability—was to rank second only to the problem of the Note Issue.

The Act of 1826 applied only to banks outside the sixty-five-mile radius, and the new banks were forbidden both to have an office within that area and to draw demand bills for any sum or bills under £50 for any date, on their London agents. All the shareholders were liable for all the debts of the company; all proceedings were to be taken against, and in the name of, two or more partners, who were to be public officers, but any judgments obtained against such officers were valid against all the partners. The only difference made to the status of these corporations by the Bank Act of 1833 was that they were henceforth free to draw bills on London on demand and for sums of less than £50. The real substantive change was that after 1833 a series of banks—which were legally nothing but common law partnerships, though known as 'joint-stock banks', since they had many partners—opened for business in London, in consequence of the failure of the Bank of England to enforce the view that *any* banking partnership with more than six partners, and not merely

[1] P. P. 1843, vol. lii.

a banking partnership with more than six partners *and issuing notes*, was an infringement of its monopoly.[1] Between 1824 and 1840 five banks—the London and Westminster, the London Joint Stock Bank, the Union Bank, the London and County, and the Commercial Bank—set up in business, unprotected by the meagre clauses of the Act of 1826 and faced by the fierce opposition of the Bank of England and the Clearing Bankers.

The evidence given before the Bank Charter Committee on the subject of joint-stock banking was, as might have been expected, mainly of an unfavourable character, though in some cases the opposition was primarily based upon the undesirability of erecting new banks *of issue* within the sixty-five-mile radius. Jeremiah Harman of the Bank of England led the attack: S. J. Loyd thought that ' Joint Stock Banks are deficient in every thing requisite for the banking business except extended responsibility; the banking business requires peculiarly persons attentive to all its details, constantly, daily and hourly watchful of every transaction, much more than mercantile or trading business. It also requires immediate, prompt decisions upon circumstances when they arise, in many cases a decision that does not admit of delay for consultation; it also requires a discretion to be exercised with reference to the special circumstances of each case. Joint Stock Banks being of course obliged to act through agents and not by a principal, and therefore under the restraint of general rules, cannot be guided by so nice a reference to degrees of difference in the character or responsibility of parties; nor can they undertake to regulate the assistance to be granted to concerns under temporary embarrassment by so accurate a reference to the circumstances, favourable or unfavourable, of each case.'[2] Still, he thought their competition would ' diminish the number of private bankers considerably ' and leave the private banking business in

[1] The discovery that a common law partnership of more than six persons engaged in banking without issuing notes was not an infringement of the Bank of England's monopoly was due to Thomas Joplin (1797–1847) of the Provincial Bank of Ireland and the National and Provincial Bank of England; *v.* his *Essay on Banking*, 1822, p. 42. Joplin's view was upheld by the law officers of the Crown; and, as already mentioned above (p. xlii), a declaratory statement was inserted in the Bank Act of 1833.

[2] Q. 3306.

weaker hands: ' those who carry on their business from an attachment to old concerns, and feelings of that description, and who, from their circumstances, are independent of the profits of business ' would be inclined to give up.[1] Samuel Gurney, Thomas Attwood, and Henry Burgess all united in attacking the new banks—the latter, of course, as official spokesman for the country bankers, thinking them ' injurious in every respect '. Only Vincent Stuckey took up a philosophical attitude: he was in favour of limited liability and thought that ' chartered banks, with a paid-up capital, and limited responsibility of partners, would, in the course of years, bring us to a sound system of banking '.

The Government's abortive plans of 1833, so far as they concerned joint-stock banks, were based on the principle of establishing ' Chartered Banks ' both inside and outside the sixty-five-mile radius; banks which desired to issue notes *outside* the sixty-five-mile radius to have paid up one-half of their capital and to be deprived of the privilege of limited liability; non-issuing banks, within and without the sixty-five-mile radius, were to enjoy the privilege of limited liability and needed to have paid up only one-quarter of their capital; though the Government was to have the right to determine whether the amount of subscribed capital were sufficient, in view of the place where the bank was to be situated. The opposition of the country bankers having killed these proposals, the reform of joint-stock banking was left to await the Reports of the Secret Committee on Joint Stock Banks, which was, in spite of the almost universal opposition to his views expressed by subsequent speakers in the debate, set up as a consequence of Clay's motion of 1836. The Committee was reappointed in 1837 and in 1838, and nothing very positive resulted beyond the collection of a vast mass of evidence. Yet the First Report[2] is interesting for the clearness with which it states the view that ' a principle of competition exists which leads to the extinction of all Private Banks, and to their conversion into Banking Companies ', and for the clear exposition of the gaps in the then existing legislation.

Between the issue of the various Reports of this Committee

[1] Q. 3269. [2] *V. infra*, vol. ii, pp. 219 *et seq.*

and the passage of the Joint Stock Banking Act of 1844, some minor changes were effected in the state of the law; on the recommendation of the Committee itself legislation was passed in 1838 [1] by which a company might sue, or be sued by, any of its members, thus overturning the common law position that 'if the same individual was a member of two partnerships, they could not go to law against each other'[2]; and the position of companies with members of the clergy as partners was also regularized.[3] The Bank Act of 1844 (Section XXVI) allowed banking companies within the sixty-five-mile radius to 'draw or endorse Bills of Exchange, not being payable to Bearer on Demand', thus ending a long conflict between the Bank of England and the Westminster and other London banks. But the Act[4] 7 & 8 Vict. c. 113 was the first serious attempt to regulate the whole organization of joint-stock banks: providing in essence that no future banking company could operate without Letters Patent granted after petition heard by the Committee of the Privy Council for Trade and Plantations. No company was to have less than £100,000 of capital; no advances were to be made on the security of its own shares; the assets and liabilities were to be published at least once a month; the accounts were to be audited annually by two auditors chosen by the shareholders and not directors of the company; no share was to be of less value than £100; and the company was not to commence business until all the shares had been taken up and half the value of each share had been paid up. The shareholder remained liable to the full for the debts of the company.

The Act *directly* applied only to new companies, but by Section XLV of the Act pre-existing companies might elect to be incorporated under the Act, on condition of conforming to its stipulations. Since the terms of the new Act were much more stringent than those of previous legislation, this was an offer not likely to be taken advantage of to any great extent; but the Act *also*, by Section XLVIII, assimilated the position of banking companies within the sixty-five-mile radius to those governed by the Act of

[1] 1 & 2 Vict. c. 96, continued by 3 & 4 Vict. c. 111.
[2] *Macleod on Banking*, ii, p. 331.
[3] *Op. cit.*, p. 332. The Act was 4 & 5 Vict. c. 14.
[4] *V. infra*, vol. ii, p. 229.

1826, so far as suing and being sued in the name of a public officer of such 'co-partnership' was concerned. There were henceforward four classes of banking companies: (1) those under the Act of 1826, (2) those under the Act of 1844, (3) those under neither of the Acts, and (4) those which were re-chartered under Section XLV of the Act.

Although, of course, the majority of banking companies did not come under the Act, it was unfortunate for the advocates of legislative control that one of the worst banking scandals of the 1857 crisis, the Royal British Bank,[1] concerned a bank which was so registered. The advocates of limited liability had never been contented with the situation, and the less so since the principle of limited liability had been conceded to companies generally in 1856. The advocates of amendments to the legislation of 1844 were met by the criticism that the events of 1857 had shown clearly that it was not by paragraphs in Acts of Parliament but by sound banking principles that the safety of banks was achieved. This was the keynote of the leading articles of the *Economist* in 1857, when amending legislation was introduced. 'The ingenuity of the law officers of the Crown; experience as elicited by the Banking Committees of both Houses of Parliament; the administrative and constructive ability of Sir Robert Peel—seem all to have been exhausted in the framing of this Act. Yet, alas for legislative contrivance in matters of trade, its chief, almost its only fruit (except the crop of banks established during the last two years), was the Royal British Bank.'[2] The Act of 1857[3] swept away the Act of 1844 altogether; provided that companies coming under the former Act were to register under the new one; and incorporated the provisions of the Companies Acts, 1856,

[1] *V. Banker's Magazine*, 1857, pp. 374, 669, 733; for other cases arising in connexion, pp. 599, 603, 728.

[2] *Economist*, 1857, p. 59. The question of auditors particularly aroused its scorn: 'There is one pretended precaution which above all others has been a fruitful source of deception, and which we trust in any bill that may be brought before Parliament in reference to Joint Stock Banks will be carefully eschewed: we allude to the appointment of auditors. We have often endeavoured to show that particularly in the case of banks, the duties of such officers are a mere mockery and delusion.' (1857, p. 502.)

[3] *V. infra*, vol. ii, p. 251. For the motive leading to change, *v.* Lowe's speech, *House of Commons Debates*, vol. cxlvi (series 3), cols. 194 *et seq.*

1857, with its own, with the very important exception, however, that banking companies could not benefit from the privilege of limited liability. Banking companies not, *ipso facto*, coming within the terms of the Act might register thereunder with the assent of a majority of their shareholders (Section VI).

The question of limited liability still remained to be solved. In the motions and debates which the question evoked,[1] the line of argument pursued differed very little from that laid down twenty years before by Mr. Clay: on the one hand, the supporters of limited liability laying stress on the deterrent effect which a provision such as unlimited liability must have on desirable parties becoming shareholders, on the encouragement to rediscounting on the strength of the unlimited liability of shareholders,[2] and on the painful results when an unlimited bank did fail. The main card in the hands of the opposition was that it was impossible to apply a limitation of liability to the note issues of a bank, since, in fact, the note-holder was often not free to choose whether or not he would take a note, whereas the depositor could change his bank if he liked. The technical financial press was somewhat divided in tone: the *Banker's Magazine* was, on the whole, doubtful of the experiment.

'To combine perfect security to the public with the principle of limited liability to the shareholders in banking, may be impossible, but where the liability is the widest, there as a rule, the public will—all things else being equal—be certain to give the preference. Although, therefore, the class of joint stock money dealing houses which, under Mr. Headlam's bill, should it pass into a law, will be sure to spring up in vast numbers, may in some exceptional cases supply a want, and tend still further to develop the banking capabilities of the country, the chances are adverse to their attaining to any large measure of success, either in the amount of business or the extent of profit. That the experiment should be made seems desirable especially if it can be done without any great risk, inasmuch as it will settle a question about which some of the highest authorities in monetary circles entertain the most directly opposite

[1] *V*. discussion on Headlam's Bill, *House of Commons Debates*, vol. cxlviii (series 3), cols. 1169 *et seq.*; vol. cl (series 3), cols. 534 *et seq.*

[2] The *Economist* supported limited liability on the ground that thereby 'the credit of a bank would be determined by its capital and its known management alone. Bills, if offered for rediscount, would be examined and dealt with upon their individual and respective merits.' (1858, p. 531.)

opinions. But that any joint stock bank which, under the existing law, is enjoying a safe and profitable business, will desire to exchange their unlimited for a limited liability, looking at the price they may have to pay for the doubtful advantage, is more than improbable.' [1]

For another twenty years the contention of the paper was to prove right; in spite of the permissive powers contained in the Act of 1858,[2] till 1879 a large part of the banking of the country was still carried on on the basis of unlimited liability.[3] Meanwhile the Companies Act of 1862 reduced the then existing statute law to something approaching coherency.[4]

Unlimited liability in joint-stock banking was eventually killed by the failure of the City of Glasgow Bank in 1878. The enormous liability of the Bank on acceptances which were rediscounted in the London market reinforced the objections voiced at the beginning of 1875 by practical bankers themselves against this form of credit extension,[5] though, of course, in the case of the City of Glasgow Bank the bills so accepted were mere accommodation paper. The *causes* which led to the failure of the Glasgow Bank and the methods by which the Directors tried to put off the evil day can be paralleled from the records of bank failures in both the 1847 and 1857 crises; what produced a change was the magnitude of the losses which had to be borne by the unfortunate shareholders, liable to make good all the liabilities of the Bank, which involved their meeting a first call of £500 for every £100 of stock held, and a second call of £2,250 per £100 of stock. The total holding of stock in the hands of the public was £840,000;

[1] *Banker's Magazine*, 1858, p. 213. One of the reasons for favouring a change was that the new Discount Companies did the same work as banks and *were* allowed limited liability; *op. cit.*, p. 210.

[2] *V. infra*, vol. ii, p. 257.

[3] A Parliamentary Paper (C. 2275 of 1878–9: P. P. vol. lxv) shows that ' there were registered under the Companies Acts 1862–7 and 1879 and believed to be still in existence ':

	Number of Companies.	*Nominal Capital.*	*Paid-up Capital.*	*Number of Shareholders.*
Limited banks*	80	£Mn. 76·787	£Mn. 19·276	38,818
Unlimited banks	53	,, 66·806	,, 22·675	51,601

* Since this includes many colonial and foreign banks, the statement in the text is almost too weak.

[4] *V. infra*, vol. ii, p. 260.

[5] *V. infra*, vol. ii, p. 263.

and the holders of £750,000 of this amount 'were absolutely ruined '.[1]

The natural consequence was a general fall in the value of shares carrying an unlimited liability, and the passage of legislation[2] permitting the unlimited companies to re-register under the Companies Acts as limited companies, and limited companies to register under the new legislation, the intention being to create a new kind of liability on shares, that is 'Reserved Liability', representing the difference between the nominal and the actual paid-up amount of a share, the difference being available only in the case of the company being wound up. In order to make the Act available to unlimited companies whose shares were fully paid up, and who yet desired to have some reserve liability available in case of winding up, such companies were to be able to increase the nominal amount of their capital, the increase not being capable of being called, except in the case of winding up.[3]

Surveying the development of English commercial banking since 1836, it will be noted that, apart from the influence of legislation upon the question of note issue, it has throughout remained relatively immune from interference by the law.[4] Economic forces have been enabled to work themselves out without overmuch deflection from the action of positive law. Where law has impinged on the development of banking, its action has not always worked in the direction of producing the best results. The provisions of the Bank Act of 1844 worked against the association of issuing with non-issuing joint-stock banks until the power to issue notes became relatively unimportant; the law of unlimited liability encouraged, rather than checked, the reckless use of the facilities afforded by the London discount market. Where the law might have assisted to strengthen the banking situation, as it might have done by insisting upon adequate publicity, it acted

[1] The circumstances are fully examined in A. S. Michie's edition of *Gilbart on Banking*.

[2] *V. infra*, vol. ii, pp. 300 *et seq*.

[3] In recent years the tendency has been for the larger banks, in issuing fresh capital, to issue only fully paid-up shares without any reserve liability—a striking tribute to the relative unpopularity of shares carrying a heavy reserve liability.

[4] The Joint Stock Bank Act of 1844 seems to be the main reason for the remarkable check to the creation of new joint-stock banks between 1845 and 1860.

tardily and inadequately, with the result that British banking statistics are to this day pitiably deficient.[1]

The characteristic feature, economically speaking, of British banking in the three-quarters of a century before the war is the gradual elimination of the private banker and the growing size of the banking unit. These are two aspects of the same general phenomenon, of which decentralized operation, or branch banking, is the third. Given competition on the one hand, a growing population and improving economic conditions on the other, all three are inevitable. For joint-stock banking, especially with limited liability, has the immense advantage of being able to raise capital more easily than the private partnership; decentralized operation has the merit of enabling the banker to spread his risks and to compensate, within the limits of his own bank, the deficit in resources of one district with the excess of resources of another. These advantages will tend to increase with every increase in the scale and area of operation. The result will be that every bank will expand outwards from its original centre of operation: banks that do not expand will suffer relatively to those that do; and, in the end, when the centrifugal forces have pushed the more enterprising banks to the limits of each other's territory, the simplest methods of expansion are to absorb banks that are not

[1] 'Having required the publication of their Issues from all Banks to which the privilege of Issue is continued,' said Peel in 1844, 'I do not propose to carry further the demand for publicity. I do not wish to pry into the affairs of each Bank, and above all I deprecate the taking of delusive securities against mismanagement and abuse. The public will hereafter know the names of the persons by whom the Banking business is to be conducted, and the public must rely on their own caution and discretion as a security against being injured or defrauded. It has been frequently proposed to require from each bank a periodical publication of its liabilities, its assets and the state of its transactions generally. But I have seen no form of account which would be at all satisfactory—no form of account which might not be rendered by a bank on the very verge of insolvency, if there were the intention to conceal a desperate state of affairs. The return, for instance, of "overdrawn accounts" might lead to very erroneous inferences as to the condition of a bank making such a return. A large amount of overdrawn accounts might in one case be indicative of gross mismanagement. It might in another case be perfectly compatible with the security of a bank, acting on the Scotch principle, and making advances at interest to customers in whom the bank had entire confidence.' (*House of Commons Debates*, vol. lxxiv (series 3), 6th May 1844, col. 746.)

expanding and to fuse with banks which otherwise would invade the home territory of the other. The limit to the expansive movement of each bank is such an organization as will represent the maximum degree of inter-local compensation of risks and resources: the limit to the expansion of all the banks taken together will be given, in so far as they are guided by calculations of pure profit and loss, by the general growth of the economic organism in which they are operating. But competition may easily force expansion beyond this point, both as regards any single bank or all banks taken together. The ultimate consequences of the forces impelling expansion were not realized till the post-war period,[1] but the same general forces have always been at work.

Given the general expansion of the joint-stock banking system, it was inevitable that the antagonistic attitude of the older organizations should have to give way. The opposition of the Bank of England to joint-stock banks[2] had never comprehended those banks which issued its notes instead of their own. Indeed, it actually agreed to discount their paper at a fixed rate of discount. In the long run, it could not afford to refuse deposit accounts to the joint-stock banks, since, after all, a Central Bank must possess resources if it is to be in a position to exercise any influence at all, and the resources available were to a growing extent those of the joint-stock banks. From the standpoint of the joint-stock banks, of course, a 'Drawing Account' at the Bank of England meant the possibility of tapping the Bank's reserve in periods of stress, but the balance of power really lay with the joint-stock banks. They could always drive the brokers into the Bank at a moment of crisis, and thus get gold or notes out of the Banking Department; and, in the end, if the Bank wanted to avoid disaster, it was in any case bound to help solvent banks. By holding their whole reserve at all times in the shape of Bank notes, they would have been just as safe as if they had held a deposit in the Banking Department; and yet the Bank,

[1] *V. infra*, vol. ii, p. 323, for the Report of the Committee on Bank Amalgamations.

[2] *V. infra*, vol. ii, p. 102, and J. W. Gilbart's evidence before the Committee on Banks of Issue, 1841, Q. 1307, as to conditions under which the Bank, having originally refused an account to the London and Westminster Bank, later agreed to open one.

under the peculiar conditions of the Bank Act of 1844, would not have benefited in the least by all the gold which the joint-stock banks would have had to pay into the Issue Department in return for the notes which they took out. By 1866 the joint-stock banks appear to have been fully conscious of their power, if the old story is true that at the height of the crisis 'one of the representatives of the joint-stock banks is reputed to have said plainly, addressing the Bank's representative, "I can draw a couple of cheques to-morrow morning which will shut you up at once" '.[1] By 1890 the Bank was actively co-operating with the joint-stock banks in the formation of the guarantee fund necessary to save the Barings from disaster.[2]

§ X

The outbreak of the war of 1914–18 was accompanied by a financial crisis. The first signs of it are noticeable in the Bank return issued on Wednesday, 29th July 1914, when the Bank rate was still 3 per cent. In the week ending on that day, the Bank Reserve had fallen £2,420,000; the bullion in the Bank had fallen £2,000,000; and, after many weeks of continuous inflows of gold from abroad, £820,000 had gone abroad; Other Deposits and Other Securities had risen by £12,233,000 and £13,674,000 respectively, whilst the note circulation had risen by £390,000. The inference is clear that the banks were already calling in funds from the bill market and that the brokers were relying on the Bank to help them out. On Thursday, 30th July, the real pressure began: Bank rate rose to 4 per cent. On Friday, 31st July, the day of the German ultimatum to Russia, the Stock Exchange was closed and Bank rate was raised to 8 per cent. On Saturday, 1st August, Bank rate was raised to 10 per cent. The next day, Sunday, 2nd August, the Bank holiday was extended to Friday, 7th August. When on Friday, 7th August, the banks reopened for business, the Bank had obtained the assent of the Government

[1] Michie, *op. cit.*, vol. ii, p. 354, quoting from Patterson's *Science of Finance*, p. 287.

[2] In the same way persistence in the refusal to admit the joint-stock banks to the Clearing House (the rule of exclusion actually broke down in 1854) would simply have led in the long run to the creation of a new Clearing House, which, as the new banks gained in strength, would have absorbed an ever-growing proportion of the total clearings of the country.

to ' suspend ' the Bank Act, an ' emergency currency ' was available to meet any panic-demand for money—there was no such demand—and the banks were protected, in addition, by moratoria. The day before the banks reopened, Bank rate was reduced to 6 per cent. The ' crisis ' was over, and the Government and the Bank could turn their attention to the problems presented by the frozen state of the Discount Market and the plight of the Accepting Houses. When the Bank return was issued on 7th August it showed movements of enormous proportions; since the only day on which business had been conducted was the previous Saturday, the Return measures the pressure since the previous Wednesday. The bullion had fallen by over £10½ millions and gold to the extent of £2,300,000 went abroad; the Reserve had fallen by nearly £17 millions (£16,908,000). The Other Securities had risen by £18,044,000, but the Other Deposits by only £2,330,000—in other words, of the additional amounts borrowed, the greater part had been taken out of the Bank; and the ' normal ' phenomenon of a crisis, a coincident rise in Other Securities and Other Deposits, was not this time present. Part of the outflow of cash from the Bank was due to the demand for currency at the beginning of the holiday period. Much the greater part represents a movement by the banks to hold additional notes and a refusal on their part to give their customers gold, so that these were, in their turn, driven to demand gold from the Bank.

On the basis of the ' emergency currency '—sanctioned by the Currency and Bank Notes Acts[1]—the greater part of the subsequent history of the financial aspect of the war was to be built up. *Some* legislation was no doubt required, since the Bank of England had no legal right to issue £1 and 10*s*. notes; but it would have been in the historic tradition to have given the Bank the power to issue these notes, and this, together with the suspension of the Bank Act,[2] would have placed the Bank in a position to meet the emergency demand, had it actually manifested itself. From the very beginning of the war, however, the idea of

[1] *V. infra,* vol. ii, pp. 320–322.
[2] On 1st August 1914 the Bank had approached the Government in terms closely following precedent, and had obtained in reply the normal

economizing the use of gold circulation played a part in the plans of the Government. Still, this does not explain why the Government thought it desirable that a new note issue, issued upon the credit of the nation, instead of upon the credit of the Bank, should be put out—especially as at the beginning of the war there was apparently no thought of making the notes inconvertible. On the contrary, the new notes were expressly declared to be convertible into gold during office hours at the Bank of England. It was only gradually that the new legislation came to be used as an engine of inflation, and it is even now doubtful whether at any time during the war the responsible authorities were fully aware of what they were doing. The original Treasury Minute of 6th August 1914,[1] 'as to the issue of Currency Notes', provided that the notes, when issued to banks and bankers, were to be regarded as advances by the Treasury to the institution in question, 'bearing interest from day to day at the current Bank Rate'; and Currency Notes were only to be issued to bankers. Under these conditions it was reasonable to suppose that banks would not hold notes a day longer than was necessary. But by 20th August the whole situation altered. On that day a new Treasury Minute[2] provided that, in addition to the methods of issue contemplated in the original Minute of 6th August 1914, Currency Notes 'shall be issued to any person upon application through the Bank of England on payment of the face value of the notes required, the amount paid being carried' to the credit of a special account, the Currency Note Redemption Account. It now became possible to 'buy' Currency Notes by transferring to the Currency Note

assurance that if, in the circumstances, the fiduciary limit were exceeded, the Government would protect the Bank by obtaining Parliamentary sanction. Section III of the Currency and Bank Notes Act, passed on 6th August, indemnified the Bank of England and any Scottish or Irish Bank of Issue against any liability in respect of illegal issues made since 1st August, and further provided that, subject to Treasury sanction, such Banks might exceed any limits fixed by law (*v. infra*, vol. ii, p. 321). The correspondence between the Government and the Bank will be found reprinted in Kirkaldy, *British Finance*, 1914 *to* 1921, pp. 3–4, and *Economic Journal*, vol. xxv, pp. 565 *et seq.* On 7th and 8th August, after the passing of the Currency and Bank Notes Act, there was a technical over-issue of £3,043,000.

[1] *Manual of Emergency Legislation* (*Financial Edition*), *August 1914 to 4th June 1915*, p. 5. [2] *Op. cit.*, p. 9.

Account a balance at the Bank of England—which the Government might borrow against any security it might like to offer[1]; and the way was open, since no limit was fixed to the total amount which might be issued in this manner, to inflationary war finance. The rise of prices associated with inflation would always appear to justify any given increase in the volume of currency, and if the increase in the volume of currency threatened to denude the Bank of England of gold—for the total note issue, that of the Bank and that of the Government alike, was convertible into gold on demand—the danger could be very materially reduced by making it an offence under the Defence of the Realm Code to export gold without a licence, or ' to melt down, break up, or use otherwise than as currency any gold coin which is for the time being current in the United Kingdom '. Patriotism and convenience alike made the population willing to *use* paper money; the law made it useless for any one not willing to be a law-breaker to get gold, and interfered quickly enough with the evilly disposed who desired to make a profit by exploiting the undoubted statutory right to obtain gold from the Bank. The legal fiction was maintained that the note was convertible; actually it was inconvertible until April 1925, for, after the war itself was over, the Gold and Silver Export Control Act continued the prohibition on the export of gold and silver without Governmental sanction originally enforced by the Defence of the Realm Code.

The situation thus created is a familiar one in the annals of currency disorganization—the pound sterling had ceased to be a certain definite weight of gold, which could be melted or exported at the will of the holder, and had become an inconvertible paper instrument, actually exchangeable inside the country at its face value in such gold coin as was still in circulation (by 1918, however, gold coin had for all practical purposes ceased to circulate), and worth less than its nominal gold equivalent in gold abroad. During the actual conduct of hostilities and for some

[1] This possibility was pointed out by Mr. J. M. Keynes as early as September 1914 (*Economic Journal*, vol. xxiv, p. 481): ' There is nothing to prevent the Treasury from making use of this account to fill up a temporary deficit in the Exchequer Balances, whether by issuing Treasury Bills to the Currency Note Redemption Account, or without this or a similar formality.'

months thereafter, the artificial support given to the dollar-sterling exchange prevented this fact from being generally realized; the ' unpegging ' of the exchange early in 1919 made it obvious to the world, and made the reform of British currency conditions a matter of urgent political and social importance.

From the standpoint of the Central Bank, the major questions were whether the two note issues should be unified and whether the opportunity would be taken to introduce changes in the organization and powers of the Bank of England in connexion therewith; and, lastly, and in the end most importantly, whether the pound sterling should again be linked up with gold. These were the issues submitted to the body which, from the name of its chairman, was to become known as the Cunliffe Committee. The first Report of the Committee,[1] dated 15th August 1918, before the end of the war was in sight, was almost necessarily confined to the laying down of general principles. The general tenor of the Report is conservative, in spite of the fact that two important permanent changes were suggested. The restoration of the Gold Standard and the unification of the note issues were to be regarded as the ultimate aims of British policy, and a restoration of the Gold Standard was impossible without a limitation of the issue of uncovered notes, which should be enforced ' as soon as practicable '. But whilst the currency should be convertible into gold for export purposes, it was not desirable that gold coin should be allowed to circulate, though legislation on the subject was not required, since the public had become fully accustomed to the use of paper notes; ' informal action on the part of the banks may be expected to accomplish all that is required. If necessary, however, the circulation of gold coin could be prevented ' by making the notes ' convertible at the discretion of the Bank of England either into such coin or into bar gold, though for our own part we should prefer to maintain the right of the note-holder to receive payment in gold coin and to trust to the informal steps suggested above to prevent gold from flowing into internal circulation '. This somewhat illogical attitude was subsequently to be rejected. Again, whilst the Committee was in favour of incorporating into the permanent legislation dealing

[1] *V. infra*, vol. ii, p. 334.

with the Bank the power to suspend the Bank Act contained in the Currency and Bank Notes Act, it was not prepared to reject the rule of a fixed, fiduciary issue in favour of a system of proportional reserve, such as had been favoured by the framers of most Central Bank constitutions.

The second Report,[1] which was issued in December 1919, was destined to have important consequences. It urged an immediate adoption of the suggestion, made in the First Report, that a maximum limit should be placed upon the issue of uncovered Treasury Notes, a recommendation which was given effect to by the Treasury Minute of 15th December 1919.[2] This imposed what was popularly known as the 'Cunliffe Limit'; and, coming at a time when prices had been rising and an exaggerated industrial boom was in process (co-effects in the main of a mistaken currency policy), it was the cause of the check to the upward trend of prices and of industrial expansion which marked the second half of the year 1920.

Between the end of 1919 and the beginning of 1925 the value of the pound sterling in terms of gold gradually but by no means continuously increased. The Cunliffe Limit simply set an upper limit to the total volume of currency notes which could be issued; the gold value of paper currency depended not only upon the volume of British currency and upon the British price-level but upon the movements contemporaneously taking place in American dollar prices. So long as the Gold and Silver Export Control Act was on the statute-book, whatever the gold value of the currency might be, gold could be prevented from moving out; though if by limitation of amount the value of the paper pound rose above \$4.86$\frac{2}{3}$, there was nothing in the Act to prevent gold from coming in. The rise in the value of the pound sterling, which was assisted from the beginning of 1925 by American anticipation that the gold standard would be restored at the old parity with the American dollar, coincided with the necessity either of allowing the Gold and Silver Export Control Act to lapse (since it had originally been passed for a period of five years only) or of renewing it for a further term of years. A variety of choices lay before the Government: (1) it could have restored the gold standard

[1] *V. infra*, vol ii, p. 366. [2] *V. infra*, vol. ii, p. 371.

at the old parity and have allowd the Act to lapse completely; (2) it could have re-enacted the Act and have continued to allow sterling 'to find its own level', subject only to the indirect effects exerted by the Cunliffe Limit; (3) alternatively, it could have re-enacted the Act, and pursued the policy of keeping sterling from falling below the old parity (*de facto* as compared with *de jure* stabilization); (4) it could have introduced *de facto* or *de jure* stabilization at a parity lower than the pre-war parity. The opponents of Government policy (including those who never desired the restoration of the gold standard in *any* form) would have preferred any of the last three policies to the first. Scientific discussion mainly turned on the question whether, taking the actual levels of prices in Great Britain and the United States, stabilization at the old parity would not be equivalent to giving the pound too high a gold value. The logical outcome of a proof that stabilization at the old parity would be to over-value the pound should have been a demand for devaluation—the choice of a lower gold parity—but this was never seriously discussed. The practical issue lay between restoring the gold standard at the old parity, or not restoring it at all for the time being. In April 1925 the Government chose the first alternative; the publicly stated grounds for the action it then took being contained in the *Report of the Committee on the Currency and Bank of England Note Issues*.[1] This Committee had been appointed in June 1924, 'to consider whether the time has now come to amalgamate the Treasury Note Issue with the Bank of England Note Issue, and, if so, on what terms and conditions the amalgamation should be carried out'. Instead of dealing with this highly technical matter in its Report, the Committee declared for an *early* return to the gold standard and the *immediate* restoration of a free market for gold in this country. These recommendations were given effect to by the passage of the Gold Standard Act, 1925[2]; the grant of a general licence to the Bank of England to export, and an intimation by the Chancellor of the Exchequer that the Gold Control Act of 1920 would be allowed to lapse at the end of 1925.

The Gold Standard Act of 1925 introduced a system of currency now usually known as the 'Gold Bullion Standard', since

[1] *V. infra*, vol. ii, p. 372. [2] *V. infra*, vol. ii, p. 383.

the British paper currency is convertible into gold bars of a minimum weight of 400 fine ounces, thus making the minimum tender of legal money, in return for which gold bars can be obtained, £1,699 11*s.* 8*d.* The right to demand gold coin from the Bank of England is abolished: the right to sell gold to the Bank is retained, and the legal status of existing gold coin is in no way interfered with.[1]

For the next two years further agitation was mainly to centre upon the question of whether or not the return to the gold standard at the old parity had added to the other economic difficulties to which the country was exposed; the terms upon which, and the date at which, amalgamation of the two note issues should take place having fallen somewhat into the background. From the beginning of 1928, however, this question began to come rapidly to the front. In certain expert circles, the possibility of a further shortage of gold, involving a fall in the long-period price-level and consequent depression of economic life, was being actively canvassed. The Genoa Conference had already, in 1920, drawn attention to the necessity of avoiding a scramble for gold and had insisted upon the necessity of co-operation among the Central Banks for the purpose of achieving a rational gold policy. The question, so far as the Bank of England was concerned, was then this: would the Bank be given a fixed fiduciary issue more than equal to the sum of the two existing uncovered issues or not? Would it be allowed to vary the fiduciary issue in the future, not only if it were required to meet the contingency of a financial panic, but also to meet the needs of an increasing population, expanding production, or falling gold output?

The Currency and Bank Notes Act, 1928, answers these questions by (1) giving the Bank a fixed fiduciary issue of rather less than the sum total of the pre-existent uncovered Bank of England and Currency Notes, but (2) couples this fixed fiduciary limit with certain permissive powers of increase for the future, the exact significance of which depends not only upon the terms of the legislation itself but also upon certain 'undertakings'[2]

[1] The legal position of the British currency under this Act is fully analysed in Chapter III of my *Return to Gold.*

[2] Sir L. Worthington-Evans on 22nd May 1928 (*House of Commons Debates,* 5th Series, vol. 217, col. 1830): 'I am authorized to say that

given by the Governor of the Bank of England as to the manner in which the Bank intends to interpret the spirit of the Act. This curious situation, which can hardly be considered legally binding in any way, arose out of the hostility to the Act when it was being discussed in Parliament. But with the passage of the Act of 1928, the seal has for the time being been put, not only on the efforts to repair the damage inflicted by the war upon the British currency standard, but also on the long effort to amend the Bank Act of 1844 which began with the Report of the House of Lords Committee in 1848.

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the Governor of the Bank has read what I said on Second Reading. For fear that I should pledge him too much, and to be more specific, he has read what I said in columns 744 to 746 of the Official Report, and he has authorized me to say that that does represent the general intentions of the Bank. That, then, is the policy of the Bank.'

The cases in which an increase of the fiduciary issue can occur would seem, accordingly, to be three in number:

(1) An emergency such as those of 1847, 1857, and 1866.

(2) 'A new kind of emergency has become possible. Now that the foreign banks have adopted the practice of accumulating a large reserve of sterling bills, it is always possible that, owing to a change in policy upon the part of those banks, a large sum might be withdrawn in a short time by the realization of those balances. The probability is that such a measure would be avoided by co-operation amongst the central banks, as was indeed advised in the Genoa resolutions. But if the withdrawal of gold was insisted upon, it might become necessary to extend the fiduciary issue, and that would be an occasion which would justify the Governor of the Bank in asking for that expansion, and the Treasury in granting it.' (Col. 744.)

(3) 'A third category is the possible competition for gold among the Central banks. . . . Should the Bank find that, owing to a world demand for gold, credit would be unduly restricted, not as a check on speculation, but to the injury of legitimate requirements, then the Bank can request the Treasury to extend the fiduciary issue and so free gold in the hands of the Bank for further credit operations. Moreover, the principle of a fixed fiduciary issue itself necessitates some provision being made for normal growth. It was only by an accidental combination of circumstances that the Act of 1844 did not require an expansion of the fiduciary issue from time to time. . . . The provision in the Bill for increasing the fiduciary issue is not intended therefore to be a mere legislative substitute for the Crisis Letter. On the contrary, it is intended to be used, not in a crisis, but before it and to prevent undue stringency from arising from any of the causes I have mentioned.' (Col. 745.)

PART I

THE BANK OF ENGLAND BEFORE THE BANK ACT OF 1844