THE NATIONALISATION OF THE BANKS

It is still too early to give a complete analysis of the Government's policy as regards the nationalisation of the banks. Sir Hugh Dalton's statements were too vague for that, he gave us to understand that all his plans were still in the experimental stage.

Nevertheless, from statements made by different Labour leaders, especially from those of Mr. Bevin, as Minister of Labour of the former Government, we can get quite a clear picture of the philosophy behind their policy, and of this philosophy I shall give a short outline and criticism.

The Labour party is convinced—and rightly so—that our reconstruction problems of today are not so much production as financial problems, that though we may have as many plans for industrial expansion as we like, while this expansion has to be financed according to the old system, in which the power to create and destroy money is left to the banks, our plans will turn out failures.

They fear especially the consequences of *deflation*. Deflation, the deliberate creation of a shortage of money, causes of necessity a sudden drop of prices, so that producers are forced either to sell below cost price, to destroy their products to keep up their price, or to cease producing at all.

This is what happened after the last war, when a period of deflation caused almost a complete standstill of production and millions were thrown out of work. The same happened again during the period of deflation in 1932-33, when not only the producers themselves, but even the Governments had official plans for destruction of foodstuffs, while the people were starving.

They correctly blame the banking system for this chaos, because the banks no longer treat money as a medium of exchange, but as a merchandise, with an independent existence, with its own rules of buying and selling, unrelated to the production and consumption of goods.

"Whoever has the right to create or destroy money, or to increase or restrict the flow of money, is able to dictate how much goods can be purchased and therefore produced. The farmer may say: 'I can produce 20,000 bags of potatoes', but the fellow who controls the supply of credit can say to him: 'Produce it if you like, but you will only be able to sell half'. What does the farmer do? He must then destroy the other half and the following year he cuts his production by half. There is a great reluctance on the part of people to accept the fact that the creation and control of the volume of credit is entirely outside the hands of the nation or of the industrial and capitalist class.''(1)

It is perhaps natural to jump to the conclusion that if deflation is an economic evil, we must continue in peace time the policy of inflation which we started in wartime. That is what the Labour Government seems to intend. They believe that although unrestrained inflation is as bad as deflation, controlled inflation, whereby as much credit is created as is necessary to meet the demand of increasing industry, will have no evil effects. They argue that if millions of pounds can be found to finance a policy of destruction, during the war, why cannot a comparatively small sum be found to finance a policy of construction in peace time. They think that all that is necessary is for the Government to take over the banks and then proceed to finance the industries of the country in exactly the same way as the banks did before. They should know that the only advantage would be that the interest on inflated money no longer would go into the pockets of private bankers, but into the coffers of the Government. But the real danger, both of inflation and deflation, would not be averted.

Let the Labour Party consider the following points:

1. You cannot indefinitely go on with the creation of credit or inflation. If you keep on inflating money, you have got to stop one day or the country will go bankrupt. *Deflation is only a necessary consequence of inflation.* We can prove this in another way by using the example borrowed from a course of economics, which students have to pass before they are admitted to membership of the Institute of Bankers: to show how money is created.

This is how the example runs:

''Let us suppose that there is one man (A) who has set himself up as a banker, and that he is the only banker. He has a capital (in gold) of £20,000 and the rest of the people in the community deposit their gold (amounting to £25,000) with him. A's Balance Sheet then reads as follows:

Liabilities		Assets	
Capital ...	£20,000	Gold ...	£45,000
Deposits	£25,000		
	£45,000		£45,000

(1) Senator Smith (of South Africa), ''Let Go Our Money'', p. 17.

"Now B, an ironfounder, wishes to rebuild his foundry, and comes to the banker and borrows £40,000. He issues cheques (over a period) totalling this amount and the various payees pay these cheques into the accounts they keep with the banker, A.

"A's Ballance Sheet will then read as follows:

Liabilities		Assets	
Capital ...	£20,000	Gold	£45,000
Deposits	£65,000	Advances ...	£40,000
	£85,000		£85,000

"Ponder this for a moment. The result of that bank giving an overdraft to the ironfounder increases the bank's own deposits by £40,000. In other words the banker has created credit to the extent of £40,000."

This is the way money is created. But, to continue the story what is B, the ironfounder, going to do? He is left with a debt of £40,000 and he is keen to pay it off as soon as possible. Suppose he makes £40,000 in one year, then he will bring the money to the bank (in cheques and not in cash) at the end of the year, his overdraft is destroyed and A's Balance Sheet will read like the first one with capital and deposits amounting to £45,000. In other words, the money which was first created and was passed on by the payees as genuine money, has now been destroyed, has completely disappeared, and a period of deflation has set in.

The same happens when a Minister of Finance cancels war loans or pays them off by taxation money. Immediately enormous amounts of money hitherto in circulation disappear completely and deflation starts. That is why I believe that since V.J. Day we have begun a period of deflation all over the world and the disastrous consequences will soon be noticeable.

Therefore a Labour Government which takes over the banking system in its entire structure will be causing as much deflation as a Conservative Government that leaves the banking system intact.

2. It is all very well to hammer on the disastrous consequences of deflation, but inflation is just as bad. Inflation must cause a rise in prices just as effectively as deflation causes a drop in prices. And with a rise of prices, the greatest part of any country, the people who live on fixed wages and salaries, will be continually cheated, because they will be able to buy less and less for their wages. The producers will make huge profits, but the wage-

earners will be pushed below the breadline, the production of the essentials will be wasted in the production of luxury articles for the elected few. Surely not a nice programme for the Labour Party. The real effect of inflation is not that it causes a surplus of money, but that the wealth of the country goes into the hands of a few at the cost of the rest of the community. If every member of the community received his share of the created credit, equally and in the same degree, no harm would be done, because then, with the rise of prices, every member would still have the same exchange value for his money as before. But this is not the case: those who have stock in hand will benefit at the cost of those who live according to fixed salaries. And therefore inflation is an instrument of usury, irrespective of whether the Government applies it or the private bank.

Mr Bevin has argued that the creation of credit, or inflation, is all right because it worked so well in wartime. "Why shouldn't we go on with it after the war?" was Mr. Bevin's favourite question in his electioneering speeches.

He forgets that war-time production is directed towards destruction and that only a limited supply of consumable goods are produced, the distribution of which was looked after by a rigorous system of rationing and price control. But as soon as we switch over to peace-time production, we must concentrate on the production of consumable goods, and we can no longer use that system of rationing and control. We can no longer say: "Everyone may only buy two pairs of shoes," when we urge the shoe industry to make six pairs for everyone. And as soon as we stop the rationing, the money that has been lying idle in the banks for all these years will come out, the inflation that has been started from the beginning of the war, but was pinned down all the time, will only now raise its ugly head. "I have got a nice few thousand pounds in the bank," I say to myself, "I hope now to build my own house and to get the materials before the prices rise." But so does everybody think that way, everyone is eager to buy as quickly as he can and the prices will just rise until chaos reigns. You cannot shout at the Government: Let go the controls! Stop the rationing! Give scope to our industries! and at the same time expect that the prices will remain stable, with all that inflated money in the banks.

Therefore, if the Labour Government really thinks that all that is required is to keep the money inflated, creating money at an ever growing pace, then that Government is doomed.

3. Has the Labour Party ever asked whether the creation of credit is really necessary for industry? So often the statement is made as if nobody could think it necessary to query it. Is it not true that most of the industries do not obtain their capital from the banks but from the sale of shares, bought by investors with genuine money? Is it not true that the banks usually refuse to lend to industry and only lend to commerce, because they receive from commerce a quick return of their money?

Why are people so afraid to condemn the creation of credit? Is it perhaps because with an increase of production the prices will go down? We should remember that a drop in prices caused by deflation is quite a different affair from the drop in prices caused by increased production combined by a stability of the issue of money; because here in the latter case, through the better employment of the machine and non-human power, the cost of production is so much lower that the prices can go down and yet the producers make the same profits, while at the same time the people with the fixed wages can buy more goods for their wages, and while increasing the consumption, can clamour for ever-increasing production.

It has been argued by Labour Members that money is only tickets, that we could continue the ration card system, only giving them the value of money. If money is only tickets—and I agree to that—it would follow that at the time when nearly all goods are consumed there should be few tickets in circulation and in time of abundance many. But it is characteristic of a period of inflation that there are more tickets than goods (the Government creating credit at a time when the new production has to start) and it is characteristic of deflation that there are less tickets than goods: *Ergo*: both are bad, because at both periods money has ceased to be a true form of exchange. Now let us see what happens when we keep the amount of money in circulation stable:

With increased production prices must go down, so that with the same amount of money in circulation this money will be split up in many tickets of smaller denomination; in other words, the tickets in circulation will correspond to the greater amount of goods available. When the wealth of the country is almost consumed, prices must go up, so that the same amount of money in circulation will be split up in few tickets of bigger denomination and again the tickets available will correspond with the amount of goods available. Here is the case where the abundance and shortage of money effects every member of the community alike and where one part of the community is not benefiting at the expense of the other.

What is more, it is still possible for money to be issued without creating credit.

"Creation of credit" is really a vague and unsatisfactory term. Generally speaking, there are two ways of creating credit. The first is to issue notes on the strength of goods *already produced;* the second is by borrowing (or issuing notes) on the strength of *future wealth.*

If I have made a piano of £200 value, I can write a note, stating: "This is good for my piano." Then this note is a perfect medium of exchange, because the man who supplies me with £200 of goods on the strength of my note receives my piano in exchange.

But if the bank issue money to the value of £200 on the strength of the fact that I am going to produce a piano in two years time, then the fellow who gives me goods to the value of £200 does not receive a piano in exchange, but he passes my note on and on, so that in reality £200 of goods have been withdrawn from the exchange, or the value of money has gone down to the extent of £200. By the time that I sell my piano and make the £200 disappear, which was in circulation and passed as genuine money, I create a sudden shortage of money and again make the goods fall in price. Thus I have not made an exchange at all, but only created a disturbance, by first taking £200 of goods out of circulation and afterwards £200 of money!

Let the Government nationalise the banks by all means, but with the firm purpose never again to allow the creation or destruction of credit. Let our money go, allow inflation to take its course, allow prices to rise until the money in circulation again covers the goods in existence. Then let us stay there, always keeping the same amount of money in circulation, so that increased production necessitates a drop of prices, and the balance is restored between production and consumption—a drop of prices, bigger consumption, greater demand.

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The Editor regrets that a long reply to Dom Aelred Graham's challenge in the November BLACKFRIARS *was received from Mr. Gregory too late for inclusion in the December issue. Since then Mr. Gregory has published the substance of his reply in* The Tablet *and Dom Graham in his turn defended himself and so the discussion terminated amicably. Readers are therefore referred to the pages of* The Tablet *for November 24th and December 1st.*