MONEY AND GOLD

SIR, — Mr. Smedley fears (Jan-Feb issue) that if the commercial banks were allowed to issue their own notes, they might be tempted to pay their debts in their notes. But Scottish banks enjoyed freedom of note issue for about 150 years and their currency was far more stable than that of England where banking was more state-controlled. The Scottish notes were cleared daily through the Clearing House, and any excess had to be balanced in gold by the deficit bank. It would have been useless for a bank to pay its debts in its own notes: it might as well pay in gold.

The Scottish system was abolished in 1845 precisely because the English government held the same opinion as Mr. Smedley, that the pound note must always be redeemable in a fixed weight of gold: if gold was being drained away from the country, we must cut down prices here by a high bank rate in order to induce foreign importers of our cheapened goods to buy here and replenish our gold reserves. This was the origin of the stop-go policy which has produced alternate booms and slumps here for over a century, bankrupting small firms and encouraging mergers among the survivors.

The remedy is a floating gold price. Gold is nowhere used as money today - there is too little of it. Gold serves today only to ensure trust in paper money. But gold is itself exposed to the law of supply and demand. Therefore if the value of a pound note is not to be jerked about by every change in the bullion market, the note must be made redeemable in a pound's *worth* of gold at the current price in a free bullion market on the day when redemption is demanded. Mr. Smedley wants a fixed gold price. What price would he fix? In view of gold's skittish behaviour recently, this poses a pretty problem for him. If the price is lower than that of the free market, the banks will be shamelessly drained of gold. If too high, they will be stuffed with gold for which they have no use. Mr. Smedley has a fine record of anti-socialist activity, and I am sorry to have to disagree with him on this point.

Will you allow me a little space in which to congratulate your contributor, Professor F. J. Jones, on his refutation of the widely-held notion that banks today create money. I have attacked this notion for 17 years in the pages of *The Individualist*, and I therefore look on Jones' efforts with a professional eye. I welcome his help because the enemy is so strong. Governments in every industrial country are today burdening banks with crippling restrictions because they are convinced that banks today create money. What the West has suffered in loss of production, bankruptcy among small firms and consequent growth of monopoly in industry is incalculable. I would, however, demur to Jones' statement that banks *create* credit. I know that the word is in common use to denote the mere lending of money, but its use plays into the hands of our opponents. A bank lends, and can lend, only the money lent it by its depositors. To give any countenance to the idea that the banks create this credit out of thin air is a great pity.

Yours faithfully,

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