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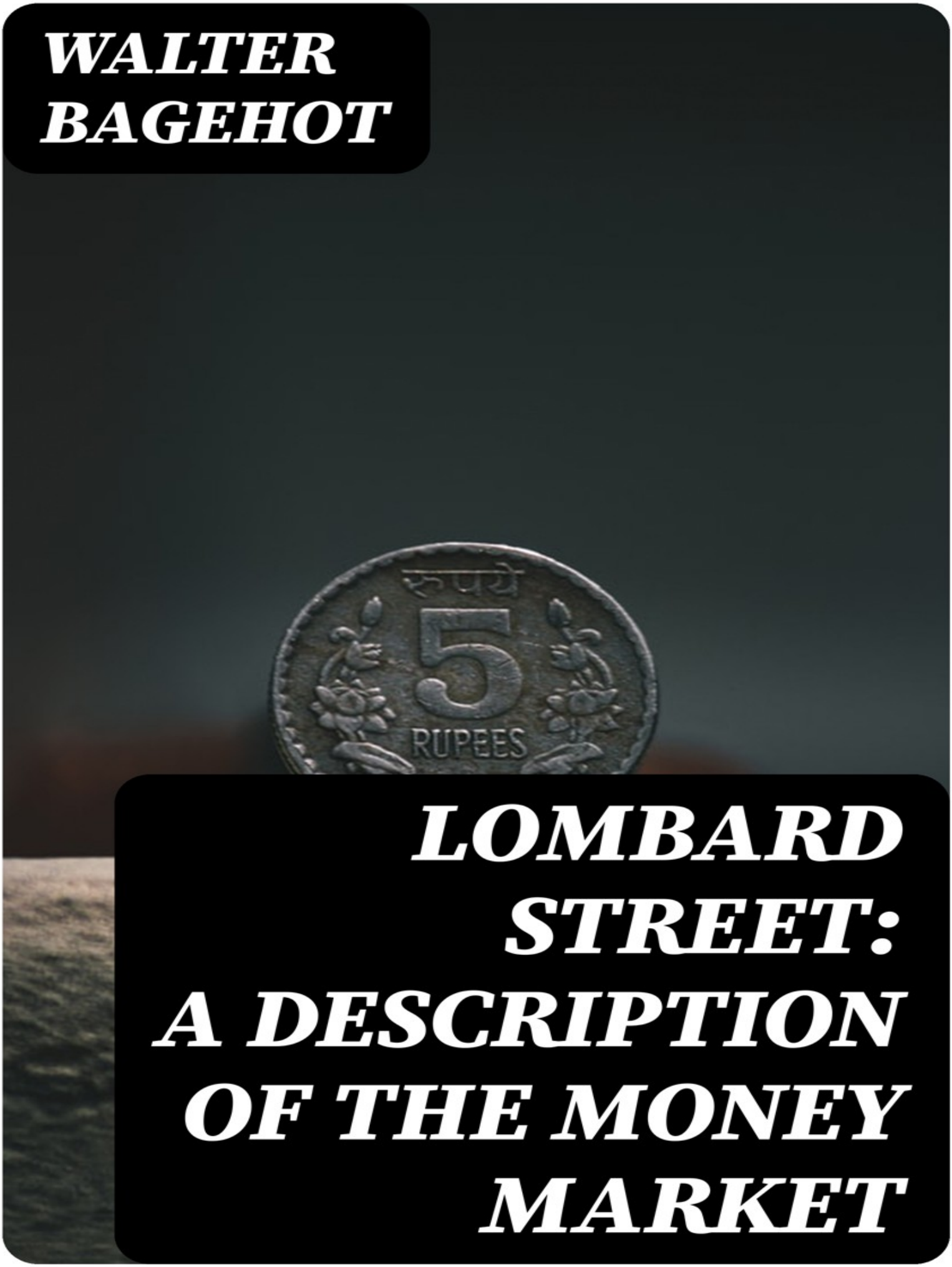
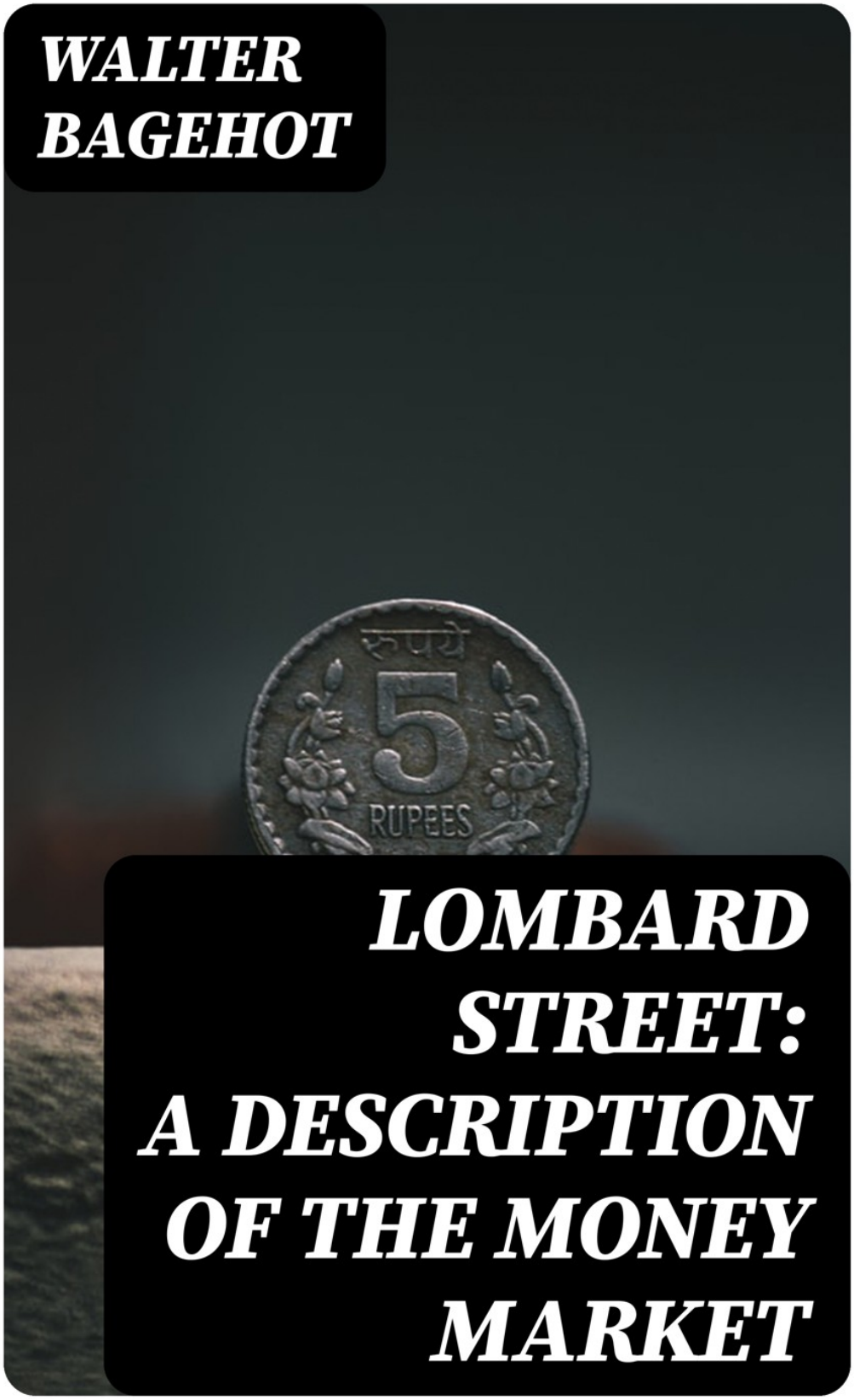


LOMBARD STREET: A DESCRIPTION OF THE MONEY MARKET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LOMBARD
STREET:
A DESCRIPTION
OF THE MONEY
MARKET

Walter Bagehot

Lombard Street: A Description of the Money Market

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CHAPTER I.

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Introductory.

I venture to call this Essay 'Lombard Street,' and not the 'Money Market,' or any such phrase, because I wish to deal, and to show that I mean to deal, with concrete realities. A notion prevails that the Money Market is something so impalpable that it can only be spoken of in very abstract words, and that therefore books on it must always be exceedingly difficult. But I maintain that the Money Market is as concrete and real as anything else; that it can be described in as plain words; that it is the writer's fault if what he says is not clear. In one respect, however, I admit that I am about to take perhaps an unfair advantage. Half, and more than half, of the supposed 'difficulty' of the Money Market has arisen out of the controversies as to 'Peel's Act,' and the abstract discussions on the theory on which that act is based, or supposed to be based. But in the ensuing pages I mean to speak as little as I can of the Act of 1844; and when I do speak of it, I shall deal nearly exclusively with its experienced effects, and scarcely at all, if at all, with its refined basis.

For this I have several reasons,—one, that if you say anything about the Act of 1844, it is little matter what else

you say, for few will attend to it. Most critics will seize on the passage as to the Act, either to attack it or defend it, as if it were the main point. There has been so much fierce controversy as to this Act of Parliament—and there is still so much animosity—that a single sentence respecting it is far more interesting to very many than a whole book on any other part of the subject. Two hosts of eager disputants on this subject ask of every new writer the one question—Are you with us or against us? and they care for little else. Of course if the Act of 1844 really were, as is commonly thought, the *primum mobile* of the English Money Market, the source of all good according to some, and the source of all harm according to others, the extreme irritation excited by an opinion on it would be no reason for not giving a free opinion. A writer on any subject must not neglect its cardinal fact, for fear that others may abuse him. But, in my judgment, the Act of 1844 is only a subordinate matter in the Money Market; what has to be said on it has been said at disproportionate length; the phenomena connected with it have been magnified into greater relative importance than they at all deserve. We must never forget that a quarter of a century has passed since 1844, a period singularly remarkable for its material progress, and almost marvellous in its banking development. Even, therefore, if the facts so much referred to in 1844 had the importance then ascribed to them, and I believe that in some respects they were even then overstated, there would be nothing surprising in finding that in a new world new phenomena had arisen which now are larger and stronger. In my opinion this is the truth: since 1844, Lombard Street is so changed that we

cannot judge of it without describing and discussing a most vigorous adult world which then was small and weak. On this account I wish to say as little as is fairly possible of the Act of 1844, and, as far as I can, to isolate and dwell exclusively on the 'Post-Peel' agencies, so that those who have had enough of that well-worn theme (and they are very many) may not be wearied, and that the new and neglected parts of the subject may be seen as they really are.

The briefest and truest way of describing Lombard Street is to say that it is by far the greatest combination of economical power and economical delicacy that the world has even seen. Of the greatness of the power there will be no doubt. Money is economical power. Everyone is aware that England is the greatest moneyed country in the world; everyone admits that it has much more immediately disposable and ready cash than any other country. But very few persons are aware how much greater the ready balance —the floating loan-fund which can be lent to anyone or for any purpose—is in England than it is anywhere else in the world. A very few figures will show how large the London loan-fund is, and how much greater it is than any other. The known deposits—the deposits of banks which publish their accounts—are, in

London (31st December, 1872) 120,000,000 L
Paris (27th February, 1873) 13,000,000 L
New York (February, 1873) 40,000,000 L
German Empire (31st January, 1873) 8,000,000 L

And the unknown deposits—the deposits in banks which do not publish their accounts—are in London much greater

than those many other of these cities. The bankers' deposits of London are many times greater than those of any other city—those of Great Britain many times greater than those of any other country.

Of course the deposits of bankers are not a strictly accurate measure of the resources of a Money Market. On the contrary, much more cash exists out of banks in France and Germany, and in all non-banking countries, than could be found in England or Scotland, where banking is developed. But that cash is not, so to speak, 'money-market money:' it is not attainable. Nothing but their immense misfortunes, nothing but a vast loan in their own securities, could have extracted the hoards of France from the custody of the French people. The offer of no other securities would have tempted them, for they had confidence in no other securities. For all other purposes the money hoarded was useless and might as well not have been hoarded. But the English money is 'borrowable' money. Our people are bolder in dealing with their money than any continental nation, and even if they were not bolder, the mere fact that their money is deposited in a bank makes it far more obtainable. A million in the hands of a single banker is a great power; he can at once lend it where he will, and borrowers can come to him, because they know or believe that he has it. But the same sum scattered in tens and fifties through a whole nation is no power at all: no one knows where to find it or whom to ask for it. Concentration of money in banks, though not the sole cause, is the principal cause which has made the Money Market of England so exceedingly rich, so much beyond that of other countries.

The effect is seen constantly. We are asked to lend, and do lend, vast sums, which it would be impossible to obtain elsewhere. It is sometimes said that any foreign country can borrow in Lombard Street at a price: some countries can borrow much cheaper than others; but all, it is said, can have some money if they choose to pay enough for it. Perhaps this is an exaggeration; but confined, as of course it was meant to be, to civilised Governments, it is not much of an exaggeration. There are very few civilised Governments that could not borrow considerable sums of us if they choose, and most of them seem more and more likely to choose. If any nation wants even to make a railway—especially at all a poor nation—it is sure to come to this country—to the country of banks—for the money. It is true that English bankers are not themselves very great lenders to foreign states. But they are great lenders to those who lend. They advance on foreign stocks, as the phrase is, with 'a margin;' that is, they find eighty per cent of the money, and the nominal lender finds the rest. And it is in this way that vast works are achieved with English aid which but for that aid would never have been planned.

In domestic enterprises it is the same. We have entirely lost the idea that any undertaking likely to pay, and seen to be likely, can perish for want of money; yet no idea was more familiar to our ancestors, or is more common now in most countries. A citizen of London in Queen Elizabeth's time could not have imagined our state of mind. He would have thought that it was of no use inventing railways (if he could have understood what a railway meant), for you would not have been able to collect the capital with which to make

them. At this moment, in colonies and all rude countries, there is no large sum of transferable money; there is no fund from which you can borrow, and out of which you can make immense works. Taking the world as a whole—either now or in the past—it is certain that in poor states there is no spare money for new and great undertakings, and that in most rich states the money is too scattered, and clings too close to the hands of the owners, to be often obtainable in large quantities for new purposes. A place like Lombard Street, where in all but the rarest times money can be always obtained upon good security or upon decent prospects of probable gain, is a luxury which no country has ever enjoyed with even comparable equality before.

But though these occasional loans to new enterprises and foreign States are the most conspicuous instances of the power of Lombard Street, they are not by any means the most remarkable or the most important use of that power. English trade is carried on upon borrowed capital to an extent of which few foreigners have an idea, and none of our ancestors could have conceived. In every district small traders have arisen, who 'discount their bills' largely, and with the capital so borrowed, harass and press upon, if they do not eradicate, the old capitalist. The new trader has obviously an immense advantage in the struggle of trade. If a merchant have 50,000 L. all his own, to gain 10 per cent on it he must make 5,000 L. a year, and must charge for his goods accordingly; but if another has only 10,000 L., and borrows 40,000 L. by discounts (no extreme instance in our modern trade), he has the same capital of 50,000 L. to use, and can sell much cheaper. If the rate at which he borrows

be 5 per cent., he will have to pay 2,000 L. a year; and if, like the old trader, he make 5,000 L. a year, he will still, after paying his interest, obtain 3,000 L. a year, or 30 per cent, on his own 10,000 L. As most merchants are content with much less than 30 per cent, he will be able, if he wishes, to forego some of that profit, lower the price of the commodity, and drive the old-fashioned trader—the man who trades on his own capital—out of the market. In modern English business, owing to the certainty of obtaining loans on discount of bills or otherwise at a moderate rate of interest, there is a steady bounty on trading with borrowed capital, and a constant discouragement to confine yourself solely or mainly to your own capital.

This increasingly democratic structure of English commerce is very unpopular in many quarters, and its effects are no doubt exceedingly mixed. On the one hand, it prevents the long duration of great families of merchant princes, such as those of Venice and Genoa, who inherited nice cultivation as well as great wealth, and who, to some extent, combined the tastes of an aristocracy with the insight and verve of men of business. These are pushed out, so to say, by the dirty crowd of little men. After a generation or two they retire into idle luxury. Upon their immense capital they can only obtain low profits, and these they do not think enough to compensate them for the rough companions and rude manners they must meet in business. This constant levelling of our commercial houses is, too, unfavourable to commercial morality. Great firms, with a reputation which they have received from the past, and which they wish to transmit to the future, cannot be guilty

of small frauds. They live by a continuity of trade, which detected fraud would spoil. When we scrutinise the reason of the impaired reputation of English goods, we find it is the fault of new men with little money of their own, created by bank 'discounts.' These men want business at once, and they produce an inferior article to get it. They rely on cheapness, and rely successfully.

But these defects and others in the democratic structure of commerce are compensated by one great excellence. No country of great hereditary trade, no European country at least, was ever so little 'sleepy,' to use the only fit word, as England; no other was ever so prompt at once to seize new advantages. A country dependent mainly on great 'merchant princes' will never be so prompt; their commerce perpetually slips more and more into a commerce of routine. A man of large wealth, however intelligent, always thinks, more or less 'I have a great income, and I want to keep it. If things go on as they are I shall certainly keep it; but if they change I may not keep it.' Consequently he considers every change of circumstance a 'bore,' and thinks of such changes as little as he can. But a new man, who has his way to make in the world, knows that such changes are his opportunities; he is always on the look-out for them, and always heeds them when he finds them. The rough and vulgar structure of English commerce is the secret of its life; for it contains 'the propensity to variation,' which, in the social as in the animal kingdom, is the principle of progress.

In this constant and chronic borrowing, Lombard Street is the great go-between. It is a sort of standing broker between quiet saving districts of the country and the active

employing districts. Why particular trades settled in particular places it is often difficult to say; but one thing is certain, that when a trade has settled in any one spot, it is very difficult for another to oust it—impossible unless the second place possesses some very great intrinsic advantage. Commerce is curiously conservative in its homes, unless it is imperiously obliged to migrate. Partly from this cause, and partly from others, there are whole districts in England which cannot and do not employ their own money. No purely agricultural county does so. The savings of a county with good land but no manufactures and no trade much exceed what can be safely lent in the county. These savings are first lodged in the local banks, are by them sent to London, and are deposited with London bankers, or with the bill brokers. In either case the result is the same. The money thus sent up from the accumulating districts is employed in discounting the bills of the industrial districts. Deposits are made with the bankers and bill brokers in Lombard Street by the bankers of such counties as Somersetshire and Hampshire, and those bill brokers and bankers employ them in the discount of bills from Yorkshire and Lancashire. Lombard Street is thus a perpetual agent between the two great divisions of England, between the rapidly-growing districts, where almost any amount of money can be well and easily employed, and the stationary and the declining districts, where there is more money than can be used.

This organisation is so useful because it is so easily adjusted. Political economists say that capital sets towards the most profitable trades, and that it rapidly leaves the less

profitable and non-paying trades. But in ordinary countries this is a slow process, and some persons who want to have ocular demonstration of abstract truths have been inclined to doubt it because they could not see it. In England, however, the process would be visible enough if you could only see the books of the bill brokers and the bankers. Their bill cases as a rule are full of the bills drawn in the most profitable trades, and *caeteris paribus* and in comparison empty of those drawn in the less profitable. If the iron trade ceases to be as profitable as usual, less iron is sold; the fewer the sales the fewer the bills; and in consequence the number of iron bills in Lombard street is diminished. On the other hand, if in consequence of a bad harvest the corn trade becomes on a sudden profitable, immediately 'corn bills' are created in great numbers, and if good are discounted in Lombard Street. Thus English capital runs as surely and instantly where it is most wanted, and where there is most to be made of it, as water runs to find its level.

This efficient and instantly-ready organisation gives us an enormous advantage in competition with less advanced countries—less advanced, that is, in this particular respect of credit. In a new trade English capital is instantly at the disposal of persons capable of understanding the new opportunities and of making good use of them. In countries where there is little money to lend, and where that little is lent tardily and reluctantly, enterprising traders are long kept back, because they cannot at once borrow the capital, without which skill and knowledge are useless. All sudden trades come to England, and in so doing often disappoint both rational probability and the predictions of philosophers.

The Suez Canal is a curious case of this. All predicted that the canal would undo what the discovery of the passage to India round the Cape effected. Before that all Oriental trade went to ports in the South of Europe, and was thence diffused through Europe. That London and Liverpool should be centres of East Indian commerce is a geographical anomaly, which the Suez Canal, it was said, would rectify. 'The Greeks,' said M. de Tocqueville, 'the Styrians, the Italians, the Dalmatians, and the Sicilians, are the people who will use the Canal if any use it.' But, on the contrary, the main use of the Canal has been by the English. None of the nations named by Tocqueville had the capital, or a tithe of it, ready to build the large screw steamers which alone can use the Canal profitably. Ultimately these plausible predictions may or may not be right, but as yet they have been quite wrong, not because England has rich people—there are wealthy people in all countries—but because she possesses an unequalled fund of floating money, which will help in a moment any merchant who sees a great prospect of new profit.

And not only does this unconscious 'organisation of capital,' to use a continental phrase, make the English specially quick in comparison with their neighbours on the continent at seizing on novel mercantile opportunities, but it makes them likely also to retain any trade on which they have once regularly fastened. Mr. Macculloch, following Ricardo, used to teach that all old nations had a special aptitude for trades in which much capital is required. The interest of capital having been reduced in such countries, he argued, by the necessity of continually resorting to inferior

soils, they can undersell countries where profit is high in all trades needing great capital. And in this theory there is doubtless much truth, though it can only be applied in practice after a number of limitations and with a number of deductions of which the older school of political economists did not take enough notice. But the same principle plainly and practically applies to England, in consequence of her habitual use of borrowed capital. As has been explained, a new man, with a small capital of his own and a large borrowed capital, can undersell a rich man who depends on his own capital only. The rich man wants the full rate of mercantile profit on the whole of the capital employed in his trade, but the poor man wants only the interest of money (perhaps not a third of the rate of profit) on very much of what he uses, and therefore an income will be an ample recompense to the poor man which would starve the rich man out of the trade. All the common notions about the new competition of foreign countries with England and its dangers—notions in which there is in other aspects much truth require to be reconsidered in relation to this aspect. England has a special machinery for getting into trade new men who will be content with low prices, and this machinery will probably secure her success, for no other country is soon likely to rival it effectually.

There are many other points which might be insisted on, but it would be tedious and useless to elaborate the picture. The main conclusion is very plain—that English trade is become essentially a trade on borrowed capital, and that it is only by this refinement of our banking system that we are

able to do the sort of trade we do, or to get through the quantity of it.

But in exact proportion to the power of this system is its delicacy I should hardly say too much if I said its danger. Only our familiarity blinds us to the marvellous nature of the system. There never was so much borrowed money collected in the world as is now collected in London. Of the many millions in Lombard street, infinitely the greater proportion is held by bankers or others on short notice or on demand; that is to say, the owners could ask for it all any day they please: in a panic some of them do ask for some of it. If any large fraction of that money really was demanded, our banking system and our industrial system too would be in great danger.

Some of those deposits too are of a peculiar and very distinct nature. Since the Franco-German war, we have become to a much larger extent than before the Bankers of Europe. A very large sum of foreign money is on various accounts and for various purposes held here. And in a time of panic it might be asked for. In 1866 we held only a much smaller sum of foreign money, but that smaller sum was demanded and we had to pay it at great cost and suffering, and it would be far worse if we had to pay the greater sums we now hold, without better resources than we had then.

It may be replied, that though our instant liabilities are great, our present means are large; that though we have much we may be asked to pay at any moment, we have very much always ready to pay it with. But, on the contrary, there is no country at present, and there never was any country before, in which the ratio of the cash reserve to the

bank deposits was so small as it is now in England. So far from our being able to rely on the proportional magnitude of our cash in hand, the amount of that cash is so exceedingly small that a bystander almost trembles when he compares its minuteness with the immensity of the credit which rests upon it.

Again, it may be said that we need not be alarmed at the magnitude of our credit system or at its refinement, for that we have learned by experience the way of controlling it, and always manage it with discretion. But we do not always manage it with discretion. There is the astounding instance of Overend, Gurney, and Co. to the contrary. Ten years ago that house stood next to the Bank of England in the City of London; it was better known abroad than any similar firm known, perhaps, better than any purely English firm. The partners had great estates, which had mostly been made in the business. They still derived an immense income from it. Yet in six years they lost all their own wealth, sold the business to the company, and then lost a large part of the company's capital. And these losses were made in a manner so reckless and so foolish, that one would think a child who had lent money in the City of London would have lent it better. After this example, we must not confide too surely in long-established credit, or in firmly-rooted traditions of business. We must examine the system on which these great masses of money are manipulated, and assure ourselves that it is safe and right.

But it is not easy to rouse men of business to the task. They let the tide of business float before them; they make money or strive to do so while it passes, and they are

unwilling to think where it is going. Even the great collapse of Overends, though it caused a panic, is beginning to be forgotten. Most men of business think—'Anyhow this system will probably last my time. It has gone on a long time, and is likely to go on still.' But the exact point is, that it has not gone on a long time. The collection of these immense sums in one place and in few hands is perfectly new. In 1844 the liabilities of the four great London Joint Stock Banks were 10,637,000 L.; they now are more than 60,000,000 L. The private deposits of the Bank of England then were 9,000,000 L.; they now are 8,000,000 L. There was in throughout the country but a fraction of the vast deposit business which now exists. We cannot appeal, therefore, to experience to prove the safety of our system as it now is, for the present magnitude of that system is entirely new. Obviously a system may be fit to regulate a few millions, and yet quite inadequate when it is set to cope with many millions. And thus it may be with 'Lombard Street,' so rapid has been its growth, and so unprecedented is its nature.

I am by no means an alarmist. I believe that our system, though curious and peculiar, may be worked safely; but if we wish so to work it, we must study it. We must not think we have an easy task when we have a difficult task, or that we are living in a natural state when we are really living in an artificial one. Money will not manage itself, and Lombard street has a great deal of money to manage.

CHAPTER II.

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A General View of Lombard Street.

I.

The objects which you see in Lombard Street, and in that money world which is grouped about it, are the Bank of England, the Private Banks, the Joint Stock Banks, and the bill brokers. But before describing each of these separately we must look at what all have in common, and at the relation of each to the others.

The distinctive function of the banker, says Ricardo, 'begins as soon as he uses the money of others;' as long as he uses his own money he is only a capitalist. Accordingly all the banks in Lombard Street (and bill brokers are for this purpose only a kind of bankers) hold much money belonging to other people on running account and on deposit. In continental language, Lombard Street is an organization of credit, and we are to see if it is a good or bad organization in its kind, or if, as is most likely, it turn out to be mixed, what are its merits and what are its defects?

The main point on which one system of credit differs from another is 'soundness.' Credit means that a certain confidence is given, and a certain trust reposed. Is that trust

justified? and is that confidence wise? These are the cardinal questions. To put it more simply—credit is a set of promises to pay; will those promises be kept? Especially in banking, where the 'liabilities,' or promises to pay, are so large, and the time at which to pay them, if exacted, is so short, an instant capacity to meet engagements is the cardinal excellence.

All which a banker wants to pay his creditors is a sufficient supply of the legal tender of the country, no matter what that legal tender may be. Different countries differ in their laws of legal tender, but for the primary purposes of banking these systems are not material. A good system of currency will benefit the country, and a bad system will hurt it. Indirectly, bankers will be benefited or injured with the country in which they live; but practically, and for the purposes of their daily life, they have no need to think, and never do think, on theories of currency. They look at the matter simply. They say 'I am under an obligation to pay such and such sums of legal currency; how much have I in my till, or have I at once under my command, of that currency?' In America, for example, it is quite enough for a banker to hold 'greenbacks,' though the value of these changes as the Government chooses to enlarge or contract the issue. But a practical New York banker has no need to think of the goodness or badness of this system at all; he need only keep enough 'greenbacks' to pay all probable demands, and then he is fairly safe from the risk of failure.

By the law of England the legal tenders are gold and silver coin (the last for small amounts only), and Bank of England notes. But the number of our attainable bank notes

is not, like American 'greenbacks,' dependent on the will of the State; it is limited by the provisions of the Act of 1844. That Act separates the Bank of England into two halves. The Issue Department only issues notes, and can only issue 15,000,000 L. on Government securities; for all the rest it must have bullion deposited. Take, for example an account, which may be considered an average specimen of those of the last few years—that for the last week of 1869:

An account pursuant to the Act 7th and 8th Victoria, cap. 32, for the week ending on Wednesday, the 29th day of December, 1869.

ISSUE DEPARTMENT.

Notes issued 33,288,640 L| Government debt 11,015,100 L
| Other securities 3,984,900 L
| Gold coin and bullion 18,288,640 L
| Silver bullion
33,288,640| 33,288,640 L

BANKING DEPARTMENT.

Proprietors' capital 14,553,000 L| Government Securities 13,811,953 L
Rest 3,103,301 L| Other securities 19,781,988 L
Public deposits, | Notes 10,389,690 L
including Exchequer, | Gold and silver coins 907,982 L
Savings' Banks, |
Commissioners of |
National Debt, |
and dividend |

accounts 8,585,215 L|
Other deposits 18,204,607 L|
Seven-day and other |
bills 445,490 L|
44,891,613 L| 44,891,613 L

GEO. FORBES, Chief Cashier.

Dated the 30th December, 1869.

There are here 15,000,000 L. bank notes issued on securities, and 18,288,640 L. represented by bullion. The Bank of England has no power by law to increase the currency in any other manner. It holds the stipulated amount of securities, and for all the rest it must have bullion. This is the 'cast iron' system—the 'hard and fast' line which the opponents of the Act say ruins us, and which the partizans of the Act say saves us. But I have nothing to do with its expediency here. All which is to my purpose is that our paper 'legal tender,' our bank notes, can only be obtained in this manner. If, therefore, an English banker retains a sum of Bank of England notes or coin in due proportion to his liabilities, he has a sufficient amount of the legal tender of this country, and he need not think of anything more.

But here a distinction must be made. It is to be observed that properly speaking we should not include in the 'reserve' of a bank 'legal tenders,' or cash, which the Bank keeps to transact its daily business. That is as much a part of its daily stock-in-trade as its desks or offices; or at any rate, whatever words we may choose to use, we must carefully distinguish between this cash in the till which is wanted every day, and the safety-fund, as we may call it, the

special reserve held by the bank to meet extraordinary and unfrequent demands.

What then, subject to this preliminary explanation, is the amount of legal tender held by our bankers against their liabilities? The answer is remarkable, and is the key to our whole system. It may be broadly said that no bank in London or out of it holds any considerable sum in hard cash or legal tender (above what is wanted for its daily business) except the Banking Department of the Bank of England. That department had on the 29th day of December, 1869, liabilities as follows:

Public deposits 8,585,000 L
Private deposits 18,205,000 L
Seven-day and other bills 445,000 L
———————
Total 27,235,000 L

and a cash reserve of 11,297,000 L. And this is all the cash reserve, we must carefully remember, which, under the law, the Banking Department of the Bank of England—as we cumbrously call it the Bank of England for banking purposes—possesses. That department can no more multiply or manufacture bank notes than any other bank can multiply them. At that particular day the Bank of England had only 11,297,000 L. in its till against liabilities of nearly three times the amount. It had 'Consols' and other securities which it could offer for sale no doubt, and which, if sold, would augment its supply of bank notes—and the relation of such securities to real cash will be discussed presently; but of real cash, the Bank of England for this

purpose—the banking bank—had then so much and no more.

And we may well think this a great deal, if we examine the position of other banks. No other bank holds any amount of substantial importance in its own till beyond what is wanted for daily purposes. All London banks keep their principal reserve on deposit at the Banking Department of the Bank of England. This is by far the easiest and safest place for them to use. The Bank of England thus has the responsibility of taking care of it. The same reasons which make it desirable for a private person to keep a banker make it also desirable for every banker, as respects his reserve, to bank with another banker if he safely can. The custody of very large sums in solid cash entails much care, and some cost; everyone wishes to shift these upon others if he can do so without suffering. Accordingly, the other bankers of London, having perfect confidence in the Bank of England, get that bank to keep their reserve for them.

The London bill brokers do much the same. Indeed, they are only a special sort of bankers who allow daily interest on deposits, and who for most of their money give security. But we have no concern now with these differences of detail. The bill brokers lend most of their money, and deposit the remnant either with the Bank of England or some London banker. That London banker lends what he chooses of it, the rest he leaves at the Bank of England. You always come back to the Bank of England at last. But those who keep immense sums with a banker gain a convenience at the expense of a danger. They are liable to lose them if the bank fail. As all other bankers keep their banking reserve at the

Bank of England, they are liable to fail if it fails. They are dependent on the management of the Bank of England in a day of difficulty and at a crisis for the spare money they keep to meet that difficulty and crisis. And in this there is certainly considerable risk. Three times 'Peel's Act' has been suspended because the Banking Department was empty. Before the Act was broken—

In 1847, the Banking Department was reduced to L 1,994,000 1857 " " L 1,462,000 1866 " " L 3,000,000

In fact, in none of those years could the Banking Department of the Bank of England have survived if the law had not been broken. Nor must it be fancied that this danger is unreal, artificial, and created by law. There is a risk of our thinking so, because we hear that the danger can be cured by breaking an Act; but substantially the same danger existed before the Act. In 1825, when only coin was a legal tender, and when there was only one department in the Bank, the Bank had reduced its reserve to 1,027,000 L., and was within an ace of stopping payment.

But the danger to the depositing banks is not the sole or the principal consequence of this mode of keeping the London reserve. The main effect is to cause the reserve to be much smaller in proportion to the liabilities than it would otherwise be. The reserve of the London bankers being on deposit in the Bank of England, the Bank always lends a principal part of it. Suppose, a favourable supposition, that the Banking Department holds more than two-fifths of its liabilities in cash—that it lends three-fifths of its deposits and retains in reserve only two-fifths. If then the aggregate of the bankers' deposited reserve be 5,000,000 L.,

3,000,000 L. of it will be lent by the Banking Department, and 2,000,000 L. will be kept in the till. In consequence, that 2,000,000 L. is all which is really held in actual cash as against the liabilities of the depositing banks. If Lombard Street were on a sudden thrown into liquidation, and made to pay as much as it could on the spot, that 2,000,000 L. would be all which the Bank of England could pay to the depositing banks, and consequently all, besides the small cash in the till, which those banks could on a sudden pay to the persons who have deposited with them.

We see then that the banking reserve of the Bank of England—some 10,000,000 L. on an average of years now, and formerly much less—is all which is held against the liabilities of Lombard Street; and if that were all, we might well be amazed at the immense development of our credit system—in plain English, at the immense amount of our debts payable on demand, and the smallness of the sum of actual money which we keep to pay them if demanded. But there is more to come. Lombard Street is not only a place requiring to keep a reserve, it is itself a place where reserves are kept. All country bankers keep their reserve in London. They only retain in each country town the minimum of cash necessary to the transaction of the current business of that country town. Long experience has told them to a nicety how much this is, and they do not waste capital and lose profit by keeping more idle. They send the money to London, invest a part of it in securities, and keep the rest with the London bankers and the bill brokers. The habit of Scotch and Irish bankers is much the same. All their spare money is in London, and is invested as all other London

money now is; and, therefore, the reserve in the Banking Department of the Bank of England is the banking reserve not only of the Bank of England, but of all London—and not only of all London, but of all England, Ireland, and Scotland too.

Of late there has been a still further increase in our liabilities. Since the Franco-German war, we may be said to keep the European reserve also. Deposit Banking is indeed so small on the Continent, that no large reserve need be held on account of it. A reserve of the same sort which is needed in England and Scotland is not needed abroad. But all great communities have at times to pay large sums in cash, and of that cash a great store must be kept somewhere. Formerly there were two such stores in Europe, one was the Bank of France, and the other the Bank of England. But since the suspension of specie payments by the Bank of France, its use as a reservoir of specie is at an end. No one can draw a cheque on it and be sure of getting gold or silver for that cheque. Accordingly the whole liability for such international payments in cash is thrown on the Bank of England. No doubt foreigners cannot take from us our own money; they must send here 'value in some shape or other for all they take away. But they need not send 'cash;' they may send good bills and discount them in Lombard Street and take away any part of the produce, or all the produce, in bullion. It is only putting the same point in other words to say that all exchange operations are centering more and more in London. Formerly for many purposes Paris was a European settling-house, but now it has ceased to be so. The note of the Bank of France has not