

SOCIALISM IN ACTION

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CURRENCY
BANKING
AND
FINANCE

1933

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Currency, Banking and Finance

THE official Labour Party Policy on certain aspects of Currency, Banking and Finance is set out in the following Report. The Resolution, which embodies the main principles of the first part of the Report, was adopted by the Annual Conference of the Party held at Leicester in October, 1932. The second part was accepted at the Hastings Conference in October, 1933, in the document entitled "Socialism and the Condition of the People."

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Resolution

This 1932 Annual Conference of the Labour Party, believing that the British trade depression and its resulting unemployment have been considerably aggravated by the deflationary monetary policy pursued in recent years and by the waste and misdirection by the Banks of capital and short credits, that the enormous power exercised by the financial system cannot continue to be left in private control, and that the public control of that system is essential for carrying out a policy of planned National Development and to prevent Socialist policy from being defeated either by active opposition or by passive obstruction from private financial interests—while requesting the National Executive to continue during the coming year its study of the short-term credit problem in close conjunction with the elaboration of plans for the reorganisation of various industries—proposes:

(1) That, in view of the breakdown of the gold standard, the aim of British monetary policy should be to stabilise wholesale prices at a suitable level in this country, to seek by international agreement the largest practicable measure of stability in the rates of foreign exchange, and to safeguard the workers against such exploitation as has been inflicted upon them in recent years by speculators and manipulators.

(2) That the Bank of England and the joint stock banks should be brought under public ownership and control; that the Governor of the Bank should be appointed by the Government and be subject to the general direction of a Minister of Cabinet rank, who should be responsible to the House of Commons for banking and credit policy, the day-to-day business of the Bank being carried on by the Governor and his staff; that the banking system should be managed with a view to utilising available capital and credit resources in accordance with a Socialist plan for the development of industry and international trade and the redistribution of purchasing power; and that with this same object in view, power should be taken to nationalise or control the other finance, acceptance and banking houses.

(3) That a National Investment Board, appointed by the Government on suitable grounds of ability and willingness to carry out loyally the policy set out below, should be set up under the general direction of the appropriate Minister and working in close co-operation with the publicly-owned Bank of England; that with the object of preventing waste and misdirection in the use of long-term capital, the Board should exercise control over all new public issues on the capital market, and its permission should be required before any such new issue could be made; that the Board should be able to refuse "leave to deal" on the Stock Exchange in any issue which, having been rejected as a public issue, had then been placed privately; and that should a Government guarantee be found necessary in order to secure priority for approved schemes of industrial reorganisation, such guarantee should be given on the lines of the Trade Facilities Acts, subject, however, to the acceptance of public control by the industries concerned.

(4) That all necessary emergency powers should be taken to deal with any attempt by private persons or institutions to obstruct the Government, damage national credit, or create a financial panic.

Part I

CURRENCY, BANKING AND FINANCE*

The control of finance stands to-day in the forefront of Labour policy. Bitter experience, in this and other countries, has taught us what disastrous effects monetary disturbances and instability may have upon trade and employment and upon the purchasing power of the people. Since the War, the workers have suffered first from inflation, and then from deflation, both of which were brought about by financial powers and forces completely outside their control. To establish control over this department of our economic life will not, by itself, bring about Socialism, nor raise the workers' standard of life to a proper level. But such control is a necessary foundation of Socialist reconstruction, and without such control the achievement of the Labour Party's aims will be impossible.

I.—CONTROL OF CURRENCY

Until recently, currency has been neglected as a subject of popular attention, owing to the belief that it is both too remote and too complicated. As a result, financial experts have had the field to themselves, and such a muddle have they made of it that a Conservative ex-Chancellor of the Exchequer, Sir Robert Horne, speaking in the House of Commons in May, 1932, said that in consequence it was "a damned close thing whether civilisation would survive." In reality, a sound currency policy is vital to the well-being of every individual in the community, and the general principles underlying it are not difficult to understand in a broad way.

Functions of Currency

Currency has two main functions. It forms a means of exchange and a basis of contracts. Barter, the primitive method of exchange, is a cumbrous business, and becomes well-nigh impossible under the complicated conditions of modern life; it has, therefore, been most conveniently replaced by the use of currency, and trading transactions consist not in exchanging goods for goods or services, but in buying and selling things for money. Even to-day, when currency is in such a muddle, it adequately fulfils its functions as a medium of exchange, provided the transactions are all within one country and are done on the basis of immediate cash payments.

But transactions are not all of this character. Sometimes buyer and seller are not citizens of the same country. The buyer, for instance, may be an Englishman who is paying in pounds sterling, while the seller may be an American selling for dollars. Currency policy, therefore, also concerns itself with the number of dollars and cents which are equivalent to a pound sterling. Sometimes, again, the transaction takes the form of a contract in which the price is not paid at once, but at some future date, perhaps many years hence. Long-term loans, leases, mortgages and a number of commercial transactions are of this character; while wage agreements expressed in terms of money often run for a long period. What concerns the contracting parties in these cases is the purchasing power of money over the period during which the contract runs. If it is fairly constant, in other words if the pound sterling will buy roughly the same basketful of goods when the contract is made and when it is fulfilled, the intentions of the parties will be realised. If it does not do this, if the purchasing power of money substantially changes so that the pound buys either a great deal more or a great deal less as time goes on, then one of the parties makes a gain at the expense of the other.

* Adopted at Labour Party Conference, at Leicester, 1932.

Recent History of World Currencies

Since the War, the currencies of the world have failed to provide either stable exchanges between different countries or stable purchasing power within them. The exchange between Britain and America, which was 4.86 dollars to the pound in 1914, was as low as 3.20 in February, 1920; was put back to 4.86 in 1925 when the British gold standard was restored; went down below 4 dollars when Britain went off gold in September, 1931; and thereafter continued to fluctuate. In 1914, twenty-five French francs bought a pound; in July, 1926, when Britain had gone back to gold and France had not, it took about 200 francs to buy a pound; then later, when France went back to a gold basis, it took 124 francs; and after September, 1931, the rate was below 100 francs. The exchanges of the pound with the currencies of Germany, Austria and other countries have been still more chaotic during the post-War period.

At the same time, not one of the chief world currencies has preserved an even purchasing power. Measured in terms of a selected average of wholesale commodities, the British pound in 1920 was able to buy less than one-third of what it bought in 1914, and in August, 1931, it had risen again until it actually bought 10 per cent. more than in 1914, and about three-and-a-half times what it bought in 1920. That is to say, between 1920 and 1931, wholesale commodities lost, on the average, over two-thirds of their value in terms of money. Similarly, according to the cost-of-living figures, what would have cost 100 shillings in 1914, cost 276 shillings in November, 1920, and 143 shillings in May, 1932. Many foreign currencies have exhibited far greater fluctuations even than these.

These figures exhibit the dual nature of the currency malady from which the world is suffering—the instability of the exchanges and the instability of the price level. When the financial experts of the world met in various international conferences in the years following the War, as, for example, at the Genoa Conference in 1922, they recommended a general return to a gold standard as a means of stabilising the exchanges, and talked about some action to stabilise prices. The first recommendation was generally adopted, but nothing was done about the latter question. Most countries went back to gold; and as the pound, the dollar, the franc, the mark, the lira, etc., each exchanged for a fixed weight of gold, they naturally had a fixed ratio of exchange with one another. But the price level was at the mercy of all sorts of influences, and the financiers took no adequate steps to control it. When prices continually fell, disorganising industry and creating widespread unemployment, the advice given by the bankers was that the peoples must make the necessary “adjustments” to the altered conditions. This was equivalent to saying that man and his affairs were to be the servant of money, and not money the servant of man. Further, as the bankers did not propose to scale down national and international debts, rents, mortgages, or debenture interest, the real meaning of their advice was simply that wages and social services should be cut.

Stable Price Level

So long as Great Britain was on the gold standard she was clamped to the world system of gold-using countries, and no independent action was possible. Now that she is off the gold standard there is freedom to adopt any currency policy which commends itself. What ought that policy to be? In the first place, should main attention be paid to prices or to exchanges?

The Labour Party resolution carried at the Annual Conference, 1931, definitely declared in favour of the former, and this declaration should be adhered to. The reason for this is that, whereas trade may be handicapped by fluctuating exchanges, it risks being substantially destroyed if prices continue to fall as they have been doing during the last few years. The havoc worked by such a fall in prices covers every field of life. It checks manufacture, because

the manufacturer hesitates to produce on a falling market; it creates unemployment; it ruins the producers of food and raw materials; it increases the burden of the national debt; it enriches the rentier class at the expense of the rest of the community; and it drives the debtor nations towards bankruptcy.

It is right, therefore, to direct main attention to the effect of currency policy on the price level. What should be the aim in this? Rapid inflationary or deflationary methods, such as have been disastrously experienced in many countries since the War, are, of course, ruled out; but there are various other possibilities. Should prices go gradually down? Should they go gradually up? Or should average prices, when once they have reached a reasonable level, remain roughly fixed? Each of these schools of thought has its advocates.

Those who want prices to go gradually down, say that this is the proper way to extend to the community as a whole the benefits of man's greater power over nature and production; and that, in particular, if the cost of living is gradually falling, the workers are gradually gaining increases in real wages, even when their money wages remain the same. The obvious objection is that at the same time the rentiers, whether they hold national debt, debentures, mortgages or other fixed charges upon industry, will take a larger and larger share of the national income; while falling prices provide a powerful weapon for wage reductions and against wage increases, so that, on balance, the workers are likely to lose.

The advocates of a gradually rising price level argue that their policy stimulates production, secures good employment, and gradually reduces the share which the rentier class takes from the national income. But a gradual rise in the price level, and therefore in the cost of living, means a gradual fall in the purchasing power of wages, health benefits, old-age pensions and the like, and large surplus profits to the employers. The workers are, therefore, constantly engaged in an uphill struggle to secure increases in wages, benefits and pensions to catch up with rising prices. Moreover, if the rate of increase of prices is rapid, stocks of unused manufactures may be put into storage in anticipation of a further rise; and this may go on until at last a halt is called, prices are broken, and widespread unemployment results.

The third policy is to secure that the average level of prices shall remain as nearly as possible constant, so that the pound shall buy roughly the same basketful of goods to-day, next month, next year and ten years hence. This is to enable money to fulfil its natural function of being a standard of value, just as the yard stick is a standard of length. The workers will know then that if they secure an increase in wages or benefits, they are securing a real increase in the standard of life. At the same time, trade and industry will have reasonable security for the future, instead of being as at present at the mercy of financial gerrymandering. In other words, industry and not the speculators will reap the reward. This is the policy recommended by the Labour Party.

Against this policy it is sometimes argued that it assumes the continuance of a capitalist organisation of industry. It does nothing of the kind. What it does is to say that so long as any capitalist industry exists, a steady level of average prices is an essential step towards steady production, towards setting the workers free from unemployment, and towards restricting anti-social speculation.

Other critics argue that the policy might be a good one, but that it is not possible of achievement.* These critics appear to acknowledge that by contraction of credit, by putting up the bank rate, and by similar means the general price level may be brought down, but they deny that monetary measures of an opposite kind will necessarily be able to put it up. In this

* Of course, it is not possible to secure, by monetary means alone, stability in the prices of particular articles. It is the average, or index number, of prices which it is proposed to stabilise.

contention they forget that a Government has various means at its disposal for attaining its purpose. If it were really true that by no Government action could prices be made to rise, then a Government could win universal popularity by remitting all taxation and spending lavishly out of borrowed money and printing notes. There can really be no doubt at all, as competent economists in many different countries agree, that a Government controlling the monetary system can lower or raise the general level of prices at will. If, therefore, prices are falling it can take action to raise them, and if they rise it can take action to lower them. It can, therefore, continually bring them back to the proper level.

It will be noticed that nothing has so far been said as to the level at which prices should be stabilised. This omission is deliberate, for much will depend upon the circumstances prevailing at the time when Labour policy is put into effect, and upon the movement of prices, wages, etc., in the meantime. The best method of carrying out the policy of stabilisation will be to aim at stabilising the index number of wholesale prices. If this is done, any large fluctuation in retail prices will be prevented; and by appropriate measures for the prevention of profiteering by middlemen, and for the better organisation of retail trade, the present excessive gap between wholesale and retail prices should be narrowed, to the general advantage of the consumers. The consideration of such measures falls outside the scope of this report; but it is clear that in this field the Co-operative Movement can play a very important part, and that every increase in its share of the retail trade of the country will make the problem easier of solution.

Stable Foreign Exchanges

Assuming that price stabilisation be accepted as the object of currency management, it follows that there must be no return to any gold standard of a kind hitherto experienced. There remains, therefore, the question of the foreign exchanges. Can anything be done to prevent fluctuations in these which are liable to cause grave inconvenience to trade? Two separate problems have to be considered. First, day-to-day fluctuations, brought about largely by speculation, should as far as possible be "ironed out" by Governmental action. Secondly, long-term changes in the rates of exchange cannot be prevented by the British Government alone, if its monetary policy is to be directed towards keeping the price level steady;* for if the purchasing power of the pound remains steady while the purchasing power of the dollar goes up, this is bound to be reflected sooner or later in the exchange, by reducing the number of dollars and cents which the pound will buy.

It follows that stable exchanges can only be brought about by international action. Already many nations in practice relate their currencies to the British pound, and others may come into this group. But the policy suggested by the Labour Party is an attempt to secure agreement among all nations to arrive at a common basis by which exchanges may be stabilised at the same time as prices are kept steady. If gold is to enter at all into this, it must be on an entirely different footing from before. And in the view of the Labour Party this country should not give up its freedom of action to keep its own price level constant, until it is completely satisfied that by international action the same result will be achieved.

Control of Financial Machinery

But control of finance, as the Labour Party understands it, is by no means limited to the control, in the social interest, of the purchasing power

* The attitude of the Labour Party towards the Exchange Equalisation Fund, set up under the Finance Act, 1932, is that while the Fund should be used to prevent undesirable day-to-day fluctuations in the exchanges, it should not be used to fix definite rates over a long period, which would be equivalent to returning to the gold standard at a new ratio; the long-term object should be to preserve a steady internal purchasing power for the pound.

of money or of the rates of foreign exchange. The Labour Party also demands such control of the banking and financial institutions of this country as may be necessary for the carrying out of a policy of planned development of the national resources on Socialist lines, for securing sufficient funds for such development, and for preventing Socialist policy from being defeated either by active opposition or by passive obstruction from private financial interests.

II.—THE BANK OF ENGLAND

At the centre of the financial system stands the Bank of England. The capital of this Bank is privately owned; in actual practice, its Governor and Deputy Governor are appointed by the directors of the Bank, while the directors are, in effect, appointed by themselves, re-electing each other from year to year and filling casual vacancies in their own ranks according to their own fancy. Most of the directors are connected with financial houses in the City of London. They are private individuals, responsible to no public authority; and the Bank of England is a private institution, possessing its own Charter and subject to Act of Parliament only as regards currency issues, certain obligations relating to gold, and one or two lesser matters. Except in the most general terms, the Bank's policy may not be debated in Parliament, nor may Parliamentary questions be asked of any Minister of the Crown regarding its actions.

Yet the powers of the Bank of England are enormous. It is the Government's banker, holds the Government balances, makes advances to the Government from time to time, issues Government loans, and administers the service of the National Debt. It also holds the balances of the joint stock banks and likewise the nation's gold reserves. By varying its bank rate, and by its so-called "open market operations" (*i.e.*, by its purchase or sale of securities on a large scale), it can expand or restrict credit and thus increase or diminish employment and bring a strong pressure to bear on rates of wages and the standard of life. The Governor of the Bank is in constant touch with Ministers and with the Treasury; he not only gives advice to the Government on financial questions, but is even understood sometimes to have exercised what amounts, in practice, to a veto on the policy proposed by Ministers. He also exercises a great authority over other powerful financial institutions in the City. The Governor, moreover, through his frequent contacts with the governors of central banks in other countries, and through his nominees on the governing body of the Bank of International Settlements, has great influence on the policy of international finance and indirectly on international politics.

It must be added that both the policy pursued by the Bank of England, and the advice which it has given, have on several important occasions since the War been disastrous to the best interests of the country. Thus, it advised the return to the gold standard in 1925, which Mr. Churchill, who as Chancellor of the Exchequer carried the policy into effect, now admits to have been disastrous;* it has advised and practised both before and since 1925, a policy of deflation which has gone far towards ruining industry and has unduly benefited bondholders and others who live on fixed interest-bearing securities; while it took no effective steps to check the reckless overlending at high rates of interest by City financiers which was the forerunner of the financial crisis in Europe in 1931. Moreover, it was Lord Cunliffe, then Governor of the Bank of England, who encouraged in 1919 by his expert advice the making of those fantastic claims for reparations against Germany which have been the

* "When I was moved by many arguments and forces in 1925 to return to the gold standard, I was assured by the highest experts that we were anchoring ourselves to reality and stability, and I accepted their advice. But what has happened? We have had no reality, no stability. The price of gold has risen since then by more than 70 per cent. . . . Look at the enormously increased volume of commodities which have to be created in order to pay off the same mortgage debt or loan. This monetary convulsion has now reached a pitch where I am persuaded that the producers of new wealth will not tolerate indefinitely so hideous an oppression."—*House of Commons, April 21, 1932.*

source of so much suffering and ill-will in Europe. The Labour Party is entitled to claim, looking back upon these incidents, that its unheeded warnings have been justified by subsequent events.

Those in authority at the Bank of England have, indeed, much expert knowledge and long practical experience in finance, of which a Labour Government should make full use. But they are not infallible supermen, and they should not be permitted either to dictate policy to the Government, or to pursue a policy of their own which, while it may bring distress to countless working-class homes, is outside the control of the Government of the day and shielded from any effective Parliamentary criticism. The declared policy of the Labour Party, that the Bank of England should be publicly owned and controlled, must once more be affirmed.

To give effect to this policy, the Governor of the Bank of England should be appointed by the Government and made subject to the general direction of a Minister of Cabinet rank, who should, in turn, be responsible to the House of Commons for banking and credit policy. Within the broad lines laid down by the Minister, the day-to-day business of the Bank would continue to be carried out by the Governor and his staff. The Minister and the Department who would naturally be responsible for controlling the policy of the Bank would be the Chancellor of the Exchequer and the Treasury; but the question of the distribution of duties between Ministers, and the possibility of the need of creating new Ministries or amalgamating existing Ministries, in order that Socialist policy may be carried out with speed and efficiency, will require careful consideration. The existing shareholders would lose whatever nominal powers of control they still possess and be given, in exchange for their shares, stock bearing a fixed rate of interest. Power should be taken to pay off the stockholders as and when desired.

The Bank of England, thus reorganised on a basis of public ownership and control, should be made, to an even greater degree than it is now, the pivot of the British financial system. It is through the Bank of England that control of other financial institutions can most effectively be operated. Such control is already exercised to a considerable extent, both through financial pressure and through tacit agreement; it should be strengthened and regularised. The practice whereby banks, acceptance houses and other financial institutions look to the Bank of England for assistance when they find themselves in trouble, but are subject to no supervision or control in normal times, must be terminated. Moreover, as the Macmillan Committee on Finance and Industry very properly recommended in 1931, much more statistical and other information regarding their financial activities should be furnished to the Bank of England by the joint stock banks, the acceptance houses, British banks doing business mainly abroad, foreign banks with branch offices in this country, and financial institutions generally, and a large part of this information should be published in an appropriate form by the Bank of England.

III.—CONTROL OF LONG-TERM CREDIT

The Bank of England is not directly concerned with the supply of capital in the form of long-term credit for industry. But it is essential to the success of the Labour Party's policy of industrial reorganisation that effective control of new capital issues should be established. For this purpose, a National Investment Board should be set up, working under general instructions from the Government and in close touch with the Bank of England, but exercising its discretion in regard to particular cases which come before it. It might have a status somewhat similar to that of the Import Duties Advisory Committee under the Import Duties Act, 1932, though Parliamentary approval of its detailed decisions would not be required. Its members would be appointed by the Government on appropriate grounds of ability and willingness to carry out loyally the policy outlined below.

The Board would not deal with the private investment of savings in private businesses, nor with the reinvestment of undistributed profits by public companies in their own businesses, nor with the operations of municipal banks, building societies, co-operative societies or other bodies operating under the Industrial and Provident Societies Acts. But it would exercise control over all new public issues on the capital market, and its permission would be required before any such new issue could be made. It would act, in short, as a licensing authority for new issues, both for home and foreign investment. It would also exercise control over the Stock Exchange to the extent of refusing "leave to deal" in any issue which, having been refused a licence by the Board as a public issue, had then been placed privately.

In deciding whether or not to license a proposed new foreign issue, the Board would be guided by official advice as to the total amount which could be lent abroad without undue disturbance to the foreign exchanges, and by other relevant considerations. The whole question of foreign lending raises large issues of world policy and of international co-operation, and the Board would need to be furnished with a general indication of the Government's policy on these matters. Loans to foreign governments raise special problems, and the Board should be satisfied before agreeing to any such loan that the proceeds would not be spent in undesirable directions, *e.g.*, on armaments. Since such loans raise questions concerning the domestic policy of debtor states, as well as the security of creditors and the development of international trade, they should be the subject of international consultation, and for this purpose some suitable machinery, under the League of Nations, should be set up.

At the present time, the British financial system is better organised for foreign than for home issues, and it would be one of the duties of the National Investment Board to correct this tendency for an excessive proportion of new capital to go abroad, while British industry is starved of resources. It may be advisable for the Treasury to retain the right to control, in case of necessity, the sale and purchase of foreign exchange, in order to strengthen the Board's control over foreign lending.

In deciding whether or not to license a proposed new home issue, the Board would aim at preventing the unnecessary addition of capital to industries that were already over-equipped or the floating of enterprises which were anti-social or otherwise contrary to the interests of the community. Here it would need general guidance from the Government. It would aim at smoothing out undue fluctuations in the demand for capital. It would also aim at checking new issues which seemed likely to compete, for the savings available at any particular time, with the capital requirements of any programme of planned development and industrial reorganisation approved by the Government.

Such a programme must have priority secured to it in the capital market over all less urgent claims. For example, housing schemes should come before dog-racing tracks, new plant for the scientific treatment of coal before new plant for the luxury trades, the establishment of a new industry in a depressed industrial area before the establishment of a new industry in the heart of the countryside. It would be made clear that the fact that the National Investment Board had licensed an application for a new issue, either home or foreign, must not be interpreted as an official invitation to the public to subscribe, still less as a Government guarantee of the interest.

The giving of a Government guarantee in suitable cases, on the lines of the Trade Facilities Acts, may, however, be found to be necessary in order to secure priority for approved projects. Such a guarantee might be given, on the advice either of the National Investment Board or of some body set up to deal specially with the reorganisation of the basic industries, but only on

condition of acceptance by the industry concerned of public control. The principle, moreover, is already accepted, in such cases as road construction, which is largely financed by the motor vehicle duties, and afforestation, which is financed from general taxation, that national development may, under appropriate conditions, be paid for out of revenue rather than by loan. This principle may be capable of further extension, and in so far as it is extended, the need for long-term borrowing will be correspondingly diminished.

IV.—CONTROL OF SHORT-TERM CREDIT

It is clear that an effective policy for the control of finance must extend also to the control of short-term credit so far as the Government's own requirements, and also those of approved schemes of industrial reorganisation and development, are concerned. Where a bank has made large short-term advances, which have become frozen, to depressed industries such as coal, cotton or iron and steel, it must not be allowed to hold up schemes of reorganisation, even if these involve a modification of its favoured creditor position. The possibility cannot be tolerated of the refusal of necessary short-term credits by private financial institutions, which for political reasons might desire to obstruct the carrying out of plans which the Government and the House of Commons had approved, or to damage the national credit, or deliberately to create a financial panic. Opinions may differ as to the probability of such tactics being attempted against a Government resolutely pursuing a constructive Socialist policy for which it had received a clear mandate from the electors. But the next Labour Government should arm itself with strong and comprehensive powers of control, to be brought into operation in the event of any serious attempt being made by its political opponents, whether private persons or institutions, to defeat the will of the electors by any misuse of the financial machine.

The 1932 Annual Conference decided to reaffirm the view expressed by the 1931 Annual Conference in favour of the public ownership and control of the joint stock banks. The 1932 Conference further decided that "the banking system should be managed with a view to utilising available capital and credit resources in accordance with a Socialist plan for the development of industry and international trade and the redistribution of purchasing power; and that with this same object in view, power should be taken to nationalise or control the other finance, acceptance and banking houses." Within the limits of these decisions a further study of certain aspects of the short-term credit question is now being made, in close conjunction with the elaboration of plans for the reorganisation of the various basic industries.

Part II

BANKING, FINANCE AND INVESTMENT*

At the Leicester Conference (1932), on the Policy Report dealing with *Currency, Banking and Finance*, a Resolution was passed, approving the establishment by a Labour Government of a National Investment Board. As was stated in that Report, this measure of control will not, in itself, bring about Socialism, nor raise the workers' standard of life to a proper level; but it is one of the necessary foundations of Socialist reconstruction. For, so long as the power to control finance—that is, to direct wealth along certain channels and to divert it from others—remains mainly in private hands, every attempt to raise the general standard of life be in danger of frustration. The people's representatives, acting in the interests of the community, must therefore take immediate steps to exercise a complete control over finance.

To understand the proposed methods of control, it is necessary first to envisage the failure of the existing system.

NATIONAL INCOME AND EXPENDITURE

The national income equals the national expenditure on consumption, plus national savings.

These savings ought to be fully employed in investment, with a view to the creation of further wealth, so that the next year's income shall be larger, the level of consumption shall rise, and there shall be still further savings available for further investment. This does not happen with any regularity under private capitalism. Because money is forthcoming for investment, not in response to social needs, but only as the expression of the investor's desire to make private profit as quickly and as largely as possible, there is no correspondence between either the amount or the direction of investment, on the one hand, and the benefit to the community on the other.

When savings are not absorbed by the expenditure on capital goods, including additions to stocks, there is less income to spend on the consumption of goods. Thus, the money forthcoming for the purchase of goods falls short of the money spent on their production, and there is a fall in prices and a decline in employment. When the fall in prices occurs, the employer has to meet losses on his stocks or the goods that are in process of being produced, and a proportion of the national savings is required to meet these losses. Once this process is started it gets worse and worse. The more savings are diverted into the mere financing of losses the less are available for fresh investment; the less money available for investment the less expenditure there is on capital goods, and the greater is the decline in prices and employment. Then further money has to be diverted for the meeting of still further losses, and so on. This has been the course of events in the present "slump."

If the opposite occurs, if money is spent on capital goods faster than actual savings are accruing for investment, there comes the opposite result: demand for goods for immediate consumption is greater than immediate supply; there is a rise in prices, profits and employment. This is a "boom," as opposed to a "slump." But because, by its very nature, it implies the existence and manipulation of unreal money (*i.e.*, money to which there is no correspondence in actual consumable goods) it is bound, sooner or later, to break, and it is then followed by a "slump." This alternation of "boom" and "slump," "slump" and "boom," is the normal and inevitable history of capitalist finance.

* Adopted at Labour Party Conference at Hastings, 1933.

The object of the national control of investment is to make investment equal to savings, and to divert investment into socially useful channels; and, further, to ensure that capital and credit are available for carrying through the Government's schemes of development and socialisation, and that such resources are directed in accordance with the economic plan.

To reverse the present "slump" tendency there must be an immediate increase both in consumption and in the expenditure on socially needed capital goods. When there is under-investment on the part of private enterprise, as there is now, the State and Municipal Authorities must fill the gap.

CONTROL OF LONG-TERM CREDIT

As was stated in our Report last year, it is essential to the success of the Labour Party's policy of industrial reconstruction that effective control of new capital issues should be established. It is indeed vital to a planned economy that capital should be directed into those activities, industrial and agricultural, which the general economic plan of the Government demands should be stimulated. It is for this purpose among others that the National Investment Board should be set up.

The Board, which would consist, as the Leicester Conference laid down, of persons chosen on grounds of ability and willingness to carry out the work, would be assisted by a permanent staff of economists, statisticians, etc., and would be essentially an instrument of the Government working under the general directions of the planning committee and of the Minister specially charged with responsibility for the banking and financial system. It would, of course, be in close touch with the Bank of England. While conforming to the general policy laid down, it would adopt the method which it deemed appropriate for the efficient performance of its functions and would have that degree of freedom in making decisions and of exercising its discretion in particular cases which is essential to the operation of any business.

It should constitute, as it were, the general staff of the Government for planning and co-ordinating the mobilisation and allocation of that part of the national wealth which is destined for capital investment.

It should prepare estimates each year of the national income showing what new money is likely to be available for investment. It should consider the schemes of capital expenditure put forward by Government Departments, municipal authorities, public boards and those industries which are to be socialised and to operate under public control. Having made this survey, it should recommend on that basis to the planning committee of the Cabinet a scheme of national investment.

SHORT-TERM CREDIT

At the beginning of the present century, there were about a hundred separate banks in England and Wales receiving deposits from the public and doing ordinary banking business. About half of these, whose deposits amounted to about 25% of the total, had no London office and kept their cash reserves mainly in their own possession or with London agents other than the Bank of England.

The process of Bank amalgamation, however, which was especially rapid during the ten years immediately preceding 1914, resulted in the absorption of practically all the country banks by the "Big Five," and the concentration of their cash reserves in the Bank of England. The process of amalgamation would, undoubtedly, have gone still further, and would have brought about fusions within the "Big Five" themselves if it had not been checked in 1919 by Treasury Order, which forbade any further Bank amalgamations without the permission of the State.

The "Big Five" (Barclays, Lloyds, the Midland, the National Provincial and the Westminster) are thus compelled to maintain their separate existence and to indulge in wasteful competition with one another, especially in the multiplication of unnecessary branches.

Between them these five Joint Stock Banks have something approaching a monopoly of deposit banking in this country, though a number of other banks also receive deposits on a comparatively small scale.

The deposits of British Banks, in April, 1933, were as follows:—

<i>Class of Bank</i>	<i>Number of Banks in this class</i>	<i>Total deposits £ millions</i>
Big Five	5	1,773
Other Clearing Banks	4	176
Country Banks (Lancs, Yorks, etc.) ..	5	128
Banks in the West End of London ..	2	5
Irish Banks	9	198
Scottish Banks	8	271
Total ..	33	2,551

To these may be added nine Co-operative Banks with total deposits of £65,000,000. Deposits are also received by certain private banks, such as Hambros and Barings, and by some of the merchant bankers, but these are relatively small in amount.

DEFECTS OF THE PRESENT SITUATION

The defects of the present situation may be summarised as follows:—

- (1) There is lack of co-ordination between the Joint Stock Banks themselves. Firms or individuals may have banking accounts with more than one bank, and may thus be enabled to conceal their true financial position. This gives opportunities (which should not exist) to financial adventurers. The banks, moreover, have no common policy regarding advances to industry, and act independently of one another in granting credits.
- (2) There is lack of co-ordination between the Joint Stock Banks and the Bank of England. This was emphasised by the Macmillan Committee, who drew attention to its evil effects.*

* See Report of Macmillan Committee (pp. 160-161).

- (3) There is wasteful competition between the banks, particularly as regards the multiplication of branches all over the country. A far larger number of branches exists—and even in some towns a larger number of branches of the same bank—than are necessary to transact the nation's banking business. The number of these branches is still rapidly increasing year by year, without any regard to economic necessity.

The number of branches of the "Big Five" in April, 1933, as compared with April, 1926, is as follows:—

	<i>April,</i> 1933	<i>April,</i> 1926
Barclays	2,080	1,837
Lloyds	1,924	1,686
Midland	2,102	1,850
National Provincial ..	1,371	1,132
Westminster	1,061	918

Many of the branches, moreover, are housed on unnecessarily expensive sites.

In the banks' balance sheets, the value of the branch offices is entered much below their market value. This is one of the methods by which the banks have created hidden reserves.

Each of the "Big Five" has a large and highly-paid directorate, many of the members of which, it may be surmised, contribute little to the formulation of the banks' policy. Thus, Barclays, in 1932, had a central Directorate of forty-four members, Lloyds of thirty-three, the Midland of thirty-three, the National Provincial of twenty-four and the Westminster of twenty-six. In addition, Barclays had ninety-eight local directors and the National Provincial thirty-one. The corresponding figures for the other three are not published. Directors' fees amounted to £304,624 for the year 1931 (Barclays, £93,236; Lloyds, £69,619; Midland, £50,411; National Provincial, £47,581; Westminster, £43,777). These figures do not include Managing-Directors' salaries. Of the above-mentioned Banks, other than the "Big Five," a number are controlled by one or other of the "Big Five." There remain, however, nine or ten independent English and Scottish deposit banks outside the "Big Five." These independent Banks include four of the above-mentioned eight Scottish Banks and four of the five principal Lancashire and Yorkshire Banks. The independent Banks play an important part in Scottish industries and in financing the textile industry.

So heavy are the banks' overhead charges that it is understood that a minimum of 2% has to be charged as interest on advances in order to cover these alone. This explains why, although the bank rate has been reduced to such a low figure, the Joint Stock Banks have refused correspondingly to reduce their interest charges on advances and overdrafts, though they have shown no reluctance in reducing the rate of interest which they allow on deposit accounts. The policy of cheap money has been held up, and in large measure rendered ineffective, by this obstacle of the excessive overhead charges of the Joint Stock Banks.

- (4) There is a lack of social purpose in the use of the banks' resources. There is no co-ordination between public policy and the granting of credits to industry. Advances are often made to speculators and to assist businesses which have no social utility, and are often withheld from socially valuable and financially sound undertakings. The banks, moreover, have shown a lack of enterprise in making advances. The absence of co-ordination between the Bank of England and the Joint Stock Banks may here again be illustrated from another angle. The Bank of England has recently, by its open market operations, been creating additional credit resources for the Joint Stock Banks, but the latter have been failing to make use of them. Thus, in the first quarter of 1933, as compared with that of 1932, the deposits of the clearing banks rose from £1,646,000,000 to £1,915,000,000, but their advances fell from £889,000,000 to £753,000,000. The Joint Stock Banks have thus been pursuing a passive rather than an active policy. They complain that they are unable to find borrowers, but they have made little active effort to do so. Instead of assisting trade recovery, they have been buying and holding gilt-edged securities.

While trade and industry have been impoverished, the banks almost alone have flourished, having maintained high dividends varying from 14 to 18 per cent.

And so, while money is cheap and abnormally plentiful, trade stagnation and unemployment are allowed to continue.

PROPOSALS FOR REMEDYING THESE DEFECTS

These defects are inherent in a competitive system and in current banking practice. In banking, as in other spheres of our economic and financial life, remedies can only be found through Government action and the application of Socialist principles. The following proposals are put forward in the belief that they are practical and that they apply Socialist principles, in their most appropriate form, to the problem of organising short-term credits.

As indicated in our Policy Report on *Currency, Banking and Finance*, issued in 1932, the Party regards it as essential that there should be much closer control by the Central Bank over the Deposit Banks, and much closer co-ordination between their respective activities.

"It is through the Bank of England," the Report stated, "that control of other financial institutions can most effectively be operated. Such control is already exercised to a considerable extent, both through financial pressure and through tacit agreement; it should be strengthened and regularised. The practice, whereby banks, acceptance houses and other financial institutions look to the Bank of England for assistance when they find themselves in trouble, but are subject to no supervision or control in normal times, must be terminated. Moreover, as the Macmillan Committee very properly recommended in 1931, much more statistical and other information regarding their activities should be furnished to the Bank of England by the Joint Stock Banks, the acceptance houses, British banks doing business mainly abroad, foreign banks with branch offices in this country and financial institutions generally."*

With the Bank of England socialised, on the lines already accepted by the Labour Party Conference, such co-ordination and control will become more essential than ever, but if the Joint Stock Banks remain in their present condition, there may be serious difficulty in securing these objects.

* *Currency, Banking and Finance*, page 9.

BANKING CORPORATION

It is proposed, therefore, that the "Big Five" should be amalgamated into a single Banking Corporation, under public ownership and control. The Government should acquire the shares of the "Big Five" and therewith the right to nominate the directors. A comparatively small directorate should be appointed by the Government, on grounds of ability and willingness to carry out the work under the new conditions, in place of the five large existing directorates. A large saving would thus be effected in Directors' fees, part of which could be devoted to the creation of a really efficient statistical and research department, which does not now exist.

The general managers, managers and other staff of the "Big Five" would continue in employment under the new directorate. If, as is very probable, it is found that, after the amalgamation had come into full effect, a smaller staff was required than at present, the reduction should be brought about, not by the dismissal of existing staff, but by stopping new recruitment and by speeding up the process, which is already taking place in the Joint Stock Banks, of retiring the older officials on pension. The overtime now worked by many bank clerks should also be abolished.

The Government would indicate the general lines of banking policy and would require the Banking Corporation to co-operate with the socialised Bank of England and the National Investment Board in giving effect to it, in conformity with the National Plan of Development.

The shares (which represent only 5% of the banks' resources, the remainder being furnished by their depositors) would be acquired on reasonable and equitable terms. The shareholders would have no further power of control over the banks, and they should be paid off as rapidly as possible, the whole transaction to be completed within a given term of years. The proceeds of the sale of redundant branch premises, which should be carried out as circumstances permitted, and should realise a considerable sum, might be used for such repayment.

Public Authorities, both national and local, should have an option to purchase redundant branch premises, which would often be well adapted for use for public purposes.

The directors of the Banking Corporation, though subject to the obligation to co-operate with the Bank of England, the National Investment Board and other financial institutions in carrying out the financial policy of the Government, should have a large measure of discretion in dealing with particular applications for credit, especially from private individuals and firms. It would be both physically impossible and politically undesirable for any Minister of the Crown to attempt to adjudicate between the claims of private individuals or firms to receive overdrafts, or for Parliament to intervene in such questions of detail, though Parliament would, of course, approve the National Plan of Development and would be entitled to discuss and to criticise the general lines of banking policy, as laid down by the responsible Minister. On the other hand, the basic industries of the country must be assured of adequate credits in accordance with the National Plan of Development.

Directors of the Banking Corporation would be required to carry on the business of deposit banking efficiently and to safeguard the interests of their depositors by keeping a sufficient proportion of their assets in liquid and easily realisable form. The position of the depositors will, in fact, be far stronger under the new system, when their money is deposited with a Statutory Corporation, operating under public auspices, than it is at present, when they are dependent on the security of a single private Joint Stock Bank.

To avoid the danger of loss of liquidity by the Banking Corporation, while furnishing the necessary credits for industry, a new credit institution should be created, as recommended by the Macmillan Committee, but under public ownership and control, to grant intermediate credits to approved industries and to agriculture.

It is hoped that the Co-operative Wholesale Bank, which has a special function to perform in financing co-operative trade, will continue to extend its activities in this field under the new system.

Of the banks and financial houses, other than the "Big Five," which now receive deposits, some, including the principal independent Deposit Banks, should obviously be merged in the Banking Corporation. Others, for special reasons, will continue to operate outside the Corporation. Branches of Foreign and Dominion Banks, and those Merchant Banking Houses which receive deposits, would fall into this category. Deposit banking, outside the Banking Corporation, should, however, only be carried on in this country in future on the grant of a licence from the Government so as to ensure that the bank in question co-operated in carrying out the Government's financial policy.

There remain the Discount Houses and the Acceptance Houses. Control over these will be secured through the socialised Bank of England and through the Banking Corporation. A discount house cannot function, unless it is able in case of need to discount its bills at the Central Bank, or to borrow on them from the Central Bank. An acceptance house, in the same way, cannot function unless its bills are taken by the Bank of England, for, unless they are so taken, they will not be bought by discount companies or by the banks. All these institutions now show their balance sheets to the Bank of England and render detailed returns of all their foreign deposits. Moreover, they are at present dependent for part of their funds on the Joint Stock Banks, and would be similarly dependent, under the new system, on the Banking Corporation.

THE LIMITS OF SHORT-TERM CREDIT

The foregoing proposals would bring our institutions for the granting of short-term credit into line with the requirements of a vigorous Socialist policy of planned development of our national resources. In particular, they would provide for proper co-ordination which is now lacking between the Government, the Central Bank, and the institutions responsible for long-term and short-term credit respectively.

It should, however, be observed that, in the execution of a Socialist financial policy, the rôle of short-term credit from the Banks is more limited than is sometimes supposed. It is one of the faults of capitalist finance to rely on short-term credits when these are an unsound method of providing the necessary financial resources. The German financial crisis of 1931, for example, was much intensified by the misuse of short-term credits from abroad, which were employed in many cases to pay for the installation of fixed capital. Some basic industries and services, such as transport, have no need for short-term credit at all. They pay their way as they go, and depend, for development, on long-term credits and on the reinvestment of their own surpluses. Certain other basic industries could, and should, be made largely independent of bank credits, and it should be one of the objects of the financial reconstruction of these industries, on Socialist lines, to bring this about. Fixed plant should be financed by long-term credits; short-term credit should be confined to the provision of working capital from time to time. Socialised industries, moreover, might find it more convenient to finance their short-term requirements largely by inland bills, based on their own credit, rather than by bank overdrafts.

FINANCIAL MIDDLEMEN

The City of London, and the financial world generally, stands in need of drastic reorganisation for the benefit of productive industry. Too many people and too many private financial institutions are getting a living in the City and elsewhere as financial middlemen, many rendering no real social service and some, by anti-social speculation and otherwise, rendering actual disservice to the community. There are too many soft jobs in the City for influential people; too many multiple directorships, carrying fat fees without real functions; too much patronage, based on family and business connections. As recent investigations in America have shown, the world of capitalist finance is dominated by little rings of "insiders" who "skim off the cream" from the labours of others and enrich themselves through a system of illegitimate privilege.

A Labour Government must seek to introduce greater efficiency and greater simplicity into our financial institutions, to squeeze out unnecessary financial middlemen and parasites, and to mobilise to the full all our financial resources and direct them in accordance with social need and Socialist planning.

The financial policy approved at last year's Conference, together with these present proposals, will succeed in carrying out these objects.

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