that it does not want, in order to deprive the outer market of a surplus which depresses discount rates to a dangerous degree —dangerous because of its effects upon the foreign exchanges. The whole operation becomes necessary because of the lack of connection between the bank rate and the market rate. In former days the London money market never had enough money to meet its needs without help from the Bank of England. Bagehot, in his great work "Lombard Street"—published in 1873—said: "At all ordinary moments there is not money enough in Lombard Street to discount all the bills in Lombard Street, without taking some money from the Bank of England."

As long as that was true the Bank rate of discount largely controlled the market rate for money. Since then, however, the credit of Lombard Street has been so greatly extended that the general money market is largely independent of the Bank rate. There are other great banks in London—three of these giant institutions have deposits of more than $500,000,000 each —which nominally can lend at rates below that of the Bank of England. Currency in England consists largely of cheques drawn against deposits which in turn have originated as loans. There is no legal limit whatever to the extent to which these loans and discounts can be multiplied. The only limits imposed are those of publicity and the prudence with which the banks conduct their business. Hence it follows that competition between the great joint-stock banks often impels them to continue to make advances or discount bills at low rates when the Bank of England, as custodian for the English gold reserve, thinks it advisable in the interests of the foreign exchanges to impose a higher rate. This it does by borrowing some of the credit manufactured by the other banks, in order to create an artificial scarcity of money and make its own official rate effective.

In normal times the Bank of England, the Bank of France, and the Imperial Bank of Germany attempt to protect their gold reserves by raising the rate of discount. Upon the declaration of war, France and Germany suspended specie payments, while England continued to meet all obligations in gold. It should be noted that neither England, France nor Germany produces gold; yet — aside from war conditions — none of the banks has any trouble in procuring and maintaining a sufficient gold reserve. The Bank of England, for instance, has an unwritten rule that the minimum of its reserve against liabilities shall be in the neighborhood of 40 per cent. By a conservative reduction of loans the Bank increases the percentage of reserves to liabilities; and the void left by the loans