

John Law, Banker and Economist

1. — Of recent years, the ferment of new ideas set in motion by Keynes has led to a number of attempts to re-assess John Law's position, in some cases even with apologetic overtones, as if his rehabilitation as an economist and a banker was now overdue.

It is no accident if Schumpeter, in his *History of Economic Analysis*, has given prominence to Law's ideas, as a theoretician of cartalism and as an advocate of the view that the economy of a large country can be controlled by the manipulation of financial levers. And not by chance has Harsin continued, for over a score of years, to devote his learned researches to the exhumation of Law's works and has even held out hopes of supplying « une histoire approfondie et peut-être définitive du système », together with a « biographie détaillée » of the Scotsman's versatile figure (1).

In the meantime a detailed biography of Law, the « banker », has come out in Italy. It is by Magri who gives a workmanlike and well balanced overall picture of Law's life, works and writings (2).

Magri's study breathes a spirit of calm, unruffled objectivity. He portrays Law as « half revolutionary, half reactionary » and as « a chaotic mixture of good and evil, of genius and folly ». This judgment, in contrast to the apologetic overtones referred to above, makes it even more essential to go deeper into the good and bad sides in his make up, to start the ball rolling again, as will be my endeavour, in a discussion of several of Law's most characteristic thoughts and actions.

(1) In the « Préface » and the « Introduction » to Law's *Oeuvres Complètes*, 1934 (pp. v and xi).

(2) S. MAGRI's, *La strana Vita del Banchiere Law (The Strange Life of Banker Law)*, 1956.

2. — In John Law, as in most people, thought and action influence each other, since both are indissolubly interwoven. The « banker's » mistakes in practice can be traced back to the « writer's » mistaken conceptions. Conversely, the writer's vogue, the present eagerness to exhume and evaluate everything he wrote, is mainly due to his notoriety as the inventor of the « system ». In reality, it cannot be said that, from the point of view of the history of economic theory (especially if interpreted in « Schumpeterian » terms as the history of analysis, theorems and models), his voluminous writings subsequent to « Money and Trade » (1705) broke fresh ground, at least as regards money and credit (3). To grasp Law's thought, therefore, we may confine our attention to « Money and Trade ». And it may even be sufficient, and indeed more to the point, to consider only the two basic ideas, which, as we shall see, constitute the fabric of his thought and which crop up on almost every page.

By the same token, I do not feel that we shall be making a contribution to the more accurate understanding of Law's « originality » and « fertility » (4) if we attach overmuch importance to Law's defence, in that work, of an « ideal » currency with a constant purchasing power. The price revolution caused by the flood of precious metals from the Americas had brought home the instability of the purchasing power of gold and silver, a point which had been stressed by Bodin in his well known *Response to Malestroit* (1568);

(3) With the single exception of the *Mémoire sur l'usage des monnaies* (1707) which (at pp. 191-193) formulates « Law's clause » to which reference is made below in note (11) on p. 99.

(4) In the sense in which JANNACCONE uses these words (in *Moneta e Lavoro*, 1956, p. 159), referring, that is, to Law's « lead over other contemporary thinkers » and to his « survival in posterity » respectively.

and, in taking as his target the stability of the currency's purchasing power, Law was merely echoing a widespread aspiration of the times, indeed « the overriding aspiration of medieval man », as Einaudi (5) puts it « towards the perpetual, the unchanging, the universal, of which the counterpart was a horror of the transient, the mutable, the particular », without, incidentally, realising that this aspiration was then, as now a will of the wisp. It had already been observed by Locke (6) « that it is impossible to have any standing, unalterable measure of the value of things ». The same point was made by Galiani who wrote that « nothing is less to be hoped for than perpetual stability or permanence because that is completely at odds with all kinds of order and the very spirit of nature » (7).

Nor would we be justified in crediting Law with originality and fertility for pointing out that currency devaluations (which at that time were effected by « raising » the value of the actual currency in terms of money of account or by reducing the weight of the actual currency) were of no avail in achieving a favorable balance of trade and hence in increasing the volume of money. However, this point, though doubtless pertinent, is certainly not essential for the development of the central ideas of « Money and Trade ». In any case, it had been expounded at great length a hundred years earlier by Serra in an analysis of this very question of « the causes which may lead to an abundance of gold and silver in kingdoms » (1613). And, if Law did not know of Serra's *Breve Trattato*, he was not unaware that the same thesis had been subsequently proved, concisely by Petty (8) and diffusely by Locke (9). The same

(5) L. EINAUDI, *Teoria della moneta immaginaria nel tempo da Carlomagno alla rivoluzione francese*, in « Rivista di Storia Economica », 1936, p. 17 (produced in *Saggi bibliografici e storici intorno alle dottrine economiche*, 1953, p. 247).

(6) J. LOCKE, *Some Considerations of the Consequences of the Lowering of Interest and Raising the Value of Money*, 1692, p. 75.

(7) F. GALIANI, *Della Moneta*, 1750, p. 99.

(8) W. PETTY, *Quantulumque*, 1682, qu. 8 and 9.

(9) In *Some Considerations*, op. cit., pp. 113 et seq. and also in *Further Considerations Concerning Raising the Value of*

applies to the export bans on money which were generally recognised as being ineffective. Serra, Petty and Locke, among others, do so explicitly (10). And the same point may be made in connection with many other features scattered throughout *Money and Trade* which have induced not a few writers to credit Law with an originality and fertility which he was far from possessing (11).

3. — Law's two main propositions may be deduced from the opening sallies of « Money and Trade »: firstly, his conception of the « influence » of money on the course and development of the economy and, secondly, his interpretation of the « nature » of money, i.e. what it is and what it can become.

As to the first of these points, it must be admitted that Law brings out very clearly whatever was living and vital in the mercant-

Money, 1695, pp. 24 et seq. In *Studies in the Theory of International Trade*, 1937, p. 60, VINER has shown that the effectiveness of raising the value of money had been denied as far back as 1559 by an unknown writer in a *Memorandum on the reasons moving Queen Elizabeth to reform the coinage*.

(10) In chapter II of Part III of the *Breve Trattato*, in qu. 22 of *Quantulumque*, pp. 115-116 of *Some Considerations* and on p. 36 of *Further Considerations* respectively.

(11) This may be illustrated by the typical example of « Law's clause » (concerning the relation between the value of gold and that of silver) which EINAUDI would prefer to attribute to Galiani and to rename « the Galiani clause » (in *Teoria della Moneta immaginaria*, op. cit., pp. 20-21), but which might also be rebaptised as « the Locke clause », since Locke had already shown that it was impossible to fix that relation by law and it could with advantage be settled by the free play of the market (in *Some Considerations*, op. cit., pp. 167-169).

In the same way, Law, in contending that the value of metallic money is not « a purely conventional value imposed by the authorities » (JANNACCONE, *Moneta e Lavoro*, op. cit., p. 161) ended up by taking the same line as Locke, who had in fact brought out that the « intrinsic » value of precious metals is influenced by their use as money, a use legalised, by general « consent », by the authorities (in *Some Considerations*, op. cit., p. 30) as was subsequently admitted by Law in his repeated references to the « added » value attributed to precious metals, precisely because of their use as money. (The term of « imaginary value », criticised by Law, is to be found, every now and then in passing, in the editions of *Some Considerations* later than 1692. That Law's criticism was not « reasonable » had been appreciated by Pagnini in his notes to the Italian translation of Locke's *Considerations* published by Bonducci in 1751, cf. p. 48 of Vol. I. In any case, the question is of very long standing. In footnotes to pp. 63 and 291, of his *History of Economic Analysis* (1954) SCHUMPETER rightly links Locke's conception with that of Aristotle).

ilist outlook which he had absorbed. He showed that money is not just a mere « veil » but an essential element in the « basic » problems of the economy. And in so doing, he acquires a definitely modern touch, so much so that it has been possible to portray him as a « fore-runner » of Keynes (12). For he credits increases in the money supply not only with the expansion of trade but also the growth of production in all sectors through the creation of wider and more intense employment. This was enunciated by him dogmatically, as something beyond question. He tells us so, right from the outset. « As Money increas'd... The Poor and Idle were employ'd, more of the Land was Labour'd, the Product increas'd, Manufactures and Trade improv'd (p. 14) (13).

And he goes on repeating this, almost on every page, up to the end. Law makes no bones about categorically affirming what is implicit in, or hinted at by, other writers in passing.

There are no limits, as he sees it, to the beneficent influence of money. Not only at home, but also in international trade. And this is always brought about by a rise in employment. In domestic trade, there is no doubt that « an Addition to the Money... adds to the National Wealth, eases the country of a number of Poor or Idle, proportioned to the Money added » (p. 16). And in the international field, too, « a greater Addition to the Money will employ yet more People,

(12) By DI FENIZIO in the opening essay in his *Studi Keynesiani* under the heading of « A forerunner; the modernity of Law » (1947). Di Fenizio writes: « If, with the help of Jannaccone, we recall the main phases through which the system passed, but above all if we re-read Law's works in the light of modern economics, and in particular of the latest Keynes, we shall be surprised to find, in works written two hundred years ago, the most up to date insights, arguments and deductions ». And JANNACONE had pointed out, in the dedication to his essay on *Moneta e Lavoro*, op. cit., that the essay itself « retraces, on the basis illustrations, from the monetary doctrines and vicissitudes of the past, aspirations, illusions, problems and theories which the constant ebb and flow of man's thought and action reproduces even today, no doubt with some additional complications, but yet substantially unchanged ».

(13) This and subsequent quotations are taken from the Harsin edition of JOHN Law's, *Oeuvres Complètes* (op. cit.).

or the same People before employed to more Advantage, which, by making a greater or more valuable Export, will make a Ballance due » (p. 18). So that « the effectual way to bring the Ballance to our side is to add to the Money » (p. 158). And conversely, « without some Addition to the Money, tis not to be suppos'd next years Export can be equal to the last; It will lessen as Money has lessen'd; a part of the People then employ'd being now idle; not for want of Inclination to work, or for want of Employers, but for want of Money to employ them with » (p. 46).

In these extracts from Law, and in many others, it is undoubtedly possible to detect « extremely up to date insights, arguments and deductions ». But this does not seem to us to throw any light on the propositions enunciated by Law. On the contrary, it casts a shadow on the recent tendencies to which we have referred. We might even go further and argue that Law's merit consists in making it easier, by the primitive ingenuousness of his reasoning, to identify those errors which it is hard to track down among the twists and turns of recent theories.

4. — One of Law's basic errors was to attach almost exclusive importance to what we would nowadays call « income effects » (more specifically to the effects of increases in the money supply on the productive process mainly as a result of full employment) and hence not to give due weight to the upward trend in prices linked with these increases in the money supply. This is so marked that he gives the impression of not being aware of, or even of meaning to contest, the embryonic « quantity theory » which was not only already in the air in his day but had been consciously formulated in England and elsewhere (14).

Actually, Law was not unaware of, and even less did he contest, the main propositions

(14) In his *Studies*, op. cit., p. 43, Viner contends that Law meant to « attack » the quantity theory. And ANGELL also suggests as much in his *The Theory of International Prices*, 1926, where he writes *inter alia*: « The refutation of the quantity theory, or at least its raw material, is given in Law and Melon » (p. 218).

of the quantity theory. Right at the beginning of « Money and Trade », he warns the reader that « Silver was lyable to a change in its value, as other Goods, from any change in its Quantity, or in the Demand for it » (p. 6). This is a point on which he harps in order to throw into relief the process whereby the mass influx of precious metals had forced down their value (pp. 86 et seq.). The singularity of his position consists rather in imagining that an increase, even an unlimited one, in the money supply could be absorbed by a parallel increase in the demand without giving rise to a considerable decline in its value, or, in other words, to a rise in prices. His error — « le gîte du paralogisme », to use Galiani's typical expression — hinges on his lack of understanding of the nexus between the extension of demand and the diminution in the value of money; that the expansion of demand to the extent that and in so far as it is not linked to an expansion in trade (or to an increase in the need for liquidity), cannot but be connected with a rise in prices (15). It was precisely this lack of understanding which led him, quite logically, to assume that the increase in the quantity of money might exert its influence almost exclusively on the level of the rate of interest while the price level remained almost unchanged. And, given this position which, as we shall see, was entirely his, but entirely wrong, it was easy for him to prove that the effects of the increase in the quantity of money on the productive process might take the form of a continuous

(15) It is in this sense, it would seem, that we should interpret the phrase used by THORNTON in his speech to the House of Commons on the Bullion Report on May 7, 1811 (published as an appendix to the von Hayek edition, 1939, of the *Paper Credit of Great Britain*, 1802): « Law considered security as everything, and quantity as nothing » a phrase which has been so thoroughly analysed by JANNACONE in *Moneta e Lavoro*, op. cit., pp. 71 and 77-78.

In that speech, Thornton added that, while « there might be no bounds to the demand for paper » (or for money in general) « the increasing quantity would contribute to the rise of commodities; and the rise of commodities require, and seem to justify, a still further increase ». So that, in wishing to regulate the quantity of money by reference to demand, Law in fact neglected the influence of quantity on the value of money, considering it, for these purpose, « as nothing ».

crescendo, conferring almost unlimited benefits on the course and on the growth of the economy.

It need only be recalled that, even in his day, people were aware of the numerous advantages to be derived from a low level of the rate of interest which had been regarded even then as the corner-stone of the economy. For if, at the time, people contested the possibility and desirability of effecting the reduction of the rate *ope legis* (i.e. by legislation), they were not unaware, any more than they are today, of the advantages in question, both in the domestic and in the international fields. The only point at issue, then as now, was whether the lowering of the rate of interest was to be regarded as a cause or an effect of the progress of the economy and whether, in any case, the lowering could be effected and maintained by increasing the money supply.

5. — That is what Law had no hesitation in claiming (16). And in his day, other writers, including Locke, had the same standpoint. Locke, however, realised clearly that an increase in the quantity of money had repercussions not only on the level of the rate of interest but also on the level of prices (17). Whereas Law attributed far greater importance to the possibility of lowering the rate of interest by increasing the

(16) In a number of passages in *Money and Trade* (from p. 18 on) and also in the *Mémoire sur les Banques*, December 1715 (at p. 283).

(17) This conception colours his whole outlook as a protagonist of the main tenets of the « quantity theory » (including the concept of the « quickness of circulation »). The dual effects of the variations in the quantity of money is explicitly brought out in *Some Considerations*, op. cit.: « in money there is double value... first as it is capable, by its interest, to yield us such a yearly income... secondly as it is capable, by exchange, to procure us the necessaries or conveniences of life » (pp. 48, 51). And he is well aware that the increase in the money supply cannot but be accompanied by a decline in its value, since he, unlike Law, correctly interprets the connection between the expansion of the demand and the decline in the value of money. For he holds that, « because the desire of money is constantly almost everywhere the same, its vent varies very little » (p. 60). And hence « its quantity alone » (that is, only the quantity offered) « is enough to regulate and determine its value, without considering any proportion between its quantity and vent » (p. 70).

quantity of money, since, as we have seen, he started from the assumption that the increase in the money supply did not affect the price level.

In this respect, Law may rightly be regarded as a typical fore-runner of the recent « monetary theories » of the rate of interest « à la Keynes », which in fact make the same assumption as to the absence of effects on the level of prices and wages. Which, it must be admitted, was not always clear to the supporters of the extreme versions of these theories, on the strength of which politicians have embarked on some none too felicitous experiments in monetary policy such as that of « cheap money » (18).

In any case, after the recent debates on Keynes' theories, it can now be maintained that this neutrality is non-existent, or, to be more precise, is somewhat precarious. So that the influence of the money supply on the interest rate is primarily temporary. That is to say, it lasts just as long as it does not have repercussions on prices and wages (19). And

(18) Of course the knowledge that it was necessary to take into account the level of prices and wages as well was not lacking among the percipient supporters of these theories and still less among their critics. The fact that this is the Achilles' heel of monetary theories of the interest rate has been demonstrated by MODIGLIANI in *Liquidity Preference and the Theory of Investment and Money* (Economica, 1944, reproduced in « Readings in Monetary Theory », 1952). His conclusion is that « the dependence of the rate of interest on the quantity of money is explained only by the assumption of rigid wages » (section 17), so that, « as long as wages are flexible, the long run rate of interest is determined exclusively by real factors » (section 21).

(19) In this context, the following remarks by MARSHALL in *Money, Credit and Commerce* (1923, p. 257) in spite of HICKS' opinion to the contrary (in *Mr. Keynes and the Classics*, 1937) have again become extremely pertinent: « The new currency, or the increase of currency, goes, not to private persons, but to banking centres; and, therefore, it increases the willingness of lenders to lend in the first instance, and lowers the rate of discount. But it afterwards raises prices; and therefore it tends to increase discounts. This later movement is cumulative... Thus, a fall in the purchasing power of money tends, after a while, to raise the rate of discount and the rate of interest on long investments ».

A full demonstration of this point had been provided, over a century before, by THORNTON in *Paper Credit*, op. cit., p. 225, and even earlier by TURGOR in *Réflexions sur la formation et la distribution des richesses*, 1176, para LXXVII, and by

there is certainly no case for ascribing to Law the merit of having erected on such an unsteady basis his conception of the continuous crescendo in the beneficent effects of the quantity of money on the employment of the « Poor and Idle » and, thence, on the course and growth of the economy. And still less can we see any virtue in his view of the influence of the money supply on international trade, since the balance of payments cannot fail to be unfavorably influenced by a trend in prices and wages resulting from the deliberate expansion of the money supply (20).

6. — Thus, his unsound approach, together with his misunderstanding of the connection between the extension of the demand for and the diminution in the value of money, gradually carried Law a very long way in the direction of a « wonderworking » conception of the possibilities of developing the economy by a crescendo of employment in a constantly expanding productive process. A conception which, instead of being based on the « magic » of credit or, to put it more clearly, on the effectiveness of an organic and systematic diffusion of credit through sound institutions, rested almost exclusively on the expansion pure and simple of the quantity of money

HUMB in the essay « Of interest » in *Political Discourses*, 1752. It is also to be found in A. SMITH (*Wealth of Nations*, Book II, Chapter IV) which refers to Law.

(20) In this connection, too, we may recall the work of THORNTON who has shown at great length how unfounded is Law's contention, which is summed up by Thornton as follows (without explicitly mentioning Law's name): « The evil of an unfavorable exchange... arises from an unfavorable balance of trade, and from that only. The way of preventing this evil, or of remedying it, if it unfortunately exists, is to increase the national industry and the way to encourage industry is to give full scope to trade and manufactures by a liberal emission of paper. The balance of trade will not fail to be rendered favorable by that abundance of exportable articles which the labour thus excited must necessarily be supposed to create » (in *Paper Credit*, op. cit., pp. 231 and 245). Thornton's opposition to such contentions is all the more significant since he admits that, generally speaking, « additional industry will be one effect of an extraordinary emission of paper » (p. 237) and later on, more specifically, that « Mr. Law's bank appeared for a time to have a very powerful influence in extending the demand for labour, and in augmenting the visible and bona fide property of the kingdom » (p. 239, footnote).

as the driving force and indeed the only force capable of creating economic progress. So much so as to differentiate him from the mercantilist writers of the age, who, while attaching great importance to money (as the « blood » rather than as the « oil » of the system), were fully conscious of the need for a certain « proportion » between money and the other factors in economic life (ranging from population to international trade) and who even went as far as to lay down the « limits » within which the quantity of money might be considered appropriate for each country (21). As Law saw it, however, there is no room for the concept of an optimum proportion. Or, to be more exact, the word « proportion » which he occasionally uses (22) takes on quite a different meaning under his pen. In this connection his failure to understand the link between the extension of demand and the value of money comes into play. The optimum proportion for him is the one which satisfies demand in full. And so, without realising it, he makes it meaningless. For him proportion (if I may be pardoned a contradiction in terms) is unlimited proportion. So much so that we are justified in saying that he lacks the sense of what is

(21) Locke continually appeals to the idea of « proportion », both in the domestic and the international sphere, in *Some Considerations*, op. cit., from p. 14 on, where he talks of « a certain proportion of money necessary for driving such a proportion of trade », and so on *passim* up to p. 33, where, after pointing out that it is « impossible to estimate the quantity of money needful to trade », he goes on to emit « some probable guess » as to the limits within which the quantities should vary. Similar conjectures had been advanced by PERRY in *Quantulumque*, op. cit., qu. 25. As against this, Law, as noted by JANNACCONE in *Moneta e Lavoro*, op. cit., p. 70, « does not believe that the quantity of money which a country needs can be calculated a priori ». Which, as we see it, is explicable not by Law's realisation that it is impossible to assess the amount exactly but by his failure to understand the limits in the meaning of the word as defined below.

(22) It is to be found at the beginning of *Money and Trade*, in the sense of « the number of people to work proportion'd to the quantity » (p. 14) and in the opposite sense in the *Mémoire sur les Banques* of July 1715, where he contends that « il est nécessaire qu'un Etat ait une certaine quantité de monnaie proportionnée au nombre de ses peuples » (II, 6). But, generally speaking, and particularly when he explains his project, he lays stress on the need to ensure that the quantity of money is maintained « always equal to the Demand for it » (I, 122).

essential in economics: proportions and limits (23).

7. — The negative elements emerging from our analysis so far of the first point in Law's thought are also to be met with in the second characteristic feature, that is, in his conception, of what money is and what it may be.

In this context, Law may be represented as in Schumpeter's *History* — as an « Ancestor of the Idea of a Managed Currency » (24). And it is true that, with far greater mastery than so many other « planners » of new banks launched both before and after him, he demonstrated clearly the advantages of the adoption of a credit money and in addition foreshadowed the possibility and desirability of not anchoring that money to a given weight of metal. For that reason, he may justifiably be credited with the merit of having initiated the theoretical discussion of pure « cartalism », a discussion which, by its subsequent evolution, has made it possible to single out more precisely the « nature » and the « functions » of money (25). And also of having developed cartalism to its extreme degree of « growing logical complexity », to use the felicitous expression of Jannaccone (26), steering a course « among the concepts of money of account, imaginary money and ideal money », postulating as « ideal » the constancy of purchasing power of the monetary unit, rather than the constancy of the quantity of metal of the unit itself (27).

(23) There seems to me all the less case for arguing from the « letter » or from the « spirit » of Law's writings that he is seeking to « solve the problem (of the optimum quantity of money) by laying down explicitly the pre-requisites of full employment of the working population and of the constancy of purchasing power », as JANNACCONE generously interprets it in *Moneta e Lavoro*, op. cit., p. 77.

(24) This is the title given, probably by MARGER, to one of the sections of the *History*, op. cit., devoted to Law (pp. 321-323).

(25) Arguing on the same lines, SCHUMPETER, in opposing cartalism to metallism, takes « it for granted that theoretical metallism is untenable » (in his *History*, op. cit., p. 289, note 5).

(26) In *Moneta e Lavoro*, op. cit., p. 32.

(27) The goal of constant purchasing power was envisaged by Law only in *Money and Trade* and in any case was pos-

As is well known, Law was forced, in his subsequent schemes, from the plan for a Bank at Turin in 1711 to the first time his system was put into practice with the Banque Générale in 1716, to fall back on constant reference to a given weight of metal (the « scudi di banco », i.e. « bank ducats »). In this way he covered the same ground as had been explored in so many other countries by the creation of « bank money ». And he ended up in 1719 by sliding down the inclined plane towards the current monetary unit with a variable metal content (the livre de Tours) when transforming the Banque Générale into the Banque Royale.

8. — Unfortunately, against these merits must be set his lack of appreciation (discussed earlier) of the role of proportions and limits, a deficiency which comes out not only in connection with the influence of the money supply on the course and growth of the economy, but also when he comes to consider what money can be. For he does not realise that the essential condition for the maintenance in being of a system of credit money, especially if not anchored by free convertibility to a given weight of metal, lies in the observation of certain proportions and appropriate limits to the issues of the money itself. In other words, he does not realise that credit money can completely replace metallic money only to the extent that the quantity can be regulated, i.e. limited in relation to demand in any given circumstances. In this connection, too, it is easy to discern his failure to understand the link between the extension of demand and the diminution in the value of money. By taking as a guiding principle for the issue of paper money the maintenance of the quantity of money at a level always equal to

tulated by him not as an objective *per se* but as being subsidiary to his vital aim of the creation of a credit money divorced from a metal base. Not by chance and not without reason does MacLEOD in his *The Theory of Credit* (1891), pp. 656, 658, emphasise that « the essence of Lawism, as we designate the scheme (of John Law), is to base Paper Money upon some other article of value than specie ».

demand (28) he succeeded in ruling out the very limitation which is essential, a *sine qua non*, if credit money is not to lose its value and, ultimately, cease to be able to discharge its monetary functions.

In the arrangements planned by Law, the request for « a good Security » does not really impose any limit on the quantity of money to be issued since it is laid down that the land to be taken as security or to be acquired is put at its current value.

Not unnaturally, almost a century was to elapse before the need for such a limitation was systematically demonstrated, once and for all, by Thornton, who, while proposing « to show the evil of a too great and sudden diminution of our circulating medium », also emphasised the equally harmful « consequences of too great augmentation of it » not only in the domestic sphere but also in international trade (29). And it would be absurd to reproach Law with not having formulated these principles. One can, however, hold it against him that he had no intuition of them

(28) For Law the principle does not admit of any limitation. Whoever asks for money must be satisfied, provided he offers the bank a real estate guarantee or cedes landed property to it. In fact, according to Law: « if the Commission do not give out money when it is demanded, where good Security is offered, 'tis a hardship on the person who is refused and a Loss to the Country: For few, if any, do borrow Money to keep it by them; and if employ'd it brings a Profit to the Nation, tho the Employer loses » (p. 122).

(29) In *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain* (p. 68, ed. cit.).

The basic work of Thornton's has come back into the limelight of late, and quite rightly so. Indeed, his theory is now considered as being more to the point than Ricardo's in the light of modern trends in monetary theory. Thornton's balanced outlook as an economist and as a banker will be evident from the following directives at the end of Chapter XI, where they follow a discussion of, *inter alia*, Law's system: « To limit the total amount of paper issued and to resort for this purpose, whenever the temptation to borrow is strong, to some effectual principle of restriction; in no case, however, materially to diminish the sum in circulation, but to let it vibrate only within certain limits; to afford a slow and cautious extension of it, as the general trade of the kingdom enlarges itself; to allow of some special, though temporary, increase in the event of any extraordinary alarm or difficulty, as the best means of preventing a great demand at home for guineas; and to lean to the side of diminution, in the case of gold going abroad, and the general exchanges continuing long unfavorable; this seems to be the true policy of the directors of an institution circumstanced like that of the Bank of England ».

and that, in any case, he defended criteria for the control of credit money running counter to these principles, which were making headway even in his day. Indeed they had been adumbrated in writings with which he was familiar, such as those of Locke (30) and had also been applied in the experiment which he himself proposed to repeat (31).

9. — The same remarks go for the essence of the two basic points in « Money and Trade » as were made when we discussed the secondary features. To paraphrase a famous dictum, it might be said that what is original in Law's thought is not fertile and what is fertile is not original. In any case, there seem to be no grounds for speaking of his « genius » as an economist, a term used and abused when referring to Law. It only remains to be seen whether, although no genius in that respect, he was as a banker and whether the somewhat severe judgments, especially of « economist bankers » such as Thornton and MacLeod (32) ought not to be given a lower rating than the rather indulgent appreciations of some « non-banker economists » as Nicholson and Harsin (33).

(30) See note (17) to n. 101.

(31) The « Banco del Giro » (Deposit Bank) of Venice was again and again forced to reduce the quantity of bank money (« partite », i.e. deposit items) not because the demand for them had declined but to bring them within the overall limits deemed necessary to safeguard their value, and the financial magistrates frequently expressed themselves to that effect in their relevant reports to the Senate of Venice, as is shown by G. LUZZATTO in *Les banques publiques de Venise* (in « History of the Principal Public Banks », 1934, pp. 68 et seq.).

(32) In the speech to the House of Commons from which we have quoted, Thornton thought himself actually obliged to apologise for mentioning Law's name in the same breath as the Bank of England Directors: « Undoubtedly the name of Mr. Law and that of the present Directors of the Bank ought not to be mentioned on the same day, if the general nature of the two establishments, or the comparative character of the person presiding over them, were the only subject for consideration » (p. 341).

For his part, MacLEOD, who is certainly no stickler for orthodoxy when it comes to credit, has taken an anything but condescending line towards Law whose name he has used, as « Lawism », to dub the various methods of banking considered unacceptable by him (in *The Theory of Credit*, op. cit., Ch. XIII, and in *The Theory and Practice of Banking*, 1955, Ch. XIV).

(33) According to NICHOLSON, in *John Law of Lauriston and the greatest speculative madness in human memory* (Biblio-

One cannot honestly disagree with the latter for having presented some aspects of Law's work in a favorable light or rather, to be more specific, some aspects of his intentions as they emerge from his writings and in particular from the mémoire on the « Restablisement du Commerce » of September 1715, in which there is a diffuse exposition of the « system », its aims and structure (34). And, even if, in this respect, too, caution is indicated in attributing to Law merits of originality (35), it cannot be gainsaid that he had correctly sized up the gravity of the financial and economic situation of France at the end of Louis XIV's reign and that he realised the need to place the State finances on a fresh and sounder basis and to have recourse systematically and on a large

teca dell'Economista, IV Series, 1905), « John Law's system, considered solely as a system of financial and industrial organisation, was a work of genius; and had it not been vitiated by a maleficent principle, which ran counter to its essence, it would have brought to its author's adopted country incalculable benefits » (p. 427). The « maleficent principle » is identified by Nicholson as the « demon of speculation », which, to start with, was the slave of John Law's system but which soon became « its master and its destroyer » (ditto). So that, « but for the extraordinary frenzy of speculation which burst out in Paris at that time, it is not improbable that he would have succeeded, in spite of his errors, in putting his system on a sound basis » (p. 430).

According to HARSIN in *Les doctrines monétaires et financières en France du XVI^e al XVIII^e siècle*, 1928, the failure of the « system » has earned Law the « malédiction des contemporains et la condamnation souvent méprisante de générations d'économistes. Mais chez beaucoup il est permis de croire que l'ignorance ou la mauvaise foi n'a pas été étrangère à la formation d'un tel jugement. Cependant les études les plus sérieuses qui lui ont été consacrées reconnaissent presque toujours une pensée de génie présidant à des conceptions parfois grandioses, une habileté de tacticien et une compétence de réalisateur très peu communes, jointes malheureusement à une trop grande précipitation dans l'exécution et à une indifférence relative quant aux moyens à employer » (pp. 188-9).

(34) First published by HARSIN in Vol. II of the *Oeuvres Complètes*, op. cit.

(35) We need only recall that the attribution to Law of the mémoire on the « Restablisement du Commerce », however probable, is by no means certain. In any case, some suggestions put down in that paper can be traced back to other mémoires of no less « genius » than those which can be definitely attributed to Law. Thus, for instance, in an anonymous *Essai d'un nouveau système sur les finances*, 1715, which Harsin considers cannot be attributed to Law, there is, according to that critic, « un programme que le système allait s'efforcer de réaliser, au moins partiellement » (*Oeuvres*, op. cit., p. xxxix, *Doctrines*, op. cit., pp. 130-134).

scale to credit rather than to the occasional expedients such as those which had hitherto been current. Nevertheless, if, instead of venturing to put the man in the dock, or rather the man's professed intentions, we concentrate on an objective examination of the « system » as it was actually put into effect by Law, we cannot but subscribe to the traditional judgment of the system as — to quote Adam Smith's words — « the most extravagant project of both banking and stock-jobbing that, perhaps, the world ever saw ». It is not really permissible to explain the collapse of the system by Law's « impatience » or by the fact that « the age was not ripe for it » (36). The collapse of the system was inevitable and would have come about sooner or later in any case as a result of its principles and of the course it took, since Law's assumptions in constructing and applying the system were simply wrong. Law's errors an economist could hardly avoid being translated into his failures as a banker.

10. — Moreover, as a banker, he not only put into practice the faulty conceptions developed in his writings as to the influence and nature of money but, in his actions, fell into another basic error which was no less grave, although not expressed in his writings. For

(36) Law himself admitted that he would have been better advised to act « plus lentement mais plus sûrement » (HARSIN, *Doctrines*, op. cit., p. 190, *Oeuvres*, op. cit., pp. 197, 408). And it was precisely the « trop grande précipitation » which appears to have been one of the main reasons for the collapse of the system according to HARSIN and also to JANNACCONE in *Moneta e Lavoro*, op. cit. p. 155.

The suggestion that the crash was due to the « immaturity » of the times is adumbrated by Nicholson and Schumpeter. According to NICHOLSON « history has shown that Law marked out with marvellous prescience the path which credit was to follow to become the driving force of industry in the modern world » (in *John Law*, op. cit., p. 429). According to SCHUMPETER, too, « the Banque Royale and the Compagnie des Indes, which it absorbed, failed because the colonial ventures combined in the latter did not, for the time being, prove to be the source of anything but losses. If these ventures had been successful, Law's grandiose attempt to control and to reform the economic life of a great nation from the financial angle — for this is what his plan eventually amounted to — would have looked very different to his contemporaries and to historians » in (*History*, op. cit., p. 295).

both in his works and his deeds he showed that he was steeped in a « wonder-working » conception, in the former case as regards the effects of the expansion of the money supply and the possibility of satisfying an unlimited demand for money, in the latter case as to the possibility of using bank credits to the point of permitting the resources immobilised in an expansion of real investments to be sustained to an unlimited extent and for an indefinite period by drawing on the credit of a national issuing bank.

Therein, in the last analysis, lay the originality of Law's system. What he had in mind was to carry out, in conjunction with the Compagnie des Indes, a gigantic investment plan which would not only have revived France's overseas trade but would have opened up immense stretches of the new continent. And the execution of this plan should have brought in sufficient profits to put the State's finances on a sound basis and to enrich, at the same time, both sovereign and subjects without calling for any sacrifices in order to effect the savings essential if the investments were to be carried out. For his purpose, he thought it was sufficient to rely on the credit of the Banque Royale, i.e. on a swelling flood of note issues. And, in effect, whereas the shareholders were asked to pay cash for only a ridiculously small part of their holdings, the Company itself was enabled to operate, without quantitative limitation, with the funds provided directly by the Bank through the typical « brainwave » of Law's whereby shares and notes were made interchangeable and both put into circulation as money and as being even preferable to gold. This brainwave which, more than any other statement or action of his, gives the measure of his alleged « genius » as a banker, enabled him to conceal the weakness of his system, i.e. the insufficiency of funds available for investment that had been noted when the Company made its first uncertain steps. But, in this way, the Company's real investments, instead of being fed by « voluntary » savings, linked to a rise

in employment and a parallel increase in real income, were buttressed in the main by the volume of « forced » savings produced by the rise in prices and incomes brought about by the crescendo of note issues. But this forced loan could not in any case go on *ad infinitum*, since the gap between planned investments and the savings available inevitably widened as the inflationary spiral got under way.

11. — What we have said of Law the economist is also valid of him as a banker. His inability to grasp what any modern schoolboy knows cannot, of course, be held against him.

After so many decades of dull discussions, it is now common ground that credit can be created « out of nothing » by mere « confidence », since, on a given base of tangible goods, a credit pyramid may be erected the height of which will vary with the degree of « credit mobilisation » obtaining as between the innumerable operators of the economic system, considered as producers and savers, and also as consumers. But there is also a fairly widely held notion that this creation out of nothing, while exerting a propulsive influence on the process of income formation, especially if the « creation » takes place through the banks, is not enough of itself to sustain the real investments as a stable « counterpart » to them. As a counterpart to the real investments, conceived of concretely as a « fund » of real goods, credits are needed which in their turn are linked to real savings, whatever their origin — whether they are the fruit of farsighted parsimony out of a given income or the fruit of increases, even unforeseen ones, in that income. And there is no escape from this perennial, timeless necessity in running a bank, and still less in administering an issuing house. Even the credit granted by note issues may give stable support to real investments only insofar as they represent (« ex post » although not « ex ante ») real savings.

It is understandable that, in his day, Law should not have realised all this very clearly.

Nevertheless, the people in charge of the main State banks from whom Law had taken his cue in working out his system had long had an intuition of this point. Not by chance and not without some justification had the banks in general (and especially the « deposit and clearing banks » in addition to the « circulation and discount » banks) been subjected to limitations in their operations by prohibitions and restrictions in the granting of credits. So much so that they were forced, or at least pretended to be forced, to observe restraints which turned out to be indefensible, even in the general interest (cf. the typical case of the Bank of Amsterdam). And what we said of Law in connection with monetary policy is also true of credit policy (since both fields are really inseparable parts of the same whole). It certainly does not speak for his alleged genius as a banker that the structure and development of his system were based on criteria incompatible with the principles which have now prevailed and which were already making headway in his time in the very experiments which he had set out to repeat.

12. — All things considered, then, we cannot but be perplexed when confronted of late with repeated attempts to rehabilitate Law.

Law's figure has so many sides to it that each of us may well form our own opinion of him. For my part, I find it impossible to share Harsin's judgment, however authoritative, according to which [as already stated in footnote (33) to page 105] « les études les plus sérieuses qui lui ont été consacrées reconnaissent presque toujours une pensée de génie présidant à des conceptions grandioses, une habileté de tacticien et une compétence de réalisateur très peu communes ». I would rather be tempted to see in him, to use Oudard's expression, « a gentleman adventurer » (37) or, to adopt the concluding expression of Magri « a gentleman financier ». And we should be particularly grateful to

(37) G. OUDARD, *La très curieuse vie de John Law, aventurier honnête homme*, 1927.

Magri for his laudable efforts to provide a strong impetus to the reassessment of Law's writings and work. It is to be hoped that Magri's example will be followed by economists and bankers. The resultant discussion will be all the more fruitful if, while fully appreciating Law's merits as a man, it does not hesitate to recognise that, as an economist and as a banker, he represents only one of

the factors in the perennial dialectics of economic thought and banking operations. As I see it, he is the negative element which is no doubt valid, but valid in the main because it throws into relief, by its very errors, the truths which stand at the opposite pole to the really original aspects of his words and deeds.

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