

Part V

Division of Profit into Interest and Profit of Enterprise. Interest-Bearing Capital

Chapter 29. Component Parts of Bank Capital

It is now necessary to examine the component parts of bank capital in greater detail.

We have just seen that Fullarton and others transform the distinction between money as a medium of circulation and money as a means of payment — also universal money in so far as it concerns a drain of gold — into a distinction between currency and capital.

The peculiar role played by capital in this instance is the reason why bankers' economics teaches that money is indeed capital *par excellence* as insistently as enlightened economics taught that money is not capital.

In subsequent analyses, we shall demonstrate that money-capital is being confused here with moneyed capital in the sense of interest-bearing capital, while in the former sense, money-capital is always merely a transient form of capital — in contradistinction to the other forms of capital, namely, commodity-capital and productive capital.

Bank capital consists of 1) cash money, gold or notes; 2) securities. The latter can be subdivided into two parts: commercial paper or bills of exchange, which run for a period, become due from time to time, and whose discounting constitutes the essential business of the banker; and public securities, such as government bonds, treasury notes, stocks of all kinds, in short, interest-bearing paper which is however significantly different from bills of exchange. Mortgages may also be included here. The capital composed of these tangible component parts can again be divided into the banker's invested capital and into deposits, which constitute his banking capital, or borrowed capital. In the case of banks which issue notes, these must be included. We shall leave the deposits and notes out of consideration for the present. It is evident at any rate that the actual component parts of the banker's capital (money, bills of exchange, deposit currency) remain unaffected whether the various

elements represent the banker's own capital or deposits, *i.e.*, the capital of other people. The same division would remain, whether he were to carry on his business with only his own capital or only with deposited capital.

The form of interest-bearing capital is responsible for the fact that every definite and regular money revenue appears as interest on some capital, whether it arises from some capital or not. The money income is first converted into interest, and from the interest one can determine the capital from which it arises. In like manner, in the case of interest-bearing capital, every sum of value appears as capital as long as it is not expended as revenue; that is, it appears as principal in contrast to possible or actual interest which it may yield.

The matter is simple. Let the average rate of interest be 5% annually. A sum of £500 would then yield £25 annually if converted into interest-bearing capital. Every fixed annual income of £25 may then be considered as interest on a capital of £500. This, however, is and remains a purely illusory conception, except in the case where the source of the £25, whether it be a mere title of ownership or claim, or an actual element of production such as real estate, is directly transferable or assumes a form in which it becomes transferable. Let us take the national debt and wages as illustrations.

The state has to annually pay its creditors a certain amount of interest for the capital borrowed from them. In this case, the creditor cannot recall his investment from his debtor, but can only sell his claim, or his title of ownership. The capital itself has been consumed, *i.e.*, expended by the state. It no longer exists. What the creditor of the state possesses is 1) the state's promissory note, amounting to, say, £100; 2) this promissory note gives the creditor a claim upon the annual revenue of the state, that is, the annual tax proceeds, for a certain amount, *e.g.*, £5 or 5%; 3) the creditor can sell this promissory note of £100 at his discretion to some other person. If the rate of interest is 5%, and the security given by the state is good, the owner A can sell this promissory note, as a rule, to B for £100; for it is the same to B whether he lends £100 at 5% annually, or whether he secures for himself by the payment of £100 an annual tribute from the state amounting to £5. But in all these cases, the capital, as whose offshoot (interest) state payments are considered, is illusory, fictitious capital. Not only that the amount loaned to the state no longer exists, but it was never intended that it be expended as capital, and only by investment as capital could it have been transformed into a self-preserving value. To the original creditor A, the share of annual taxes accruing to him represents interest on his capital, just as the share of the spendthrift's fortune accruing to the usurer appears to the latter, although in both cases the loaned amount was not invested as capital. The possibility of selling the state's promissory note represents for A the potential means of regaining his principal. As for B, his capital is invested,

from his individual point of view, as interest-bearing capital. So far as the transaction is concerned, B has simply taken the place of A by buying the latter's claim on the state's revenue. No matter how often this transaction is repeated, the capital of the state debt remains purely fictitious, and, as soon as the promissory notes become unsaleable, the illusion of this capital disappears. Nevertheless, this fictitious capital has its own laws of motion, as we shall presently see.

We shall now consider labour-power in contrast to the capital of the national debt, where a negative quantity appears as capital—just as interest-bearing capital, in general, is the fountainhead of all manner of insane forms, so that debts, for instance, can appear to the banker as commodities. Wages are conceived here as interest, and therefore labour-power as the capital yielding this interest. For example, if the wage for one year amounts to £50 and the rate of interest is 5%, the annual labour-power is equal to a capital of £1,000. The insanity of the capitalist mode of conception reaches its climax here, for instead of explaining the expansion of capital on the basis of the exploitation of labour-power, the matter is reversed and the productivity of labour power is explained by attributing this mystical quality of interest-bearing capital to labour-power itself. In the second half of the 17th century, this used to be a favourite conception (for example, of Petty), but it is used even nowadays in all seriousness by some vulgar economists and more particularly by some German statisticians.^[1] Unfortunately two disagreeably frustrating facts mar this thoughtless conception. In the first place, the labourer must work in order to obtain this interest. In the second place, he cannot transform the capital-value of his labour-power into cash by transferring it. Rather, the annual value of his labour-power is equal to his average annual wage, and what he has to give the buyer in return through his labour is this same value plus a surplus-value, *i.e.*, the increment added by his labour. In a slave society, the labourer has a capital-value, namely, his purchase price. And when he is hired out, the hirer must pay, in the first place, the interest on this purchase price, and, in addition, replace the annual wear and tear on the capital.

The formation of a fictitious capital is called capitalisation. Every periodic income is capitalised by calculating it on the basis of the average rate of interest, as an income which would be realised by a capital loaned at this rate of interest. For example, if the annual income is £400 and the rate of interest 5%, then the £100 would represent the annual interest on £2,000, and the £2,000 is regarded as the capital-value of the legal title of ownership on the £100 annually. For the person who buys this title of ownership, the annual income of £100 represents indeed the interest on his capital invested at 5%. All connection with the actual expansion process of capital is thus completely lost, and the conception of capital as something with automatic self-expansion properties is thereby strengthened.

Even when the promissory note — the security — does not represent a purely fictitious capital, as it does in the case of state debts, the capital-value of such paper is nevertheless wholly illusory. We have previously seen in what manner the credit system creates associated capital. The paper serves as title of ownership which represents this capital. The stocks of railways, mines, navigation companies, and the like, represent actual capital, namely, the capital invested and functioning in such enterprises, or the amount of money advanced by the stockholders for the purpose of being used as capital in such enterprises. This does not preclude the possibility that these may represent pure swindle. But this capital does not exist twice, once as the capital-value of titles of ownership (stocks) on the one hand and on the other hand as the actual capital invested, or to be invested, in those enterprises. It exists only in the latter form, and a share of stock is merely a title of ownership to a corresponding portion of the surplus-value to be realised by it. A may sell this title to B, and B may sell it to C. These transactions do not alter anything in the nature of the problem. A or B then has his title in the form of capital, but C has transformed his capital into a mere title of ownership to the anticipated surplus-value from the stock capital.

The independent movement of the value of these titles of ownership, not only of government bonds but also of stocks, adds weight to the illusion that they constitute real capital alongside of the capital or claim to which they may have title. For they become commodities, whose price has its own characteristic movements and is established in its own way. Their market-value is determined differently from their nominal value, without any change in the value (even though the expansion may change) of the actual capital. On the one hand, their market-value fluctuates with the amount and reliability of the proceeds to which they afford legal title. If the nominal value of a share of stock, that is, the invested sum originally represented by this share, is £100, and the enterprise pays 10% instead of 5%, then its market-value, everything else remaining equal, rises to £200, as long as the rate of interest is 5%, for when capitalised at 5%, it now represents a fictitious capital of £200. Whoever buys it for £200 receives a revenue of 5% on this investment of capital. The converse is true when the proceeds from the enterprise diminish. The market-value of this paper is in part speculative, since it is determined not only by the actual income, but also by the anticipated income, which is calculated in advance. But assuming the expansion of the actual capital as constant, or where no capital exists, as in the case of state debts, the annual income to be fixed by law and otherwise sufficiently secured, the price of these securities rises and falls inversely as the rate of interest. If the rate of interest rises from 5% to 10%, then securities guaranteeing an income of £5 will now represent a capital of only £50. Conversely, if the rate of interest falls to $2\frac{1}{2}\%$; the same securities will represent a capital of £200. Their value is always merely capitalised income, that is, the income calculated on the basis of a fictitious capital at the prevailing rate of interest. Therefore, when

the money-market is tight these securities will fall in price for two reasons: first, because the rate of interest rises, and secondly, because they are thrown on the market in large quantities in order to convert them into cash. This drop in price takes place regardless of whether the income that this paper guarantees its owner is constant, as is the case with government bonds, or whether the expansion of the actual capital, which it represents, as in industrial enterprises, is possibly affected by disturbances in the reproduction process. In the latter event, there is only still another depreciation added to that mentioned above. As soon as the storm is over, this paper again rises to its former level, in so far as it does not represent a business failure or swindle. Its depreciation in times of crisis serves as a potent means of centralising fortunes.^[2]

To the extent that the depreciation or increase in value of this paper is independent of the movement of value of the actual capital that it represents, the wealth of the nation is just as great before as after its depreciation or increase in value. "The public stocks and canal and railway shares had already by the 23rd of October, 1847, been depreciated in the aggregate to the amount of £114,752,225." (Morris, Governor of the Bank of England, testimony in the Report on Commercial Distress, 1847-48 [No. 3800].) Unless this depreciation reflected an actual stoppage of production and of traffic on canals and railways, or a suspension of already initiated enterprises, or squandering capital in positively worthless ventures, the nation did not grow one cent poorer by the bursting of this soap bubble of nominal money-capital.

All this paper actually represents nothing more than accumulated claims, or legal titles, to future production whose money or capital value represents either no capital at all, as in the case of state debts, or is regulated independently of the value of real capital which it represents.

In all countries based on capitalist production, there exists in this foreman enormous quantity of so-called interest-bearing capital, or moneyed capital. And by accumulation of money-capital nothing more, in the main, is connoted than an accumulation of these claims on production, an accumulation of the market-price, the illusory capital-value of these claims.

A part of the banker's capital is now invested in this so-called interest-bearing paper. This is itself a portion of the reserve capital, which does not perform any function in the actual business of banking. The most important portion of this paper consists of bills of exchange, that is, promises to pay made by industrial capitalists or merchants. For the money-lender these bills of exchange are interest-bearing, in other words, when he buys them, he deducts interest for the time which they still have to run. This is called discounting. It depends on the prevailing rate of interest,

how much of a deduction is made from the sum represented by the bill of exchange.

Finally, the last part of the capital of a banker consists of his money reserve in gold and notes. The deposits, unless tied up by agreement for a certain time, are always at the disposal of the depositors. They are in a state of continual fluctuation. But while one depositor draws on his account, another deposits, so that the general average sum total of deposits fluctuates little during periods of normal business.

The reserve funds of the banks, in countries with developed capitalist production, always express on the average the quantity of money existing in the form of a hoard, and a portion of this hoard in turn consists of paper, mere drafts upon gold, which have no value in themselves. The greater portion of banker's capital is, therefore, purely fictitious and consists of claims (bills of exchange), government securities (which represent spent capital), and stocks (drafts on future revenue). And it should not be forgotten that the money-value of the capital represented by this paper in the safes of the banker is itself fictitious, in so far as the paper consists of drafts on guaranteed revenue (*e.g.*, government securities), or titles of ownership to real capital (*e.g.*, stocks), and that this value is regulated differently from that of the real capital, which the paper represents at least in part; or, when it represents mere claims on revenue and no capital, the claim on the same revenue is expressed in continually changing fictitious money-capital. In addition to this, it must be noted that this fictitious banker's capital represents largely, not his own capital, but that of the public, which makes deposits with him, either interest-bearing or not.

Deposits are always made in money, in gold or notes, or in drafts upon these. With the exception of the reserve fund, which contracts or expands in accordance with the requirements of actual circulation, these deposits are in fact always in the hands of the industrial capitalists and merchants, on the one hand, whose bills of exchange are thereby discounted and who thus receive advances; on the other hand, they are in the hands of dealers in securities (exchange brokers), or in the hands of private parties who have sold their securities, or in the hands of the government (in the case of treasury notes and new loans). The deposits themselves play a double role. On the one hand, as we have just mentioned, they are loaned out as interest-bearing capital and are, therefore, not in the safes of the banks, but figure merely on their books as credits of the depositors. On the other hand, they function merely as such book entries, in so far as the mutual claims of the depositors are balanced by cheques on their deposits and can be written off against each other. In this connection, it is immaterial whether these deposits are entrusted to the same banker, who can thus balance the various accounts against each other,

or whether this is done in different banks, which mutually exchange cheques and pay only the balances to one another.

With the development of interest-bearing capital and the credit system, all capital seems to double itself, and sometimes treble itself, by the various modes in which the same capital, or perhaps even the same claim on a debt, appears in different forms in different hands.^[3] The greater portion of this "money-capital" is purely fictitious. All the deposits, with the exception of the reserve fund, are merely claims on the banker, which, however, never exist as deposits. To the extent that they serve in clearing-house transactions, they perform the function of capital for the bankers-after the latter have loaned them out. They pay one another their mutual drafts upon the non-existing deposits by balancing their mutual accounts.

Adam Smith says with regard to the role played by capital in the loaning of money: *"Even in the moneyed interest, however, the money is, as it were, but the deed of assignment which conveys from one hand to another those capitals which the owners do not care to employ themselves. Those capitals may be greater in almost any proportion than the amount of the money, which serves as the instrument of their conveyance, the same pieces of money successively serving for many different loans, as well as for many different purchases. A, for example, lends to W £1,000, with which W immediately purchases of B £1,000 worth of goods. B, having no occasion for the money himself, lends the identical pieces to X, with which X immediately purchases of C another £1,000 worth of goods. C, in the same manner, and for the same reason, lends them to Y, who again purchases goods with them of D. In this manner the same pieces, either of coin or of paper, may, in the course of a few days, serve as the instrument of three different loans, and of three different purchases, each of which is, in value, equal to the whole amount of those pieces. What the three moneyed men, A, B and C, assign to the three borrowers, W, X and Y, is the power of making those purchases. In this power consist both the value and the use of the loans. The stock lent by the three moneyed men is equal to the value of the goods which can be purchased with it, and is three times greater than that of the money with which the purchases are made. Those loans, however, may be all perfectly well secured, the goods purchased by the different debtors being so employed, as, in due time, to bring back, with a profit, an equal value either of coin or of paper. And as the same pieces of money can thus serve as the instrument of different loans to three, or for the same reason, to thirty times their value, so they may likewise successively serve as the instrument of repayment."* ([An Inquiry into the Nature and Causes of the Wealth of Nations, Aberdeen, London, 1848, p. 236. — Ed.] Book II, Chap. IV.)

Since the same piece of money can be used for various purchases, corresponding to its velocity of circulation, it can similarly be used for various loans, since the

purchases take it from one person to another, and a loan is but a transfer from one person to another without the mediation of a purchase. To every seller, money represents the transformed shape of his commodities. Nowadays, when every value is expressed as capital-value, it represents in the various loans various capitals in succession. This is simply another way of expressing the earlier statement that it can successively realise various commodity-values. At the same time it serves as a medium of circulation, in order to transfer the real capitals from person to person. In the case of loans, it does not pass from person to person as a medium of circulation. As long as it remains in the hands of the lender, it is in his hands not a medium of circulation, but the value existence of his capital. And in this form he transfers it when lending it to another. If A had lent the money to B, and B to C, without the mediation of purchases, the same money would not represent three capitals, but only one — a *single* capital-value. The number of capitals which it actually represents depends on the number of times that it functions as the value-form of various commodity-capitals.

The same thing that Adam Smith says about loans in general also applies to deposits, which are merely another name for the loans which the public makes to the bankers. The same pieces of money may serve as the instruments for any number of deposits.

"It is unquestionably true that the £1,000 which you deposit at A today may be reissued tomorrow, and form a deposit at B. The day after that, reissued from B, it may form a deposit at C... and so on to infinitude; and that the same £1,000 in money may, thus, by a succession of transfers, multiply itself into a sum of deposits absolutely indefinite. It is possible, therefore, that nine-tenths of all the deposits in the United Kingdom may have no existence beyond their record in the books of the bankers who are respectively accountable for them... Thus in Scotland, for instance, currency has never exceeded £3 million, the deposits in the banks are estimated at £27 million. Unless a run on the banks be made, the same £4,000 would, if sent back upon its travels, cancel with the same facility a sum equally indefinite. As the same £1,000, with which you cancel your debt to a tradesman today, may cancel his debt to the merchant tomorrow, the merchant's debt to the bank the day following, and so on without end; so the same £1,000 may pass from hand to hand, and bank to bank, and cancel any conceivable sum of deposits." (*The Currency Theory Reviewed*, pp. 62-63.)

Just as everything in this credit system is doubled and trebled and transformed into a mere phantom of the imagination, so it is with the "reserve fund," where one would at last hope to grasp on to something solid.

Let us listen once more to Mr. Morris, Governor of the Bank of England: *"The reserves of the private bankers are in the hands of the Bank of England in the shape of deposits... An export of gold acts exclusively, in the first instance, upon the reserve of the Bank of England; but it would also be acting upon the reserves of the bankers, inasmuch as it is a withdrawal of a portion of the reserves which they have in the Bank of England. It would be acting upon the reserves of all the bankers throughout the country."* (Commercial Distress, 1847-48, Nos. 3639, 3642.)

Ultimately, then, the reserve funds actually merge with the reserve fund of the Bank of England.^[4] However, this reserve fund also has a double existence. The reserve fund of the banking department is equal to the surplus of notes which the Bank is authorised to issue over and above the notes in circulation. The legal maximum of the note issue is £14 million (for which no bullion reserve is required; it is the approximate amount owed by the state to the Bank) plus the amount of the Bank's supply of precious metal. If the supply of precious metal in the Bank amounts to £14 million, the Bank can thus issue £28 million in notes, and if £20 million of these are in circulation, the reserve fund of the banking department is £8 million. These £8 million's worth of notes are then legally the banker's capital at the disposal of the Bank, and at the same time the reserve fund for its deposits. Now, if a drain of gold takes place, whereby the supply of precious metal in the Bank is reduced by £6 million — requiring the destruction of an equivalent number of notes — the reserve of the banking department would fall from £8 million to £2 million. On the one hand, the Bank would raise its rate of interest considerably; on the other hand, the banks having deposits with it, and the other depositors, would observe a large decrease in the reserve fund covering their own credits in the Bank. In 1857, the four largest stock banks of London threatened to call in their deposits, and thereby bankrupt the banking department, unless the Bank of England would secure a "government letter" suspending the Bank Act of 1844.^[5] In this way the banking department could fail, as in 1847, while any number of millions (*e.g.*, 8 million in 1847) are held in its issue department to guarantee the convertibility of the circulating notes. But this is again illusory.

"That large portion (of deposits) for which the bankers themselves have no immediate demand passes into the hands of the bill-brokers, who give to the banker in return commercial bills already discounted by them for persons in London and in different parts of the country as a security for the sum advanced by the banker. The bill-broker is responsible to the banker for payment of this money at call; and such is the magnitude of these transactions, that Mr. Neave, the present Governor of the Bank [of England], stated in evidence, 'We know that one broker had 5 million, and we were led to believe that another had between 8 and 10 million; there was one with 4, another with 3 1/2, and a third with above 8. I speak of deposits with the brokers.'" (Report of Committee on Bank Acts, 1857-58, p. 5, Section 8.)

"The London bill-brokers carried on their enormous transactions without any cash reserve, relying on the run off of their bills falling due, or in extremity, on the power of obtaining advances from the Bank of England on the security of bills under discount." *Ibid.*, p. VIII, Section 17. "Two bill-broking houses in London suspended payment in 1847; both afterwards resumed business. In 1857, both suspended again. The liabilities of one house in 1847 were, in round numbers, £2,683,000, with a capital of £180,000; the liabilities of the same house, in 1857, were £5,300,000, the capital probably not more than one-fourth of what it was in 1847. The liabilities of the other firm were between £3,000,000 and £4,000,000 at each period of stoppage, with a capital not exceeding £45,000." (*Ibid.*, p. XXI, Section 52.)

Notes

1. "The labourer possesses capital-value, which is arrived at by considering the money-value or his annual wage as income from interest... Capitalising... the average daily wage at 4%, we obtain the average value of a male agricultural labourer to be: German Austria, 4,500 taler; Prussia, 4,500; England, 3,750; France, 2,000; inner Russia, 750 taler." (Von Reden, *Vergleichende Kulturstatistik*, Berlin, 1848, p. 434.)

2. [Immediately after the February Revolution, when commodities and securities were extremely depreciated and utterly unsaleable, a Swiss merchant in Liverpool, Mr. B. Zwilchenbart — who told this to my father — cashed all his belongings, travelled with cash in hand to Paris and sought out Rothschild, offering to participate in a joint enterprise with him. Rothschild looked at him fixedly, rushed towards him, grabbed him by his shoulders and asked: "Avez-vous de l'argent sur vous?" — "Oui, M. Le baron." — "Alors vous êtes mon homme!" ("Have you money in your possession?" — "Yes, Baron." — "Then you are my man!") — And they did a thriving business together. — *F.E.*]

3. [This doubling and trebling of capital has developed considerably further in recent years, for instance, through financial trusts, which already occupy a heading of their own in the report of the London Stock Exchange. A company is organised for the purchase of a certain class of interest-bearing of foreign government securities, English municipal or American public bonds, railway stocks, etc. The capital, for example, £2 million, is raised by stock subscriptions. The Board of Directors buys up the values in question or speculates more or less actively therein, and after deducting the expenses distributes among the stockholders the annual interest as dividends. Furthermore, some stock companies have adopted the custom of dividing the common stock into two classes, preferred and deferred. The preferred receive a fixed rate of interest, say, 5%, provided that the total profit permits it; if there is anything left after that, the deferred receive it. In this manner, the "solid" investment of capital in preferred shares is more or less separated from

actual speculation — with deferred shares. Since a few large enterprises have been unwilling to adopt this new custom, the expedient has been resorted to of organising new companies which invest a million or several million pounds sterling in shares of the former companies and then issue new shares amounting to the nominal value of the purchased shares, but half of them are issued as preferred and the other half as deferred. In such cases the original shares are doubled, since they serve as a basis for a new issue of shares. — *F.E.*]

4. [To what extent this has intensified since then is shown by the following official tabulation of the bank reserves of the fifteen largest London banks in November 1892, taken from the *Daily News* of December 15, 1892:

Name of Bank	Liabilities	Cash Reserves	Percentages
City	£9,317,629	£746,551	8.01
Capital and Counties	11,392,744	1,307,483	11.47
Imperial	3,987,400	447,157	11.22
Lloyds	23,800,937	2,966,806	12.46
Lon. and Westminster	24,671,559	3,818,885	15.50
Lon. and S. Western	5,570,268	812,353	14.58
London Joint Stock	12,127,993	1,288,977	10.62
London and Midland	8,814,499	1,127,280	12.79
London and County	37,111,035	3,600,374	9.70
National	11,163,829	1,426,225	12.77
National Provincial	41,907,384	4,614,780	41.01
Parrs and the Alliance	12,794,489	1,532,707	11.98
Prescott & Co	4,041,058	538,517	13.07
Union of London	15,502,618	2,300,084	14.84
Williams, Deacon & Manchester & Co.	10,452,381	1,317,628	12.60
Total	£232,655,823	£27,845,807	11.97

Of this total reserve of almost 28 million, at least 25 million are deposited in the Bank of England, and at most 3 million are in cash in the safes of the 15 banks themselves. But the cash reserve of the banking department of the Bank of England amounted to less than 16 million during that same month of November 1892 — *-F. E.]*

5. The suspension of the Bank Act of 1844 permits the Bank to issue any quantity of bank-notes regardless of the gold reserve backing in its possession; thus, to create an arbitrary quantity of fictitious paper money-capital, and to use it for the purpose of making loans to banks, exchange brokers, and through them to commerce. — *[F. E.]*

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