

## Chapter 15

# On Commodity Acquisition, Arbitrage, and Lending

A bank for the issuance of a stable alternative currency would have to (1) acquire the commodities in its unit of redemption so as to have them available for redemption; (2) arbitrage and store them, and (3) make loans and discount loans for which the collateral would finally be commodities.

Assuming that the proportion of paper-money printed and issued to the amount of new bank-money created and issued by such an institution as BISC would be the same as is the case with most of the existing currencies of the West, then in *theory* about 20% of BISC's assets would consist of commodities either in its own vaults, in public warehouses, or in transit. The *actual* percentage, however, need be only enough to cover all calls for redemption in commodities. In practice, once BISC became an established institution, the reserve needed might be only a few percent. That anything like twenty percent would be needed is extremely improbable.

The biggest calls for redemption would probably come from central banks, and these calls would probably be for gold rather than for all the commodities in the unit of redemption. BISC should be free to redeem the constants it

issues in all commodities if for any reason its supply of gold was insufficient. It should, of course, have an ample reserve of all the commodities to cover every probable call.

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The funds for the purchase of the commodity reserve would come in part from deposits and in part from the issue of constants. In the beginning, since nobody would have any constants, the deposits would consist only of existing currencies; later, when constants began to be accepted and to circulate, they would include both constants and existing currencies. In acquiring the commodity reserves needed, existing currencies rather than constants should be used; this would be one way of avoiding the accumulation of a superfluity of depreciating currencies.

1. Acquisition of the commodities can be provided for in two ways: (a) by arbitraging them and (b) by buying them outright for storage. Arbitraging is the preferred method for two reasons. First, it would avoid all costs for storage, and second it would produce a substantial income over and above all the costs involved. Even though the commodities would be in transit, those needed for redemption would be available because they would be arriving at their destinations constantly.

Outright purchase of some commodities in the unit of redemption, specifically gold and silver, for storage might under various circumstance be advisable. They would then become available not only for redemption but would also be be a part either of BISC's commodity reserve or of its surplus reserves for various contingencies.

2. One of the things which arbitrage on a large scale would do would be to make it possible to redress the imbalance in the low prices paid ever since the industrial revolution, to the growers and producers of raw materials and the high prices middlemen and manufacturers have and still are

able to realize on them. Middlemen and manufacturers get all the loans they want for this purpose; growers and producers do not.

Manufacturing has been particularly favored for nearly two centuries. The limitless financing of manufacturing is made possible today by two facts: (a) the fact that commercial banks create new money for this purpose by making loans on the securities manufacturing corporations issue, often disguised in the form of brokers' loans, and by (b) the fact that they transfer their reserves and surplus funds to banks in the financial centers which use them to finance industry. The cheaper the raw materials which industry uses, the greater its profits. Unconsciously sometimes, though very often consciously and deliberately, growers and producers are denied loans which would enable them to market their commodities at the time they could do so most profitably. Yet loans of this kind are strictly commercial loans—the only kind which justify the creation of new money. If the financing of industry was limited to actual savings in the form of existent money, the handicap under which growers and producers now labor would be ended.

As it is now, agricultural products, for instance, are bought from farmers at harvest time, when their prices are naturally lowest because of the amount thrown on the market, while the rise in price during the period they are in storage is pocketed by middlemen or by manufacturers and processors. What makes this situation even worse is the fact that the markets are in effect rigged to promote commodity speculation, since it is to the interest of the brokers to increase the number of commissions they earn through the buying and selling in which speculators indulge.

Bank financing of such speculation, not only in commodities but also in securities, is among the worst of existing banking practices. BISC's lending policies should give priority to loans to (a) farmers and (b) for storage of farm products. No farmer should ever have to sell what he has produced

except when prices are at their maximum for the year. He should be able to get all the credit he needs for storing his produce in public warehouses until such a time.

3. The loans and discounts by BISC on the security of commodities should have three characteristics: (a) they should be loans made to growers and producers and to importers and exporters, or discounts of such loans made by commercial banks; (b) they should be made on the security of warehouse receipts evidencing the fact that the commodities are in public storage or of bills-of-lading evidencing the fact that they are in transit, and (c) they should be made in limitless volume by creating bank-money or issuing paper-money to meet every legitimate need of those who grow and produce or import and export commodities.

The need for loans of this kind is enormous, particularly in underdeveloped nations such as India where the masses of growers are in the clutches of money-lenders. In the developed nations of the world, loans of this kind provide strictly commercial banks with a substantial part of all the loans they make. BISC should aim at acquiring the commanding position in this field. Its operations should be so large that they tend to reduce the existing instability of commodity prices.

BISC could very well become the biggest maker of loans and discounts of this kind in the world because its interest charges could be minimal. Assuming that its operating costs are around one percent, which is not unusual for any fairly large bank, it could make loans at an interest charge of 1 1/2 to 2 percent and still obtain a substantial net income from them. At the time I am writing this in 1974 the prime interest rate charged to preferred borrowers by the banks in this country is 11 percent; BISC could make loans of this kind for less than a third of this. To create new bank-money for this purpose would cost it no more than the cost of the accounting involved; to issue new paper-money, no more than the cost of printing it. This is the reason its interest rates on such loans would be so attractive.