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**Essays, Moral, Political, and Literary**

**Hume, David**

(1711-1776)

CEE

**Part II, Essay IV**

**OF INTEREST**

II.IV.1

NOTHING is esteemed a more certain sign of the flourishing condition of any nation than the lowness of interest: And with reason; though I believe the cause is somewhat different from what is commonly apprehended. Lowness of interest is generally ascribed to plenty of money.<sup>\*33</sup> But money, however plentiful, has no other effect, *if fixed*, than to raise the price of labour. Silver is more common than gold; and therefore you receive a greater quantity of it for the same commodities. But do you pay less interest for it? Interest in BATAVIA and JAMAICA is at 10 *per cent.* in PORTUGAL at 6; though these places, as we may learn from the prices of every thing, abound more in gold and silver than either LONDON or AMSTERDAM.

II.IV.2

Were all the gold in ENGLAND annihilated at once, and one and twenty shillings substituted in the place of every guinea, would money be more plentiful or interest lower? No surely: We should only use silver instead of gold. Were gold rendered as common as silver, and silver as common as copper; would money be more plentiful or interest lower? We may assuredly give the same answer. Our shillings would then be yellow, and our halfpence white; and we should have no guineas. No other difference would ever be observed; no alteration on commerce, manufactures, navigation, or interest; unless we imagine, that the colour of the metal is of any consequence.

II.IV.3

Now, what is so visible in these greater variations of scarcity or abundance in the precious metals, must hold in all inferior changes. If the multiplying of gold and silver fifteen times makes no difference, much less can the doubling or tripling them. All augmentation has no other effect than to heighten the price of labour and commodities; and even this variation is little more than that of a name. In the progress towards these changes, the augmentation may have some influence, by exciting industry; but after the prices are settled, suitably to the new abundance of gold and silver, it has no manner of influence.

II.IV.4

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An effect always holds proportion with its cause. Prices have risen near four times since the discovery of the INDIES; and it is probable gold and silver have multiplied much more: But interest has not fallen much above half. The rate of interest, therefore, is not derived from the quantity of the precious metals.

## II.IV.5

Money having chiefly a fictitious value,<sup>a</sup> the greater or less plenty of it is of no consequence, if we consider a nation within itself; and the quantity of specie, when once fixed, though ever so large, has no other effect, than to oblige every one to tell out<sup>o</sup> a greater number of those shining bits of metal, for clothes, furniture or equipage, without encreasing any one convenience of life. If a man borrow money to build a house, he then carries home a greater load; because the stone, timber, lead, glass, &c. with the labour of the masons and carpenters, are represented by a greater quantity of gold and silver. But as these metals are considered chiefly as representations, there can no alteration arise, from their bulk or quantity, their weight or colour, either upon their real value or their interest. The same interest, in all cases, bears the same proportion to the sum. And if you lent me so much labour and so many commodities; by receiving five *per cent.* you always receive proportional labour and commodities, however represented, whether by yellow or white coin, whether by a pound or an ounce. It is in vain, therefore, to look for the cause of the fall or rise of interest in the greater or less quantity of gold and silver, which is fixed in any nation.

## II.IV.6

High interest arises from *three* circumstances: A great demand for borrowing; little riches to supply that demand; and great profits arising from commerce: And these circumstances are a clear proof of the small advance of commerce and industry, not of the scarcity of gold and silver. Low interest, on the other hand, proceeds from the three opposite circumstances: A small demand for borrowing; great riches to supply that demand; and small profits arising from commerce: And these circumstances are all connected together, and proceed from the encrease of industry and commerce, not of gold and silver. We shall endeavour to prove these points; and shall begin with the causes and the effects of a great or small demand for borrowing.

## II.IV.7

When a people have emerged ever so little from a savage state, and their numbers have encreased beyond the original multitude, there must immediately arise an inequality of property; and while some possess large tracts of land, others are confined within narrow limits, and some are entirely without any landed property. Those who possess more land than they can labour, employ those who possess none, and agree to receive a determinate part of the product. Thus the *landed* interest is immediately established; nor is there any settled government, however rude, in which affairs are not on this footing. Of these proprietors of land, some must

presently discover themselves to be of different tempers from others; and while one would willingly store up the produce of his land for futurity,<sup>o</sup> another desires to consume at present what should suffice for many years. But as the spending of a settled revenue is a way of life entirely without occupation;<sup>o</sup> men have so much need of somewhat<sup>o</sup> to fix and engage them, that pleasures, such as they are, will be the pursuit of the greater part of the landholders, and the prodigals among them will always be more numerous than the misers. In a state, therefore, where there is nothing but a landed interest, as there is little frugality, the borrowers must be very numerous, and the rate of interest must hold proportion to it. The difference depends not on the quantity of money, but on the habits and manners which prevail. By this alone the demand for borrowing is encreased or diminished. Were money so plentiful as to make an egg be sold for sixpence; so long as there are only landed gentry and peasants in the state, the borrowers must be numerous, and interest high. The rent for the same farm would be heavier and more bulky: But the same idleness of the landlord, with the higher price of commodities, would dissipate it in the same time, and produce the same necessity and demand for borrowing.<sup>b</sup>

II.IV.8

Nor is the case different with regard to the *second* circumstance which we proposed to consider, namely, the great or little riches to supply the demand. This effect also depends on the habits and way of living of the people, not on the quantity of gold and silver. In order to have, in any state, a great number of lenders, it is not sufficient nor requisite, that there be great abundance of the precious metals. It is only requisite, that the property or command of that quantity, which is in the state, whether great or small, should be collected in particular hands, so as to form considerable sums, or compose a great monied interest. This begets a number of lenders, and sinks the rate of usury; and this I shall venture to affirm, depends not on the quantity of specie, but on particular manners and customs, which make the specie gather into separate sums or masses of considerable value.

II.IV.9

For suppose, that, by miracle, every man in GREAT BRITAIN should have five pounds slipt into his pocket in one night; this would much more than double the whole money that is at present in the kingdom; yet there would not next day, nor for some time, be any more lenders, nor any variation in the interest. And were there nothing but landlords and peasants in the state, this money, however abundant, could never gather into sums; and would only serve to encrease the prices of every thing, without any farther consequence. The prodigal landlord dissipates it, as fast as he receives it; and the beggarly peasant has no means, nor view, nor ambition of obtaining above a bare livelihood. The overplus of borrowers above that of lenders continuing still the same, there will follow no reduction of interest. That depends upon another principle; and must proceed from an encrease of industry and frugality, of arts and commerce.

II.IV.10

Every thing useful to the life of man arises from the ground; but few things arise in that condition which is requisite to render them useful. There must, therefore, beside the peasants and the proprietors of land, be another rank of men, who receiving from the former the rude materials, work them into their proper form, and retain part for their own use and subsistence. In the infancy of society, these contracts between the artisans and the peasants, and between one species of artisans and another are commonly entered into immediately by the persons themselves, who, being neighbours, are easily acquainted with each other's necessities, and can lend their mutual assistance to supply them. But when men's industry encreases, and their views enlarge, it is found, that the most remote parts of the state can assist each other as well as the more contiguous, and that this intercourse of good offices may be carried on to the greatest extent and intricacy. Hence the origin of *merchants*, one of the most useful races of men, who serve as agents between those parts of the state, that are wholly unacquainted, and are ignorant of each other's necessities. Here are in a city fifty workmen in silk and linen, and a thousand customers; and these two ranks of men, so necessary to each other, can never rightly meet, till one man erects a shop, to which all the workmen and all the customers repair. In this province, grass rises in abundance: The inhabitants abound in cheese, and butter, and cattle; but want bread and corn, which, in a neighbouring province, are in too great abundance for the use of the inhabitants. One man discovers this. He brings corn from the one province and returns with cattle; and supplying the wants of both, he is, so far, a common benefactor. As the people encrease in numbers and industry, the difficulty of their intercourse encreases: The business of the agency or merchandize becomes more intricate; and divides, subdivides, compounds, and mixes to a greater variety. In all these transactions, it is necessary, and reasonable, that a considerable part of the commodities and labour should belong to the merchant, to whom, in a great measure, they are owing. And these commodities he will sometimes preserve in kind, or more commonly convert into money, which is their common representation. If gold and silver have encreased in the state together with the industry, it will require a great quantity of these metals to represent a great quantity of commodities and labour. If industry alone has encreased, the prices of every thing must sink, and a small quantity of specie will serve as a representation.

II.IV.11

There is no craving or demand of the human mind more constant and insatiable than that for exercise and employment; and this desire seems the foundation of most of our passions and pursuits. Deprive a man of all business and serious occupation, he runs restless from one amusement to another; and the weight and oppression, which he feels from idleness, is so great, that he forgets the ruin which must follow him from his immoderate expences. Give him a more harmless way of employing his mind or body, he is satisfied, and feels no longer that insatiable thirst after pleasure. But if the employment you give him be lucrative, especially if the profit be

attached to every particular exertion of industry, he has gain so often in his eye, that he acquires, by degrees, a passion for it, and knows no such pleasure as that of seeing the daily encrease of his fortune. And this is the reason why trade encreases frugality, and why, among merchants, there is the same overplus of misers above prodigals, as, among the possessors of land, there is the contrary.

II.IV.12

Commerce encreases industry, by conveying it readily from one member of the state to another, and allowing none of it to perish or become useless. It encreases frugality, by giving occupation to men, and employing them in the arts of gain, which soon engage their affection, and remove all relish for pleasure and expence. It is an infallible consequence of all industrious professions, to beget frugality, and make the love of gain prevail over the love of pleasure. Among lawyers and physicians who have any practice, there are many more who live within their income, than who exceed it, or even live up to it. But lawyers and physicians beget no industry; and it is even at the expence of others they acquire their riches; so that they are sure to diminish the possessions of some of their fellow-citizens, as fast as they encrease their own. Merchants, on the contrary, beget industry, by serving as canals to convey it through every corner of the state: And at the same time, by their frugality, they acquire great power over that industry, and collect a large property in the labour and commodities, which they are the chief instruments in producing. There is no other profession, therefore, except merchandize, which can make the monied interest considerable, or, in other words, can encrease industry, and, by also encreasing frugality, give a great command of that industry to particular members of the society. Without commerce, the state must consist chiefly of landed gentry, whose prodigality and expence make a continual demand for borrowing; and of peasants, who have no sums to supply that demand. The money never gathers into large stocks or sums, which can be lent at interest. It is dispersed into numberless hands, who either squander it in idle show and magnificence, or employ it in the purchase of the common necessaries of life. Commerce alone assembles it into considerable sums; and this effect it has merely from the industry which it begets, and the frugality which it inspires, independent of that particular quantity of precious metal which may circulate in the state.

II.IV.13

Thus an encrease of commerce, by a necessary consequence, raises a great number of lenders, and by that means produces lowness of interest. We must now consider how far this encrease of commerce diminishes the profits arising from that profession, and gives rise to the *third* circumstance requisite to produce lowness of interest.

II.IV.14

It may be proper to observe on this head, that low interest and low profits of merchandize are two events, that mutually forward each other, and are both originally derived from that extensive commerce, which

produces opulent merchants, and renders the monied interest considerable. Where merchants possess great stocks, whether represented by few or many pieces of metal, it must frequently happen, that, when they either become tired of business, or leave heirs unwilling or unfit to engage in commerce, a great proportion of these riches naturally seeks an annual and secure revenue. The plenty diminishes the price, and makes the lenders accept of a low interest. This consideration obliges many to keep their stock employed in trade, and rather be content with low profits than dispose of their money at an under-value. On the other hand, when commerce has become extensive, and employs large stocks, there must arise rivalships among the merchants, which diminish the profits of trade, at the same time that they encrease the trade itself. The low profits of merchandize induce the merchants to accept more willingly of a low interest, when they leave off business, and begin to indulge themselves in ease and indolence. It is needless, therefore, to enquire which of these circumstances, to wit, *low interest or low profits*, is the cause, and which the effect? They both arise from an extensive commerce, and mutually forward each other. No man will accept of low profits, where he can have high interest; and no man will accept of low interest, where he can have high profits. An extensive commerce, by producing large stocks, diminishes both interest and profits; and is always assisted, in its diminution of the one, by the proportional sinking of the other. I may add, that, as low profits arise from the encrease of commerce and industry, they serve in their turn to its farther encrease, by rendering the commodities cheaper, encouraging the consumption, and heightening the industry. And thus, if we consider the whole connexion of causes and effects, interest is the barometer of the state, and its lowness is a sign almost infallible of the flourishing condition of a people. It proves the encrease of industry, and its prompt circulation through the whole state, little inferior to a demonstration. And though, perhaps, it may not be impossible but a sudden and a great check to commerce may have a momentary effect of the same kind, by throwing so many stocks out of trade; it must be attended with such misery and want of employment in the poor, that, besides its short duration, it will not be possible to mistake the one case for the other.

II.IV.15

Those who have asserted, that the plenty of money was the cause of low interest, seem to have taken a collateral effect for a cause; since the same industry, which sinks the interest, commonly acquires great abundance of the precious metals. A variety of fine manufactures, with vigilant enterprising merchants, will soon draw money to a state, if it be any where to be found in the world. The same cause, by multiplying the conveniencies of life, and encreasing industry, collects great riches into the hands of persons, who are not proprietors of land, and produces, by that means, a lowness of interest. But though both these effects, plenty of money and low interest, naturally arise from commerce and industry, they are altogether independent of each other. For suppose a nation removed

into the *Pacific* ocean, without any foreign commerce, or any knowledge of navigation: Suppose, that this nation possesses always the same stock of coin, but is continually increasing in its numbers and industry: It is evident, that the price of every commodity must gradually diminish in that kingdom; since it is the proportion between money and any species of goods, which fixes their mutual value; and, upon the present supposition, the conveniencies of life become every day more abundant, without any alteration in the current specie. A less quantity of money, therefore, among this people, will make a rich man, during the times of industry, than would suffice to that purpose, in ignorant and slothful ages. Less money will build a house, portion a daughter, buy an estate, support a manufactory, or maintain a family and equipage. These are the uses for which men borrow money; and therefore, the greater or less quantity of it in a state has no influence on the interest. But it is evident, that the greater or less stock of labour and commodities must have a great influence; since we really and in effect borrow these, when we take money upon interest. It is true, when commerce is extended all over the globe, the most industrious nations always abound most with the precious metals: So that low interest and plenty of money are in fact almost inseparable. But still it is of consequence to know the principle whence any phenomenon arises, and to distinguish between a cause and a concomitant effect.\*34 Besides that the speculation is curious, it may frequently be of use in the conduct of public affairs. At least, it must be owned, that nothing can be of more use than to improve, by practice, the method of reasoning on these subjects, which of all others are the most important; though they are commonly treated in the loosest and most careless manner.

II.IV.16

Another reason of this popular mistake with regard to the cause of low interest, seems to be the instance of some nations; where, after a sudden acquisition of money or of the precious metals, by means of foreign conquest, the interest has fallen, not only among them, but in all the neighbouring states, as soon as that money was dispersed, and had insinuated itself into every corner. Thus, interest in SPAIN fell near a half immediately after the discovery of the WEST INDIES, as we are informed by GARCILASSO DE LA VEGA:\*35 And it has been ever since gradually sinking in every kingdom of EUROPE. Interest in ROME, after the conquest of EGYPT, fell from 6 to 4 *per cent.* as we learn from DION.\*36

II.IV.17

The causes of the sinking of interest, upon such an event, seem different in the conquering country and in the neighbouring states; but in neither of them can we justly ascribe that effect merely to the increase of gold and silver.

II.IV.18

In the conquering country, it is natural to imagine, that this new acquisition of money will fall into a few hands, and be gathered into large

sums, which seek a secure revenue, either by the purchase of land or by interest; and consequently the same effect follows, for a little time, as if there had been a great accession of industry and commerce. The encrease of lenders above the borrowers sinks the interest; and so much the faster, if those, who have acquired those large sums, find no industry or commerce in the state, and no method of employing their money but by lending it at interest. But after this new mass of gold and silver has been digested, and has circulated through the whole state, affairs will soon return to their former situation; while the landlords and new money-holders, living idly, squander above their income; and the former daily contract debt, and the latter encroach on their stock till its final extinction. The whole money may still be in the state, and make itself felt by the encrease of prices: But not being now collected into any large masses or stocks, the disproportion between the borrowers and lenders is the same as formerly, and consequently the high interest returns.

## II.IV.19

Accordingly we find, in ROME, that, so early as TIBERIUS'S time, interest had again mounted to 6 *per cent.*<sup>\*37</sup> though no accident had happened to drain the empire of money. In TRAJAN'S time, money lent on mortgages in ITALY, bore 6 *per cent.*;<sup>\*38</sup> on common securities in BITHYNIA, 12.<sup>\*39</sup> And if interest in SPAIN has not risen to its old pitch; this can be ascribed to nothing but the continuance of the same cause that sunk it, to wit, the large fortunes continually made in the INDIES, which come over to SPAIN from time to time, and supply the demand of the borrowers. By this accidental and extraneous cause, more money is to be lent in SPAIN, that is, more money is collected into large sums than would otherwise be found in a state, where there are so little commerce and industry.

## II.IV.20

As to the reduction of interest, which has followed in ENGLAND, FRANCE, and other kingdoms of EUROPE, that have no mines, it has been gradual; and has not proceeded from the encrease of money, considered merely in itself; but from that of industry, which is the natural effect of the former encrease, in that interval, before it raises the price of labour and provisions. For to return to the foregoing supposition; if the industry of ENGLAND had risen as much from other causes, (and that rise might easily have happened, though the stock of money had remained the same) must not all the same consequences have followed, which we observe at present? The same people would, in that case, be found in the kingdom, the same commodities, the same industry, manufactures, and commerce; and consequently the same merchants, with the same stocks, that is, with the same command over labour and commodities, only represented by a smaller number of white or yellow pieces; which being a circumstance of no moment, would only affect the waggoner, porter, and trunk-maker. Luxury, therefore, manufactures, arts, industry, frugality, flourishing equally as at present, it is evident, that interest must also have been as low; since that is the necessary result of all these circumstances; so far as



they determine the profits of commerce, and the proportion between the borrowers and lenders in any state.

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### Notes for this chapter

33. [Mercantilist writers had held that a lowering of interest, or the price paid for the use of resources over time, is one of the benefits of increasing the quantity of money. Hume continues his attack on mercantilism by denying that rates of interest are caused by the quantity of money in circulation. Hume turns to his theory of human nature as well as to historical examples in order to prove that low interest is produced ultimately by the growth of industry and commerce, which reduces the proportion of borrowers and increases the number of lenders with savings available to supply the demand for money. For an assessment of Hume's views on interest, see Rotwein, *David Hume: Writings on Economics*, pp. lxvii-lxxii.]
34. [Hume offers several rules for distinguishing causes from accidental circumstances: see *Treatise of Human Nature* 1.3.15.]
35. [Garcilaso de la Vega, "El Inca" (1539-1616), was born in Peru, the son of a Spanish conqueror and an Indian princess, and he was brought up there until the age of twenty. He is best known for a two-part history of Peru: I. *Comentarios Reales que tratan del origen de los Yncas* (1608 or 1609) and II. *Historia general de Peru* (1617); translated as *The Royal Commentaries of Peru, in Two Parts* (1688). Hume possibly has in mind the discussion of the return on leases in pt. 2, bk. 1, chap. 6.]
36. Lib. ii. [Dio(n) Cassius (A.D. 155-235), *Roman History* 51.21.5: "... loans for which the borrower had been glad to pay twelve per cent. could now be had for one third that rate" (Loeb translation by Earnest Cary).]
37. COLUMELLA, lib. iii. cap. 3. [Columella (first century A.D.), *Rei Rusticae* (On agriculture) 3.3.9.]
38. PLINII epist. lib. vii. ep. 18. [Pliny the Younger, *Letters* 7.18.]
39. Id. lib. x. ep. 62. [*Ibid.* 10.54 in the Loeb edition.]

Part II, Essay V

### End of Notes

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