

# The Morality of Moneylending: A Short History

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**I**t seems that every generation has its Shylock—a despised financier blamed for the economic problems of his day. A couple of decades ago it was Michael Milken and his “junk” bonds. Today it is the mortgage bankers who, over the past few years, lent billions of dollars to home buyers—hundreds of thousands of whom are now delinquent or in default on their loans. This “sub-prime mortgage crisis” is negatively affecting the broader financial markets and the economy as a whole. The villains, we are told, are not the borrowers—who took out loans they could not afford to pay back—but the moneylenders—who either deceived the borrowers or should have known better than to make the loans in the first place. And, we are told, the way to prevent such problems in the future is to clamp down on moneylenders and their industries; thus, investigations, criminal prosecutions, and heavier regulations on bankers are in order.

Of course, government policy for decades has been to *encourage* lenders to provide mortgage loans to lower-income families, and when mortgage brokers have refused to make such loans, they have been accused of “discrimination.” But now that many borrowers are in a bind, politicians are seeking to lash and leash the lenders.

This treatment of moneylenders is unjust but not new. For millennia they have been the primary scapegoats for practically every economic problem. They have been derided by philosophers and condemned to hell by religious authorities; their property has been confiscated to compensate their “victims”; they have been humiliated,

framed, jailed, and butchered. From Jewish pogroms where the main purpose was to destroy the records of debt, to the vilification of the House of Rothschild, to the jailing of American financiers—money-lenders have been targets of philosophers, theologians, journalists, economists, playwrights, legislators, and the masses.

Major thinkers throughout history—Plato, Aristotle, Thomas Aquinas, Adam Smith, Karl Marx, and John Maynard Keynes, to name just a few—considered moneylending, at least under certain conditions, to be a major vice. Dante, Shakespeare, Dickens, Dostoyevsky, and modern and popular novelists depict moneylenders as villains.

Today, anti-globalization demonstrators carry signs that read “abolish usury” or “abolish interest.” Although these protestors are typically leftists—opponents of capitalism and anything associated with it—their contempt for moneylending is shared by others, including radical Christians and Muslims who regard charging interest on loans as a violation of God’s law and thus as immoral.

Moneylending has been and is condemned by practically everyone. But what exactly is being condemned here? What *is* moneylending or *usury*? And what are its consequences?

Although the term “usury” is widely taken to mean “excessive interest” (which is never defined) or illegal interest, the actual definition of the term is, as the *Oxford English Dictionary* specifies: “The fact or practice of lending money at interest.” This is the definition I ascribe to the term throughout this essay.

Usury is a financial transaction in which person A lends person B a sum of money for a fixed period of time with the agreement that it will be returned with interest. The practice enables people *without* money and people *with* money to mutually benefit from the wealth of the latter. The borrower is able to use money that he would otherwise not be able to use, in exchange for paying the lender an agreed-upon premium in addition to the principal amount of the loan. Not only do both interested parties benefit from such an exchange; countless people who are not involved in the trade often benefit too—by means of access to the goods and services made possible by the exchange.

Usury enables levels of life-serving commerce and industry that otherwise would be impossible. Consider a few historical examples.

Moneylenders funded grain shipments in ancient Athens and the first trade between the Christians in Europe and the Saracens of the East. They backed the new merchants of Italy and, later, of Holland and England. They supported Spain's exploration of the New World, and funded gold and silver mining operations. They made possible the successful colonization of America. They fueled the Industrial Revolution, supplying the necessary capital to the new entrepreneurs in England, the United States, and Europe. And, in the late 20th century, moneylenders provided billions of dollars to finance the computer, telecommunications, and biotechnology industries.

By taking risks and investing their capital in what they thought would make them the most money, moneylenders and other financiers made possible whole industries—such as those of steel, railroads, automobiles, air travel, air conditioning, and medical devices. Without capital, often provided through usury, such life-enhancing industries would not exist—and homeownership would be impossible to all but the wealthiest people.

Moneylending is the lifeblood of industrial-technological society. When the practice and its practitioners are condemned, they are condemned for furthering and enhancing man's life on earth.

Given moneylenders' enormous contribution to human well-being, why have they been so loathed throughout history, and why do they continue to be distrusted and mistreated today? What explains the universal hostility toward one of humanity's greatest benefactors? And what is required to replace this hostility with the gratitude that is the moneylenders' moral due?

As we will see, hostility toward usury stems from two interrelated sources: certain economic views and certain ethical views. Economically, from the beginning of Western thought, usury was regarded as *unproductive*—as the taking of something for nothing. Ethically, the practice was condemned as *immoral*—as unjust, exploitative, against biblical law, selfish. The history of usury is a history of confusions, discoveries, and evasions concerning the economic and moral status of the practice. Until usury is recognized as both economically productive and ethically praiseworthy—as both practical and moral—moneylenders will continue to be condemned as villains rather than heralded as the heroes they in fact are.

Our brief history begins with Aristotle's view on the subject.

## Aristotle

The practice of lending money at interest was met with hostility as far back as ancient Greece, and even Aristotle (384–322 B.C.) believed the practice to be unnatural and unjust. In the first book of *Politics* he writes:

The most hated sort [of moneymaking], and with the greatest reason, is usury, which makes a gain out of money itself, and not from the natural use of it. For money was intended to be used in exchange, but not to increase at interest. And this term Usury which means the birth of money from money, is applied to the breeding of money, because the offspring resembles the parent. Wherefore of all modes of making money this is the most unnatural.<sup>1</sup>

Aristotle believed that charging interest was immoral because money is not productive. If you allow someone to use your orchard, he argued, the orchard bears fruit every year—it is productive—and from this product the person can pay you rent. But money, Aristotle thought, is merely a medium of exchange. When you loan someone money, he receives no value over and above the money itself. The money does not create more money—it is barren. On this view, an exchange of \$100 today for \$100 plus \$10 in interest a year from now is unjust, because the lender thereby receives more than he gave, and what he gave could not have brought about the 10 percent increase. Making money from money, according to Aristotle, is “unnatural” because money, unlike an orchard, cannot produce additional value.

Aristotle studied under Plato and accepted some of his teacher’s false ideas. One such idea that Aristotle appears to have accepted is the notion that every good has some *intrinsic value*—a value independent of and apart from human purposes. On this view, \$100 will be worth \$100 a year from now and can be worth only \$100 to anyone, at any time, for any purpose. Aristotle either rejected or failed to consider the idea that loaned money loses value to the lender over time as his use of it is postponed, or the idea that money can be invested in economic activity and thereby create wealth. In short, Aristotle had no conception of the productive role of money or of the moneylender. (Given the relative simplicity of the Greek economy,

he may have had insufficient evidence from which to conclude otherwise.) Consequently, he regarded usury as unproductive, unnatural, and therefore unjust.

Note that Aristotle's conclusion regarding the unjust nature of usury is derived from his view that the practice is *unproductive*: Since usury creates nothing but takes something—since the lender apparently is parasitic on the borrower—the practice is unnatural and immoral. It is important to realize that, on this theory, there is no dichotomy between the economically practical and the morally permissible; usury is regarded as immoral *because* it is regarded as impractical.

Aristotle's economic and moral view of usury was reflected in ancient culture for a few hundred years, but moral condemnation of the practice became increasingly pronounced. The Greek writer Plutarch (46–127 A.D.), for example, in his essay “Against Running In Debt, Or Taking Up Money Upon Usury,” described usurers as “wretched,” “vulture-like,” and “barbarous.”<sup>2</sup> In Roman culture, Seneca (ca. 4 B.C.–65 A.D.) condemned usury for the same reasons as Aristotle; Cato the Elder (234–149 B.C.) famously compared usury to murder;<sup>3</sup> and Cicero (106–43 B.C.) wrote that “these profits are despicable which incur the hatred of men, such as those of . . . lenders of money on usury.”<sup>4</sup>

As hostile as the Greeks and Romans generally were toward usury, their hostility was based primarily on their economic view of the practice, which gave rise to and was integrated with their moral view of usury. The Christians, however, were another matter, and their position on usury would become the reigning position in Western thought up to the present day.

## The Dark and Middle Ages

The historian William Manchester described the Dark and Middle Ages as

stark in every dimension. Famines and plague, culminating in the Black Death [which killed one in four people at its peak] and its recurring pandemics, repeatedly thinned the population. . . .

Among the lost arts were bricklaying; in all of Germany, England, Holland and Scandinavia, virtually no stone buildings, except cathedrals, were raised for ten centuries. . . . Peasants labored harder, sweated more, and collapsed from exhaustion more often than their animals.<sup>5</sup>

During the Dark Ages, the concept of an economy had little meaning. Human society had reverted to a precivilized state, and the primary means of trade was barter. Money all but disappeared from European commerce for centuries. There was, of course, some trade and some lending, but most loans were made with goods, and the interest was charged in goods. These barter-based loans, primitive though they were, enabled people to survive the tough times that were inevitable in an agrarian society.<sup>6</sup>

Yet the church violently opposed even such subsistence-level lending.

During this period, the Bible was considered the basic source of knowledge and thus the final word on all matters of importance. For every substantive question and problem, scholars consulted scripture for answers—and the Bible clearly opposed usury. In the Old Testament, God says to the Jews: “[He that] Hath given forth upon usury, and hath taken increase: shall he then live? he shall not live . . . he shall surely die; his blood shall be upon him.”<sup>7</sup> And:

Thou shalt not lend upon usury to thy brother; usury of money; usury of victuals; usury of anything that is lent upon usury.

Unto a stranger thou mayest lend upon usury; but unto thy brother thou shalt not lend upon usury, that the Lord thy God may bless thee in all that thou settest thine hand to in the land whither thou goest to possess it.<sup>8</sup>

In one breath, God forbade usury outright; in another, He forbade the Jews to engage in usury with other Jews but permitted them to make loans at interest to non-Jews.

Although the New Testament does not condemn usury explicitly, it makes clear that one’s moral duty is to help those in need, and thus to give to others one’s own money or goods without the expectation of anything in return—neither interest nor principal. As Luke plainly

states, “lend, hoping for nothing again.”<sup>9</sup> Jesus’ expulsion of the moneychangers from the temple is precisely a parable conveying the Christian notion that profit is evil, particularly profit generated by moneylending. Christian morality, the morality of divinely mandated altruism, expounds the virtue of self-sacrifice on behalf of the poor and the weak; it condemns self-interested actions, such as profiting—especially profiting from a seemingly exploitative and unproductive activity such as usury.

Thus, on scriptural and moral grounds, Christianity opposed usury from the beginning. And it constantly reinforced its opposition with legal restrictions. In 325 A.D., the Council of Nicaea banned the practice among clerics. Under Charlemagne (768–814 A.D.), the Church extended the prohibition to laymen, defining usury simply as a transaction where more is asked than is given.<sup>10</sup> In 1139, the second Lateran Council in Rome denounced usury as a form of theft, and required restitution from those who practiced it. In the 12th and 13th centuries, strategies that concealed usury were also condemned. The Council of Vienne in 1311 declared that any person who dared claim that there was no sin in the practice of usury be punished as a heretic.

There was, however, a loophole among all these pronouncements: the Bible’s double standard on usury. As we saw earlier, read one way, the Bible permits Jews to lend to non-Jews. This reading had positive consequences. For lengthy periods during the Dark and Middle Ages, both Church and civil authorities allowed Jews to practice usury. Many princes, who required substantial loans in order to pay bills and wage wars, allowed Jewish usurers in their states. Thus, European Jews, who had been barred from most professions and from ownership of land, found moneylending to be a profitable, albeit hazardous, profession.

Although Jews were legally permitted to lend to Christians—and although Christians saw some practical need to borrow from them and chose to do so—Christians resented this relationship. Jews appeared to be making money on the backs of Christians while engaging in an activity biblically prohibited to Christians on punishment of eternal damnation. Christians, accordingly, held these Jewish usurers in contempt. (Important roots of anti-Semitism lie in this biblically structured relationship.)

Opposition to Jewish usurers was often violent. In 1190, the Jews

of York were massacred in an attack planned by members of the nobility who owed money to the Jews and sought to absolve the debt through violence.<sup>11</sup> During this and many other attacks on Jewish communities, accounting records were destroyed and Jews were murdered. As European historian Joseph Patrick Byrne reports:

“Money was the reason the Jews were killed, for had they been poor, and had not the lords of the land been indebted to them, they would not have been killed.”<sup>12</sup> But the “lords” were not the only debtors: the working class and underclass apparently owed a great deal, and these violent pogroms gave them the opportunity to destroy records of debt as well as the creditors themselves.<sup>13</sup>

In 1290, largely as a result of antagonism generated from their moneylending, King Edward I expelled the Jews from England, and they would not return en masse until the 17th century.

From the Christian perspective, there were clearly problems with the biblical pronouncements on usury. How could it be that Jews were prohibited from lending to other Jews but were allowed to lend to Christians and other non-Jews? And how could it be that God permitted Jews to benefit from this practice but prohibited Christians from doing so? These questions perplexed the thinkers of the day. St. Jerome’s (ca. 347–420) “solution” to the conundrum was that it was wrong to charge interest to one’s brothers—and, to Christians, all other Christians were brothers—but it was fine to charge interest to one’s enemy. Usury was perceived as a weapon that weakened the borrower and strengthened the lender; so, if one loaned money at interest to one’s enemy, that enemy would suffer. This belief led Christians to the absurd practice of lending money to the Saracens—their enemies—during the Crusades.<sup>14</sup>

Like the Greeks and Romans, Christian thinkers viewed certain economic transactions as zero-sum phenomena, in which a winner always entailed a loser. In the practice of usury, the lender seemed to grow richer without effort—so it had to be at the expense of the borrower, who became poorer. But the Christians’ economic hostility toward usury was grounded in and fueled by biblical pronouncements against the practice—and this made a substantial difference. The combination of economic and biblical strikes against usury—



with an emphasis on the latter—led the Church to utterly vilify the usurer, who became a universal symbol for evil. Stories describing the moneylenders' horrible deaths and horrific existence in Hell were common. One bishop put it concisely:

God created three types of men: peasants and other laborers to assure the subsistence of the others, knights to defend them, and clerics to govern them. But the devil created a fourth group, the usurers. They do not participate in men's labors, and they will not be punished with men, but with the demons. For the amount of money they receive from usury corresponds to the amount of wood sent to Hell to burn them.<sup>15</sup>

Such was the attitude toward usury during the Dark and early Middle Ages. The practice was condemned primarily on biblical/moral grounds. In addition to the fact that the Bible explicitly forbade it, moneylending was recognized as self-serving. Not only did it involve profit; the profit was (allegedly) unearned and exploitative. Since the moneylender's gain was assumed to be the borrower's loss—and since the borrower was often poor—the moneylender was seen as profiting by exploiting the meek and was therefore regarded as evil.

Beginning in the 11th century, however, a conflicting economic reality became increasingly clear—and beginning in the 13th century, the resurgence of respect for observation and logic made that reality increasingly difficult to ignore.

Through trade with the Far East and exposure to the flourishing cultures and economies of North Africa and the Middle East, economic activity was increasing throughout Europe. As this activity created a greater demand for capital and for credit, moneylenders arose throughout Europe to fill the need—and as moneylenders filled the need, the economy grew even faster.

And Europeans were importing more than goods; they were also importing knowledge. They were discovering the Arabic numerical system, double-entry accounting, mathematics, science, and, most importantly, the works of Aristotle.

Aristotle's ideas soon became the focus of attention in all of Europe's learning centers, and his writings had a profound effect on the scholars of the time. No longer were young intellectuals satisfied

by biblical references alone; they had discovered reason, and they sought to ground their ideas in it as well. They were, of course, still stifled by Christianity, because, although reason had been rediscovered, it was to remain the handmaiden of faith. Consequently, these intellectuals spent most of their time trying to use reason to justify Christian doctrine. But their burgeoning acceptance of reason, and their efforts to justify their ideas accordingly, would ultimately change the way intellectuals thought about everything—including usury.

Although Aristotle himself regarded usury as unjust, recall that he drew this conclusion from what he legitimately thought was evidence in support of it; in his limited economic experience, usury appeared to be unproductive. In contrast, the thinkers of this era were confronted with extensive use of moneylending all around them—which was accompanied by an ever-expanding economy—a fact that they could not honestly ignore. Thus, scholars set out to reconcile the matter rationally. On Aristotelian premises, if usury is indeed unjust and properly illegal, then there must be a logical argument in support of this position. And the ideas that usury is unproductive and that it necessarily consists in a rich lender exploiting a poor borrower were losing credibility.

Public opinion, which had always been against usury, now started to change as the benefits of credit and its relationship to economic growth became more evident. As support for usury increased, however, the Church punished transgressions more severely and grew desperate for theoretical justification for its position. If usury was to be banned, as the Bible commands, then this new world that had just discovered reason would require new, non-dogmatic explanations for why the apparently useful practice was wrong.

Over the next four hundred years, theologians and lawyers struggled to reconcile a rational approach to usury with Church dogma on the subject. They dusted off Aristotle's argument on the barrenness of money and reasserted that the profit gained through the practice is unnatural and unjust. To this they added that usury entails an artificial separation between the ownership of goods and the use of those same goods, claiming that lending money is like asking two prices for wine—one price for receiving the wine and an additional price for drinking it—one price for its possession and another for its use. Just as this would be wrong with wine, they argued, so it is

wrong with money: In the case of usury, the borrower in effect pays \$100 for \$100, plus another fee, \$10, for the use of the money that he already paid for and thus already owns.<sup>16</sup>

In similar fashion, it was argued that usury generates for the lender profit from goods that no longer belong to him—that is, from goods now owned by the borrower.<sup>17</sup> As one Scholastic put it: “[He] who gets fruit from that money, whether it be pieces of money or anything else, gets it from a thing which does not belong to him, and it is accordingly all the same as if he were to steal it.”<sup>18</sup>

Another argument against usury from the late Middle Ages went to a crucial aspect of the practice that heretofore had not been addressed: the issue of time. Thinkers of this period believed that time was a common good, that it belonged to no one in particular, that it was a gift from God. Thus, they saw usurers as attempting to defraud God.<sup>19</sup> As the 12th-century English theologian Thomas of Chobham (1160–1233) wrote: “The usurer sells nothing to the borrower that belongs to him. He sells only time, which belongs to God. He can therefore not make a profit from selling someone else’s property.”<sup>20</sup> Or as expressed in a 13th-century manuscript, “Every man stops working on holidays, but the oxen of usury work unceasingly and thus offend God and all the Saints; and, since usury is an endless sin, it should in like manner be endlessly punished.”<sup>21</sup>

Although the identification of the value of time and its relationship to interest was used here in an argument *against* usury, this point is actually a crucial aspect of the argument in *defense* of the practice. Indeed, interest is compensation for a delay in using one’s funds. It is compensation for the usurer’s time away from his money. And although recognition of an individual’s ownership of his own time was still centuries away, this early acknowledgment of the relationship of time and interest was a major milestone.

The Scholastics came to similar conclusions about usury as those reached by earlier Christian thinkers, but they sought to defend their views not only by reference to scripture, but also by reference to their observational understanding of the economics of the practice. The economic worth of usury—its productivity or unproductively—became their central concern. The question became: Is money barren? Does usury have a productive function? What are the facts?

This is the long arm of Aristotle at work. Having discovered

Aristotle's method of observation-based logic, the Scholastics began to focus on reality, and, to the extent that they did, they turned away from faith and away from the Bible. It would take hundreds of years for this perspective to develop fully, but the type of arguments made during the late Middle Ages were early contributions to this crucial development.

As virtuous as this new method was, however, the Scholastics were still coming to the conclusion that usury is unproductive and immoral, and it would not be until the 16th century and the Reformation that usury would be partially accepted by the Church and civil law. For the time being, usury remained forbidden—at least in theory.

Church officials, particularly from the 12th century on, frequently manipulated and selectively enforced the usury laws to bolster the financial power of the Church. When it wanted to keep its own borrowing cost low, the Church enforced the usury prohibition. At other times, the Church itself readily loaned money for interest. Monks were among the earliest moneylenders, offering carefully disguised interest-bearing loans throughout the Middle Ages.

The most common way to disguise loans—and the way in which banking began in Italy and grew to be a major business—was through money exchange. The wide variety of currencies made monetary exchange necessary but difficult, which led to certain merchants specializing in the field. With the rapid growth of international trade, these operations grew dramatically in scale, and merchants opened offices in cities all across Europe and the eastern Mediterranean. These merchants used the complexities associated with exchange of different currencies to hide loans and charge interest. For example, a loan might be made in one currency and returned in another months later in a different location—although the amount returned would be higher (i.e., would include an interest payment), this would be disguised by a new exchange rate. This is one of many mechanisms usurers and merchants invented to circumvent the restrictions. As one commentator notes, “the interest element in such dealings [was] normally . . . hidden by the nature of the transactions either in foreign exchange or as bills of exchange or, frequently, as both.”<sup>22</sup> By such means, these merchants took deposits, loaned money, and made payments across borders, thus creating the beginnings of the modern

banking system.

Although the merchant credit extended by these early banks was technically interest, and thus usury, both the papal and civic authorities permitted the practice, because the exchange service proved enormously valuable to both. In addition to financing all kinds of trade across vast distances for countless merchants, such lending also financed the Crusades for the Church and various wars for various kings.<sup>23</sup> Everyone wanted what usury had to offer, yet no one understood exactly what that was. So while the Church continued to forbid usury and punish transgressors, it also actively engaged in the practice. What was seen as moral by the Church apparently was not seen as wholly practical by the Church, and opportunity became the mother of evasion.

The Church also engaged in opportunistic behavior when it came to restitution. Where so-called “victims” of usury were known, the Church provided them with restitution from the usurer. But in cases where the “victims” were not known, the Church still collected restitution, which it supposedly directed to “the poor” or other “pious purposes.” Clerics were sold licenses empowering them to procure such restitution, and, as a result, the number of usurers prosecuted where there was no identifiable “victim” was far greater than it otherwise would have been. The death of a wealthy merchant often provided the Church with windfall revenue. In the 13th century, the Pope laid claim to the assets of deceased usurers in England. He directed his agents to “inquire concerning living (and dead) usurers and the thing wrongfully acquired by this wicked usury . . . and . . . compel opponents by ecclesiastical censure.”<sup>24</sup>

Also of note, Church officials regularly ignored the usury of their important friends—such as the Florentine bankers of the Medici family—while demonizing Jewish moneylenders and others. The result was that the image of the merchant usurer was dichotomized into “two disparate figures who stood at opposite poles: the degraded manifest usurer-pawnbroker, as often as not a Jew; and the city father, arbiter of elegance, patron of the arts, devout philanthropist, the merchant prince [yet no less a usurer!].”<sup>25</sup>

In theory, the Church was staunchly opposed to usury; in practice, however, it was violating its own moral law in myriad ways. The gap between the idea of usury as immoral and the idea of usury as

impractical continued to widen as the evidence for its practicality continued to grow. The Church would not budge on the moral status, but it selectively practiced the vice nonetheless.

This selective approach often correlated with the economic times. When the economy was doing well, the Church, and the civil authorities, often looked the other way and let the usurers play. In bad times, however, moneylenders, particularly those who were Jewish, became the scapegoats. (This pattern continues today with anti-interest sentiment exploding whenever there is an economic downturn.)

To facilitate the Church's selective opposition to usury, and to avoid the stigma associated with the practice, religious and civil authorities created many loopholes in the prohibition. Sometime around 1220, a new term was coined to replace certain forms of usury: the concept of interest.<sup>26</sup> Under circumstances where usury was legal, it would now be called the collecting of interest. In cases where the practice was illegal, it would continue to be called usury.<sup>27</sup>

The modern word "interest" derives from the Latin verb *intereo*, which means "to be lost." Interest was considered compensation for a loss that a creditor had incurred through lending. Compensation for a loan was illegal if it was a gain or a profit, but if it was reimbursement for a loss or an expense it was permissible. Interest was, in a sense, "damages," not profit. Therefore, interest was sometimes allowed, but usury never.

So, increasingly, moneylenders were allowed to charge interest as a penalty for delayed repayment of a loan, provided that the lender preferred repayment to the delay plus interest (i.e., provided that it was seen as a sacrifice). Loans were often structured in advance so that such delays were anticipated and priced, and so the prohibition on usury was avoided. Many known moneylenders and bankers, such as the Belgian Lombards, derived their profits from such penalties—often 100 percent of the loan value.<sup>28</sup>

Over time, the view of costs or damages for the lender was expanded, and the lender's time and effort in making the loan were permitted as a reason for charging interest. It even became permissible on occasion for a lender to charge interest if he could show an obvious, profitable alternative use for the money. If, by lending money, the lender suffered from the inability to make a profit elsewhere, the interest was allowed as compensation for the potential

loss. Indeed, according to some sources, even risk—economic risk—was viewed as worthy of compensation. Therefore, if there was risk that the debtor would not pay, interest charged in advance was permissible.<sup>29</sup>

These were major breakthroughs. Recognition of the economic need for advanced calculation of a venture's risk, and for compensation in advance for that risk, were giant steps in the understanding of and justification for moneylending.

But despite all these breakthroughs and the fact that economic activity continued to grow during the later Middle Ages, the prohibition on usury was still selectively enforced. Usurers were often forced to pay restitution; many were driven to poverty or excommunicated; and some, especially Jewish moneylenders, were violently attacked and murdered. It was still a very high-risk profession.

Not only were usurers in danger on Earth; they were also threatened with the "Divine justice" that awaited them after death.<sup>30</sup> They were considered the devil's henchmen and were sure to go to Hell. It was common to hear stories of usurers going mad in old age out of fear of what awaited them in the afterlife.

The Italian poet Dante (1265–1321) placed usurers in the seventh circle of Hell, incorporating the traditional medieval punishment for usury, which was eternity with a heavy bag of money around one's neck: "From each neck there hung an enormous purse, each marked with its own beast and its own colors like a coat of arms. On these their streaming eyes appeared to feast."<sup>31</sup> Usurers in Dante's Hell are forever weighed down by their greed. Profits, Dante believed, should be the fruits of labor—and usury entailed no actual work. He believed that the deliberate, intellectual choice to engage in such an unnatural action as usury was the worst kind of sin.<sup>32</sup>

It is a wonder that anyone—let alone so many—defied the law and their faith to practice moneylending. In this sense, the usurers were truly heroic. By defying religion and taking risks—both financial and existential—they made their material lives better. They made money. And by doing so, they made possible economic growth the likes of which had never been seen before. It was thanks to a series of loans from local moneylenders that Gutenberg, for example, was able to commercialize his printing press.<sup>33</sup> The early bankers enabled advances in commerce and industry throughout Europe, financing

the Age of Exploration as well as the early seeds of technology that would ultimately lead to the Industrial Revolution.

By the end of the Middle Ages, although everyone still condemned usury, few could deny its practical value. Everyone “knew” that moneylending was ethically wrong, but everyone could also *see* that it was economically beneficial. Its moral status was divinely decreed and appeared to be supported by reason, yet merchants and businessmen *experienced* its practical benefits daily. The thinkers of the day could not explain this apparent dichotomy. And, in the centuries that followed, although man’s understanding of the economic value of usury would advance, his moral attitude toward the practice would remain one of contempt.

### **Renaissance and Reformation**

The start of the 16th century brought about a commercial boom in Europe. It was the Golden Age of Exploration. Trade routes opened to the New World and expanded to the East, bringing unprecedented trade and wealth to Europe. To fund this trade, to supply credit for commerce and the beginnings of industry, banks were established throughout Europe. Genoese and German bankers funded Spanish and Portuguese exploration and the importation of New World gold and silver. Part of what made this financial activity possible was the new tolerance, in some cities, of usury.

The Italian city of Genoa, for example, had a relatively relaxed attitude toward usury, and moneylenders created many ways to circumvent the existing prohibitions. It was clear to the city’s leaders that the financial activities of its merchants were crucial to Genoa’s prosperity, and the local courts regularly turned a blind eye to the usurious activities of its merchants and bankers. Although the Church often complained about these activities, Genoa’s political importance prevented the Church from acting against the city.

The Catholic Church’s official view toward usury remained unchanged until the 19th century, but the Reformation—which occurred principally in northern Europe—brought about a mild acceptance of usury. (This is likely one reason why southern Europe, which was heavily Catholic, lagged behind the rest of Europe economically



from the 17th century onward.) Martin Luther (1483–1546), a leader of the Reformation, believed that usury was inevitable and should be permitted to some extent by civil law. Luther believed in the separation of civil law and Christian ethics. This view, however, resulted not from a belief in the separation of state and religion, but from his belief that the world and man were too corrupt to be guided by Christianity. Christian ethics and the Old Testament commandments, he argued, are utopian dreams, unconnected with political or economic reality. He deemed usury unpreventable and thus a matter for the secular authorities, who should permit the practice and control it.

However, Luther still considered usury a grave sin, and in his later years wrote:

[T]here is on earth no greater enemy of man, after the Devil, than a gripe-money and usurer, for he wants to be God over all men. . . . And since we break on the wheel and behead highwaymen, murderers, and housebreakers, how much more ought we to break on the wheel and kill . . . hunt down, curse, and behead all usurers!<sup>34</sup>

In other words, usury should be allowed by civil authorities (as in Genoa) because it is inevitable (men will be men), but it should be condemned in the harshest terms by the moral authority. This is the moral-practical dichotomy in action, sanctioned by an extremely malevolent view of man and the universe.

John Calvin, (1509–1564), another Reformation theologian, had a more lenient view than Luther. He rejected the notion that usury is actually banned in the Bible. Since Jews are allowed to charge interest from strangers, God cannot be against usury. It would be fantastic, Calvin thought, to imagine that by “strangers” God meant the enemies of the Jews; and it would be most unchristian to legalize discrimination. According to Calvin, usury does not always conflict with God’s law, so not all usurers need to be damned. There is a difference, he believed, between taking usury in the course of business and setting up business as a usurer. If a person collects interest on only one occasion, he is not a usurer. The crucial issue, Calvin thought, is the motive. If the motive is to help others, usury is good, but if the motive is personal profit, usury is evil.

Calvin claimed that the moral status of usury should be determined

by the golden rule. It should be allowed only insofar as it does not run counter to Christian fairness and charity. Interest should never be charged to a man in urgent need, or to a poor man; the “welfare of the state” should always be considered. But it could be charged in cases where the borrower is wealthy and the interest will be used for Christian good. Thus he concluded that interest could neither be universally condemned nor universally permitted—but that, to protect the poor, a maximum rate should be set by law and never exceeded.<sup>35</sup>

Although the religious authorities did little to free usury from the taint of immorality, other thinkers were significantly furthering the economic understanding of the practice. In a book titled *Treatise on Contracts and Usury*, Molinaeus, a French jurist, made important contributions to liberate usury from Scholastic rationalism.<sup>36</sup> By this time, there was sufficient evidence for a logical thinker to see the merits of moneylending. Against the argument that money is barren, Molinaeus (1500–1566) observed that everyday experience of business life showed that the use of any considerable sum of money yields a service of importance. He argued, by reference to observation and logic, that money, assisted by human effort, does “bear fruit” in the form of new wealth; the money enables the borrower to create goods that he otherwise would not have been able to create. Just as Galileo would later apply Aristotle’s method of observation and logic in refuting Aristotle’s specific ideas in physics, so Molinaeus used Aristotle’s method in refuting Aristotle’s basic objection to usury. Unfortunately, like Galileo, Molinaeus was to suffer for his ideas: The Church forced him into exile and banned his book. Nevertheless, his ideas on usury spread throughout Europe and had a significant impact on future discussions of moneylending.<sup>37</sup>

The prevailing view that emerged in the late 16th century (and that, to a large extent, is still with us today) is that money is not barren and that usury plays a productive role in the economy. Usury, however, is unchristian; it is motivated by a desire for profit and can be used to exploit the poor. It can be practical, but it is not moral; therefore, it should be controlled by the state and subjected to regulation in order to restrain the rich and protect the poor.

This Christian view has influenced almost all attitudes about usury since. In a sense, Luther and Calvin *are* responsible for today’s so-called capitalism. They are responsible for the guilt many people feel

from making money and the guilt that causes people to eagerly regulate the functions of capitalists. Moreover, the Protestants were the first to explicitly assert and sanction the moral-practical dichotomy—the idea that the moral and the practical are necessarily at odds. Because of original sin, the Protestants argued, men are incapable of being good, and thus concessions must be made in accordance with their wicked nature. Men must be permitted to some extent to engage in practical matters such as usury, even though such practices are immoral.

In spite of its horrific view of man, life, and reality, Luther and Calvin's brand of Christianity allowed individuals who were not intimidated by Christian theology to practice moneylending to some extent without legal persecution. Although still limited by government constraints, the chains were loosened, and this enabled economic progress through the periodic establishment of legal rates of interest.

The first country to establish a legal rate of interest was England in 1545 during the reign of Henry VIII. The rate was set at 10 percent. However, seven years later it was repealed, and usury was again completely banned. In an argument in 1571 to reinstate the bill, Mr. Molley, a lawyer representing the business interests in London, said before the House of Commons:

Since to take reasonably, or so that both parties might do good, was not hurtful; . . . God did not so hate it, that he did utterly forbid it, but to the Jews amongst themselves only, for that he willed they should lend as Brethren together; for unto all others they were at large; and therefore to this day they are the greatest Usurers in the World. But be it, as indeed it is, evil, and that men are men, no Saints, to do all these things perfectly, uprightly and Brotherly; . . . and better may it be born to permit a little, than utterly to take away and prohibit Traffick; which hardly may be maintained generally without this.

But it may be said, it is contrary to the direct word of God, and therefore an ill Law; if it were to appoint men to take Usury, it were to be disliked; but the difference is great between that and permitting or allowing, or suffering a matter to be unpunished.<sup>38</sup>

Observe that while pleading for a bill permitting usury—on the grounds that it is necessary (“Traffick . . . hardly may be maintained

generally without [it]”—Molley concedes that it is evil. This is the moral-practical dichotomy stated openly and in black-and-white terms, and it illustrates the general attitude of the era. The practice was now widely accepted as practical but still regarded as immoral, and the thinkers of the day grappled with this new context.

One of England’s most significant 17th-century intellectuals, Francis Bacon (1561–1626), realized the benefits that moneylending offered to merchants and traders by providing them with capital. He also recognized the usurer’s value in providing liquidity to consumers and businesses. And, although Bacon believed that the moral ideal would be lending at 0 percent interest, as the Bible requires, he, like Luther, saw this as utopian and held that “it is better to mitigate usury by declaration than suffer it to rage by connivance.” Bacon therefore proposed two rates of usury: one set at a maximum of 5 percent and allowable to everyone; and a second rate, higher than 5 percent, allowable only to certain licensed persons and lent only to known merchants. The license was to be sold by the state for a fee.<sup>39</sup>

Again, interest and usury were pitted against morality. But Bacon saw moneylending as so important to commerce that the legal rate of interest had to offer sufficient incentive to attract lenders. Bacon recognized that a higher rate of interest is economically justified by the nature of certain loans.<sup>40</sup>

The economic debate had shifted from whether usury should be legal to whether and at what level government should set the interest rate (a debate that, of course, continues to this day, with the Fed setting certain interest rates). As one scholar put it: “The legal toleration of interest marked a revolutionary change in public opinion and gave a clear indication of the *divorce of ethics from economics* under the pressure of an expanding economic system.”<sup>41</sup>

In spite of this progress, artists continued to compare usurers to idle drones, spiders, and bloodsuckers, and playwrights personified the moneygrubbing usurers in characters such as Sir Giles Overreach, Messrs. Mammon, Lucre, Hoard, Gripe, and Bloodhound. Probably the greatest work of art vilifying the usurer was written during this period—*The Merchant of Venice* by Shakespeare (1564–1616), which immortalized the character of the evil Jewish usurer, Shylock.

In *The Merchant of Venice*, Bassanio, a poor nobleman, needs cash in order to court the heiress, Portia. Bassanio goes to a Jewish

moneylender, Shylock, for a loan, bringing his wealthy friend, Antonio, to stand as surety for it. Shylock, who has suffered great rudeness from Antonio in business, demands as security for the loan not Antonio's property, which he identifies as being at risk, but a pound of his flesh.<sup>42</sup>

The conflict between Shylock and Antonio incorporates all the elements of the arguments against usury. Antonio, the Christian, lends money and demands no interest. As Shylock describes him:

Shy. [Aside.] How like a fawning publican he looks!  
I hate him for he is a Christian;  
But more for that in low simplicity  
He lends out money gratis, and brings down  
The rate of usance here with us in Venice.  
If I can catch him once upon the hip,  
I will feed fat the ancient grudge I bear him.  
He hates our sacred nation, and he rails,  
Even there where merchants most do congregate,  
On me, my bargains, and my well-won thrift,  
Which he calls interest. Cursed be my tribe,  
If I forgive him!<sup>43</sup>

Shylock takes usury. He is portrayed as the lowly, angry, vengeful, and greedy Jew. When his daughter elopes and takes her father's money with her, he cries, "My daughter! O my ducats! Oh my daughter!"<sup>44</sup> —not sure for which he cares more.

It is clear that Shakespeare understood the issues involved in usury. Note Shylock's (legitimate) hostility toward Antonio because Antonio loaned money without charging interest and thus brought down the market rate of interest in Venice. Even Aristotle's "barren money" argument is present. Antonio, provoking Shylock, says:

If thou wilt lend this money, lend it not  
As to thy friends,—for when did friendship take  
A breed for barren metal of his friend?—  
But lend it rather to thine enemy:  
Who if he break, thou mayst with better face  
Exact the penalty.<sup>45</sup>

Friends do not take “breed for barren metal” from friends; usury is something one takes only from an enemy.

Great art plays a crucial role in shaping popular attitudes, and Shakespeare’s depiction of Shylock, like Dante’s depiction of usurers, concretized for generations the dichotomous view of money-lending and thus helped entrench the alleged link between usury and evil. As late as 1600, medieval moral and economic theories were alive and well, even if they were increasingly out of step with the economic practice of the time.

## The Enlightenment

During the Enlightenment, the European economy continued to grow, culminating with the Industrial Revolution. This growth involved increased activity in every sector of the economy. Banking houses were established to provide credit to a wide array of economic endeavors. The Baring Brothers and the House of Rothschild were just the largest of the many banks that would ultimately help fuel the Industrial Revolution, funding railroads, factories, ports, and industry in general.

Economic understanding of the important productive role of usury continued to improve over the next four hundred years. Yet, the moral evaluation of usury would change very little. The morality of altruism—the notion that self-sacrifice is moral and that self-interest is evil—was embraced and defended by many Enlightenment intellectuals and continued to hamper the acceptability of usury. After all, usury is a naked example of the pursuit of profit—which is patently self-interested. Further, it still seemed to the thinkers of the time that usury could be a zero-sum transaction—that a rich lender might profit at the expense of a poor borrower. Even a better conception of usury—let alone the misconception of it being a zero-sum transaction—is anathema to altruism, which demands the opposite of personal profit: self-sacrifice for the sake of others.

In the mid-17th century, northern Europe was home to a new generation of scholars who recognized that usury served an essential economic purpose, and that it should be allowed freely. Three men made significant contributions in this regard.

Claudius Salmasius (1588–1653), a French scholar teaching in Holland, thoroughly refuted the claims about the “barrenness” of moneylending; he showed the important productive function of usury and even suggested that there should be more usurers, since competition between them would reduce the rate of interest. Other Dutch scholars agreed with him, and, partially as a result of this, Holland became especially tolerant of usury, making it legal at times. Consequently, the leading banks of the era were found in Holland, and it became the world’s commercial and financial center, the wealthiest state in Europe, and the envy of the world.<sup>46</sup>

Anne-Robert-Jacques Turgot (1727–1781), a French economist, was the first to identify usury’s connection to property rights. He argued that a creditor has the right to dispose of his money in any way he wishes and at whatever rate the market will bear, because it is *his* property. Turgot was also the first economist to fully understand that the passing of time changes the value of money. He saw the difference between the present value and the future value of money—concepts that are at the heart of any modern financial analysis. According to Turgot: “If . . . two gentlemen suppose that a sum of 1000 Francs and a promise of 1000 Francs possess exactly the same value, they put forward a still more absurd supposition; for if these two things were of equal value, why should any one borrow at all?”<sup>47</sup> Turgot even repudiated the medieval notion that time belonged to God. Time, he argued, belongs to the individual who uses it and therefore time could be sold.<sup>48</sup>

During the same period, the British philosopher Jeremy Bentham (1748–1832) wrote a treatise entitled *A Defense of Usury*. Bentham argued that any restrictions on interest rates were economically harmful because they restricted an innovator’s ability to raise capital. Since innovative trades inherently involved high risk, they could only be funded at high interest rates. Limits on permissible interest rates, he argued, would kill innovation—the engine of growth. Correcting another medieval error, Bentham also showed that restrictive usury laws actually harmed the borrowers. Such restrictions cause the credit markets to shrink while demand for credit remains the same or goes up; thus, potential borrowers have to seek loans in an illegal market where they would have to pay a premium for the additional risk of illegal trading.

Bentham's most important contribution was his advocacy of contractual freedom:

My neighbours, being at liberty, have happened to concur among themselves in dealing at a certain rate of interest. I, who have money to lend, and Titus, who wants to borrow it of me, would be glad, the one of us to accept, the other to give, an interest somewhat higher than theirs: Why is the liberty they exercise to be made a pretence for depriving me and Titus of ours.<sup>49</sup>

This was perhaps the first attempt at a moral defense of usury.

Unfortunately, Bentham and his followers undercut this effort with their philosophy of utilitarianism, according to which rights, liberty, and therefore moneylending, were valuable only insofar as they increased "social utility": "the greatest good for the greatest number." Bentham famously dismissed individual rights—the idea that each person should be free to act on his own judgment—as "nonsense upon stilts."<sup>50</sup> He embraced the idea that the individual has a "duty" to serve the well-being of the collective, or, as he put it, the "general mass of felicity."<sup>51</sup> Thus, in addition to undercutting Turgot's major achievement, Bentham also doomed the first effort at a moral defense of usury—which he himself had proposed.

An explicitly utilitarian attempt at a moral defense of usury was launched in 1774 in the anonymously published *Letters on Usury and Interest*. The goal of the book was to explain why usury should be accepted in England of the 18th century, and why this acceptance did not contradict the Church's teachings. The ultimate reason, the author argued, is one of utility:

Here, then, is a sure and infallible rule to judge of the lawfulness of a practice. Is it useful to the State? Is it beneficial to the individuals that compose it? Either of these is sufficient to obtain a tolerance; but both together vest it with a character of justice and equity. . . . In fact, if we look into the laws of different nations concerning usury, we shall find that they are all formed on the principle of public utility. In those states where usury was found hurtful to society, it was prohibited. In those where it was neither hurtful nor very beneficial, it was tolerated. In those where it was useful, it was authorized. In ours, it is absolutely necessary.<sup>52</sup>



And:

[T]he practice of lending money to interest is in this nation, and under this constitution, beneficial to all degrees; therefore it is beneficial to society. I say in this nation; which, as long as it continues to be a commercial one, must be chiefly supported by interest; for interest is the soul of credit and credit is the soul of commerce.<sup>53</sup>

Although the utilitarian argument in defense of usury contains some economic truth, it is morally bankrupt. Utilitarian moral reasoning for the propriety of usury depends on the perceived benefits of the practice to the collective or the nation. But what happens, for example, when usury in the form of sub-prime mortgage loans creates distress for a significant number of people and financial turmoil in some markets? How can it be justified? Indeed, it cannot. The utilitarian argument collapses in the face of any such economic problem, leaving moneylenders exposed to the wrath of the public and to the whips and chains of politicians seeking a scapegoat for the crisis.

Although Salmasius, Turgot, and Bentham made significant progress in understanding the economic and political value of usury, not all their fellow intellectuals followed suit. The father of economics, Adam Smith (1723–1790), wrote: “As something can everywhere be made by the use of money, something ought everywhere to be paid for the use of it.”<sup>54</sup> Simple and elegant. Yet, Smith also believed that the government must control the rate of interest. He believed that unfettered markets would create excessively high interest rates, which would hurt the economy—which, in turn, would harm society.<sup>55</sup> Because Smith thought that society’s welfare was the only justification for usury, he held that the government must intervene to correct the errors of the “invisible hand.”

Although Smith was a great innovator in economics, philosophically, he was a follower. He accepted the common philosophical ideas of his time, including altruism, of which utilitarianism is a form. Like Bentham, he justified capitalism only through its social benefits. If his projections of what would come to pass in a fully free market amounted to a less-than-optimal solution for society, then he advocated government intervention. Government intervention is the logical outcome of any utilitarian defense of usury.

(Smith’s idea that there need be a “perfect” legal interest rate remains with us to this day. His notion of such a rate was that it should be slightly higher than the market rate—what he called the “golden mean.” The chairman of the Federal Reserve is today’s very *visible* hand, constantly searching for the “perfect” rate or “golden mean” by alternately establishing artificially low and artificially high rates.)

Following Bentham and Smith, all significant 19th-century economists—such as David Ricardo, Jean Baptiste Say, and John Stuart Mill—considered the economic importance of usury to be obvious and argued that interest rates should be determined by freely contracting individuals. These economists, followed later by the Austrians—especially Carl Menger, Eugen von Böhm-Bawerk, and Ludwig von Mises—developed sound theories of the productivity of interest and gained a significant economic understanding of its practical role. But the moral-practical dichotomy inherent in their altruistic, utilitarian, social justification for usury remained in play, and the practice continued to be morally condemned and thus heavily regulated if not outlawed.

### **The 19th and 20th Centuries**

Despite their flaws, the thinkers of the Enlightenment had created sufficient economic understanding to fuel the Industrial Revolution throughout the 19th century. Economically and politically, facts and reason had triumphed over faith; a sense of individualism had taken hold; the practicality of the profit motive had become clear; and, relative to eras past, the West was thriving.

Morally and philosophically, however, big trouble was brewing. As capitalism neared a glorious maturity, a new, more consistent brand of altruism, created by Kant, Hegel, and their followers, was sweeping Europe. At the political-economic level, this movement manifested itself in the ideas of Karl Marx (1818–1883).

Marx, exploiting the errors of the Classical economists, professed the medieval notion that all production is a result of manual labor; but he also elaborated, claiming that laborers do not retain the wealth they create. The capitalists, he said, take advantage of their control over the means of production—secured to them by private property—and

“loot” the laborers’ work. According to Marx, moneylending and other financial activities are not productive, but exploitative; moneylenders exert no effort, do no productive work, and yet reap the rewards of production through usury.<sup>56</sup> As one 20th-century Marxist put it: “The major argument against usury is that labor constitutes the true source of wealth.”<sup>57</sup> Marx adopted all the medieval clichés, including the notion that Jews are devious, conniving money-grubbers.

What is the profane basis of Judaism? *Practical need, self-interest.*  
What is the worldly cult of the Jew? *Huckstering.* What is his worldly god? *Money.*

Money is the jealous god of Israel, beside which no other god may exist. Money abases all the gods of mankind and changes them into commodities.<sup>58</sup>

Marx believed that the Jews were evil—not because of their religion, as others were clamoring at the time—but because they pursued their own selfish interests and sought to make money. And Marxists were not alone in their contempt for these qualities.

Artists who, like Marx, resented capitalists in general and moneylenders in particular, dominated Western culture in the 19th century. In Dickens’s *A Christmas Carol*, we see the moneygrubbing Ebenezer Scrooge. In Dostoyevsky’s *Crime and Punishment*, the disgusting old lady whom Raskolnikov murders is a usurer. And in *The Brothers Karamazov*, Dostoyevsky writes:

It was known too that the young person had . . . been given to what is called “speculation,” and that she had shown marked abilities in the direction, so that many people began to say that she was no better than a Jew. It was not that she lent money on interest, but it was known, for instance, that she had for some time past, in partnership with old Karamazov, actually invested in the purchase of bad debts for a trifle, a tenth of their nominal value, and afterwards had made out of them ten times their value.<sup>59</sup>

In other words, she was what in the 1980s became known as a “vulture” capitalist buying up distressed debt.

Under Marx’s influential ideas, and given the culture-wide con-

tempt for moneylenders, the great era of capitalism—of thriving banks and general financial success—was petering out. Popular sentiment concerning usury was reverting to a Dark Ages-type of hatred. Marx and company put the moneylenders back into Dante's *Inferno*, and to this day they have not been able to escape.

The need for capital, however, would not be suppressed by the label “immoral.” People still sought to start businesses and purchase homes; thus usury was still seen as practical. Like the Church of the Middle Ages, people found themselves simultaneously condemning the practice and engaging in it.

Consequently, just as the term “interest” had been coined in the Middle Ages to facilitate the Church's selective opposition to usury and to avoid the stigma associated with the practice, so modern man employed the term for the same purpose. The concept of moneylending was again split into two allegedly different concepts: the charging of “interest” and the practice of “usury.” Lending at “interest” came to designate lower-premium, lower-risk, less-greedy lending, while “usury” came to mean specifically higher-premium, higher-risk, more-greedy lending. This artificial division enabled the wealthier, more powerful, more influential people to freely engage in moneylending with the one hand, while continuing to condemn the practice with the other. Loans made to lower-risk, higher-income borrowers would be treated as morally acceptable, while those made to higher-risk, lower-income borrowers would remain morally contemptible. (The term “usury” is now almost universally taken to mean “excessive” or illegal premium on loans, while the term “interest” designates tolerable or legal premium.)

From the 19th century onward, in the United States and in most other countries, usury laws would restrict the rates of interest that could be charged on loans, and there would be an ongoing battle between businessmen and legislators over what those rates should be. These laws, too, are still with us.

As Bentham predicted, such laws harm not only lenders but also borrowers, who are driven into the shadows where they procure shady and often illegal loans in order to acquire the capital they need for their endeavors. And given the extra risk posed by potential legal complications for the lenders, these loans are sold at substantially higher interest rates than they would be if moneylending were fully

legal and unregulated.

In the United States, demand for high-risk loans has always existed, and entrepreneurs have always arisen to service the demand for funds. They have been scorned, condemned to Hell, assaulted, jailed, and generally treated like the usurers of the Middle Ages—but they have relentlessly supplied the capital that has enabled Americans to achieve unprecedented levels of productiveness and prosperity.

The earliest known advertisement for a small-loan service in an American newspaper appeared in the *Chicago Tribune* in November 1869. By 1872, the industry was prospering. Loans collateralized by furniture, diamonds, warehouse receipts, houses, and pianos were available (called “chattel” loans). The first salary-loan office (offering loans made in advance of a paycheck) was opened by John Mulholland in Kansas City in 1893. Within fifteen years he had offices all across the country. The going rate on a chattel loan was 10 percent a month for loans under \$50, and 5–7 percent a month for larger loans. Some loans were made at very high rates, occasionally over 100 percent a month.<sup>60</sup>

The reason rates were so high is because of the number of defaults. With high rates in play, the losses on loans in default could ordinarily be absorbed as a cost of doing business. In this respect, the 19th-century small-loan business was a precursor of the 20th-century “junk” bond business or the 21st-century sub-prime mortgage lender. However, unlike the “junk” bond salesman, who had recourse to the law in cases of default or bankruptcy, these small-loan men operated on the fringes of society—and often outside the law. Because of the social stigmatization and legal isolation of the creditors, legal recourse against a defaulting borrower was generally unavailable to a usurer. Yet these back-alley loans provided a valuable service—one for which there was great demand—and they enabled many people to start their own businesses or improve their lives in other ways.

Of course, whereas most of these borrowers paid off their loans and succeeded in their endeavors, many of them got into financial trouble—and the latter cases, not the former, were widely publicized. The moneylenders were blamed, and restrictions were multiplied and tightened.

In spite of all the restrictions, laws, and persecutions, the market found ways to continue. In 1910, Arthur Morris set up the first bank

in America with the express purpose of providing small loans to individuals at interest rates based on the borrower's "character and earning power." In spite of the usury limit of 6 percent that existed in Virginia at the time, Morris's bank found ways, as did usurers in the Middle Ages, to make loans at what appeared to be a 6 percent interest rate while the actual rates were much higher and more appropriate. For instance, a loan for \$100 might be made as follows: A commission of 2 percent plus the 6 percent legal rate would be taken off the top in advance; thus the borrower would receive \$92. Then he would repay the loan at \$2 a week over fifty weeks. The effective compound annual interest rate on such a loan was in excess of 18 percent. And penalties would be assessed for any delinquent payments.<sup>61</sup> Such camouflaged interest rates were a throwback to the Middle Ages, when bankers developed innovative ways to circumvent the restrictions on usury established by the Church. And, as in the Middle Ages, such lending became common as the demand for capital was widespread. Consequently, these banks multiplied and thrived—for a while.

(Today's credit card industry is the successor to such institutions. Credit card lenders charge high interest rates to high-risk customers, and penalties for delinquency. And borrowers use these loans for consumption as well as to start or fund small businesses. And, of course, the credit card industry is regularly attacked for its high rates of interest and its "exploitation" of customers. To this day, credit card interest rates are restricted by usury laws, and legislation attempting to further restrict these rates is periodically introduced.)

In 1913, in New York, a moneylender who issued loans to people who could not get them at conventional banks appeared before a court on the charge of usury. In the decision, the judge wrote:

You are one of the most contemptible usurers in your unspeakable business. The poor people must be protected from such sharks as you, and we must trust that your conviction and sentence will be a notice to you and all your kind that the courts have found a way to put a stop to usury. Men of your type are a curse to the community, and the money they gain is blood money.<sup>62</sup>

This ruling is indicative of the general attitude toward usurers at

the time. The moral-practical dichotomy was alive and kicking, and the moneylenders were taking the blows. Although their practical value to the economy was now clear, their moral status as evil was still common “sense.” And the intellectuals of the day would only exacerbate the problem.

The most influential economist of the 20th century was John Maynard Keynes (1883–1946), whose ideas not only shaped the theoretical field of modern economics but also played a major role in shaping government policies in the United States and around the world. Although Keynes allegedly rejected Marx’s ideas, he shared Marx’s hatred of the profit motive and usury. He also agreed with Adam Smith that government must control interest rates; otherwise investment and thus society would suffer. And he revived the old Reformation idea that usury is a necessary evil:

When the accumulation of wealth is no longer of high social importance, there will be great changes in the code of morals. We shall be able to rid ourselves of many of the pseudo-moral principles which have hag-ridden us for two hundred years, by which we have exalted some of the most distasteful of human qualities into the position of the highest virtues. . . . But beware! The time for all this is not yet. For at least another hundred years we must pretend to ourselves and to everyone that fair is foul and foul is fair; for foul is useful and fair is not. Avarice and usury and precaution must be our gods for a little longer still. For only they can lead us out of the tunnel of economic necessity into daylight.<sup>63</sup>

Although Keynes and other economists and intellectuals of the day recognized the need of usury, they universally condemned the practice and its practitioners as foul and unfair. Thus, regardless of widespread recognition of the fact that usury is a boon to the economy, when the Great Depression occurred in the United States, the moneylenders on Wall Street were blamed. As Franklin Delano Roosevelt put it:

The rulers of the exchange of mankind’s goods have failed, through their own stubbornness and their own incompetence, have admitted failure, and have abdicated. Practices of the unscrupulous money changers stand indicted in the court of public opinion,

rejected by the hearts and minds of men . . . [We must] apply social values more noble than mere monetary profit.<sup>64</sup>

And so the “solution” to the problems of the Great Depression was greater government intervention throughout the economy—especially in the regulation of interest and the institutions that deal in it. After 1933, banks were restricted in all aspects of their activity: the interest rates they could pay their clients, the rates they could charge, and to whom they could lend. In 1934, the greatest bank in American history, J. P. Morgan, was broken up by the government into several companies. The massive regulations and coercive restructurings of the 1930s illustrate the continuing contempt for the practice of taking interest on loans and the continuing distrust of those—now mainly bankers—who engage in this activity. (We paid a dear price for those regulations with the savings and loan crisis of the 1970s and 1980s, which cost American taxpayers hundreds of billions of dollars.<sup>65</sup> And we continue to pay the price of these regulations in higher taxes, greater financial costs, lost innovation, and stifled economic growth.)

## The 21st Century

From ancient Greece and Rome to the Dark and Middle Ages, to the Renaissance and Reformation, to the 19th and 20th centuries, money-lending has been morally condemned and legally restrained. Today, at the dawn of the 21st century, moneylending remains a pariah.

One of the latest victims of this moral antagonism is the business of providing payday loans. This highly popular and beneficial service has been branded with the scarlet letter “U”; consequently, despite the great demand for these loans, the practice has been relegated to the fringes of society and the edge of the law. These loans carry annualized interest rates as high as 1000 percent, because they are typically very short term (i.e., to be paid back on payday). By some estimates there are 25,000 payday stores across America, and it is “a \$6 billion dollar industry serving 15 million people every month.”<sup>66</sup> The institutions issuing these loans have found ways, just as banks always have, to circumvent state usury laws. Bank regulators have severely restricted the ability of community banks to offer payday



loans or even to work with payday loan offices, more than 13 states have banned them altogether, and Congress is currently looking at ways to ban all payday loans.<sup>67</sup> This is in spite of the fact that demand for these loans is soaring and that they serve a genuine economic need, that they are a real value for low-income households. As the *Wall Street Journal* reports: “Georgia outlawed payday loans in 2004, and thousands of workers have since taken to traveling over the border to find payday stores in Tennessee, Florida and South Carolina. So the effect of the ban has been to increase consumer credit costs and inconvenience for Georgia consumers.”<sup>68</sup>

A story in the *LA Weekly*, titled “Shylock 2000”—ignoring the great demand for payday loans, ignoring the economic value they provide to countless borrowers, and ignoring the fact that the loans are made by mutual consent to mutual advantage—proceeded to describe horrific stories of borrowers who have gone bankrupt. The article concluded: “What’s astonishing about this story is that, 400 years after Shakespeare created the avaricious lender Shylock, such usury may be perfectly legal.”<sup>69</sup>

What is truly astonishing is that after centuries of moneylenders providing capital and opportunities to billions of willing people on mutually agreed-upon terms, the image of these persistent businessmen has not advanced beyond that of Shylock.

The “Shylocks” du jour, of course, are the sub-prime mortgage lenders, with whom this article began. These lenders provided mortgages designed to enable low-income borrowers to buy homes. Because the default rate among these borrowers is relatively high, the loans are recognized as high-risk transactions and are sold at correspondingly high rates of interest. Although it is common knowledge that many of these loans are now in default, and although it is widely believed that the lenders are to blame for the situation, what is not well known is, as Paul Harvey would say, “the rest of the story.”

The tremendous growth in this industry is a direct consequence of government policy. Since the 1930s, the U.S. government has encouraged home ownership among all Americans—but especially among those in lower income brackets. To this end, the government created the Federal Home Loan Banks (which are exempt from state and local income taxes) to provide incentives for smaller banks to make mortgage loans to low-income Americans. Congress passed

the Community Reinvestment Act, which requires banks to invest in their local communities, including by providing mortgage loans to people in low-income brackets. The government created Fannie Mae and Freddie Mac, both of which have a mandate to issue and guarantee mortgage loans to low-income borrowers.

In recent years, all these government schemes and more (e.g., artificially low interest rates orchestrated by the Fed) led to a frenzy of borrowing and lending. The bottom line is that the government has artificially mitigated lenders' risk, and it has done so on the perverse, altruistic premise that "society" has a moral duty to increase home ownership among low-income Americans. The consequence of this folly has been a significant increase in delinquent loans and foreclosures, which has led to wider financial problems at banks and at other institutions that purchased the mortgages in the secondary markets.

Any objective evaluation of the facts would place the blame for this disaster on the government policies that caused it. But no—just as in the past, the lenders are being blamed and scapegoated.

Although some of these lenders clearly did take irrational risks on many of these loans, that should be their own problem, and they should have to suffer the consequences of their irrational actions—whether significant financial loss or bankruptcy. (The government most certainly should not bail them out.) However, without the perception of reduced risk provided by government meddling in the economy, far fewer lenders would have been so frivolous.

Further, the number of people benefiting from sub-prime mortgage loans, which make it possible for many people to purchase a home for the first time, is in the millions—and the vast majority of these borrowers are *not* delinquent or in default; rather, they are paying off their loans and enjoying their homes, a fact never mentioned by the media.

It should also be noted that, whereas the mortgage companies are blamed for all the defaulting loans, no blame is placed on the irresponsible borrowers who took upon themselves debt that they knew—or should have known—they could not handle.

After four hundred years of markets proving the incredible benefits generated by moneylending, intellectuals, journalists, and politicians still rail against lenders and their institutions. And, in spite of all the damage done by legal restrictions on interest, regulation of non-

eylenders, and government interference in financial markets, whenever there is an economic “crisis,” there is invariably a wave of demand for *more* of these controls, not less.

Moneylenders are still blamed for recessions; they are still accused of being greedy and of taking advantage of the poor; they are still portrayed on TV and in movies as slick, murderous villains; and they are still distrusted by almost everyone. (According to a recent poll, only 16 percent of Americans have substantial confidence in the American financial industry.<sup>70</sup>) Thus, it should come as no surprise that the financial sector is the most regulated, most controlled industry in America today.

But what explains the ongoing antipathy toward, distrust of, and coercion against these bearers of capital and opportunity? What explains the modern anti-moneylending mentality? Why are moneylenders today held in essentially the same ill repute as they were in the Middle Ages?

The explanation for this lies in the fact that, fundamentally, 21st-century ethics is no different from the ethics of the Middle Ages.

All parties in the assault on usury share a common ethical root: altruism—belief in the notion that self-sacrifice is moral and self-interest is evil. This is the source of the problem. So long as self-interest is condemned, neither usury in particular, nor profit in general, can be seen as good—both will be seen as evil.

Moneylending cannot be defended by reference to its economic practicality alone. If moneylending is to be recognized as a fully legitimate practice and defended accordingly, then its defenders must discover and embrace a new code of ethics, one that upholds self-interest—and thus personal profit—as moral.

## Conclusion

Although serious economists today uniformly recognize the economic benefits of charging interest or usury on loans, they rarely, if ever, attempt a philosophical or moral defense of this position. Today’s economists either reject philosophy completely or adopt the moral-practical split, accepting the notion that although usury is practical, it is either immoral or, at best, amoral.

Modern philosophers, for the most part, have no interest in the

topic at all, partly because it requires them to deal with reality, and partly because they believe self-interest, capitalism, and everything they entail, to be evil. Today's philosophers, almost to a man, accept self-sacrifice as the standard of morality and physical labor as the source of wealth. Thus, to the extent that they refer to moneylending at all, they consider it unquestionably unjust, and positions to the contrary unworthy of debate.

It is time to set the record straight.

Whereas Aristotle *united* productiveness with morality and thereby condemned usury as immoral based on his mistaken belief that the practice is unproductive—and whereas everyone since Aristotle (including contemporary economists and philosophers) has *severed* productiveness from morality and condemned usury on biblical or altruistic grounds as immoral (or at best amoral)—what is needed is a view that again *unifies* productiveness and morality, but that also sees usury as productive, and morality as the means to practical success on earth. What is needed is the economic knowledge of the last millennium *combined with* a new moral theory—one that upholds the morality of self-interest and thus the virtue of personal profit.

Let us first condense the key economic points; then we will turn to a brief indication of the morality of self-interest.

The crucial economic knowledge necessary to a proper defense of usury includes an understanding of why lenders charge interest on money—and why they would do so even in a risk-free, noninflationary environment. Lenders charge interest because their money has alternative uses—uses they temporarily forego by lending the money to borrowers. When a lender lends money, he is thereby unable to use that money toward some benefit or profit for himself. Had he not lent it, he could have spent it on consumer goods that he would have enjoyed, or he could have invested it in alternative moneymaking ventures. And the longer the term of the loan, the longer the lender must postpone his alternative use of the money. Thus interest is charged because the lender views the loan as a better, more profitable use of his money over the period of the loan than any of his alternative uses of the same funds over the same time; he estimates that, given the interest charged, the benefit to him is greater from making the loan than from any other use of his capital.<sup>71</sup>

A lender tries to calculate in advance the likelihood or unlikeli-

hood that he will be repaid all his capital plus the interest. The less convinced he is that a loan will be repaid, the higher the interest rate he will charge. Higher rates enable lenders to profit for their willingness to take greater risks. The practice of charging interest is therefore an expression of the human ability to project the future, to plan, to analyze, to calculate risk, and to act in the face of uncertainty. In a word, it is an expression of man's ability to reason. The better a lender's thinking, the more money he will make.

Another economic principle that is essential to a proper defense of usury is recognition of the fact that moneylending is *productive*. This fact was made increasingly clear over the centuries, and today it is incontrovertible. By choosing to whom he will lend money, the moneylender determines which projects he will help bring into existence and which individuals he will provide with opportunities to improve the quality of their lives and his. Thus, lenders make themselves money by rewarding people for the virtues of innovation, productiveness, personal responsibility, and entrepreneurial talent; and they withhold their sanction, thus minimizing their losses, from people who exhibit signs of stagnation, laziness, irresponsibility, and inefficiency. The lender, in seeking profit, does not consider the well-being of society or of the borrower. Rather, he assesses his alternatives, evaluates the risk, and seeks the greatest return on his investment.

And, of course, lent money is not "barren"; it is fruitful: It enables borrowers to improve their lives or produce new goods or services. Nor is moneylending a zero-sum game: Both the borrower and the lender benefit from the exchange (as ultimately does everyone involved in the economy). The lender makes a profit, and the borrower gets to use capital—whether for consumption or investment purposes—that he otherwise would not be able to use.<sup>72</sup>

An understanding of these and other economic principles is necessary to defend the practice of usury. But such an understanding is *not* sufficient to defend the practice. From the brief history we have recounted, it is evident that all commentators on usury from the beginning of time have known that those who charge interest are self-interested, that the very nature of their activity is motivated by personal profit. Thus, in order to defend moneylenders, their institutions, and the kind of world they make possible, one must be armed with a moral code that recognizes rational self-interest and therefore the

pursuit of profit as moral, and that consequently regards productivity as a virtue and upholds man's right to his property and to his time.

There is such a morality: It is Ayn Rand's Objectivist ethics, or rational egoism, and it is the missing link in the defense of usury (and capitalism in general).

According to rational egoism, man's life—the life of each individual man—is the standard of moral value, and his reasoning mind is his basic means of living. Being moral, on this view, consists in thinking and producing the values on which one's life and happiness depend—while leaving others free to think and act on their own judgment for their own sake. The Objectivist ethics holds that people should act rationally, in their own long-term best interest; that each person is the proper beneficiary of his own actions; that each person has a moral right to keep, use, and dispose of the product of his efforts; and that each individual is capable of thinking for himself, of producing values, and of deciding whether, with whom, and on what terms he will trade. It is a morality of self-interest, individual rights, and personal responsibility. And it is grounded in the fundamental fact of human nature: the fact that man's basic means of living is his ability to reason.

Ayn Rand identified the principle that the greatest productive, life-serving power on earth is not human muscle but the human mind. Consequently, she regarded profit-seeking—the use of the mind to identify, produce, and trade life-serving values—as the essence of being moral.<sup>73</sup>

Ayn Rand's Objectivist ethics is essential to the defense of moneylending. It provides the moral foundation without which economic arguments in defense of usury cannot prevail. It demonstrates why moneylending is supremely *moral*.

The Objectivist ethics frees moneylenders from the shackles of Dante's inferno, enables them to brush off Shakespeare's ridicule, and empowers them to take an irrefutable moral stand against persecution and regulation by the state. The day that this moral code becomes widely embraced will be the day that moneylenders—and every other producer of value—will be completely free to charge whatever rates their customers will pay and to reap the rewards righteously and proudly.

If this moral ideal were made a political reality, then, for the first

time in history, moneylenders, bankers, and their institutions would be legally permitted and morally encouraged to work to their fullest potential, making profits by providing the lifeblood of capital to our economy. Given what these heroes have achieved while scorned and shackled, it is hard to imagine what their productive achievements would be if they were revered and freed.

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