

(March 27, 1933)

Canada's Monetary Policy

By PROFESSOR J. P. DAY.

PRESIDENT CHALMERS:—To-day, we have the pleasure of hearing an address on an important subject, "Canada's Monetary Policy," by Dr. J. P. Day who is Associate Professor of economics at McGill University. Professor Day I have known ever since his arrival in Canada ten years ago. I have always been impressed with the fact that he is an economist without a panacea for the world's troubles. He speaks with the calm, good sense that we expect from the Scot. Professor Day is not a Scot but he has the background of the University of St. Andrew's where he was lecturer in economics before coming to Canada. I have great pleasure in asking him to address you.

PROFESSOR DAY:—I thank you, Mr. Chairman, for your kind introduction. I thank you, gentlemen, for the opportunity you are giving me to speak to you this morning. I am not an entertaining speaker, as many of you know, but I do welcome the opportunity of speaking to an audience like this on a subject which, as your chairman has said and as you know, is one of very considerable importance to all of us.

May I begin by drawing your attention to the very singular position in which Canada stands with regard to her money. If you look round the rest of the world, what do you see? Many of the countries, over thirty anyhow, have, so far as international trade is concerned, reverted to barter. The exporter to such a country can only receive the money of that country. He can only be paid in money that is of use to him to buy goods from that country.

Now, apart from those countries, taking the rest of the

world where the foreign exchange is still free—I do not mean the export of gold is free, but you are free to buy foreign currencies if you get a quotation—taking the rest of the world in mentioning the freedom of exchange, Canada is in a singularly unique position. Other countries of the world fall into two groups. There is the group which includes Britain, Egypt, India and the Scandinavian countries and their monetary policy is to maintain the purchasing power of their money to whatever level suits them best—the level that best suits their economic welfare. Lately South Africa has joined that group and Australia and New Zealand also. Just at present, I suppose that group would not be averse to a rise in the price level but, under normal conditions, it would mean that sterling would keep the stable purchasing power of the other countries of the group and keep foreign exchanges steady. There is a second group called the gold group, comprising Switzerland, Belgium, Holland, France and the United States, and their monetary policy is to maintain the purchasing power of their money as represented by the gold content of the coin. And since, as we know, gold has appreciated some thirty per cent since September, 1931, it means that their money has been steadily rising in purchasing power and prices have been correspondingly falling. The assurance that their money is equal to gold is the right of redemption but, as we have seen recently, the United States has, for a time, taken away that right and has even gone so far as to threaten to fine and imprison those of her citizens who have exercised their legal right to change their money into gold. I suggest to you, gentlemen, that means faith in the guarantee of redemption is worth nothing at all. I have never believed that it was worth anything. I have told my students that the belief that you have faith in money, that you can get gold for it, is foolish and that there is nothing to back it up. When conditions are better your faith is all right—when money is as good as gold and you do not want gold and do not ask for it, but as soon as the country begins to ask for gold then the government says, "We cannot let you have it." That will always happen and has always happened

but, I never expected to live to see the day when the government would say to those who have turned their money into gold, "You will go to jail if you do not turn it back." It means this, really, that the guarantee of being able to redeem your money in gold is worthless now.

The only faith that countries have that their money will maintain its value is that the government will manage the currency satisfactorily and the only faith in the American dollar to-day is that the American Government will so manage the currency that it will maintain the value of their dollar equivalent to gold parity.

Now, practically midway between those groups we have one lone country—one country by itself—our own country, Canada. Why is that? I think it is worth thinking about. Is it a result of any monetary policy? Is there a degree of management—any sort of management, which is responsible for that position? Well, to a certain extent, it is the result of conscious action. The Government prohibited the export of gold except under license but I think the resulting position has been just due to economic forces and not to any conscious management at all. Our trade with Britain and the Empire pulls us towards sterling. Our trade and financial relationships with the United States pulls us towards the dollar and gold. We drift in between. The point is do we want to drift? One answer to that may be, whether we want to drift or not, we cannot help it, because we have not, in this country, developed the necessary mechanism for controlling our faith. I do not want to speak to you to-day on how that necessary mechanism may be obtained. But on that point I would just like to say this, that though I do not think it is necessary to introduce into this country some imitation of a Central Bank from a country outside, yet I do think we need some additional mechanism which will enable us to achieve what a Central Bank is supposed to achieve—the formulation of a monetary policy, which shall be in the interests of the nation as a whole, and effective power to enforce it. I think we need that. I do not mind how it comes. I think we need someone who is responsible. We want them to have that responsibility and to accept it so that we can hold them responsible.

What I am to talk to you about to-day, however, is: what should our monetary policy be? Now, there are four possible policies. Only two of them, I think, are worthy of consideration. We might go back to gold by deflation. That means paring down our prices until our money is worth more, until, eventually, it becomes on a parity with the United States dollar. The country could not stand that. If I had the time I would like to speak at length on these two policies. I will only say, until the future of gold is a good deal less uncertain than it is at present, I do not see any advantage at all in returning to it. That leaves us with only two policies: the policy of drift, going on as we are at the present time; or the policy of inflation, reducing the value of our money to the sterling level or to whatever level may suit us.

Now, the simplest and most characteristic form of inflation is the printing of additional money. There are all sorts of other forms. Every day I get men coming to me with some ingenious schemes of inflation. They all amount very much to the same thing and the effect is to decrease the purchasing power of every dollar in the country. It is, of course, absurd to say that you can have inflation without commodity prices rising or to think that prices did not rise in Britain. They did rise. If gold had not fallen thirty per cent in value, British prices would have been very much higher in actual figures. It is only a chance that gold happened to fall at the same time. Inflation, indeed, has a hidden effect on all who hold cash or receive cash. If you have \$100 and the Government taxes you \$20, surely it is the same thing if they had never taxed you anything at all—or \$100 paid not more than \$80. Inflation is a hidden tax on all who hold cash and who receive cash. It is equally a tax on the poor man's dollar as on the rich man's dollar. Moreover, it is not a tax on any of the rich man's wealth except on the cash he has in his pocket, the cash deposit in the bank or any money he may have out on loan. It is not a tax on his property or on any of his capital except liquid capital. Moreover, in so far as additional money is going to be used for providing

work for those at present unemployed, you would find prices would rise first and most in the case of necessities and that the tax, in reality, therefore, is very much harder on the poor man's dollar than on the rich man's.

If the wealthier classes of this country were as selfish as a few think they are, they would welcome inflation. Another obvious unfairness is that some wages and some salaries have already been reduced. If you have inflation, you will have a uniform reduction and some people will be suffering twice over. I doubt very much whether we would do well to welcome any additional taxation at this time. What we want is government economy. Not only do we want it but all other countries want it. Governments have got into the habit of regarding with complacent familiarity, long rows of figures that would have made Mr. Gladstone insane even to look at. It is just, unfortunately, that we have got used to them.

However, if we have to have additional taxation, do not let us have any hidden or unjust form of inflation. Now, the answer of the inflationist is this. Those of them who know what they are talking about is what I mean. I do not want to try and be superior, but there is a division. They say, "We know that this means hidden and unequal taxation, unpleasant and rather of the nature of a subterfuge, but it will cause a revival of business, for prices will rise and business will become profitable again. Prices will rise, the cost of production especially, wages will not rise but will nominally be at the same figure but actually be lowered." The essence of the plan is this, inflation is the easiest and quickest way of bringing about a universal reduction of wages and salaries and so making business profitable again. Now, added to that is the plan that it will bring relief to the debtor classes and that it is a very important point. I am an inflationist for the world at large. I do not see any way out of the economic distress into which the world has got unless you have a general rise of commodity prices. But for this country alone, in isolation, to attempt, or even to dally with, the policy of inflation would, I am sure, be a fatal mistake. One of the forms economic

disease takes to-day is in panic flights from currency. We have seen flights from the mark, flights from the franc, flights from sterling and the tremendous selling of the American dollar. You are dealing with the world in a very nervous state of affairs with regard to any currencies. If there were any reason to believe that the Canadian dollar was likely to depreciate because of probable action of our government on the policy of inflation, some foreigners would, at once, withdraw their money from Canada and the result would be that the Canadian dollar would fall on the exchange and when it started to fall there would begin a tremendous flood of selling of Canadian securities and Canadian money. Our securities would slump on the exchange and our money would slump on the foreign exchange. We should get into the class of the foreign countries I spoke of at the start and our foreign trade would vanish.

Fear of inflation, coupled with some doubt as to how we are going to meet our foreign commitments this year and some doubt as to how these tremendous contingent liabilities which the Dominion Government has taken over are likely to work out, those three things are reasons why our money is under-valued. It is under-valued. We are not getting for the Canadian dollar what it is really worth. I want to drive that point home because it is an important point—to some extent it is rather a cheerful point which may be useful to us by and by.

Now, what known means should determine what money is worth? Its purchasing power over commodities: the piece of money which will buy most is worth most. Now, that is not academic nonsense. It is plain common sense. The piece of money which will buy most is worth most. Since 1926, the United States dollar has been increasing in purchasing power as prices have fallen and the index number for commodity prices in the United States has fallen from 100 in 1926 to 63 last December. Now, our money has increased in value almost exactly to the same extent. The index number for last December was 64. If our dollar, therefore, is maintaining its parity of purchasing power,

why is it not maintaining its parity on the foreign exchanges? The two chief reasons, obviously, are the agitation for inflation—partly the agitation for inflation and partly the half-hearted attempts of the Government at economy. The reason why we have to pay more to meet our obligations in the United States than we should have to pay; the reason why we have to pay more for our imports than we should pay; the reason why we do not get as much as we should get for our exports is the premium on New York funds. That premium only exists because of a fear that we shall not be able to hold our present position. Our money is really worth as much as theirs. These are the two things which have been forcing down the exchange value of money: fear that we may be going into inflation and doubt as to how the Government is going to carry out its obligations on these heavy commitments. I would ask you to note in passing that for neither of these two factors are the banks or banking system responsible.

If, then, we reject inflation as a monetary policy, we are left with the policy of drift—what Mr. Rhodes calls allowing the dollar to find its own level. It is perhaps not right to call it a policy of drift. You might call it a policy of taking no risk. It is silly to try and cross the ice when it may break under one's weight. We do not want to do anything which would be risky at present and which, in a few months time, may be simple because of arrangements the World Economic Conference may make. Our own immediate policy, therefore, should be to try to keep our dollar where it is, strengthening the underlying position by strict economy in public expenditure and by reduction of interest rates both on deposit accounts and on loans. I am strongly in favor of that. I think, therefore, we might very well strengthen our position by the strictest economy in public expenditures while seeking to maintain foreign confidence in our dollar and also to prevent any developing tendency of a rise in value. That may come. You may find the Canadian dollar tending to go up. I do not know that we are particularly anxious to see it go up at present. We would do well to keep money where it is. This waiting

policy, I know, is putting a great strain on the patience of our people. I know there will be a lot of people in this room who would like to say something of this sort to me. I have still got a job. I have just had an excellent lunch free. But supposing I were in the position of a good many people to-day who are having to cut down their standard of living and having their hopes of doing something or other for their family swept away—supposing I were in the position of the unemployed with that bitterness that bites so deeply—should I still be complacently advocating a policy of doing nothing for a month or so? Well, I hope so, gentlemen. What you are really asking me is: if I were desperate, should I recommend taking nothing rather than anything; should I recommend jumping out of the frying pan into the fire? This great country of ours is linked up with the rest of the world by trade, migrations, and financial links of all kinds. This is a world depression. The causes are world-wide and the remedy must be international. I say, unfortunately, we must wait a little bit longer.

We are waiting for the World Economic Conference. The disease is international and the cure must be. The country which will come out best from this economic distress is the country whose citizens will keep their heads and their sense of social solidarity with all that it implies. It implies a great deal—mutual helpfulness and things of that kind. Enduring these last three, long, evil years, the people of Canada have shown a splendid spirit of patience, forbearance and fortitude and, believe me, gentlemen, they will not be without their reward.

PRESIDENT CHALMERS:—Dr. Day, I wish on behalf of the members of the Canadian Club to thank you for your most interesting address. This has been the second half of the debate on the subject of inflation. Last November we had an address from another gentleman from your city who gave us an address on the other side. He was more of an inflationist than you are. After a lapse of a few months, it is good to have the other side of the case set before us. I knew that your address would be interesting and would be expressed in language simple enough to suit

the mentality of the chairman and others who attempt to keep up with the changing tides of economic knowledge and find it practically impossible. We hope that when economic conditions throughout the world have changed somewhat and you will be able to point back and look back on what has happened in the next two years, that you will come again and give us another address. We thank you.