

THE  
FUTURE OF EXCHANGE  
AND THE  
INDIAN CURRENCY

THE  
FUTURE OF EXCHANGE  
AND THE  
INDIAN CURRENCY

BY

H. STANLEY JEVONS

PROFESSOR OF ECONOMICS IN THE UNIVERSITY OF ALLAHABAD

1922

HUMPHREY MILFORD  
OXFORD UNIVERSITY PRESS  
LONDON BOMBAY MADRAS CALCUTTA

Printed by Apurva Krishna Bose, at The Indian Press, Ltd.,  
Allahabad.

## PREFACE

This book is written for readers in India, and everything is expressed from the Indian point of view. It is not intended to be a scientific treatise, nor in any sense an academic discussion of currency and exchange; neither is it a popular exposition of the subject. It is designed more especially for the information and assistance of business men in India, for those engaged in public affairs, and for all who take a keen and understanding interest in the problems of exchange.

At first my intention was to limit the book to an attempt to forecast the probable course of exchange during the next year or two; and the first eight chapters were written with that purpose. Continued study of the subject led to the alteration of my views as to the permanent policy which ought to be adopted in regard to exchange; and I seemed to arrive at conclusions of some novelty and importance. I therefore wrote three more chapters, leading

up to the last and longest which sets forth a practicable policy for the immediate attainment of stability, and defines the principles which should guide the subsequent regulation of currency and exchange.

Since the deplorable failure of the policy recommended by the Exchange and Currency Committee of 1919, it has become the fashion to decry the advice of "doctrinaires" and "theorists." Whilst the Government has adopted "a policy of masterly inaction"—apparently not knowing which way to turn—the general demand is for a solution of the problem to be found by men of commerce and affairs. It is because of this appeal to business men, and because any change of policy will, I hope, be decided by the Legislative Assembly, that this book has been written with the special purpose of indicating the bearing of economic theory on the exchange problem. I make no apology for being a theorist; for, without a profound knowledge of theory, a true understanding of the very complicated factors influencing exchange is impossible. The objection to the theorist does not lie in the fact that he applies theory to a practical problem—which it is as essential for the financier to do as it is for the engineer—but rather in the application of theory without a

sufficient appreciation of the facts of the situation, and with a deficient judgment of the probable effects of the changes proposed. That was how the mistakes in 1920 came to be made. I was one of the first to recommend the adoption of the two-shilling exchange in a lengthy letter to the "Pioneer" of Allahabad in 1919;<sup>1</sup> but I think I may claim that if my proposal that the exchange rate should be raised "by one penny at a time whenever the demand for Councils becomes particularly strong"<sup>2</sup> had been adopted, the exchange crisis of 1920 might have been averted (or at least very much modified), and so the 2s. rate might conceivably have been maintained.

This book, then, is an attempt to present just those parts of economic theory which bear upon the exchange problem in its present form, and the principal relevant facts. There is a logical sequence in the development of ideas throughout each part of the book; and a desire to marshal the facts for each section fully has led to a certain amount of repetition. Moreover, I have adopted the rather risky device of proving certain things to be possible which I do not advocate. For all these reasons I

<sup>1</sup> Issue of June 12th, 1919, p. 7.

<sup>2</sup> See my written statement of evidence. Report of Committee on Indian Exchange and Currency, Vol. III, Appendices (1920), p. 148.

must beg the reader to be good enough to read the whole book ; or, at any rate, not to judge of any proposals by reading detached portions. The casual reader might well say that I am making impracticable proposals ; but I venture to think that if he reads all I have said, and considers carefully, he will be converted to the view that my actual proposals, as summarised at the end of the last chapter, are eminently practicable, and would confer an immense and early benefit on the country's trade. I can only add that I have not spared myself in thinking these proposals over again and again, and in testing them by reference to all the facts of the present situation that I can ascertain, and by comparison with all the suggestions which other people have been making for the solution of the present difficulties.

Such a book as this deals mainly with an immediate problem and current conditions, and ought therefore to be written at a given moment and published instantly like a daily paper. With many other duties claiming my time, the writing has taken several months ; but worse still has been a pause in the printing due to the strike on the East Indian Railway, which caused a delay of over two months in receiving a needed consignment of paper. The

whole of the book was written and in type, except a portion of the last chapter, when the situation was modified by the Government accepting in the Legislative Assembly, on 22nd March, 1922, Sir Montagu Webb's amendment to the Finance Bill, suspending for 1921-22 and 1922-23 the operation of Section 13 (c) of the Paper Currency Act (1920) requiring the interest on the securities in the Reserve to be applied to reducing the "created securities." Frequent references to this provision of the Paper Currency Act would have been omitted or altered had this event occurred before going to press.

Another event not recorded in the body of the book is the first issue, in March, 1922, of Currency notes to the amount of Rs. 2 crores against internal bills of exchange (presumably mainly *hundis*) according to the provision incorporated in law for the first time in the Paper Currency Act of 1920. The occasion for utilizing this resource was doubtless the tightness of the money-market and need of funds for financing the crops.

A result of the unavoidable delay in issuing the book is that some of the statistics are not quite so up-to-date as I hoped they would have been. To remedy this defect I have arranged for a supplement to be printed and inserted



at the end of the book after it is bound. In this way most of the monthly statistics are brought up to the end of March, 1922; and a few even later.

In conclusion, I wish to express my cordial thanks to gentlemen in official positions who have assisted me with information, and to assistants—old students of my Department—who have helped me by collating and setting out the statistics. Willing labor is always given in the search for India's welfare.

To Mr. D. S. Dubey, Lecturer on Economics in Allahabad, I am indebted for the preparation of the index.

# CONTENTS

	PAGE
CHAPTER I	
GOVERNMENT AND EXCHANGE	
Introductory Remarks	1
Indian and English Currency Systems	2
The Status of Gold	4
The Present Price of Gold in India	7
Status of the Paper Currency	9
Paper Currency Reserve	12
Gold Standard Reserve	20
CHAPTER II	
PRICES AND VOLUME OF CIRCULATION	
Quantity Theory of Money	25
Prices with Gold Currency	30
Inelastic Representative Currency	32
Inflation of the Currency in India during the War	34
Silver in Circulation	36
Paper Currency Circulation	41
Total Circulation and Prices	43
Mechanism of the Inflation of the Currency	46
Government and Inflation	50
Deflation of the Currency	55

CHAPTER III		PAGE
WORLD WIDE TRADE DEPRESSION		
The Short-Lived Boom		60
Beginning of the Collapse		61
Present Level of World Prices		64
Volume of Trade		66
CHAPTER IV		
CAUSES OF THE TRADE DEPRESSION		
Causes of the Collapse of Prices in 1920-21		72
Destructive Effects of the War		74
Disorganized Exchanges		76
Disposal of Government Surplus Stocks		78
Cycle of Trade Fluctuations		80
CHAPTER V		
HARVESTS AND TRADE FLUCTUATIONS		
The $3\frac{1}{2}$ years period of oscillation		85
Variability of the World's Harvests		90
Influence of Harvests on Trade		91
CHAPTER VI		
PROBABLE FUTURE COURSE OF PRICES		
Effects of Falling World Prices		95
Extent of the Fall of Prices		98
The Napoleonic Parallel		99
Secular Change of Price Level		103
Duration of the Fall of Prices		107
The Near Future		111

## CONTENTS

ix

### CHAPTER VII

	PAGE
GOVERNMENT'S EXCHANGE POLICY	
Policy limited by Economic Conditions	117
The Two-Shilling Rupee	119
Gold Standard Reserve	120
The Government's Policy	126
Deficits and Inflation	128
Policy as regards Gold	136

### CHAPTER VIII

THE PROBABLE COURSE OF EXCHANGE	
Trustworthiness of Forecasts	137
Exchange Policy	139
Relative Price Levels	141
The Balance of Trade—Imports	142
Export Trade	144
Gold and Silver	147
Movements of Funds	149
European Exchanges	150
General Summary	152

### CHAPTER IX

TARIFF POLICY AND EXCHANGE	
Policy of Protection Probable	155
Effect of Protective Tariff on Foreign Trade	158
Effect upon Exchange	160
Effects of Export Duties	162
Import of Capital	165

## CONTENTS

CHAPTER X		PAGE
PRICE LEVEL POLICY		
Connection between Price-Level and Exchange		168
The Effects of Rising Prices		170
The Currency Committee on High Prices		172
Price Movements since 1919		174
Effects of a Fall of Prices		177
Desirable Restriction of the Fall of Prices		180
CHAPTER XI		
STABILITY OF EXCHANGE		
Early Attainment of Stability Essential		183
Contraction of the Circulation		185
Amount of Contraction Necessary		189
Ways of Contracting the Circulation		190
Difficulties of Deflation		193
Mobilization of the Currency Medium		196
Urgency of Regaining Stability		198
CHAPTER XII		
THE POLICY ADVOCATED		
Abandonment of the 2s. Exchange		201
Immediate Stability at 1s. 4d.		203
Deflation		208
Sale of Reverse Councils		213
Abolition of the Gold Standard Reserve		216
Future of the Paper Currency Reserve		220
Proposed Limit to Securities in the Reserve		225
The Gold Currency Alternative		228
Organization of the Money Market		231
The Finance of Deficits		234

## CONTENTS

xi

	Page
Control of Currency Policy	237
A Currency Commission in India	242
Summary of Proposals	244

## APPENDIX

Index Numbers of Prices in India	249
Table of Exchange Rates, 1917 to 1922	255
Index of Contents	257
Supplement containing latest Statistics	<i>(See after Index)</i>