

INDIA'S
CURRENCY EXCHANGE
AND
BANKING PROBLEMS

1925—1928

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THE BOOK COMPANY, LTD.,
COLLEGE SQUARE, CALCUTTA.

Published by
GIRINDRA NATH MITRA
THE BOOK COMPANY, LTD.,
4/4A, College Square, Calcutta

June, 1928

Printer : S. C. MAJUMDAR
SRI GOURANGA PRESS
71/1, Mirzapur Street, Calcutta.

NOTE.

I venture to place this brochure before the public in the hope that it might assist the public in general and students of economic matters in particular, to make up their minds about the main issues in the present controversy on Indian Exchange, Currency and Banking. The articles contained in the brochure have appeared as contributions to local newspapers. I am obliged to the "*Statesman*" for the publication of one of the interviews. My obligations are even greater to the "*Forward*" and to its editors who have displayed a generous and impartial spirit in allowing some of the other contributions to appear in its columns. Obviously a newspaper follows the true path of journalistic duty when it allows both sides to have their say, leaving the public to sit in judgment on the issues. I am also much indebted to the editor of the "*Capital*" for his kind permission to include three recent articles on Banking contributed to that paper. I have also to thank Mr. H. Sinha, M.Sc., Mr. Manoranjan Bhattacharyya, M.A. and Mr. S. Roy, M.A. for encouragement or assistance in getting the pages through the press.

J. C. C.

THE 1s. 6d. RATIO AND AGRICULTURE* IS ADJUSTMENT TO 1s. 6d., COMPLETE?

VERDICT OF CO-OPERATIVE STATISTICS

ISSUES RAISED IN THE CONTROVERSY

The first question put to the professor was whether the adjustment to the new ratio had already come about and, if so, what were the economic tests to be applied.

“In my opinion” replied Prof. Coyajee, “the method selected by the Royal Currency Commission to prove the fact of the new adjustment is a proper and convincing one. It shows the adjustment of prices to the ratio, by demonstrating a close relation over a sufficiently long period between former prices in India and the rise of exchange.”

A Table with Triple Distinction.

When asked to elaborate his views in this matter, he proceeded to say: “Let us turn to the table cited in the Minute of Dissent, paragraph 94. This table has enjoyed the triple good fortune of having been utilised by the writers of the Report; of having been accepted and cited by Sir Purshottamdas Thakurdas; and of having been brought up-to-date by the Finance Member himself. This table thus can be accepted for the purposes of this controversy as authoritative.

“Sir Basil Blackett deduced the following results from this table: ‘80 per cent. of the adjustment of prices of commodities at 1s. 6d. ratio had already taken place a month before the Commission’s report.’ In this at least, Sir Purshottamdas is not behind the Finance Member and makes a notable admission, which has not been properly remarked upon.”

* This interview appeared in the “*Forward*” of Dec. 24, 1926.

What is Admitted?

Asked as to what was implied in that admission Prof. Coyajee referred to the table published in the "Times of India" dated November 27, and pointed out that, according to Sir P. Thakurdas, out of adjustment of 36 points (176—140) between December, 1922 and May, 1926, an adjustment of 26 points (176—150) had already been achieved. He then went on: "This implies that an adjustment of 73 p. c. has already taken place, which is a great deal of adjustment to expect in complicated economic matters. Further, the value of the admission by Sir Purshottamdas is greatly enhanced by other collateral considerations."

Inconsistencies of Sir P. Thakurdas.

When requested to explain these "collateral considerations." he pointed out that Sir P. Thakurdas was inconsistent when he argued that the process of adjustment of domestic prices to exchange was slow and at the same time assumed that foreign prices quickly reacted on Indian prices. "Sir Purshottamdas would have admitted the full eighty per cent. adjustment, but for the fact that according to him the American prices had fallen by 4 points, Indian prices had been adjusted to this fall forthwith and allowance should be made for this circumstance. But as coming from him it is difficult for us to accept such a quick adjustment of Indian to foreign prices. Indeed his whole case is that in India the adjustment of prices to the exchange is a very slow process indeed. But if this is so, why should the adjustment of Indian prices to foreign prices be so rapid a process as he would not make it out to be when it suits his case—specially as the pace of both sets of adjustment depends on the same circumstance, viz., the proportion of the foreign trade transactions of India to her total commercial transactions. When allowance is made for this consideration, there is little real difference between the position of Sir Purshottamdas and that of the Finance Member. It is therefore inconsistent for Sir Purshottamdas to write in the columns of the "Times of India" of November 27, 1926 that the utmost that he would

concede was that the disturbances involved in the reversion of rs. 4d. should be as great as the disturbances seem to come with the adoption of rs. 6d. He is contradicting himself. Having admitted an adjustment of more than 73 per cent. he now asserts that adjustment is 50 per cent. only. Consequently, in his comparison of 'the arithmetic of both of us' he does not come out so triumphantly as he imagines."

Other "Inconsistencies."

When our reporter pointed out that Sir P. Thakurdas was an able but not the only protagonist for rs. 4d. Prof. Coyajee went on to say, "There are further admissions by other notable authorities on the same side. The fact of adjustment is so undisputable and undeniable and so all-pervading a factor in our economic situation that many of our critics pass it over with wonderful naivete. To take an example, Mr. Madon in his able work on EXCHANGE FALLACIES EXPOSED Part II, pages 15 and 16, urges that the twisting of exchange up from rs. 4d. to rs. 6d. means that all agriculturists must find $12\frac{1}{2}$ per cent. more in the shape of commodities, to meet the charge for interest as well as the debts. But, surely, this is to admit the fact of the fall of prices in commodities in accordance with the new ratio. Because, to say that more goods have to be given for each rupee is the same thing as to say that prices have fallen by $12\frac{1}{2}$ per cent. fully."

"Mr. Madon makes a similar admission when he talks of the additional burden on land revenue and agriculturists which 'is today extracting $12\frac{1}{2}$ per cent. more out of those who have to pay land revenue or rent.' Surely such an able writer as Mr. Madon must not have failed to see that the same appreciated rupee will go further than before in the cultivator's purchases. Thus his cost of living and of production will also fall by $12\frac{1}{2}$ per cent. in terms of the rupee."

Condition of Agriculturists.

The conversation then turned towards the condition of the agriculturists. Our interviewer pointed out that there was an

acute difference of opinion on the subject and enquired what economic tests could be applied to ascertain the present condition of Indian agriculture. "In my opinion," replied the professor, "the Co-operative Societies form a microcosm and give a general idea of the condition of agriculture in India, partly because of the frequent reports published on the conditions of the standard of indebtedness, rate of interest, punctuality in repayment etc., and partly because numerous non-official workers interest themselves in the matter and supplement official reports from first hand knowledge. "Now if the alleged great increase of the burden of debt and the material reduction of cultivators' income were positive facts, we would expect to see the following symptoms making their appearance without fail: (a) the growth of the capital and deposit of the rural societies would have been materially checked and even reduced; (b) proportion of arrears to outstandings would increase largely; (c) the rate of interest would rise remarkably; and (d) loans for unproductive purposes, like repayment of debt, would increase materially."

Growth of Agricultural Capital.

"Coming to the first factor we find a very steady increase of deposit, and share-capital during the whole period when the exchange had been 1s. 6d. The 'Co-operative Statistics' of 1923-24 showed that capital was increasing steadily and stood during September at Rs. 175 per member. The working capital of Central Banks had also increased in the course of the year. "The co-operative Statistics of 1924-25 showed a similar increase of resources. Capital had increased to Rs. 183 per member, while average capital per society had gone up to Rs. 6,730 from Rs. 6,682 in the earlier year. Such a state of things would have been impossible when anything affected an agricultural district.

"Let us come now to arrears and overdues. Here also the figures are as significant as before and more decline has come about.

“As regards the rate of interest, there is no rise at all. On the other hand, during the year of 1923-24 in the United Provinces, the number of Primary Societies which completed 10 years of working were allowed the facilities of getting loans from the Central Bank at reduced rate.”

Loans for Productive purposes.

“Nor is there any sign of any growth of loans for unproductive purposes. The Bombay report of 1924-25 notices that in some places instances were not wanting to indicate that members of the societies had improved their economic condition to such an extent that leaving aside the question of dealing with the Baniyas they had ceased to borrow even from the Societies. The Punjab Report of 1924-25, which analyses the purposes of loans does not show any alteration in their purposes. The Madras Report of 1924-25 observes that tabular analysis of loans indicates that the percentage of loans for non-productive purposes continued to decrease. In the year 1924-25 only Rupees 2'62 lakhs were lent out of the total amount of Rupees 158.33 lakhs. Considering that Madras is an agricultural province and not a rich one at that, we might have expected a vastly larger proportion of loans for redemption of debts, if the burdens on agriculturists were anything like what they have been alluded to be.”

The alleged “Farmers’ ruin.”

“I hope shortly to place before the public a detailed study of these questions. I may remark that even more instructive than the official reports would be to glance at the numerous articles appearing in our Co-operative Journals. These articles are contributed by voluntary and non-official workers who are fully in touch with agricultural conditions. None of them seems to have heard of ‘the farmers’ ruin’ or even of the abnormal distress. In fact that piece of information seems to be the cherished monopoly of a few Bombay industrialists and their friends.”

RYOT AND 1s. 6d. RUPEE*

HAS THE AGRICULTURIST SUFFERED A NET LOSS ?

CURRENCY REPORT JUSTIFIED

Interviewed on behalf of the *Statesman* with regard to the movement in Bombay against the recommendations of the Currency Commission, Professor J. C. Coyajee of the Presidency College in this City and a member of the Commission, gave the following replies to the questions put to him :—

“What is your opinion as regards the facts and statistics brought forward to show that the 1s. 6d. rupee has injured the interests of the Indian agriculturist?”

“The contention has been put forward repeatedly and emphatically that the rise of exchange to 1s. 6d. has mulcted the agriculturist to the extent of 12½ per cent. of the value of his entire produce and has similarly added to his debts.”

“Let us understand what this exactly means in order that we might realize the calamity which would have overtaken the country had the statement been entitled even to the dignity of a half-truth. The change in ratio has been alleged to be the equivalent of a tax of 12½ per cent. not merely on the profits of the farm, but on his whole produce and annual turnover. It is very difficult to envisage this burden without arithmetical figures ; but fortunately there is no lack of statistical efforts to calculate the alleged stupendous levy.” Mr. Madon finds that “the cultivator loses about 40 to 45 crores of rupees a year on some 360 crores of our exports and must lose at least another 40 to 45 crores a year on the portion of the crops that is consumed at home.”

* These views, expressed in course of an interview, appeared in the “*Statesman*” of 16th December, 1926.

“Presumably according to Mr. Madon this immense loss is *continuous*, going on from year to year, irrespective of any price adjustment. The Indian Merchants' Chamber of Bombay puts the increase in the real burden of the agriculturist's debt at 100 crores. Thus we are asked to believe that the annual loss to the agriculturists, due to the exchange ratio is about 200 crores of rupees. Indeed, these losses seem to be growing larger at each repetition, and assuming a *crescendo* movement. Mr. Khaitan goes further and argues that Indian agriculturists got Rs. 250 crores less per year on their crops alone. Further burdens have been added in the shape of losses caused by the rise of exchange to the mortgagees and lessees of agricultural lands. An additional 12½ per cent. loss is to be debited for the supposed increased incidence of the land revenue. To complete the tale of wrong to the agriculturists we heard last month that the agriculturist has lost a few hundred crores more by the fall in the price of silver—itself the effect of the manipulation of exchange. Now if these calculations are at all correct the Indian agriculturist has been robbed of many hundreds of crores of rupees. The resources of the *ryots* must be unlimited indeed to have been able to stand all this.”

Impossible Figures of Burdens.

“These are absolutely impossible figures. Surely, if the facts of life corresponded even remotely to such fearful anticipations, we would have unmistakable signs and symptoms of such a general cataclysm. The first thing we should see would be wide-spread default in the payment of land revenue. The Indian agriculturist, no doubt, honestly faces his normal burdens but such burdens as have recently been imagined for him, would break the back of the wealthiest agricultural community.

“The second symptom to be expected would be an immense number of suits and forfeiture proceedings instituted by *mahajans* and *sahukars* all over the country, because no creditor can rest in peace while his claims are being submerged in such an avalanche of new liabilities, and by now immense areas of

land should have passed into the hands of the *sahukars*. It might be remembered that a much smaller transfer of land to the creditor and the mortgagee brought on the agrarian disturbances which led to the passing of the Punjab Land Alienation Act and the Deccan Agriculturists' Relief Act.

"Mr. Madon tells us in the same pamphlet that the agriculturist 'has no spare money with which he can pay off the *sahukar*. The result will be eviction proceedings and the cultivator and his family will become landless and homeless wanderers going about the country as hired labourers to get such work as they can.' All these might be supposed to be reflected in the statistics of the law courts ; and agricultural and urban wages would be profoundly influenced by such a state of things.

"Mr. Madon, having the courage of his conviction, argues that 'the 18d. rupee leads to a loss to the agriculturist not only of 12½ per cent. of the price, but of all the 100 per cent. of his net earnings, and a further loss of Rs. 20 a *khandy*. It will be at once seen that he will have no margin left to meet either the Government dues or the dues of the *sahukar* and will have to borrow an additional Rs. 20 per *khandy* merely to meet his actual outgoings and keep body and soul together.' Needless to say every line of the statistics of India must bear witness to such a state of things. But as a matter of fact, the statistics of the country have kept going on an even and smooth course and have shown no trace of any, such upsetting factor."

Evidences of Agricultural Prosperity

"What aspect of agricultural economy would you mainly emphasize as disproving the contentions of the advocates of the 1s. 4d. rupee?"

"A study of the last three years' reports of co-operative societies is the most convincing answer to the allegations of the "farmer's ruin." Let us glance at a few relevant incidents in the co-operative history of the last two or three years. The report of co-operative societies in Bombay for 1924-25 informs

us of the all-round progress of central banks, and of the increase of their share capital. The deposits from primary societies in these banks increased largely. The Madras report for the same year shows the following features ; the addition of 1,200 new societies, the persistent fall of loans for non-productive purposes ; and the steady growth of the reserve and deposits of central banks. In the same presidency, the year 1923-24 saw a reduction of the rate of interest and yet the societies continued to work at a profit, while the Registrar observed that the reduction of interest was fully justified. The story can be repeated from other provinces."

Debtors and Creditors.

"How far have the agriculturists been penalized by the higher ratio in their capacity as debtors?"

"The question of equity as between the agriculturist and his creditor is highly complicated and with regard to it easy generalizations are out of place. A little economic analysis might be offered to clear the issues.

"(1) Even assuming that such an increase of burden to the tune of 12½ per cent. has taken place, we should not forget that it is only a partial set off against the earlier and much larger reduction of his debts. Surely, if the agriculturist is entitled to justice, so is his creditor. It is an undeniable fact that the real burden of the farmers' pre-war debts has been greatly reduced, since the purchasing power of the rupee is much lower now than it was in 1914. For many years prices have been falling, with the result that all creditors have been losing and all debtors have been gaining, and the case of the agriculturist is only one out of many. With the reversal of the process, the creditor is only getting back some of his own. To perpetuate the old state of things would be to perpetuate an injustice.

"(2) It is generally known that in the case of the Indian agriculturist, the renewal of debts at intervals is a very common practice. As the renewal takes place on a rupee for rupee basis,

we have another way in which rural indebtedness has been scaled down during the period of rising prices.

“(3) We have also to remember that a great deal of the rural debt is incurred in kind, *i.e.*, in grain. So far as this is the case an appreciation or depreciation of the rupee can matter little to the Indian agriculturist. On the other hand, four or five bumper crops must have reduced that kind of indebtedness very materially.

“(4) In India most of the agriculturist's debt consists of short period obligations ; and all these must have been incurred necessarily in the last two or three years. As regards this mass of indebtedness no one can even suggest the possibility of the exchange doing any injury to the ryot.

The fact is that it is only by jumbling up old debts and new debts, original debts and renewed debts, short period and long period obligations, debts in kind and money debts, that a plausible case has been put forward for the “farmer's ruin.”

The fall in purchasing power.

“Do you agree with the assertion that the exchange policy has been the cause of the fall in the purchasing power of the ryot?”

“A great deal has been made of the fact that the Indian agriculturist has been purchasing a smaller quantity of piece-goods than usual, and this has been held as a proof of the blow dealt by the exchange policy to his prosperity. But, in the first place, we note that it was only to be expected that the agriculturist should transfer his custom to the precious metals which have fallen in value very materially. In the second place, with successive heavy crops the relative price of the farmer's products has fallen in India (as elsewhere), while the prices of other commodities have remained comparatively higher. The same phenomenon has been attracting a great deal of attention in America and a very able writer has put forward the view that ‘in so far as the farmer's financial outlay is for goods, his chief concern is that there be no disparity between the prices of his own products and those of other things.’

Whenever such disparity has appeared between agricultural prices and the prices of other commodities, the farmer naturally hesitates to make purchases on the usual scale.

"In India the agriculturist finds that successive large harvests have brought down the price of his goods, while the prices of piece-goods have been comparatively little affected. He is, therefore, content to bide his time and wait for a fall in the prices of textile goods, and meanwhile invests his savings in gold and silver. One should not therefore believe that because he does not purchase textile goods as before his resources are exhausted ; witness the unexpected and unwonted resource shown by the Indian farmer in holding up his jute and cotton in the face of low prices."

Narrow Limits of the Influence of Exchange.

"What are the limits to the influence of any exchange policy on the prosperity of agriculture?"

"My answer is that exchange policy can directly and in the main influence only the general price-level ; while what the agriculturist is now suffering from is the condition of relative prices—*i.e.*, the prices of agricultural produce have gone down relatively to the prices of other commodities.

"It is necessary to see that such a complicated problem as that of the reaction of the higher exchange on the fortunes of the agriculturists is not to be solved by the free use of popular slogans. We have just had an example in another country of the consequences of the reckless use of such slogans as—'Not a minute, on our day ; not a penny off our pay.' There is a family resemblance between that shibboleth and another which we have been hearing in this connection in India for a couple of years—'Twelve per cent.' on farmer's debt ; 'Twelve per cent.' off his income, net."

THE TRUTH AS REGARDS MANIPULATION OF CURRENCY

THE RATIO OF 1s. 6d. AND ITS MAINTAINABILITY

The critics of the Report of the Royal Currency Commission have argued that "the ratio of rs. 6d. was attained by official administration of the currency" and a drastic process of deflation. They have further alleged that as that ratio is a forced ratio (and not the "natural" ratio), it can be maintained only a little further by a policy of continuous deflation ; but that ultimately the ratio cannot be maintained since its maintenance "would expose the resources of the Government of India to the point of deflation" (Minute of dissent paras. 68—70 and 128). These allegations deserve to be examined carefully.

War-Time Inflation.

It will soon appear that both the extent and the influence of the preliminary deflation of the period ending in August 1923 have been greatly exaggerated. Having regard to the great inflation of our currency during and after the war which raised the circulation of rupees and notes from 248 crores in 1914 to 407 crores in 1918 and which the author of the dissenting minute himself terms "an immense inflation"—the subsequent deflation was both partial and hesitating. As an authority on Indian finance has put it: "the existence of budget deficits of a substantial amount clearly made currency contraction a matter of unusual difficulty, but in the three years 1920-21, 1921-22 and 1922-23 Government was able to effect a reduction in the currency circulation amounting to Rs. 38½ crores." The minute of dissent admits that taking the last five years together, even during the epoch of deflation the average expansion of currency was 12.12 crores a year (paragraph 63). Only it

* This was the first of a series of articles contributed to the "Forward" and appeared on 9th January, 1927.

expresses a regret that the pre-war average expansion of currency (viz. 20 crores of rupees per annum) was not maintained all through. The answer to this obviously is that we cannot conceive of a normal rate of currency expansion which should be carried on at all times irrespective of the relative demand and supply of currency at home or of important movements of prices abroad. It is hard to conceive why expansion of currency should proceed in India at full speed regardless of the "immense inflation" which preceded or of "the tremendous fall in world prices" which was contemporaneous with the deflation in our currency. The idea of carrying on an average expansion of currency, regardless of radical changes in conditions, is worthy of the best traditions of inflationism.

Influence of Contraction.

The influence of the contraction on Exchange and on prices has also been exaggerated. Thus in 1920-21 when the net contraction was about 31½ crores (i.e. when by far the greatest portion of the preliminary deflation had been already carried out) such deflation failed even to check the downward course of the rupee. Surely this is proof positive that the deflation was nothing like so drastic as has been alleged. Another proof of the same, if indeed more proof was wanted, is that the fall of prices in India was much smaller than the very substantial fall which was taking place at the same time abroad. It was well observed that an automatic system would have required an even greater contraction in India.

The fact is that neither in 1924-25 nor in the epoch of 1898 (when the Exchange was raised to rs. 4d.) was contraction of currency the main factor in the raising of exchange, although at both periods a great deal was made of such contraction of currency as had taken place. In both cases the great factors of the economic situation of the world and the favourable balances of trade on the part of India formed the dominating elements in the maintenance of exchange. But on both occasions the business community was up in arms against such deflation as took place. This illustrates the

remarks of Sir James Brunyate that the Indian money markets are disposed to be somewhat specially intolerant of deflation and that there is a disposition among them to expect more in this line from the Government of India than is expected in other countries from their controlling financial authorities.

Inconsistency of Critics.

It might be noted in passing that there is a certain inconsistency in the attitude of the critics of the Currency Reports as regards the topics of the contraction of currency and the adjustment of prices. On the one hand they do their very best to exaggerate the contraction of Currency ; on the other hand they stoutly deny that prices have fallen so as to adjust themselves to the ratio. To the economist there is a startling anomaly in the same party's assuming both these positions. There was no reconciling these attitudes except by denying the Quantity Theory : and that bold step was taken before the Commission by no less a critic than Mr. B. F. Madon. Economic history shows that it is impossible to advocate inflation, even in a veiled manner, without throwing overboard the Quantity Theory. Monetary fallacies cannot survive in its searching light.

Recent Deflation.

Since the Currency Report was issued our critics have again raised the cry of deflation. But I would request them to bear in mind the following circumstances :

(a) The Currency has been expanded too in every one of the recent years, for meeting seasonal requirements as well as for securing funds for the purchases of sterling by Government.

(b) Large quantities of hoarded currency have come into circulation in recent years, having been replaced by gold in the hoards. Hence the large return of rupees from circulation during the slack season and also the exceptionally small absorption of rupees in the busy season.

(c) As the Controller of Currency observes, the cash balances of the Imperial Bank bear witness to the redundancy of Currency during the slack season. Nor should one fail to note the slackening of the grip of seasonal stringency in recent years.

Maintainability of 18d. Ratio.

Having thus shown that the complaints, as regards the deflation having been of a drastic character, are themselves exaggerated, we might come to discuss the second question to be dealt with in this paper, viz., the maintainability of the ratio of rs. 6d. There are three aspects of the problem of maintainability.

(1) It might be argued that it is easier, generally speaking, to maintain a lower ratio like rs. 4d. than a higher ratio like rs. 6d. To this the answer is that, once an adjustment of prices has taken place, it is no more difficult to maintain the higher than the lower ratio, because with the higher exchange ratio and lower internal prices our products cost the same to the foreigner and have the same world price in terms of gold as they would with a lower exchange ratio and correspondingly higher internal prices.

(2) It has been argued that, in the case of an unfavourable monsoon, the higher ratio would be more difficult to maintain than a lower ratio. But here also the difficulty would be no greater, once our prices have adjusted themselves to the ratio. To quote an eminent expert, "Any rate established over a period of normal years must tend to break down in bad years unless sustained by the exchange machinery."

(3) It has been contended that we are entering on a long period of low world prices and that a higher ratio will be against the interest of India under such conditions and, generally speaking, that it cannot be maintained.

Another Inconsistency

Before dealing with this contention, I venture to point out another glaring inconsistency or anomaly on the part of

the critics of the Report. If they are so apprehensive of the evil effects of a fall of world prices, it is curious that they insist on demanding a gold currency which would form a considerable drain on the gold resources of the world and would materially contribute towards ushering in a period of falling prices. It is most inconsistent to express apprehensions of an imminent fall of world prices and yet to propose to make large drafts on the available gold supply of the world, which is a sure way of aggravating any possible fall of prices in the world. Thus our critics can be hardly regarded as serious when making this move.

Still, their contention must be considered here for what it is worth. Supposing, for the sake of argument, that a period of steady and substantial fall of prices is coming on, what is the value of the remedy proposed by them? Who ever contended seriously that a local inflation of currency, say by 12½ per cent., is a panacea for low prices all over the world? We had a long period of depression of prices in the seventies and eighties of the last century; but hardly any one seriously advocated local inflation as a remedy. Supposing we did try the inflation by lowering exchange, how long would it be before a readjustment of costs of production and of living supervened to deprive our industrialist and agriculturist of any short-lived advantage thus artificially secured?

Will Prices Fall?

So much of the remedy proposed. But in the first place, are we so sure that a long period of steadily falling prices is imminent? It is true that, as Professor Cassel points out, according to the Index number of the United States Bureau of Labour the prices in the years 1923, 1924 and 1925 are to be represented as 154, 150 and 159: whereas the prices in August 1926, stood at 149. But Prof. Cassel does not consider this a sufficient basis for apprehension as to prices. He observes in his latest communication: "Whether this fall of prices signifies any thing more than a reaction from a small boom, it is too early to decide. We are still justified in hoping that

the United States will succeed in maintaining on the whole the price level which has subsisted in the last few years." This attitude is any thing but pessimistic as regards the future of the prices ruling in the world. He goes on to say that "with a judicious use of gold reserves, which hitherto have practically been left untouched, it should be possible for a fairly long time ahead to maintain with perfect security a price level of, say, about 150." Hence, to say that Prof. Cassel prophesies an imminent fall of prices is not true. His warning is only against any increase of new demands for gold: for the rise of such new demands would not only by itself increase the shortage of gold but "would also increase the eagerness of various countries to guard their accumulated gold reserves and, if possible, to increase them."

Surplus Stock of Gold

There are, in fact, numerous circumstances which would tend to counteract any steady fall of world prices. We note, in the first place, the great surplus stock of gold in the United States which that country would unhesitatingly use to offset any serious fall of world prices; for such a fall would be against the interests of that country itself as a leading industrial area. Not only is such a great stock of gold ready to be thrown into the scale, but, as Prof. Sprague of Harvard told the Currency Commission, the reserve Banks of America could easily reduce their reserves from 70 to 50 per cent. and thus release an additional 800 million dollars. Another 700 million dollars could be made available by a substitution of Federal Reserve notes for gold certificates. The conclusion is that "the excess reserves of the United States are sufficient to supply any deficiency in the world's gold production for a good many years."

But the economy of gold will not be confined to the American Banks. A reference to the reports of the banks of Europe will show a very important factor at work—foreign exchange represents the cash reserves of banks in so many countries in place of gold. Again, as Prof. Cannan of the London University observed before the Currency Commission,

the production of gold would automatically increase if a substantial fall of prices took place, because there is a considerable amount of gold produced on the margin. Thus we have very little to fear as regards the maintainability of our exchange unless we ourselves begin the introduction of gold currency at the wrong time i.e., when there is a great need to economise the gold resources of the world in the general interest.

Certain Dynamic Factors

In conclusion, I would emphasize certain dynamic factors which are specially favourable to the maintenance of the 1s. 6d. ratio by India. In the first place, the favourable balance of trade of India which has been steadily rising for decades, and which never rose so rapidly as now, will undoubtedly play a decisive part in the maintenance of the 1s. 6d. ratio. In the second place, there is to be counter on the great repurchase by India of its own securities during and after the war. The process of converting our external debt into an internal debt is going on rapidly and steadily, and it is to be noted that in some foreign countries this process of buying back national securities has sufficed by itself to raise and maintain the exchange. Finally, in future we might count on the growing demand of the western countries for our raw materials during the period of the revival of industries when the industrial and trade depression which forms the aftermath of war has passed away.

THE RYOT AND THE RATIO *

So numerous have been the aspects of Indian agriculture brought into issue in the present controversy regarding Indian currency and exchange, that it is necessary to advert to them again for a time.

The Verdict of Co-operative Statistics

In the interview published sometime back in the columns of this paper, I have argued that the progress and prosperity of rural Co-operation in India constitute the best answer to the repeated allegation that the Indian farmer has been ruined by the rise of exchange to 1s. 6d. So damaging to our critics was this verdict of Co-operative Statistics that an attempt has been recently made to minimize its force by arguing that the Co-operative bodies form but a small part of the system of Indian agriculture. Consequently, it was contended that we could not argue from the prosperity of the one to the prosperity of the other.

To this the answer is that Co-operative Societies, being scattered and spread evenly over the whole country, are fairly representative of the country's agricultural conditions. So far there never has been any question about their re-presentative character: none of our numerous economic enquiries or land settlement reports has made any distinction between villages possessing Co-operative Societies and those without. The method of "sampling" is well-known in statistical enquiries. In this case we are in the fortunate position of being able to apply this method of "sampling" with a vengeance to the problem in hand—because we are dealing with about 70,000 samples in the shape of rural Co-operative Societies, while many thousands of more are being formed every year. Surely, arguments drawn from so many samples so evenly distributed can claim to be unshakable. But above all, if, as has been alleged, there is general and pronounced agricultural distress,

* This article appeared in the "Forward" of 18th January, 1927.

how can the Co-operative Societies be immune from it? In any case, their financial conditions 'must at least be made worse' if such conditions existed. But as a matter of fact we find their finances improving very noticeably. The inference is obvious.

The Agriculturist's Interest In Imports

We might now proceed to examine another favourite contention of the critics of the Report. This is to the effect that the agriculturist hardly benefits by the cheapening of imports (through the rise of exchange) to any appreciable extent. For example, Mr. Madon believes that the cheapening of imports can only benefit the wealthier classes at the expense of the producer. But, surely, he will agree that the agriculturist is greatly interested in the large imports of railway and other material, of all accessories of irrigation, of agricultural implements, of imported yarn and, to some extent of piece-goods. Let me quote one who is known all over India as a great scientist and who has for years made an intensive study of rural India by spending all his time in travelling through the districts and studying their condition. I refer, of course, to Sir P. C. Roy whose intimate knowledge no one will question and who very recently complained before the Royal Agricultural Commission that "owing to the increased price of jute there has certainly been a larger circulation of money, but the *largest percentage of that money is now sent away in the shape of purchases of foreign imported goods* for which our ignorant rustics have a kind of fancy." Other observers have recently noticed that in Bengal the standard of living of village labourers and cultivating peasants has decidedly improved and they are using foreign imports in the shape of piece-goods, trinkets, cheap stationery etc., indeed it has been by the "*bhadralokas*" in the town, they are being more and more patronised by the peasant class in the villages.

The Agriculturist And The Price Of Silver.

We might proceed to notice a fresh item in the indictment of the Government's currency policy. Thus it has been recently

argued that the total imports of silver into India between 1835 and 1925 amounted in value to 913 crores of rupees. Of this mass of silver the value has fallen by 400 crores on account of the alleged manipulation of currency ; and much of this alleged loss must needs have fallen on the agriculturist. With reference to this sort of contention, I would draw the attention of the reader to an article by Mr. Joseph Kitchin in the "Financial News" of 29th October, 1926. In that article Mr. Kitchin examined the various recommendations and showed that there was nothing in them which could have or should have produced the recent drop in the silver quotation. An unfounded and sentimental fear arising from the proposals might have had some undesirable effect. But no Commission can prevent a misreading of its recommendations : and according to Mr. Kitchin the most tangible reason for the fall in the price of silver is given by the temporarily lessened demand on the part of China and India. Sir Purushottamdas himself—who, to do him justice does not countenance the extreme statements made by his followers—has recently observed to a Bombay audience that "to-day silver prices are very low due to world causes," and all that he emphasized was the apprehension entertained as regards future action in the matter of the surplus silver holding.

But if the mere apprehensions as regards the potential and future action of the Government, or such as were roused by the misreading of a report, produced such an effect on the silver market, how much greater would have been the fall of silver had the alternative favoured by our critics—the immediate introduction of a gold currency—been adopted? Then indeed there would have been no sense in calling the apprehensions sentimental ; then there would have been a real and unprecedented *debacle*. How easy it is to see a mote in another's eye and how difficult to observe the beam in one's own ! Some stalwarts, however, have freely admitted the immense loss "to the Indian masses" when silver falls in price on the introduction of gold currency but they go on to say "that is the least price which the country must pay for the adoption of a gold

standard." Obviously, such speakers do not belong to "the Indian masses." Finally one may remind those who try to connect the rs. 6d. ratio with the fall in the price of silver, that the white metal is no respecter of ratios but has shown, not many years ago, a phenomenal fall in value while our exchange ratio kept steady at rs. 4d.

Land Revenue and the Ratio

It has also been urged that the policy of having a higher ratio has done another injustice to the agriculturist by increasing the burden of land-revenue by $12\frac{1}{2}$ per cent. Thus Mr. Madon observes that the Government, by twisting the exchange up, is to-day exacting $12\frac{1}{2}$ per cent. more out of all those who have to pay land revenue. It can be replied to this that, in the first place it assumes an adjustment of prices, since the argument is that the ryot pays the former land revenue "in an appreciated rupee." But if the price adjustment has taken place, the cost of production and cost of living of the agriculturists have also fallen correspondingly, and this constitutes an undoubted gain to be set against the loss.

But, in the second place, we must recognize, as economists, that as between the agriculturist on the one hand and the Government, or rather the general tax-payer, on the other the rise of prices which has been going on for three decades has been giving the former a great advantage which still persists in spite of some recent fall of prices. Thus, it was observed before the Taxation Inquiry Committee by an eminent professor of economics that between the years 1900 and 1925 the real burden of land revenue had fallen by 42 per cent. owing to the steady rise of prices. This diminution of the real contribution of our agriculturist to the Indian taxation system was expedited by the steep rise of prices during the war. Now such an alleviation of the agriculturist's burden would by itself afford unalloyed satisfaction to all; but, as is natural, a reduction of taxation at one end, due to inflation, leads only to corresponding additional taxation in other ways; and some portion of the extra taxation in pre-war days has to

be explained in this way. In this connection, the reader's attention should be drawn to the remarks on this aspect of the problem made by Sir Robert Giffen, the famous statistician and economist, before the Fowler Committee. He pointed out that a rise of prices due to monetary inflation is equivalent to a remission of taxation, since the Government obtains the same number of rupees as before, but depreciated in value ; consequently, resort must be had to additional taxation to make good the State's income.

On this point also there is noteworthy disagreement among the critics of the report. Mr. Madon argues that, as the result of the rise of exchange, Government gets more out of the farmer, while Sir Purushottamdas suggested that, as a consequence of the rise, the revenues would be reduced (*vide* his questions No. 85-92 in the evidence before the Currency Commission). Which of these gentlemen is right?

Who Gains What The Farmer Loses?

This is a very interesting and relevant question and is worth examining, in spite of the opinion of a Bombay critic who recently observed that "if the loss is proved, it is secondary as to who profits by that loss." With all respect, it seems to us very important to trace the gain of so many millions per annum. If we could find some class who had become suddenly very rich in the last two or three years, the fact of the farmer's ruin would be irrefutably established. But as to the identity of this beneficiary we are not given much information. A suggestion has been made that "a very small number of bankers, financiers and investors" have profited by the alleged immense losses of the farmer. But if such had been the case, indeed, banking and investing would have become extraordinarily profitable occupations in the last two or three years ; and the statistics of banking and financing tell us no such tale of the accruing of vast unearned increments. Others have suspected the importer of gaining the many millions which the farmer is said to have lost. But, surely, if the import trade people had been gathering the shekels

in such abundance, that trade would have been making great strides forward. But what are the actual facts? The last Review of Trade informs us that "during the last three years the volume of India's Export Trade has regained its pre-war level, while, for import trade, recovery is still very far from being complete." So it does not look as if the import trade had been making exceptional gains. Finally, at the last Economic Conference, Mr. Madon, when questioned on the point, suggested that the Government had been gaining what the farmer had been losing, on the ground that it had made a gain of three crores or so on its sterling expenditure. He did not trace any connection—either arithmetical or theoretical—between the three crores gained by the Government and the two or three hundreds of crores alleged to have been lost by the Indian agriculturists.

World Factors Affecting Agriculture

When we take into consideration the last decade or so, we find that there has been a race between agricultural prices and the prices of manufactured goods, so that the advantage has sometimes been with the agriculturist and sometimes with the manufacturer. In the last five years the agriculturist has been losing and, relatively speaking, the prices of his wares have been falling. This state of things, however, has nothing to do with exchange nor is at all peculiar to India; and the relative fall of agricultural prices might be said to be a world-wide phenomenon. Thus in America, it has been observed that "the continued concentration of price declines on the products of the farm has brought about a disturbance of the price equilibrium." On this subject, I had the privilege of examining Dr. Hollander before the Currency Commission. He observed that the general opinion was that, after a period of war, farm products seem to suffer in a greater degree from the post-war correction of price. Their production is stimulated during war either by price fixing or by the natural advance of prices, because their supply is inelastic; hence the relative fall in agricultural prices. In any case exchange is not responsible

for these results, nor is inflation, as we shall soon see, any remedy for this state of things. The evil of this swing of relative prices—for so it is—is to some extent mitigated by the large and successive harvests which we have had.

As we have seen, the United States has been the first country to feel the stress of the world-conditions which are hampering the farmer. The experience of that country in the matter and the opinion of its leading economists on the subject, are of great value to us under the conditions prevailing in India. The influence of the exchange and currency conditions on the relative prices of agricultural products has naturally attracted much attention there. Mr. R. J. McFall of the Massachusetts Agricultural College, writing in the *Annals of American Academy* in 1925, argues that, to the extent to which alterations of exchange are due to monetary inflation or deflation and have been thoroughly reflected in a country's prices, the influence of foreign exchange is negligible. What is of importance is this: "Any country that competes with the United States, in the sale of farm products and has materially lower prices for those products than our prices, by reason of either the exchange rate or the domestic price level, has the advantage over us in making sales." Consequently Mr. McFall desires the reduction of the price-level in the United States. This dictum should furnish matter for thought to those in India who are apprehensive of a fall of world prices, but who would prepare for it with surprising inconsistency by raising prices in India.

We might with advantage quote the opinions of the same economic authority as regards the great importance of the relative prices of his products to the farmer. In another article in the same number of the *Annals*, Mr. McFall observes that "to the farmer, the general price level is less important than that his products exchange on a par with others." Now it must be remembered that the general rate of exchange can only modify and affect the *general* price level in a country; it can have little influence on the relative prices. This important consideration indicates the limits of the effect of any

manipulation of exchange on the fortunes of the agriculturist. No doubt, if Mr. McFall had been living in India, he would have pointed out another aspect of the comparative inefficiency of any exchange policy on the agriculturist's fortunes ; for, where there are such gigantic fluctuations from year to year in the prices of crops like jute and cotton, any possible effects of exchange on prices sink into comparative insignificance.

AN EXAMINATION OF THE PROPOSALS FOR A GOLD-CURRENCY IN INDIA

Diversity of views on gold currency

It would appear at first sight that the enlightened public opinion in India was overwhelmingly in favour of a gold currency. But when we come to analyse and classify the views put forward, we find that the same phrase—"gold currency" has been made to cover a wide diversity of views. The large school of Indian economists and even many of the commercial circles are too well acquainted with the progress of monetary theory and practice in the world to advocate a gold currency as generally understood. Drawn, as they are in one direction, by the traditional policy laid down for them decades ago, and in the opposite direction by their scientific studies and their observation of the economic facts and tendencies of their own day, their actual position becomes a series of varying individual compromises in which the emphasis of opinion is very variously distributed, but it is rarely indeed that the essentials of gold circulation are insisted on. Thus we have eminent witnesses who are anxious not so much for the circulation of gold coins as of gold notes. No one has advocated the issue of a gold coin of such a small value as to ensure its use in daily transactions and in general circulation ; while researches into the monetary history of India have shown that a very large portion of the former gold currency consisted of the *fanam* and other small coins. Almost all witnesses who asked for a gold currency expressed a strong desire and hope that gold coins would not circulate strongly. They expressly want "some circulation of gold but not a large circulation because the people of India are poor and the masses would not be able to get any amount of gold ; it would be mainly the middle classes that would be able to get it." Hardly any one expressed a desire to force gold into circulation ; many stated expressly that they would not even "encourage

the circulation of gold." In fact, if most of the witnesses were certain that the introduction of a gold currency would result in anything but a golden fringe to our currency, they would hardly press for it with any consistency.

Futility Of A Slender Gold Currency

These are discreet views—to say the least—behind which we can trace the struggle between the traditional desire for the yellow metal and the reaction of the greatly changed aspect of monetary theory and practice. But will not such lukewarm advocacy involve us in a lot of expense and yet fail in achieving its professed objects? If, indeed, the gold coin is going to form so small a portion of our currency, how is it going to fulfil the important functions which are claimed for it? Unless there are very substantial amounts of gold currency in circulation, how is the anticipated psychological revolution to be brought about which will cause the hoarding habit to disappear? We quite agree with the view that has been put forward that "once a thing becomes common, people do not want to hoard it." Hence to weaken the hoarding habit we must make gold coin available commonly and freely to the people and not merely show it to them occasionally. How is a coin, which does not circulate substantially and which is, besides, too large for daily transactions in the country, to inspire that general confidence in the currency system which has been claimed for it? How are the people to be weaned from their age-long attachment to silver unless we encourage the circulation of gold markedly? Have not Dr. Cannan and Dr. Gregory in England and Dr. Ambedkar of Bombay assured us that the proper way to introduce gold currency is to suspend all additional issues of silver coin and to stop all additional issues of notes? Thus, in the opinion of these eminent experts, we have not only to "encourage" the circulation but also to "force it in" by starving other forms of currency—which implies that we shall have to push into circulation a substantial amount. It is all very well for our critics to hope and desire that India will absorb only a

little gold currency. On the one hand, if only a little gold is absorbed, the great expectations based on such currency cannot be fulfilled; on the other hand, we cannot base currency systems on pious hopes and good wishes; nor can we—town-bred economists and industrialists—safely dogmatize about the psychology of a vast rural continent and forecast exactly what these great rural masses will do when particularly tempting opportunities of hoarding are placed in their way.

Arguments For Gold Currency

It is advisable to examine successively the leading arguments put forward in favour of a gold currency.

(1) The general argument advanced is that the rupee has forfeited the public confidence while the institution of a gold currency will secure such confidence in the monetary system. As a matter of fact, however, so great is the public confidence in and liking for the rupee that most even of the advocates of gold currency recoil in fear from the first step proposed in the dethronement of the rupee—viz. the limitation of its legal tender quality. Many call it a heroic step; others term it an impracticable proposal. No less an advocate of gold currency than Mr. Madon frankly and sincerely admits it. "In view of the enormous amount that must now be in circulation and in hoards, it is not practicable to consider any limitation at this stage. I would, therefore, allow the existing rupees to continue to be full legal tender for any amount as at present. When the gold currency gets fully established in the minds of the public as the real money of India, the position of the rupee can be reconsidered." This constitutes a very fair and frank admission that the rupee commands such public confidence that it is largely hoarded and that it is dangerous to try to shake this confidence prematurely. It implies further that it will take a lot of time to transfer such confidence to the gold coin. Nor can any cheap and half-hearted attempts at a slender circulation of gold secure such confidence.

(2) Another contention has been put forward to the effect that the gold standard is more automatic than the present system. To those who argue this it is well to remind that under gold standard, as at present understood, the prices will be "managed prices" and that the prices will be managed from abroad—perhaps from the country which possesses the largest available supply of gold ; or there might be very likely international co-ordination to avoid a scramble and any fluctuation of prices which might be considered undue. For this latter purpose the credit policies of different countries might have to be managed. In any event, in the future, the gold standard and prices in the gold standard countries will be "managed" in a very thorough sense of the word.

But, further, while we are on this point, it is relevant to quote Prof. Kemmerer's view that "the pure Gold Exchange standard is almost as automatic in its functioning as is the gold standard with a gold currency"; and it can be added that the proposed Gold Bullion Standard worked by a central bank is even more automatic than the pure Gold Exchange standard, and as automatic as the gold standard and gold currency for there is no administrative discretion, as regards the working of the standard, no confusion of monetary and fiscal objectives in the sale of exchange and in the detailed management of the system.

(3) Little addition is made to the real arguments for gold currency by the conjuring up of a pseudo-historical law of monetary evolution by which it is implied that nations cannot pass from silver currency to paper currency which is the final goal, without going through an intermediate and educative stage of gold currency. No proof has ever been offered of the existence of such a law of monetary progress : and in various provinces of India the note is already very popular. But, in any case, such an educational stage, if it is to be of any value in educating the backward masses, should see a very thorough saturation of the country with gold currency, and will naturally prove a very costly one.

Difficulties In The Working Of A Gold Standard In India

It can be easily shown that even with a full gold standard India cannot escape some of the main difficulties of the present system. The main causes of these difficulties are two—hoarding and the great and abrupt demands for currency made by our foreign trade in favourable seasons. The loudly proclaimed difficulties of Gold Exchange Standard are due to these causes chiefly, and the trouble will continue with full gold standard. Whenever there is a good export season, gold will be imported largely and the country's currency will expand not in proportion to the demands of the country's trade as a whole but in proportion to the demands of its foreign trade which are abrupt and large. Again, the habit of hoarding opposes another obstacle in the way of the automatic action of any monetary system—for part of the currency goes out of circulation and will thus not exert its expected influence on prices. A third factor also exists which renders the contraction of currency difficult in India viz. the sensitiveness of our money markets. With these three factors any monetary system whatever is bound to work in India to some extent erratically.

Cost Of A Gold Currency

In some quarters the cost of introducing gold currency into a continent like India has been regarded with a light-hearted spirit of over-confidence which is quite out of place. It is thus assumed by some that by utilising our gold reserves and through the action of our usually favourable balance of trade we shall, without more cost, come into possession of a gold currency. But this facile statement misses the most important factors in the cost of the introduction of a gold currency :

(1) As soon as the legal tender quality of the rupee is touched, there will be a great fall in the value of the silver hoarded by the country or used as ornaments. The price of silver might easily fall to 24d. or even lower ; and the fall

in the value of this silver treasure which has been accumulated for centuries will amount to hundreds of crores of rupees.

(2) Eminent advocates of a gold currency like professors Cannan, Gregory and Ambedkar have justly argued that the only practical way of supplanting silver by a gold currency is by ceasing to coin additional rupees and by depriving silver of the legal tender quality ; they further advocate that no additional issues of notes should be made. Their argument is unassailable—that as long as the masses get their accustomed currency they are not likely to take to new money. But their proposal avowedly is to starve the Indian currency in order to make room for gold coins. Dr. Gregory avowed this before the Commission. What the cost of such a process of preliminary curtailment of currency is likely to be in the shape of very high discount rates over a long period, I leave our industrialists and business men, who champion gold currency, to guess.

(3) It is obvious that, before undertaking such a great national policy, our preparation of resources should be fully adequate before we change our monetary system. We cannot afford to drop the scheme once we have taken it up ; for, we should have ruined our present monetary system and squandered its reserves and would have failed to attain the Gold Currency and Standard. To avoid such a double failure a careful estimate of the requisite resources has to be made. The Finance Department tried to make an estimate before the Commission ; their rather optimistic calculation put the required resources at 103 millions. But eminent experts like Professors Cassel, Hollander, and Sprague showed that the estimate was much under the mark. Insufficient allowance had been made for several important factors—much of the gold issued might be hoarded ; large amounts of silver might be thrown on the market in order to acquire gold ; and a large quantity of notes might be presented to secure gold. The conclusion was that the extra demand for gold caused by the gold currency scheme could easily attain a figure several times higher than assumed by the officers of the Finance Department.

An Untimely Proposal

It would be difficult to imagine a more inopportune moment than the present for adopting a gold currency for India, and even for taking any step in that direction. America has warned us in the plainest terms that none of its gold supply will be made available for the object proposed. In London we were told that "the Treasury or the Bank of England would be absolutely justified in making difficulties about such a loan." The bottom has dropped out of the silver market at the very suspicion of touching the legal tender quality of the rupee, which has already caused substantial loss to Indian interests. World-renowned and absolutely impartial authorities like Prof. Cassel assure us that the present moment is one in which every effort should be made to economise the use of gold ; and that, failing such efforts towards systematic economy in the use of gold, we shall inevitably approach a period of falling prices and slackened economic progress. This general depression of the economic life of the countries to which India sends her exports must infallibly react on her own prosperity. Any substantial fall of her increasing balance of exports would undoubtedly injure the financial system, the currency and the general economic life of India.

In conclusion, I would draw attention to some remarks by Mr. Keynes on the subject in hand. "We are not at the end of currency discussions but at the beginning of them. The future currency of the world is going to be determined not by what happened in the last two or three years, but by what is going to happen in the next 10 years. It is impossible to say what the experience of the countries which are going over to the gold standard is going to be. I think that India will be well advised to hold her hand until some experience has been gained."

THE CURRENCY REPORTS OF 1898 & 1926.

A Close and Instructive Parallel.

In the growing literature of the present Exchange controversy it is indeed surprising to find that the critics of the Currency Report of 1926 refer so frequently and fondly to the Fowler Committee's Report: for—excepting in the matter of gold currency—the Fowler Committee has expressly overruled every plea and answered every argument that the opponents of the 1s. 6d. ratio have put forward in our days. So similar were the exchange and currency problems of 1898 and 1926-27, so high is the authority of the members on and witnesses who appeared before the Fowler Committee, and so varied and rich have been the experience and results of the policy of 1898, that we might draw valuable lessons from the earlier conjuncture to clear up the issues of our own days.

It is remarkable, in the first place, that every single argument which the Fowler Report employed on behalf of the 1s. 4d. rupee can be used to-day, without the alteration of a phrase or a word, to support the 1s. 4d. ratio. Indeed, the arguments of 1898 gain in weight when applied to the circumstances of our own day. Thus the main argument on behalf of the 1s. 4d. ratio was that "the rate of 1s. 4d. is that of the present day; prices in India may be assumed to have adjusted themselves to it, and the adoption of materially lower rate at the present time would cause a distinct and, in our opinion, a mischievous disturbance of trade and business." (Fowler Report, para 65). One has only to compare this with the Currency Report of 1926, paras 176-188 and note that while using that identical argument the Royal Commission has proved the same point with a much greater recourse to statistical weapons of precision as was to be expected in the days of Keynes and Cassel.

Another argument employed by the Fowler Committee in favour of the 1s. 4d. ratio was that the ratio was found in

the year 1898-99 quite compatible with a volume of the export trade which exceeded that of all past years (Paragraph 64). Is it necessary to refer to the much larger series of record balances in favour of India in recent years under the 1s. 6d. ratio?

Nor did the Fowler Committee fail to notice that "a rise in prices which expresses only the depreciation of the currency is no gain to the community as a whole, and although the fixing of a lower denomination in sterling for the rupee might for a time give some advantage to producers, this would be at the expense of every holder of a rupee, or debt or security for a fixed amount of rupees." (para 66).

Again, as in 1926, the dissenting minutes of 1898 raised the pleas that in the matter of exchange "the status quo had not been arrived at in a natural way," also that "to arrive at a rate in this manner and then to point to the accomplished fact as disposing of any question of its propriety is not convincing." Further they were unable to see "where the prices and wages adjustment were to come from." The lapse of a little time showed them where, and silenced these critics effectually.

Sir Purshottamdas and his friends make light of the effect of a reversion to the 1s. 4d. ratio on the public finances. On this point the views which Sir R. Giffen and Prof. Marshall put forward before the Fowler Committee are very instructive. Thus, Sir R. Giffen argued that if the lower ratio (of 1s. 2d. in those days) was reverted to, new taxation would be necessary to balance the budget. So also he argued in favour of raising the railway rates in case a lower exchange ratio was fixed. These views of those eminent economists agree entirely with those put forward by Mr. McWatters and others before the Commission of 1926.

The "Natural" Ratio.

What is a "natural ratio"? The whole literature of classical economics might be vainly searched for the use of such an expression. But in 1898, and in 1922 and in 1926-27 the

advocates of the lower exchange in India believed that they had found it. *Eureka*. Only in 1898 it was 1s. 2d. as opposed to 1s. 4d., which is in our days "the natural ratio" but was then condemned as "a forced ratio." However, in 1922 the late Sir Vithaldas Thakersey strongly asserted that 1s. 6d. was the natural ratio; this was the second time when we meet with the idea of a natural ratio. In 1926-27, however, 1s. 4d. has been extolled as the natural ratio and indeed a Calcutta publicist has gone further and has told us that it is "the only natural ratio."

The interests of Indian producers in general and of agriculturists in particular were kept as much to the fore in 1898 as in 1926. All the arguments with which we have been familiarized of late as regards the increase of the burden of the agriculturists's debt and interest thereon and of the land revenue under a higher exchange were brought forward in 1898 also. History, however, shows us that the higher ratio—as it then was—of 1s. 4d. was quite compatible with a great increase of India's export trade in food-grains. It was also firmly believed in those days by many that numerous industries of India were in danger of ruin under the regime of 1s. 4d.—notably tea and textiles. These gloomy forebodings were soon dispelled by the march of events.

The industrialists of those days used to put the potential effect of a lower exchange (and the resultant inflation) on the interests of labour with a praiseworthy frankness and brevity. Thus Mr. S. A. Ralli observed: "If you have a tea-garden, and the exchange, instead of being 1s. 4d., is 1s. 1d. then for the wages you pay in India you make a profit of 2d. per rupee." How crude it sounds now!

The success of the policy of 1898 in raising and stabilising the ratio has been undoubted; and yet the case for 1s. 4d. was much less strong in those days than the case for 1s. 6d. in our days. We must remember that in 1898 the 1s. 4d. ratio was a very bold experiment. The constantly rising balance of trade to which we are now accustomed did not then exist to give confidence in the maintainability of the ratio. Nor

did our reserves hold such resources as we have now to fall back upon. Nor was there in those days a surplus stock of gold as we have now in America to be thrown into the scale in case of an important decline of world prices. In fact, the policy recommended by the Report of 1926 has all the arguments of the Report of 1898 behind it and much brighter prospects before it. It is the task of economic history and retrospect to give us a true perspective of the facts of the present-day situation, and thus to fulfil the poet's wish—

O wad some Pow'r the giftie gie us
To see oursels as others see us!

REPORT OF THE ROYAL COMMISSION ON
INDIAN CURRENCY AND FINANCE *
(1925-26).

The real test of the value of the Report.

It is a difficult and a delicate task to attempt to appraise the merits of a work in the composition of which one has had a share however humble. I venture to suggest, however, that the true criterion of the merits of the Report of the Royal Currency Commission consists in the large number of long-standing controversies, criticisms and allegations that would be set at rest, silenced and made obsolete, were the recommendations contained in that Report to be adopted. We have an extensive literature of the criticisms of the monetary policy of the country, and almost all of it would retain only a historical interest, were the proposals in the Report carried out. The name of such criticisms is legion ; but I would select a few of the leading ones to illustrate my remark. Thus the perennial complaints of the former practice as regards remittances by Government and the stream of controversy as regards the overlapping between the Currency Reserves with the balances of the Secretary of State would be a matter of the past. Once the Report is adopted, no one could even suggest that "immense sums are being transferred from India to London" needlessly, and that the Indian money market was deprived of the use of funds to which it was legitimately entitled. We shall no more suffer from the difficulties caused by the distribution of our resources in different reserves, and from misapprehension in the matter of the separation and location of the two great reserves. The difficulties which were due to the fact that the control of currency and credit were in different hands will have been overcome ; and the whole currency, exchange and banking system of India will have been

* Speech delivered before the Indian Economic Conference of 1927.

placed upon its true practical and scientific pivot in the shape of the Reserve Bank. The earlier Currency Commissions did not possess similar opportunities for a radical and scientific reconstruction of the Indian monetary system. They were cramped by their restricted terms of reference. The Fowler Committee could not possibly foresee that rich and varied evolution of monetary theory and practice which has taken place in the first quarter of the present century. The Chamberlain Commission, again, was too much pre-occupied with the particular dangers manifested in the crisis of 1907-8 ; and the war followed so closely upon its report that its recommendations never really had the chance of being carried out. Above all, there was no great Central Bank in India in those days to serve as the base of currency reform.

A Land-mark in Economic Liberalism.

The proper way to appreciate the merits of the Currency Report is to investigate its true place in the economic history of India. I claim that regarded from one point of view, it is a most important step in the evolution of economic autonomy of India, while it is, at the same time, a great chapter in the long and honourable history of Economic Liberalism. We little realise the great pace at which our economic history has gone forward in the post-war decade. The virtual grant of fiscal and tariff autonomy, labour legislation of a liberal character and a series of budgetary and financial reforms have all followed each other at a very rapid pace, and the future historian will occupy himself a great deal with their importance. It is probable that he will compare the pace of the economic reforms we are witnessing with the momentum at which economic liberalism went forward in England in the days of Peel and Gladstone. But, even in the present epoch of economic progress in India the Report of Currency Commission will, if its recommendations be adopted, form a very conspicuous feature, for, the transfer of government functions, as proposed by it, is likely to be epoch-making indeed. The Government will cease to operate directly in the exchange

market and will hand over the remittance operations to a reserve bank. The balances of the Government of India and of the Secretary of State outside India are also to be given up to the same bank. The Government will also divest itself of its right of issuing notes. As the Honourable Sir Basil Blackett has put it "the whole burden of the Currency Commission was to recommend a transfer to India of the control of India's finances under the auspices of a Reserve Bank independent of Government control." The principle is fully accepted, and the strongest precautions have been taken to keep the Bank free from all political pressure. To secure that object, it has been provided that, a predominant majority of the members of the Local as well as Central Boards of the Bank should derive their mandate from the shareholder of the Bank by election. The critics of the Report might very pertinently be asked to point out another example from economic history of such a general transfer of so many important functions by a Government at one stroke into popular control. The credit for such a step should be given in a special measure to the authors of the Finance Department Memoranda placed before the Currency Commission. But the momentum thus imparted has been carried forward fully by the Report and hence, as has been said before, many of the chapters of that Report form also notable chapters in the growth and development of Economic Liberalism.

Inconsistencies of its Critics.

I have no time in this meeting to defend the Report against the criticisms that have been levelled against it. But I can in a brief space present a small list of the inconsistencies which might be found in the writings and speeches of these critics. A body of economic experts is the best judge of such inconsistencies in reasoning. I reserve the right to add to the list later on, as the flood of criticism broadens :—

(1) The main argument of the Report's critics consists of two inconsistent propositions. They assert, on one hand, that the Government has resorted to a most drastic deflation ; on

the other hand, they assert that this deflation has had very little effect on prices, and consequently there has been only a small reduction of prices and a very inadequate adjustment of these prices. The economists assembled here will no doubt see the difficulty and dilemma into which the hasty critics of the Report have worked themselves. To exaggerate the deflation and yet to deny to it any corresponding effect on prices is inconsistent economic reasoning. Those who desire to know the alleged extent of the deflation are referred to Mr. Madon's well-known work on "Exchange Fallacies Exposed, Part I."

(2) The critics argue that the high exchange has injured the agriculturist because he has to pay his debts and his land-revenue in an *appreciated rupee*. In the same breath, however, they deny that prices have adjusted themselves to the exchange. But if the rupee has, according to them, appreciated by 12½ per cent. is that not the same thing as to say that rupee prices have also adjusted themselves to the rise of Exchange by 12½ per cent. from rs. 4d. to rs. 6d.

(3) On the one hand, our critics would introduce a gold currency, on the other hand they express apprehensions of the fall in world prices. Will not extra demands by India on the world's gold supply for establishing a gold currency, contribute materially to a fall of world prices?

(4) On the one hand they assert most emphatically that the Indian agriculturist has been ruined by the high exchange, and that the most monstrous financial burdens have been laid on him ; on the other hand, they fail to produce any statistical evidence of such a state of things. How about the 70,000 flourishing co-operative societies working all over India and increasing in prosperity under the rs. 6d. regime along with their central banks and provincial banks?

(5) According to our critics, the higher exchange has dealt a great blow to our producers and exporters, and has vastly facilitated import operations. Yet under the present ratio is it not a fact that the export trade has progressed much better than the import trade?

(6) As to the extent of adjustment, no consistent position

has been taken up ; indeed the inconsistency is most glaring and conspicuous. It is not merely a case of doctors disagreeing ; for here the same doctor repeatedly disagrees with himself. In the Dissenting Minute Sir Purushottamdas is of opinion that the adjustment of prices is only 30 points against 50 i.e. 60 per cent. (paragraph 95). But in an article in the *Times of India* of the 27th November, 1926, he admits that it is above 73 per cent. (i.e. 26 points out of 35.5 points). However, in the same article he suggests later that the adjustment is less than 50 per cent, for he observes : "Even if it is granted that the disturbance involved in the former (i.e. in a reversion to 1s. 4d.) would be as great as the disturbance still to come with an adoption of 1s. 6d. ratio *which is the utmost that could be conceded etc.*" so that in one place, the adjustment is said to be 60 per cent : in a second place it is represented as 73 per cent : and on a third occasion as less than 50 per cent. Which of these three estimates is to be accepted?

(7) There is another inconsistency which is the property of our critics. In paragraphs 92 and 94 of the minute of dissent as well as in the above-mentioned article in the *Times of India*, the world prices are represented as acting on Indian prices at once and by their entire and full extent. Thus, any rise and fall of foreign prices is supposed to act at once and to its full 100 per cent measure on *all* Indian prices (not merely on the prices of our exports) : at the same time, it is the whole case of Sir Purushottamdas that the adjustment of Indian prices to the foreign exchange is extremely slow. How is this strange behaviour of prices to be explained, and what sort of economic theory lies behind this striking distinction between the two kinds of adjustment?

A REPLY TO MR. BIRLA.
To the Editor of the "Statesman."

SIR,—Permit me to reply to Mr. Birla's remarks (in your issue of the 24th instant) regarding my interview.

(1) The Reports on co-operation, to which I referred do not prove merely that "the agriculturist has not been ruined," as Mr. Birla says. They go a good deal further, and show that he is in a state of progressive prosperity. This disproves the assertion so often made that the farmer has been ruined (see Mr. Madon's pamphlet No. 2 published by the Indian Currency League). I might point out that Mr. Birla is shifting his ground in the letter where he says, "let a bad year come and the Professor will see, etc." The Currency League assures us that the Indian cultivator has already been ruined; but Mr. Birla would now ask us to wait until a bad year supervenes for the accomplishment of such ruin.

(2) Mr. Birla observes: "But the most amazing portion of his interview lies in the statement that because the higher prices in comparison with the pre-war level have led to a large reduction in the burden of the debtor class the process should be reversed." But, surely, there is a limit to the process of any class gaining at the expense of its creditors, and it cannot complain of any partial and incidental readjustment. Nor is Mr. Birla right in stating that the cultivator's gain was due to "natural circumstances created by God." The rise of prices was due not to any divine ordinance but to the inflation of currency during the War. No class has a vested right in any advantage resulting from an abnormal price-fluctuation.

(3) Mr. Birla asks "what remedy will the professor suggest if the world prices fall further? If the world prices are indeed

* Mr. G. Birla having attempted to meet the arguments in my interview to the *Statesman*, the above letter was written to meet his contentions.

going to fall, how would a currency inflation protect our agriculturist against it? How could we prevent the readjustment of the cultivator's costs of living and production to such inflation? Who ever heard of a local currency inflation as the remedy for a fall of world prices?

Yours, etc.

J. C. COYAJEE.

A REPLY TO SIR PURUSHOTTAMDAS THAKURDAS.

To the Editor of the "Statesman."

SIR,—I have read with great interest Sir Purushottamdas Thakurdas's letter in your columns to-day. I submit that, generally speaking, a Commission's Report is not the place for detailed and lengthy polemics against the authors of dissenting minutes. It might be noted in this connexion that neither the Fowler Committee's Report nor the Chamberlain Report contains answers *in extenso* to notes of dissent. Nor can any criticism be "belated" provided it appears before the decision is taken by the Legislature.

I wish my treatment of the subject was as original as Sir Purushottamdas would make it out to be. As a matter of fact, it is only the application of elementary economic theory and ordinary sense of justice to the problem in hand. Treating of the question of equity between the debtor and the creditor I pointed out that the debtor gained for a time incidentally, because of inflation and the consequent rise of prices. The inflation during the war was not intended to provide any advantage for the debtor class ; the gain was only an incidental effect. Similarly the raising of exchange and the resulting adjustment of prices reversed the former process partially, and incidentally deprived the debtor of some of his unearned gain. In this case, too, the rising of exchange was not intended to deprive the debtor (agriculturist or other) of his windfall. My main proposition is that the debtor has no right to complain when an incidental advantage, for which he has paid nothing, is taken away wholly or partly. I confidently affirm *the principle that no class has any vested right in an incidental advantage which it might have obtained as the result of price fluctuations*. Sir Purushottamdas refers to the case of other

* Sir Purushottamdas having attempted to meet the arguments in my interview to the *Statesman*, the above letter was published to meet his contention.

countries. Now, in almost every other country prices went up, at first, during the last decade, as the result of inflation during war ; and they were brought down later by the process of deflation. The debtor gained at first in the foreign countries also but later on he lost this gain through deflation. In no country did the Government raise prices to benefit the debtor, nor did they lower prices to benefit the creditor. Sir Purushottamdas's criticism would have been relevant if I had argued that exchange should be raised only to help the creditors.

Sir Purushottamdas has expressed a hope that I shall stand by my arguments and exposition. I shall take good care not to dissappoint such an energetic controversialist—Yours, etc.,

J. C. COYAJEE.

Calcutta, Jan. 18.

THE NEW RESERVE BANK BILL.

Few bills have passed through so many phases or have seen such transmigrations as the Reserve Bank Bill. Its life was often despaired of, and the Press, in describing its condition, used language denoting dire distress. At one time its condition was "comatose"; at other times it was said to be "sinking" or "floundering in the communal bog". However, it has survived all those phases, and it would appear after all that it

"Was doomed to death but fated not to die".

It now appears again before the Legislature in a much improved shape. While modifying the details of the Bill, so as to adapt it to circumstances and to minimise opposition, its author has taken care to maintain intact the sound and scientific principles underlying it. Compromise on details is perfectly compatible with adherence to principles.

In the new Bill, the problem of "vested interests" has been tackled with a vengeance, though not exactly in the sense in which it was meant to be solved by those who were most zealous against such interests. The Bill attempts to make short work even of future vested interests, by giving the country in general its due as against the great financial centres, and by ensuring that no vested or sectional interests should grow to unduly large dimensions in these latter localities. Herein the Bill deserve high encomium, since there is always some cleavage of interests everywhere between the great towns and the country; and, in days to come, with the *pari passu* development of agriculture and industries in India, and with their growing competitive demands for capital, the rival character of these respective interests will be emphasised.

It is satisfactory to find that Indian predominance in the electorate and the directorate of the bank is to be assured. But that position would have been reached anyhow, with the

* Appeared in the "Capital" of 19-1-28.

preference given to small applicants at allotment and the regional plan of the electorate. However, it is a pity, in view of these ample safeguards, to introduce anything like racial discrimination among the provisions of the most liberal of the many recent measures having for their object the building-up of the financial autonomy of our country. It is curious that India, which is aiming at a Dominion status, should do what no Dominion has done by preventing British subjects with an English domicile from holding shares of the Reserve Bank. This is the more strange since the maximum of shares held by any such individual would be worth Rs. 20,000 only.

The principle of a shareholders bank seems about to triumph, as was indeed very desirable. India cannot have forced upon it fantastic schemes of a central bank which would amaze, and arouse the ridicule of other nations, and would lead to the loss of confidence in the Reserve Bank on the part of the other banks. In the words of the ablest commercial writer in India—the late Mr. Pat Lovett—“What is certain is that a Reserve Bank is not of such urgent importance as to render *any* type of Reserve Bank better than none at all”. If we can draw an inference from the history of State banks it is this, that State banks can thrive only when they are run by financial dictators and autocrats. As is well known, the Commonwealth Bank of Australia owes what reputation and prestige it possesses to the regime of a single Governor unhampered by a Board of Directors. The State Bank of Russia, too, was at its best when under the rule—a better word in this connection than “management”—of Count de Witte. Are we in India desirous of giving a trial to a regime of *Petat o'est moi* in the banking sphere?

It has been claimed indeed that the quintessence of the State bank proposal has been extracted and blended in the new scheme. But the claim does not do justice to the merits of that scheme in certain very important respects. It would have been more to the point to say that, while a State bank as an institution leads to autocratic management, the scheme of regional directors as laid down in the Bill will be one of

the early experiments in the democratisation of the control of central banking. It is a valuable innovation in banking practice and will form one of the feature of Indian banking which other countries will study with interest. Every care has been taken in the Bill to foster this democratisation of control of introducing the broad based distribution of the share capital, both at the time of allotment and after and the regional plan of the directorate. In the United States too, when the Aldrich plan tried to centralise banking power too much, there was an agitation against it ; and now democratic organisation and control are secured there by the plan that Federal Reserve Banks are managed by boards of directors democratically chosen and representing all classes of interest. The American method and the method employed in our Reserve Bank Bill form alternative methods for attaining the same object.

It is a welcome feature of the Bill that the reference to the gold *mohur* inserted by the joint committee has been removed. Attempts are being made to mix up the currency and the banking problems of the country ; such efforts and tendencies should be firmly resisted. The great task of a general monetary and banking reconstruction, on which India is now engaged, can never be finished if the Reserve Bank Bill is made an excuse and an occasion for "re-thinking the whole problem of our standard". The suggestion that the question of a gold currency for India should be taken up as one of the side issues of the Reserve Bank Bills needs only to be stated clearly in order to be rejected. For one thing, Indian economists are coming to recognise the impossibility of anything like an actual gold currency, at any rate for years to come. What then, is the use of calling into existence a mere abstraction and shadow of a gold currency, which would surely be taken by the rest of the world as the sign at once of our hankering after gold and of an unpractical temperament ? Why mix up the immediate and practical object with a remote and unpractical one ?

It deserves to be noticed that the minimum amount of

gold to be purchased or sold has been reduced in the Bill from 1,065 tolas to 250 tolas. Such a reduction of the amount proves conclusively—if, indeed, proof were needed—the *bonâ fides* of those who are organising the Reserve Bank scheme, and demonstrates that the currency and exchange business of the country is to be run on scientific and satisfactory lines. The mechanism of the free sale and purchase of gold by the Reserve Bank will make our currency and exchange systems as perfectly automatic as they can be rendered. Critics have spoken, indeed, of potential manipulations of these by the future Reserve Bank. But none of them have defined, indicated or even suggested how, or in what direction, any such manipulations are possible in the face of the Reserve Bank's obligation to buy and sell gold freely from and to the public once the brief period of transition is over. The acceptance and working of this obligation will render impossible any apprehended "manipulations of currency" or "regulations of exchange". That obligation is the central proposal of the bill and dwarfs all the others. [Indeed, a few years' working of that obligation will render obsolete most of the criticism of our monetary system as well as the demands for a gold currency.]

The proposed restriction on open market operations is put in avowedly in order to reassure the commercial banks. But even without it there was no possibility of "indiscriminate competition" with them, looking to the restrictions placed on the work of the Reserve Bank and the severe limitation of its profits. The importance of open market operations is particularly great in this country, where means have yet to be found to make the Bank rate effective. Nor should we forget that the possession of a certain amount of commercial business is of great advantage to a central bank. Let us hope, therefore, that the scope of open market operations will not be unduly restricted.

It is to be also hoped that in the final scheme means will be found to secure the just interests of the Imperial Bank. This is urged here, not in the interests of its shareholders, but

with the view of securing some measure of consistency in the banking policy of this country. For how will the problem appear to the future historian of banking in India? He will start with a study of the prospects—indeed, pledges—offered to the Presidency Banks to secure their amalgamation. For this purpose he will study the famous Minute written on this subject by the Government of India in 1919, which defined the objects, the conditions and the ends of the amalgamation. That Minute state explicitly and repeatedly that the scheme in many of its features went far beyond a mere amalgamation, such as would have served the interests of the Presidency Banks themselves. Among other things, the increase of capital was certainly not called for by the interest of the Banks themselves. Further, before the amalgamated banks were held out the prospects of being a “banker’s bank” and “a strong unified bank in intimate relations with Government”. But only five years later the Indian Currency Commission reduced the functions and resources of the Imperial Bank from those of a central bank to those of a mere “initiator of banking facilities”, and of an agent of the Reserve Bank and now voices are heard, asking that it be deprived of even that position. Let India, however, do justice to an institution which is her oldest and strongest child in the banking sphere, tracing that claim through the Presidency Banks. It is one of the merits of the Bill that it stands in the way of the extreme proposals which would give a great shock to the status of the largest Indian Bank with the longest traditions behind it. Let us plan and legislate to the best of our ability for the future, but so as not to lose and relinquish the solid achievement of a century of banking experiments in India. It is but fair to expect that the second schedule of the Bill will be studied with a due regard to these considerations, which form its full basis and justification.

SIR BASIL BLACKETT'S ACHIEVEMENTS.*

Apart from the stabilisation of our currency and the projecting of centralised banking on sound lines, the great achievement of Sir Basil Blackett's tenure as Finance Member has been the rehabilitation of Indian Finance. Perhaps, indeed, the word rehabilitation does less than justice to his successful work ; because he has not only removed the aftermath of war, but has made notable permanent improvements in our system of finance. Other financiers had created the railway asset of Indian finance—he gave a permanent form to its contribution to the public purse, and reconciled the claims of the State to a just share of profits and of the Railway system to its development. Others have regretted or apologized for the Provincial Contributions ; he has abolished them permanently. It was left for him also to abolish the old controversial impost—the cotton excise duty. The long-awaited reduction of railway rates and fares was realised in his regime. Nor should we forget the changes in the budgetary form and improvements in the financial machinery, e.g., the changes in the form of the Demands for Grants and improvement of Appropriation reports. Any one of these measures would have sufficed to make a financial reputation. It is very desirable to realise the general plan which appears to underlie the financial achievements of Sir Basil Blackett. The first thing to be done, and the one which he felt to be the most important item in his programme, was the reduction and avoidance of our unproductive debt and the improvement of the credit of India. He carried on this vitally important task in spite of protests and criticisms directed against him about "the surpluses going into the huge machine for the reduction or avoidance of the debt." The matter next in importance was the reduction of the salt tax and the abolition of admittedly objectionable taxes like

* Appeared in the "Capital" of 5-4-28.

certain export duties. *Pari passu* and by gradual approaches, the problem of Provincial Contributions was to be solved. The next problem to be attacked was that of the readjustments of the burden of taxation in general and the reduction of the import tariff in particular. This problem is being rendered more urgent by the constant rise of the average level of the duties through the growth of protection. Sir Basil had gone so far as to institute a departmental inquiry on the subject. The problem of the readjustment of import duties would have been best tackled as a whole. But the depression of the textile industry compelled him to anticipate the general arrangement in one direction. Had his term of office been a couple of years longer a far more harmonious readjustment could probably have been arranged.

In this year's budget we find the full results of the policy of debt redemption followed so scientifically. The permanent machinery for debt redemption was installed none too soon, seeing that the five successive deficit budgets which preceded his arrival had resulted in a total deficit of 100 crores. The new scheme did its work with phenomenal rapidity. By 1927 the unproductive debt had fallen from 231 crores to 201 crores while India could borrow at the rate of 4'69 per cent. (subject to income tax) as compared with 6 per cent. income tax free in 1922. This year's budget tells an even satisfactory tale; for, "the saving in the interest on dead-weight debt in the five years is more than three-and-a-half times the increase in the provision for debt redemption and over a crore more than the actual provision on this account in 1928-29." It is idle to cavil at such very substantial results by taking advantage of the fact that there was no proper compilation of the debt position of India before Sir Basil's tenure of office. Yet there are critics of the budget who cannot understand how the unproductive debt has been recently reduced. They might be referred to such standard works as Strachey's on "Indian Finance" for a full discussion of the successful procedure which nearly wiped out the unproductive debt before the war. The proper way of envisaging the problem is to look at the aggregate debt and

assets, and to balance the assets created by the productive debt against the unproductive debt. But, after all, the best judges of the situation are not critical politicians but the business men of the market place, and the purchasers of the Government loans both at home and abroad. They are perfectly satisfied ; nor are they to be alarmed by any references to the liability on postal cash certificates, since they look on Government liabilities as a whole, and they are fully aware that the surpluses have enabled the Finance Member to outdistance even his own fixed programme of debt redemption. Is it fair to point to individual liabilities and yet to ignore the accelerated speed at which the aggregate liabilities are being reduced ?

The judicious and tentative way in which the problem of the Provincial Contributions has been tackled is notable. By 1926 half of the total contributions had been remitted while in 1927 the entire amount was wiped out, though through an excess of financial caution the remission was stated to be temporary only. This year the contributions, which "have brought curses and not blessings both to him who has given and to him who has taken," are gone for good. No other Finance Member has shown such consideration and sympathy for the Provinces as Sir Basil, who laid down the dictum that "the natural use of a recurring surplus is to reduce Provincial Contributions." Indeed, but for the urgent need of helping the cotton industry by abolishing the excise duty, the remission would have come even earlier.

Yet, efforts are being made to belittle these achievements by hinting that in the higher exchange ratio the Finance Member has discovered "an invisible income" to assist him. To this plea the answer is that the proper basis of comparison is not the gold value of the Rupee but its commodity value. The rise of prices no doubt embarrasses finance, and as was pointed out in 1927 "even now gold prices are about 50 per cent. higher than they were in 1914." The ground which the fisc lost by the persistent and long-sustained rise of prices has been only partially regained since. As Sir R. Giffen showed, if prices have risen and their action has not been counter-

balanced by increase of taxation, there is a virtual remission of taxation.

But there is a very real sense in which the stabilisation of currency has brought a financial reward. As the present budget shows, the figures of India's trade reflect the advantages which have accrued from the stabilisation of the Rupee. In the last twelve months, both the imports and the exports of merchandise have increased *pari passu*. Indeed, these figures are the best answer to the fear that the higher exchange will penalise exports. As a corollary of the stable prices and the increase of trade we have "the remarkable improvement in the railway figures for 1927-28, which by enabling important reductions to be made in railway charges, will itself give a new stimulus towards business and agricultural prosperity." Thus, the established ratio does indirectly help Indian finance though not in the sense in which its critics envisage the matter.

As Sir Basil has put it, the budget is not a spectacular one. But, he himself has established the standards and conditions which have deprived it of its spectacular character. Six years ago such a budget as the present would have appeared spectacular enough ; and, even now, if to the disposal surplus of five lakhs we add the 258 lakhs utilised for wiping out the contribution as well as the 84 lakhs spent on helping the Bombay textile industry we perceive how successful the budget really is. However, successive remissions of taxation and a host of financial improvements have terminated for the present the dynamic stage of Indian Finance, and we are now in the statical condition of benefiting steadily from the financial work of the past quinquennium. Perhaps in the next stage, the successor of Sir Basil Blackett, working on the foundations so well and truly laid by the latter, will make further progress by reducing, for instance, the income tax and super-tax still retained at the high post-war level.

CENTRAL BANKING.

About the time that the Reserve Bank Bill was wrecked there appeared a notable and meritorious work on "Central Bank" by Mr. Kisch and Miss Elkin which is likely to remain for a long time the standard work on the subject with which it deals. The authors are to be congratulated alike on their lucid and suggestive exposition of the principles of Central Banking, on the wealth of details of the legislation on the topic which they have brought together and on their manner of tracing the evolution and development of banking centralisation. Had the work appeared a little earlier it would have certainly influenced for the better the debates of the Legislature as well as of the Joint Committee and would have rendered yeoman's service by freezing out a number of fallacies and correcting the great many negligent statements which passed for current at the time. However, even so the Reserve Bank Bill is not dead—it is only in a state of suspended animation. To use the phraseology of economists, the Reserve Bank Bill is a long-period phenomenon not so easily or quickly disposed of. In the near future, India must take up again the task of the formation of a Central Bank, and when that time comes the experience garnered by Mr. Kisch and Miss Elkin will prove of great value. As it is, the work forms a valuable commentary on the banking proposals of the Royal Commission on Indian Currency as well as upon the Reserve Bank Bill. It is as such that it is proposed to examine the book here, and to show with its help that whenever India resumes the work of building up a Central Bank it cannot advisedly depart materially from the provisions of the last Bill.

Let us begin with the dominating issue—that of the State Bank. In the Assembly Pandit Madan Mohon Malaviya summarised the prevailing misconception on the subject thus: "I have given instances of State Banks which have come down

from a long time. How many Shareholders' Banks are there in existence?" The answer can be easily given with the help of the present book. It is impossible to discover a single State Bank "coming down from a long time." They have all been formed virtually in the last decade, and have still to win their spurs. They are very few in number—those of Russia, Finland, Australia, Latvia, Esthonia and Scandinavia. Not only is the list a small one and the countries comprised in it of second-rate importance but the present movement is distinctly away from the ownership of the capital of Central Banks by the State. Thus in Esthonia the constitution of its Bank contemplates that the shares of it held by the State should be sold to the public in two years' time from the start. In Japan, the State was allowed by law to hold half the capital of the Central Bank but actually none of the capital is so held at the present time. But, what is more, even among the recently established or recently reorganised Banks there is already a *tendency to move away from complete State control*. Thus, Bulgaria has introduced an independently elected element on to the Governing Body of the Bank, in Esthonia a new bank is to be set up in place of the State Bank and more independence is to be given to the Bank of Czecho-Slovakia. Two important considerations form the motives for this divorce of Governments from control of Central Banks. In the first place the danger of State control of the currency lies in the temptation to the Government to treat its political difficulties as justifying an inadvisable currency policy. Again such control by State is becoming particularly dangerous at the present time when Socialism is trying to dominate both the political and economic spheres.

In the course of discussions on the Reserve Bank Bill the contention was very energetically put forward that members of our Legislature should be directly, and as such, elected to the Directorate of the Reserve Bank. But the wealth of material collected in the book makes short work of this contention and proves decisively that the general practice is to debar legislators from serving on the Board while the Executive is usually given proper facilities for supervising and influencing the work

of the Board. Thus in Belgium "no member of either Chamber may be a member of the Board of Directors." In France, the Governor and the Deputy Governor are appointed on the proposal of the Finance Minister but may not be members of Parliament. In the United States no senator or representative of Congress can be a member of the Federal Reserve Board or even an officer or a director of a Federal Reserve Bank. Similar disqualification of legislators only can be found on reference to the Charters of the Central Banks of Austria, Czecho-Slovakia, Esthonia, Poland, etc. Only Sweden and, to a certain extent Switzerland, follow the opposite practice.

On another important and much-debated point in our recent controversy the work of Mr. Kisch and Miss Elkin throws much-needed light. It has been argued in the Legislative Assembly that the obligation to keep statutory reserves with the proposed Reserve Bank "will work as a millstone round the necks of the indigenous banks" and will handicap them. The answer is that it is only by controlling the reserves of the commercial banks that any Central Bank can acquire the power to control credit, and in particular, to enforce a restriction of credit if that is considered desirable. It is only then that the Reserve Bank can become a real bankers' bank "strong enough to carry out a definite line of policy." This general line of reasoning is reinforced by recent and concrete examples of the ill consequences of the want of such a provision. It was for want of such a provision that in 1925 the Bank of Poland failed to control credit and the policy of fixing the fixed exchange value broke down within a year. Again, a very important contributory cause of the frequent financial crises of Japan has been the continued granting of excessive credits by the commercial banks—a state of affairs which is due to the fact that only a few of these banks keep their balances with the Bank of Japan or co-operate closely with it. These matters deserve to be pondered over by those who believe that without any legislative compulsion our commercial banks will keep the necessary balances with our future Central Bank. In the face of the persistent misfortune, miscalculation and

mismanagement which have been afflicting our indigenous banks for the last fifteen years we cannot afford to be slack. When Sir Purshotamdas complained that the indigenous banks "are not multiplying very fast" he was not on the right track. They multiply at an adequate and satisfactory pace, but they die out even faster—witness the statistics of 1913 and of 1923. The infant mortality of which we justly complain as regards our population is but small as compared with the infant mortality in our banking world. That is the proper answer to those who contend that "it would have been better if the Reserve Bank had come in the course of natural evolution." Had a Reserve Bank with its proper influence on the formation and practice of banks existed in 1913 and in 1923 the evolution of indigenous banking would have proceeded far more rapidly, and many of the banks which have gone down then would be prospering and serving national interests at present.

We were also told in the course of the debates in the Assembly that "the Reserve Bank is intended not to cure the unsound currency system in India, but somehow to bring it in a line for other purposes with foreign nations." That was a strange way of defining the potentialities of a Reserve Bank which was to work the Gold Standard in India, to control credit and to secure the formation and working of commercial banks on secure and sound lines. Nor should we forget that in course of time a Reserve Bank of India will take its full and equal share in the great work of co-operation between central banks in ensuring the smooth working of the gold standard in the world, in holding gold values stable and in securing the stability of price levels.