

# **BANK FOR INTERNATIONAL SETTLEMENTS**

## **SEVENTH ANNUAL REPORT**

**1st APRIL 1936 — 31st MARCH 1937**

**BASLE**

**3rd May 1937**

## TABLE OF CONTENTS

	Page
I. Introduction . . . . .	5
II. Exchange rates, Price Movements and Foreign Trade . . . . .	18
III. A Year of Mounting Gold Supplies . . . . .	37
IV. Capital Movements and International Short-Term Indebtedness . . . . .	57
V. Trend of Interest rates . . . . .	69
VI. Developments in Central and Commercial Banking during the year . . . . .	92
VII. Current Activities of the Bank:	
(1) Operations of the Banking Department . . . . .	99
(2) Trustee and agency functions of the Bank . . . . .	103
(a) Annuity payments of Germany, Hungary, Bulgaria and Czechoslovakia . . . . .	104
(b) German External Loan 1924 and German International 5½% Loan 1930 . . . . .	104
(c) Austrian Government International Loan 1930 . . . . .	105
(d) Other agency functions . . . . .	105
(3) Net profits and distribution . . . . .	106
(4) Changes in Board of Directors and Executive Officers . . . . .	108
VIII. Conclusion . . . . .	110

## ANNEXES

- I. Central banks or other banking institutions possessing right of representation and of voting at the General Meeting of the Bank.
- II. Balance sheet as at 31st March 1937.
- III. Profit and loss account and appropriation account for the financial year ended 31st March 1937.
- IV. Trustee for the Austrian Government International Loan 1930:
  - (a) Statement of receipts and payments for the sixth loan year (1st July 1935 to 30th June 1936).
  - (b) Statement of funds in the hands of depositaries as at 30th June 1936.
- V. Trustee for the Austrian Government International Loan 1930 — Interim statement of receipts and payments for the half-year ended 31st December 1936.
- VI. International Loans for which the Bank is Trustée or Fiscal Agent for the Trustees — Funds on hand as at 31st March 1937.
- VII. The Tripartite Monetary Agreement of 25th September 1936:
  - (a) Statement of the French Government;
  - (b) Statement of the British Treasury;
  - (c) Statement of the United States Secretary of the Treasury.

**SEVENTH ANNUAL REPORT**  
**TO THE ANNUAL GENERAL MEETING OF THE**  
**BANK FOR INTERNATIONAL SETTLEMENTS**

Basle, 3<sup>rd</sup> May 1937.

Gentlemen:

I have the honour to submit to you the Annual Report of the Bank for International Settlements for the seventh financial year, beginning 1st April 1936 and ending 31st March 1937. The results of the year's business operations — approximately the same as those of the preceding year — are set out in detail in chapter VII. After careful provision for contingencies, the Board recommends to this General Meeting an annual dividend of 6 per cent. and the statutory allocation to reserves.

In the year which has passed since the last General Meeting great monetary changes have occurred. In France, a new economic and financial policy was adopted in the spring of 1936, and in the early autumn a decision was taken to readjust the value of the French currency. On 25th September 1936 simultaneous declarations were issued by the French, British and United States Governments in which the three governments declared their intention to continue to use appropriate available resources so as to avoid as far as possible any disturbance of the basis of international exchange resulting from the proposed readjustment. During the same week-end a decision was taken in Berne to change the value of the Swiss franc and at The Hague an embargo was placed on the export of gold; shortly afterwards the Italian authorities readjusted the lira to a new gold basis, while the Czechoslovakian crown was further devalued in relation to gold and the Latvian currency was devalued and attached to sterling.

The technical measures taken in the various countries and the arrangements agreed upon by the different monetary authorities will be referred to later in this report. Here it may be noted that the changes in the values of the currencies concerned were carried out with a minimum of disturbance to the foreign commodity and capital markets and that no setback was caused to the upward trend of world affairs.

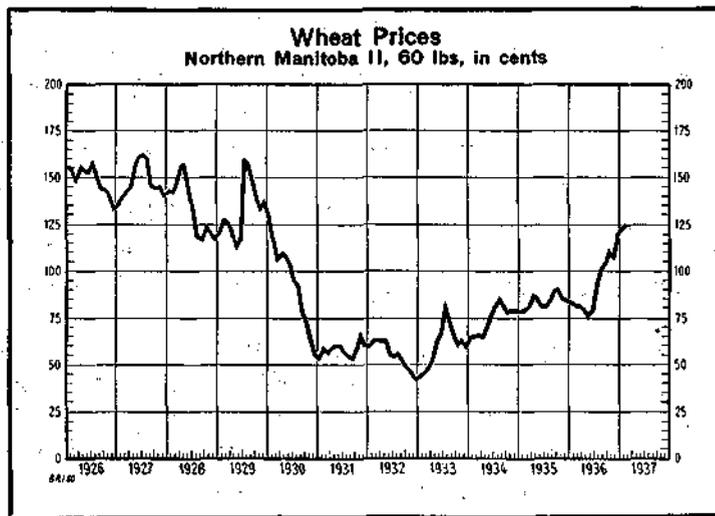
Economic recovery has continued at an accelerated pace in the past year; for the first time since the beginning of the depression practically every important sphere of business has been brought into the upward movement. The basis of this recovery has been the restoration of equilibrium between costs and prices, making business again remunerative and thus enabling it to assert its own natural tendency towards expansion.

The recovery in industrial activity which is a distinct sign of the turn in the business cycle is without doubt due in part to the readjustments made in the course of the depression through liquidations, capital reconstruction,

and an adaptation of costs in different lines of business. Normally, however, the process of readjustment would have been completed in two or three years and the prolongation of the depression beyond that period must be attributed to additional adverse elements which, originating in the past, complicated the process of recovery. It is against the background of the economic and financial developments in the post-war decade that, apart from political complications, the correction which has since been achieved and the leeway which still remains to be made up can most clearly be seen.

First, a world-wide agricultural depression coincided with the industrial decline and the importance of this juxtaposition may be judged from the fact that more than sixty per cent. of the world's population is still engaged in agriculture. The simultaneous occurrence of an agricultural and an industrial depression is contrary to the experience of many earlier business cycles. For instance, there was no decline in the prices of agricultural products in the depressions which started in 1900 and 1907 respectively. In the post-war period prices of agricultural products kept abreast of industrial raw material prices up to 1928; from that year, however, a decline, especially in the prices of cereals, began to make itself felt. For a time prices were sustained by government intervention; large purchases (especially of wheat) were made and the supplies so acquired kept in stock. When commitments became too heavy and purchases were discontinued, the existence of the accumulated stocks weighed heavily on the markets and the price of wheat fell, in terms of gold, to the lowest figure recorded for four centuries.

As cereal production became more unremunerative farmers in many countries began to shift towards greater production of live stock and live-stock products, and from 1931 onwards the prices of these latter products also fell rapidly. The following curve shows the prices quoted for wheat on the Winnipeg market from 1926 to 1937. The lowest point was reached at the



beginning of 1933 and the first upward turn was connected with the depreciation of the Canadian and United States dollars. There followed government action in the United States to limit the output of agricultural products and thus to lift prices, but a more powerful influence was exerted in the years 1935 and 1936 by bad weather conditions re-

sulting in deficient crops. In the latter year there was drought in the United States and too much rain in Europe, and owing to the resulting crop failure the price of wheat in Winnipeg was brought up to about \$1.25 in the be-

ginning of 1937. The recovery was thus largely accidental; even so it must not be overlooked that there are also a number of permanent factors which are likely to have a sustaining influence on the prices of agricultural products.

The large stocks of wheat which previously had a depressing effect upon the markets have now been practically disposed of. Moreover, the volume of future agricultural production seems to have been somewhat impaired, not only as a result of the dust-storms which will affect large areas in North America for years to come, but also by other factors. During the depression farmers in the large producing countries were unable to manure their land, renew their equipment and generally to maintain their production at the same level of efficiency as in the past. The following table shows that the total output of agricultural products has remained almost stationary since 1929, although in the same period there has been an increase of about ten per cent. in world population. For the sake of comparison an index of the production of raw materials of non-agricultural origin has been included in the table.

Indexes 1925-29 = 100 *	1929	1932	1933	1934	1935
World production of agricultural products	103	103	104	102	102
of raw materials of non-agricultural origin	114	75	84	95	104

\* Source: League of Nations' "World Economic Survey 1935/36", pp. 59-60.

Trade all over the world consists to a large extent of an exchange of goods between industrial and agricultural communities. When, in the depression, the production of agricultural products was more or less maintained but industrial production became restricted, the uneven development was necessarily injurious to the terms of trade at which agricultural products could be marketed. It can be seen from the figures in the above table that from 1934 onwards a better balance has been attained once more between the volume of agricultural and industrial production. Considering that in most agricultural pursuits remuneration is still at a relatively low rate, it seems unlikely that in the world as a whole any increase in agricultural production may be expected comparable to the increase in industrial production. While the aggregate output of agriculture will continue to increase, agriculture will presumably form a declining proportion of the economic activity of the world; but such a development is fully consistent with, and indeed a necessary condition for, a return to agricultural prosperity.

Secondly, the gold market in the post-war decade was largely characterised by a tension connected with the large movements of funds from one market to another and the support of a price level which was fully forty per cent. higher than in 1913 — and this at a time when the world's annual gold production remained at a somewhat lower figure than in the years immediately before the war. From 1924 to 1929 gold was produced in the world at an annual rate of 19 million ounces which, at the price

of 84s. 11½d. per ounce, gave a value of just over £80 million. Of this amount some £30 million were used for non-monetary purposes, including the demand from India, China and some other oriental countries, leaving about £50 million a year as the supply available to meet monetary requirements.

When in the course of the depression commodity prices and costs began to fall the world's gold production gradually increased. This increase became accentuated after 1931 when in terms of depreciated national currencies the price of gold rose suddenly by 40 per cent. or more. From 1929 to 1936 gold production rose from under 20 million ounces to over 35 million ounces, or by nearly 80 per cent.; and at the London gold price of about 140s. per ounce the output of gold attained an aggregate value of £245 million in 1936. In recent years the industrial demand for gold has been met largely by the recovery of gold from the public. Furthermore, not only did the hoarding of gold in Europe for private account, which had assumed large proportions during the depression, come to an end in 1936 but some dehoarding set in; and shipments of gold were still received from India, China and other eastern countries.

On balance the whole new production of gold in 1936 was available for monetary purposes; instead of the £50 million per annum available ten years ago, fully £245 million of newly-mined gold was available in 1936 at the price ruling on the London market. The whole situation has radically changed in comparison with the post-war decade: there is now an abundant — even a too abundant — supply of gold.

Thirdly, certain of the main currencies were stabilised in the years 1924–1930 at rates which were 10 or 15 per cent. out of keeping with their inherent values as measured by relative cost and price levels. The task of necessary adjustment might not in itself have been too difficult had it not been for the decline in world prices which, at first gradual, became more accentuated after the turn of affairs in 1929. One result of the currency depreciations which began in 1931 and the subsequent movements of costs and prices has been, on the whole, to bring the various currencies subject to these changes into a better relative position to one another. Moreover, the upward movement of prices should make it easier for the various currencies to adapt themselves to the requirements of an international standard and should eliminate the disturbances which arise from an over or undervaluation of currencies.

Fourthly, interest rates, especially on long-term obligations, remained high after the war, but a reduction was bound to come when the capital equipment of the world had been restored. This adjustment was even more imperative after the depression had begun, as a downward movement of interest rates is one of the classical means of promoting recovery. In view of the large government debts which had been incurred during and after the war, it was impossible, however, to bring down interest rates before these debts had been converted to lower levels. The great conversion of British war loan in the second half of 1932 was, therefore, of outstanding importance not only for Great Britain herself but also as a lead for other countries.

During the last five years great progress has been made in a large number of countries in bringing about a reduction of domestic interest rates.

A fair number of foreign loans have also been converted, but here the difficulties have been greater and an important uncompleted task is the application of lower interest rates to foreign obligations.

Fifthly, the heavy burden of debts both domestic and foreign was also in other ways an obstacle to economic recovery, especially as the debt structure inherited from the war was augmented by extensive international borrowing in the 'twenties both on long and short-term account. In some countries the main difficulties were caused by an excessive volume of private indebtedness, e. g. mortgage debts of farming communities, in other countries by internal government indebtedness weighing heavily on the budgets, and again in others mainly by foreign liabilities which were a charge on balances of payments and on monetary reserves.

Some progress has been made during the depression in scaling down the debt structure. In addition to the effects of currency depreciations, the burden of domestic debts has been alleviated by conversions, and foreign indebtedness by repayments, repatriations and arrangements of different kinds. The volume of international short-term indebtedness has thus been brought down by about one-third in terms of sterling (a currency in itself depreciated by almost 40 per cent.) and by still more in terms of gold. Long-term indebtedness has not been reduced to the same extent, but there has been a very important movement in the repatriation and redemption of foreign securities, especially from the United States and Great Britain.

Sixthly, increased tariff levels represented a great hindrance to the attainment of equilibrium and the difficulties increased when, with the advance of the depression, the volume of international lending was suddenly reduced and as a consequence the balances of payments and monetary reserves of the debtor countries became exposed to a most severe strain. In this field the depression brought not only no relief but a change for the worse. Human ingenuity has excelled itself in the invention of obstacles in the path of the international exchange of goods and services. When a development of foreign trade seemed hopeless, a great many countries concentrated on production for their home markets to provide increased employment, and this is one of the reasons for the strengthening of autarchic tendencies in recent years. The remedies thus adopted were however pregnant with new difficulties, the growing artificiality of the various national expansions hindering a general world improvement.

Periods of falling prices have usually been periods of rising tariffs and it is therefore not surprising that the precipitous price fall after 1929 led to an increase in economic nationalism. But will the reverse now be true? Will the rise in prices which has set in produce a return movement towards freer trade? There are already some signs which, though still faint, indicate a certain change in the attitude both of the public and of those in power. The bilateral commercial treaties negotiated by the United States Government provide for mutual reductions in tariff rates and in some countries quotas and similar restrictions begin to be loosened by unilateral action taken, as a rule, to prevent a sharp rise in prices on the home market. Moreover, specific duties if maintained unaltered represent a lower percentage of the value of the goods

to the extent that prices have risen. The improvement so far achieved is, however, slight and the world is still far from enjoying that freedom of trade which obtained in 1929.

It is now possible to sum up the changes that have occurred with regard to the various adverse elements responsible for the depression. In most cases there has been a distinct change for the better: the cyclical movement of industrial activity has turned and is now moving in an upward direction; the supply of gold has risen to the point of abundance; the currencies which have been subject to depreciation have been brought into better relation to one another; and interest rates on domestic borrowing have been reduced though there still exists a substantial volume of unadjusted foreign indebtedness. As regards agriculture, the position is relieved for the moment by increased prices, but this relief is to some extent, though not wholly, the accidental result of unfavourable weather conditions. Some important progress has been made in the adjustment of debts by means of conversions and other operations but the burden of indebtedness is still heavy in many countries and many foreign debt problems have still to be tackled. As regards tariffs and other trade restrictions, the situation is very much worse than before the depression and this setback is at the core of some of the most difficult problems with which the world has to grapple at present.

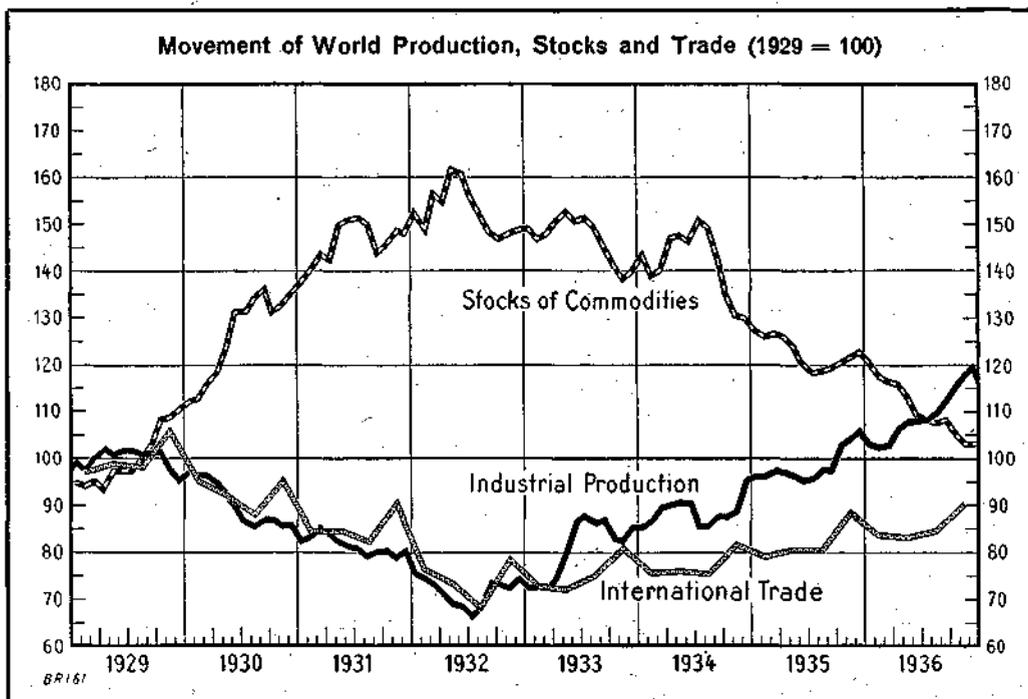
The better equilibrium between costs and prices which is at the basis of the present recovery has been achieved in a number of different ways. It has been attained partly by adaptation of costs, partly also by monetary changes, including the currency depreciations which have reversed the trend of price movements. In some countries intense activity in the building trade due primarily to private initiative has been the mainspring of recovery; in others, government outlay has been the most important factor. There has been much controversy as to the part that public spending of borrowed funds can play in overcoming a depression. In fact, the budgets of most countries have shown large deficits and the policy of defraying expenditure from proceeds of loans has thus been almost universal. In some countries where this occurred recovery set in early, while in others it was delayed. The conclusion would seem to be that only if general conditions making for an equilibrium between costs and prices are in process of being established will government spending assist recovery; if these conditions are lacking the result of such spending may on balance be directly injurious, for continuous borrowing to meet excess expenditure may undermine confidence and retard the natural fall of interest rates.

Whatever may be said for a policy of public works in times of depression, there can be no question about the undesirability of increased government outlay once the expansion of business is in full swing, for then there is the danger that the extra stimulus may produce an unhealthy boom. From this point of view the present rise in armaments expenditure is to be deplored. Let it be said in passing that in the Anglo-Saxon countries as well as in most of the smaller countries of Europe, expenditure on armaments began to rise substantially only in the course of 1936 and that up to then this expenditure

had relatively little to do with the increase in production in those countries. Now, however, their expenditure for armaments has been increased to a higher level than ever before in peace-time. Considering the phase that has been reached in the business cycle, this increase comes at the wrong time; and it tends to stimulate the wrong trades, i. e. those that are already benefiting most from the general recovery in business. It has been calculated that for the world as a whole the level of armaments expenditure in 1936 was, on a gold basis, three times as high as in 1913 and more than twice as high as in the years 1924/30. Moreover, the amount of money involved in the orders placed for armaments in 1936 was in many countries in excess of the current armaments expenditure in that year, and it is the placing of orders which primarily affects business arrangements.

One of the results of the armaments expenditure is that the attention of producers is concentrated on the home markets and they therefore become less interested in export business. For the countries which are arming this certainly constitutes a grave disadvantage, but such is the irony of circumstances that this situation, although it is a consequence of armaments, may ease the tension of international competition; when manufacturers are fully occupied they are less concerned about the shifting of trade to other countries and are more willing to share contracts in foreign markets with producers who would normally be their strongest competitors.

The stimulus thus added by heavy government expenditure has been superimposed on a recovery which in a number of countries has already been in progress for a considerable period. Even taking the world as a whole a turning-point in the depression came in 1932, though at first the improvement was slight and subject to setbacks. The following graph shows the changes



that have occurred during the past eight years in the physical volume of production and of international trade and also in the stocks of raw materials. In the autumn of 1932 industrial production began to increase and stocks of commodities to decline. The improvement in production continued up to the summer of 1933, but then for nearly two years there came a distinct slackening in the upward movement until, in the summer of 1935, the recovery became more definite.

Since the turning-point in 1932 five years have now passed, and in the history of business cycles the duration of an upward trend for a period longer than five years has been a very rare occurrence. The records of Great Britain furnish no examples of a past improvement in business continuing uninterruptedly for more than five years, and in other countries only a few isolated instances may be found. In view of this experience in the past, is it to be expected that the present recovery will soon come to an end? It is, of course, impossible to give any definite answer to this question, but it can be pointed out that in some fundamental respects the present recovery possesses certain very distinctive characteristics which may make it possible to take a somewhat hopeful view of the position as it now presents itself.

First of all, the change for the better began in the various countries at quite different dates. Only as regards the sterling area is it possible to speak of an improvement lasting over five years. In the United States the recovery, apart from a spurt after the depreciation of the dollar in 1933, began in the course of 1934 and the German recovery, conditional upon large government expenditure, dates roughly from the same year. In the countries belonging to the former gold bloc little sustained improvement was seen before the autumn of 1936. There is a possibility that the development in those areas which were late in joining the upward movement may in a certain measure give support to the general trend of affairs and postpone any setback in world business.

Further, it is to be observed that the recovery which began in 1932 has been very gradual, extending over several years before the level of production of the previous period of prosperity was reached. The deeper the fall, the longer the period of improvement; but recovery is not the same thing as prosperity and the long time taken to regain lost ground does not in itself limit the possible duration of prosperity. The graph reproduced above shows that for the world as a whole the volume of production at the beginning of 1936 had just reached the 1929 level. For years there was very little extension of industrial plant and equipment apart from the industries which have been developed under protection, and their expansion was often held back by the decline in the purchasing power of the public. In general such recovery as there has been in recent years has consisted in the better employment of existing capacity. This is particularly true of the countries producing raw materials, which have only gradually been able to make normal use of their existing means of production. Indeed, it would seem as if the shadow of depression remained in the minds of producers so long as existing plant was only partially employed.

In so far as prosperity means development beyond levels previously attained, the raw material producing countries really only began to emerge

from the depression in the course of 1936. Also in the industrialised countries in western Europe and in the United States there seems so far to have been less extension of industrial plant and equipment than was the rule in previous periods of business expansion. Industrial concerns have in a large measure been able to finance whatever extensions were undertaken from funds which they had previously accumulated. Corporate issues of shares and bonds for the purpose of obtaining additional capital have been relatively limited. In the United States such issues amounted to \$ 1,200 million in 1936 compared with an average of \$ 5,000 million for the years 1925/29. Only in two directions has there been any notable increase in industrial investments: additional capital has gone into gold mining and, as a result of government expenditure, also into armament industries. It is to be expected that the recent reduction of unsold stocks and the rising prices of industrial raw materials will lead to an increase in plant and equipment over a wider field, but this is a development which in most countries is still in its initial stages.

It is a peculiarity of the present upward trend of business that it lacks some of the typical characteristics of past periods of expansion. There remains, for instance, a degree of unemployment higher than has been known in such periods in the past. Up to a point the difference may be purely statistical in that more complete information is obtainable now that organised assistance is given to the unemployed; but even so the present figures of unemployment must be regarded as unusually high, it being calculated that at the end of 1936 the number of unemployed in Europe and North America still exceeded 12 million. One of the reasons for this large figure of unemployment is the comparatively low rate of extension of plant and equipment mentioned above. It is only in the past year that outside a few countries in the sterling area and Germany there has been any marked improvement in the industries producing machinery and material required for construction. In many different branches of industry there is a strong demand for skilled workers which cannot be fully satisfied, the shortage being due in part to the relatively small number of apprentices in training during the depression. Unfortunately, the lack of skilled workers does not always lead to their replacement by other workers but rather acts as an impediment to production and may thus reduce the total volume of employment.

The return to full employment is further impeded by the difficulty of transferring workers from one trade to another and from one district to another. It is as a rule easier to enlist into the ranks of industry new recruits from the agricultural population (the sons of small farmers and agricultural labourers) than to draw unemployed from depressed areas. From 1933 to 1936 the number of agricultural labourers in the United Kingdom dropped from 716,000 to 640,000 or by 76,000, and in the same years about 50,000 immigrants came to the United Kingdom from the Irish Free State, these newcomers finding work at a time when the figure of unemployment in many industrial occupations remained exceptionally high.

It should further be noted that in a number of countries the highest percentage of unemployment is found in the export trades. When the income of the workers belonging to these trades is reduced, they are able to buy less

in the shops and spend less on services, and in that way the effects of their unemployment are spread to other occupations. In two countries in which unemployment has been reduced to more or less normal levels, Finland and Sweden, the export trade has not only reached but surpassed the peak attained in 1929 — these two countries having been fortunate in finding a very strong demand for the products which they sell, viz: pulp, paper, timber and, in the case of Sweden, also iron ore.

At present no greater impetus could be given to employment than a recovery in international trade. It can be seen from the graph reproduced above that the physical volume of international trade is still ten per cent. below the 1929 level. In previous periods of expansion improvement in international trade often led the way, while it is now lagging behind. The present trend of business may be characterised as a series of national expansions which have not yet become generalised into a common world expansion.

In these circumstances there has been very little scope for new foreign investment. The difficulties which debtor nations have experienced in meeting their obligations have acted as a deterrent to new lending, and there was little or no inducement to undertake new industrial investment so long as existing plant in raw material producing countries was not being used to capacity. With the exception of the increase in gold mining, the possibilities of profitable investment in new enterprises in overseas countries have, as a rule, been lacking. Large amounts have been invested, however, on foreign markets in shares of already existing concerns, the recovery in stock exchange quotations after the depression making such investments attractive. In the two years 1935 and 1936 foreign investors put more than \$900 million on balance into American securities and in addition bought from the United States securities, other than American, to an amount of over \$300 million. These transactions have involved a transfer of ownership of capital but no absorption of savings in new production and no such expansion of international trade as would be produced by a resumption of foreign lending for new enterprise.

A similar development has also occurred internally in some countries as, for instance, on the British market where private concerns have been turned into companies with limited liability and shares issued for public subscription. The amount paid for the shares is received by those who sell the businesses and they in their turn will have to invest the money. The capital markets in the countries where monetary confidence has been restored are characterised by a great mass of funds seeking investment; there is a substantial amount of private savings to be invested, an important element of which is the large volume of premiums collected by insurance companies, in a number of countries exceeding all previous records. On the British, American and some other markets it is this tremendous "weight of money" that seems to be the main explanation of the low rates of interest which have persisted in these years of industrial recovery despite the rise in commodity prices.

In recent months there has been some stiffening of rates, both for liquid funds and for long-term borrowing in New York, and of long-term rates in London, but the general tone of these markets is still one of cheap

money and relatively high prices for government securities. While the supply of savings in a depression is considerable in relation to the possibilities of investment, it is natural that interest rates should decline to low levels; when, however, the excess capacity of existing plant is becoming exhausted and unsold stocks of raw materials are reduced to a minimum, the time comes for an extension in productive capacity and the demand that then arises for both long and short-term credit facilities will naturally be one of the main factors influencing interest rates. Moreover, the price paid for capital tends to have some relation to the income which can be obtained from industrial activities. Statistics established in Great Britain show to what extent profits have been rising in recent years: they amounted in 1932/33, for the companies from which information was collected, to 5.9 per cent. of the paid-up capital and in 1935/36 to 9.4 per cent., and since then there has been a further rise.

At present there may be a danger that profits will be swollen by temporary factors, and that this temporary earning power will be capitalised on a new basis at too low a rate of interest. In a period of expansion, the earning power of industrial companies generally tends to be over-rated. At the present juncture there are at least two additional factors of which account must be taken. One is the tremendous increase in armaments expenditure, which presumably cannot become a permanent feature of world economy; the other is the general rise in prices, which is not only a feature of the cyclical upturn in business or a consequence of armaments activity but may also reflect a long-term trend connected with the growth of gold production. A rise in prices so long as it continues is likely to result in higher profits both real and nominal. Certain cost elements usually lag behind in the upward movement; moreover, business firms often neglect to make due allowance in their calculations for the fact that the cost of replacing materials and supplies is increasing and that, therefore, a part of the difference between their aggregate buying and selling prices should not be regarded as profit but should be set aside in order to maintain working capital intact.

Present high rates of taxation no doubt have a moderating effect on the scale of profits but, when there is an underlying tendency to a rise in prices and governments are spending more than their current revenue, high rates of taxation are not in themselves an infallible preventative against the development of a pronounced boom. The question naturally arises whether any change should be made in general credit conditions. Within the banking system a selection is regularly made of the objects for which credits are granted and greater caution than was usual in the past is now generally exercised in order to prevent lending for speculative purposes; but large liquid amounts are owned by the public and by private concerns and in so far as these are concerned selective credit control is of no avail. Steps to reduce the plethora of liquid funds have been taken in some markets — by the prescription of higher cash reserves of commercial banks (United States), by the operations of an exchange fund (England) or by other open-market operations (the issue of Solawechsel in Germany and the sale of government securities by the central bank in the Argentine).

At the London Conference in 1933 certain principles of monetary policy were laid down and it may be opportune to quote the following resolution dealing particularly with the regulation of credit: central banks "should endeavour to adapt their measures of credit regulation, as far as their domestic position permits, to any tendency towards an undue change in the state of general business activity. An expansion of general business activity of a kind which clearly cannot be permanently maintained, should lead central banks to introduce a bias towards credit restriction into the credit policy which they think fit to adopt, having regard to internal conditions in their own countries. On the other hand, an undue decline in general business activity in the world at large should lead them to introduce a bias towards relaxation".

In judging whether the present expansion of business activity is of a kind which clearly cannot permanently be maintained, it is pertinent to remember that in most areas the improvement so far has consisted mainly in the better utilisation of existing productive capacity. But the upward movement has recently gathered speed and should be closely studied. If there is an increased effective demand for capital, an adjustment of rates to a higher level need not in any way retard sound economic progress, but should rather help to ensure that industrial expansion is carried out on the basis of a correct calculation of real costs. One of the difficulties in the present situation is that in certain countries where confidence has been lacking or other disturbing conditions have prevailed, the rates of interest have remained high and must be brought down further. This also applies to a number of international obligations. A possible stiffening of the rates in certain directions should therefore coincide with continuous efforts to reduce them in others.

In the years of depression the main objectives of monetary policy have been, on the one hand, to facilitate as far as the conditions on each market permitted a downward adjustment of interest rates and, on the other hand, to restore orderly conditions in international monetary relationships by an increased exchange stability and the gradual abolition of exchange restrictions. Taking the world as a whole, these objectives have as yet been only partially achieved; and already new problems have arisen out of the change in business conditions. One important element in the present monetary situation is the budget policy of the various governments. Inevitably, governments at present must be concerned with the monetary questions of the day and consider these questions in conjunction with the central banks, which possess special machinery for the execution of the monetary policy to be pursued and for gathering the knowledge required in dealing with the monetary problems. The daily management of the exchange funds that have been established has been entrusted to the central banks and this arrangement makes contact necessary. Far wider problems than the policy of these funds, however, must also be considered by the governments in consultation with the central banks, for it is increasingly necessary to take into account the monetary and financial repercussions of general political measures. To achieve and maintain orderly conditions in public finance and on the money and capital markets is still of fundamental importance and no technical measures of exchange intervention can avail so long as basic equilibrium is lacking. Nothing can be more

dangerous than to overlook the conditions essential for an improvement, in the belief that purely technical arrangements will suffice as correctives to an unbalanced position.

In the international field the Bank for International Settlements has continued to serve as a link between the central banks. Never has closer contact between monetary institutions in the different countries been more needed than at the present time when great uncertainty as to the future of the monetary mechanism is still prevailing. The Bank for International Settlements has endeavoured to follow closely the problems which arise in the different countries and in their relations to one another. The personal contact in Basle between the representatives of central banks has continued to serve the same purpose as in previous years: to enable those who participate in the meetings to consult in common on technical and other problems affecting the monetary situation.

## II. EXCHANGE RATES, PRICE MOVEMENTS AND FOREIGN TRADE.

### 1. EXCHANGE RATES.

In the course of 1935 a fair measure of stability in the world's exchange position was achieved after the period of great pressure to which first the British and then several continental markets were exposed in the first half of that year. In fact, after the devaluation of the Belgian currency on 1st April and the Danzig currency on 2nd May 1935, the exchange rates of all European and practically all extra-European currencies moved within very narrow limits for more than a year. The underlying position was however beset with great difficulties and monetary confidence had not then been restored internationally.

In 1936 the situation in France was affected by the political changes consequent upon the elections in May. The outward movement of funds from the French market, which had gone on intermittently since 1933, began again to assume large proportions and, after a respite in the summer of 1936, attained in September a very high figure. These losses, added to previous reductions in the gold reserves, led to an intense discussion about possible devaluation both among the public and by expert bodies. The Report of the Economic Committee of the League of Nations to the Council on 14th September 1936 dealt with the necessity of filling the gap which separated the price levels of the majority of the countries on a gold standard (whether real or nominal) from those of the majority of the countries with depreciated currencies. While the Committee stated that it had no wish to pronounce dogmatically for or against monetary devaluation, it pointed out that in order to maintain an overvalued currency in the face of opposing tendencies a whole series of restrictive measures must inevitably be applied, whereas in its opinion the only sound policy was that which ensured freedom of action and, by allowing active economic forces to operate with maximum facility, enabled normal relations to be resumed with other countries. The Financial Committee to which the report was submitted recorded its general agreement with the conclusions and stated that the experience of recent years had clearly demonstrated that there are limits to the extent to which a stable internal equilibrium is attainable by a process of deflation (reduction of costs).

As became known later — the secret having been well kept — the French Government had for some time been discussing with the Governments of the United States and the United Kingdom the arrangements to be made in case of a change in the value of the French franc, and on 25th September 1936, five years and four days after the suspension of the gold standard by Great Britain in 1931, the French Government made known its decision to propose to its Parliament a readjustment of the value of the franc. This announcement was made in a declaration, which will be found in Annex VII together with the simultaneous declarations made by the British and United States Governments, embodying the so-called Tripartite Agreement.

The most important point to retain from these declarations is that the readjustment of the French franc was welcomed by the other two governments;

it was regarded by them not as a setback to collaboration but as a means of establishing more solid foundations for the stability of international economic relations. In conformity with the attitude thus adopted, the governments of the United Kingdom and the United States not only abstained from taking any counter-measures against the action of the French Government, but joined with that government in declaring their intention to continue the use of appropriate available resources so as to avoid as far as possible any disturbance of the basis of international exchange resulting from the proposed readjustment and to arrange for consultations for this purpose whenever necessary. While there was no pooling of resources, it was made clear that efforts would be made to maintain orderly conditions on the exchange markets. Moreover, the three governments emphasised the importance they attached to the development of international trade and especially to action being taken to relax progressively quotas and exchange controls with a view to their abolition. Finally, other countries were invited to co-operate and the hope was expressed that no currency depreciation would be undertaken in order to obtain unreasonable competitive exchange advantages which would hamper the efforts to restore more stable economic relations. In the declarations there is an implied distinction between a currency adjustment likely to produce a more stable basis for international economic relations and the reduction of the exchange value of a currency to such a low point as to be regarded as a measure of competitive exchange depreciation.

On 1st October 1936, six days after the announcement of the Tripartite Agreement, a new monetary law in France relieved the Bank of France of the obligation to redeem its notes in gold and provided for the devaluation of the franc within a margin extending between 25.19 and 34.35 per cent. of the previous parity. The provisions for a margin would appear to have been made in order to enable the French authorities to adapt the value of the franc to the varying needs of the situation. The United States Government is still entitled to alter the gold content of the dollar within a margin of 50 to 60 per cent. of the dollar's previous value and the British authorities retain full freedom with regard to the exchange value of the pound.

At the time of the adjustment of the franc the gold holdings of the Bank of France amounted to 50,218 million francs, which revalued at a rate of depreciation of 25.2 per cent. gave a book profit of about 17,000 million francs. Of this profit about 7,000 million were credited to the accounts of the Treasury and 10,000 million allotted to an exchange equalisation fund, which was established with the task of regulating the relations between the franc and foreign currencies and maintaining the parity of the franc in relation to gold within the limits fixed. The fund also received the amount of gold which, in accordance with the monetary law, was to be surrendered at the previous par rate of the franc by all persons or corporate bodies domiciled in France who owned gold ingots, bars or coins on 26th September 1936. The importation or exportation of gold without the authorisation of the Bank of France was prohibited and the authorisation of the bank was also required for transactions in gold.

Following the publication of the Tripartite Agreement, measures affecting the currency position were also taken in the following countries:

In Switzerland it was announced on 26th September 1936 that the Federal Council had decided to alter the value of the franc and by a decree of the following day the Swiss National Bank was released from the obligation to redeem its notes in gold or gold foreign exchange; on the other hand, it was still obliged to maintain the gold cover of its notes in circulation at the level of at least 40 per cent. It was also required to maintain the gold parity of the franc at a value between 215 and 190 milligrammes of fine gold, i. e. within a margin corresponding to a 25.94 to 34.56 per cent. devaluation from the old parity. By special instructions from the Federal Council the bank was further directed to keep the franc at a level approximately 30 per cent. below the old parity and to earmark in a special account the book profits resulting from the revaluation of its gold holdings at a rate of devaluation of 25.94 per cent. On 26th September 1936 the gold holdings of the Swiss National Bank amounted to 1,537 million, which were revalued to 2,075 million new francs, giving a book profit of 538 million.

In the Netherlands a Royal Decree was issued on 26th September 1936 prohibiting the export of gold coins and gold bullion, and this decree was ratified by the Act of 30th September 1936. By a further Act of the same date an equalisation fund was established for the purpose of influencing foreign exchange rates by buying and selling money transfers, bills and similar paper payable abroad, and gold. The Minister of Finance was authorised to make advances to the fund to a maximum of 300 million guilders and to procure the amounts required for this purpose by the sale of Treasury paper or by borrowing on the security of such paper. While the exchange funds authorised in France and Switzerland were constituted from the profits arising from the revaluation of the gold holdings of the central banks (in accordance with the precedent set by the United States), the fund authorised in the Netherlands obtained its working capital by the issue of Treasury bills (thus following the method adopted in the case of the Exchange Equalisation Account in London). No provision was made in the Netherlands for any margin of devaluation and, while the fund intervened in the market, the exchange rates of the guilder were allowed to fluctuate somewhat under the influence of the movements of funds. In the Dutch East Indies the gold standard was also suspended. The government declared that the parity of the currency with that of the mother country would be maintained.

In Latvia by a decision of the Cabinet Council on 28th September 1936 the lat, which up to that date had been maintained at its par value equal to the Swiss franc, was devalued and attached to sterling at a rate of 25.22 lats to the pound (the rate obtaining before 21st September 1931), the change involving a devaluation of about 40 per cent. At the same time the gold holdings of the Latvijas Banka were revalued on the basis of the average rates quoted on the Riga exchange on 28th and 29th September 1936. The book profits resulting from the revaluation were allotted to an exchange stabilisation fund.

In Italy, by the Royal Decree Law of 5th October 1936, the value of the Italian lira was made equal to 4.677 grammes of fine gold for every 100 lire nominal value, representing a devaluation of 40.94 per cent. (i. e. the same as the devaluation of the U. S. A. dollar) in relation to the previous parity, provision being made in the decree for a possible further devaluation within a margin of 10 per cent. The Banca d'Italia was authorised to revalue its assets in gold and foreign exchange on the basis of the new value of the lira, the surplus resulting from the devaluation being transferred to the State.

In Czechoslovakia a law of 9th October 1936 fixed the value of the Czech crown between 32.21 and 30.21 milligrammes fine gold, this margin representing a devaluation of from 13.3 to 18.7 per cent. in relation to the existing parity, and of from 27.7 to 32.2 per cent. in relation to the old parity of 1929. Within these limits the government was empowered to fix by decree the precise value of the crown in relation to gold, and on the same day the gold content of the crown was fixed at 31.21 milligrammes fine gold, representing a devaluation of 30 per cent. in relation to the 1929 parity. The reserves of gold and foreign exchange held by the National Bank were revalued provisionally on the basis of the upper limit for the value of the crown. The book profits resulting from the revaluation were credited to the State, but the amount was left as a standing deposit at the National Bank to enable the bank to carry out the duty placed upon it of maintaining the exchange value of the crown.

In addition to these more outstanding measures in seven countries, a series of other monetary changes was made following the announcement of the Tripartite Agreement.

In Turkey, on 28th September 1936, the Government adopted sterling instead of the French franc as the basis for the currency. The buying rate was fixed at £T 6.35 and the selling rate at £T 6.38 to the pound sterling, with little change from the rates previously ruling.

In Greece, on 29th September 1936, the Bank of Greece, in agreement with the government, decided to attach the currency to the pound instead of maintaining, as previously, a stable rate in terms of the French franc. The purchase price for sterling was to be fixed, by decision of the Governor of the bank, between a minimum rate of 540 and a maximum of 550 drachmae, and a decision was taken to fix the purchase price at 546 and the selling price at 550 drachmae to the pound (against a rate of about 540 preceding the change).

In the U. S. S. R. a decision was taken to maintain the exchange link with the French franc, but the rate of exchange was altered from 3 francs equal one rouble (as fixed in February 1936) to a rate of 4.25 francs to a rouble.

In Rumania reference was made in a Royal Decree dated 6th November 1936 to an authorisation given to the National Bank on 27th June to pay a premium of 38 per cent. on fine gold, and provision was made for the gold holdings of the bank to be revalued at that rate, the increment resulting from this revaluation to be used in accordance with a convention agreed upon

by the State and the National Bank. After the allocation of various amounts for special reserves and repayments the balance accruing to the State was to be used exclusively to cover exceptional military expenditure.

If comparison be made between the currency changes in the autumn of 1936 and the wave of depreciation which swept over the world in the autumn of 1931, some very marked differences are to be noted. In 1931, when the gold standard was suspended in Great Britain and a number of other countries, the exchange values of the currencies were as a rule left to find their own level in the markets with little or no support from the mostly depleted reserves of the central banks. There followed a period of often violent and highly disturbing fluctuations, which were only gradually brought under control. In 1936, on the other hand, provisions were made in almost every case for the maintenance of the exchange rates at a certain point or within certain limits and special funds were instituted or other steps taken to avoid undue fluctuations.

In order to establish effective co-operation between the monetary authorities in the countries which had joined in the Tripartite Agreement certain technical arrangements were agreed upon to enable the competent bodies in the United States, Great Britain and France to obtain, each of them on the two other markets concerned, gold in exchange for the currency held by them. The Secretary of the U. S. Treasury announced on 13th October 1936 that, subject to twenty-four hours' notice, he would sell gold for immediate export to, or earmark for the account of, the exchange equalisation funds of those countries whose funds likewise were offering to sell gold to the United States, provided such offerings of gold were at such rates and upon such terms and conditions as the Secretary would deem most advantageous to the public interest. The Secretary would announce daily the names of the foreign countries complying with the foregoing conditions — on the same day he named Great Britain and France. Statements were also issued by the British Treasury and the French Ministry of Finance, announcing the day-to-day working arrangements which had been agreed upon.

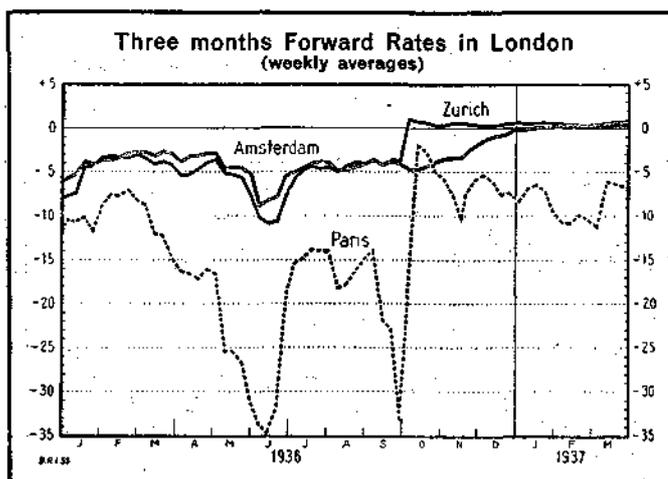
Already on 26th September 1936 the Belgian Government had declared that it adhered to the principles of the Tripartite Agreement, and on 21st November the Swiss and Dutch Governments also announced their adherence to the principles of this agreement. Three days later the Secretary of the U. S. Treasury included Belgium, the Netherlands and Switzerland in the list of countries complying with the conditions for obtaining gold from the U. S. Treasury; the British Treasury and the French Ministry of Finance also made it known that these three countries had become parties to the agreement.

By these various arrangements the monetary authorities in the six countries which have adopted the principles of the Tripartite Agreement extended to one another technical facilities for the changing of their respective currencies into gold. The United States, Belgium and Switzerland have indicated the price in their respective national currencies at which they will for the time being accept and part with gold, while the other countries have not gone so far in fixing a price in advance. The monetary authorities in countries

which have not adhered to the Tripartite Agreement have not the same clearly defined rights to obtain gold against currency. Apart from such arrangements as may be made with regard to individual transactions, gold can be obtained by them only against the belga as the National Bank of Belgium is bound to redeem its notes with gold, which in fact may be exported, and against sterling as gold can be bought at the current price on the London market within the limits of the available supply.

It would contribute to the smooth conduct of international monetary relations if technical facilities similar to those agreed upon by the countries which have adhered to the principles of the Tripartite Agreement were more generally adopted, especially as gold is being used increasingly for the settlement of exchange balances. The present more extensive use of gold is due, in part, to the restricted holdings of foreign currencies in the possession of central banks and exchange funds (outside the sterling area), in part, to the smaller scope afforded to private arbitrage transactions once the exchange markets have become dominated by the intervention of central monetary authorities, and, in part, to a reduction, at least for certain countries, in the total volume of commercial and other credits between one market and another. Technical methods are being developed differing from those which were employed in working the gold and gold exchange standards. The new system may be described as a daily gold settlement system dependent upon the action of the monetary authorities. In the last year the Bank for International Settlements has similarly seen a great increase in the gold transactions it has carried out for the account of its customers, over and above all figures known in the past.

During the year transfers of funds from one market to another have continued on a large scale and the effects of these transfers have again overshadowed the effects of seasonal and similar movements. When, however, spot rates are kept more or less rigidly at the same point, forward rates often give an indication of the direction and strength of a movement of funds. In the past year the quotations on forward exchange markets have largely reflected the distrust felt as to the future value of currencies under pressure.



The discount on the forward market for the French franc reached the high figure of about 35 per cent. (on a yearly basis) in the middle of June and the second half of September 1936.

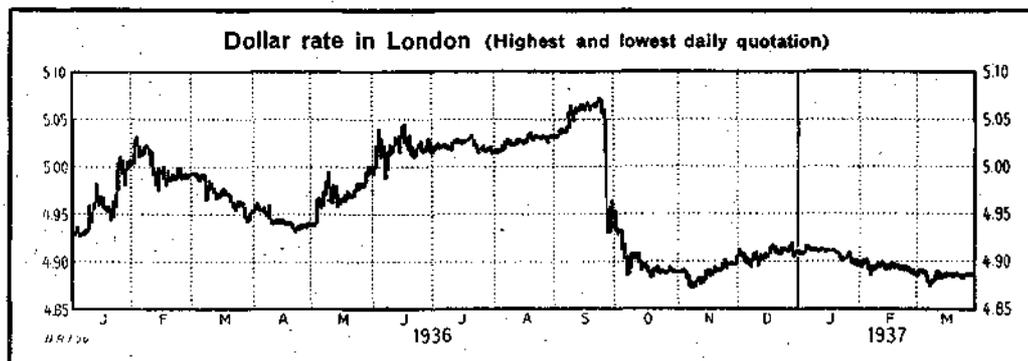
That such high rates have been quoted has been partly due to a restriction of the amounts put at the disposal of the forward markets, the central banks being anxious to limit the

possibilities of exporting capital by means of forward transactions. Naturally such high rates were an obstacle to genuine business and in some instances special facilities were arranged to meet the needs of bona fide trade transactions. The rates for forward French francs have been quoted at a heavy discount also since the devaluation, while the forward rates for the Swiss franc and the guilder have kept within narrow limits. Since the departure from the gold standard spot quotations of the guilder have reflected variations in the movement of funds into the domestic market. In the last quarter of 1936 the exchange value of the guilder in terms of the dollar moved between a maximum and minimum depreciation of 22.67 per cent. on 5th October and 19.54½ per cent. on several days in December.

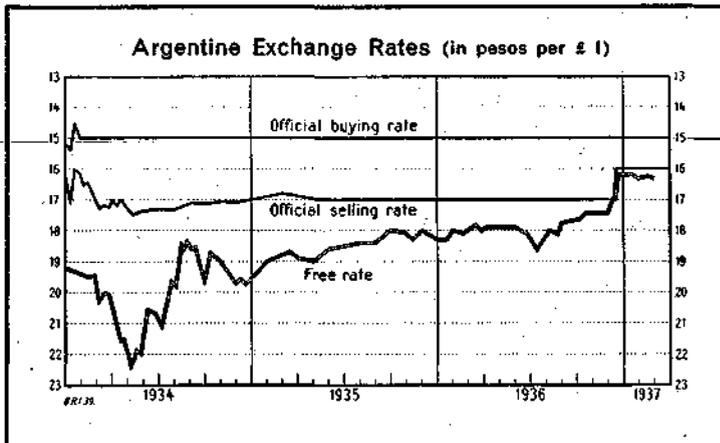
The gold standard having been suspended in France, Switzerland and the Netherlands, there is, apart from Albania, no longer any country free from exchange restrictions which remains on gold at the parity existing before the depression began. Among the countries which apply exchange restrictions, Germany, Poland and Lithuania have not altered the par value of their currencies and in the clearing agreements concluded by these countries the par value is taken as the basis for the accounts. Certain exceptions have been allowed by Germany under special arrangements, mostly with overseas countries, but the field of these exceptions has recently been restricted — particularly by a decree issued in February 1937. The "registered mark", available mainly for tourist purposes, was quoted at a discount varying between 40 and 56 per cent. during 1936. It may be mentioned that in Italy lire are made available to tourists at a price about 10 per cent. below the ordinary rate.

Exchange restrictions were introduced by Poland in the spring of 1936 and in a number of countries, notably Germany, Greece, Hungary and Yugoslavia, which have retained the exchange control already existing, the methods have been perfected and more stringent measures taken to prevent leakages and evasions. On account of the civil war the value of the Spanish peseta has fallen rapidly. A debt moratorium was declared on 2nd August 1936 and great difficulty has been experienced in dealing with the many problems arising from the impossibility of fulfilling contracts and meeting maturing obligations.

The following graph shows the sterling-dollar rate from the beginning of 1936.



There is a difference of 4 per cent. between the highest and the lowest quotation in the period covered by the graph. On 25th September 1936, the sterling rate influenced by the flow of funds from France rose to \$ 5.06, dropping to \$ 4.93 on 28th September and to \$ 4.87 at the beginning of November. Changes in the dollar-sterling rate remained narrow up to April 1937, when somewhat wider movements occurred. Latvia, Greece and Turkey, as mentioned above, have joined the sterling area and in the autumn of 1936 the Uruguayan currency was also linked to sterling. The "free peso" of the Argentine appreciated in



the course of the year, and in December 1936 the official selling rate was lowered from 17.00 to 16.00 pesos per £, the buying rate remaining at 15.00. This change reflects a distinct improvement in the export trade and budget position. South American countries in general have benefited from the rise which

has occurred in prices of raw materials. The Brazilian currency appreciated to the extent of nearly 10 per cent. over the year 1936; on 15th October the currency was attached to the dollar and more normal conditions were established on the exchange market.

Peru and Venezuela remain the only South American countries in which no exchange control is in force, but the restrictions existing in the other countries have in the past year as a rule been eased in their practical application and the transfer of funds has been facilitated. In Chile, it should be mentioned, foreign exchange for the import of products qualified as luxury articles is only available under certain conditions and at a premium of 35 per cent. above the ordinary rate, but otherwise there has in general been a consolidation of foreign exchange rates.

The Japanese currency was adversely affected inter alia by the enhanced prices of raw material imports (since the abandonment of the gold standard in 1931 the development of prices in foreign trade has been unfavourable to Japan — the average price of exports increasing by some 50 per cent., while the prices of imports have more than doubled). The exchange rate, which has been maintained on sterling by the unofficial operations of the Yokohama Specie Bank for four years at 1s.2d., showed signs of weakness towards the end of 1936 and in January 1937 exchange restrictions were imposed largely to prevent heavy semi-speculative imports. There have been no private exports of capital such as those from France but large Japanese investments in Manchukuo and heavy military expenditure have added to the strain caused by the increase in the adverse trade balance from Yen 15 million

in 1935 to Yen 135 million in 1936. It is recognised that the rapidly rising prices in the country would render a further devaluation of the yen particularly dangerous. In January 1937 the rate of 1s.2d. was officially recognised, the Finance Minister announcing that the exchange would remain pegged at this rate and in March and April gold was exported to the United States. The gold reserve of the Bank of Japan amounts to some Yen 1,600 million at present prices, while over 100 million Yen are obtained annually from domestic gold mines. The Manchukuo currency, the yuan, has been maintained at par with the Japanese yen.

Since breaking the link with silver the Chinese dollar has been maintained at a stable value with the result that fluctuations of the rates of exchange in relation to the United States dollar and sterling have been reduced to a minimum. In 1936 the import surplus of merchandise diminished considerably and including the export of silver an active balance was obtained.

Foreign Trade of China in 1936	Merchandise	Silver	Gold	Total
	in millions of C. S. \$			
Exports . . . . .	705.7	254.3	19.1	979.1
Imports . . . . .	941.5	4.7	1.1	947.3
Balance . . .	-235.8	+249.6	+18.0	+ 31.8

Of the C.S. \$254.3 million of silver exports, C.S. \$216.9 million (corresponding to 153 million ounces) were exported to the United States. During the year the Chinese authorities sold large quantities of silver to the U.S. Treasury Department, though the exact amounts and the price paid have not been announced. Against the silver sold, the Chinese authorities obtained United States dollars which were in part converted into gold and the funds thus obtained enabled them to consolidate their monetary position. In May 1936 the Chinese Government announced that it had been decided to maintain an adequate reserve of gold, silver and foreign currencies as cover for the note circulation and that the holdings of silver would represent a minimum of 25 per cent. of the notes outstanding; that further increases would be made in the holdings of gold and foreign currencies; and that silver token coins of a half and a full dollar would be issued. Moreover, restrictions on the artistic and industrial use of silver were abolished. It is expected that by the middle of 1937 the transformation of the Central Bank of China into a central reserve bank will have been completed.

Apart from the Spanish currency which has lost ground, the exchange position has been maintained practically stable since the readjustments in the autumn of 1936. The conclusion of the Tripartite Agreement was a recognition of the fact that no country can alter the external value of its currency without affecting the relative position of other currencies and that the exchange fluctuations of one currency, particularly an important one, are the legitimate concern

of all nations. The Agreement also recognised that the basis for exchange equalisation must be gold and by technical arrangements provided a mechanism for the settlement of balances.

At the meeting of the Board of the Bank for International Settlements on 12th October 1936, a resolution was passed taking note of the various measures adopted and "again drawing attention to the urgent necessity of assuring a general stabilisation of exchange rates". The previous week the Chancellor of the Exchequer had made the following statement:

"... I do not see any reason to alter the view which I have expressed before, that in the end we will probably come back to an international monetary standard on the only basis which appears to give general confidence. Of course, it would be necessary before we did that, to provide security against those violent fluctuations in the value of gold, as expressed in terms of commodities which have occasioned so much disturbance in recent years. If we can do that — and that is a matter for further international co-operation — then I do not see myself any insuperable difficulties in the way of our ultimately arriving again at a currency system based on the free exchange of gold..."

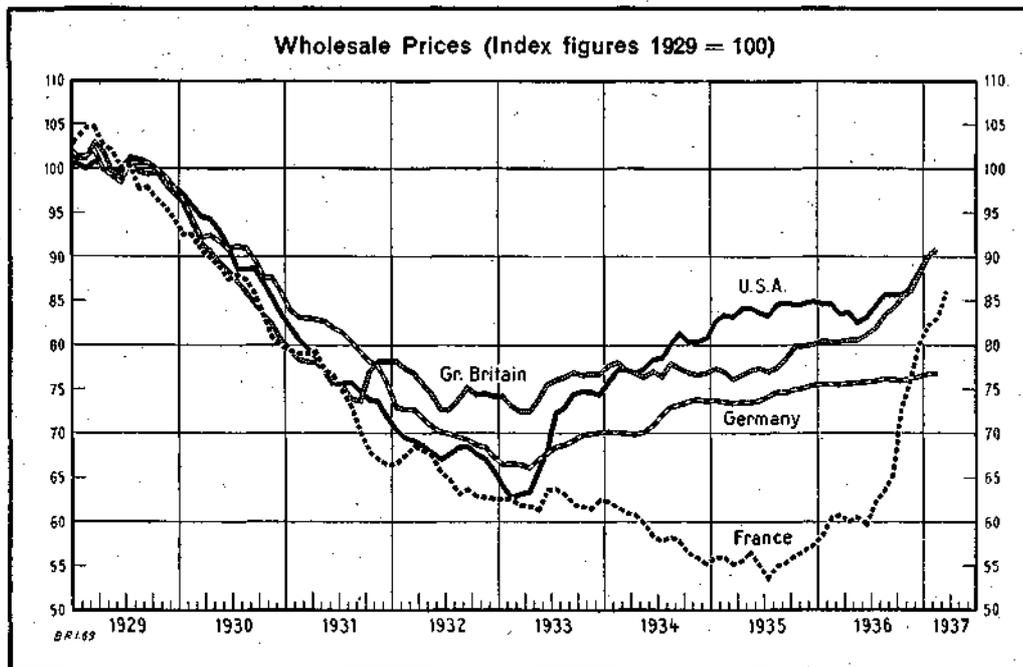
(London, 6th October 1936)

The Swiss National Bank in its annual report for 1936 finds the importance of the Tripartite Agreement to lie particularly in the fact that it created a basis for collaboration in the monetary field. In a declaration on 30th September the President of the Reichsbank explained inter alia that the German Government and the Reichsbank would not add to the uncertainty of the international monetary situation by any change in the value of the Reichsmark. Though the shortcomings of a system of exchange control as practised in Germany were recognised, this system could not be abolished simply by the devaluation of the mark. The German Government would, however, be ready at any time to take part in efficacious international negotiations aiming at greater freedom of international trade and payments on the understood condition, emphasised in the three-power declaration, of the safeguarding of national interests.

While therefore the underlying conditions vary from country to country and there is a diversity in the emphasis laid on different aspects and in the precise interpretation of the measures taken, there is undoubtedly a common desire to construct a monetary basis which will provide the greatest possible equilibrium in the system of international exchange and thus facilitate the development of international trade.

## 2. PRICE MOVEMENTS.

In the year under review the recovery in business has been reflected in the strong upward trend of prices. The following graph shows the movement of wholesale prices in national currencies for four important countries in the period 1929–1937, reduced to the common basis of 1929.



After the marked rise in prices that had occurred in the autumn of 1935 there followed a period of relative stability in the first half of 1936, in which some prices tended even to decline slightly. The turning-point came in the course of the summer. For world trade the development of prices in Great Britain and the United States is of the greatest importance. It will be seen from the graph that in these two countries the upward movement continued with great strength all through the autumn and into 1937. The increase in armaments expenditure led to a spectacular rise in the prices of metals and certain other staple commodities. A more widespread influence was, however, exerted on the price level by the increase in effective demand as revealed by the larger volume of retail sales concurrent with a rise in national incomes and a renewed activity in industries producing capital goods.

In the United States the national income (technically: income paid out) was about \$60,000 million in 1936, according to estimates of the U. S. Department of Commerce, as compared with the low level of \$45,000 million in 1933; and it is reported that distribution of commodities to consumers increased throughout 1936 at a more rapid rate than in any other year of the recovery period. In Great Britain the rise in retail sales from 1935 to 1936 was at the rate of 7 per cent. i. e. at a higher rate than in any year since 1932 (the first year for which statistics of retail sales were collected).

The growth of demand in the wholesale trade at times became very intense, especially as many buyers placed large forward orders partly to anticipate price increases and to be assured of supplies adequate to an increased volume of business. It is particularly noticeable that since 1933 or 1934 there has been a shift of location of stocks from producing to consuming centres. A decline in the visible stocks of raw materials while production of them is

increasing is a sign of industrial activity, but stocks held by manufacturers or wholesale merchants tend to increase when business improves and prices are rising. The position is naturally much healthier when stocks are held voluntarily by manufacturers instead of involuntarily by the original producers. As effective demand has strengthened and stocks have been cleared, higher quotas have as a rule been allowed for the production or export of commodities subject to international schemes of regulation.

Obviously all the factors which influence the trend of economic recovery must be taken into account in appraising the causes of the upward trend of prices. Depreciation of a currency in terms of gold enters among such factors, not only because it may re-establish a better relationship between domestic and foreign prices but also because of its effect on the money markets and the volume of gold production. It is significant that the readjustment of currencies in the autumn of 1936 caused no dent in the world price curve. It came at a time when world prices were rising (and not, as the depreciation of sterling, in the midst of an exceptionally severe depression) and it was generally regarded as restoring monetary equilibrium of a kind likely to facilitate the revival of international trade.

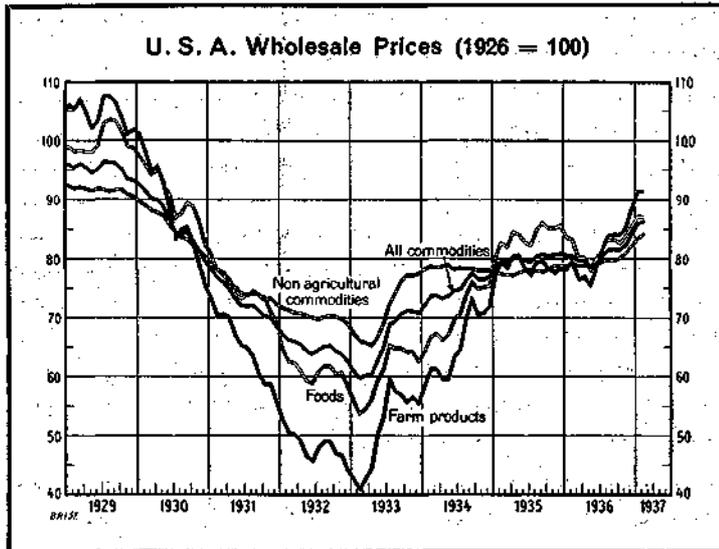
The following table shows the increase in British prices during 1936 in each of the groups into which the Board of Trade index is divided:

Wholesale Prices in Great Britain (averages 1930 = 100)	December 1935	December 1936	% increase in 1936
Cereals . . . . .	91.8	118.1	+28.6
Meat, fish and eggs . . . . .	82.4	85.0	+ 3.2
Other food and tobacco . . . . .	91.0	98.1	+ 7.8
Total food and tobacco . . . . .	88.6	99.3	+12.1
Coal . . . . .	108.1	111.2	+ 2.9
Iron and steel . . . . .	102.1	110.5	+ 8.2
Non-ferrous metals . . . . .	91.7	106.6	+16.2
Cotton . . . . .	88.9	94.5	+ 6.3
Wool . . . . .	97.7	122.7	+25.6
Other textiles . . . . .	74.4	75.5	+ 1.5
Chemicals and oils . . . . .	93.6	97.1	+ 3.7
Miscellaneous . . . . .	87.5	97.4	+11.3
Total industrials and manufactures . . . . .	92.9	101.6	+ 9.4
Total all articles . . . . .	91.5	100.8	+10.2

Besides wool, the largest increases are found in cereals and non-ferrous metals. As regards cereals, the increase is due mainly to a shortage of supply resulting from drought in America and an unusually rainy summer in most importing countries in Europe. Non-ferrous metals have been particularly affected by the demand resulting from armaments. The increase in armaments expenditure has had a distinct effect on prices but this should not be overrated. The increased demand, for instance, in the United States market has on the whole been a more important factor. Something like 40 per cent. of the world production of rubber, copper and several other industrial materials is absorbed by the United States market, and the conditions of business in that country are therefore of paramount importance for the trend of prices.

The following graph shows the price movements of main groups of commodities in the United States since 1929.

Prices for industrial commodities ("non-agricultural commodities" as shown in the graph) began to move upwards in the summer of 1936 after having



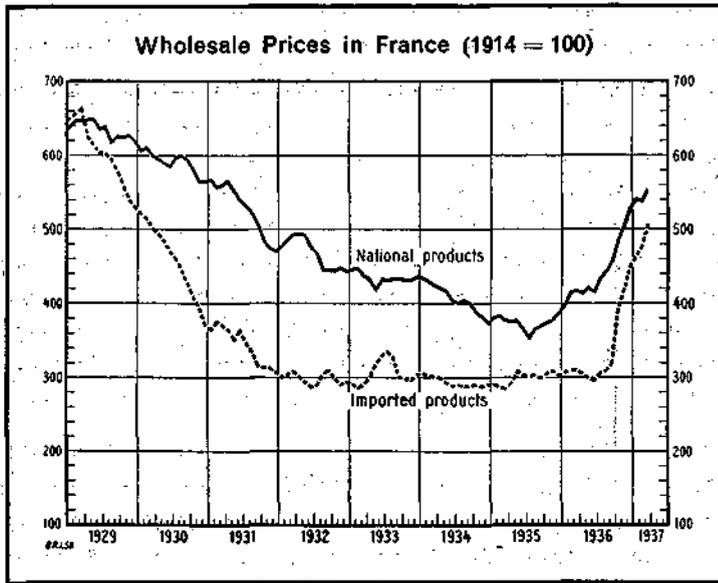
remained practically stable for two and a half years. The recent rise in prices has affected a wide range of goods, raw materials as well as semi-manufactured and finished products.

Among the few commodities which registered a fall in price during 1936, butter shows the most marked decline. This commodity fell by not less than 15 per cent. on

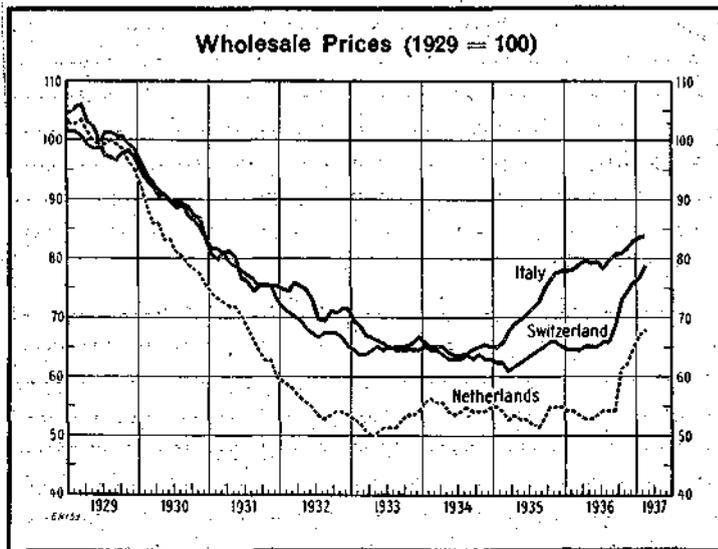
the British market, which is of special importance because it absorbs more than two-thirds of all exported butter. Recently consumption in Great Britain has risen from year to year but the price has nevertheless fallen. In most exporting countries the export of butter has been subsidised in one form or another and production has thus been increased in spite of falling prices. On the other hand, the price of wool rose by about 25 per cent. in 1936, wool being an example of an agricultural product which has been hardly affected at all by artificial assistance to maintain the price during the depression. Australia, which is the country most concerned, is reaping the reward for the drastic policy she pursued in the depression years of selling all wool supplies without the accumulation of stocks to hang over future markets.

The price of cotton stiffened somewhat during the year in response to increasing demand and a certain decline in the United States output as a result of the drought. In 1931/32 and 1935/36 world production was hardly changed at 26¼ million American running bales, but of this total the American production fell from over 60 to slightly under 40 per cent. To a large extent the decline in American production was the result of official planning; in the meantime, however, production in the rest of the world increased by over 60 per cent. and prices improved to the advantage of those countries, such as Brazil and Egypt, which have taken the place of the United States in the world's supply.

Among the countries which adjusted their currencies in the autumn of 1936, France was the one in which the rise of prices was the most important; it was effected not only by devaluation at a time when world prices were rising, but



In Holland and Switzerland the rise in prices since devaluation has been less marked than in France. Italian prices rose rapidly during 1935 but since the devaluation the increase has been relatively moderate.



also by a series of measures, largely of a social character, that raised internal costs of production. The graph shows, separately for imported and national products, the movement in prices from 1929 to date. The price index of national products, which, as may be seen from the graph, rose steeply from the middle of 1935, is strongly affected by the prices of agricultural products.

The adjustment of the lira was accompanied by the prohibition for two years of any rise in rent, water, gas, electric power, rates and transport tariffs, while the emergency duties on raw materials were removed or substantially reduced; since then measures have been taken to control the price movements of all commodities and services. A price commission

has also been appointed in Switzerland and certain increases in prices prohibited. In Germany, Italy, Poland and some other countries increasingly strong measures have been taken to prevent an undue rise in prices. As part of the German Four-Year Plan a price commissioner was appointed with the task not only of controlling costs of living but of supervising the whole national price structure. By decree, price increases if not specially authorised are forbidden, in particular for all requirements of daily life, for the whole agricultural trade and industrial production, transport of goods as well as ser-

vices; the decree also covers any modification in the terms of payment and delivery and any indirect increase in prices by the substitution of inferior materials.

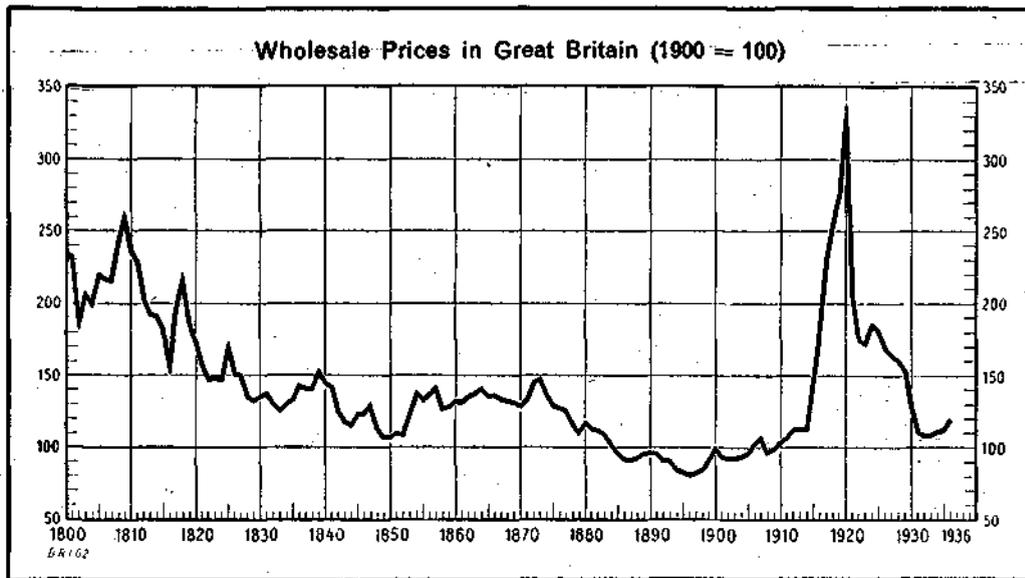
Higher prices and increased demand for raw materials have naturally improved the position of those primary commodity countries which were severely hit by the depression. The remarkable change in economic conditions in the Argentine since the middle of 1936 is directly due to the sharp rise of cereal and linseed prices following the drought and dust-storms in the United States and Canada. The outlook for Brazil and other South American countries is also brighter. The improvement in the primary producing countries should lead to a higher return on the capital invested in them, to the benefit of those countries such as England and the Netherlands which invested large sums in the past and during the depression met with considerable losses.

In a period of recovery the initiative comes from the large industrial countries which are obliged to import larger quantities of raw materials to meet the requirements of expanding industrial production. Such imports are a sign of reviving activity and cannot be taken as an indication of some permanent disequilibrium in the balance of payments. The strengthening of the purchasing power of overseas producers will in due time enable them to expand their imports of manufactured articles.

When conditions are rapidly changing it is not easy to determine whether any given currency ought or ought not to be regarded as overvalued. Indices of wholesale prices certainly cannot be taken as a sufficient measure of the inherent value of the different currencies. Account must also be taken of changes in the cost level and of other elements affecting current balances of payments which do not lend themselves easily to international comparison. It is as a rule easier for a country to attain equilibrium on the foreign account when world prices are rising than when they are falling. The present tendency towards a rise in prices, though most marked in raw materials, is also definitely permeating to the cost of living.

During 1936 the increase in the cost of living in Great Britain was at a rate of nearly 3 per cent.; in the United States slightly less; in the Netherlands, in spite of the devaluation, no increase; in Switzerland an increase of 2 per cent.; in Italy about 6 per cent. and in France still more, the upward movement in the last-mentioned country being influenced by the legislative and other measures which have been taken affecting the cost of production. In Germany and Austria, on the other hand, the index shows hardly any change. In the large majority of countries where the cost of living has gone up the increase began to be more accentuated in the winter months of 1936/37. The movement is thus of recent date and has so far not had very much effect in the direction of a modification of import restrictions and other measures which tend to keep up the cost of living. It has, however, affected the movement of wages in a number of countries and has in general intensified the problems of the labour markets.

The following graph shows the development of wholesale prices in Great Britain from 1800 onwards.



It took thirty years up to the end of the 'forties before the decline in prices following the Napoleonic wars came to an end and the curve turned in an upward direction. It would now seem as if the decline in prices after the Great War had been arrested in half that time and changed into an upward movement. In a world struggling under a large volume of indebtedness some improvement in prices is no doubt desirable, but if the rise be too violent it may lead to a distortion of production and contain the germ of later difficulties. It is natural that some concern should be felt about the strength of recent price developments and that already attention should be directed to the consideration of what measures may eventually have to be taken.

### 3. FOREIGN TRADE.

As compared with the level in 1929, the physical volume of international trade had fallen by 25 per cent. in 1932. Since then there has been a gradual recovery, but the volume of world trade in 1936 was still 14 per cent. below what it was in 1929. A marked improvement occurred in the closing months of 1936 and was continued in 1937. If the countries are arranged according to the percentage improvement during 1936 in imports and exports as returned in their national currencies, the order shown in the next table is obtained.

A substantial improvement occurred in the countries of the Danubian region (Rumania, Bulgaria, Hungary) which benefited from a good harvest in a year when prices of cereals were rising. Among overseas countries the highest percentage increases in exports are found in Indo-China, Manchukuo, the Dutch East Indies, China, Canada, New Zealand, Brazil, Chile and British India. The Dutch East Indies remained on gold at the old par rate up to September 1936, but nevertheless exports increased by nearly 20 per cent., the country benefiting particularly from the rise in the price of rubber. South African exports, consisting mainly of gold, continued the steady rise

Changes from 1935 to 1936 in the foreign trade of different countries.\*

Imports				Exports			
in millions of national currencies							
Country:	1935	1936	% changes	Country:	1935	1936	% changes
U. S. S. R. . . . .	1,067	1,353	+ 28.0	Philippines . . . . .	186	270	+ 45.2
Estonia . . . . .	69	87	+ 26.3	Haiti . . . . .	34	49	+ 42.0
Belgium-Luxemburg	17,112	21,098	+ 23.3	Latvia . . . . .	99	138	+ 39.4
Iran . . . . .	718	878	+ 22.3	Danzig . . . . .	235	325	+ 38.2
New Zealand . . . . .	36	44	+ 21.5	Manchukuo . . . . .	356	474	+ 33.1
Lithuania . . . . .	129	156	+ 21.4	Indo-China . . . . .	1,298	1,682	+ 29.6
France . . . . .	20,974	25,387	+ 21.1	Rumania . . . . .	16,756	19,692	+ 17.5
Latvia . . . . .	101	122	+ 20.8	Morocco . . . . .	621	782	+ 25.9
Finland . . . . .	5,344	6,343	+ 18.7	Lithuania . . . . .	152	191	+ 25.1
U. S. A. . . . .	2,047	2,420	+ 18.2	Belgium-Luxemburg	15,786	19,724	+ 24.9
Chile . . . . .	295	347	+ 17.7	Turkey . . . . .	96	118	+ 22.9
Czechoslovakia . . . . .	6,716	7,888	+ 17.5	China . . . . .	576	706	+ 22.7
Poland . . . . .	861	1,003	+ 16.5	Canada . . . . .	838	1,028	+ 22.6
Canada . . . . .	560	635	+ 15.4	New Zealand . . . . .	47	57	+ 21.9
Union of South Africa	73	84	+ 14.9	Bulgaria . . . . .	3,253	3,910	+ 20.2
Philippines . . . . .	169	192	+ 13.6	Brazil . . . . .	4,104	4,896	+ 19.3
Australia . . . . .	76	86	+ 12.8	Dutch East Indies . . . . .	447	533	+ 19.2
Manchukuo . . . . .	572	644	+ 12.6	Chile . . . . .	465	549	+ 18.2
United Kingdom . . . . .	701	789	+ 12.6	Sweden . . . . .	1,297	1,515	+ 18.8
Denmark . . . . .	1,276	1,431	+ 12.1	Finland . . . . .	6,241	7,215	+ 15.6
Norway . . . . .	816	912	+ 11.8	India . . . . .	1,571	1,805	+ 14.8
Colombia . . . . .	107	119	+ 11.4	Norway . . . . .	598	675	+ 12.9
Japan . . . . .	2,427	2,702	+ 11.3	Australia . . . . .	113	127	+ 12.4
Mexico . . . . .	406	452	+ 11.2	Hungary . . . . .	452	507	+ 12.2
Uruguay . . . . .	60	67	+ 11.2	Irish Free State . . . . .	20	22	+ 12.1
Peru . . . . .	181	201	+ 11.0	Germany . . . . .	4,270	4,768	+ 11.7
Brazil . . . . .	3,856	4,269	+ 10.7	Union of South Africa	100	112	+ 11.6
Greece . . . . .	10,680	11,808	+ 10.6	Switzerland . . . . .	792	881	+ 11.2
Yugoslavia . . . . .	3,603	3,984	+ 10.6	Colombia . . . . .	143	158	+ 10.5
Sweden . . . . .	1,476	1,619	+ 9.7	Poland . . . . .	925	1,026	+ 10.9
Indo-China . . . . .	899	979	+ 8.9	Netherlands . . . . .	675	745	+ 10.4
Netherlands . . . . .	936	1,017	+ 8.6	Portugal . . . . .	924	1,020	+ 10.4
Algeria . . . . .	2,844	3,079	+ 8.3	British Malaya . . . . .	572	630	+ 10.1
British Malaya . . . . .	470	507	+ 7.9	Denmark . . . . .	1,327	1,327	+ 9.3
Hungary . . . . .	402	433	+ 7.7	Peru . . . . .	309	336	+ 8.7
Rumania . . . . .	10,846	11,535	+ 6.3	Yugoslavia . . . . .	4,030	4,376	+ 8.6
Irish Free State . . . . .	37	39	+ 6.3	Czechoslovakia . . . . .	7,396	8,003	+ 8.2
Bulgaria . . . . .	3,009	3,181	+ 5.7	U. S. A. . . . .	2,283	2,455	+ 7.5
Turkey . . . . .	86	93	+ 5.7	Japan . . . . .	2,454	2,631	+ 7.2
Danzig . . . . .	88	93	+ 5.6	Austria . . . . .	895	952	+ 6.4
Haiti . . . . .	38	40	+ 4.7	Ceylon . . . . .	230	244	+ 6.3
Austria . . . . .	1,206	1,247	+ 3.4	Argentina . . . . .	1,568	1,652	+ 5.3
Dutch East Indies . . . . .	275	282	+ 2.8	Italy . . . . .	5,239	5,458	+ 4.2
China . . . . .	919	942	+ 2.4	Estonia . . . . .	80	83	+ 3.8
Germany . . . . .	4,159	4,218	+ 1.4	Greece . . . . .	7,101	7,371	+ 3.8
Morocco . . . . .	1,139	1,151	+ 1.1	Syria . . . . .	1,174	1,217	+ 3.7
Switzerland . . . . .	1,257	1,263	+ 0.5	United Kingdom . . . . .	426	441	+ 3.5
Egypt . . . . .	31	31	- 2.1	Mexico . . . . .	750	773	+ 3.0
Siam . . . . .	105	101	- 3.7	Siam . . . . .	149	151	+ 1.8
Argentina . . . . .	1,175	1,117	- 5.0	Iran . . . . .	1,942	1,960	+ 0.9
Ceylon . . . . .	204	190	- 6.9	France . . . . .	15,496	15,454	- 0.3
India . . . . .	1,343	1,221	- 9.1	Algeria . . . . .	2,613	2,534	- 3.0
Portugal . . . . .	2,295	1,967	- 14.3	Egypt . . . . .	34	33	- 4.2
Syria . . . . .	2,979	2,406	- 19.2	Palestine . . . . .	4	4	- 14.0
Italy . . . . .	7,790	6,002	- 23.0	Uruguay . . . . .	95	81	- 14.9
Palestine . . . . .	18	13	- 23.7	U. S. S. R. . . . .	1,609	1,359	- 15.5
Tunis . . . . .	1,341	925	- 31.0	Tunis . . . . .	873	597	- 31.6

\* Partly provisional figures

of recent years. Imports also increased by 15 per cent. and it is of interest to note that in 1936 South Africa was the most important customer of the United Kingdom, India losing the first place which she had held for many years.

In the countries producing raw materials and foodstuffs, exports with few exceptions have risen more than imports, the improvement in purchasing power not yet having led to larger purchases abroad. Indeed in the case of the Dutch East Indies imports rose only slightly in comparison with the previous year. On the other hand, imports increased more than exports in a number of European countries and particularly in the United Kingdom, France and Czechoslovakia; the rise was due to the larger requirements of raw materials for the expanding industrial production. The United States have increased

not only imports of raw materials but also of semi-manufactured products (wood-pulp, oils, fats, etc.), foodstuffs and finished articles (newsprint, textiles, furs, diamonds, beverages, etc.). In 1936, for the first time in ten years, there was an import surplus during the first half of the year. Exports however rose sharply in the autumn, especially those of finished products and notably those of machinery and other iron and steel products, refined mineral oils, aircraft and textile manufactures. Over the whole year the export surplus amounted to \$ 34 million (the lowest since 1895) as compared with \$ 235 million in 1935.

The expansion of trade of the Belgian-Luxemburg customs union is remarkable, exports having risen by 25 per cent. on the year; to a large extent this rise is due to the increased demand for iron and steel goods.

Germany increased her export surplus from RM 111 million in 1935 to RM 550 million in 1936. This surplus was due entirely to the balance with Europe, that with overseas countries being as usual in deficit. The increase in the export surplus did not result in any improvement in the immediate foreign exchange position of the country, partly because larger amounts were earmarked for current financial charges; an amount of about RM 100 million has been absorbed by the reduction of debts on clearing accounts which at the beginning of the year totalled some RM 500 million. The New Plan instituted in September 1934 has now been in existence for more than 2½ years and, although much transit trade has been lost, Germany has to a large extent succeeded in balancing imports and exports and in reducing accumulated trade debts. In spite of all difficulties, Germany still remains the third most important trading country in the world.

Exchange restrictions and clearing arrangements are still obstructing world trade, though in recent years some technical improvements have been effected which give more scope to ordinary methods of commerce and financing. When clearings are instituted payments are made to exporters in turn through accounts kept in the two countries. If arrears are accumulated an individual exporter must wait until his turn comes for payment and, what is more important, he may not be able to calculate the exact duration of the delay. In such circumstances little or no use can be made of the normal facilities provided by the banking systems and exchange markets and the working capital of the exporter may be tied up in involuntary trade credits; prices are influenced by the uncertainty inherent in the transactions and business is frightened off to the detriment of the general exchange of goods.

In November 1934 a new type of payments agreement was concluded between Germany and Great Britain which eliminated some of the worst disadvantages of the ordinary clearing arrangement. The conclusion of the new agreement was made possible by the German system of foreign trade control, according to which every German importer must obtain a permit for payment in order to be able to obtain foreign exchange. The German authorities are in a position to maintain the volume of imports within such limits as they wish to impose, not only in relation to the outside world as a whole but also in relation to each individual country. In the agreement of 1934, referred to above, it was laid down that Germany's monthly imports from the

United Kingdom should amount to 55 per cent. of the German exports to the United Kingdom two months previously; apart from an amount which at the beginning was earmarked to clear off existing commercial debts, the remaining 45 per cent. is partly used for interest and certain other charges and partly left at the free disposal of Germany. In a later agreement with the Belgian-Luxemburg customs union the contingents were calculated not on the basis of the foreign trade statistics but on the declaration of foreign exchange made by the German exporters, and in other agreements the basis adopted was the amount of actual deliveries of foreign exchange to the Reichsbank.

Similar payments agreements have been concluded with some five countries in all and experience of the working has on the whole been satisfactory. A German importer who has obtained a proper permit of payment is assured that foreign exchange will be available when the date of payment arrives and this enables the parties to the transaction to use the ordinary facilities of the banking system. A foreign firm which sells to Germany must of course carry the ordinary trading risk as far as the standing of the German purchaser is concerned, but he will not have to fear a delay in payment resulting from the difficulty of obtaining foreign exchange against Reichsmarks.

The ordinary clearing arrangements suffer from the grave defect that they tend to destroy direct relations between the buyer and the seller, interposing administrative bodies through which payments are obtained. As a result, the traders lose touch with their markets and are inclined to give less attention to the credit standing of their debtors, relying upon the administrative arrangements which involve more or less extended government action. The great advantage of the "payments agreements" is that direct contact is maintained between buyer and seller and particularly that the seller must look to the buyer for payment. These agreements thus represent a step forward but their working presupposes the institution of a control on foreign trade such as is in force in Germany with all the complications which such control involves. Many proposals have been made in recent years to perfect the system of clearings, for instance by the offsetting of balances between a number of countries and the arrangement of credits to pay off accumulated clearing balances. The more closely these proposals are studied the clearer it becomes that the advantages of the international division of labour and the normal exchange of goods between nations are not compatible with a system which forces trade into defined channels and which, especially for transactions of limited amounts, becomes unduly cumbersome and costly. Clearings may have had their uses in preserving some trade in existence when exchange restrictions were carried to extremes, or in ensuring the reimbursement of accumulated commercial debts or at least part-payment in respect of other debt charges. And the authorisation of so-called private clearings or compensations, constituting a derogation from the clearing principle, may sometimes have introduced an element of flexibility into an otherwise rigid system. But the objective of world trade must be the return to the ordinary methods of commerce and payments, under which all those facilities which have been developed for the benefit of commercial intercourse between nations can once more be fully and profitably utilised.

### III. A YEAR OF MOUNTING GOLD SUPPLIES.

World gold production again reached a new high figure in 1936, registering an increase over 1935 of 4.3 million ounces, which is the largest absolute annual increase ever known. It corresponds to a percentage increase of 13<sup>1</sup>/<sub>2</sub>, which has only been surpassed at times of great new discoveries of gold deposits, i. e. in the 'forties and 'fifties of the last century when gold was found in California and Australia and in the 'nineties after the discovery of the gold fields in the Transvaal. Shipments of gold from India and China, representing dehoarding in the East, still continued in 1936, although at a reduced rate. For the first time since the beginning of the depression not only did hoarding in the western world come to an end but there was in the last quarter of the year a substantial disgorging of gold. Moreover, the consumption of gold in the arts remained at a low figure, taking not more than 5 per cent. of the total gold production. Consequently a very large amount — at least 5,000 million gold francs or £335 million at the present market price of gold in London — was available for monetary purposes. This abundant supply of gold has radically changed the situation which existed in the post-war decade and raises a number of new problems, which are engaging the attention of the monetary authorities to an increasing extent.

#### 1. THE SUPPLY OF GOLD.

The output of gold increased during 1936 in all of the main producing areas, as can be seen from the following table:

Year	South Africa	U. S. S. R.	U. S. A. **	Canada	Other producing countries	World Production	
	in thousands of fine ounces						millions of gold Swiss francs
1915*	9,096	1,546	4,888	918	6,146	22,594	2,420
1923	9,149	438	2,503	1,233	4,463	17,786	1,905
1924	9,575	594	2,529	1,525	4,827	19,050	2,041
1925	9,598	693	2,412	1,736	4,592	19,031	2,039
1926	9,955	895	2,335	1,754	4,430	19,369	2,075
1927	10,122	810	2,197	1,853	4,464	19,446	2,083
1928	10,354	899	2,233	1,891	4,206	19,583	2,098
1929	10,412	1,085	2,208	1,928	4,040	19,673	2,108
1930	10,716	1,434	2,286	2,102	4,184	20,722	2,220
1931	10,878	1,701	2,396	2,694	4,702	22,371	2,397
1932	11,559	1,990	2,449	3,044	5,264	24,306	2,604
1933	11,014	2,667	2,537	2,949	6,336	25,503	2,732
1934	10,480	4,263	2,916	2,972	6,999	27,630	2,960
1935	10,774	5,831	3,619	3,283	7,484	30,991	3,320
1936	11,339	7,350	4,295	3,721	8,549	35,254	3,777

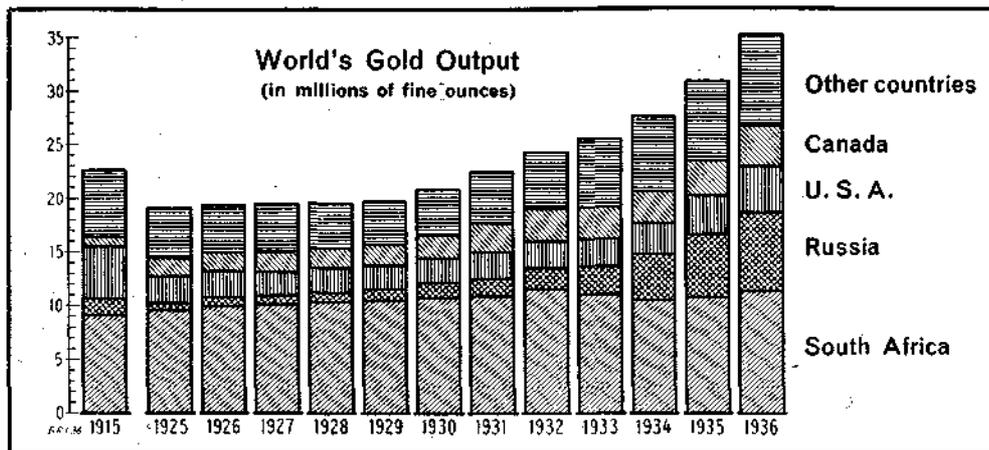
\* Record year before 1932

\*\* Including the Philippines

In order to facilitate comparison with the data given in earlier reports, the monetary value of the gold production, as well as certain other figures in this report, is still given in gold Swiss francs of the old parity. (To convert

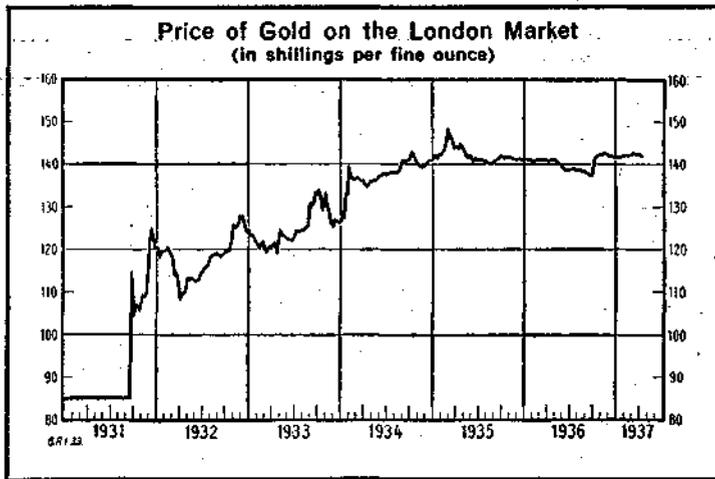
approximately into present-day dollars it is sufficient to divide by three, and to convert into sterling, when the gold price in London stands at around 140 s. per ounce, the amount should be divided by roughly fifteen.)

Nearly a third of the gold produced is obtained from South Africa, a fifth from Russia, a ninth from the United States and a tenth from Canada, other countries together producing the remaining quarter.



The South African producers have continued to exploit lower-grade ores, which at the present level of costs and the higher price obtainable for the metal can be milled profitably. Though the gross tonnage of the ore milled has increased by 9 per cent., there has been a rise of only 5 per cent. in the output of gold, the figure for 1936 being still somewhat lower than that of the record year 1932. The use of lower-grade ores and the extension of milling capacity has necessitated a larger supply of labour and the number of native and coloured workers employed has risen from 213,000 in 1930 to 299,000 in 1935 and 310,000 in 1936.

No great difficulty has as yet been experienced in obtaining either European or native labour, the technical education of the former being supplied by the opening of new schools. Wage rates paid remained practically constant in the years 1929-1935, the average daily wage for European workers in 1929 being 24s.4d., in 1935 24s.10d. and in 1936 25s.1d.; if the native and coloured workers only are considered there has even been a slight tendency to fall. A certain allowance must, however, be made for an increase in other benefits such as, for example, those in respect of paid holidays. In comparison with 1929 there has been a reduction rather than an increase in the cost of machinery and materials needed for production. In these circumstances, the increase from 84s.11½d. to more than 140s. an ounce, or by nearly 70 per cent., in the price obtainable for gold in terms of the local currency and in sterling has naturally resulted in great profits which, however, have been subject to increased taxation. It is only because mining companies have saved their high-grade ores and the seams more easily exploited for the future that the increase in production has kept within such narrow limits. There is every possibility of a further large increase and, to judge from the reports of



the leading mining companies, the foundations have already been laid for a substantial rise in the output in the next few years.

The volume of Russian production is known only approximately, for the Soviet authorities do not publish figures of the total amount of gold produced each year

but only indicate the percentage increase from one year to another. For 1936 the increase is given as having been at the rate of 26 per cent., which, on the basis of previous estimates, leads to a figure of 7.35 million ounces as the amount produced during the year. It seems as if the Five-Year Plan, as far as it concerned the gold-mining industry, had been realised by the end of 1936 with a year to spare. New gold mining centres have been established in recent years in Siberia and Central Asia, some of them with a population of over 25,000. More than 750,000 workmen and 12,000 trained Soviet engineers are reported to be employed in the gold-mining industry.

In the United States also gold production has been rising rapidly, the output in 1936 being 19 per cent. higher than in 1935 and nearly twice as high as in 1929. In Canada too production is rising as a result of new discoveries and exploitation in districts which had previously been inaccessible but are now within reach by air transport. Since 1929 the output has nearly doubled and thus risen at about the same rate as in the United States. The following table sets out for the main producing districts the gold production in 1929 and 1936 and the percentage increase over the period:

Gold production in the principal countries	1929	1936	Percentage increase
	in thousands of fine ounces		
South Africa . . . . .	10,412	11,339	+ 9
U. S. S. R. . . . .	1,085	7,350	+ 577
U. S. A.* . . . . .	2,208	4,295	+ 95
Canada . . . . .	1,928	3,721	+ 93
Australia . . . . .	426	1,199	+ 181
Mexico . . . . .	652	755	+ 16
Japan . . . . .	335	676	+ 102
Rhodesia . . . . .	562	802	+ 43
Other countries . . . . .	2,065	5,117	+ 148
<b>Total</b>	<b>19,673</b>	<b>35,254</b>	<b>+ 79</b>

\* Including the Philippines

Of the world's total output of gold in 1929, 72 per cent. was produced in countries belonging to the British Empire and in 1936 only 53 per cent. by these countries. The fall is due to the reduction in the share of South Africa, whose production in 1929 amounted to 53 per cent. and in 1936 to 32 per cent. of the world production.

In addition to the gold obtained in 1936 from current production, an amount to the value of 437 million gold Swiss francs was shipped from the East, this being a reduction in comparison with the previous year as the following table shows:

Gold from the East	India	China	Hong Kong	Total
	in millions of gold Swiss francs			
1931 . . . . .	477	54	63	594
1932 . . . . .	1,014	118	59	1,191
1933 . . . . .	653	74	100	827
1934 . . . . .	706	54	68	828
1935 . . . . .	495	43	34	572
1936 . . . . .	371	37	29	437
Total	3,716	380	353	4,449

A substantial reduction has again occurred in the shipments from India and shipments from China and Hong Kong have also fallen. The likelihood appears that the outward movement of gold from the East will soon be arrested, if not reversed. The increase in the price of gold in local currencies no longer exercises the same attraction as in the years immediately following the depreciations in 1931 and the improvement in economic conditions is putting an end to so-called distress sales. It is reported from Java that gold coins are beginning to be absorbed again by the natives. It may also be mentioned that after the four-year period during which India's annual absorption of silver averaged merely 10 million ounces, in 1936 the consumption of silver suddenly rose to an amount estimated at 100 million ounces, an indication of a renewed demand for precious metals in the East.

Against the new gold that has become available during the year there should be set off in the first place whatever amount has been required for use in the arts and in industry. It has been estimated that in the period 1920-1929 about 20 per cent. of the annual gold production was taken for such purposes. During the depression there was not only a decline in the absolute amount of gold used industrially and in the arts, but also an increase in the amount of gold recovered by the purchase of old jewels etc. In the United States, for which country fairly complete statistics on this subject exist, the industrial absorption of gold was given at \$14 million and the recovery of old gold at \$62 million in 1934, the corresponding figures for 1935 being \$26 million and \$32 million respectively. With increasing prosperity the industrial use of gold may have risen further and in 1936 it may not have been fully met by recovery of old gold, but the net amount needed is probably still insignificant.

In Great Britain the industrial use of gold is estimated at about £2 million per annum and in recent years this amount has been covered by old gold obtained from the public. In France the industrial use of gold is somewhat greater, being estimated for the last two years at 25,000 kilogrammes, or about 85 million gold Swiss francs; per annum (over and above the needs met by the recovery of old gold). In Germany, consumption of new gold has been estimated for 1936 at about RM30 million. For other countries only incomplete information is available; it is safe to assume however that the net world consumption of gold by industry does not exceed 190 million gold Swiss francs, representing about 5 per cent. of the current gold production. It is possible that in coming years the industrial demand for gold may rise somewhat but it is unlikely that the pre-war figure will be reached again. There seems to have been a distinct change in jewellery fashions for women, in that gold objects are less in favour, being replaced on the one hand by cheap jewellery which can be changed often and, on the other hand, by platinum for more expensive tastes.

	Million gold Swiss francs
To sum up, the amount of gold available in 1936 from new production	3,777
increased by shipments from the East of . . . . .	437
but reduced by the amount absorbed by the arts and industry, namely . . . . .	- 190
thus totalled . . . . .	<u>4,024</u>

These 4,024 million gold Swiss francs correspond to about £ 270 million or \$ 1,300 million. An even larger amount was actually available for monetary purposes in 1936, for more than 1,000 million gold Swiss francs were obtained from dehoarding.

## 2. DEHOARDING OF GOLD.

One of the most curious changes produced by the depression was the simultaneous occurrence of large-scale dehoarding of gold in the East and extensive hoarding in the West. From 1931 to the end of 1936 nearly 4,500 million gold Swiss francs (equal to 42 million ounces) were shipped from India, China and Hong Kong, corresponding to 2¼ years' pre-depression gold production. For many reasons it has been somewhat difficult to obtain exact figures of the amount of gold hoarded in the West since 1931, though sufficient indications have been available to give a general idea of the movement in and out of hoards in these years. For some countries more complete data have recently been procured: for France certain particulars are given in the following table which shows for the period June 1931 to September 1936 the amounts of gold bought from, and sold to, the Bank of France by the French public, and also the amounts imported and exported for account of the public. The figures given in the table have been calculated by deducting from the gold movements at the Bank of France or through the customs all transfers of the metal known to have had a foreign origin or destination (foreign markets, central banks or exchange funds).

Movements of gold to or from the public in France	1931 (June- Dec.)	1932	1933	1934	1935	1936 (Jan.- Sept.)	Total
	in millions of French francs - 1928 parity						
<b>at the Bank of France</b>							
Gold bought from the Bank	858	618	3,477	631	2,243	395	8,222
Gold sold to the Bank . . .	80	443	788	1,035	455	597	3,398
	+ 778	+ 175	+2,689	- 404	+1,788	- 202	+4,824
<b>through the Customs</b>							
Gold imported . . . . .	1,274	2,836	2,412	1,805	1,835	2,379	12,541
Gold exported . . . . .	382	607	2,546	2,638	2,039	1,714	9,926
	+ 892	+2,229	- 134	- 833	- 204	+ 665	+2,615
<b>Balance . . . . .</b>	<b>+1,670</b>	<b>+2,404</b>	<b>+2,555</b>	<b>-1,237</b>	<b>+1,584</b>	<b>+ 463</b>	<b>+7,439</b>

+ signifies increase in the gold holdings of the public; - signifies decrease in the gold holdings of the public.

Internal hoarding of gold in France began in the summer of 1931 and continued until the devaluation in 1936, except for a break in 1934 when not only did the gold holdings of the Bank of France rise by 4,532 million francs but also, as can be seen from the table, the amount of gold hoarded internally was reduced by more than a milliard. For the period June 1931 to September 1936 the net amount of gold acquired by the public from the Bank of France or from imports amounted to 7,439 million francs (of the old parity). This amount, however, includes the gold absorbed by the arts and industry which, for the period under review, is estimated at about 2,000 million francs over and above the recoveries of old gold. There thus remains an amount of about 5,400 million French francs which may be taken as a maximum figure of the gold hoarded in France up to 30th September 1936. It should be added that only negligible amounts of the gold coins issued before the war are still held by the public, and that smuggling of gold across the frontiers can hardly have been of any substantial volume.

During the first nine months of 1936 the amount of gold held by the French public continued to increase, but after the devaluation at the end of September the movement was reversed. It will be recalled that the new monetary law made surrender of gold obligatory, with certain exceptions, for all persons and corporate bodies domiciled in France. From the beginning of October 1936 up to March 1937 private gold sales to the stabilisation fund and declarations by traders and industrialists are valued at nearly 40 per cent. of the estimated gold held privately within France.

During the last period of 1936 an amount of about 150 million gold Swiss francs was obtained from hoards within Switzerland and an amount equivalent to about 100 million gold Swiss francs within the Netherlands. Less precise information is available for other countries; it is known, however, that dehoarding of gold occurred in the London market on a fairly extensive scale during the last quarter of 1936. In its comments on the balance of payments of the United Kingdom for the year 1936, the Board of Trade Journal explains that "it

seems likely from the recorded exports that some part of the gold sent to this country at an earlier date to be held on foreign account was repatriated after the devaluation of the gold-bloc currencies at the end of September". It seems safe to assume that during 1936 in all an amount of at least 1,000 million gold Swiss francs was obtained in Europe from hoards previously accumulated.

The movement out of hoards has continued during the opening months of 1937 reflecting, it may be stated, a change in the attitude of the public towards the holding of assets in the form of gold. More attention is being paid to the fact that gold not only earns no interest but that its hoarding involves the payment of charges for the hire of safe deposits etc.; another consideration is the increased possibilities of making profits on investments at a time of rising quotations on the world's stock exchanges. Moreover, gold is no longer regarded as providing the same measure of safety as it did in the past. Under the legislation passed in the United States in 1934, gold held in the country had to be surrendered to the government and was paid for only at the old par value. In France after the devaluation in 1936 gold held by all persons or corporate bodies domiciled in the country had to be surrendered at the previous par rate of the franc, while holders of foreign exchange, for instance, were subject to no such obligation. Though the full market price was later paid to the French holders of gold, the memory of the original provision remains, and it is not surprising that those who seek protection against monetary risks at present prefer the holding of notes and money on deposit in foreign banks to the hoarding of gold. In this connection, it may be mentioned that during 1936 the note circulation of the Bank of England rose by about £50 million, of which it is estimated that perhaps £25 million were hoarded abroad and, in addition, there has been some hoarding of United States dollar notes in Europe.

### 3. MOVEMENTS OF GOLD TO CENTRAL BANKS AND OTHER MONETARY AUTHORITIES.

The total amount of gold available for monetary purposes in the year 1936 (as a result of current production, shipments from the East and deliveries from hoards in the West, allowance being made for the requirements of the arts and industry) attained a figure of 5,000 million gold Swiss francs. Where has this gold gone?

About 3,300 million gold Swiss francs are accounted for by a net increase in the reported gold holdings of banks of issue and governments, which rose in 1936 from about 69,000 million to 72,300 million gold Swiss francs. This leaves at least 1,700 million gold Swiss francs, which, it may be concluded, have been incorporated in exchange funds and other unreported holdings of monetary authorities. In the absence of published information regarding these funds, it is impossible to indicate in detail the destination of the gold. Relatively little guidance can be obtained from statistics of the gold movements between different countries. Since the currency changes at the end of September 1936, the foreign trade returns of France and the Netherlands have given no

information about exports and imports of gold; and even when trade figures are available the following observation of the Board of Trade in its comments on the balance of payments of the United Kingdom for 1936 must be borne in mind: "with the practice so frequently adopted at the present time of purchasing gold and earmarking it in the country of sale, instead of shipping it immediately to the country to which it belongs, the physical movements of gold do not necessarily coincide in point of time with the operations giving rise to them". There are, however, certain allocations of gold to government exchange funds which have been made known and which throw light on the absorption of gold during the year.

(i) On 2nd October 1936 the gold holdings of the Bank of France amounted to 50,218 million French francs of the old parity, and after revaluation to 67,275 million francs, giving a book profit of 17,057 million francs. Of this profit the Bank of France under various arrangements retained in its gold reserve about 7,000 million; the remaining 10,000 million francs in gold were allocated to the exchange stabilisation fund and, statistically, that amount was thus transferred from the reported gold holdings of the bank to the unreported holdings of the government fund. In October 7,000 million were sold back from the fund to the bank, but at the end of November the bank's holding was reduced by 4,000 million — the balance taken out of the bank being thus 7,000 million, corresponding to somewhat more than 1,000 million gold Swiss francs. It is known that during the last two months of 1936 the French exchange fund utilised part of its holdings for the repayment of the government credit taken up in London in February 1936 and to support the franc, but at the end of the year it still held part of the gold allocated to it.

(ii) When an embargo was placed on the export of gold from the Netherlands at the end of September 1936, no revaluation was made of the gold holdings of the Nederlandsche Bank. Gold to the value of 100 million florins (corresponding to about 210 million gold Swiss francs) however was obtained from the bank against government securities and put at the disposal of the newly-formed exchange equalisation fund. In the last quarter of the year the fund acquired by purchases in various markets an additional amount of gold and the Nederlandsche Bank also increased its gold holdings; the fund retained to the end of the year the 100 million florins transferred to it at the time when it was constituted.

By the end of 1936 the French and Dutch exchange funds thus held gold which had been transferred to them from the holdings of the Bank of France and the Nederlandsche Bank respectively, and the amount of such gold in their possession explains the destination of one part of the 1,700 million gold Swiss francs which, during 1936, went into exchange funds and other unreported holdings of monetary authorities. Apart from these special allocations, however, the aggregate holdings of unreported gold in the hands of the various exchange funds also increased in 1936.

The reported reserves of banks of issue and governments still constitute the overwhelmingly greater part of the monetary gold stocks of the world. To indicate the changes that have taken place in monetary reserves generally,

the table on this page sets out the reported gold stocks of each country at the end of 1934, 1935 and 1936 respectively, the countries being divided into three groups: those in which the reserves fell during 1936 (group 1); those where there was practically no change in the magnitude of the reserves (group 2); and those in which an increase occurred (group 3).

Reported gold reserves of banks of issue and governments	End of 1934	End of 1935	Loss (-) or Gain (+) during 1935	End of 1936	Loss (-) or Gain (+) during 1936
	in millions of gold Swiss francs				
<b>Group 1:</b>					
France . . . . .	16,675	13,455	- 3,220	9,168	- 4,287
Spain . . . . .	2,268	2,255	- 13	1,600 *	- 655
Italy . . . . .	1,585	928	- 759	638	- 188
Czechoslovakia . . . . .	343	344	+ 1	279	- 65
Germany . . . . .	188	192	+ 4	141	- 51
Poland . . . . .	293	258	- 35	228	- 30
South Africa . . . . .	562	649	+ 87	621	- 28
Greece . . . . .	122	104	- 18	78	- 26
Uruguay . . . . .	249	226	- 23	209	- 17
Australia . . . . .	13	13	0	5	- 8
Canada . . . . .	669	578	- 91	575	- 3
Ecuador . . . . .	16	13	- 3	11	- 2
<b>Total</b>	<b>22,993</b>	<b>18,913</b>	<b>- 4,070</b>	<b>13,553</b>	<b>- 5,360</b>
<b>Group 2:</b>					
Albania . . . . .	7	8	+ 1	8	0
Algeria . . . . .	43	43	0	43	0
Argentina . . . . .	1,235	1,235	0	1,235	0
Austria . . . . .	139	140	+ 1	140	0
Belgian Congo . . . . .	9	9	0	9	0
Chile . . . . .	89	90	+ 1	90	0
Denmark . . . . .	185	164	- 21	164	0
Egypt . . . . .	165	165	0	165	0
Estonia . . . . .	34	40	+ 6	40	0
India . . . . .	840	840	0	840	0
Latvia . . . . .	46	46	0	46	0
New Zealand . . . . .	76	71	- 5	71	0
<b>Total</b>	<b>2,868</b>	<b>2,951</b>	<b>- 17</b>	<b>2,851</b>	<b>0</b>
<b>Group 3:</b>					
Portugal . . . . .	208	208	0	209	+ 1
Bulgaria . . . . .	58	60	+ 2	62	+ 2
Morocco . . . . .	22	22	0	24	+ 2
Danzig . . . . .	24	12	- 12	17	+ 5
Hungary . . . . .	71	71	0	76	+ 5
Peru . . . . .	57	58	+ 1	64	+ 6
Colombia . . . . .	59	48	- 11	58	+ 10
Turkey . . . . .	67	72	+ 5	83	+ 11
Rumania . . . . .	319	335	+ 16	350	+ 15
Yugoslavia . . . . .	163	131	- 32	148	+ 17
Dutch East Indies . . . . .	236	167	- 69	185	+ 18
Lithuania . . . . .	27	19	- 8	38	+ 19
Norway . . . . .	187	257	+ 70	299	+ 42
Finland . . . . .	42	62	+ 20	106	+ 44
Belgium . . . . .	1,837	1,957	+ 20	1,934	+ 77
Japan . . . . .	1,205	1,302	+ 97	1,416	+ 114
Netherlands . . . . .	1,754	1,340	- 414	1,499	+ 159
Sweden . . . . .	488	566	+ 78	735	+ 169
Switzerland . . . . .	1,910	1,389	- 521	2,006	+ 617
U.S.S.R. . . . .	2,277	2,569	+ 292	3,535 *	+ 966
United Kingdom . . . . .	4,850	5,046	+ 196	7,911	+ 2,865
U. S. A. . . . .	25,216	30,992	+ 5,776	34,439	+ 3,447
<b>Total</b>	<b>41,077</b>	<b>46,583</b>	<b>+ 5,506</b>	<b>55,194</b>	<b>+ 8,611</b>
<b>Grand total **</b>	<b>67,300</b>	<b>69,000</b>	<b>+ 1,700</b>	<b>72,300</b>	<b>+ 3,300</b>

\* Estimated.      \*\* Partly estimated and including also other countries.

As regards the gold-bloc countries, it is of interest to distinguish between the period before the monetary changes took place, comprising the first nine months of 1936, and the second period extending over the last three months of the year.

Gold Reserves End of month figures in millions	France		Netherlands		Switzerland	
	Gold holdings	Increase(+) / Decrease(-)	Gold holdings	Increase(+) / Decrease(-)	Gold holdings	Increase(+) / Decrease(-)
<b>1936</b>	francs of 0.05895 gr. fine gold		florins of 0.6048 gr. fine gold		francs of 0.2903 gr. fine gold	
January . . . . .	65,223	— 1,041	670.7	+ 27.3	1,388.8	— 0.0
February . . . . .	65,789	+ 566	680.3	+ 9.6	1,445.2	+ 56.3
March . . . . .	63,917	— 1,872	713.6	+ 33.3	1,508.5	+ 63.3
April . . . . .	60,768	— 3,149	710.0	— 3.6	1,516.4	+ 7.8
May . . . . .	57,022	— 3,746	640.2	— 69.8	1,483.5	— 32.9
June . . . . .	54,341	— 2,681	594.2	— 46.0	1,407.0	— 76.5
July . . . . .	54,942	+ 601	651.2	+ 57.0	1,440.6	+ 33.6
August . . . . .	54,511	— 431	682.2	+ 31.0	1,496.7	+ 56.1
September . . . . .	50,111	— 4,400	669.8	— 12.4	1,553.7	+ 57.0
<b>Movement to end September</b>		<b>—16,153</b>		<b>+ 26.4</b>		<b>+164.9</b>
	francs of 0.0441 gr. fine gold		florins of 0.6048 gr. fine gold		francs of 0.215 gr. fine gold	
October . . . . .	64,359		569.9		2,408.4	+310.4
November . . . . .	64,359		569.9		2,581.0	+172.6
December . . . . .	60,359	—4,000	719.6	+149.7	2,709.0	+128.0
<b>Movement in last quarter . .</b>		<b>— 4,000</b>		<b>+149.7*</b>		<b>+611.0*</b>

\* In addition the Exchange Funds acquired gold.

There is this striking difference between the gold movements of the three countries, that during the first nine months of the year the Nederlandsche Bank and the Swiss National Bank both added to their gold holdings, while the Bank of France sustained on balance a very heavy loss, which was only for a relatively small part due to a deficit on the current account of the balance of payments. During 1936 the gold holdings of the Bank of France dropped every month except in February, when the proceeds of the £40 million loan taken up in London by the French Treasury became available, and in July, when there was some repatriation of French funds. This period however was of short duration; in August the current again turned and the loss of gold during the first three and a half weeks of September 1936 was the heaviest ever experienced by the bank.

The immediate result of the devaluation of the French franc in the autumn of 1936 was the liquidation of the large volume of forward engagements, and this in itself caused a return movement of funds to the French market. After a short period in the latter half of October of no distinct movement in either direction, French funds again began to be transferred abroad and this movement continued into the opening months of 1937; in spite of the raising of a credit of £40 million by the French Railways the movement became intense in February and in the first days of March, and the position was only relieved after various measures had been initiated in the second week of that month. These measures included the payment of the full market price for gold and the successful issue of two "tranches" of the National Security Loan made repayable in terms of certain foreign currencies.

In Switzerland the sale of gold from domestic hoards and the return flow of funds from abroad set in immediately upon the devaluation of the

franc. The Swiss National Bank and the exchange fund acquired gold to an amount exceeding 500 million gold Swiss francs in the course of a few months. As the quotations of shares and bonds on the Swiss stock exchanges rose very rapidly immediately after the devaluation, there was very little inducement for foreign capital to invest in Swiss securities and, in fact, few such investments were made. By the end of the year the return flow of Swiss funds was coming to a standstill and at the beginning of 1937 there were even some signs of renewed export of Swiss capital for the purchase of securities in the United States and elsewhere.

In the Netherlands, after the liquidation of some forward engagements in the first half of October 1936, the movement on the exchange market remained for a while without any definite tendency; but soon a demand by foreigners for guilders for the purchase of Dutch securities set in. Gradually the Dutch themselves began to move to the home market funds that had been previously exported, and towards the end of the year and at the beginning of 1937 the return movement became very strong. The amount of gold acquired by the exchange fund has not been made known but the Nederlandsche Bank increased its gold holdings from 669.8 million guilders on 28th September 1936 to 919.5 million at the end of March 1937.

The large amounts of gold which were taken by Switzerland and the Netherlands did not cause any strain on the outside gold markets for, quite apart from any measures taken by the various exchange funds, an abundant supply of gold was available not only from the mounting gold production but also from the outflow from France and the gold coming out of hoards. Even the last quarter of 1936 saw a substantial increase in the gold reserves of Great Britain and the United States.

In order to get a comprehensive idea of the amount of gold which had to be effectively disposed of in 1936, account must be taken not only of the amount of at least 5,000 million gold Swiss francs available from current production, shipments from the East and dehoarding in the West, but also of the amount of gold which came out of the reserves of the Bank of France and of other central banks. In the first nine months of 1936 the Bank of France lost 16,153 million francs of the 1928 parity and in the last three months 4,000 million francs of 0.0441 grammes fine gold were transferred to the exchange fund on the occasion of the repayment of the London credit, altogether making 3,888 million gold Swiss francs. With the gold from other central banks, something like 10,000 million gold Swiss francs was disposed of altogether.

It should be mentioned that the Soviet monetary authorities retained practically the whole of the gold produced in 1936 within the territory of the U. S. S. R. although some important sales abroad were made in the spring of 1937. Of the gold which moved internationally in 1936, the largest acquisitions were made by the Bank of England and the United States Treasury Department; next in order of magnitude come the purchases of the monetary authorities in Switzerland and the Netherlands. The disposal of the gold, as far as information is available, is shown in the following diagram:

Main Gold Movements in 1936 (in millions of gold Swiss francs)	
Origins of Supply	Destination
New Gold 4,024	Bank of England 2,865
Dehoarding 1,000 <i>(estimate)</i>	U.S.A. Treasury 3,447
From Bank of France 3,888	Russian State Bk. 966 <i>(estimate)</i>
	Swiss Nat. Bank 617
From other Central Banks 1,073	Other Central Banks & Exchange Funds 2,090

"New Gold" includes production plus shipments from the East less industrial requirements.  
 "Dehoarding" includes only dehoarding in the West.

The increase in the gold reserves of the Bank of England, valued at £113.6 million at the old parity or about £188 million at the market prices prevailing on the dates when the gold was acquired by the bank, has absorbed the greater part of the country's net import of gold, which valued in sterling at current prices amounted to £228 million. This large import of gold was not due to any surplus on the current account of the balance of payments for, according to the estimates of the Board of Trade there was a debit balance on this account of £19 million. Although in comparison with 1935 there were substantial increases in the sums received in respect of shipping and overseas investments, the import surplus of commodities rose by £73 million (mainly as a result of larger imports of raw materials) and net exports of silver fell by £13 million. It may be added that subscriptions to

new overseas issues on the London market amounted to only £32 million in 1936 and were probably covered more than twice over by the amount received from sinking funds and from repayments at maturity of overseas loans. Such credit balances as may have resulted from these transactions and from profits which have accrued during the year from sales and purchases of foreign securities account, however, for only a part of the net gold imports; these imports have in the main been the result of large-scale capital movements reflecting the increased holding of foreign capital, principally French, in London.

The gold reserves of the United States increased in 1936 by \$1,133 million: \$102 million were obtained from domestic sources and \$1,031 million on balance from abroad. Net imports were in fact \$1,117 million but \$86 million were earmarked for foreign account. For the third consecutive year the net gold imports exceeded \$1,000 million and reflected the general movement of capital funds from foreign centres to the United States. On current account of the balance of payments a passive balance appeared for the first time since before the war. Total trade and service transactions, including interest and dividend items, resulted in a debit balance of \$132 million in 1936 instead of a credit balance of \$208 million in the previous year. The change-over was brought about, on the one hand, by a reduction in the export surplus of merchandise from \$236 million in 1935 to \$34 million in 1936 and, on the other hand, by a net increase in freight and shipping payments, tourist expenditure and immigrants' remittances of \$128 million. Net receipts from dividends and in-

vestments remained unchanged at the figure of \$375 million to the credit of the United States. As a result of continued foreign purchases of American corporate shares and of the higher dividend rates declared in the course of the year, interest and dividend payments to foreign holders of American securities rose by \$54 million, but this increase was offset by an increase in the income from American direct investments abroad.

Net recorded movements of capital to the United States amounted to \$1,141 million as compared with \$1,536 million in 1935; and it is this continued flow of capital which accounts for the large movement of gold to the United States. It is indeed an interesting phenomenon that the two countries which in 1936 were the largest recipients of gold both reported an adverse balance on the current account of their balances of payments in that year.

Reference has already been made to the increase in the reserves of the Swiss National Bank and of the Nederlandsche Bank. Among other central banks which have increased their gold holdings during 1936, the largest additions have been made by the Sveriges Riksbank by about 169 million gold Swiss francs, the result partly of purchases of internal production and partly of imports from abroad. The Bank of Japan increased its gold holdings by 114 million gold Swiss francs as a result of purchases of domestically produced gold and the National Bank of Belgium by 77 million gold Swiss francs. 44 millions were added to the reserves of the Bank of Finland; in 1936, as in the previous year, the bank converted part of the amount accruing from a surplus on the current account of its balance of payments into gold in its monetary reserves. The Bank of Norway was also able to increase its gold holdings — thanks in part to an improvement in the country's balance of payments. And among the Baltic countries the gold holdings of the Lietuvos Bankas were doubled during the year.

The gold holdings of the Banca d'Italia were revalued at the time of the devaluation in the autumn of 1936 and, the book profits having been allocated to the State, amounted at the end of the year to 3,959 million lire as compared with 3,027 million at the end of 1935. In terms of gold, however, there was a diminution over the year amounting to about 188 million gold Swiss francs. The gold holdings of the Reichsbank fell from RM 82.5 million at the end of 1935 to 66.5 million at the end of 1936, the decrease being accounted for mainly by the internal requirements of gold for the arts and industry. The imports and exports of gold during 1936, as returned by the German customs statistics, approximately balanced; at the beginning of 1937 there was, however, an increase in the imports of gold resulting from the conversion into gold of the proceeds of foreign exchange and certain foreign securities surrendered under the new exchange decree.

In the course of the year the gold holdings of the National Bank of Czechoslovakia were reduced by the equivalent of 65 million gold Swiss francs and those of the Bank Polski by 30 million. In Czechoslovakia no important gold movements occurred after the devaluation in the autumn. Finally, it should be mentioned that gold was exported from Spain in connection with the civil war.

In those countries where exchange control has been imposed, outward movements of capital are prohibited except under special authorisation, and a free inflow of capital is, as a rule, excluded in the circumstances. For these countries, therefore, gold movements in the main still reflect changes on the current account of the balances of payments, but the amounts involved are small in comparison with the gold movements which result from international transfers of capital. It should be noted that the funds thus moving have only to a very small extent been obtained by credit operations; they have consisted chiefly of capital effectively owned by the individuals or bodies for whose account the transfer was made.

#### 4. ABUNDANT GOLD SUPPLY IN THE MONETARY SYSTEM.

The large movements of gold in recent years have given rise to a series of problems which have engaged the attention of the authorities in the various monetary centres. In addition to the task of preventing undue fluctuations in exchange rates, account has to be taken of the influence that an influx or efflux of gold may have on the internal currency and credit conditions in the countries affected. If the influx of gold into a market is the result of a movement of funds liable to be withdrawn again at any time, it may be dangerous for the central bank in the market receiving the funds to acquire the gold without any offsetting operation; for such acquisitions would lead to an increase in the credit base without any guarantee that the increase could be permanently maintained.

Considerations of this kind have largely determined the working of the British Exchange Equalisation Account, and it is interesting to note that the underlying idea of the policy of offsetting temporary movements of funds from one market to another was suggested by the Macmillan Committee in paragraph 355 (pp. 151 and 152) of the report published in the summer of 1931. Since that time the further question has arisen whether such acquisitions of gold as are not the counterpart to more or less temporary movements of funds should be allowed to raise the reserve balances of the commercial banks to a level which, especially during an upward trend in the business cycle, might be considered undesirable or whether measures should be taken to neutralise as far as possible the effects of such acquisitions.

In Great Britain the establishment of the Exchange Equalisation Account in the spring of 1932 provided for the funds (mainly in the form of Treasury bills) required for intervention on the exchange market and, at the same time, for the regulation of the internal credit position. When the Account intervenes in the case of an inflow of funds the sale of the Treasury bills acts as an offsetting operation, preventing the inflow from increasing the cash balances of the joint stock banks at the Bank of England; when funds flow from the London market the Exchange Equalisation Account effects an offsetting movement by acting in the opposite way, namely, selling foreign exchange or gold and purchasing Treasury bills. An addition to the gold holdings of the Account does not, therefore, lead to an increase in bankers' balances.

To provide for more notes in circulation or an increase in bankers' balances, the Bank of England may take over part of the gold without a counteracting sale of securities, or purchase securities on its own initiative.

The technique of offsetting has gradually been adapted to allow for different kinds of movements of credit and currency. If the funds coming to the London market are put into bank deposits and thus cause an increase in the total volume of these deposits, the amount of bankers' cash (their coin, notes and balances at the Bank of England) must be allowed to increase by about a tenth of the amount of the new deposits if it is desired to avoid a tightening of the banks' ratios (traditionally kept at the rate of about a tenth of total deposits). If, on the other hand, there is an increased demand for notes, the clearing banks will have to draw on their balances at the Bank of England in order to procure the notes to be paid out. To offset, in this case, the resulting reduction in the banks' "cash", the Bank of England must take steps to restore the balances of the banks up to the full amount of the increase in the note circulation. In the course of 1936 the note circulation increased by roughly £50 million and the Bank of England provided for the increase by an addition to its gold holdings. There was, however, a further increase of £65 million in the gold holdings of the Bank of England in December 1936; in this case the object was to take over gold from the Exchange Equalisation Account (to render the Account more liquid) without causing a corresponding alteration in the credit base of the market. The gold was acquired by the Bank of England mainly against securities in a way that did not affect the balances of the joint stock banks. Simultaneously the fiduciary note issue (i. e. the amount of notes which may be issued by the Bank of England over and above its gold holdings) was reduced from £260 to £200 million.

In the United States the Exchange Stabilisation Fund, established at the beginning of 1934, bought gold for account of the Treasury and paid for it with funds obtained at the Federal Reserve banks against gold certificates, but it was not part of the Fund's task to undertake any offsetting open-market operations. Consequently, the inflow of gold, which amounted to approximately \$4,000 million from the beginning of 1934 to the end of 1936, had the effect of adding an equivalent amount to the reserve balances of the member banks as well as to the deposits held with them. In this way reserve balances were built up far in excess of the statutory requirements; at the beginning of 1936 the excess reserves amounted to \$3,000 million (see graph on p. 76).

It was feared that this increase in the credit base would lead to a dangerous expansion in the supply of money in the form of bank credit and, in order to counteract such a potential expansion, the Board of Governors of the Federal Reserve System decided to increase the reserve requirements for member banks. In July 1936 these requirements were increased by 50 per cent. and in January 1937 a further 50 per cent. increase of the original amount was ordered; the reserve requirements of the member banks have thereby been fixed at the highest rates allowed under the law. It was estimated in January 1937 that from 1st May, when the increases become fully effective,

the excess reserves of member banks will have been reduced to approximately \$500 million which, in the opinion of the Board of Governors, is considered to be "an amount ample to finance further recovery and to maintain easy money conditions".

Another measure to counteract the effects of additions to the gold holdings was adopted in December 1936. On the 21st of that month the Secretary of the Treasury announced that the Treasury would take appropriate action with respect to net acquisitions or releases of gold "by the sale of additional public debt obligations, the proceeds of which will be used for the purchase of gold, and by the purchase or redemption of outstanding obligations in the case of movements in the reverse direction". It was explained in the *Federal Reserve Bulletin* of January 1937 that, in so far as such action is taken, effects on reserves of additions to the gold supply, either from imports or from new production, will be offset by the sale to the public of an equivalent amount of United States Government obligations and by the setting aside of the purchased gold in an "inactive account" in the Treasury. An outward movement of gold will be similarly offset by the purchase or redemption of United States obligations in the market, thus restoring to it the funds lost through the export of gold. To this extent, therefore, the volume of member bank reserves will be neither increased nor decreased by changes in the supply of gold. By the end of April 1937, the amount of so-called "inactive gold" held by the Treasury and purchased out of ordinary Treasury resources since the measure was introduced in December 1936 amounted to over \$500 million.

In other countries also steps have been taken to offset the effects of large increases in the gold holdings. In the Argentine the Central Bank continued to sell during 1936 government securities out of its own holdings to the commercial banks; with the exhaustion of the Central Bank's own securities, the government created Treasury bills to absorb the incoming gold under a plan similar to that described above for the United States. In New Zealand powers have been given to the Reserve Bank to increase the minimum cash requirements of the commercial banks. In several other countries similar measures are being discussed and proposals framed to enable the monetary authorities either to tighten cash requirements or to intervene on the markets by the sale of securities. The measures thus taken or envisaged in different countries indicate the growing preoccupation with problems arising from an abundant supply and massive movements of gold. A policy of "sterilising gold" is being widely adopted and the question arises to what extent the measures involved will adequately neutralise the effects which an increased monetary supply of gold would normally exert. Considering the variety of circumstances that may occur, only a few typical and simplified cases can be considered to emphasize some of the more important points.

Suppose that gold is moved from one market to another, not to fill a gap in the current balance of payments but as a means of effecting the transfer of capital funds. Against the gold an equivalent amount of deposits is obtained with commercial banks of the recipient country and, if the central bank acquires the gold without any offsetting operation, the

reserve balances of the commercial banks are also increased by a similar amount. Now, if the central bank sells securities to the amount of the gold acquired, the increase made in the reserve balances of the commercial banks will be wiped out. What happens to the deposits with the commercial banks will depend upon whether these banks or the outside market buy the securities. It is important to stress that the funds which were transferred from abroad were of a capital nature and, therefore, presumably will not be spent on the purchase of commodities but, if no longer kept on deposit, will be used for the acquisition of capital assets. As, however, the financial market has been provided with an increased amount of securities by the action of the central bank, a balance is brought about between the demand for, and the supply of, capital assets on the market. In individual cases there may be variations in that funds may move into the stock market or be otherwise invested instead of going into the market for government securities, but on the whole it may be assumed that the inflow of funds and gold has been more or less offset in the way described. It is necessary, however, that the money received in payment for the securities sold by the central bank should remain unspent, and the interest on these securities will, therefore, be a net burden on the central bank or the government, as the case may be. No essential change is produced by the substitution of an exchange fund for the central bank as the body performing the offsetting operations. It is simply necessary that a sufficient amount of government securities should be available for intervention on the market, and the establishment of an exchange fund may have been the method chosen (as in London) to provide these securities.

A more difficult problem arises when the gold is derived from current production. The first result of an acquisition of such gold is of course, as in the previous case, to produce an increase in the deposits with commercial banks and an increase in the banks' reserve balances at the central bank. It is also true that a sale of securities by the central bank to the amount of the gold acquired reduces the balances of the commercial banks with the central bank and in that way a multiple expansion of credit within the monetary system is avoided. But what happens to the deposits which were obtained in the commercial banks? These deposits in the hands of the gold producers are not a form of capital assets but must in the main be expended by them for the payment of wages, materials, taxes and dividends. The result is an additional demand for commodities based on an expansion of monetary purchasing power. Such an expansion may be desirable to counterbalance an increased production of goods, but if the expansion should be too great, the question arises how the increase in the volume of purchasing power can be offset. There would have to be, in some way, a restriction in the volume already existing corresponding to the amount obtained by the gold producers, as long as they can sell their gold within the monetary system. A restriction of the kind required would be produced if the amounts needed to acquire the gold were raised by taxation or through loans raised from effective savings. In the case of securities being sold by the central bank to neutralise the gold acquisitions, these securities must absorb part of current savings in order to prevent not only an enlargement of the credit base but also an increase

in the volume of purchasing power directed towards the purchase of commodities. Even then, in order to make the intervention effective, the absorption of savings to provide funds for the acquisition of the new gold may have to be carried to the point at which it stiffens interest rates. In so far as credit measures are adopted to neutralise the effects of a too abundant gold production, it may thus be asked whether it is possible to continue for long the application of a cheap money policy.

In practice it may be difficult to follow the effects of the newly-mined gold as it moves from the producers to the various monetary centres, but the tendency that such gold has to increase the demand for commodities cannot be doubted.

In 1936 the amount of gold that moved internationally was exceptionally large for, in addition to the mounting gold production, gold continued to be shipped from the East and was dehoarded in the West. Moreover, an amount fully as large as the year's production came out of the reserves of the Bank of France. Obviously, some of these supplies will prove to be only temporary: the shipments from the East were smaller than in previous years and may soon be reversed; dehoarding in the West, which began after the devaluation of the gold-bloc currencies, has already accounted for a fair portion of the accumulated hoards; and the improvement in the economic and financial position of France has had a moderating effect on the outflow of gold from that country. There remains the current gold production. In the year 1936 the world's output of gold was in ounces nearly 80 per cent. above the average annual output in the period 1924/29. In this period, at the gold price in London of 84s. 11½d. an ounce, the annual output had a value of about £80 million, of which about £50 million were available for monetary purposes; and in 1936, at a gold price of about 140s. an ounce, the value of the output had risen to £245 million, the whole being available for monetary purposes. All the indications from the producing countries point to a continued rise in output: in South Africa the work of development is just beginning to make itself felt; in the U.S.S.R. gold production is still mounting and exports were resumed in March and April 1937; in Canada, official reports predict a further large increase; only in the United States would the output seem to have reached, if not its maximum, at least a level which is unlikely to be greatly exceeded. It has been forecast that before long the world's gold production may be at the rate of 40 million ounces per annum, or more than twice as high as in 1929.

The recent extension of production has been based on present price and cost conditions, and it may be questioned whether an increase in costs, itself an effect of the larger supply of gold, may not be expected to exert a restraining influence on future production. This presupposes, it should be noted, that the measures for sterilising gold at present applied do not succeed in preventing the increased supply from raising the level of costs and prices. Let it be assumed, however, that costs and commodity prices reach a level approximating to that obtaining in the years 1926/29; at \$35 or 140s. an ounce, the price of gold would still be nearly 70 per cent. higher than it was in those years. The Union Corporation in its report for 1936 states that "weighted by the population of the various countries, the average price for gold throughout

the world is now some 85 per cent. above the average price for 1929'. In these circumstances, there is not much prospect for a number of years to come that a rise in costs and prices will really exert a restraining influence on gold production.

Turning to the demand for gold, it seems likely that countries in the East will soon begin to hoard the metal again. In the period 1926/29 the gold demand from the East amounted to something like £15 million a year, and may be a somewhat higher demand can be expected as prosperity returns. Moreover, the adoption of gold as part of the monetary reserves of China may provide a new outlet for gold in the East. The gold that goes into the eastern hoards has, however, as a rule to be acquired out of current savings and a surplus in the balance of payments, and the amounts which will be absorbed cannot be very large.

An exceptional demand for gold may come from countries in which present monetary reserves are deficient. In the absence of foreign lending, however, the replenishment of these reserves will most likely only be undertaken gradually. As far as France is concerned, a return flow of capital will no doubt be accompanied by a large movement of gold, but this movement will essentially be a redistribution of existing supplies, being a reversal of a previous outflow. At a time when current gold production is at the rate of £245 million a year, the influence of even a substantial return movement of funds will hardly produce more than a temporary alleviation.

It should also be mentioned that the demand for gold in the arts and industry, which previously absorbed as much as 20 per cent. of the yearly production, at present absorbs less than 5 per cent. of the current output.

In these circumstances the countries that already possess large monetary reserves will presumably continue to be faced with the task of absorbing large and increasing amounts of new gold; and a continuation of the policy of sterilisation will involve them in ever-increasing expenses. It is not surprising that the problems that have thus arisen are being seriously considered and that alternative solutions are being put forward. For instance, the suggestion has been made that gold production should be controlled and reduced; but the adoption of such a measure, which deserves further consideration, has become more difficult in recent years owing to the increase in the number of producing centres. It has also been suggested that gold coins should again be put into circulation. In some countries it might be possible to do so, but experience shows that, once the public has lost the habit of carrying gold coins, it is difficult to re-introduce them into active circulation. And even if it were possible, it would not solve the whole problem. There would certainly be no increase in the commercial banks' balances at the central bank so long as the gold went into circulation, but the new coins when not hoarded might also constitute an addition to the existing volume of purchasing power, while gold production would not be reduced. It is pertinent to remember that in the years before the war, when gold was effectively in circulation to an extent that it would be difficult to attain again, the increase in the South African gold production brought about an appreciable rise in prices.

It has also been suggested that the price paid per ounce of gold should be lowered from the high figures to which it has risen in terms of depreciated currencies; in that way the amount of monetary purchasing power produced by a given weight of gold would be reduced, and a restraining influence would also be exerted on the output of gold, for gold mining would become less profitable. It can hardly be doubted that at present a lowering of the price of gold would help to cope with the serious problems resulting from the overabundant production. It would, however, cause certain difficulties with regard to valuation of existing gold reserves and the relative position of currencies (the latter, in so far as equilibrium has already been attained, should be disturbed as little as possible). It would, moreover, involve the danger of manipulation of currencies in the future, which would add an element of instability and distrust to the monetary structure.

In the discussion of a reconstruction of the world's monetary system these various questions, difficult though they may be, cannot be avoided. Also from the point of view of the gold producers, it is important to establish conditions that will render gold continuously useful as a basis for currencies, instead of concentrating attention on immediate profits.

#### IV. CAPITAL MOVEMENTS AND INTERNATIONAL SHORT-TERM INDEBTEDNESS.

Large movements of capital between creditor countries continued to dominate the exchange markets in 1936 as in the two previous years. The flow of funds effected through transfers of gold to England, the Netherlands, Switzerland and particularly the United States, has become an embarrassment and the possible effects of these large movements is a subject for serious consideration. Foreign investment for the initiation of new enterprises is still at a low ebb, in fact, debtor countries whose exchange conditions have improved are repaying old loans and credits, particularly to England and the United States. There are, however, signs of direct private investment in such countries as the Argentine and Australia, which have been able to carry out their obligations during the depression. Short-term foreign-owned balances have continued to accumulate in London and New York, while short-term credits previously obtained from abroad by countries where exchange restrictions are in force, as well as other blocked and frozen debts, continue to be slowly and painfully liquidated. The countries making these liquidations have in general insufficient external resources, while those receiving the funds are concerned about the growth of their monetary reserves.

The most important movement has been in the direction of the United States, and it can be followed, as in the case of no other country, with a large degree of accuracy — thanks to the statistical information made available by the U. S. Department of Commerce and recently also by the U. S. Treasury.

Before the war the foreign holding of American securities was estimated at about \$5,000 million and, as foreign securities held in the United States were negligible, this figure represented roughly the net debtor position. During the war about half of these American investments were sold back and the world borrowed in the United States, which became a strong creditor country and in the 'twenties the biggest lender to foreign countries. To a certain extent, however, foreigners again built up a substantial holding of American investments. In 1931 American lending on long and short-term account ceased but foreigners drew heavily on their accumulated short-term dollar assets and on balance the outflow of capital from the United States continued during 1931/33, accompanied at times by an efflux of gold and augmented during the latter year by a flight of American funds from the depreciating dollar.

After the fixing of the new value of the dollar at the end of January 1934 at the rate of \$35 an ounce of gold, compared with the old price of \$20.67, a violent change occurred in the trend of capital movements: the United States became overnight the biggest capital-importing country in the world. In the three years 1934/36 the import of capital amounted to \$4,000 million, corresponding almost exactly to the import of gold over the same period (the active balance on current account of the balance of payments being well covered by silver imports from abroad). This global figure includes a number of diverse movements: American flight-capital returned, credits from American banks to foreign countries were withdrawn, foreigners repurchased and

redeemed issues previously made in New York and bought American securities, and also increased their short-term assets in the United States.

Of the \$4,000 million capital flow some three-quarters are "recorded" in the annual statistics on the balance of payments published by the U. S. Department of Commerce, while the remainder appears only in a "residual item", which must also be taken to include a certain allowance for the balance of errors and omissions on current account. On the basis of these data, as well as from information recently issued by the U. S. Treasury Department, the following table has been made showing the composition of the capital influx for the years 1934/36:

Net Capital Influx to U. S. A.	recorded			"residual"*	Grand Total	Gold Imports (net)
	long-term	short-term	total			
in millions of dollars						
1934	194	192	386	482	868	1,132
1935	442	969	1,411	455	1,866	1,739
1936	792	403	1,195	146	1,341	1,117
<b>Totals</b>	<b>1,428</b>	<b>1,564</b>	<b>2,992</b>	<b>1,083</b>	<b>4,075</b>	<b>3,988</b>

\* Including, for convenience of presentation, some recorded miscellaneous items (which explains the difference in the totals of the recorded movements compared with those given on page 49).

The movement was at its strongest in 1935 when the influx of short-term capital was greatest; it continued, however, on a large scale in the following year with a preponderance of long-term transactions.

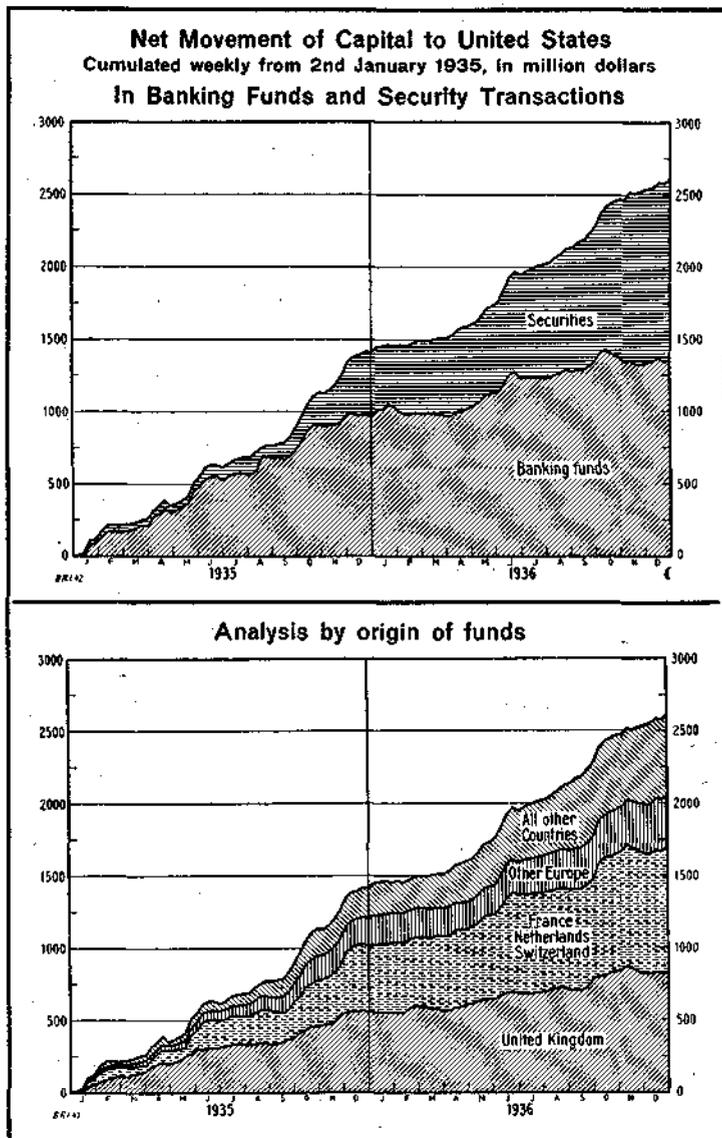
Of the net recorded influx of short-term capital amounting in the three years to about \$1,560 million, withdrawals by American banks from abroad account for \$560 million, of which nearly half represents the gradual liquidation of frozen claims on European and Latin American countries. Foreigners (i. e. persons and institutions domiciled abroad) increased their balances and other short-term claims in the United States by \$1,000 million, the total amount accumulated at the end of 1936 being \$1,500 million, i. e. about three times as much as at the end of 1933 but only half the volume of corresponding assets in 1929. When, however, comparison is made with the position seven or eight years ago, it must be remembered that central banks then possessed much larger dollar holdings than at present, and also that recent figures are somewhat more comprehensive than in previous years. At the end of September 1936 the principal holders of short-term assets in the United States were as follows:

	\$ millions
United Kingdom . . . . .	300
France . . . . .	172
Netherlands . . . . .	81
Switzerland . . . . .	154
Canada . . . . .	174
Latin America . . . . .	203
Far East . . . . .	211
All other . . . . .	201
<b>Total</b>	<b>1,496</b>

There was little decline of the balances of France, the Netherlands and Switzerland after September 1936, but some reflux of British balances took place, accompanied by a reduction of the discount on forward sterling and some stiffening of interest rates in London. British banking funds employed in New York, as well as American balances in London, are very sensitive to movements of short-term interest rates and the forward dollar-sterling exchange rate.

Some of the short-term assets held by foreigners in the United States may be "refugee" funds and the fact that the building-up of funds, on account of England and the old gold-bloc countries, took place at irregular intervals during periods of political and monetary uncertainty in Europe may suggest possible instability in the future. But the fact must not be overlooked that a very substantial part of these funds and the funds of other countries which have built up balances in a regular manner represents an accumulation of working balances customarily employed in foreign markets. "With an improvement in world trade, it is not improbable that the working balances which would be kept here will increase markedly", wrote the Secretary of the U.S. Treasury in an open letter in September 1936; this is particularly true at the present time when so many countries are forced to finance their own foreign trade instead of being able to obtain dollar credits.

The recorded net purchases of securities by foreigners over the three years



amount to \$1,430 million, but of this \$535 million, or more than a third, represented net purchases and redemptions of foreign securities and may thus be regarded as a movement of a permanent character. As regards purchases of American securities by foreigners, aggregating \$895 million, the movement did not get under way until May 1935 and on the whole has tended to gain in force since then. The Federal Reserve Bulletin for July 1936 makes the observation that "the purchase of American securities by foreigners since May 1935 appears to reflect conditions in the United States more than conditions in Europe" and that "the sustained character of the movement at times when European balances were

not increasing, or were being reduced, as in the five months ending April 1936, suggests that foreign investors believe the American market offers an opportunity for profitable investment of their funds". Similarly, after the currency changes of September 1936, purchases of American securities continued as actively as ever.

The total of foreign investments in the United States was not known with any certainty until the U. S. Department of Commerce published the results of a detailed enquiry, which gave the following picture for the end of 1935:

Total of foreign Investments in the United States	Great Britain	Gold* bloc	Canada	Other Countries	Total
	in millions of dollars				
Common stocks (market value)	372	552	408	683	2,015
Preferred stocks (par value)	146	64	66	53	329
Bonds (par value)	91	338	49	129	607
Direct investments	362	276	322	85	1,045
Other investments	403	235	161	240	1,039
<b>Total</b>	<b>1,374</b>	<b>1,465</b>	<b>1,006</b>	<b>1,190</b>	<b>5,035</b>

\* France, Netherlands and Switzerland.

"Although securities may have changed hands and market values fluctuated, foreigners have maintained in this country throughout the depression a volume of securities substantially as great as the amount now held", observes the Federal Reserve Bulletin, adding, "not more than 10 per cent. of the \$5,000 million of long-term assets shown in the table as held by foreigners at the end of 1935 appears to have been acquired since 1933". The purchase of \$600 million American securities by foreigners in 1936, together with the rise of market values, is estimated to have increased the foreign holding of American investments at the end of 1936 to about \$6,250 million. Many of these investments may not be disturbed for years, if past experience is any guide. "There appear to have been no sustained foreign withdrawals from the American security markets even during the early years of the depression when confidence was at a low ebb and prices were declining sharply", says the Federal Reserve Bulletin. Although naturally an influx of capital continuing for more than three years at an average rate of over \$100 million a month must be a cause of preoccupation, it seems unlikely that a sudden reversal of the movement will set in.

On the whole, American investments abroad have been far more variable during the last decade than foreign investments in the United States. In 1926, 1927 and 1928 new foreign issues were floated in the United States at a rate of over \$1,000 million a year. But, during the past three years the creditor position of the United States in respect of bond issues and short-term credits has been reduced at a very rapid rate. It should be mentioned that American direct investments abroad in the form of industrial and commercial businesses and participations etc. have shown much greater stability than the volume of bonded investments and short-term credits. In fact, American direct investments abroad increased throughout the depression and at the end of 1935 accounted for \$7,835 million out of the total of all American foreign investments of \$12,630 million.

Where have the funds come from that have sustained the large capital movement to the United States in recent years? To throw light on this question it is of interest to summarise the figures published by the U. S. Treasury covering the influx of capital during the years 1935 and 1936 (upon which the graphs given earlier in this chapter were based):

	in millions of dollars	Origin of influx	in millions of dollars
Short-term capital		United Kingdom . . . . .	830
American net withdrawals from abroad . . . . .	456	France . . . . .	300
Net influx of foreign money . . . . .	916	Netherlands . . . . .	230
	1,372	Switzerland . . . . .	335
Security transactions		Other European countries . . . . .	356
Net purchases of American securities . . . . .	917	Total Europe . . . . .	2,051
Net purchases of foreign secu- rities . . . . .	316	All others . . . . .	556
	1,234		
Total capital influx . . . . .	2,607	Total . . . . .	2,607

American bank credits withdrawn in the two years were met, by and large, from the current balances of payments of the countries concerned — either from a general surplus, as in Finland, or from the earmarking of a particular item, as in the case of Germany (through the sale of registered marks). The amounts employed for repatriations and cash redemptions of dollar bonds were also in a large measure obtained from an active balance on current account in the countries which like Finland, Belgium and the Argentine have been able thus to reduce their foreign indebtedness. With regard to the purchase of American securities and the building-up of dollar balances, on the other hand, it cannot be said that the funds involved were produced from an active current balance of payments, except perhaps in a few cases, such as Canada. For England, the transfer of genuinely English funds was probably largely offset by receipts from repayments of old sterling loans (long as well as short-term), but for France, in particular, the outflow of funds was covered only by a charge on the monetary gold reserves.

Capital exports from France went partly to the United States, largely to England, but also to Belgium, Switzerland and the Netherlands. The U. S. Treasury figures do not show a very large capital import from France. In the twenty-one months from the beginning of 1935 to the devaluation in September 1936 only \$200 million are recorded as being from France (\$130 million short-term and \$70 million security purchases) — equivalent to 3,000 million of 1928 francs. But French capital exports were several times as great. In the same twenty-one months the Bank of France lost Fcs. 32,000 million of gold, to which should be added Fcs. 5,000 million of credits raised abroad. Allowance must, however, be made for the adverse current balance of payments over the period considered, withdrawals of foreign funds, hoarding of gold in France and certain other items, together some Fcs. 14,000 million, which, deducted from the gross figure of Fcs. 37,000 million, gives Fcs. 23,000 million (say, \$1,500 million) as a measure of the French capital exported over

this period. This figure although large is little more than half of the estimated export of French capital that took place in the years 1924/26; but in the earlier period the French current balance of payments was active, whereas the strain of the efflux in recent years has fallen directly on the Bank of France and the Paris market.

The heavy outflow of funds from the French market during the first nine months of 1936 was the main factor responsible for the forcing-up of the dollar-sterling rate from 4.95 early in March to over 5.05 in September 1936. After the devaluations at the end of September 1936 the sterling-dollar rate, released suddenly from the pressure of incoming funds from the continent, fell rapidly to 4.90 early in October. Short sales of French francs before devaluation were mostly against sterling, and this position was covered in the first three weeks of October 1936. The return flow of funds to France after devaluation did not assume large proportions and, in fact, was reversed in November and the following months. In February 1937 a credit of £40 million was raised in London by the French Railways and after the successful issue of the National Security Loan in France in the middle of March 1937 French banks sold some sterling to cover their subscriptions in francs, while dollars were also sold against francs.

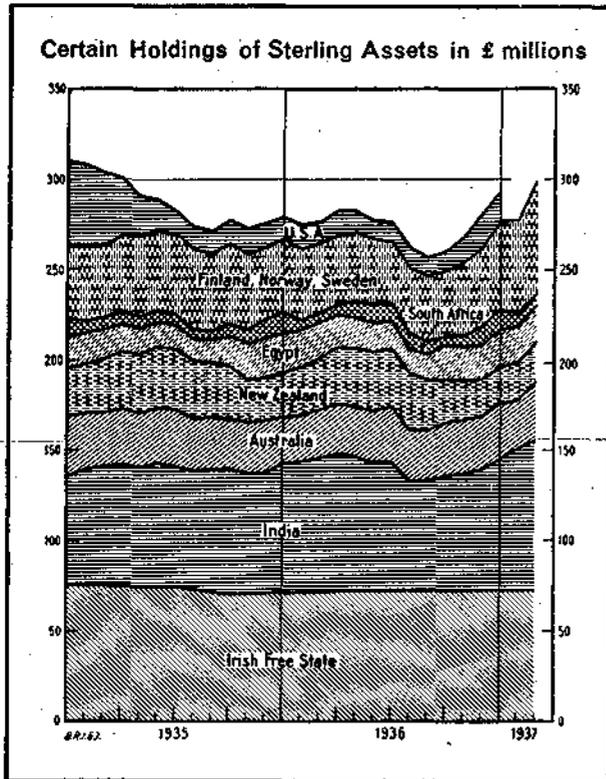
The return of Swiss capital, on the other hand, was rapid after devaluation of the currency and appears to have been completed by December 1936, since when some slight efflux has taken place. In the last quarter of 1936 the cash assets of the two biggest banks in Switzerland with large international business rose from Sw.fcs.250 million to Sw.fcs.660 million, those of four smaller banks from Sw.fcs.135 million to Sw.fcs.225 million, while the cash of the cantonal banks rose from Sw.fcs.150 million to Sw.fcs.300 million; at the same time sight balances at the Swiss National Bank increased from Sw.fcs.460 million at the end of September to Sw.fcs.1,360 million at the end of the year. The rapidity of the influx is shown by the fact that 85 per cent. of this increase took place in the month of October alone.

Besides Swiss capital there is doubtless some foreign capital which has taken refuge in Switzerland and the employment of this large accretion of funds without an inflation of values raises an acute problem. In the absence of new foreign issues on the market, it has been suggested that approved foreign securities already quoted on foreign stock exchanges should be introduced to the Swiss bourses; but, while such a measure might somewhat ease the plethora in Switzerland, it seems likely that if successful it would involve the export of gold to countries which already have abundant reserves.

The return of Dutch capital was somewhat slower in starting and was in fact rather preceded by foreign funds. Towards the end of the year, however, the inward flow gathered momentum and by the middle of February 1937 appeared to have ceased. Despite the large transfers of gold caused by the flow of funds to the Swiss and Dutch markets, the monetary reserves in London and New York, far from being reduced, rose substantially in the last quarter of 1936 and at the beginning of 1937. The gold supplies on the markets were increased by current production, large dehoarding on private account and the outflow of gold from France from November onwards.

The rise of spot sterling against the dollar in the summer of 1936 to a level which it was expected would not be maintained led to a flow of banking funds from London for employment in New York, which could be advantageously covered owing to the wide discount on forward sterling. The following graph, giving the volume of certain funds in London, shows how the balances of American banks were reduced during 1935 from the high level at the end of 1934, the development of a forward discount on sterling being

sufficient to offset the higher interest rate in London and thus making the employment of American balances in London no longer profitable. The low level reached in the autumn of 1935 appears to be the working minimum of these banks.

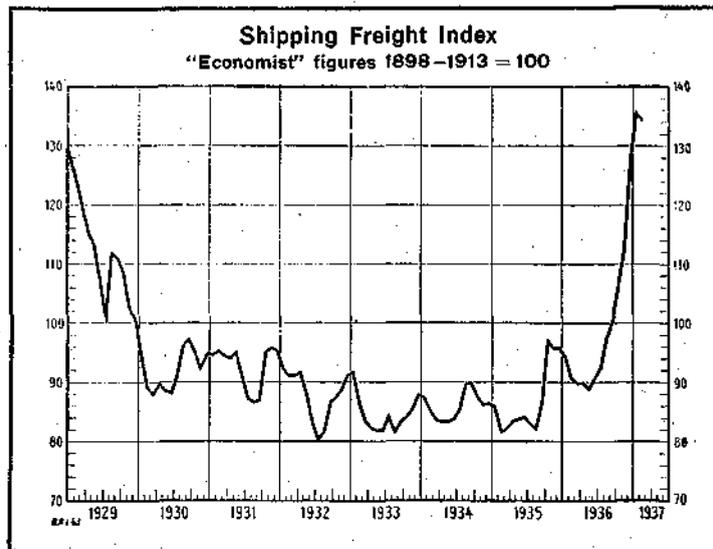


Besides the balances of United States banks, the graph shows holdings of sterling funds by certain bodies in British and sterling-area countries. The sterling assets of the Currency Commission and the excess of sterling assets over sterling liabilities of the banks operating in the Irish Free State have remained very stable, being largely a form of permanent foreign investment. India and South Africa together, as mentioned in the next chapter,

repaid in 1936 some £35 million of old sterling loans from their own resources. Australia had a better year in 1936 largely owing to the increased prices obtained for Australian exports in the latter part of the year; there was also some influx of foreign funds. The sterling holdings of the Commonwealth Bank increased by about £5 million over the year but this does not tell the whole story. The trading banks were also able to make a much-needed addition to their London funds, sorely depleted in the depression years. The Directors' Report of the Commonwealth Bank for 30th June 1936 says: "London funds at present are sufficient for normal requirements but are not sufficiently high to provide an adequate reserve against adverse circumstances". On the other hand, London funds of the Reserve Bank of New Zealand and the trading banks shown in the graph fell by £5 million sterling on balance over the year to £20 million sterling, the lowest point since the formation of the Reserve Bank. Although the total of London funds now held compares very favourably with the period before the acquisitions of sterling by the government in 1933, the wide seasonal fluctuations to which New Zealand's exports are subject make

the conservation of an adequate holding of London funds desirable. The sterling holdings of the central banks of Finland, Norway and Sweden rose by £10 million, while these banks added some £20 million sterling to their gold holdings in 1936, the movement continuing in the early months of 1937. All three banks hold part only of their gold as metallic reserve, the balance being considered as secondary cover and in Norway specifically called "funds placed temporarily in gold". The Swedish position is unusual. The Swedish commercial banks normally hold net foreign short-term assets to the amount of Kr. 100–200 million, and in September 1936 these assets amounted to Kr. 130 million. In the following months, however, the position was suddenly reversed and at the end of March 1937 the banks' returns showed a net deficit of Kr. 155 million. This appearance of a net liability was in no way due to an adverse development of the balance of payments, which, on the contrary, was active, but to a movement into krona assets (see page 75) connected with the belief that the krona would appreciate about 7 per cent. to the old parity with sterling. The foreign exchange was sold to the Riksbank and accounts for the increase of its holdings of gold and foreign exchange to abnormal proportions in the first quarter of 1937.

Finland, besides repaying a long-term dollar loan in 1936, was able to increase its short-term foreign assets. The improvement in the short-term foreign position of Norway and Denmark is, however, in both cases partly due to the raising of new long-term debt abroad. Swedish lending to the



Norwegian Government and the Mortgage Bank of the Kingdom of Norway amounted to Kr. 40 million in 1936 and Norway benefited also from an improvement of freight rates, of great importance to its merchant fleet now in full activity. The Danish Government borrowed Kr. 40 million in Stockholm in May 1936 (producing the equivalent of 45 million Danish kroner)

and the Mortgage Bank of the Kingdom of Denmark raised £1½ million in London in December 1936 (which was sanctioned by the British Treasury as the proceeds went to strengthen the sterling resources of a country in the sterling area). The short-term foreign debt of Danmarks Nationalbank was reduced in 1936, even showing a small net surplus of assets in the middle of the year for the first time since 1933. In January 1937 the net debt in foreign exchange of the Nationalbank at Kr. 14 million showed an improvement of some Kr. 54 million compared with January 1936.

During 1936 the trade balance of Italy improved, the passive balance being reduced to Lit. 2,100 million from Lit. 3,200 million in 1935. The publication of the state of the various clearing accounts to which Italy is a party was resumed in December 1936 and these accounts showed a not unfavourable situation.

The foreign indebtedness of Germany on account of repayments, devaluation of creditor currencies and other factors has been reduced as follows in recent years:

in milliard Reichsmarks at end of month	July 1931	Nov. 1931	Feb. 1932	Feb. 1933	Feb. 1934	Feb. 1935	Feb. 1936
Long-term . . . . .	10.7	10.7	10.5	10.3	7.2	6.4	6.1
Short-term . . . . .	13.1	10.6	10.1	8.7	6.7	6.7	6.3
Total . . . . .	23.8	21.3	20.6	19.0	13.9	13.1	12.4

The figures for 1931 should be somewhat higher as in the returns for that year only debts above RM. 50,000 were included, whereas for later years the limit was lowered to RM. 5,000. The German foreign debt in gold values has thus been halved since the liquidity crisis. The devaluations in 1936 brought further reductions of the capital debt, which now amounts to about RM. 11,500 million. Credit lines under the standstill agreement continued to be reduced from RM. 1,567 million at the end of February 1936 to RM. 1,165 million at the end of February 1937 (of which RM. 1,041 million were availed of). Conversions into registered marks in the first nine months of the 1936 agreement accounted for RM. 306 million (of which RM. 255 million were employed for travel purposes). The standstill agreement was renewed in February 1937 for a further year with only slight modifications. The check to the rapid reduction of the German short-term indebtedness in 1934 was due partly to the maturing of long-term debt, which under the exchange restrictions was not transferred, and partly to the accumulation of new indebtedness. In the first half of 1934 the quotas of foreign exchange allotted to importers were gradually reduced and during the year commercial debts to foreign countries grew considerably. German debts on clearing and similar accounts reached their highest point of RM. 567 million in March 1935, after which time the effects of the New Plan for balancing imports and exports began to be felt and a gradual reduction of these debts took place. From about RM. 500 million at the beginning of 1936 the total clearing debts had fallen to RM. 415 million in November 1936. These accounts give, of course, only the cash balances remaining of matured debts and thus do not give a complete picture. In particular, Germany has in recent years exported to an increasing extent on credit and the sums owing to German exporters and not yet due for payment are not inconsiderable. During 1936 the old commercial debts to England and Belgium were completely repaid and under the present system of payments with these countries no similar debts can be accumulated in future; some other countries such as the Netherlands and France were also able to obtain substantial reductions; on the other hand, German clearing

debts to certain other countries increased, particularly to Poland for railway transit through the Corridor.

The difficulties experienced with regard to this and other amounts owing to Poland came at a bad time for that country, which suffered early in 1936 from a flight of capital; exporters tended to leave the foreign exchange proceeds of exports abroad, imports against cash increased and banks accelerated the repayment of foreign credits. Foreign exchange restrictions were introduced in April 1936, foreign trade control in May and transfer restrictions on the foreign debt service in June. The active balance of trade fell from Zl. 177 million in 1934 to Zl. 64 million in 1935 and Zl. 23 million in 1936, while, in addition, gold coin was imported for hoarding purposes. The gold reserve of the Bank Polski fell from Zl. 510 million in the middle of 1935 to below Zl. 370 million in the summer of 1936, but there was some relief in the latter part of the year. Foreign credits granted to Polish banks were reduced by the equivalent of over Zl. 50 million during the year by repayments and by the devaluations of foreign currencies in September, but in the meantime interest and other sums blocked under the exchange restrictions were accumulating. At the end of the year an important credit was obtained in France.

The total foreign debt of Hungary has recently been estimated at 2,400 million pengö compared with 4,300 million in 1931, but these figures are given in gold values and the depreciation of the currencies of the creditor countries accounts for the greater part of the apparent reduction, although some repayments of capital and repatriations of bonds have also contributed.

There are few signs of a revival of international trade financing. Over a wide area the working of clearing agreements precludes the financing of foreign trade through the normal mechanism. The Governor of the Bank of England recently gave the amount of trade bills circulating in the London market at £130 million in the spring of 1936 compared with £220/230 million five years earlier (these figures being not necessarily complete but comparable). The decline of trade financing in dollars is even more remarkable, dollar bank acceptances outstanding declining from over \$1,500 million at the end of 1930 to under \$400 million in 1935/36.

Exports of foodstuffs and raw materials are, in general, made against very short credit terms or cash, in some cases even payment in advance (for crop financing purposes) while credit for three months or longer is given for industrial goods. It follows that agricultural countries, having been paid cash for their exports, are normally indebted on commercial account in respect of their imports over three months and more. In so far as the industrial countries have in recent years shortened the period of credit or, maybe, insisted on cash payment for their exports, they have often placed severe burdens on the agricultural (usually debtor) countries, even to the extent of forcing them into exchange restrictions.

There is unfortunately insufficient information available as to the terms of credit given in international trade but in some countries, for which these

credits are of great importance, estimates have been made in connection with balance of payments calculations. As an example it may be mentioned that Polish imports in 1928/29 were at the rate of over Zl. 3,000 million per annum, while trade credits outstanding were over Zl. 1,000 million, so that an average of four months' imports was regularly made on credit. Credits granted by Polish exporters, on the other hand, were around Zl. 300 million, equivalent to about 1½ months' exports only. When trade fell off after 1929, trade credits were reduced even more severely — Polish imports fell, requiring proportionately less financing, but the foreign exporters gave shorter as well as smaller credits. Polish imports declined by one-third from 1929 to 1930, but the credits outstanding were reduced by more than one-half — imports were again cut by one-third from 1930 to 1931 and again credits were reduced by over 50 per cent. By 1932 the value of Polish imports was little more than one-quarter of what it had been in 1928/29 while the trade credits received from foreign exporters were only one-eighth and represented the value of less than two months' imports. The credits granted by Polish exporters were not so easily reduced and remained the equivalent of about 1½ months' exports. In terms of cash this meant that on balance Poland repaid in three years about Zl. 800 million of trade credits — a striking proof of the liquidity of these credits; the magnitude of this sum for Poland may best be realised when compared with the total gold and foreign exchange reserve of the Bank Polski, which at its highest point in 1928 was Zl. 1,350 million.

Several other countries which export mainly agricultural or similar products are now in a similar position, having almost entirely repaid the normal trade credits on account of imports and buying almost solely on a cash basis. These countries should be in a strong position when trade revives — any lengthening of import credits will go directly to ease the exchange position and help towards the reconstitution of the central bank's reserves. The marked increase in foreign trade since the summer of 1936 has, no doubt, been accompanied by some growth of commercial lending internationally but hardly any new facilities have been extended to countries with difficult exchange positions. From a purely technical point of view, it is not easy to combine the granting of credits with the existing system of clearings.

In the field of middle-term credits, mention should be made of the arrangement of a £10 million trade credit for Russia in the United Kingdom to run for five years at 5½ per cent. with the principal and interest guaranteed by the Export Credits Guarantee Department. In addition a representative of this department was sent to China to study the possibility of similar trade credits to that country. While these schemes are designed primarily to increase British exports, they certainly facilitate the general increase of trade by prolonged credit terms. Now that for several reasons, including the large production of gold, Russia is in less need of trade credits than formerly, it has been granted middle-term credits on favourable conditions by a number of countries including Czechoslovakia, Germany and England.

The continued stagnation of international lending is partly the result of technical difficulties (such as the clearing systems) and partly due to a feeling of uncertainty as to general monetary and political developments. Actually, the influence of the different factors is closely intertwined. It would seem, however, as if there were a growing realisation of the losses imposed upon the world by the insufficient use made of the existing credit apparatus in international intercourse. In recent years great emphasis has often been laid on the part that appropriate credit conditions may play in assisting recovery in the various national economies. But the same need is found internationally; and at a time when the development of foreign trade is urgently needed to maintain a balanced recovery this factor should not be minimised.

### V. TREND OF INTEREST RATES.

Taking the world as a whole the tendency in the year 1936 continued to be towards the establishment of low levels of interest rates both on the short and long-term markets. Of twenty-six European central banks nine reduced their official discount rates on balance during the year, only two rates were increased, and the remainder were unchanged throughout the year. Outside Europe the same tendency prevailed, official discount rates being reduced in Japan and the Dutch East Indies (January 1937) and no increases being made. The money markets have been characterised by a continued, and in many cases increased, liquidity; only in certain countries of the sterling area, including Australia, Denmark and Norway, were there certain signs of a stiffening of rates during the year, while in the first quarter of 1937 the abnormally low rates which had prevailed on the New York market became somewhat higher. During the year there was a downward adjustment of long-term interest rates; but here also a reaction began to be noticeable in some countries, especially in the early months of 1937 when the quotations of British gilt-edged securities moved sharply down in January and February, and United States government bonds declined in March. There was generally very little increase in bank credit for industrial purposes, but in a large number of countries a rather marked advance in the volume of commercial financing reflected the increase in commodity prices.

#### 1. SHORT-TERM MARKETS.

The extent to which official discount rates have been reduced as compared with the rates obtaining in the period 1925/29, as well as the changes made in recent years, are shown in the following table.

Discount rates of European central banks	1925-1929		End 1935	End 1936	Change in 1936	End March 1937 (d)
	high	low				
<b>1. Rates decreased in 1936</b>						
Switzerland . . . . .	4	3½	2½	1½	-1	-
France . . . . .	7½	3½	6	2	-4	4
Netherlands . . . . .	5½	3½	3½	2	-1½	-
Czechoslovakia . . . . .	7	5	3½	3	-½	-
Italy . . . . .	7	5½	5	4½	-½	-
Portugal . . . . .	9	8	5	4½	-½	-
Latvia . . . . .	8	6	5½ (a)	5½ (a)	-	-
Lithuania . . . . .	8	7	6	5½	-½	-
Albania . . . . .	12	9	7½	7	-½	6½
<b>2. Rates unchanged in 1936</b>						
Belgium . . . . .	7½	4	2	2	-	-
England . . . . .	6½	4	2	2	-	-
Sweden . . . . .	5½	3½	2½ (b)	2½ (b)	-	-
Austria . . . . .	13	6	3½	3½	-	-
Hungary . . . . .	12½	6	4	4	-	-
Finland . . . . .	9	6	4	4	-	-
Germany . . . . .	10	5	4	4	-	-
Estonia . . . . .	10	7½	4½ (c)	4½ (c)	-	-
Rumania . . . . .	9½	6	4½	4½	-	-
Danzig . . . . .	10	5½	5	5	-	4
Poland . . . . .	12	8	5	5	-	-
Spain . . . . .	5½	5	5	5	-	-
Yugoslavia . . . . .	7½	5½	5	5	-	-
Bulgaria . . . . .	10	9	6	6	-	-
Greece . . . . .	11	7½	7	7	-	6
<b>3. Rates increased in 1936</b>						
Denmark . . . . .	7	5	3½	4	+½	-
Norway . . . . .	6½	4½	3½	4	+½	-

(\*) ½ per cent. higher for private firms.  
 (b) ½ per cent. lower for rediscounts of banks.

(c) ½ per cent. lower for bankers' acceptances.  
 (d) where changed since the end of 1936.

At the end of 1936 every country in Europe had a bank rate below the lowest quoted in the years 1925/29, Spain being the only exception. The position of the central and southern European countries is particularly striking, Austria, for example, at present enjoying a  $3\frac{1}{2}$  per cent. bank rate against rates of from 6 to 13 per cent. in the 1925/29 period. The nine European countries in which on balance the official rates were reduced during 1936 included every one of the six countries which in the autumn of that year readjusted the value of their currencies or imposed an embargo on gold, namely: Czechoslovakia, France, Italy, Latvia, the Netherlands and Switzerland. Five years earlier, when the currencies of Great Britain and a number of other countries depreciated in the middle of the severe liquidity crisis, the discount rates of the central banks in these countries were kept for several months at a level of 6 per cent. or even higher, to react against the losses of funds. No similar measures were adopted in the autumn of 1936 when, on the contrary, the immediate effect of the currency changes was a return flow of funds to the markets in which the changes were made.

Among the former gold-bloc countries, Switzerland has in recent years maintained a fairly stable discount rate; an increase from 2 to  $2\frac{1}{2}$  per cent. was made only when there was great pressure on the Swiss franc in the summer of 1935. In France and the Netherlands, on the other hand, the official discount rate was changed repeatedly in conformity with, or as a means of influencing, current market conditions: in France there were ten effective changes of bank rate during 1935 and no fewer than twelve in 1936, and in the Netherlands fifteen changes during 1935 and nine in 1936. The pressure on the Dutch market was, however, never so strong as that on the French market, the latter being affected all through 1936, with some relief only after the devaluation in the autumn, by a persistent outflow of funds and by continuous government borrowing. In France, the burden of financing the government fell partly on the Bank of France, which during the year not only discounted bills for the market, but also made advances to the government. Article 13 of the Law of 24th July 1936, revising the statutes of the Bank of France, provides that all securities forming part of the floating debt of the government and due within a maximum of three months are admitted without limit to the rediscount facilities of the bank, except directly for the Treasury. As a result of laws passed in August 1936 the Bank of France has also taken bills endorsed by the Wheat Office and re-discounted bills for the Caisse Centrale des Banques Populaires, the aggregate of the credits thus granted amounting to 1.4 milliard francs at the end of December 1936.

The turnover of advances for a maximum of thirty days on government securities with a maturity not exceeding two years has continued active during the year and these facilities, which were introduced in February 1935, have become a regular feature of the market, especially as a relief to the end-of-month pressure. During the year the rate for these advances has been equal to and fluctuating with bank rate. An aggregate of Fcs. 38 milliards of these advances was granted during the year against  $16\frac{1}{2}$  milliard in 1935 (10 months).

Capital exports and currency hoarding during the first nine months of the year resulted in continuous pressure on the money market, attaining at

times an acute tension. The contraction of the funds available on the market is illustrated by the fall of savings banks deposits from 63 milliard at the end of January to 58 $\frac{1}{2}$  milliard at the end of September; over the same period the deposits of the four big Paris banks fell from 27 $\frac{1}{2}$  milliard to 21 $\frac{1}{2}$  milliard, while the circulation of "bons de la défense" contracted by over 1 milliard (compared with a slight increase over the corresponding period of previous years). These influences were reflected in market rates, which, particularly at moments of severe pressure, were in the close vicinity of the official discount rate, and at times, indeed, above this rate — an altogether abnormal condition. It is characteristic of this, as well as last, year that increases of bank rate have occurred only when pressure on the market forced them, whereas reductions have, contrary to the usual practice of the Bank of France, tended to lead and direct the market.

One of the difficulties of maintaining effective control of interest rates on the market was the high discount on forward exchange, which at times made it possible to earn up to 35 per cent. on a three months exchange swap. Although such rates are quoted only for particular transactions, market rates tend to be influenced by them, whatever measures may be taken by official restrictions or otherwise to prevent heavy engagements in the forward exchange market.

On 7th July 1936 the Nederlandsche Bank lowered its discount rate from 3 $\frac{1}{2}$  to 3 per cent., and this was the rate in force when the embargo on gold was decreed. By two successive reductions in October and December respectively the rate was brought down to 2 per cent., which, except for the brief period from May to September 1931, is the lowest quoted in the Netherlands since 1850. The Amsterdam money market was exposed to pressure only during a short time in the summer, when the private discount rate for a time rose above bank rate and was a factor in the increase of bank rate to 4 $\frac{1}{2}$  per cent., the highest rate for the year, which was maintained for three weeks in June; but the pressure passed and in September 1936 the private discount rate was between 1 $\frac{1}{8}$  and 1 $\frac{1}{2}$  per cent. In the Netherlands the money market did not have to carry any new burden of government borrowing; in fact the floating debt (Treasury bills and Treasury bonds) decreased from about Fl. 590 million in January to Fl. 525 million in the last week of September. The characteristic rate of the Amsterdam market, the "prolongatie" (one month's advances on securities), was at its highest at 4 $\frac{3}{4}$  per cent. in June compared with 6 $\frac{1}{2}$  per cent. on several occasions in 1935. By September 1936 the average rate was 1.3 per cent., almost the lowest for the year; but the demand for this accommodation was in fact comparatively small, although bourse activity as measured by the tax on stock exchange transactions was higher than in previous years, purchases in 1936 being made largely out of liquid resources.

In Switzerland there was even less sign of pressure on the market than in the Netherlands — in fact the Swiss National Bank lowered its official rate from 2 $\frac{1}{2}$  to 2 per cent. on 9th September, three weeks before devaluation of the currency. A further decrease on 26th November brought bank rate to 1 $\frac{1}{2}$  per cent., the lowest quoted since the National Bank was established in 1907,

and very low indeed even for a country with such traditionally low interest rates as Switzerland, where, during the past 10 years, bank rate has never been above  $3\frac{1}{2}$  per cent. The gold reserve, which had been below Sw. fcs. 1,200 million in 1935, was over Sw. fcs. 1,500 million when the gold standard was suspended, and rising steadily even in the last week of September.

The easier conditions of 1936 were due to a reflux of funds to the big banks, whose combined quarterly balance sheet, the total of which had fallen continuously from 1930 to the end of 1935, rose by some 9 per cent. during the first three quarters of 1936. Private discount rate remained some  $\frac{1}{4}$  per cent. below bank rate until early in September and when bank rate was reduced to 2 per cent. the margin increased to  $\frac{1}{2}$  per cent., so that the further reduction of bank rate to  $1\frac{1}{2}$  per cent. was necessary to get the central bank again in touch with the market. Money has continued to flow into the banks and in February 1937 the private discount rate fell to 1 per cent.

In Italy the official discount rate was reduced from 5 to  $4\frac{1}{2}$  per cent. in May 1936. During the year the advances by the Banca d'Italia to the Istituto per la Ricostruzione Industriale were increased from 802 million lire to 4,708 million lire, and at the end of the year the ordinary advances to the Treasury were fixed at 1,000 million lire and extraordinary advances, against Treasury bills, at 2,000 million lire. In order to offset these various advances the Banca d'Italia restricted its volume of discounts and private advances from 8,988 million lire at the end of 1935 to 2,866 million lire at the end of 1936. This reduction was possible because the private banks were in a liquid position as a result of Government spending and the operations of the Istituto. In this way, an expansion of the total credit volume outstanding was avoided; the note circulation rose only from 16,297 million at the end of 1935 to 16,525 million lire at the end of 1936, and it should be mentioned that the latter figure includes an amount of notes, estimated at 1,480 million lire, transmitted to East Africa.

The increases of bank rate, in Denmark and Norway, were moderate, being only of  $\frac{1}{2}$  per cent. and leaving bank rate at 4 per cent. in each case. In Denmark the official rate was raised on 19th November 1936, owing to the development of a tighter devisa position following increased imports and the difficulty of obtaining payments for exports to countries with foreign exchange restrictions. The hardening of money rates must be seen, however, against the wider background of the reversal of the expansionist policy undertaken in 1933/34 to favour long-term debt conversions. Bank rate was lowered to  $2\frac{1}{2}$  per cent. in November 1933 and the Nationalbank and the Crisis Fund (which borrowed directly from the bank) bought bonds heavily on the open market, causing an appreciable rise in quotations. In March 1935, the point of greatest expansion, the bank held Kr. 153 million bonds and the Crisis Fund account rose to Kr. 142 million. From the spring of 1935 the Nationalbank started selling its bonds and bank rate was increased to  $3\frac{1}{2}$  per cent. in August 1935. Steady selling of bonds for twenty months reduced the bank's holding by the end of December 1936 to under Kr. 50 million, that is, to around the normal level, while the account of the Crisis Fund was reduced to Kr. 130 million as the result of repayments of certain credits, no bonds having

been sold. The bond market showed great resistance, especially as the commercial banks also sold some Kr. 50 million bonds during 1936. The increase of bank rate by  $\frac{1}{2}$  per cent. in November 1936 was followed by a similar increase of the lending rates of the commercial banks.

The increase of bank rate in Norway has a very different background. The receipt of the proceeds of loans in Sweden and increased receipts from certain exports and especially from shipping have made the foreign exchange position easy and the reserve of the Norges Bank has risen appreciably. The improved external position would normally have been reflected in a higher degree of liquidity in the banking system. The expansion of bank deposits in 1935, however, gave way in 1936 to a rather sharp reversal following the introduction of a tax on bank deposits and, towards the end of the year, a high degree of activity developed in the share market, with sharp rises in quotations. The increase of bank rate on 7th December 1936 enabled the banks to increase their deposit rates which, it is hoped, with a modification of the bank deposit tax, will cause a reflux of cash to the banks.

In other European countries where there has been no change of bank rate, the year has not been uneventful. The official discount rate in England has now been maintained at 2 per cent. (a rate equalled only in the 'nineties) for nearly five years without interruption, but it still remains well above market rates, the average Treasury bill rate in 1936 being 0.58 per cent. In the first nine months of the year there was a large influx of funds, particularly from France. During the year as a whole, there was an expansion of the (ten) clearing banks' internal advances, which rose by £80 million, or three times as much as in 1935 and an increase in investments by £25 million. In spite of some reflux of foreign funds during the last three months of the year, the total deposits of the original ten clearing banks at the end of 1936 reached the high record of £2,238 million, £500 million higher than at the end of 1931. Owing to the stabilising influence of the Exchange Equalisation Account and the purchases of gold by the Bank of England, the influx of foreign money, the monetary changes in the autumn of 1936, the granting and repayment of the £40 million credit to the French Government, and the further French railway credit in 1937 had less effect on market rates than did purely seasonal and technical factors.

The seasonal fluctuations of government revenue and expenditure and the out-payments from the banks tend to concentrate pressure on the money market at the end of June and December. The wide margin between bank rate and market rates combined with the predominance of Treasury bills on the market (the average of bills issued by tender being some four times the amount of other bills dealt in on the money market) has led, however, to some shifting of the seasonal pressure. Treasury bills having a three-months' maturity, the banks apply heavily for bills due at the end of June and December and to some extent the effect on interest rates is thus reversed and shifted forward three months. At the end of June and December the banks allow Treasury bills to run off and in this way force the borrowing from the Bank of England to be done by the government.

Among influences on the market during the autumn was an unusual increase of public deposits (i. e. government and other official accounts),

which caused the clearing banks' cash ratio to fall to the low level of 9.9 per cent. in October. This percentage is, of course, an average for all the banks, the actual ratios varying in October from 8.7 to 10.4 per cent. It is commonly assumed that the English clearing banks keep a cash ratio of 10 per cent. practically unchanged, but in fact the fluctuations from time to time and from bank to bank are very appreciable, and as short a time ago as April 1934 the average ratio was 12.0 per cent., while that of the individual banks varied from 7.9 to 14.6 per cent.

Bank rate has been at 4 per cent. in Germany for 4½ years. Except for a brief period in 1930, this rate is the lowest since the war and compares with an average of over 7 per cent. from 1925 to 1929, when the influx of foreign funds was at its heaviest. At the same time market rates continue to fall:

Average rate per cent	Daily money	Private discount
1931	8.4	6.8
1932	6.4	4.9
1933	5.5	3.9
1934	4.4	3.8
1935	3.4	3.2

— and for 1936 both rates were slightly below 3 per cent.

The deposits of the big Berlin banks rose from RM 6,120 million in January 1936 to RM 6,530 million in January 1937, while book credits fell from RM 3,850 to RM 3,600 million; on the other hand the holdings of bills have increased from RM 1,660 to RM 2,390 million (true commercial bills have, however, tended to decline, their place being taken by public bills). In addition the endorsement liabilities of the banks have fallen and the whole of the emergency re-discounting of the crisis has been repaid. The bill holdings of the Reichsbank also increased considerably, especially during 1936 when the total of bills and cheques rose from RM 4,498 to RM 5,448 million. This development, at a time when the banking system is very liquid and in fact repaying its debts, indicates an increase in the direct discounting of public bills by the central bank (without the intermediary of the commercial banks).

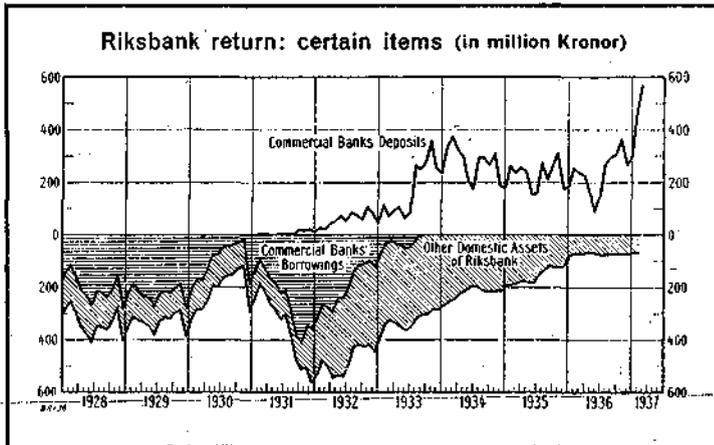
Golddiskontbank Solawechsel	1935	1936	1937
	in RM millions		
January . . . .	—	629	700
February . . . .	—	716	1,185
March . . . . .	—	750	1,082
April . . . . .	—	862	
May . . . . .	202	655	
June . . . . .	358	716	
July . . . . .	546	396	
August . . . . .	651	71	
September . . . .	495	30	
October . . . . .	492	406	
November . . . .	701	463	
December . . . .	701	400	

In order to mop up surplus funds on the Berlin market, Solawechsel, which are rediscountable, have been issued by the Golddiskontbank since the spring of 1935. The fluctuations of the total of these bills outstanding are shown in the table.

The very large amounts issued in the spring of 1936 and again early in 1937 reflect the easiness of the market. The contraction to low figures at the end of August and September 1936 is connected with the issue of Treasury bonds by the Reich; the temporary tightening of the market of that time had passed by October.

In Belgium the Institute of Rediscount and Guarantee made several issues of bills by tender during the year, the rates, varying from 0.425 to 1.25 per cent., are without precedent on the Brussels market. Bank rate has remained at 2 per cent. for two years.

The liquidity of the Stockholm market, which has been a characteristic feature of Swedish conditions for some years, became more pronounced early in 1937. Before 1932 the Swedish banks had cash balances of only a nominal amount at the Riksbank, to which they were normally indebted, as the

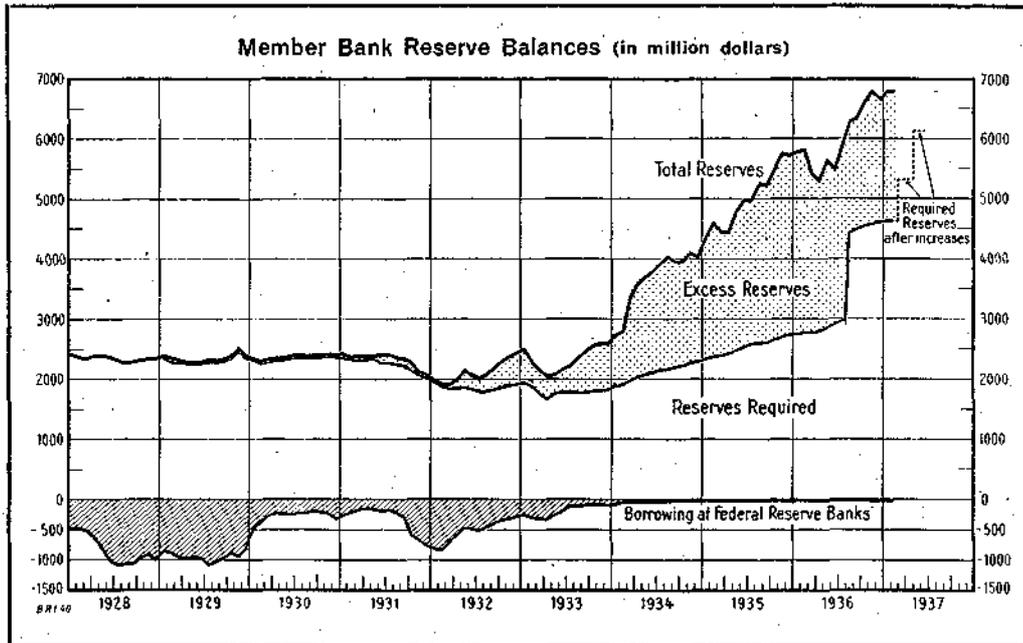


accompanying graph shows, to the extent of some Kr. 200 million. From the autumn of 1931 the indebtedness of the banks was rapidly repaid and from the middle of 1933 (when the krona was pegged on sterling at the rate of 19.40) to early in 1936 the banks' cash holdings stood at around Kr. 200-300 million. The Riksbank's

other assets in Sweden fell more slowly and reflect the assistance given by the government to the Skandinaviska Kreditaktiebolaget, now completely repaid. At the present time the total domestic assets of the Riksbank are below Kr. 100 million while the balances of the commercial banks rose in March 1937 to Kr. 590 million. The total cash items of all the banks amounted to Kr. 755 million at the end of March 1937, of which Kr. 635 million were held by the three largest banks. To be able to reduce the amount of liquid resources available, the National Debt Office has been authorised to place bills and bonds at the disposal of the Riksbank for sale on the market. It has also been proposed to introduce a system of compulsory minimum cash requirements for current accounts at the commercial banks, which proposal is still under consideration (April 1937).

Although there has been no increase of bank rate anywhere outside Europe, important measures affecting credit conditions have nevertheless been taken, especially in the United States. The rediscount rates of the Federal Reserve banks have remained unchanged since May 1935, New York and Cleveland applying 1½ per cent. and the remaining ten banks 2 per cent.; the New York Reserve bank's minimum buying rate for 90-day bankers' acceptances (which more closely corresponds to the bank rates of European central banks) is unaltered at ½ per cent., to which it was reduced in October 1933 (although in March 1937 market rates tended to rise above this level). While short-term money rates remain at very low levels, measures have been taken to eliminate the excess reserves of the member banks, which provided a possible basis for dangerous expansion of credit.

The problem of excess reserves is a comparatively new one. From 1925 to 1929 the position was that, of the \$2,250–2,500 million reserve balances which the member banks were required by law to maintain at the Federal Reserve banks, some \$500–1,000 million were borrowed from the Reserve banks.



Generally speaking, the member banks not only had no "excess" reserves but in fact directly borrowed up to some 40 per cent. of their "required" reserves. Excess reserves did not appear until 1932, following heavy purchases of government securities made by the Reserve banks, and did not increase rapidly until 1933. The Board of Governors of the Federal Reserve System stated in January 1937: "... Between the time of the banking holiday in 1933 and December 24, 1936, ... the gold inflow aggregated approximately \$4,000 million. This inflow of gold had the effect of adding an equal amount to the reserves of member banks as well as to their deposits. The total amount of deposits in banks and the postal savings system, plus currency outside of banks, is now \$2,000 million larger than in the summer of 1929 ..."

Total reserves of member banks rose to \$6,000 million in 1936, or twice the amount required and, theoretically at least, deposits might also have been expanded to double those then existing. This situation contained elements of danger which were already recognised when the Bank Act of 1935 (adopting with modifications the emergency measures in the Agricultural Relief Act 1933) gave powers to the Board of Governors to raise member bank reserve requirements to not more than double those then existing "in order to prevent injurious credit expansion". The Board decided that from 16th August 1936 the percentage of required reserves to deposits be increased by 50 per cent. As gold continued to be imported in the autumn of 1936 the Board decided to use its powers in full and ordered a further 50 per cent. increase (thus doubling the original percentages) to be made in two equal instalments on 1st March

and 1st May 1937. The absorption of excess reserves in this way, rather than by selling government securities as recommended by the Advisory Council of the Federal Reserve System in November 1935, was decided upon because the changes in percentages affect all member banks regardless of their reserve position "and consequently should be made while reserves are widely distributed".

From 1st May 1937 member banks in New York and Chicago must hold balances at the Reserve banks the equivalent of 26 per cent. of their net demand deposits; at the other "reserve cities" 20 per cent. must be held and in country districts 14 per cent. Time deposits must everywhere have a 6 per cent. reserve backing. It was expected that the new increase ordered in 1937 would, when completed, bring the excess reserves down to about \$500 million as compared with over \$3,000 million at the beginning of August 1936; but further purchases of securities by the Reserve banks in April 1937 may cause some modification of this estimate.

In its statement on 31st January 1937 the Board expressed the opinion that "the present volume of deposits, if utilised at a rate of turnover comparable to pre-depression levels, is sufficient to sustain a vastly greater rate of business activity than exists to-day. In order to sustain and expand recovery, the country's commerce, industry, and agriculture, therefore, require a more complete and productive utilisation of existing deposits rather than further additions to the amount now available".

The increase in the percentage of reserve requirements applies only to member banks of the Federal Reserve System. It is true that the relative importance of the member banks has increased since the closing of the banks in 1933, but at the end of June 1936 member banks' deposits (excluding interbank) accounted for only \$34,000 million out of the total for all banks of \$51,000 million — \$10,000 million being held by mutual savings banks and \$7,000 million by other non-member banks. The annual report of the Federal Deposit Insurance Corporation for 1936 calls attention to this lack of unified authority. In fact, however, non-member banks hold most of their reserves with member banks, so that in the final analysis reserve balances of member banks constitute the reserves for all deposits in the United States.

On the stock market also measures to restrict potential expansion of credit were taken in 1936 under the Securities Exchange Act of 1934, the Federal Reserve Board raising the margin requirements for loans against securities to comparatively high levels — 55 per cent. of the market value of securities carried must be deposited by clients with their brokers and banks must also require a similar margin. Various other regulations have also been issued.

A feature of the year was the increase of commercial borrowing at all member banks, indicated by the rise of \$1,035 million of "other loans" (1935: increase \$300 million only); but the aggregate of \$6,040 million at the end of 1936, although the highest since the "banking-holiday" of 1933, remains small compared with earlier years and with the volume of funds available for lending. The increase of commercial borrowing is usually taken to show a demand for additional funds by producers and distributors of goods. A further explanation advanced is the increased bank holdings of finance company paper, but it appears that the

increase in such holdings was probably not the major element in the rise of "other loans". Published statements of fifteen of the principal finance companies indicate that on 30th June 1936 the aggregate amount of credit extended by such companies was about \$1,200 million, an amount 45 per cent. greater than in 1929 and three or four times the volume in 1932. The credit granted by these companies is primarily to finance sales of automobiles, but also of various other

Credit extended by 15 finance companies	Twelve motor	Three diversified industries	Total
	End of year in \$ millions		
1929	677	152	829
1932	275	63	338
1933	368	80	448
1934	500	101	601
1935	715	155	870
1936 (30th June)	971	225	1,196

goods such as heating and ventilating apparatus, mechanical refrigerators and other household appliances, the finance companies obtaining about two-thirds of their funds through bank loans and the sale of notes. These figures are considered to give some indication of

the movement of consumer credit in the United States. Consumer buying has been given non-recurrent stimulus in 1936 by the payment of the Soldiers' Bonus in June and by the operation of the Tax Act, which forced out taxable undistributed earnings so that dividends declared in November amounted to \$880 million against \$400 million in November 1935 (December 1936, \$440 million against \$300 million).

On the other hand, credit granted through government agencies now tends to decline as the following figures of the loans outstanding of three important credit agencies wholly financed by the U. S. Government show:

in \$ millions	end 1935	end 1936
Reconstruction Finance Corporation . . . . .	1,401	1,174
Commodity Credit Corporation . . . . .	271	212
Public Works Administration . . . . .	165	129
	<u>1,837</u>	<u>1,515</u>

In July 1936 interest rates on loans granted by the Reconstruction Finance Corporation were reduced, loans to banks from 4 to 3 per cent. and other loans correspondingly; from October the rate of interest payable by banks on preferred stock, notes and debentures held by the Reconstruction Finance Corporation was also reduced to 3 per cent.

There has been, especially in the opening months of 1937, some hardening of short-term rates in New York, where certain rates in the past few years had been excessively low. A measure of the firming-up is given by the following characteristic examples: stock exchange call loans rose from  $\frac{3}{4}$  per cent. early in 1936 to 1 per cent. in June, and 90-day bankers' acceptances from  $\frac{1}{8}$  to  $\frac{3}{16}$  per cent. in July 1936, to  $\frac{1}{4}$  per cent. in January,  $\frac{5}{16}$  per cent. in February and  $\frac{7}{16}$  per cent. in March 1937; U. S. Treasury bills (273 days) were placed at  $\frac{1}{4}$  per cent. and under in 1936 while a gradual increase of the rate from the beginning of 1937 brought it up to 0.7 per cent. at the end of March.

The new central banks in Canada, New Zealand, India and the Argentine, with bank rates between 2 and  $3\frac{1}{2}$  per cent., have had to meet few or no calls for rediscount facilities, in fact, the commercial banks in each country are in an exceptionally liquid condition. In Canada the banks have double the minimum cash and reserves balances required by law, in New Zealand and India three times the required reserves. The cash reserves of the banks in the Argentine have not risen appreciably above the legal minimum although the gold and foreign exchange reserves of the Banco Central have increased by 170 million pesos during the year. As explained in the last Annual Report the Banco Central had 400 million Consolidated Treasury 3 per cent. bonds at its inception in May 1935, of which 180 million had been sold on the market by December 1935. During 1936 the balance of 220 million was also sold to mop up the surplus cash of the banks. It was reported early in 1937 that any further influx would be offset by sales of Treasury bills. Bank rate has been maintained at  $3\frac{1}{2}$  per cent. while the rate for non-rediscountable Treasury bills, the monthly tender for which has become a regular feature in Buenos Aires, declined during the year to December when 30-day bills were placed at 2 per cent. and 90-day bills at  $2\frac{1}{2}$  per cent.

The Reserve Bank of India maintains its official discount rate at 3 per cent., which is, however, out of touch with the market, where the average rate for Treasury bills in 1936 was below  $\frac{3}{4}$  per cent. Similarly in Canada, where the Bank of Canada has kept its rate of  $2\frac{1}{2}$  per cent. unchanged, the Treasury bill rate fell from  $1\frac{1}{4}$  per cent. at the beginning of 1936 to under  $\frac{3}{4}$  per cent. in December. During the year the cash balances of the banks have been increased as the result of purchases of securities by the central bank. Money is increasingly easy and the banks have discontinued the practice of allowing interest on current accounts, while the rate on savings deposits has been reduced a further  $\frac{1}{2}$  per cent. to  $1\frac{1}{2}$  per cent. Lending rates have also declined but advances against collateral, for example, still cost from 5 to 6 per cent. to the borrower. The Reserve Bank of New Zealand Amendment Act of April 1936 under which the Reserve Bank was nationalised also extended the possibilities for the State and State undertakings to borrow at the bank. The amount of advances to the State and State undertakings were increased from nil during the first half of the year to £NZ 8 million in December 1936, and the bank also added £NZ 1 million to its investments. In the course of the year the note issue rose by £NZ 3 million and bankers' balances by £NZ  $1\frac{1}{2}$  million and during the same time the reserve of sterling fell by £NZ 5 million. The actual reserve balances of the commercial banks amounted at the end of 1936 to £NZ 11 million, while the legal minimum required under the law was less than £NZ  $3\frac{1}{2}$  million. By virtue of the Amendment Act mentioned above the Governor of the Reserve Bank, "acting with the authority of the Minister of Finance", has power to increase the required reserves of the banks. Bank rate was lowered from  $2\frac{1}{2}$  to 2 per cent. in the middle of the year 1936.

The South African commercial banks have long had large excess reserves at the Reserve Bank. In 1932 the banks just covered their legal requirements of £SA 4 million. The gold standard was suspended at the

end of December 1932 and in the next few months the bankers' balances rose above £SA 20 million. In February 1936 they touched their highest point at £SA 33 million, some four times the legal minimum of rather under £SA 8 million, but declined rather rapidly to under £SA 18 million in September. In the six months ending 30th September 1936 the banks took up £SA 8 million securities. As mentioned in the next section the government raised an internal loan to repay maturities in London, thus relieving at the same time both the internal and external plethora of available funds. But the bankers' balances soon increased again to more than £SA 20 million and continued to rise in the early months of 1937. Bank rate remains unchanged since 1933 at 3½ per cent.

Although the rate for advances of the Commonwealth Bank of Australia at 4¼ per cent. has not been changed since 1934 there has been a perceptible stiffening of short-term rates in the country, as is shown by the increase in March 1936 from 1 to 2 per cent. for three-months' fixed deposits at the Commonwealth Bank itself. The hardening of rates is due to a continued expansion of lending by the trading banks, which has not had the encouragement of the Commonwealth Bank. With depleted cash and other liquid assets the trading banks' position has become tighter and their overdraft rates have been increased to 5½ per cent., although recently some relaxation of the position is apparent as a result of the more favourable development of the export markets.

Bank rate in Japan was reduced from 3.65 to 3.29 per cent. in April 1936, open-market rates in Tokio and the bankers' deposit rates also declining during the year. Money was easy throughout the year, the February (1936) incident having had only a passing influence.

Although short-term interest rates in certain markets have recently stiffened somewhat, the general characteristic has been a high degree of liquidity permeating the credit systems. The accumulation of reserve balances by commercial banks has in many centres been very great; in some cases extraordinary measures have been taken to reduce the basis of credit already existing and to prevent dangerous additions in the future. It is notable that the system of requiring by law a minimum percentage of cash reserves, which was originally introduced in order to ensure that the banks should maintain a sufficient degree of liquidity, is being converted into a weapon to reduce the liquidity of the banks. In many respects, however, the present situation is wholly unprecedented; never before has an attempt been made on so large a scale to immobilise cash balances and particularly to neutralise the effects of gold acquisitions. Action is being taken that aims at a restriction of the volume of credit, while the price to be paid for credit (the rate of interest) has so far hardly been raised.

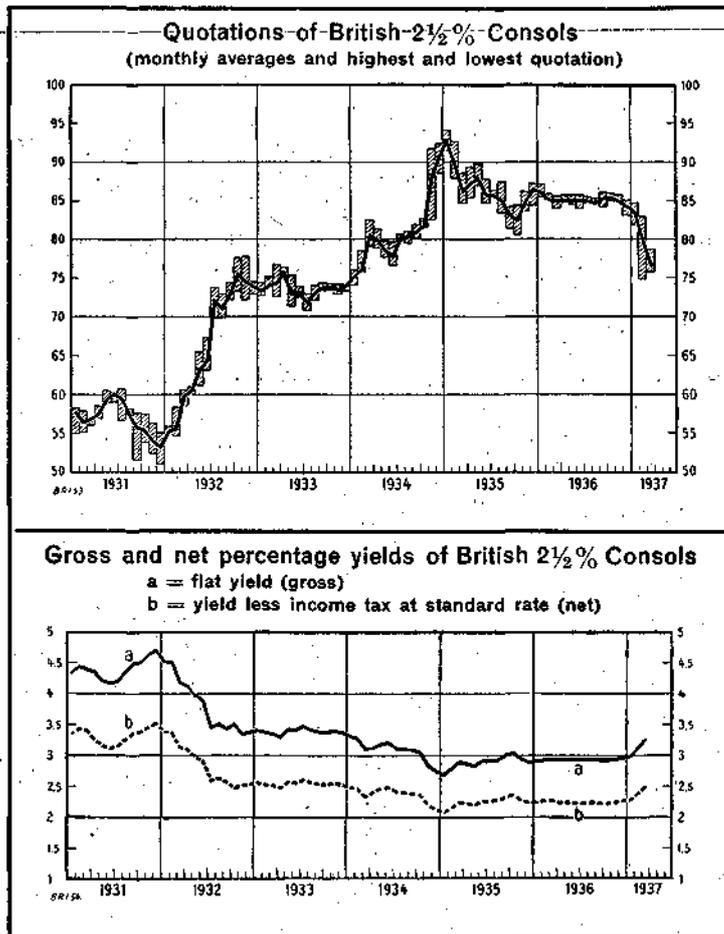
## 2. LONG-TERM MARKETS.

The recent tendency of long-term interest rates has been towards a reduction of the difference existing between the levels ruling in the various parts of the world. While in recent months a stiffening of yields on long-term

government obligations was noticeable on the British, American and some other markets where rates were already relatively very low, the conversion of debt to lower interest levels has continued in a great number of other countries where the downward movement had not previously been so pronounced.

The highest quotations of British government securities were reached in January 1935 when a false peak was made by over-optimistic buying; after a recession lasting for about nine months there was a period of comparative stability during the year 1936. An abrupt weakness on the gilt-edged security market occurred early in 1937, when in a few weeks the yield on British government securities rose by nearly  $\frac{1}{2}$  per cent. This weakness may be attributed to a number of causes affecting the movement of funds on the market; psychologically, the announcement of the borrowing to be undertaken for the execution of the armaments programme no doubt had a marked influence on investors. The following graph shows the quotations of  $2\frac{1}{2}$  per cent. consolidated stock (Consols), which on account of its standing and irredeemability is a very sensitive barometer of market conditions in London. This stock fell 10 points in the first two months of 1937, whereas in the whole of 1936 the range was only  $4\frac{1}{2}$  points. At the lowest quotation of 74

touched in February 1937, Consols were 20 points below the high peak of January 1935 (which approximately marked the close of the heavy commercial bank buying of securities) and back to the level at the beginning of 1934. The behaviour of other long-term fixed-interest stocks was not so temperamental but was influenced by the same fundamental trend. Stiffer terms for long-term borrowing in London were already foreshadowed in November 1936 when £100 million  $2\frac{3}{4}$  per cent. funding bonds of 16-21 years were issued at  $98\frac{1}{2}$ . These terms were distinctly more unfavourable to the Treasury



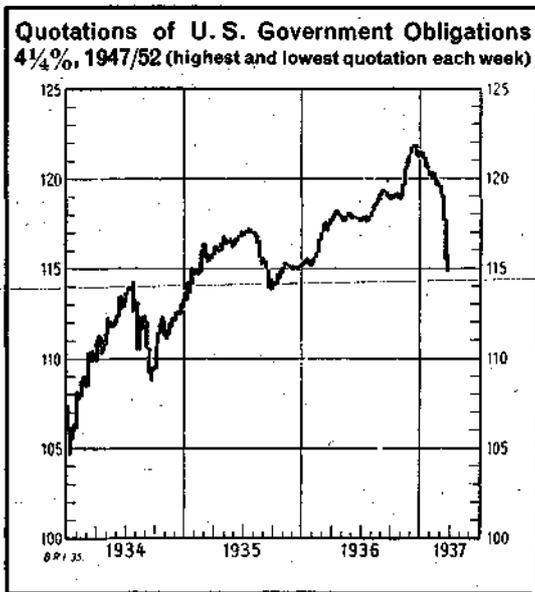
than those of the £200 million loan of December 1935 when a 2½ per cent. issue of 20–25 years' maturity was offered at 96½. This earlier loan was, however, largely absorbed by official and semi-official institutions and, in spite of increases of the "tap price" (i. e. the price at which securities are offered to the market by some official or semi-official body) in preparation for the new issue, the quotation in November 1936 stood 3 points below the original issue price.

In the United States the yield of Treasury bonds continued to decline during 1936, the reversal of the trend occurring only in the first quarter of 1937. The average yield for all outstanding Treasury bonds due or callable after the lapse of eight years fell from 2.73 per cent. in December 1935 to 2.27 per cent. in December 1936. When comparisons of rates are made between New York and London, it is important to remember that United States government securities carry tax-exemption rights, while for the holder of British government securities the effect of income tax on the yield is considerable, as can be seen from the graph on the preceding page. During the year the Treasury proceeded with its programme of debt consolidation. The short-term debt of notes, certificates and bills was reduced by \$1,800 million to \$13,100 million, notwithstanding an increase in the total interest-bearing debt by \$4,100 to \$33,700 million. Meanwhile bond maturities were lengthened:

issue date	maturity
1935 September . . . . .	10–12 years
1936 March . . . . .	12–15 "
" June . . . . .	15–18 "
" September . . . . .	20–23 "

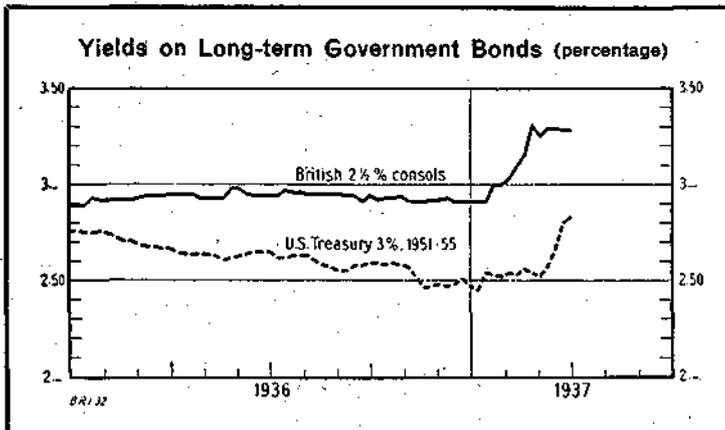
The rate of interest was 2¾ per cent. in each case. In December 1936, however, bonds were issued at 2½ per cent. with a maturity of only 13 to 17 years, and another issue on similar terms was made for conversion purposes in March 1937. By that time high-grade bonds had already begun to feel the change in market conditions and the municipal bond market, in particular, had been suffering from some indigestion of new issues. At first government bonds were not affected but the spread between yields was becoming wider. Several factors influenced the market: short-term rates in New York showed signs of stiffening; preparations were made for the coming into force of the latest measures reducing excess reserves of member banks; and a certain psychological effect was also produced by the downward adjustment of the gilt-edged market in London. But whereas the investments of the eleven London clearing banks grew by £30 million in the six months ending January 1937, after an increase of only £10 million in the previous six months, all member banks of the Federal Reserve System, after increasing their holdings of U. S. government obligations (direct and indirect) by \$1,400 million in the first half of 1936, showed a decrease of over \$125 million in the second half of the year. New York banks sold \$555 million, while other banks bought \$430 million. Reductions of bank holdings of U. S. government obligations continued in 1937: the weekly reporting member banks showed a fall of \$885 million in the first three months of 1937 compared with \$320 million in

the last six months of 1936: the decline since the beginning of 1937 has been registered at outside banks as well as in New York and in February and March selling came from other holders as well as the banks. The Federal Reserve banks have recently increased the proportion of U. S. government bonds they hold (\$635 million end March 1937 against \$265 million a year earlier) in their total holding of \$2,430 million U. S. government obligations at the expense of shorter-dated notes and bills. Early in April 1937 the Open Market Committee of the Federal Reserve Board announced that, "with a view to exerting its influence toward orderly conditions on the money market" and to facilitating the orderly adjustment of member bank reserves to the new requirements, open-market purchases of U. S. government obligations would be made "in such amounts and at such times as may be desirable". In the first two weeks



of April 1937 the Reserve System added \$56 million to its holding of U. S. government obligations, thus increasing the total of its holdings of these securities for the first time for more than three years. As an example of the general trend of the market, it may be mentioned that the 4 1/4 per cent. bonds 1947/52 declined from the highest point ever reached, namely 121 7/8, on 12th December 1936, to around 120 in February, and then fell abruptly to 115 at the end of March and 113 1/2 (the lowest since the end of 1934) on 2nd April 1937. On this day the 2 1/2 per cent. issue previously mentioned touched 96 1/4 compared with 101 3/4 in the second week of February 1937.

Some \$14,000 million of the United States interest-bearing government debt of \$33,700 million at the end of 1936 will mature within the next five years. It has recently been pointed out that almost the whole of the U. S. government debt will come to maturity within twenty-five years, whereas in England about 70 per cent.



of the internal government debt is either uncallable by the holder or of longer maturities, a further factor which makes international comparison of long-term interest rates extremely difficult. With appropriate reservations as to comparability, the accompanying graph gives

the trend of the yields of Consols (gross) in London and of 3 per cent. U. S. Treasury bonds 1951/55 in New York since the beginning of 1936.

Continued consolidation of floating debt has further characterised the capital market in Germany, where available savings have been carefully canalised into government securities. In July and November 1936 and February 1937 issues of  $4\frac{1}{2}$  per cent. Treasury bonds were made of RM 700, 600 and 700 million respectively at  $98\frac{3}{4}$  with an average life of nine years. Altogether about RM 5,000 million of the short-term debt of the Reich has been consolidated since 1933, but the amount still outstanding is considerable. At the beginning of 1937 the ban on new industrial issues was lifted for comparatively large amounts needed by companies working under the Four-Year Plan. In addition, a Prussian RM 200 million  $4\frac{1}{2}$  per cent. loan was floated in December 1936 at  $97\frac{1}{4}$ — $97\frac{1}{2}$ , of which RM 40 million was for new money.

The reflux of funds after devaluation into the Netherlands and Switzerland greatly eased the position of the capital markets in these countries, bringing the long-term rate of interest in both cases down to a level of 3 to  $3\frac{1}{2}$  per cent. by the end of 1936 and thus providing a basis for future conversions of government securities. Even before the devaluation a 3 per cent. loan for defence was issued at par on the Swiss market and oversubscribed, but in this case patriotic motives and tax-exemption rights made a special appeal to the public.

The persistency with which French capital has been exported and has remained abroad greatly complicates the problem of lowering the long-term interest rate in France. In December 1936 a convention was signed whereby Fcs. 3,000 million of the book profit from the revaluation of the gold holding of the Bank of France was allocated by the government to the Crédit Foncier so that the latter institution could reduce the rates charged on its loans as follows:

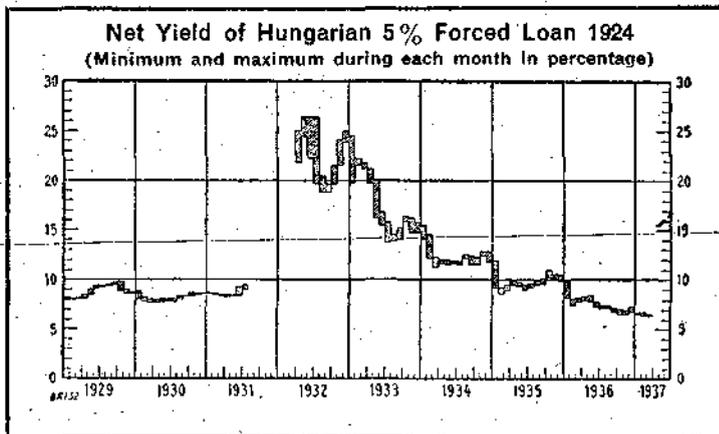
- for loans to public bodies from 6.80 per cent. previously ruling to 5.00 per cent.;
- for loans on landed property from 8.05 to 6.30 per cent.; and
- for maritime loans from 8.45 to 6.70 per cent.

The reduction of ten per cent. from the coupons of rentes and other government securities instituted by decree in July 1935 was abolished, with certain conditions, by the Finance Act of December 1936.

In March 1937 a  $4\frac{1}{2}$  per cent. 60-year National Security Loan of Fcs. 5,000 million was issued at 98 with special conditions (as to payment of interest and principal at the option of the holder) which guaranteed the exchange rates in sterling or dollars at those near the level existing when the loan was floated (sterling 106.95 francs and dollar 21.90 francs). This loan was immediately oversubscribed and a further tranche of Fcs. 3,000 million was issued a week later. The yields on French rentes, after a slight improvement in October 1936, were again early in 1937 as high as they had been a year previously. On the one hand, the capital market was strained by an outflow of funds and, on the other hand, it was exposed to continuous borrowing by the government to cover budget deficits and extra-

budgetary expenditure. Including the accumulated debts of the railways, the French government internal debt has increased by some 40 per cent. in the past six years.

In Czechoslovakia also a defence loan was issued in the course of 1936. It was divided into two categories —  $4\frac{1}{2}$  and 3 per cent. issues at 97 redeemable by drawings in the years 1938–87, the bonds bearing the lower interest rate having certain taxation privileges. Subscriptions to these issues exceeded Kc. 4,000 million. In Belgium a  $3\frac{1}{2}$  per cent. 60-year government loan for B.fcs.1,500 million was issued on 1st March 1937 at 97, following a 4 per cent. issue in the autumn of 1936. A number of Swedish pre-war loans have been converted from  $3\frac{1}{2}$  to 3 per cent. levels, involving some redemptions of amounts held abroad. In Hungary the yield of the forced loan of 1924 (as calculated from the prices quoted in private dealings) fell below 8 per cent. in



1936 for the first time since the closing of the stock exchange in the summer of 1931. This favourable development was attributable to an improvement in the general economic position reflected inter alia in increased tax receipts and the consequent cessation of Treasury issues on the market.

Among extra-European countries a series of conversion operations have been carried out during the past year in Japan, over Yen 2,000 million of 5 per cent. exchequer bonds having been replaced by  $3\frac{1}{2}$  per cent. bonds issued slightly under par. By January 1937 the average yield of government bonds had declined to 3.9 per cent. compared with 4.3 per cent. a year previously. In Japan the internal government debt has been doubled during the past six years, as has also been the case in the United States. In both these countries commercial banks and savings banks, which found little outlet for their funds during the depression, have substantially increased their holdings of government bonds, but the power of absorption of the banks may become quickly restricted when, with returning business activity and higher prices, the demand for capital increases.

In India long-term market rates continued to decline in 1936 to very low levels. The yield of the 4 per cent. government loan 1960–70, for example, falling from 3.4 per cent. in December 1935 to 3.1 per cent. in December 1936; but early in 1937 government securities weakened in sympathy with conditions in London. In May 1936 the Indian Government was able to issue successfully a 12–16 year internal loan for Rs. 12 crores (equivalent to £9 million) new money at the low rate of  $2\frac{3}{4}$  per cent. The greatly improved economic conditions in the Argentine during the year and the firmness of the

market enabled the government to float an issue of 100 million pesos at 4 per cent. in December 1936, the lowest rate in the history of the Republic for such an issue. In Australia, on the other hand, long-term interest rates tended to increase during 1936, as may be seen from the following table:

Date of issue	Amounts in £A millions	Terms				Result
		interest per cent	price	years maturity	yield per cent	
1935 November . .	7½	3¾	99¾	14	3.775	over-subscribed £A 0.3 million
1936 June . . . .	9	3¾	98½	15	3.875	under-subscribed £A 1.8 million
1936 November . .	7½	3¾	97½	15	3.967	under-subscribed £A 2 million

In April 1937 the Loan Council approved a further issue of £A 7½ million 37/8 per cent. bonds at 99½.

According to the report of the Commonwealth Bank for June 1936, the firmer tendency may be attributed largely to the growing demands of Australian industry for new capital. Rates are also becoming somewhat firmer in New Zealand, where a government issue (3½ per cent. for 20 years, or 3 per cent. for 4½ years) for £NZ 13.9 million in January 1937 (partly for conversion purposes and partly to obtain new cash) was undersubscribed by nearly £NZ 3 million.

Adjustment of interest rates to lower levels has also been made in respect of foreign obligations, although in this field conversion operations have as a rule been limited to issues on which the service has been maintained in full during the depression. Of first importance has been the Argentine conversion plan affecting the whole of the country's outstanding dollar debt. In the years 1933 and 1934 conversions of the internal Federal debt were made and in 1934 and 1935 some £15 million bonds were converted on the London market from a 5-5½ per cent. basis to 4½ per cent. In October 1936 the debt outstanding in the United States amounted to \$236 million, composed chiefly of 6 per cent. bonds issued between 1923 and 1928. A first issue of \$23½ million 4½ per cent. 35-year bonds was made at 92½ for conversion purposes in November 1936. The success of this operation made it possible to issue a second conversion loan of \$70 million 35-year bonds in February 1937 at the reduced rate of 4 per cent. and at an issue price of 91; a further \$35 million 4 per cent. 35-year issue was announced in April 1937, the greater part at 89½. In addition \$118 million in cash have been supplied out of the country's own resources. The whole of the dollar debt has now been cared for, twenty years and more before the final maturity dates — about half being repaid in cash and half covered by conversion issues at low interest rates. Moreover, the Argentine Government has called certain provincial dollar bonds, carrying interest at 7 per cent., and has made arrangements to repay small outstanding loans in French francs and gold pesos. Advantage was also taken of the enhanced credit of the government to convert on the London market in October 1936 certain 4 per cent. railway bonds,

amounting to £2½ million, into a 35-year government loan at 3½ per cent., the conversion terms corresponding to an issue price of 84½ per cent. With the completion of present plans, the whole external debt of the Argentine, amounting to the equivalent of some £100 million, will be on a 4 to 4½ per cent. basis.

The Belgian Government in the years of violent currency fluctuations (1924/26) raised a number of foreign loans totalling \$230 million at heavy rates of interest. Of the total, \$180 million were obtained on the American market and the equivalent of \$50 million (half of the 7 per cent. Stabilisation Loan of 1926) on European markets. In May 1935 \$99 million of the \$180 million originally placed on the American market were stamped and converted into 4 per cent. internal franc bonds (giving a measure of the repatriation to that date) in addition to normal retirements by sinking fund. At the end of August 1936 the position of the American loans was as follows:

	\$ millions
Amount converted in May 1935	99
„ retired	37
„ outstanding	44
	<hr/>
Total	180

On 1st November 1936 the Belgian Government repaid the remaining dollar bonds of the Stabilisation Loan and at the end of the year only \$30 million dollar bonds were still in circulation. The English, Dutch and Swedish tranches of the 7 per cent. Stabilisation Loan were also put on to a 4 per cent. basis during the year and the Swiss tranche was repaid. In addition, certain short-term foreign debts of the government and of the Belgian Congo were repaid, bringing the total repayments during the year 1936 on various foreign markets up to B.fcs.1,450 million (say, \$50 million).

Further progress has also been made by the Government of Finland in repaying foreign debts contracted at high rates of interest. Notice of repayment was given for 1st September 1936 to holders of the 6½ per cent. dollar loan of 1926. This loan was originally for \$15 million but by the date it was called only \$12.8 million remained outstanding, of which more than a third was held in Finland; a 4½ per cent. internal 30-year loan for Fmk.400 million was issued at 98½ to raise the necessary funds for redemption. By successive repayments the Finnish Government foreign funded debt was reduced from a total equivalent to \$76 million at the end of 1930 to \$39 million at the end of 1936. During the same time the total government debt, internal and external, was reduced from the equivalent of \$90 million to \$82 million, but foreign loans were replaced to such an extent by domestic issues that the proportion of foreign debt in the total fell from 90 to less than 50 per cent.

On 1st February 1937 the outstanding balance of \$20 million of the United Kingdom \$144 million 5½ per cent. bonds of 1917 was repaid. Some \$90 million Canadian Government 5 per cent. bonds were repaid on 1st March 1937 as to \$7½ million in cash and as to \$82½ million with the proceeds from two new issues — \$30 million 7-year 2¼ per cent. bonds issued at 99½ and \$55 million 30-year 3 per cent. bonds at 98. The Finance

Minister in his 1937 budget speech stated that \$255 million Canadian bond and debenture holdings abroad (of all kinds) had been retired in 1936, and, as only \$110 million had been re-financed (at prevailing low interest rates) through the sale of new issues mostly in the United States, foreign indebtedness had been reduced by \$145 million. In January 1937 the Norwegian Government raised a 4 per cent. 26-year loan for \$29 million at  $98\frac{1}{4}$  to repay the 5 per cent. \$30 million loan of 1928.

Very large repayments of old loans have also taken place on the London market during the year out of the debtor countries' own resources. The governments of India and South Africa together repaid some £35 million in 1936, India redeeming the £16.8 million  $5\frac{1}{2}$  per cent. stock of 1936/38 and South Africa repaying the £18.5 million domiciled in London of the  $3\frac{1}{2}$  per cent. 1929/49 and 4 per cent. 1936 loans, funds being raised in both cases by internal issues. The government of Sweden has given notice to redeem early in 1937 some £3 million of pre-war loans, of which less than half is in foreign hands. The amount of Swedish Government bonds held abroad is now insignificant.

Nowhere in the world are there any real signs of a revival of new long-term capital issues for foreign countries. Not only lending to public authorities but also direct investment in new enterprises have remained at minimum figures. In the United States new foreign issues amounted to \$20 million in 1936, as compared with \$1,330 million in 1927 and in England foreign issues (for countries outside the British Empire) were only £3 million in 1936 as against £56 million in 1927 — even for British overseas countries, the total new issues amounted to only £28 million in 1936 as compared with £95 million in 1927. Loans totalling Sw. Kr. 75 million were made in Stockholm during the year for Norway and Denmark, the amount issued being more than twice as high as in the previous year. A Franco-Polish financial agreement was signed in September 1936 covering a total of Fr. fcs. 2,600 million, of which 2,060 million represents a loan to the Polish State and 540 million bonds to be issued on the Paris market for the Franco-Polish Railway Company with the guarantee of the Polish Government. The loan to the Polish State is to be 810 million in cash and the remainder in various goods credits, the utilisation of the loan to be spread over four years. The loan is to be repaid partly in 15 and partly within 35 years, the average interest rate being  $5\frac{1}{4}$  per cent.

A number of countries, which ten years ago were in need of foreign capital, now possess sufficient resources not only to finance their domestic requirements but also to redeem part of the foreign debt previously incurred. In other directions difficulties with regard to existing loans have made new borrowing impossible, and prevailing uncertainties of a monetary or political character have also put a check to foreign lending. Legal and administrative conditions in some of the lending countries also affect the situation. In the United States there has been no modification of the Johnson Act, which restricts the foreign lending of that country. In April 1936 the British Chancellor of the Exchequer appointed a Committee to advise him on particular applications for foreign loans in London and on the principles which

govern the ban on foreign lending, which has been in force since 1932. In March 1937 the Chancellor stated that he concurred in the Committee's opinion, which had recently been communicated to investment trust companies, that such companies proposing to make new issues in London should confine the proportion invested abroad "to the minimum necessary to the conduct of the business in accordance with the ordinary practice of investment trusts", and, further, that if the actual proportion were "unusually high" it should be reduced as occasion might serve. Since this announcement further detailed provisions have been made.

A situation has now arisen in which the redemptions, repayments and repatriations of old foreign loans greatly exceed the amount of new issues on foreign account on the American, British and probably other lending markets. There have, indeed, been large capital movements, as described in the previous chapter, for the purchase of bonds and shares on foreign markets, but this involves merely the acquisition of existing capital assets. Such transactions do not, unfortunately, give rise to a movement of commodities to the countries receiving the capital funds to the same extent as do new issues on foreign account, whether for public works or for industrial investment. The small volume of foreign issues is, therefore, one of the reasons for the depressed level of international trade.

The requirements of new capital for domestic purposes have risen on the British market during the past three years and on the American market particularly in 1936, while in other centres shown in the following table the degree of activity is still at a low ebb.

Internal new capital issues on private and industrial account (excluding all government and similar issues and conversions)					
Year	U. S. A.	England	France	Switzerland	Netherlands
	in millions of national currencies				
1927	4,660	121	7,000	287	81
1928	5,350	159	9,900	322	281
1929	8,000	135	14,700	529	259
1930	4,480	93	20,500	269	107
1931	1,550	33	14,200	302	26
1932	325	77	5,300	121	14
1933	160	70	3,200	114	8
1934	180	91	3,100	122	28
1935	400	141	2,100	117	5
1936	1,190	166	1,150	52	9

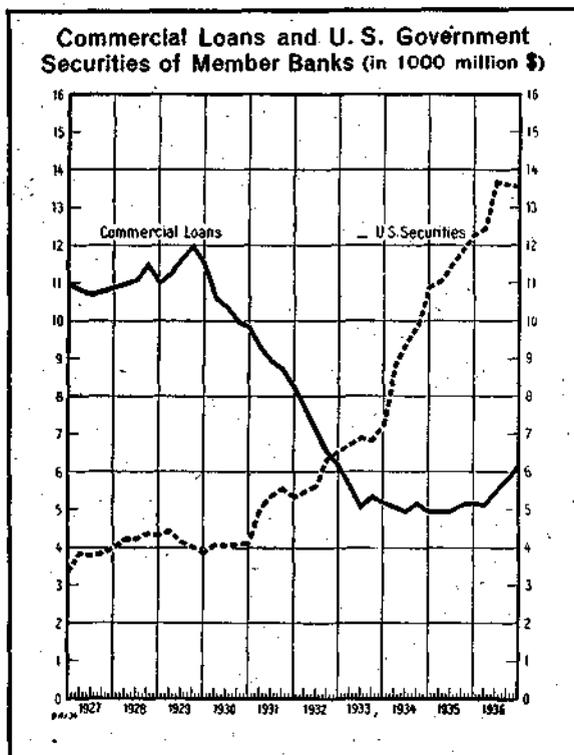
In the United States the amount issued in 1936 was still low compared with pre-depression standards. The market was mostly occupied with re-funding issues, which reached the record of \$3,385 million, compared with an annual average of \$1,250 million in the years 1925/29. According to the above table new home industrial issues in England were as high in 1936 as in the exceptional year 1928. In fact, there are reasons to believe that the increase was even greater than the figures suggest. The usual statistics of

capital issues are compiled from prospectuses and do not include "placing" of new capital by way of the stock exchange instead of making a direct offer to the public by way of a prospectus. Calculations have been made showing that over £200 million was raised for industrial and other companies in this way in 1936 compared with £100 million in 1935. Unfortunately, figures for earlier years are not available, but there can be little doubt that "placings" are now considerably higher than previously. While a direct flotation must be made on a given date, when some temporary influence may spoil the market, an issue placed on the stock exchange may be retailed at the most favourable moment. Somewhat similar tactics have been observed with recent government loans when the direct issue has been largely subscribed from the cash of public departments and semi-official institutions and later distributed as occasion offered through the mechanism of the stock exchange. Refunding and conversion of home industrial issues, which was active at over £60 million in 1933 (following the stimulus to lower rates given by the war loan conversion of the previous year), fell off in 1936 to under £30 million.

The first large loan on the Italian market since the summer of 1935 was made when 900 million lire 4½ per cent. 20-year participating bonds were issued by the Istituto per la Ricostruzione Industriale at 99, four hundred million lire being placed privately and the balance offered for public subscription.

In the course of the year there have been large purchases of shares and rising quotations on stock exchanges in a wide range of countries. The demand for government securities and other fixed-interest obligations has, to

a considerable extent, emanated from such institutions as insurance companies and savings banks, which by the nature of their activity are more or less excluded from investment in equities. By legal enactments commercial banks in many countries have been precluded from holding shares and participations. In so far as these institutions have increased their investments, therefore, they have bought bonds (mainly government securities) and in many countries have in that way been a factor in government financing and in the downward adjustment of interest rates. There is however, a limit to the absorption of securities by banks, and this is especially true when growing activity and higher prices produce increased



calls on the banks by trade and industry, which have passed the stage in recovery characterised by the unfreezing and repayment of old bank advances. In addition, funds accumulated in the hands of industrial and commercial concerns above the amounts needed in the depression, which were often applied in the purchase of government securities, now become employable in the business. The Federal Reserve Bulletin for February 1937 points out that as regards the United States the outstanding banking developments for 1936 were "a considerable growth, for the first time since 1929, of commercial borrowing from the banks, the cessation of the large growth in the banks' holdings of U. S. Government obligations, and a further large increase in deposits".

## VI. DEVELOPMENTS IN CENTRAL AND COMMERCIAL BANKING DURING THE YEAR.

The recovery in business, extending to almost every country in the world, is reflected in a general improvement in the liquidity and solvency of credit institutions. There is no longer the need for public authorities to intervene in the way they did during the depression when in a great many countries assistance was given not only in the form of direct financial help but also by the formation of new institutions to give liquidity in place of frozen assets, government guarantees for deposits and various partial or total moratoria. On the contrary, many emergency measures have either lapsed or become superfluous, whether legally abolished or not. As regards the more permanent banking legislation, new comprehensive laws governing commercial banks have been adopted in Turkey, Venezuela and Costa Rica; but elsewhere the measures taken during the year have had reference to some particular section of the credit system as, for instance, the position of the central bank or the management of public or semi-public institutions. There are certain signs of the fact that with returning recovery a new set of problems arises, in that measures have been authorised aiming not at an increase but at a curtailment of too great liquidity of commercial banks (the imposition of increased cover requirements for deposits and the adoption of restrictive open-market operations).

Typical of the liquidation of the special crisis measures adopted in the depression is the repayment of emergency financing; for example, German banks have now entirely repaid the emergency credits they received and in April 1936 the Skandinaviska Kreditaktiebolaget in Sweden repaid the last portion of the government assistance it obtained in 1932. Equally typical is the gradual freeing of the banks from direct and indirect State ownership exemplified in Germany by the re-sale of the government's shareholding in the Deutsche Bank und Disconto Gesellschaft, the whole of the shares of this bank being now in private hands, and in the United States by large repayments by the banks of preference shares previously taken up by the Reconstruction Finance Corporation. Of particular interest is the formation in Belgium of a special "office for the liquidation of emergency interventions". This office will centralise the administration of credits previously granted with the guarantee of the State and further their progressive liquidation. In general, the number of bankruptcies and liquidations of banks is now low even in comparison with the pre-depression period. In Switzerland, a few more cases occurred of the application of the Federal Bank Law of 1934, granting such measures as the lengthening of the maturity dates for certain debts, but the reflux of capital to the Swiss market in the last quarter of 1936, as well as the upturn in business, has generally improved the position of the banks. Where in the course of the year State assistance has been given to start new credit institutions (e. g. in Norway and Egypt) it has been a question not of emergency measures but of establishing institutions of a permanent character.

In the sphere of central banking, some important changes have been effected during the year in the relations between certain central banks and their respective governments.

By the Law of 7th April 1936 the Nationalbank i Kjøbenhavn was transformed into Danmarks Nationalbank on the basis of a proposal that had been elaborated two years earlier. It is interesting to recall that the bank of issue which became the Nationalbank i Kjøbenhavn was founded as a State bank in 1813; after operating for five years in this way, it was changed into a private shareholders' bank, was thus made independent of the State and functioned in this form for over 100 years. In 1936 it was again nationalised, the shareholders being bought out by an allocation of bonds (at twice the nominal value of the shares) and the government providing a general capital fund of Kr. 50 million in the form of a certificate which will gradually be written off by certain allocations out of annual profits. The interest on the bonds is charged to the working account of the bank before the yearly profits are calculated.

The management of Danmarks Nationalbank is in the hands of a board of directors, a committee of directors and a board of governors. The board of directors consists of twenty-five members: eight of them are members of, and elected by, the Riksdag (while none of the remaining seventeen members may be from the Riksdag); two members are appointed by the Minister of Trade, Industry and Shipping, one of them must be an economist and the other a lawyer; and the fifteen other members, who must have a thorough knowledge of trade, are elected by the entire board of directors. Due regard will be paid to the principle of establishing a comprehensive representation of the various trades (also of the workers occupied in them) and of securing a representation of geographical divisions of the country. The committee of directors is composed of seven members and is a delegation of the board of directors. Finally, the board of governors consists of three members, one nominated by the King and the two others by the board of directors. When the transformation from the old to the new bank was effected, a large measure of continuity was maintained. All the members of the board of the Nationalbank i Kjøbenhavn, except one who expressed the wish to retire, were appointed members of the new board of directors of Danmarks Nationalbank. Moreover, no change was made in the main lines of the monetary policy; in particular the open-market policy of selling bonds, which had been inaugurated early in 1935 by the Nationalbank i Kjøbenhavn, was continued by the new bank.

Even more fundamental changes have been made in the constitution and working of the Reserve Bank of New Zealand. This bank was founded in 1934 as a private shareholders' bank constituted on commonly accepted lines; it was managed by a board consisting of the governor and deputy-governor, both appointed by the government, four "shareholders' directors" elected by the shareholders' meeting, three "State directors" appointed by the Governor General, and in addition the Secretary of the Treasury as ex-officio member without voting rights. By an Amendment Act that came into force in April 1936, the Reserve Bank was nationalised, the

shares being cancelled and the holders given in exchange government stock or cash computed on the market valuation of the shares. While under the Act the existing members of the Board continue to serve, provisions were made for their successive retirement; the distinction between shareholders' directors and State directors was abolished and all appointments are made at the pleasure of the government. Moreover, the Secretary of the Treasury, as member of the Board, was given the right to vote at meetings.

The main function of the Reserve Bank within the limit of its powers as defined by the new law is "to give effect as far as may be to the monetary policy of the government as communicated to it from time to time by the Minister of Finance". In carrying out its functions the bank is authorised to "regulate and control credit and currency in New Zealand, the transfer of moneys to and from New Zealand, and the disposal of moneys that are derived from the sale of any New Zealand products and for the time being are held overseas". The bank was more particularly given authority to underwrite any loan proposed to be raised by the government, to make advances against Treasury bills up to a maximum equal to the full amount of estimated revenue for the year, and to finance the purchase and marketing of New Zealand produce for account of the government or any special body entrusted with such purchase and marketing. (It should be mentioned that new powers were obtained by the government under another law to make special arrangements about the ownership and marketing of any primary products produced for export, and that these powers have been used with regard to butter and cheese.) Furthermore, the Governor of the Reserve Bank, acting with the authority of the Minister of Finance, was given the right to alter the minimum cash reserve requirements of commercial banks, it being stipulated, however, that the minimum balances at the Reserve Bank should amount to at least 7 per cent. of the demand liabilities and 3 per cent. of the time liabilities in New Zealand (i. e. the percentages already existing under the old law). Finally, provisions were made for more information to be furnished to the Reserve Bank, especially as to the aggregate amount of overdraft facilities granted by the commercial banks to their customers.

Certain important changes, though less far-reaching than in the case of New Zealand, were made in the ownership and administration of the Bank of Canada by the Law of 23rd June 1936. This bank had been established in 1935, the capital being wholly in the hands of private shareholders but the governor and deputy-governor being appointed by the government. Under the new law the bank remains a corporate body, but an increase was made in the capital of the bank by the issue at par of 102,000 class B shares to the Minister of Finance to be held by him on behalf of the Dominion of Canada, while the old shareholders remain (as holders of class A shares). The directors holding office at the time this change was made continued in office until the expiration of their mandate, but, as the holder of the class B shares, the Minister of Finance, with the approval of the Governor in Council, is entitled to appoint to the Board of the Bank six directors, each of whom has two votes, prior to the annual general meeting in 1940, at which time the number of directors elected by class A shareholders will have been reduced to three.

In the course of the year the administration of the Bank of France was subject to important changes. By the Law of 24th July 1936 the Regency Council, the members of which were appointed by the two hundred largest shareholders, was replaced by a General Council composed of the governor, the two deputy-governors, twenty councillors and three censors, the last-mentioned having the right to partake in the discussions but no vote. The new provisions aim at a varied representation of different interests in the General Council. Thus two of the councillors are appointed by the shareholders from among industrialists, manufacturers or merchants (with the exclusion, however, of all persons connected with banking establishments) and one by the Superior Commission of the Savings Banks; one councillor is elected by the personnel of the Bank of France, one by the National Economic Council from among its vice-presidents, six are chosen by the Minister of Finance from lists of three names presented by certain important economic federations or assemblies (as e.g. the National Federation of Consumers' Cooperatives, the General Confederation of Labour, the Permanent Assembly of Presidents of Chambers of Agriculture). Further, the Ministers of Finance, National Economy and Colonies each have their representative on the Council; and, in addition, six holders of high offices under the Minister of Finance or in certain public or semi-public credit institutions, e.g. the Caisse des Dépôts et Consignations and the Crédit Foncier, are members ex officio. No member of Parliament may be a member of the General Council; and all councillors appointed by the Ministers on recommendation of interested parties may not serve longer than three consecutive years, being eligible for re-election only after an interval of three years. As to the actual management of the bank, the General Council may delegate all, or part, of its powers to a permanent committee comprising the governor, deputy-governors and four councillors including one appointed by the Minister of Finance from among the ex-officio members and three appointed by the General Council.

Approval was given by the Law of 23rd June 1936 to a convention between the French Treasury and the Bank of France providing for the refunding, up to an amount of 14,000 million francs, of government bills rediscounted by the bank, and for the extension of additional advances of Fcs. 10,000 million to the Treasury. At the same time it was laid down that the return of the bank should show in separate items the amount of government bills rediscounted by the bank and the amount advanced to the Treasury under the convention.

By the Law of 10th February 1937 certain changes were made in the statutes of the German Reichsbank, of which the most important are the following: (i) the elimination of the provision concerning the Reichsbank's independence of the government, (ii) the placing of the Reichsbank-Direktorium directly under the Führer and Chancellor, and (iii) the wiping-out of certain provisions connected with the execution of reparation charges. The President of the Reichsbank explained at the time these changes were made that the placing of the Reichsbank immediately under the highest State authority meant that the fiscal administration would have no possibility of recourse to the note-issuing power of the bank, for in the hypothetical case of such an attempt

being made, the bank of issue would be in the position to appeal directly to the chief of the State. As regards the elimination of certain provisions relating to the connection with the Bank for International Settlements, the President said that the Reichsbank would continue to work with this bank, though no longer on a compulsory basis but voluntarily in the same way as other banks of issue.

In Paraguay a new central bank has been formed in that the Bank of the Republic of Paraguay, established in the form of a State bank by a decree of 23rd February 1936, has taken over the assets and liabilities of the "Officina de Cambios". The powers of the Bank of Mexico were extended in August 1936, in connection with monetary reorganisation involving the renewed issue of silver coins.

The currency devaluations in the autumn of 1936 did not involve any modification of the legal provisions for the cover of notes or other liabilities of central banks by gold or other assets. In Latvia, however, the minimum gold cover against notes in circulation had been reduced from 50 to 30 per cent. at an earlier date (end of May 1936). In Denmark, the law establishing the National Bank fixed the minimum cover requirements at 25 per cent. in gold of the total active note circulation, as compared with a metallic reserve of  $33\frac{1}{3}$  per cent. previously. Up to 5 per cent. of the note circulation, non-interest-bearing net credit balances on demand with foreign central banks may take the place of gold. In Norway, by a law of 30th June 1936, the note-issuing power of the Norges Bank in excess of the gold stock was increased from Kr. 250 million to Kr. 325 million. The gold holdings of the bank are still valued at the old parity and, as the note circulation was rising, it was thought desirable to increase the flexibility of the bank by an extension of the note-issuing power. By the same law it was made clear that the Norges Bank is entitled to carry out open-market operations, the position under the old law being open to some doubt.

The Nederlandsche Bank has also been given power to undertake open-market operations, the new right being conferred in connection with the extension for a period of five years of the charter of the bank, this period being prolonged from year to year unless the charter is denounced either by the government or by the bank, in which case the charter comes to an end on 1st April after a period of three years has elapsed since the date of the denouncement (by law of 22nd February 1937). The operations will consist in the buying and selling of bills accepted by banks or bankers established within the Netherlands and of Treasury paper, the latter kind of paper to be bought from third parties so as to exclude the possibility of the bank's financing the government directly. In a number of countries the question of enabling the central bank to undertake open-market operations is under consideration, measures being sought to restrict, by appropriate means, very high liquidity of commercial banks. In order to be able to withdraw resources from the market, the Sveriges Riksbank was given power in June 1936 to pay interest on all deposits, whereas previously interest could be paid only on time deposits (but this power has not yet been utilised).

In order to rationalise the statutes of public and semi-public credit institutions a new law is under consideration in Belgium, the purpose being

to make a better distribution of the functions of the various institutions and to readjust their working in relation to one another, to the money and capital markets and to the general public.

In the field of commercial banking no major legislative changes have been made in the course of the year as far as Europe and the United States are concerned. The most important addition to existing legislation is the issuing in France of a law on so-called "popular banks" (cooperative and similar banks). Some further decrees have been issued in Germany on the basis of the Law of 5th December 1934 in execution of the banking reform; certain changes in the existing provisions have been made in the Swedish and Swiss bank laws. In Rumania, as well as in Japan, measures have been taken to facilitate the amalgamation of small banks. The new Turkish bank Law of 1st June 1936 on the whole follows the lines of other modern legislation on the subject: credit institutions must possess minimum capital and reserves in order to be entitled to receive deposits, and provisions are made to ensure liquidity, the distribution of risks and the accumulation of reserves.

On the completion of the first year of the Belgian Bank Commission a comprehensive report was published, giving for the first time the quarterly combined balance sheets of the commercial banks as prescribed in the law. It may also be mentioned that the English clearing banks now publish figures showing the distribution of advances in a form proposed by the Macmillan Committee in 1931. The new comprehensive banking laws which have been passed in recent years in a number of countries in general provide for increased publicity and, with or without legal provisions, a considerable amount of information is regularly being made available regarding credit institutions on various markets. On the basis of the information thus furnished, it is usually possible to examine more closely the position of each individual institution, which in a sense gives some measure of control. The information may also serve a wider purpose in that it allows the closer following of the general development of business conditions as reflected in the activity of the credit systems. The banking world is naturally interested in the significance of the data that are made available, and in many respects it assists in the interpretation and furnishes supplementary information by its own commentaries in annual reviews and monthly publications. The realisation is spreading that there is need for increased knowledge of the banking structure — the way it operates and the proportions of its component parts.

In previous sections of this Report mention has been made of the greater liquidity of credit institutions generally and of the increasing extension of bank credit for commercial advances in certain markets. It remains to add that, with the exception of only a few countries, there was an increase in the note circulation during 1936, in many cases at a rate of 10 per cent. or more. The increase corresponds in a general way to the higher cash requirements of businesses and private persons following the rise in sales and wage payments concomitant with an increase in the national income. Even in countries where payments are commonly made by cheque a very substantial part of the national income — particularly income of wage earners — is expended in the form of notes.

In certain countries particular causes have contributed to the accentuation of the movement. Part of the increase in the note circulation of the Bank of England went, as mentioned earlier in this Report, into the hands of foreign hoarders. In some countries, as for instance in Finland, greater use has been made of settlements in cash, these replacing payments in kind or exchange by barter; but even in Finland the main factor has been the upward trend of business, as recently explained by the Governor of the central bank. In a few countries it would also seem as if the execution of large public works, designed to give as much employment to labour as possible, had led to a distinct increase in the note circulation. It is more difficult to estimate to what extent changes in the velocity of circulation have influenced the volume outstanding; there are some signs of a reduction of velocity as compared with the pre-depression period, but it is doubtful whether within the last few years any marked change has occurred in this respect.

Note circulation	Currency	End of	End of	End of	Percentage change from 1935 to 1936
		1929	1935	1936	
in millions of national currencies					
Argentina . . . . .	Peso	1,247	1,178	1,302	+ 10.5
Austria . . . . .	Sch.	1,094	976	944	- 3.2
Belgium . . . . .	Fr.	13,933	20,864	22,702	+ 8.8
Bulgaria . . . . .	Lev	3,609	2,497	2,571	+ 3.0
Canada . . . . .	\$		170	191	+ 12.4
Czechoslovakia . . . . .	Kč.	8,230	5,761	6,478	+ 12.4
Danzig . . . . .	Fl.	38	29	32	+ 9.7
Denmark . . . . .	Kr.	367	384	399	+ 3.8
Estonia . . . . .	Kr.	34	40	44	+ 11.3
Finland . . . . .	FM	1,361	1,381	1,630	+ 18.1
France . . . . .	Fr.	68,571	81,150	89,342	+ 10.1
Germany . . . . .	RM	5,624	4,833	5,348	+ 10.7
Greece . . . . .	Dr.	5,193	5,988	6,203	+ 3.6
Hungary . . . . .	Pengő	501	417	436	+ 4.6
Italy . . . . .	Lira	16,774	16,297	16,525	+ 1.4
Japan . . . . .	Yen	1,642	1,767	1,866	+ 5.81
Latvia . . . . .	Lat	48	38	44	+ 14.0
Lithuania . . . . .	Lita	95	104	110	+ 6.6
Netherlands . . . . .	Fl.	851	809	792	- 2.0
Norway . . . . .	Kr.	318	348	429	+ 23.2
Poland . . . . .	Zł.	1,340	1,007	1,034	+ 2.7
Rumania . . . . .	Leu	21,144	23,127	25,663	+ 11.0
Sweden . . . . .	Kr.	569	786	893	+ 13.6
Switzerland . . . . .	Fr.	999	1,366	1,482	+ 8.5
United Kingdom . . . . .	£	370	412	467	+ 13.5
United States . . . . .	\$	4,578	5,882	6,543	+ 11.2
Yugoslavia . . . . .	Din.	5,818	4,890	5,409	+ 10.6

\* No comparable figure available.

No doubt in certain countries special circumstances have influenced the movements in the volume of notes outstanding, but the more or less universal increase in the past few years can on the whole be taken to reflect the upturn in business. Note issues did not generally decrease during the depression and the recent increases have thus carried the total circulation in a number of countries to levels as much as 40 per cent. above those of 1929. Some concern begins to be felt at the rise in the volume of notes in the hands of the public, especially when accompanied by a distinct advance in the cost of living. The possibility of checking what may be considered a dangerous increase in the volume of circulating media is a question dependent upon general monetary policy; in a period of increasing gold supplies and monetary reserves little restraining effect will as a rule be exercised by existing legal cover requirements.

## VII. CURRENT ACTIVITIES OF THE BANK.

### 1. OPERATIONS OF THE BANKING DEPARTMENT.

The balance sheet of the Bank as at 31st March 1937, examined and found correct by the Bank's auditors, is reproduced in Annex II to the present Report. It shows a total of 619 million gold Swiss francs, against 661 million of the same units at 31st March 1936. These units, corresponding to 0.29032258... grammes of fine gold, are those in which the Bank's capital is expressed. This weight of gold, however, was not valued on the same basis for both the dates mentioned above. At 31st March 1936 the calculation was made on the basis of the official selling price applied to gold by the Bank of France in Paris, our assets and commitments in the various currencies having been previously converted into French francs on the basis of the exchange rates quoted on the respective markets on the last day of the month. At 31st March 1937, on the other hand, the official selling price for gold in New York was taken as the basis for calculating the value of the gold units of 0.29 grammes in which the Bank's situation is presented, while the exchange rates applied to our assets and commitments in foreign currencies were the rates quoted against dollars on the respective markets.

It is therefore difficult to make a comparison between the two balance sheets, especially as a certain number of important currencies have, since the end of September 1936, represented a smaller number of gold Swiss francs.

On the whole it may be said that, in comparison with the previous financial year, the Bank's activities have shown a very definite extension, especially since December 1936. This increase is the more interesting since it marks a further advance in the development already mentioned in the last Report. In this connection it is particularly satisfactory to note that this year a larger number of central banks or international institutions have shown an interest in the services which the Bank can offer. In various spheres of the Bank's activity new machinery is now at disposal which experience has shown to be flexible and capable of further development. This machinery has been available throughout the year to central banks having recourse to us and it has been possible to apply new methods evolved within the limits imposed by the Statutes and by the special nature of certain commitments.

Although, for the reasons set forth above, the figures at 31st March 1936 and 31st March 1937 are not fully comparable, many items of the two balance sheets nevertheless admit of comparison:

1. Liabilities. During the financial year under review the total of long-term deposits fell from 295 to 274 million gold Swiss francs. This decline is merely a consequence of the changes that have occurred in the value of the currencies in which these deposits are expressed. From the end of October 1936 onwards the figure has been 274 millions, whereas — leaving out of account variations resulting from more or less normal exchange fluctuations — the first figure of 295 million appeared in the situation as at 30th September 1936.

Deposits of central banks for their own account total 130 million at 31st March 1937 against 139 million at the beginning of the financial year, while deposits for account of third parties total 4 against 14 million. Before September 1936 deposits of the first category had risen to 155 million; after falling to 108 million at the end of October, these deposits rose again to 150 million at 31st January 1937.

Sight deposits (gold) amount to 23 million at 31st March 1937 against 19 million a year ago. A total of 28 million was several times reached and even exceeded during the financial year. Here again a considerable increase was apparent in the volume of operations passing through these accounts, the number of which is also larger. Not only do withdrawals of gold from these accounts afford a rapid means of procuring any foreign exchange desired by the depositors, but the accounts have also proved particularly useful in facilitating certain practical adjustments occasioned by gold operations — especially the exchange of gold between various markets. By transfers between deposits of gold under earmark and bank deposits expressed in a weight of gold, it is possible to keep the latter down to a minimum or, on the other hand, to replenish them in preparation for operations to be effected by their debit.

2. Assets. A comparison between the assets at 31st March 1936 and 31st March 1937 reveals a number of fairly definite movements.

The items immediately realisable have grown considerably. "Gold in bars" now shows a total equivalent to 45 million, the highest figure recorded as yet, against 24 million a year ago; the various cash holdings, which at one moment reached the level of 39 million, now total 26 million, against 10 million a year ago, while sight funds, after registering considerable fluctuations, total 26 million against 13 million. The aggregate increase in these three items thus amounts to 50 million.

On the other hand, the portfolio of commercial bills, bankers' acceptances and Treasury bills shows a decrease which, though proportionately smaller, reduces their total by the larger amount of 106 million.

Time funds have declined from 36 to 29 million, while "Sundry Bills and Investments" have increased from 227 to 259 million.

In the aggregate the items comprising the realisable assets have fallen by 56 million, while time funds have increased by only 25 million. The decrease of 11 million under "Other Assets" brings the total reduction of the balance-sheet figure to 42 million.

The liquidity of the Bank is not thereby impaired. At 31st March 1937 the whole of the short-term and sight deposits in various currencies and the sight deposits (gold) represented 25.4 per cent. of the balance-sheet total, while the sight assets, including bar gold, alone amounted to more than twice that figure and comprised 53.2 per cent. of the total.

The note appearing on the balance sheet in Annex II shows the manner in which the principles of equilibrium and liquidity already referred to in earlier Reports have been respected in the administration of the assets. Thanks to their strict application, the transition from the monetary system existing before September 1936 to that which followed was accomplished in the best possible

conditions. The exchange differences registered at that time were of minor importance since the few exchange positions which were not completely balanced reflected only current operations of a normal character.

For the rest, two main trends, which may be briefly indicated, are apparent in the practical development of the Bank's situation during the financial year.

In the first place there is a growing tendency on the part of central banks to repay the credits placed at the disposal of their markets in the form of investments for indeterminate periods, that is to say, investments which in course of time had acquired something of a permanent character. In addition there is among the subscribers of the Bank's capital a large number of countries in which the proceeds of such subscriptions used to be invested but in which no funds are kept to-day, either because Art. 21 of the Statutes precludes the Bank in present circumstances from investing in their currencies or because it has been impossible to obtain a gold guarantee. Thus the Bank has been led to adopt "long" positions in a certain number of currencies or to remain in gold. In the first case it incurs a currency risk; in the second — however useful the existence of a stock of gold for its own account may be in other respects — it obtains no interest on its holdings.

Furthermore, on all the markets benefiting by monetary conditions considered favourable there has been such an abundance of liquid funds during the year that investments of the kind which we are authorised to effect (the choice of which is extremely limited) have in general proved to be but slightly remunerative.

The difficulties thus encountered by the Bank are by no means peculiar to it but they are, in its case, accentuated by the rigid rules governing the nature and choice of its investments. It must be added, however, that in its search for investments the Bank has always had the whole-hearted assistance of the central banks concerned.

The reasons set forth above are, to a large extent, at the root of the substantial increase in the items immediately realisable: that is to say, gold and cash holdings in various currencies, the latter assuming fairly considerable proportions on one or two markets. For the same reasons the Bank has been led to effect, in the best possible conditions and with the consent of the central banks concerned, certain medium-term investments, which account for the increase in "Sundry Bills and Investments".

As mentioned above, certain central banks seem to prefer to call upon the Bank for International Settlements for seasonal operations, when occasion arises, rather than maintain credits of a fixed volume and indefinite maturity. In this domain, as in the covering of exchange risks incidental to the financing of international trade, and the improvement of the operation of clearing systems, the Bank has on various occasions been asked for assistance, which it has always given within the limits of existing possibilities and of the guarantees offered. Here again, a simple mechanism of credits or advances, with or without security, has been evolved, from which a further development of operations of this nature may be hoped.

In the previous Annual Report attention was drawn to the continued development of operations in gold and to the more or less logical character of that development. During the past year there has been a further extension of these operations. The swift changes of direction in the movements of capital and consequently in exchange rates, the evolution of the methods of intervention on the foreign exchange markets employed by central banks, their transfers of gold for the purpose of ensuring the service of international loans or meeting national commercial requirements and, lastly, repatriations of gold previously held under earmark have considerably increased the part played by the central banks in gold movements.

The Bank has not failed to benefit by the increase in this form of international activity among members of its organisation. A few figures demonstrate this better than any comment:

Gold earmarked for account of central banks or international institutions does not appear in the Bank's situation. The total of such gold rose from the equivalent of 268 million gold Swiss francs at 31st March 1936 to 358 million at 30th June, falling again to 313 million at 31st October and reaching 433 million at the end of the financial year. At 31st March 1937, taking into account the 45 million constituting the Bank's own stock of bar gold, the gold held under earmark in the name of the Bank for International Settlements on 8 different markets totalled nearly 480 million units of 0.29 grammes of fine gold, that is to say the equivalent of some 670 million Swiss francs or 3,350 million French francs.

Gold operations with central banks during the year have assumed a variety of forms. To mention only the most important and the most characteristic, there have been exchanges, transfers, advances in foreign currencies against gold deposited on any big market, advances on gold in transit or in process of shipment, negotiations of gold against a currency other than that of the market of delivery or consignment, surrender of gold earmarked on a given market, repatriation being arranged as desired by the party receiving the gold, etc. In this connection, thanks to the existence of a stock of gold for its own account, the Bank has on many occasions been able to anticipate certain movements, to provide for necessary adjustments and to secure the more rapid execution of operations entrusted to it. Furthermore, the facilities granted by certain central banks in regard to the choice of markets for the delivery of gold purchased by them have also contributed to the flexibility and efficiency of the procedure for certain arbitrage operations.

The Bank's task has often been facilitated by the fact of its having received from various central banks standing orders enabling it, in certain circumstances, to organise a kind of market for offsetting offers and enquiries. Big central banks have even emphasized the importance they attach to the co-operation, in this domain, of the Bank for International Settlements with the principal banks of issue, as a factor in the re-establishment of normal relations between the major currencies. We would add that, the greater the number of central banks actually co-operating with us in this connection, the wider the opportunities of useful and effectual work for the Bank for International Settlements.

In addition to its operations in connection with the administration of its own resources and those entrusted to it, the Bank for International Settlements has effected a certain number of transactions in the rôle of Trustee. These operations are described later in this chapter. It may, however, be well at this point to mention a definite task for which the Bank for International Settlements has devised special machinery which is at present being studied by central banks throughout the world, i. e. the settlement of international postal payments through the Bank.

In the new system the gold franc, the unit of account for international postal payments, is taken as the basis not only for the calculation of amounts due but also for the actual discharge of payments. The operation is carried out in two stages. For the first stage the central banks of each of the countries concerned must keep in the books of the Bank for International Settlements a gold sight account to the debit and credit of which payments will be made in gold francs, that is to say, in a weight of metallic gold, grammes or ounces. The second stage in the settlement of these amounts takes place between the central bank and the postal administration, on each of the markets concerned, in the national currency in accordance with agreements to be made in each country between the central bank and the postal administration.

One of the advantages of the system is that, from the time the debtor postal administration effects payment in national currency to its central bank until the time payment is made in the other national currency to the creditor postal administration by its own central bank, the value of the amount due is not subject to any variations in relation to the international unit chosen for the settlement.

A number of adhesions to this system have already been received. Amongst other advantages it offers freedom from expense and delay. As the benefits which may be derived by the postal administrations of all countries come to be realised in practice, it is to be hoped that this system will serve as an example and be taken as a model for other international payments presenting the same difficulties.

## 2. TRUSTEE AND AGENCY FUNCTIONS OF THE BANK.

During the period under review, 1st April 1936 to 31st March 1937, the Bank's trustee and agency functions in connection with the annuity payments arising from the New Plan adopted at the Hague Conference of January 1930 and in connection with the German "Dawes" and "Young" loans have remained merely formal in character. On the other hand, the functions of the Bank as trustee for the Austrian Government International Loan 1930 have proceeded normally and the Bank has continued to act as agent in connection with the settlement of the financial questions involved in the transfer of the Saar territory to Germany. In addition, towards the close of the year, the Bank agreed to act as intermediary for the service in Switzerland of the French National Security 4½% Loan 1937.

(a) Annuity payments of Germany, Hungary, Bulgaria and Czechoslovakia.

As a result of the terms of the Lausanne Agreement of July 1932, the execution of the annuity obligations of Germany under the New Plan adopted at the Hague Conference of January 1930, has been reserved pending ratification of the Agreement. The execution of the annuity obligations of Hungary, Bulgaria and Czechoslovakia was also reserved until 15th December 1932. The interested Governments subsequently agreed that this reservation should be extended until 15th December 1934 and negotiations are in progress with a view to a similar extension covering the period after that date. During the year under review, therefore, the Bank has received nothing in respect of the annuity payments of the above-mentioned Powers.

(b) German External Loan 1924  
and German Government International 5½% Loan 1930.

Since 1st July 1934, the German Government has not furnished to the Trustees any of the funds required in the currencies of the respective issues for the service of these Loans, and the position of the Trustees remains as described in pages 69 to 71 of the Bank's sixth annual report.

During the year under review, however, although the service of the Loans has not been effected through the respective Trustees, certain groups of bondholders have continued to benefit under special agreements concluded between the German Government and various other Governments. Bondholders specified in these agreements have been able to obtain payment in the currency of their country of domicile, of the whole or a part of the nominal value of their coupons. Moreover, as regards bondholders who do not receive payment of the full nominal amount of their coupons in this manner but have not surrendered their right to such payment, the German Government has offered to liquidate the outstanding amounts by a payment in reichsmarks calculated at the Reichsbank's official rate of exchange, the employment of such reichsmarks being governed by principles similar to those regulating the use of registered marks. The Trustees for the respective Loans are not parties to any of these special agreements, have had nothing to do with their execution and have considered them as incompatible with the General Bonds and the international agreements relating thereto.

Reference has been made in earlier reports to the fact that the Bank, as Trustee for the German Government International 5½% Loan 1930, had been sued in a Swiss Court by a bondholder of one of the issues of that Loan claiming damages for alleged improper distribution of the funds provided by the German Government on account of the service of the Loan. The Basle Civil Court of first instance found in favour of the Trustee and dismissed the case with costs. The bondholder appealed to the Basle Court of Appeal which affirmed the decision of the lower Court; the bondholder then appealed to the Federal Court of Appeal where the appeal was dismissed with costs.

In the existing circumstances Statements of Receipts and Payments in respect of the year to 15th October 1936 for the 1924 Loan and the year to

1st June 1936 for the 1930 Loan have not been prepared but the Swiss gold franc equivalent of the various currencies relating to the respective Loans which were deposited in the names of the Trustees, as at 31st March 1937, is shown in Annex VI.

(c) Austrian Government International Loan 1930.

During the year under review, the Bank, as Trustee for the Austrian Government International Loan 1930, has regularly and punctually received and distributed the monthly service instalments required pursuant to the terms of the General Bond. The operations of the Sinking Fund during the year have resulted in the redemption of bonds of a total nominal value equivalent to 5,219,000 Swiss gold francs.

The Austrian Government International Loan 1930 is secured by a first charge upon the gross receipts of the customs and of the tobacco monopoly of the Austrian Government, subject only to the charge in respect of the Czechoslovakian Conversion Loan. During the year under review, the pledged revenues amounted to a total of 438,753,000 Austrian Schillings and the amount required for the service of the Austrian Government International Loan 1930 amounted to the equivalent of 32,386,000 Austrian Schillings.

A Statement of Receipts and Payments, as certified by the auditors, for the last completed Loan year to 30th June 1936, is appended as Annexes IVa and IVb. In order to show the position to the last interest coupon due date, there is also appended as Annex V an Interim Statement of Receipts and Payments for the half-year to 31st December 1936. In addition, the Swiss gold franc equivalent of the funds relating to this Loan which were deposited in the name of the Trustee as at 31st March 1937, is shown in Annex VI.

(d) Other Agency Functions.

The Bank has continued to take its part in the settlement of the financial questions involved in the transfer of the Saar Territory to Germany. The German Government agreed to repurchase the mines, railways etc. in the Saar from France for a lump sum of 900 million French francs on the understanding that payment should be effected (a) by the delivery to the Bank of France, for the account of the French Government, of 95 per cent. of the French francs and other foreign currencies collected in the Saar in exchange for reichsmarks (b) by free deliveries of coal and (c) through the payment by the German Government to the interested parties on behalf of the French Government of sums due by the latter in the Saar Territory for various reasons, e. g. compensation for surface damage, indemnities, taxes etc.

The table on the next page shows the progress made in the repurchase of the Saar mines, railways etc.

The remaining 5 per cent., or 14.4 million French francs, of the French francs and other foreign currencies collected in the Saar in exchange for reichsmarks, which was allocated towards the service of certain foreign loans

In millions of French Francs	Period to 31st March 1936	Year to 31st March 1937	Total
95 per cent. of the French francs and other foreign currencies exchanged for reichsmarks . . . . .	274.4	—	274.4
Free deliveries of coal . . . . .	89.9	147.3	237.2
Payments by the German Government as compensation for surface damages, indemnities, taxes etc. . . . .	3.1	11.7	14.8
	367.4	159.0	526.4

authorised by the former Saar Governing Commission has now been almost completely utilised for that purpose. At 31st March 1936, 4.1 million French francs remained in hand and at 31st March 1937, this amount had been reduced to the equivalent of 0.8 million French francs.

The amount of 14.5 million French francs which was deposited with the Bank in order to provide for the capitalisation of the pensions of Saar officials of French nationality has been paid out during the year under review.

The Bank has also agreed to act as intermediary for the service in Switzerland of the French National Security 4½% Loan, 1937 and to nominate the Swiss banks and branches of French banks in Switzerland which are to act as Paying Agents for the Loan. The Bank will receive from the French Government, fifteen days before each coupon due date, the amount in Swiss francs which it is estimated will be required to meet the coupons of the Loan presented in Switzerland and arrangements have been made for the provision by the French Government of any further sums which may prove to be necessary. The Bank will distribute the amounts thus received among the various Paying Agents as and when necessary so that they may be in a position to pay all coupons on presentation.

### 3. NET PROFITS AND DISTRIBUTION.

It is for the present General Meeting to consider the declaration of a dividend and to make appropriations to reserves. The net profit for the year, after making allowance for contingencies, is 9,071,570.02 Swiss gold francs, the Swiss gold franc being as defined by Article 5 of the Bank's statutes i. e. the equivalent of 0.29032258... grammes fine gold. This compares with a figure of 9,193,671.— Swiss gold francs for the sixth fiscal year. In the balance sheet as at March 31, 1937, all currencies are valued at or below the least favourable market rate prevailing on that date and all assets are valued at or below market quotations, if any, or at or below cost. In computing the above profits, no account has been taken of exchange gains arising by reason of the Bank happening to be short in any depreciated currency; whereas exchange losses have been written off.

After providing for the Legal Reserve that is required by Article 53 of the Statutes, in an amount equal to 5 per cent. of the net profits, i.e. 453,578.50 Swiss gold francs (1936: 459,683.55 Swiss gold francs) it is recommended that the General Meeting declare a dividend at the rate of 6 per cent. per annum in respect of the seventh fiscal year. The payment of this dividend requires 7,500,000 Swiss gold francs (1936: 7,500,000 Swiss gold francs). The net profits still remaining after the declaration of the dividend would amount to 1,117,991.52 Swiss gold francs, the appropriation of which is fixed by Article 53 of the Statutes.

Exercising the discretion vested in it by paragraph (c) of Article 53 of the Statutes, the Board of Directors has determined to place to the credit of the Special Dividend Reserve Fund provided for by the Statutes, the sum of 223,598.30 Swiss gold francs, which is the maximum amount which it is permissible, under the Statutes, to set aside for this purpose out of the net profits of the present year (1936: 246,797.49 Swiss gold francs).

After making provision for the foregoing items, you are requested, from the balance still remaining, to make an appropriation to the General Reserve Fund in the manner stipulated by paragraph (d) of Article 53, to the amount of 447,196.61 Swiss gold francs (1936: 493,594.98 Swiss gold francs). The aggregate of the Legal, Dividend and General Reserves at the end of the seventh year would then be 23,183,521.77 Swiss gold francs.

The same article of the Statutes lays down the distribution of the sum finally remaining, namely, 447,196.61 Swiss gold francs, between such of the Governments or central banks of Germany and the countries entitled to share in the annuities payable under the New Plan, defined in the Hague Agreement of January 1930, as shall have maintained time deposits at the Bank subject to withdrawal in not less than five years. No central bank has such time deposits at present but the following Governments have these deposits and are entitled, in view of this minimum duration of their deposits, to participate in the residual amount of 447,196.61 Swiss gold francs (1936: 493,594.98 Swiss gold francs) in the following sums:

Annuity Trust account deposits in accordance with Article IV (e) of the Trust Agreement:—	Swiss gold francs	
	1936/37	1935/36
France . . . . .	131,366.53	140,409.56
Great Britain . . . . .	51,335.04	54,868.85
Italy . . . . .	26,813.93	28,659.75
Belgium . . . . .	14,505.10	15,503.61
Rumania . . . . .	2,534.17	2,708.62
Yugoslavia . . . . .	10,546.97	11,273.01
Greece . . . . .	868.86	928.67
Portugal . . . . .	1,665.31	1,779.95
Japan . . . . .	1,665.31	1,779.95
Poland . . . . .	48.27	51.59
	<u>241,349.49</u>	<u>257,963.56</u>
German Government non-interest-bearing deposit in accordance with Article IX of the Trust Agreement	120,674.74	128,981.78
French Government deposit (Saar) . . . . .	2,703.89	3,385.71
French Government Guarantee Fund in accordance with Article XIII of the Trust Agreement . . . . .	82,468.49	103,263.93
	<u>447,196.61</u>	<u>493,594.98</u>

The accounts of the Bank and its seventh Annual Balance Sheet have been duly audited by Messrs. Price, Waterhouse & Co., Chartered Accountants. The Balance Sheet will be found in Annex II, as well as the certificate of the auditors to the effect that they have obtained all the information and explanations they have required and that in their opinion the Balance Sheet, together with the note thereon, is properly drawn up so as to exhibit a true and correct view of the state of the Bank's affairs according to the best of their information and the explanations given to them and as shown by its books. The Profit and Loss Account and the Appropriation Account are reproduced in Annex III.

#### 4. CHANGES IN BOARD OF DIRECTORS AND EXECUTIVE OFFICERS.

By the terms of the Statutes, the members of the Board, appointed by the ex-officio Directors, hold office for three years and are eligible for re-appointment. The Bank having been founded in May 1930, certain reappointments to the Board were made in May 1936 for the third period of three years. At the same time Professor Beneduce and Mr. de Vogüé were re-elected Vice-Chairmen. Governor Jean Tannery, an ex-officio Director, whose cordial co-operation had been of the greatest value to the Bank, was succeeded, upon his retirement as Governor of the Bank of France, by Mr. Emile Labeyrie, the new Governor, who has held important financial appointments under the French Government. Mr. Munakata, who had served with distinction on the Board since 1934 as the substitute-nominee of the Governor of the Bank of Japan, returned to his own country and was succeeded in the same capacity by Mr. Yanagita, the representative for Europe of the Bank of Japan.

In December last, the undersigned having intimated his intention to resign at the end of the financial year as Chairman of the Board and President of the Bank, the Board decided to propose to an Extraordinary General Meeting certain amendments to the Statutes, which would make it possible, inter alia, to separate the functions of Chairman of the Board and President of the Bank. Subject to the approval by the Extraordinary General Meeting of the amendments in question, the Board elected Sir Otto Niemeyer Chairman of the Board and nominated Dr. J. W. Beyen, at present Alternate of the President, as President of the Bank; both appointments are for a period of three years and become effective on the date of approval of the amendments to the Statutes. The President of the Bank will carry out the policy decided upon by the Board and will control the administration of the Bank. While not a member of the Board, he will be entitled to attend all meetings, to speak and have his opinions recorded in the Minutes.

Mr. Ivar Rooth, Governor of the Sveriges Riksbank, whose constructive work of collaboration is well known and whose previous term of office expired by limitation on 31st March 1933, was again elected to the Board in April 1937. At the same meeting the undersigned, whose term of office as a Director expired at the end of the financial year, was re-elected for a further period of three years.

Among the Alternates of Members of the Board, Mr. R. Lacour-Gayet retired as one of the Alternates of the Governor of the Bank of France upon relinquishing his appointment with that Bank. Mr. Lacour-Gayet had not only attended the Board meetings for a number of years but had also given valuable assistance in connection with various international conferences held at the Bank. The Governor of the Bank of Italy has appointed as one of his Alternates Dr. M. Pennachio, who took part in the work of the Organising Committee of the Bank at Baden-Baden and who has been present at the meetings of the Board since the foundation of the Bank.

### VIII. CONCLUSION.

A year ago recovery was well on its way and spreading; now it has reached the stage where strong upward forces dominate world economy and threaten even to produce in some branches a too rapid advance in costs and prices, suggestive of boom conditions. It may not be sufficiently realised how rapid the change has been and there may be a tendency still to hold fast to certain pessimistic ideas, which may have been appropriate during the depression but are out of date now that conditions have changed. Account must be taken of the fact that there has been an almost complete reversal of many of the problems before us and the policy to be pursued must be modified accordingly. To mention only one example: as far as government finance is concerned, not only has the need for extraordinary spending to stimulate general business activity disappeared but such spending may be directly harmful to a healthy development.

On the whole it may probably be assumed that, mindful of the violent economic changes during the post-war period, not only those in authority but also the public are more fully aware of the dangers arising from the development of an unbalanced position. It is important, however, to concentrate attention not on the symptoms but to deal with the more fundamental causes liable to produce a dangerous disequilibrium. During the difficulties that prevailed in the black days of the depression, it was perhaps unavoidable that many hasty measures should be taken, but these, although understandable in an emergency situation, tended to increase rather than reduce the state of uncertainty. It is to be hoped that in a period of relative prosperity more calm and more caution will be observed and that efforts will be made to build up a more enduring stability both in the economic and monetary sphere.

There still remains the pressing need of reducing trade barriers and particularly those extraordinary hindrances to trade in the form of quotas and prohibitions built up in the past seven years; the other acute problem is that of establishing a monetary system that will combine an international stability of exchanges with a policy, both national and international, directed as far as possible towards the maintenance of a sound credit and currency position. In addition, the burden of international financial obligations must be alleviated, where this has not yet been done, by conversions to a level of interest rates more in conformity with present conditions. Without attacking these fundamental problems of world economy and finance, little hope can be held out as to the chances of achieving a lasting improvement in the various national economies. It cannot be denied, however, that a mastering of the problems involved in business fluctuations is connected with the question of government expenditure, particularly in view of the recent increase in outlay on armaments; and this connection is only one example of the political aspects of the problems before us. It would be vain to think that purely technical arrangements can guarantee sound economic developments and make an improvement in the standard of living possible, if the underlying conditions

for a peaceful interchange of goods and a balanced position in the different countries are not fulfilled. All economic activity must reckon with the future and if there is a continued lack of stability, the soundest businesses will be forced either into a curtailment of their operations or compelled to take speculative risks. Instead of embarking upon expedients that would bring little or no advantage and might easily hamper normal economic development an attempt should be made to get to the root of the matters responsible for the present difficulties. World opinion is beginning to demand that a serious effort be made towards the solution of the great outstanding problems, and this task must be attacked with the understanding, courage and goodwill necessary to achieve satisfactory results.

Respectfully submitted,

L. J. A. TRIP,  
President.

# ANNEXES

## CENTRAL BANKS OR OTHER BANKING INSTITUTIONS POSSESSING RIGHT OF REPRESENTATION AND OF VOTING AT THE GENERAL MEETING OF THE BANK

"The ownership of shares of the Bank carries no right of voting or representation at the General Meeting. The right of representation and of voting, in proportion to the number of shares subscribed in each country, may be exercised by the central bank of that country or by its nominee. Should the central bank of any country not desire to exercise these rights they may be exercised by a financial institution of widely recognized standing and of the same nationality, appointed by the Board, and not objected to by the central bank of the country in question. In cases where there is no central bank, these rights may be exercised, if the Board thinks fit, by an appropriate financial institution of the country in question appointed by the Board." (Article 15, Bank Statutes.)

Institutions	Number of votes	Date of acquisition of right of representation and of voting
Bank of England, London . . . . .	16,000	20th May 1930
do. do. . . . .	3,772 (a)	31st May 1932
Banque Nationale de Belgique, Brussels . . . . .	16,000	20th May 1930
do. do. . . . .	3,772 (a)	31st May 1932
Banque de France, Paris . . . . .	16,000	20th May 1930
do. do. . . . .	3,772 (a)	31st May 1932
Banca d'Italia, Rome . . . . .	16,000	20th May 1930
do. do. . . . .	3,772 (a)	31st May 1932
Reichsbank, Berlin . . . . .	16,000	20th May 1930
do. do. . . . .	3,772 (a)	31st May 1932
The Industrial Bank of Japan, Tokyo . . . . .	16,000	20th May 1930
do. do. . . . .	3,770 (a)	31st May 1932
The First National Bank of New York, New York . . . . .	16,000	20th May 1930
do. do. . . . .	3,770 (a)	31st May 1932
De Nederlandsche Bank N. V., Amsterdam . . . . .	4,000	20th May 1930
Schweizerische Nationalbank, Zurich . . . . .	4,000	20th May 1930
Sveriges Riksbank, Stockholm . . . . .	4,000	20th May 1930
Bank von Danzig, Danzig . . . . .	4,000	25th June 1930
Finlands Bank, Helsingfors . . . . .	4,000	25th June 1930
Banque de Grèce, Athens . . . . .	4,000	25th June 1930
Oesterreichische Nationalbank, Vienna . . . . .	4,000	25th June 1930
Bulgarska Narodna Banka, Sofia . . . . .	4,000	25th June 1930
Danmarks Nationalbank, Copenhagen . . . . .	4,000	25th June 1930
Banca Nationala a Romaniei, Bucarest . . . . .	4,000	25th June 1930
Bank Polski, Warsaw . . . . .	4,000	25th June 1930
Magyar Nemzeti Bank, Budapest . . . . .	4,000	25th June 1930
Narodni Banka Ceskoslovenska, Prague . . . . .	4,000	25th June 1930
Eesti Pank, Tallinn . . . . .	100	31st Oct. 1930
Latvijas Banka, Riga . . . . .	500	30th Dec. 1930
Lietuvos Bankas, Kaunas . . . . .	500	31st March 1931
Banca Nazionale d'Albania, Rome . . . . .	500	30th April 1931
Norges Bank, Oslo . . . . .	4,000	30th May 1931
Banque Nationale du Royaume de Yougoslavie, Belgrade . . . . .	4,000	28th June 1931
	200,000 (b)	

(a) Representing shares reserved until 31st May, 1937, for possible subsequent transfer to central banks of other countries.

(b) "The authorised capital of the Bank . . . shall be divided into 200,000 shares of equal gold nominal value." (Article 5, Bank Statutes.)

# BALANCE SHEET

IN SWISS GOLD FRANCS (UNITS OF 0.290322 58...)

ASSETS			
			%
I—GOLD IN BARS. . . . .		45,087,291.06	7.3
II—CASH			
On hand and on current account with Banks . . . . .		25,636,097.02	4.1
III—SIGHT FUNDS at interest. . .		26,538,408.01	4.3
IV—REDISCOUNTABLE BILLS AND ACCEPTANCES			
1. Commercial Bills and Bankers' Acceptances . . . . .	101,346,933.92		16.4
2. Treasury Bills . . . . .	130,696,121.68		21.1
		232,043,055.60	
V—TIME FUNDS at interest			
1. Not exceeding 3 months . . .	27,011,756.14		4.4
2. Between 3 and 6 months . . .	1,668,688.73		0.3
		28,680,444.87	
VI—SUNDRY BILLS AND INVEST- MENTS			
1. Treasury Bills. . . . .	111,390,144.87		18.0
2. Railway and Postal Adminis- tration Bills and Sundry In- vestments . . . . .	148,041,735.68		23.9
		259,431,880.55	
VII—OTHER ASSETS			
1. Guaranty of Central Banks on Bills sold . . . . .	1,328,725.18		0.2
2. Sundry items . . . . .	96,299.95		0.0
		1,425,025.13	
		618,842,202.24	100.0

NOTE — The whole of the short term and sight deposits in various currencies (Item IV — Liabilities) are more than covered by assets either in the currencies of the deposits or in currencies free from exchange restrictions, and of the long term commitments the French Government Deposit (Saar) and the French Government Guarantee Fund (Items III — 3 and 4) are similarly covered. The remaining long term commitments (Items III — 1 and 2) which are recorded in a restricted currency (although the Bank's commitment in respect of Item III — 1 is not clearly established), are covered by assets of the same currency, the gold value of a substantial part of which is specially guaranteed.

The Capital, Reserves and Surplus are represented to a large extent by assets in countries where exchange restrictions now prevail and do not permit of free conversion of their currencies into gold or other currencies; however, as to these assets an important part is secured by special contracts guaranteeing their gold value and in one case specifically permitting their transfer. Moreover, under Article X of the Hague Agreement of January 1930, the signatories thereto declared the Bank to be immune from any "prohibition or restriction of export of gold or currency and other similar interferences, restrictions or prohibitions".

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS  
OF THE BANK FOR INTERNATIONAL SETTLEMENTS, BASLE.

In conformity with Article 52 of the Bank's Statutes, we have examined the books and accounts and explanations we have required and that in our opinion the above Balance Sheet, together with the affairs according to the best of our information and the explanations given to us and as shewn by the concerned.

BASLE, April 22, 1937.

## AS AT MARCH 31, 1937

GRAMMES FINE GOLD — ART. 5 OF THE STATUTES)

LIABILITIES			%
<b>I—CAPITAL</b>			
Authorised and issued 200,000 shares, each of 2,500 Swiss gold francs . . . . .	500,000,000.—		
of which 25 % paid up . . . . .		125,000,000.—	20.2
<b>II—RESERVES</b>			
1. Legal Reserve Fund . . . . .	3,784,029.10		
2. Dividend Reserve Fund . . . . .	6,091,706.43		
3. General Reserve Fund . . . . .	12,183,412.83		
		22,059,148.36	3.6
<b>III—LONG TERM COMMITMENTS</b>			
1. Annuity Trust Account Deposits . . . . .	153,157,500.—		24.8
2. German Government Deposit . . . . .	76,578,750.—		12.4
3. French Government Deposit (Saar) . . . . .	1,403,900.—		0.2
4. French Government Guarantee Fund . . . . .	42,818,835.73		6.9
		273,958,985.73	
<b>IV—SHORT TERM AND SIGHT DEPOSITS (various currencies)</b>			
1. Central Banks for their own account:			
(a) Not exceeding 3 months . . . . .	105,482,000.41		17.0
(b) Sight . . . . .	24,148,370.78		3.9
2. Central Banks for the account of others:		129,630,371.19	
Sight . . . . .		4,248,186.75	0.7
3. Other depositors:			
(a) Not exceeding 3 months . . . . .	8,320.88		0.0
(b) Sight . . . . .	229,032.91		0.0
		237,353.79	
<b>V—SIGHT DEPOSITS (Gold) . . . . .</b>		23,309,485.38	3.8
<b>VI—MISCELLANEOUS</b>			
1. Guaranty on Commercial Bills sold . . . . .	1,353,739.49		0.2
2. Sundry items . . . . .	29,973,361.53		4.8
		31,327,101.02	
<b>VII—SURPLUS</b>			
Profit for the financial year ended March 31, 1937 . . . . .		9,071,570.02	1.5
		618,842,202.24	100.0

of the Bank for the financial year ending March 31, 1937, and we report that we have obtained all the information with the Note, is properly drawn up so as to exhibit a true and correct view of the state of the Bank's books of the Bank, as expressed in the above-described Swiss gold franc equivalents of the currencies

PRICE, WATERHOUSE & Co.  
Chartered Accountants.

# PROFIT AND LOSS ACCOUNT

for the financial year ended March 31, 1937

	<u>Swiss gold francs</u>
Net Income from the use of the Bank's capital and the deposits entrusted to it, after necessary allowance for contingencies . . . . .	11,203,938.69
Commissions earned:—	
As Trustee (or Fiscal Agent to Trustees) for International Loans . . . . .	199,143.76
In connection with special credits . . . . .	81,670.45
Transfer fees . . . . .	451.99
	<u>11,485,204.89</u>
Costs of Administration:—	
Board of Directors — fees and travelling expenses . . . . .	216,475.82
Executives and staff — salaries and travelling expenses . . . . .	1,761,939.19
Rent, insurance, heating, light and water . . . . .	135,041.94
Consumable office supplies, books, publications . . . . .	72,780.88
Telephone, telegraph and postage . . . . .	58,866.40
Experts' fees (Auditors, interpreters, etc.) . . . . .	18,021.78
Cantonal taxation . . . . .	41,881.06
Tax on French issue of Bank's shares . . . . .	40,822.85
Miscellaneous . . . . .	67,804.95
	<u>2,413,634.87</u>
NET PROFIT:—	<u>9,071,570.02</u>

## APPROPRIATION ACCOUNT

	Swiss gold francs
NET PROFIT FOR THE FINANCIAL YEAR ENDED MARCH 31, 1937 . . . . .	9,071,570.02
Applied in accordance with Article 53 (a) (b) (c) and (d) of the Statutes, as follows:—	
To the Legal Reserve Fund — 5 % of 9,071,570.02 . . . . .	453,578.50
	8,617,991.52
Dividend at the rate of 6 % per annum on paid-up capital . . . . .	7,500,000.—
	1,117,991.52
To the Dividend Reserve Fund — 20 % of 1,117,991.52 . . . . .	223,598.30
	894,393.22
To the General Reserve Fund — 50 % of 894,393.22 . . . . .	447,196.61
Remainder	447,196.61

Distributed in accordance with Article 53 (e) (1) of the Statutes, as follows:—

	Swiss gold francs
Annuity Trust Account deposits in accordance with Article IV (e) of the Trust Agreement:—	
France . . . . .	131,366.53
Great Britain . . . . .	51,335.04
Italy . . . . .	26,813.93
Belgium . . . . .	14,505.10
Rumania . . . . .	2,534.17
Yugoslavia . . . . .	10,546.97
Greece . . . . .	868.86
Portugal . . . . .	1,665.31
Japan . . . . .	1,665.31
Poland . . . . .	48.27
	241,349.49
German Government non-interest-bearing deposit in accordance with Article IX of the Trust Agreement . . . . .	120,674.74
French Government deposit (Saar) . . . . .	2,703.89
French Government Guarantee Fund in accordance with Article XIII of the Trust Agreement . . . . .	82,468.49
	447,196.61

# TRUSTEE FOR THE AUSTRIAN

## Statement of Receipts and Payments

### Receipts

	American Issue \$	British and Dutch Issues £
1. BANK BALANCES as at July 1, 1935 . . . . .	810,098.61	111,805.11. 3
2. RECEIVED FROM THE AUSTRIAN GOVERNMENT in respect of:—		
Interest coupons		
In cash . . . . .	1,505,911.23	212,283. 1. 6
Accrued in bonds ceded for cancellation (see below) . . . . .	8,741.32	1,178. 2. 1
Bond redemption		
In cash . . . . .	743.73	332.13.11
In bonds ceded for cancellation (see below) . . . . .	588,683.27	81,014. 6. 1
Expenses . . . . .	3,423.60	985. 5.—
3. INTEREST RECEIVED on cash employed pending application to service of the Loan . . . . .	1,104.93	299. 3. 6
	2,918,706.69	407,898. 3. 4

### Payments

1. INTEREST		
Matured coupons paid and accrued interest paid on bonds purchased for redemption . . . . .	1,535,313.97	215,220.12.—
Accrued interest on bonds ceded by the Austrian Government (see above) . . . . .	8,741.32	1,178. 2. 1
2. REDEMPTION		
Drawn bonds reimbursed . . . . .	—	—
Bonds purchased for redemption . . . . .	838.—	369. 3. 5
Bonds ceded by the Austrian Government against refund of cash . . . . .	—	—
Bonds ceded by the Austrian Government in part-payment of service instalments (see above) . . . . .	588,683.27	81,014. 6. 1
3. EXPENSES		
Commission and expenses of Paying Agents and fees and expenses of Trustee . . . . .	4,120.56	1,175.15. 8
4. BANK BALANCES as at June 30, 1936, held in respect of the items shown on Annex IVb . . . . .	781,009.57	108,940. 4. 1
	2,918,706.69	407,898. 3. 4

NOTE — The definitive bond of the American issue of the Loan contains a "gold coin" clause but the Austrian

AUDITORS'

We have audited the Books and Accounts of the Trustee for the Austrian Government International and Disbursements is correctly prepared therefrom and, read together with the Note thereon, properly by certificates obtained from the depositaries.

BASLE, October 8, 1936.

## GOVERNMENT INTERNATIONAL LOAN 1930

for the Sixth Loan Year (July 1, 1935 to June 30, 1936)

Italian Issue Lire	Swedish Issue Sw. Cr.	Swiss Issue Sw. Fr.	Austrian Issue Sch.	General Expenses	
				£	Sw. Fr.
3,250,101.55	521,955.20	824,125.16	2,096,232.29	—	—
6,095,689.49	645,716.14	1,520,800.65	3,954,187.07	—	—
41,348.15	—	8,804.84	—	—	—
10,883.20	202,965.—	6,644.84	1,447,816.95	—	—
2,262,966.80	—	566,435.16	—	—	—
30,622.50	2,909.50	7,645.80	18,180.32	300.—.—	27,634.80
9,165.30	3,907.50	2,279.49	—	—	—
11,700,776.99	1,377,453.34	2,936,735.94	7,516,416.63	300.—.—	27,634.80

6,198,800.42	655,480.—	1,544,901.15	3,988,079.83	—	—
41,348.15	—	8,804.84	—	—	—
—	190,550.—	—	—	—	—
—	—	6,820.—	1,411,229.99	—	—
11,559.58	—	—	—	—	—
2,262,966.80	—	566,435.16	—	—	—
33,409.52	3,508.65	7,893.67	23,350.06	300.—.—	27,634.80
3,152,692.52	527,914.69	801,881.12	2,093,756.75	—	—
11,700,776.99	1,377,453.34	2,936,735.94	7,516,416.63	300.—.—	27,634.80

Government, following the practice adopted in July 1933, has not provided the sums necessary to give effect thereto.

### CERTIFICATE

Loan 1930 for the sixth fiscal year ending June 30, 1936 and certify that the above Statement of Receipts sets forth the transactions for that year. We have also verified the bank balances on hand at June 30, 1936

PRICE, WATERHOUSE & Co.  
Chartered Accountants.

# TRUSTEE FOR THE AUSTRIAN

## Statement of Funds in the hands

The Bank Balances as at June 30, 1936 were held in respect of:—

- |   |  |
|---|--|
| 1. (a) Unpresented matured coupons . . . . .  |  |
| (b) Interest coupons maturing on July 1, 1936 . . . . .   |  |
| 2. Expenses accrued to June 30, 1936, but not claimed until thereafter . . . . .  |  |
| Funds on hand for the liquidation of accrued or accruing liabilities . . . . .  |  |
| 3. Bond redemption account . . . . .  |  |
| 4. Other funds on hand (of which Sw. Fr. 5,609.80 is deposited with a bank formerly a Paying Agent, which has suspended payments) . . . . . |  |
| Total balances on hand as per Statement of Receipts and Payments — Annex IVa . . . . .  |  |

## Statement of Bonds outstanding

- |   |  |
|---|--|
| Nominal value of bonds issued . . . . .   |  |
| Less: Nominal value of bonds redeemed during:—                                    |  |
| 1. First five Loan years . . . . .  |  |
| 2. Sixth Loan year . . . . .  |  |
| Nominal value of bonds outstanding as at June 30, 1936 (see note below) . . . . . |  |

NOTE: When drawn for redemption,

## GOVERNMENT INTERNATIONAL LOAN 1930

of Depositories as at June 30, 1936

American Issue \$	British and Dutch Issues £	Italian Issue Lire	Swedish Issue Sw. Cr.	Swiss Issue Sw. Fr.	Austrian Issue Sch.
12,894.— 748,986.— 1,959.45	990.10.— 105,542.10.— —.—. 6	29,195.25 3,026,240.— 15,406.37	— 321,265.— 1,852.78	15,890.— 757,050.— 3,866.25	55,477.94 1,954,323.84 9,793.87
763,839.45 26.79 17,143.33 781,009.57	106,533.—. 6 19. 6. 5 2,387.17. 2 108,940. 4. 1	3,070,841.62 160.88 81,690.02 3,152,692.52	323,117.78 203,075.— 1,721.91 527,914.69	776,806.25 638.26 24,436.61 801,881.12	2,019,595.65 36,667.64 37,493.46 2,093,756.75

as at June 30, 1936

25,000,000	3,500,000	100,000,000	10,000,000	25,000,000	50,000,000
3,006,100 594,300	404,100 80,400	10,778,000 2,758,000	636,000 185,000	2,760,000 610,000	5,305,100 1,071,600
21,399,600	3,015,500	86,464,000	9,179,000	21,630,000	43,623,300

bonds are repayable at 103 per cent.

# TRUSTEE FOR THE AUSTRIAN

## Interim Statement of Receipts and

	Dollars
Nominal amount originally issued . . . . .	25,000,000.—
Nominal amount outstanding as at December 31, 1936 . . . . .	21,089,200.—

### Receipts

1. BANK BALANCES as at July 1, 1936 . . . . .	781,009.57
2. RECEIVED FROM THE AUSTRIAN GOVERNMENT in respect of:—	
Interest coupons	
In cash . . . . .	727,687.82
Accrued in bonds ceded for cancellation (see below) . . . . .	4,530.75
Bond redemption	
In cash . . . . .	530.53
In bonds ceded for cancellation (see below) . . . . .	314,983.47
Expenses . . . . .	1,879.50
3. INTEREST RECEIVED on cash employed pending application to service of the Loan . . . . .	540.91
	1,831,162.55

### Payments

1. INTEREST	
Matured coupons paid and accrued interest paid on bonds purchased for redemption . . . . .	749,064.73
Accrued interest on bonds ceded by the Austrian Government (see above) . . . . .	4,530.75
2. REDEMPTION	
Bonds purchased for redemption . . . . .	487.50
Bonds ceded by the Austrian Government against refund of cash . . . . .	—
Bonds ceded by the Austrian Government in part-payment of service instalments (see above) . . . . .	314,983.47
3. EXPENSES	
Commission and expenses of Paying Agents and fees and expenses of Trustee . . . . .	2,405.04
4. BANK BALANCES as at December 31, 1936, in respect of:—	
Interest coupons maturing on January 1, 1937 . . . . .	738,122.—
Bonds drawn for payment on January 1, 1937 . . . . .	—
Matured coupons unrepresented . . . . .	12,824.—
Bond redemption . . . . .	69.82
Miscellaneous items (of which Sw. Fr. 5,609.80 is deposited with a bank formerly a Paying Agent, which has suspended payments) . . . . .	8,675.24
	1,831,162.55

## GOVERNMENT INTERNATIONAL LOAN 1930

Payments for the half-year ended December 31, 1936

Sterling	Lire	Swedish Crowns	Swiss Francs	Schillings
3,500,000.—.—	100,000,000.—	10,000,000.—	25,000,000.—	50,000,000.—
2,972,700.—.—	84,895,000.—	9,179,000.—	21,313,000.—	43,488,500.—

108,940. 4. 1	3,152,692.52	527,914.69	801,881.12	2,093,756.75
102,824.—. 9	2,924,050.80	319,831.99	735,136.22	1,918,163.73
627. 7. 1	23,520.03	—	3,842.41	—
325. 8.10	3,375.03	104,720.—	27,929.70	771,916.15
43,162. 1. 2	1,230,079.97	—	279,960.30	—
633.15.—	15,104.25	1,444.50	17,808.70	8,906.79
147. 9. 1	4,483.66	2,249.68	1,117.41	—
256,460. 6.—	7,353,306.26	956,160.86	1,867,675.86	4,792,743.42

105,382. 4. 5	2,922,015.85	321,265.—	755,179.05	1,964,755.84
627. 7. 1	23,520.03	—	3,842.41	—
283.—. 7	—	—	10,007.50	19,650.—
—	1,559.15	—	18,540.—	157,944.32
43,162. 1. 2	1,230,079.97	—	279,960.30	—
736.19.—	16,576.12	1,606.33	17,884.09	10,205.74
104,044.10.—	2,971,325.—	321,265.—	745,955.—	1,948,284.80
—	—	202,910.—	—	—
1,155.—.—	133,460.25	—	18,585.—	49,738.06
61.14. 8	1,976.76	104,885.—	20.46	630,989.47
1,007. 9. 1	52,793.13	4,229.53	17,702.05	11,175.19
256,460. 6.—	7,353,306.26	956,160.86	1,867,675.86	4,792,743.42

## INTERNATIONAL LOANS

FOR WHICH THE BANK IS TRUSTEE OR FISCAL AGENT FOR THE TRUSTEES

Funds on hand as at March 31, 1937

	German External Loan 1924	German Govt. International 5½% Loan 1930	Austrian Govt. International Loan 1930	Totals
Swiss gold francs				
<b>FUNDS HELD IN RESPECT OF:—</b>				
Redemption of bonds . . . . .	639,467.49	732.79	127,370.—	767,570.28
Interest in respect of the next coupon falling due . . . . .	—	—	3,084,267.39	3,084,267.39
Drawn bonds not yet presented for re- demption . . . . .	3,632.10	—	—	3,632.10
Interest coupons due but unrepresented	106,420.95	94,631.74	243,422.58	444,475.27
Miscellaneous items . . . . .	394,632.44	56,147.66	19,008.03	469,788.13
<b>TOTALS . .</b>	<b>1,144,152.98</b>	<b>151,512.19</b>	<b>3,474,068.—</b>	<b>4,769,733.17</b>

**THE TRIPARTITE MONETARY AGREEMENT**

of September 25, 1936.

**Statement of French Government**

**relating to monetary agreement**

**reached between**

**France, United States and Great Britain. (\*)**

**September 25, 1936.**

1. The French Government, after consultation with the United States Government and the British Government, join with them in affirming a common desire to foster those conditions which will safeguard peace and will best contribute to the restoration of order in international economic relations, and to pursue a policy which will tend to promote prosperity in the world and to improve the standard of living of peoples.

2. The Governments of the United States of America and of Great Britain must, of course, in their policy towards international monetary relations, take into full account the requirements of internal prosperity of the American Republic and of the British Empire, as corresponding considerations will be taken into account by the French Government in regard to the economic system of the country itself and of its overseas possessions. They welcome this opportunity to reaffirm their purpose to continue the policy which they have pursued in the course of recent years, one constant object of which is to maintain the greatest possible equilibrium in the system of international exchanges and to avoid to the utmost extent the creation of any disturbance of that system by American or British monetary action. The French Government share with the Governments of the United States and of Great Britain the conviction that the continuation of this two-fold policy will serve the general purpose which all Governments should pursue.

3. The French Government, judging that the desired stability of the principal currencies cannot be ensured on a solid basis except after the re-establishment of a lasting equilibrium between the various economic systems, have decided with this object to propose to their Parliament the readjustment of their currency. The Governments of the United States and of Great Britain have welcomed this decision in the hope that it will establish more solid foundations for the stability of international economic relations. The Governments of the United States of America, of Great Britain and of France declare their intention to continue to use the appropriate available resources so as to avoid as far as possible any disturbance of the basis of international exchanges resulting from the proposed readjustment. They will arrange for such consultation for this purpose as may prove necessary with the other two Governments and the authorised agencies.

4. The French Government are moreover convinced, as are also the Governments of the United States of America and of Great Britain, that the success of the policy set forth above is linked with the development of international trade. In particular, they attach the greatest importance to action being taken without delay to relax progressively the present system of quotas and exchange controls with a view to their abolition.

(\*) Translation.

5. The French Government, in common with the Governments of the United States of America and of Great Britain, desire and invite the cooperation of the other nations to realise the policy laid down in the present declaration. They trust that no country will attempt to obtain an unreasonable competitive exchange advantage and thereby hamper the effort to restore more stable economic relations, which it is the aim of the three Governments to promote.

**Statement of British Treasury**  
relating to monetary agreement  
reached between  
**Great Britain, France and United States.**  
September 25, 1936.

1. His Majesty's Government, after consultation with the United States Government and the French Government, join with them in affirming a common desire to foster those conditions which will safeguard peace and will best contribute to the restoration of order in international economic relations, and to pursue a policy which will tend to promote prosperity in the world and to improve the standard of living.

2. His Majesty's Government must, of course, in its policy towards international monetary relations, take into full account the requirements of internal prosperity of the countries of the Empire, as corresponding considerations will be taken into account by the Governments of France and of the United States of America. They welcome this opportunity to reaffirm their purpose to continue the policy which they have pursued in the course of recent years, one constant object of which is to maintain the greatest possible equilibrium in the system of international exchanges and to avoid to the utmost extent the creation of any disturbance of that system by British monetary action. His Majesty's Government share with the Governments of France and the United States the conviction that the continuation of this two-fold policy will serve the general purpose which all Governments should pursue.

3. The French Government inform His Majesty's Government that, judging that the desired stability of the principal currencies cannot be ensured on a solid basis except after the re-establishment of a lasting equilibrium between the various economic systems, they have decided with this object to propose to their Parliament the readjustment of their currency. His Majesty's Government have, as also the United States Government, welcomed this decision in the hope that it will establish more solid foundations for the stability of international economic relations. His Majesty's Government, as also the Governments of France and of the United States of America, declare their intention to continue to use the appropriate available resources so as to avoid as far as possible any disturbance of the basis of international exchanges resulting from the proposed readjustment. They will arrange for such consultation for this purpose as may prove necessary with the other two Governments and the authorised agencies.

4. His Majesty's Government are moreover convinced, as are also the Governments of France and the United States of America, that the success of the policy set forth above is linked with the development of international trade. In particular, they attach the greatest importance to action being taken without delay to relax progressively the present system of quotas and exchange controls with a view to their abolition.

5. His Majesty's Government, in common with the Governments of France and the United States of America, desire and invite the cooperation of the other nations to realise the policy laid down in the present declaration. They trust that no country will attempt to obtain an unreasonable competitive exchange advantage and thereby hamper the effort to restore more stable economic relations, which it is the aim of the three Governments to promote.

**Statement of United States Secretary of the Treasury**  
**announcing the monetary agreement**  
**reached between:**  
**United States, France and Great Britain.**  
**September 25, 1936.**

By authority of the President, the Secretary of the Treasury makes the following statement:

1. The Government of the United States, after consultation with the British Government and the French Government, joins with them in affirming a common desire to foster those conditions which safeguard peace and will best contribute to the restoration of order in international economic relations and to pursue a policy which will tend to promote prosperity in the world and to improve the standard of living of peoples.

2. The Government of the United States must, of course, in its policy toward international monetary relations take into full account the requirements of internal prosperity, as corresponding considerations will be taken into account by the Governments of France and Great Britain; it welcomes this opportunity to reaffirm its purpose to continue the policy which it has pursued in the course of recent years, one constant object of which is to maintain the greatest possible equilibrium in the system of international exchange and to avoid to the utmost extent the creation of any disturbance of that system by American monetary action. The Government of the United States shares with the Governments of France and Great Britain the conviction that the continuation of this two-fold policy will serve the general purpose which all the Governments should pursue.

3. The French Government informs the United States Government that, judging that the desired stability of the principal currencies cannot be insured on a solid basis except after the re-establishment of a lasting equilibrium between the various economic systems, it has decided with this object to propose to its Parliament the readjustment of its currency. The Government of the United States, as also the British Government, has welcomed this decision in the hope that it will establish more solid foundations for the stability of international economic relations. The United States Government, as also the British and French Governments, declares its intention to continue to use appropriate available resources so as to avoid as far as possible any disturbance of the basis of international exchange resulting from the proposed readjustment. It will arrange for such consultation for this purpose as may prove necessary with the other two Governments and their authorised agencies.

4. The Government of the United States is moreover convinced, as are also the Governments of France and Great Britain, that the success of the policy set forth above is linked with the development of international trade. In particular it attaches the greatest importance to action being taken without delay to relax progressively the present system of quotas and exchange controls with a view to their abolition.

5. The Government of the United States, in common with the Governments of France and Great Britain, desires and invites the cooperation of the other nations to realise the policy laid down in the present declaration. It trusts that no country will attempt to obtain an unreasonable competitive exchange advantage and thereby hamper the effort to restore more stable economic relations, which it is the aim of the three Governments to promote.

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3rd May 1937.