

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE: October 12, 1934.

TO Mr. Eccles

FROM Mr. Edmiston

Re: The Australian Situation

I have just been checking up on the policy followed by the Australian Government in the current depression. The information about Australian budgetary inflation and public works program which Mr. Currie gave you in the conference we had with him sometime ago was not in the magnitude that he seemed to indicate. He tells me that Mr. Copland who was recently in this country and who was a member of the Government Committee that was instrumental in formulating the program, had given an erroneous impression as to the extent of the short-term financing operations and the public works spending program of the Government.

The inflationary action of the Commonwealth Bank was of rather small magnitude and was significant in increasing the deposits of the banks of the country and in forestalling the terrific deflationary pressure which a country, that depends very considerably for its national income upon the export of foodstuffs and raw materials which had fallen so greatly in price during the depression, would ordinarily be subject to.

What happened was that the short term debt of the Commonwealth and the various States was increased to take care of the budgetary deficit and the Commonwealth Bank which is the central bank of the country increased its holdings of short term Government loans by about 40 million pounds during the period from 1929 to 1933. An operation of this type has a somewhat similar effect to that of open-market operations in this

country and the commercial banks of Australia found their deposits and reserves increased.

Of course the difficulties of Australia were intensified by their unfavorable balance of trade and the necessity of making interest payments abroad. These payments become much more difficult when the prices of their exports were rapidly declining in the world market. Under these circumstances the banks were placed under great deflationary pressure and there was a continual decline in the deposits of the commercial banks until September 1951. From that time on the action of the central bank in putting out new funds had the effect of increasing deposits and improving the liquid position of the Australian commercial banks, consequently these banks started a small expansion of loans and investments. With the expansion of central bank credit, increased deposits in banks and no public long term borrowing, combined with a heavy decline in the demand for private investment the rate of interest naturally fell. Government credit improved but there were no attempts to refund bonds upon a long term basis. In October 1952 the Commonwealth Bank began a funding operation when Government 4% bonds reached par. The effort, however, was not successful and the loan of 8 million pounds at $5\frac{1}{4}$ which was offered failed to attract sufficient public support and a portion was left with the underwriting banks. Later, however, as the banking situation continued to improve with further purchases of short-term bills by the Commonwealth Bank and as there was an increase in general business activity in the last half of 1952 and early 1953, the Government and the Bank decided to float a 5 million pound loan for public works and this was highly successful at the rate of $5\frac{3}{4}$.

It is to be noted that these operations were of relatively small

amount and although the expansion of central bank credit was over 40% during the period of the whole depression, the budgetary deficit and public works programs were not of any considerable amount. The budget deficit itself amounted to approximately a little over 40 million pounds for the 4 years ending June, 1954. The public works fund itself does not show up separately in the figures for Government expenditures and the total expenditures of the Commonwealth and States decreased at the rate of about 5 million pounds a year during this period.

The table below shows the deposits and advances of the Australian commercial banks over the period under consideration.

CASH DEPOSITS AND ADVANCES OF THE TRADING BANKS

Quarter ended	Total Deposits £ m.	Advances and securities £ m.
Sept. 1929	279.5	281.9
Dec. 1929	277.2	292.0
Mar. 1950	274.4	287.7
June 1950	268.6	282.0
Sept. 1950	262.5	276.7
Dec. 1950	265.4	278.0
Mar. 1951	265.5	268.9
June 1951	261.4	262.6
Sept. 1951	255.8	268.4
Dec. 1951	268.5	269.8
Mar. 1952	285.6	268.2
June 1952	275.0	272.9
Sept. 1952	268.0	279.4
Dec. 1952	274.6	285.8
Mar. 1953	276.9	285.0
June 1953	274.7	286.9

Thus in general the Australian policy was not significantly inflationary but did in part offset the tremendous deflationary pressure that the country was subject to. Also, the Government took certain deflationary steps in their program by cutting some types of Government expenses

and the only really inflationary policy was with regard to their short-term borrowing from the central bank, which increased reserves of the other commercial banks and kept up Government expenditures to a higher level than they otherwise would have been had the Government had to finance through long-term bonds. The central bank policy lead to lower interest rates and helped the commercial banks but did not have an important effect in increasing the total monetary incomes of the country which would be available for new expenditure for goods and services and increase greatly production and employment. The results of their policy must be considered as negative in merely forestalling deflation rather than positive in creating recovery.

Source of information:

"Australia in the World Crisis 1929-1933"

By - Douglas Barry Copland

Published by Macmillan Company, Cambridge, England, 1934.