BRITISH GOLD STANDARD ACT AND REPORT OF COMMITTEE ON CURRENCY

There is presented below the text of the bill passed by the British Parliament "to facilitate the return to a gold standard and for purposes connected therewith." Following the bill is the full text of the report of the committee of experts on the currency and Bank of England note issues presented on February 5 and made public on April 28.

GOLD STANDARD ACT, 1925

1. (1) Unless and until His Majesty by proclamation otherwise directs—

(*a*) The Bank of England, notwithstanding anything in any act, shall not be bound to pay any note of the bank (in this act referred to as "a bank note") in legal coin within the meaning of section 6 of the Bank of England act, 1833, and bank notes shall not cease to be legal tender by reason that the bank does not continue to pay bank notes in such legal coin.

(*b*) Subsection (3) of section 1 of the currency and bank notes act, 1914 (which provides that the holder of a currency note shall be entitled to obtain payment for the note at its face value in gold coin), shall cease to have effect.

(*c*) Section 8 of the coinage act, 1870 (which entitles any person bringing gold bullion to the mint to have it assayed, coined, and delivered to him), shall, except as respects gold bullion brought to the mint by the Bank of England, cease to have effect.

(2) So long as the preceding subsection remains in force the Bank of England shall be bound to sell to any person who makes a demand in that behalf at the head office of the bank during the office hours of the bank, and pays the purchase price in any legal tender, gold bullion at the price of £3 17s. 10½d. per ounce troy of gold of the standard of fineness prescribed for gold coin by the coinage act, 1870, but only in the form of bars containing approximately 400 ounces troy of fine gold.

2. (1) Any money required for the purpose of exchange operations in connection with the return to a gold standard may be raised within two years after the passing of this act in such manner as the treasury think fit, and for that purpose they may create and issue, either within or without the United Kingdom and either in British or in any other currency, such securities bearing such rate of interest and subject to such conditions as to repayment, redemption, or otherwise as they think fit, and may guarantee in such manner and on such terms and conditions as they think proper the payment of interest and principal of any loan which may be raised for such purpose as aforesaid:

Provided that any securities created or issued under this section shall be redeemed within two years of the date of their issue, and no guarantee shall be given under this section so as to be in force after two years from the date upon which it is given.

(2) The principal and interest of any money raised under this act, and any sums payable by the treasury in fulfilling any guarantee given under this act, together with any expenses incurred by the treasury in connection with, or with a view to the exercise of, their powers under this section shall be charged on the consolidated fund of the United Kingdom or the growing produce thereof.

(3) Where by any appropriation act passed after the commencement of this act power is conferred on the treasury to borrow money up to a specified amount, any sums which may at the time of the passing of that act have been borrowed or guaranteed by the treasury in pursuance of this section and are then outstanding shall be treated as having been raised in exercise of the power conferred by the said appropriation act and the amount which may be borrowed under that act shall be reduced accordingly.

3. This act may be cited as the gold standard act, 1925.

REPORT OF THE COMMITTEE ON THE CURRENCY AND BANK OF ENGLAND NOTE ISSUES

TREASURY MINUTE DATED JUNE 10, 1924

The Chancellor of the Exchequer proposes to the board that the following committee should be appointed to consider whether the time has now come to amalgamate the Treasury note issue with the Bank of England note issue, and, if so, on what terms and conditions the amalgamation should be carried out: The Right Hon. Austen Chamberlain, M. P. (chairman); Sir John Bradbury, G. C. B.; Mr. Gaspard Farrer; Sir O. E. Niemeyer, K. C. B.; and Mr. A. C. Pigou.

My lords concur.

TEXT OF REPORT

May it please your lordships,

(1) By Treasury minute of June 10, 1924, we were appointed a committee to consider whether the time has now come to amalgamate the Treasury note issue with the Bank of England note issue, and, if so, on what terms and conditions the amalgamation should be carried out.

(2) We have held 9 meetings and have heard 13 witnesses, including the governor of the Bank of England, Mr. McKenna, Sir Robert Horne, Professor Cannan, Sir George Paish, Mr. Keynes and representatives of the clearing banks, the Association of British Chambers of Commerce, and the Federation of British Industries.

(3) The greater part of our evidence was taken during the months of June, July, and September, 1924, when the sterling dollar exchange was still at a discount of 10 to 12 per cent, but we heard the governor of the Bank of England a second time on the 28th of January, 1925.

On accepting office as Secretary of State for Foreign Affairs, Mr. Chamberlain ceased to act as a member of the committee. Sir John (now Lord) Bradbury took the chair at the remaining meetings.

THE CUNLIFFE COMMITTEE'S RECOMMENDATION

(4) The natural starting point of our inquiry was the recommendation of the committee on currency and foreign exchanges after the war (the Cunliffe committee), that the currency note issue should be transferred to the Bank of England when it had been ascertained, from experience in a free gold export market, what fiduciary issue is compatible with the maintenance of a central gold reserve of £150,000,000.

(5) These conditions have not yet been fulfilled, and we have found it necessary to enter somewhat fully into the questions whether a return to the gold standard on the basis of the pre-war sovereign is, in present circumstances, no less desirable than at the time of the Cunliffe committee's report; and if so, how and when the steps required to achieve it should be taken.

THE GOLD STANDARD

(6) The alternatives are—

(*a*) To return to the gold standard on the basis of a devalued sovereign, i. e., the reestablishment of a free gold market with a unit identical in name but of a lesser gold content than the pre-war unit, and

(*b*) To attempt to find a basis for the currency unit other than gold.

(7) The former need not, now that the current exchange rates are already within a small percentage of the pre-war parity, be seriously considered. It was never, in our opinion, a policy which the United Kingdom could have adopted.

(8) The latter, in the form of proposals for substituting the price level of commodities in general for gold as the regulating principle of the currency, has been fully and carefully explained in evidence before us. We need not here set out the arguments by which it is supported, which have been published and are now well known. We need only say that, as a practical present-day policy for this country, there is, in our opinion, no alternative comparable with a return to the former gold parity of the sovereign. In this conclusion we are supported by the overwhelming majority of opinion, both financial and industrial, represented in evidence before us.

(9) Starting from this fundamental position, we propose to confine ourselves to answering the questions when and how this restoration is to be brought about.

(10) When we first began to consider our report in September last, the ruling rates of exchange on New York were still 10 to 12 per cent below gold parity, and there was some anxiety whether the normal autumn pressure would not result in a renewed depreciation of the pound, and whether the limitation on the amount of the fiduciary issue of currency notes prescribed by the Treasury minute of December 15, 1919, could be maintained over Christmas without giving rise to conditions necessitating a sharp rise of money rates.

(11) We entertained no doubt, however, even at that time, of the ability of Great Britain, notwithstanding the fact that her international financial situation is in some respects less satisfactory than it was before the war, to restore and maintain the gold standard at the pre-war parity, at any time it might be thought prudent to do so.

(12) In spite of the special influences which have, during the last few years, exercised an adverse influence (of which the principal are industrial stagnation and the disturbance of international trade resulting from post-war conditions, and the fact the we are paying interest and sinking fund on our war debt to America without as yet receiving an adequate counterpart from our continental debtors), our existing volume of exports, visible and invisible, together with the income we derive from foreign investments is still undoubtedly sufficient to meet our foreign debts and pay for our necessary imports, and even to supply a moderate balance for new foreign investment.

(13) In these circumstances a free gold market could readily be established and maintained at the pre-war parity, provided that by control of credit we adjusted the internal purchasing power of the pound to its exchange parity, and restricted our foreign investments to our normal export surplus.

(14) Further, we were satisfied that the mere announcement that the power to prohibit the export of gold would not be continued beyond December 31, 1925, would automatically and rapidly bring about the credit conditions necessary to effect these adjustments, and that the effective gold standard could thus be restored without further danger or inconvenience than that which is inevitable in any period of credit restriction and falling prices.

(15) At that time the British and American price levels appeared on the surface—though it is not safe to attempt to draw precise conclusions from a comparison of index figures compiled on different bases—to be fairly well adjusted to the current rate of exchange; and it was, therefore, to be expected that a fall in sterling prices of some 10 or 12 per cent, or a similar rise in dollar prices, would have had to take place before equilibrium could be secured with the exchanges at the pre-war parity.

(16) The problem as it then presented itself was whether the undoubted advantages of an immediate return to parity were a sufficient compensation for the inconveniences—temporary though possibly severe while they lasted—of the measure of "deflation" necessary to bring about the adjustment, or whether it would not be more prudent to pursue, at least for a few months longer, a waiting policy in the hope that the disparity would disappear through a rise in American prices (of the probability of which there appeared to be indications).

(17) Our provisional conclusion was that the return to parity and resumption of the free gold market, though it ought not to be much longer deferred, could not be regarded as a matter of such extreme urgency as to justify a credit policy calculated to bring down domestic prices if the same practical result could reasonably be expected to be attained within a very few months by a policy designed merely to prevent them from rising concurrently with a rise elsewhere.

(18) The favorable course since September of the dollar exchange (which now stands only 1½ per cent below gold parity) and the fact that the restrictions on the fiduciary issue of currency notes have been maintained without inconvenience have, however, altered the situation. Indeed, if British domestic prices had already adjusted themselves to the improved exchange value of sterling, the problem would have been solved and we are satisfied that the free export of gold could have been resumed forthwith without danger either of appreciable depletion of our existing gold reserves or of making recourse necessary to any special measures in restriction of credit.

(19) The discrepancy between British and American gold prices which existed in September has not, however, disappeared, though it has been reduced. We must still be prepared to face a fall in the final price level here of a significant, though not very large, amount, unless it should happen that a corresponding rise takes place in America, if the rate of exchange is to be restored to and held at the pre-war parity.

(20) In present conditions, however, this argument against immediate action has not, in our opinion, great weight. For the adjustment of price levels required to restore and maintain pre-war parity needs to be only some 1½ per cent larger than that required to hold the exchange at its present rate. If the adjustment of price levels necessary to this end is long deferred, the exchange will inevitably fall back to the

rate justified by the comparative price levels—or below it, since the psychological causes which have operrated to force it up will tend to act in the other direction—and a period of fluctuating values is likely to ensue. To allow the exchange to fall back now with the certainty of having later on to raise it again would be a short-sighted policy, injurious to trade and industry. But, if this view is accepted and we are prepared to face any price adjustment which may be necessary to maintain the present exchange rate, there is nothing to be said for refusing to accept the very small (1½ per cent) extra adjustment involved in the reestablishment of an effective gold standard.

(21) The attitude of the Dominions and foreign countries toward the question of an early return to the gold standard is also a material consideration. The Union of South Africa has already decided to take the step in the course of this summer. Other Dominions will undoubtedly follow our lead and may if we delay precede us. The same is true of Holland and Switzerland and possibly other European countries. Although the convertibility of the new German currency into gold is under existing legislation suspended, a high degree of stability has been attained and the establishment of the full gold standard—effectively and even formally—may take place in the early future.

(22) Economic conditions in America give promise of a period of financial stability, thus reducing the risk of dangerous reactions during the initial months of a free gold market; and prevailing sentiment there would be likely to be helpful.

(23) We therefore recommend that the early return to the gold basis should forthwith be declared to be the irrevocable policy of His Majesty's Government and that it should be definitely stated that the existing restrictions on the export of gold, which expire on the 31st December next, will not be renewed. A general license should at the same time be given to export gold sold by the bank for export and the bank should between now and the date of expiry of the export prohibition avail themselves freely of it whenever the exchange is below the normal export specie point, making good any consequential drafts upon the reserve in the Banking Department in accordance with traditional practice. As from the date of the announcement until such time as the arrangements governing the fiduciary issue can be put on a permanent basis, the existing limitation of that issue should be strictly maintained.

(24) We are satisfied that this policy can, given the loyal cooperation of the principal British institutions which control the supply of credit, be carried through without risk by the Bank of England without external assistance. Indeed such assistance, if it took the form of foreign credits to be used on any considerable scale to mitigate the effect of the policy upon credit conditions in the United Kingdom, would really serve to counteract the very forces on the operation of which we rely for its success.

(25) On the other hand, the existence of a substantial American credit known to be available for use in sudden emergencies would tend to discourage speculation and contribute to the creation of a general atmosphere of confidence favorable to the smooth working of the operation.

(26) The appreciation of sterling which has taken place since November, 1924, has been due partly to the belief that an effective gold standard will shortly be restored in this country, and only partly to a lessening of the difference between the purchasing power of sterling and of gold.

(27) In so far as this confidence in the future of sterling has allowed the resumption of those normal operations between New York and London which had been interrupted by political uncertainty and distrust in the preceding 12 months, no reactionary consequences are to be feared.

(28) There has, however, undoubtedly been a considerable element of speculation in connection with that movement, the extent of which can not be exactly determined. To this unknown extent there may be a tendency, when parity has been reached, for realization of the speculative positions to throw a concentrated strain on the exchange.

(29) The proper safeguard against such a danger is in the size of the gold reserves and in the resolute use of these reserves (if required) for the purposes for which they have been accumulated.

(30) We believe that the existing gold reserves are amply sufficient for this purpose, and that a conviction that there will be no hesitation in using them, even though this may involve a temporary increase in bank rate, will go far to obviate the danger we refer to. If, however, it is thought necessary to make assurance doubly sure by the provision of a gold credit, we feel strongly that recourse should not be made to it unless and until substantial gold exports have taken place and are already producing their normal effects on the monetary situation at home, and in the event of the credit being actually drawn upon, the amount drawn should, until it has been repaid, be treated from the point of view of the Bank of England's monetary policy as equivalent to a corresponding loss from its own reserves.

(31) Unless these precautions are taken, borrowing abroad will, as has again and again happened when it has been resorted to as a remedy for exchange difficulties, merely aggravate the mischief which it has been applied to cure.

(32) In making these observations and suggesting these precautions, we must not be understood as anticipating that either the steps which we propose should be taken at once to prepare the way for the return to a free gold market at the end of the year or the actual return on that date may be expected to lead either to a heavy loss of gold or to a serious consequential restriction of domestic credit. British experience of the restoration of the gold standard after the French wars, 100 years ago, and the recent experience of continental countries which have taken steps, under far more difficult conditions, to rehabilitate their currencies, have shown that a courageous policy in currency matters surmounts apparently formidable obstacles with surprising ease. We believe that on this point history will repeat itself. It is possible that some temporary increase in money rates will be necessary to bring about the necessary adjustment of sterling prices to the gold level. We are satisfied, however, that the assimilation of British currency to the gold currencies of the world is so necessary for the ultimate prosperity of British trade that any temporary disadvantage, if such arise, from the measures necessary to maintain parity will be many times outweighed.

(33) Indeed, such credit restriction as may become necessary to adjust the general level of sterling prices to a free gold market may well be less drastic than that which would be required in order to maintain a "managed" pound in the neighborhood of parity. If the gold standard is firmly reestablished, the danger of apprehensions as to the future of exchange leading to sudden withdrawals of foreign balances or foreign investment money will be eliminated, and the risk—

inevitable under the present regimé—of excessive British lending to foreign countries will be reduced.

(34) With a free gold market, any tendency to lend abroad more than we can afford leads to a drain of gold, which, unless redressed by the sale of existing foreign investments, reacts on the general credit situation in London in such a way as to put a stop to new foreign borrowing.

(35) Under existing conditions the result of excessive lending to foreign countries instead of giving an immediate danger signal through its effect on the gold reserves is more obscurely reflected in the general disturbance of the exchanges.

(36) We are of the opinion that unless a free gold market is restored the danger of such overlending on foreign account in the near future will be considerable and a situation may easily develop in which the pressure on our foreign exchanges, resulting from overlending to foreign countries, will necessitate a restriction of general credit.

THE AMALGAMATION OF THE NOTE ISSUES

(37) We return now to the recommendation of the Cunliffe committee with respect to the amalgamation of the note issues. We have to consider whether the assumption by the Bank of England of the currency note issue must await the experience of the problem of maintaining a minimum gold reserve, whether of £150,000,000, as recommended by the Cunliffe committee, or of some other figure.

(38) It is clear that throughout their report the Cunliffe committee contemplated a much earlier removal of the prohibition of gold exports than has actually been deemed expedient, and suggestions have been made to us that the amalgamation of the issues should precede instead of following the restoration of the free gold market, with a view to indicating that the policy of the Government is to restore parity and for the sake of the effect of such an indication upon the foreign exchanges.

(39) If our recommendation in regard to the nonrenewal of the prohibition of gold exports is adopted the arguments for altering the sequence of events proposed by the Cunliffe committee cease to operate, and the precise date of amalgamation loses most of its importance. We associate ourselves with the decided preference expressed by the Cunliffe committee for the principle of a fixed fiduciary issue, and it is as true to-day as five years ago that the permanent fiduciary issue can not be fixed, except with reference to the actual conditions of a free gold market. It is hardly more feasible to legislate for a progressive reduction to the final figure by definite stages, at any of which the process may be subjected to unforeseen disturbances. The Treasury can not escape from the responsibility for the existing issue; we doubt whether the bank would accept it until the time when effective control can also be given to them.

(40) In this connection we think it necessary to observe that the ultimate dimensions both of the central gold reserve and of the fiduciary issue must be to some extent dependent on whether, after the restoration of the gold standard, gold is or is not largely used for internal circulation.

(41) The figure of £150,000,000 suggested for the gold reserve by the Cunliffe committee is based on the assumption that it will not be so used. If it were, a lower figure would suffice, regard being had to the value of gold in circulation as an emergency reserve, as was demonstrated in 1914. On the other hand, the total note circulation would be pro tanto reduced and the fiduciary portion would have to be smaller, both absolutely and proportionally than if there were no gold in circulation.

(42) Any considerable flow of gold into domestic circulation would thus necessitate imports of the metal which would place an unnecessary burden on our foreign exchanges in a very difficult period.

(43) We are of opinion that the use of gold for domestic circulation is a luxury which can well be dispensed with, and which we are in fact, at any rate during the next few years, not likely to be able to afford.

(44) The payment of notes in gold coin upon demand is not in itself essential to the maintenance of the gold standard under modern conditions. An obligation upon the bank of issue to buy and sell gold at a fixed price is all that is necessary, and if in fact specie payments had been suspended during the war, we should not have recommended their resumption.

(45) We should be glad, though mainly for historical and sentimental reasons, to make no formal change in the existing position under which gold coin is still legally obtainable for notes, and we think that the national habit of using paper currency, now firmly established, may suffice to prevent the absorption of any appreciable quantities of gold into domestic circulation, provided that the joint stock banks are able to assist such a policy by undertaking to abstain from asking for gold coin in exchange for notes either for themselves or for their customers, and from holding gold themselves, and in general by actively discouraging the use of gold among their customers.

(46) If, however, there is any doubt whether this will be effective, then we are decidedly of opinion that steps must be taken forthwith by legislative enactment to prevent the internal circulation of gold coin, until such time as the gold standard has been firmly reestablished for the purposes of international transactions.

(47) We think that, in any circumstances, all Bank of England notes, including the £1 and 10s. notes ultimately to be substituted for currency notes, should in future be payable in coin only at the head office of the bank, and not at the branch offices.

(48) In any case the coinage of standard half-sovereigns should not be resumed.

(49) Subject to this observation, we recommend that the policy with regard to the transfer of the currency note issue to the Bank of England should remain as recommended by the Cunliffe committee. We should mention that the machinery of issue by the Bank of England of £1 and 10s. Bank of England notes can not be improvised at short notice. We understand that if the bank is to print its own notes at least a year will be required to set up the necessary organization, and this must be borne in mind in order that sufficient notice may be given to the bank. As soon as parity is restored we recommend that the bank be authorized to begin the provision of this machinery. Legislation would also be required to enable the bank to issue notes below £5, and to make those notes legal tender.

(50) We anticipate that if the free gold market is restored at the end of 1925, the experience necessary to enable the amount of the fiduciary issue to be definitely fixed will have been obtained by the end of 1927. The transfer of the issue could then take place early in 1928. But it may well be possible to accelerate these dates in the light of experience.

BRADBURY.
GASPARD FARRER.
O. E. NIEMEYER.
A. C. PIGOU.

N. E. YOUNG, *Secretary*.
FEBRUARY 5, 1925.