

# SIGNS OF A NEW ORDER

## INTERNATIONAL CO-OPERATION ON CREDIT PROBLEMS

### TRUE FUNCTION OF CENTRAL BANKS

#### End of Professor Gregory's Lecture

We publish below the concluding section of Professor Gregory's lecture on International Finance. In it he declares that the germ of a new order, which may bring real international co-operation in the use of credit to stabilise prices, is to be seen in the creation of the Bank of International Settlements at Basle. The earlier parts of his lecture have already been published in "The Advertiser," the first appearing last Tuesday.

If you look at the balance-sheets and the constitution of the majority of the central banks in the modern world, you find they are required to keep a certain minimum reserve ratio against liabilities. For instance, the Federal reserve system is required to keep actually in gold against any note issue a minimum of 40 per cent., and against deposits 35 per cent.; but, in fact, if ever there were an internal panic in the United States, it would be met, not by paying out gold over the counter, but by paying out more notes. The only reason why the Federal reserve system wants to keep all that, is in case it has to make payments, or in case the American money market as a whole has to make payments, to other parts of the world. It does not require it for internal purposes, but for international payments.

Upon these very simple facts we economists rest the whole of our case for the international functioning of the central banks in the sphere of monetary regulation. We say that if only they will adjust the value of credit to the price level, instead of adjusting the price level to the value of credit, they can exert a pressure in the direction of stabilisation. You may ask how can they do it. They can do it by not worrying if they happen to hold only 25 per cent. of gold against the liabilities, instead of 35 per cent. In other words, as the price level falls, you work it back towards a position of greater stability by increasing the volume of credit against a given gold basis. That is the only way in which the central banks can affect the problem, but if they were to do it it would affect the problem in the shortest possible way.

#### Different Types of Bankers

Why do they not do it? The answer to that is a very complicated one. Let me indicate two reasons at least why this is not so easy as it looks at first sight. In the first place, there is a very large number of central banks in the world, and some of them are governed by persons of very much less economic intelligence and foresight than others. It is no use grumbling about that, but the fact remains that the degree of intelligence possessed by central bankers is not evenly distributed amongst all of them. There are some of them, like the governor of the Bank of France, who think that it is the aim of a central bank to accumulate, in the course of the financial year, more gold than is actually produced in the year, and available for addition to the monetary stock. If you have that kind of central bank, it is quite clear it is no good for economists to go around preaching the virtues of disgorging the quantity of gold you possess. If all the central bankers were like the governor of the Bank of France, you simply could not attempt co-operation at all. In the second place, even certain central bankers who possess a high degree of intelligence are unfriendly towards other countries, the population of which is not so highly educated as themselves. One of the difficulties of the modern central banking world is to secure the co-operation of the Federal Reserve System with the rest of the world in a combined and definite way. This reflects no discredit, say, upon the directors of the New York Reserve Bank, who are assisted by a highly competent economic and statistical staff, who are perfectly normal and well-educated human beings.

#### Influence of Politics

Unfortunately, they are surrounded by hordes and masses of voters, who are neither intelligent or highly educated, and who very strongly object to what they would describe as the entanglements of the Federal Reserve System, with its nefarious complications of European central banking. So long as the average middle-west voter holds this opinion we are not likely to get very much further with co-operation. If all central banks were agreed, it is not clear that the population which surrounds the central banks would fall in with the views which the central banks desire to express, and the policies they would desire to carry out. Therefore, although it is as clear daylight that the problem of the stabilisation of the price level can only be achieved, if it is going to be done at all, through the intimate co-operation of the central banks of the world, we think it is not clear as yet that we have reached a stage when central banks can effectively co-operate to secure this particular end.

Even if you had the whole of the central bankers of the world unanimous on this particular subject there is still one difficulty to which I want to draw your attention—the last of the many difficulties to which I have drawn your attention to-night. You can, as an international group of central bankers, do your best by the expansion of credit—in other words, by the

reduction of reserve ratios, by the reduction of bank rates, the purchase of securities in the open market, and what not—to increase the volume of credit, and therefore raise the price level, but it would be mere affectation to pretend that this is not a process which may take much longer than people think.

#### Heartbreaking Problem

For instance, the New York slump is already eleven months old. It came at the end of October, 1929; nevertheless, in spite of the fact that every central bank in the world has been pushing its bank rate down ever since, and that bank rates are still falling, prices are still falling, too. In other words, there is a time lag in these things, and it is sometimes of very long duration. In other words, you have not only to face certain technical difficulties of co-operation between the central bankers, but you are face to face with the difficulty that you must not expect a very intricate, a very highly integrated and complicated modern economic system, to respond to the efforts of central bankers as easily as a modern liner responds when you turn the wheel a little bit one way or the other. If economic life were as easily adjustable as that, it would be a highly delightful and very satisfactory thing; but, unfortunately, economic systems are much more rigid and less amenable to direct control than one would think at first sight. I am convinced in my own mind that the problem of prices, if it is going to be solved at all, must be solved by the agency of central bankers; but I am bound to admit that the process of solving this particular problem is much more heartbreaking than it appears at first sight.

#### Germ of New Order

For all these reasons it is just as well that there has been created one agency, which, in the course of years, certainly not in the immediate future, certainly not in the next twelve months, but in the long run, may help to overcome some of these difficulties. That is the institution that was created under the last definitive reparations settlement, namely, the so-called Bank of International Settlements at Basle. The Bank of International Settlements, in the first instance, was created to take the place of the old reparations machinery, by which Germany transferred reparations to her European and her American creditors; but the Bank of International Settlements contains the germ of a very fruitful institution, namely, it contains implicitly the idea that the central banks of the world should have for themselves a central bank with which they should all bank. Just as the commercial banks of a country, by banking with their central bank, can economise reserves, so, if all the central banks of the world were to keep their entire gold stocks with the Bank of International Settlements at Basle, in the end they could practise a highly desirable and highly useful economy of gold reserves. Of course, I need not conceal from you that we are very far from the day when the governor of the Bank of England, and particularly the governor of the Bank of France, will be willing to transfer the whole of their gold reserves to the keeping of a new institution in Swiss territory. There is the germ of a new international central banking order in the creation of the Bank of International Settlements, but it is only a germ.

#### International Co-operation

Meanwhile, the Bank of International Settlements serves a highly desirable purpose, because it represents a private meeting place for the heads of the various central banking institutions all over Europe. One of the difficulties connected with getting conferences of central bankers together is that everyone begins to ask, Why do they want a conference at this particular moment? And at once you have a renewed wave of uncertainty and unrest; but through the creation of the Bank of International Settlements the heads of the central banks can meet at Basle, and nobody takes too much notice. Of course, astute journalists all over Europe invent explanations of what central bankers say and do; but, in the course of time, everyone will accept it as a perfectly normal thing that, once a month, or once every two months, Mr. Norman and the president of the Reichsbank should go to Basle and discuss the affairs of the Bank of International Settlements. In other words, the problem of prices has not been solved. Even the problem of how to tackle the question has not been solved; but we have done two things in Europe. We are beginning to see the way in which the problem of prices must be solved, and we are beginning to understand the kind of machinery which will help us to solve it.