account and that the Gold Mining Company deposits its $2,500 worth of notes in a current account. The liability side of the Bank of Canada's balance sheet (No. 2 above) has now been determined in the following form:—

Chartered Bank Deposits	$ 6,000
Notes—in Hands of Banks	11,500
in Hands of Public	4,500
Capital and Other Liabilities	3,000
	$25,000

It is likely that the chartered banks would, for convenience of transfer, exchange some of their Bank of Canada notes for an increase in their deposits with the Bank of Canada. For present purposes it does not matter whether this happens or not. The important point is that their cash reserves have increased by $10,000.

For convenience of illustration we shall now assume that there is only one chartered bank operating in Canada. The changes in its balance sheet (hypothetical as to figures and condensed as to form) are shown below:—

3. Before

Assets		*Liabilities*	
Cash	$ 7,500	Deposits	$75,000
Loans and Investments	70,000	Capital	5,000
Other Assets	7,500	Other Liabilities	5,000
	$85,000		$85,000

4. After

Assets		*Liabilities*	
Cash (Previous 7,500+10,000 deposited by Gold Mining Company and John Smith)	$17,500	Deposits (Previous 75,000+10,000 from Gold Mining Company and John Smith)	$85,000
Loans and Investments	70,000	Capital	5,000
Other Assets	7,500	Other Liabilities	5,000
	$95,000		$95,000

As the balance sheets show the Chartered Bank's cash ratio has risen from the conventional 10 per cent (7,500:75,000) in No. 3 to 20·6 per cent (17,500:85,000) in No. 4.

The changes in earnings which have taken place up to this point are as follows:—

1. John Smith who had bonds giving him an income of $225 per year has, for reasons of his own, exchanged them for the more liquid form of a savings deposit, giving him only $112.50 per year. He has lost $112.50 a year in income.
2. The Bank of Canada, on the assumption that it had decided upon an expansionist policy, i.e. on the assumption that it took no action to offset this purchase by selling other bonds, would have increased its income by the interest on the $7,500 of bonds, i.e. by $225 a year.
3. The Chartered Bank would have added nothing to its earning assets, while its savings deposits would have increased by $7,500. Its net income would therefore have been reduced by the amount of interest it had to pay on the deposits, i.e. $112.50 a year, plus whatever net additional costs it might incur in servicing its increased deposits.

Summary

Loss of income to John Smith	$112.50 a year
Additional expense to Chartered Bank, at least	$112.50 a year
Additional earnings of Bank of Canada	$225.00 a year