Obviously, if the banks were forced to carry 100 per cent cash reserves against deposits, their loans and investments, in fact all their assets other than cash, would be restricted to an amount not exceeding their capital and reserve funds. At December 31st last this amount was $279 millions—an amount which is obviously inadequate to finance the requirements of agriculture, industry and individuals. As the banks would have very little in the way of earnings, they would be forced to eliminate any interest payments to depositors. To cover their operating expenses they would, in fact, have to require anyone who wanted to maintain a deposit account to pay a substantial charge for that service.

I am not sure that the suggestion was *intended* to convey a recommendation that the banks should be practically debarred from making loans and investments, and that presumably some other form of organization should be set up for this purpose. I say that I am not sure, because at a later point in the speech it is recommended that the reserve requirements should be increased "to a point where the banks will be able truly to say that for every dollar they loan they have to have a dollar on deposit." It is the case to-day that for every dollar the banks loan or invest they have a dollar on deposit. Under the system proposed they would have a dollar in *cash* for every dollar on deposit. But, as I have already stated, their loans, investments and other assets in that case could not exceed the amount of their capital and reserve fund.

Any policy of monetary expansion which leads to a material reduction in interest rates undoubtedly causes suffering to many people; but to the extent to which such a policy remedies maladjustments and raises the level of economic prosperity, there is some justification for it—a justification, however, which disappears when further monetary expansion becomes unnecessary. Quite apart from any risk of inflation—which might be offset by counter measures—an additional issue of currency to finance Government expenditures could be criticized as being a discriminating policy which would not ensure a fair distribution of the burden it would impose. In essence, therefore, Mr. Tucker's proposal that the Bank of Canada should issue additional currency to the Government, and that any inflationary effects should be obviated by an increase in the legal minimum cash ratio of the chartered banks, is not a proposal related to monetary policy but rather to taxation. As such, it comes within the sphere of Government fiscal policy rather than central banking activity.

I have gone into this matter at some length—perhaps the Committee will feel at undue length—because I am convinced that there are certain fundamental misconceptions—widely held—in respect to banking operations. If I am right in this belief, it must often be the case that proposals for changing the present procedure refer to a procedure which, in fact, does not exist. A discussion on this basis necessarily leads to considerable confusion.

(*b*) Further Analysis of the 100% Reserve Proposal

(Submitted by Mr. Towers in reply to Mr. Tucker)

(Volume 8, page 197)

I should like to make these remarks before replying to Mr. Tucker's question. During the meetings of the committee many of the questions which have been put to me have been really questions on matters of government policy. In such instances I do not believe that it is proper for me to state that certain policies should or should not be adopted. I have tried to indicate, therefore, the various implications of those policies, the nature of sacrifices involved and generally the pros and cons of the situation. I mention this method of reply at the present time because it affects the treatment of some of the questions to which I shall attempt to reply to-day.