

EMERGENCY BANK CIRCULATION.

Should the Act Be Amended?—Some Observations and Suggestions.

(Specially Contributed to The Monetary Times).

The coming revision of the Bank Act, and, more particularly, that portion referring to circulation, is a subject receiving the earnest attention of Canadian bankers and financiers. The fact that at the highest point in September, (the last month before the Emergency Circulation Act takes effect), the bank notes outstanding came within less than \$2,000,000 of the legal limit, would appear to indicate that unless the present act be amended, the time is not far distant when the circulation supplied by the banks will be inadequate to the growing needs of the country. The end of September showed a margin of \$4,200,000 between paid-up capital and circulation, as against \$9,200,000 on the corresponding date last year. While the total of paid-up capital will be augmented during the next twelve months by the advent of the International Bank, and further issues by banks already in existence, it is hardly likely that such large increases will be effected every year.

It must be borne in mind that large areas of virgin prairie were brought under cultivation during the past summer, and this, with a favorable spring, will result in a largely increased acreage for next season's crop; also, that the general volume of business, as reflected in railroad earnings, bank clearings, building permits, etc., shows no sign of diminution, and, although the crop is disappointing when considered in the light of earlier indications, the result is likely to be sufficiently encouraging to cause further expansion in trade during the coming months.

Requires More Currency.

During the grain moving season, there are several reasons why Western Canada, especially, requires a much larger amount of currency in proportion to its population and wealth than older and more closely settled countries. The principal one is the enormous extent of the crop area, and the fact that at every point where there is an elevator, funds have to be provided to purchase grain. At points where chartered banks are not established private parties have to act as paying agents for the elevators, and the total amount of currency outstanding in their custody often represents a large sum, when the crop is heavy.

In the towns, and districts within a reasonable radius, cheques have largely replaced actual cash as a medium of settlement between debtor and creditor, although there are still a number, among the older settlers and foreigners especially, who persist in carrying the more bulky article (sometimes in large quantities) notwithstanding that banking facilities are at their disposal. On the other hand, farmers living long distances from towns and banks have practically no alternative but to make their settlements in currency, and the process frequently results in large amounts being outstanding for a considerable length of time.

How the Farmer Works.

As an example;—A farmer ships and sells a car of wheat, receiving in return a parcel of currency. Owing to the average crop acreage being so large, the Western farmer is obliged to exert every effort to prepare as much soil as possible before the ground freezes, and when the remittance arrives from the grain company, he may be busy ploughing or engaged in some other urgent pursuit, and is almost compelled to delay the disposal of his money. It is, therefore, either secreted on his person or in the house, and may remain there for several weeks. Whenever he has a respite, he usually takes advantage of the opportunity to pay, or endeavor to pay, his debts. Although the greater portion of these may consist of payments due on land, interest on mortgages, accounts due machine companies and merchants, the settlement of which, almost invariably sends the currency back to clearing centres, he has other debts of a more local character, often involving considerable sums, and the adjustment of which results in no speedy return of the medium to the banks. He may owe a neighbor for money borrowed, for stock, feed, or seed purchased; and frequently, there is the regular hired help to pay. These creditors in turn will often retain the cash in their possession indefinitely.

The extraordinary amount of railroad construction and development work taking place in the Dominion at present, is also an important factor in creating a heavy demand for currency.

The banks are making reasonable efforts to cope with the situation by increasing their paid-up capital as frequent-

ly as the procedure seems warranted. It appears, however, as if they will hardly be able to keep pace with requirements, unless aided by legislation. As far as actual funds are concerned, the manner in which legitimate business has been taken care of during the past year would indicate that the banks are not seriously handicapped in this regard; it is the extraordinary demand for circulating medium, occasioned to a large extent by features peculiar to the country at its present stage of development, that is creating attention.

No Radical Changes.

As intimated in The Monetary Times, it is unlikely that any radical change will be permitted in the laws governing bank issues, and the majority of men, well informed in financial affairs, will probably approve the wisdom of this course. Nevertheless, it would appear that the emergency circulation, might, with advantage, be amended along lines suggestive of an evolution of the principles on which the ordinary circulation is based. The act at present permits the banks, from October 1st till January 31st, in addition to issuing notes to the amount of their unimpaired paid-up capital, (the ordinary circulation privilege), to issue notes to the extent of 15 per cent. of their combined paid-up capital and reserve fund. While the ordinary circulation is free of interest, the excess is subject to a tax, not to exceed 5 per cent. per annum (4 per cent. is the rate exacted) to be paid into the Finance Department.

By way of amendment to the above, the writer submits the following suggestions:—

(1) That the excess issues be based on reserve funds only, and be permitted to the extent of 50 per cent. thereof;

(2) That the tax be either withdrawn or reduced to a rate which will admit a profit to institutions availing themselves of the act, and rendering a public service thereby;

(3) That the time be extended at least two months, making the period from August 31st till the end of February, and be subject to further extension, if, in the opinion of the Minister of Finance and his advisors, circumstances warranted the action, and the best interests of the country would be served in so doing; and,

(4) In the event of the adoption of the first suggestion, that a clause be inserted in the Bank Act prohibiting the reduction of reserve funds without permission of the Government.

Basing excess issues on 50 per cent. of reserve funds would provide about \$16,000,000 additional circulation as compared with the present system, taking paid-up capital and reserve fund figures as at 30th September.

Banks' Reserve Funds.

The reserve fund of a bank, in addition to engendering a sense of security in the minds of depositors, and its consequent value as an advertisement, is virtually so much additional paid-up capital. It represents shareholders' profits reinvested, as it were, in the business. Although dividends are disbursed on the actual paid-up capital only, the earning power of a bank is increased by each addition to the fund.

The reserve, it is true, is not subject to a double liability call, and may be reduced without permission from the Government, hence the suggestion that excess circulation be permitted to the extent of 50 per cent. only, and that reserve funds, once created, be not subject to unauthorized reduction. No reputable institution is likely to resort to the expedient of reducing its reserve fund unless heavy losses have been sustained which it cannot recoup out of the bad debt reservations or surplus earnings.

The present Emergency Act empowers a bank to issue notes in excess of its paid-up capital, whether it possesses a reserve fund or not, while the plan suggested would prevent this, and therefore, in the writer's opinion, be more in keeping with the principles on which the ordinary circulation is based. As a bank, when first established, is allowed to circulate notes to the full extent of its paid-up capital, it seems reasonable, when prudent management has accumulated a reserve fund which is practically equivalent to additional capital, that in the event of commercial conditions requiring the circulation, additional powers of issue should be conferred, based on this fund and its relation to paid-up capital.

To Receive Full Benefit.

In order that the country receive full benefit from the operation of the Emergency Act, it is almost necessary that all the banks take advantage of its provisions, in accord-

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