The Problem of the Fourth War Loan

By H. M. P. ECKARDT.

The recent rise of the interest yields on high class Canadian municipal and provincial bonds has created some perplexing problems for the Finance Minister. This circumstance, along with the stiff prices exacted by the New York bankers in connection with new flotations made in that market, apparently make it necessary to raise the interest yield on the next domestic loan. No doubt it would be advantageous for Canada in some respects to place the next war loan in the United States; but the indications are that the issue will be made in the home market. The Government will need fresh credits before the end of the calendar year, and the New York market would probably prefer that Canada should refrain from fresh financing there until six months or so after the August flotation of $100,000,000. Then the cost of a loan negotiated in the American market would probably be greater than the cost of a domestic loan. It is understood that the two year loan of last month cost the Dominion Treasury 7 per cent. After the flotation these bonds went to a slight discount. In case of the Canadian Northern issue of $10,000,000 in one-year notes taken by New York bankers in the latter part of August, the net interest was approximately 8 per cent, nothwithstanding that the loan was secured by Dominion-guaranteed debentures. Of course, it is to be remembered that both of these were short date issues; and that long term credits, assuming that such could be negotiated under present conditions, would probably bear lower interest rates.

With reference to conditions at home, one point to be noted is that the yield to subscribers in case of the three preceding domestic war loans was slightly above the yield obtainable at the same time on the best municipal and provincial issues. The fact that the bonds of the cities, such as Montreal, Toronto, and Ottawa, as well as those of some lesser cities and of the eastern provinces, were selling in the market at from 5 to 5⅛ per cent while the Dominion war issues gave from 5.30 to above 5.40, occasioned considerable comment. It was pointed out that as the supreme taxing power rested in the Dominion Government, the war loans should rank superior to the issues of the provinces and the municipalities. The explanation, as accepted by the markets, was that inasmuch as the Dominion Government demanded credit in huge amounts—its loans being in amounts of $100,000,000 or $150,000,000 with prospects an indefinite succession of the same—the tendency would be for its interest rate to rise above the rates applying to the provinces and large cities which would require to borrow in amounts ranging from $500,000 up to $5,000,000.

If that line of reasoning still holds good, the obvious conclusion would be that our fourth war loan must yield something like 6 per cent—for the new issues of high class provincial and municipal bonds are practically at that level. The August offerings of the bond dealers have included such yields as the following: Montreal, 5¾ per cent; Hamilton, 5⅞ per cent; Quebec, 6 per cent; London, 6 per cent; Winnipeg Water District, 6¼ per cent; Province of Alberta, 6¼ per cent; City of Edmonton, 6¼, 6⅜, and 6½ per cent (respectively, on 1, 2, and 3-year bonds). According to this list 5¾ per cent represents practically the lowest rate at which any of our important cities can issue new loans of any consequence with the situation as at present; and if the much more formidable amounts required by the Dominion are to yield slightly more than the city bonds, as in the case of the previous war loans, the Dominion rate cannot be much less than 6 per cent. The situation has, however, changed in one respect since the third domestic war loan was launched. On that occasion, and on the launching of the first and second loans, there was no Dominion income tax definitely in prospect. A considerable number of far-seeing investors realized that an income tax would be forthcoming sooner or later as a result of the huge expenditures on war; but the Government had given no intimation that such a tax was to be imposed in the immediate future. Recent utterances of the Finance Minister had created the impression that he was not in favor of taxing incomes; and it appeared that he did not intend to impose the tax at that time. However, the strong demands for conscription of wealth, which arose when the military service bill was introduced, forced the government's hands and investors with incomes over the prescribed amounts, now have before them the practical certainty that they will be taxed upon them in 1918.

Thus, it is clear that the tax exemption feature of the war loan issues will be a more potent factor in aiding the flotation of the fourth loan than the same feature proved to be in facilitating the placing of the previous issues. In other words the exemption feature must now be taken as something that will begin next year to count actively in favor of investments in the war bonds. In case of investors whose incomes are not subject to the new tax the exemption feature of course has no value. In case of investors subject to the normal tax of 4 per cent, it saves one twenty-fifth part of the yield, which with a yield of 6 per cent would mean about ¼ per cent —so that a Dominion bond yielding 5¾ per cent exempt from income tax would be practically equivalent to a non-exempt bond yielding 6 per cent in the matter of net revenue. And in case of rich people subject to the super-tax the exemption is worth more than ¼ per cent on a bond yielding 6 per cent. Thus, the income tax having arrived, so to speak, this point will tell more strongly when the fourth war loan makes its appearance.

It is apparently considered advisable to widen the circle of subscribers to our domestic war loans. Compared with the United States Liberty Loan, our national flotations have been supported by a very small proportion of the population. Less than 50,000 people sent in subscriptions to the $150,000,000 loan floated last March. That means only one person in 160; or one person out of 32 families. There is much room for improvement here, and it is hoped that the next loan will attract 150,000 to 200,000 supporters. It is generally expected that bonds of $50 denomination will be offered next time, and that the small savers will thus have a better opportunity to participate. Latterly the bond market has experienced a strong demand for the $100 denominations of the existing war loans; and these $100 bonds are said to have been selling at slightly better prices than the large denominations of the same issues. This circumstance points to the desirability of issuing $50 bonds in future. Then there is no doubt that an interest yield of a full or round per cent appeals more strongly to the masses than a rate expressed in some odd fraction. So if the Minister were to offer his next loan at the round 6 per cent and advertise it well we may be sure that many thousands of Canadians who have not yet interested themselves in Dominion bonds would be attracted. It might be advisable to follow the plan adopted by the United Kingdom in connection with the last British war loan and divide the issue into two parts—one being subject to income tax and the other being exempt. If the 6 per cent bonds were subject to income tax and the other part of the issue, at a lower rate, were exempt, the small savers would get their full 6 per cent, while the large subscribers would get 5¾ per cent or less, and the terms of the loan would conform nicely to current conditions.

Another perplexing problem is seen in the conversion privilege attaching to the existing bonds. Should a new issue be made on a basis of 5¾ or 6 per cent ,there would be a decided advantage gained through converting the old bonds. If the term of the new loan is fixed at 20 years or more, the whole $350,000,000 of existing war loans would be eligible for conversion, and if so converted the animal interest charge on $350,000,000 would be increased by say $2,000,000. In view of the high rates now ruling, it might be deemed inadvisable to make a long term loan; and on the other hand if the term of the fourth loan is fixed at five or ten years, then the recent action of the Government in making the bonds of the second and third loans convertible into future war loans of 20 years or more, would take on something of the appearance of an empty performance. Finally, there is the consideration that six or eight months hence the current market rate of interest might conceivably be higher than at present.

The C. P. R. and the Canadian Northern Bill

Statement by Lord Shaughnessy

On being asked to make a statement in connection with the proposed acquisition of the Canadian Northern Railway by the Canadian Government, Lord Shaughnessy, president of the Canadian Pacific Railway, on Monday, made the following reply:

"I wish to deny most emphatically the statement published in a number of newspapers, and evidently inspired, that the Canadian Pacific Company is offering organized opposition to the Government proposals about the Canadian Northern. Up to the present time no effort of any kind has been made by the company to influence the vote of a single member of the House of Commons or the Senate upon the measure now before Parliament.

"This reference to the Canadian Pacific is the same old threadbare ruse to which resort has been had on more than one occasion, during the past thirty years, when railway schemes of one character or another were being considered by Parliament.

"It is true that the acquisition of the Canadian Northern by the Canadian Pacific was discussed by representatives of the parties concerned, but the discussion was at the suggestion of members of the Dominion Cabinet.

"After a time it was evident that no transaction was possible, and negotiations were dropped.

"The fate, or destiny, of the Canadian Northern is not a matter of special moment to our company as a common carrier, but the company, having enormous interests in Canada, naturally views with apprehension the possibility of the payment of an excessive price for the alleged equity of the holders of the majority stock, and feels that some less speculative and more direct means should have been used to fix the amount than the very uncertain process of arbitration.

"It is to be hoped that if the transaction is carried out the country will not, in consequence, be saddled with heavy liabilities heretofore undisclosed, and that in fixing the amount to be paid under the arbitration proceedings, no consideration whatever shall be given to personal investments in unfortunate ventures such as coal mines, lumber mills, blast furnaces and other works alleged to have been undertaken for the advantage of the Canadian Northern enterprises, but being in fact private speculations of the promoters of the railway company.

"The references to my own attitude on conscription are offensive and unwarranted. On this subject and on every other question or work connected with the prosecution of the war, I require no advice or inspiration from that little coterie of men who are engaged in fixing standards of patriotism, and whose catechism fails to distinguish between loyalty to the King and loyalty to their particular projects or interests."

AID FOR G. T. P.

The Government's resolution to assist the Grand Trunk Pacific Railway Company with a loan of $7,500,000 passed without opposition, in the House of Commons, on Monday, September 3.

BANK OF ENGLAND'S WEEKLY STATEMENT.

The weekly statement of the Bank of England shows the following changes:

Total reserve, decreased, £322,000.
Circulation, increased, £473,000.
Bullion, increased, £150,851.
Other securities, increased, £4,169,000.
Public deposits, increased, £1,825,000.
Other deposits, increased, £3,849,000.
Notes in circulation, decreased, £282,000.
Government securities, increased, £1,416,000.

The proportion of the bank's reserve to liability last week was 18.21 per cent; the previous week it was 10.00 per cent.