

# Re-Discounting the British Treasury Bills

*How the Dominion Government May Purchase the Bills Taken by the Banks in Connection with the Imperial Munitions Board's Operations.*

By H. M. P. ECKARDT.

Several of the daily papers stated recently that arrangements had been made whereunder the Dominion Government would stand ready to re-discount the British Treasury bills which the Canadian banks are now taking in connection with the loans to the Imperial Munitions Board. The term "re-discount" implies that the Government would buy the bills from the banks and hold them till maturity. When commercial and other bills are rediscounted in the London market the party disposing of the paper endorses it, and thus remains liable until payment is finally made. In the case of these bills, however, as they are the obligations of the British Government, probably no endorsement would be required. So, if the "re-discounting" process is as above outlined, it would practically amount to outright purchase by the Dominion Government of the bills turned over by the banks.

## Bonds May be Taken as Collateral on Loans.

It may be that the suggestion of rediscounting was made in another sense. Perhaps the intention is that if any Canadian bank desires to raise money on all or a part of its holding of British bonds, the Dominion Treasury will accept them as collateral and make loans there-against. In some respects the latter method would be more advantageous for the Treasury, while the banks might conceivably prefer the former plan as it would leave their resources freer. If a bank borrows in this way, it is under obligation to repay the loan or loans at maturity, and there is a certain amount of risk that the collateral may depreciate in value during the currency of the loan; whereas if the bonds are sold the transaction is definitely closed out and risks in connection with fluctuations of value are avoided. Presumably if the arrangement is for loans on collateral, it would be desired to have the terms and rates so fixed as not to cause or induce the banks to take advantage too extensively of the facilities provided. For example, if the banks in the first place took the treasury bills on a basis yielding them 5½ per cent, and the Dominion Government agreed to lend on the collateral at 5 per cent, there would be strong inducements for the bankers to turn over to the Treasury a large part, if not all, of their holdings, as, by so doing they could make a profit or brokerage of ½ per cent without having any capital of consequence employed. In other words the Government might be required to provide practically all of the funds and it might not be convenient for it to do so.

## The Rate of Interest.

Were the rate of interest charged by the Treasury exactly the same as that received by the banks, borrowing against the Imperial treasury bills would only be resorted to as a means of taking up necessary or desirable credit transactions connected with Canadian industry and trade. The treasury bills in themselves would constitute an eminently satisfactory investment from the banking point of view, and while the banker had plenty of funds for looking after the needs of his customers his inclination would be to keep them unpledged or free. (The general understanding is that the banks get 5 per cent or possibly more on the British bonds). When, however, funds began to run somewhat low and demands from the mercantile community were growing decidedly keen, as for instance in the crop moving season, he could take the British bills to the Finance Department and by means of the loans there procured continue to lend freely to the merchants, manufacturers, etc., who looked to his bank for support.

## Influence on the Banks.

Sometimes in schemes of this nature it is arranged that the rate of interest payable by the banks on loans against the pledged collateral shall be fractionally higher than the rate they receive from the collateral. Thus the government might charge 5½ per cent for loans on collateral which yielded the banks 5 per cent; or 6 per cent on col-

lateral yielding 5½. Then the banks as a rule do not borrow excepting in case of a considerable emergency or in case of a very extraordinary demand from their customers. Of course, if the emergency is heavy withdrawal of deposits, the bank might be forced to realize or raise money where it could — the matters of cost or profit and loss being secondary considerations. Notwithstanding the higher rate charged by Government, the operation of rediscounting might yield the bank a satisfactory profit, particularly during a period of exceptional demand for bank credits. In such periods the interest rate has a tendency to rise, and if by borrowing from the Government at 5½ per cent, on collateral yielding 5 per cent the banker is enabled to make good new loans to his customers at 6 or 6½, the transaction is profitable. On the whole, however, the Government might assume that demands on it by the banks by way of re-discounting British treasury bills would not perhaps be great while conditions remained normal, unless the aggregate of the banks' holdings of such bills reached very large dimensions.

## Retiring the Notes After the War.

The total amount taken by the banks in connection with the first loan to the Munitions' Board was \$76,000,000. They are said to have provided this amount in April, May and June, and to have made an additional loan of \$25,000,000 in July; and the supposition is that by the end of July their holdings of British bonds would amount to roundly \$100,000,000. The newspapers state that a fresh credit is in the way of being arranged, and under its working we may see these bonds rise to \$150,000,000 or more in the course of two or three months. The figures indicate clearly why it was necessary to arrange a plan by which the banks would be enabled to liquidate this portion of their assets in case of necessity. Probably on conclusion of the war or very shortly afterwards, London will arrange to retire or take over the outstanding short date obligations of the British Government; or the financial settlement may provide for the offsetting of the Dominion Government's temporary loans at the Bank of England against the Canadian holdings of British treasury bills. As at May 31st, 1916, the temporary loans of our government appear in the Finance Department's monthly statement as \$187,207,017. This includes the \$45,000,000 loan negotiated a year ago in New York; so the Bank of England's loan could not then have exceeded \$145,000,000.

For such bonds or bills of the British Government as our government owned in its own right, it would be a simple matter to get credit on the books of the Bank of England. Before, however, the Ottawa Government could utilize the Canadian banks' holdings of British paper as a means of satisfying its debt to London, it would have to pay the banks for the paper. This might be done through giving them in exchange Dominion bonds, or through issuing Dominion bonds in New York or London, according as circumstances warranted, and buying the bank holdings for cash. With respect to the loans or advances which the Finance Department is to make to the banks on pledge of the British treasury bills, it is not exactly clear what monies or funds the Department could use for the purpose. The Government's holdings of gold amounting on May 31st to \$114,172,696 are not legally available, as these funds represent reserves against the Dominion note issues and the Government and Post-Office savings banks balances. As a matter of fact there has been a deficiency of \$24,000,000 or more in these reserves since the outbreak of war.

One way of providing the funds would be to issue domestic loans and apply the proceeds to this purpose, just as the extra \$50,000,000 subscribed to the war loan of last year was applied to a similar purpose. It would be better still if when next the Dominion Government borrows in New York, the amount be made large enough to cover a substantial sum which might be used in the manner described. Perhaps it will be deemed advisable to make the loans to the banks in the form of new issues of

Dominion notes — this being one of the easiest forms in which such loans can be made. There would be then in evidence an expansion of the Dominion's inconvertible paper currency, the expansion being based not on gold but on British government bonds. In certain respects issues of paper so secured would be less objectionable than issues based on the bonds of the issuing government. It would be virtually a British Government guarantee on a Dominion Government obligation; but on the other hand, further expansion of the Dominion note issues under present conditions is something that should only be undertaken within very moderate limits and with the greatest carefulness. One important objection thereto is that it might make a detrimental effect on the United States market for Dominion bonds; and another is that it would perhaps have a tendency to make the bank holdings of Dominion notes somewhat redundant.

## WHY THE GERMANS WANT VERDUN.

The reason why the Germans want Verdun will be understood after reading the following extract of a speech made in the French Senate:

"From the beginning of the war Germany has sought to maintain possession of the basin of Briey, which represents ninety per cent of our iron production, and the attack on Verdun has been for the purpose of confirming and perpetuating his possession. The basin of Briey lies between Verdun and Metz, like a gigantic key of the war thrown at equal distance from these two fortresses of the Lorraine frontier. From this fact may not one perceive the interest which the Germans have in taking Verdun?"

"Before the war Germany produced annually 23,000,000 tons of iron, of which 21,000,000 came from the part of the basin of Briey, which had been annexed to Germany since 1870. France produced annually 22,000,000 tons of iron, of which 15,000,000 tons came from that part of the basin of Briey which had remained French. Since the war began France, having lost the basin through invasion, has been almost exclusively furnished with iron from England and the United States. Germany, on the contrary, having occupied the basin of Briey in France and in Luxemburg, has added 21,000,000 tons to her production, a total of 49,000,000 tons, which means 45,000,000 of steel.

"These facts suffice to explain the prolonged fierceness of the attacks on Verdun. Once masters of Verdun, the Germans will be able to believe themselves masters of the indefinite continuation of the war, because the basin of Briey incloses in the totality of its subsoil more than 3,000,000,000 tons of iron.

"This slight enlargement of German territory would be enough to turn upside down from top to bottom the whole balance of the old world. It would reduce all continental Europe to vassalage under a protectorate of Germany, and would put England and her Empire in the greatest danger that she has run in all her history.

"Now, if we understand that the territory of Briey in French Lorraine contains perhaps the most colossal and the richest layers of iron in all Europe; that Luxemburg also is very rich in iron; that in the French territory now occupied by the Germans near Belgium there are the richest mines of coal in France, some of them being among the richest in the world, the conclusion is clear.

"If Germany could succeed in getting possession of Belgium and Luxemburg and in swelling her boundary to the disadvantage of France, she would be gaining possession of almost all the mines of coal and iron in Europe. Exception being made of Russia, she would have almost a monopoly on the continent of metallurgical industries.

"The permanent annexation of the Briey Basin would almost ruin France for all future time."

## CORPORATION TAXATION.

Ontario's taxation of corporations is not likely to come under the attack which the Alberta Corporation Tax Act has been subjected to, by the Canadian Manufacturers' Association. The Ontario Act is not as wide as the Alberta Act. Manufacturing and other commercial companies are not taxed as in Alberta, and no company is taxed on any business except that done within the Province. The Ontario Act confines the taxation to banks, insurance companies, loan companies, trust companies, telegraph and telephone companies, steam and electric railways, power companies, express companies, sleeping and parlor car companies, gas and electric companies.