STERLING AND GOLD

WE have had experience now of sterling divorced from gold for over sixteen months, and nothing catastrophic has happened. A number of other countries are using sterling as their standard, and it is still the medium of a large amount of trade throughout the world. How have the groups of countries using gold or sterling respectively fared during this period? The clear evidence of improvement in a number of countries off the gold standard has no counterpart in those still on gold, whose position, generally speaking, has become worse.

This fact demonstrates afresh the ravaging effects of falling prices and the benefits to be obtained by relief from the downward movement. A rise in commodity prices has indeed become much more essential for the gold standard countries, whose plight is growing worse, than for other countries, whose position is improving. Yet we cannot rely upon the so-called "natural" action of gold for such a movement. The pre-war gold standard, so far as its control over the level of prices is concerned, is no longer operative, the misnamed "immutable law" of supply and demand, which was thought to apply to gold as to any other commodity, is of no effect. The enlarged output of the mines and the unloading of hoarded gold from India and Great Britain on the one hand, and on the other the reduced demand for gold involved in widespread departure from its use, have in no way checked its unceasing appreciation.

It is sometimes alleged that our departure from gold was itself responsible for the continued downward movement of gold prices, and that a fall in the gold exchange value of sterling provokes a further decline in gold prices. The price level in each country, however, is governed by the quantity of money available for immediate spending, and the goods and services available to be bought. It follows that the exchange rate between any two of the dominant currencies tends to move in accord with the fluctuations in their respective purchasing powers, though the movement may be temporarily deflected from its course by disturbing transfers of capital and short-term funds. Price levels affect exchange rates, but exchange rates have little effect on price levels as distinguished from the prices of individual commodities.

The price level in Great Britain is of the first importance to the world at large, not because of its effect upon exchange rates, but because of our predominance as a consumer of primary commodities produced abroad. If sterling prices move upward, the ultimate result is to stimulate demand throughout the wide area on a sterling basis for the products of countries not within the group. The increased demand for such commodities as cotton, wheat, copper, and coffee tends to harden their quotations in the countries producing them, whether these countries are on a gold basis or not. Thus a rise in the sterling price level to a strengthening of prices even in the gold standard area.

But is it possible for us to raise our internal price level, in particular can we do so by monetary management; and if we can and do, will it not be evidence of that abhorrent thing inflation? In the actual circumstances we have so much ground to recover that I confess the thought of inflation, so long as it is controlled, does not alarm me. In these days the word is no longer a term of reproach, though some tender consciences find ease in using the innocent substitute "reflation." Almost everyone now recognizes that a rise in primary commodity prices is essential to world recovery, and most would agree with Mr. Hawtrey when he argues, in his recent book, that the evil consequences even of uncontrolled inflation "are definitely surpassed by the evils of deflation." Controlled inflation, from being the remedy of fools or knaves, has become widely regarded as the best available solution of our troubles, particularly since it has become realized that a substantial rise in wholesale prices need have no more than slight effect upon the cost of living.