As a nation we cannot choose between price stability and growth, we must aim at both. Inflation, and the attempt to expand at an excessive rate which produces inflation, are not an effective means of overcoming unemployment, because inflation in the end will create more unemployment than it cures.

Sound Financial Policy

There are not one but several major requirements for the prevention of inflation, the maintenance of sound and steady growth and the prevention or mitigation of fluctuations in the level of unemployment. One requirement, certainly, is the maintenance of a sound monetary policy, which means restraint in the process of expanding the stock of money. Another is moderation in spending and borrowing by governments and public bodies. A third is the development and maintenance of appropriate fiscal policies and public policies of various other kinds designed to promote sound expansion in private business but to discourage excessive spending throughout the economy.

In any country the central bank has the power to encourage an increase in the money supply. By buying government securities in the market it places additional cash in the hands of the sellers, and their deposits increase the cash reserves and therefore the lending capacity of the chartered banks.

Clearly the central bank must see to it that there is enough money in circulation to facilitate the daily exchange of goods and services, the daily volume of payments that must be made, whether by notes or by cheques transferring claims to bank deposits. In the process, the central bank must also see to it that the commercial banks have sufficient lending power to be able to facilitate the essential short-term credit needs of businesses and individuals in order to enable economic activity to continue on the highest level that can be consistently maintained without promoting inflation. But beyond this necessary creation and expansion of money and credit, it must be the duty of the central bank to exercise restraint in its own activities, restraint on its own expansionary potential.

The greater the amount of direct monetary expansion by the central bank, the greater will be the capacity of the commercial banks to increase their loans and investments and thereby put additional spending power into the hands of would-be spenders. But increasing the quantity of money and credit does not of itself increase the supply of goods and services. There is no monetary manipulation or magic trick that can achieve this. Beyond some point, further increases in the total supply of money and credit simply provide fuel for inflation and actually retard and hamper the growth of efficient production.