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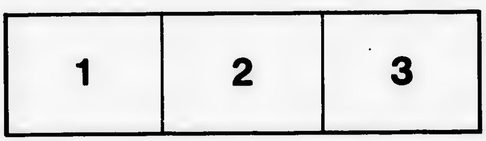

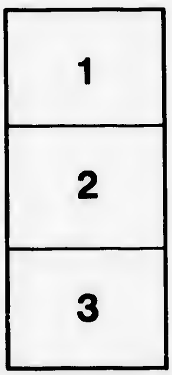

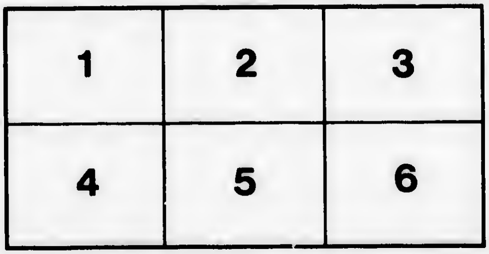

LETTERS

ON

BANKING AND CURRENCY

BY

PETER JACK,

CASHIER PEOPLE'S BANK OF HALIFAX.

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LETTERS

ON

BANKING AND CURRENCY.

LETTER I.

THE Banking system of the several Provinces forming the Dominion is likely to come up for review during the ensuing session of Parliament. As a preparatory measure, the Dominion Government, through a Committee of the House of Commons, issued during last session a series of questions on the subject, having reference principally to the note circulation, to be answered by the cashiers of the several banks and other persons conversant with the subject. The peculiar character of these questions shows a very decided leaning on the part of the Government in favor of the adoption of a note circulation based on Government securities, or one issued altogether by the Government, involving, of course, the withdrawal of the notes at present issued by the banks in all the Provinces.

The Government of the late Province of Canada, sorely pressed for want of money, and as an easy means of borrowing, commenced the issue of its own notes through the medium of the Bank of Montreal. The Dominion Government adopted the same system, and extended it to the Lower Provinces. The charters of the Canadian Banks expire soon, and it is supposed that the policy of the Government is to withdraw the privilege of issuing notes when they are renewed. Considerable alarm has in consequence been felt in Ontario and Quebec, and the attention of the public and members of the Legislature has been drawn to the subject by discussions in the newspapers. Although the effect of such a policy, if carried out, will be quite as disastrous in Nova Scotia as in the Upper Provinces, the subject has not received the attention its importance demands.

Some time since Senator Wilmot, moved by the financial difficulties lately experienced in New Brunswick, published his answers to the questions referred to, in advance of their submission to the Committee of the House of Commons. Although there is not the remotest probability of his main views being adopted, there is a possibility of the end which he desires being arrived at in an indirect manner by the success of the policy of the Government. Mr. Wilmot advocates a radical change in the currency of the Dominion, by substituting for the bank note circulation a Government irredeemable paper currency. Every sane and thoughtful man in the United States admits and deplores the evils connected with such a currency there, and one of the greatest problems they are trying to solve is how to return to specie payments,—yet Mr. Wilmot recommends its adoption in the Dominion. In his opinion the gold sovereign or dollar should not have any fixed relations to its paper representative—the five or one dollar note, but should be an article of merchandize, now at one rate of premium, and now at another, ever varying in relation to the paper currency according to the supply and demand. He attributes all the financial crises under the sun at one time to the fixed price of gold, which, he says, causes "wealth to accumulate in the hands of the few and untold misery to the masses;" and at another to the selling of goods on credit, "creating debt unnecessarily." The foreign trade and exchanges, too, come in for a large share of blame, as proving injurious to the country. Two things Mr. Wilmot appears to dislike—a fixed price of gold and the foreign exchanges; apparently his idea is to raise an impassable barrier between the Dominion and the outer world, to prevent exportation and importation, or all foreign trade, and to issue Government paper money, inconvertible into gold, based on nothing, and of ever-varying nominal value, to stimulate internal trade. He would drive gold with its fixed price, and notes payable in gold on demand, out of circulation, and substitute paper of no value, and then he expects the millenium, when the poor would become rich and the rich somewhat poorer. This seems to be his grand cure for the financial evils under which New Brunswick has been groaning for some time past; and it is a strange remedy, totally inapplicable to the disease. It has not, according to him, been bad banking, but a deficiency of currency that has caused the distress there experienced.

Most persons imagine that the Banks which failed in New Brunswick and Canada did so because they made imprudent advances to parties who declined to repay the amount advanced. But Senator Wilmot takes a different view of the matter. More currency, which would not require to be repaid, would work like magic. But he does not shew how a bank which invests half its capital in a railway, is to be prevented from becoming embarrassed, nor how a bank can remain solvent when two-thirds of its capital is lost. This is the real difficulty It would seem that no amount of currency could prevent disaster in these cases, and had Mr. Wilmot shewn how it could, then would he be a benefactor to his country. Failing in this, it is difficult to discover the value of his publication in relation to the peculiar state of affairs in New Brunswick. Still it may be of service by provoking discussion, and awakening the public mind of the Lower Provinces to the consideration of a question of the utmost importance to the future welfare of the Dominion. Preoccupied as the people of this Province are at present with exciting questions, the time is not propitious for calm thought about it. But as the Dominion Parliament will meet in April, and the future of our Banking system will then be decided, and believing that the foreshadowed policy of the Government is one which, if adopted, will be productive of much injury to our mercantile and industrial interests, I take the liberty of calling attention to the subject, and hope that others better qualified will also raise their voices, that a sound public opinion may be formed for the strengthening of the opposition to the proposed changes already in existence in the other Provinces, and which, I trust, may yet lead the Government to reconsider their policy, and induce them to let well alone.

LETTER II.

QUESTION 2.—State your views on the Banking system obtaining in the late Province of Canada, as well as in the Provinces of Nova Scotia and New Brunswick respectively; and whether, in your opinion, it has been conducive to the development of the material interests of the country?

MR. WILMOT'S REPLY.

ANSWER.—The Banking system prevailing in the late Province of Canada and in New Brunswick has been similar. In Nova Scotia, as in England, banks are restricted from issuing notes of a smaller denomination than five pounds ($20). The circulation below that consists of Provincial notes to the extent of about two dollars per head of the population. That this circulation has not been injurious to the banks is proved by the fact that no bank has ever failed, nor any lower dividend been declared than at the rate of six per cent.,—usually much more; while in the other

Provinces disastrous failures have occasionally occurred, causing loss to the stockholders and noteholders, and inconvenience to the public at large. Doubtless the existing Banking system has been conducive to the development of the material resources of the country, but being too much dependent upon credit and the state of the foreign trade, has, when the foreign exchanges have been adverse, intensified the periodical revulsions in business which have been so disastrous to individuals, and of great inconvenience to the trading community.

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As the foreign trade of the Dominion bears but a small proportion to the value of the domestic trade, and as the bank note circulation depends so much upon the state of the foreign trade, (for an importation of a few millions, beyond the value of the exports, causes such a demand upon the banks for bills of exchange, and in their absence for specie, that they must necessarily contract their discounts, restrict their note circulation, and make money scarce, reducing values 10, 20, or 30 per cent.), I am of opinion that the present Banking system does not afford the facilities necessary for the most beneficial development of the industrial resources of the Dominion.

It will be seen from the above extract that Mr. Wilmot, while admitting that the present Banking system has been of some service in advancing the material interests of the Provinces, gives it as his opinion that it does not "afford the facilities necessary for the most beneficial development" of their industrial resources. His reasons are that the system is too much dependent upon credit and the state of the foreign trade; that when the foreign exchanges are adverse, it intensifies the periodical revulsions in business which take place; that the banks foster the foreign trade, while they do not grant the necessary facilities for the domestic, and do not circulate a sufficient amount of notes.

Now, with all due deference to Mr. Wilmot's authority, we think he has here confounded two things which are quite distinct, namely: the mode in which banks conduct their operations, and the Banking system. The system may be perfect, and yet very imperfectly administered. As a matter of fact, it was under the same Banking system that the Commercial Bank failed and the Bank of New Brunswick flourished, and still flourishes, in our sister Province. The banks in Nova Scotia have also prospered under the system, which is the same in all the Provinces. It is similar to that which has been so successful in Scotland, although even there banks have failed. The banks are all banks of deposit, discount, and circulation. But the trade of the several Provinces is somewhat different, and consequently the securities on which banks lend are also different. And it is here that the causes of their failure must be sought for, and not in their note circulation.

Mr. Wilmot would lead the public to believe that, because the banks in Nova Scotia are not allowed to issue notes of a lower denomination than $20, they have been exempt from failure, while some banks in the other Provinces have unfortunately gone to the wall because they were permitted to issue small notes. Now, there is no connection whatever between the failure of banks and the value of the notes they issue. The banks which failed did so partly because they made loans on securities which deteriorated in value, and on which they could not realize, and partly because their debtors could not repay the loans made to them. But this would have happened if these banks had not issued any notes. If Mr. Wilmot would only tell us how banks may sink their funds in advances to railways, and on real estate, and by means of bad debts, until two-thirds or three-fourths of their capital is lost, and yet remain solvent, he would do good service ; but when he tells us that disastrous failures have occurred in the other Provinces, where small notes have been issued, and that none have happened in Nova Scotia, where the banks are not allowed to issue them, and thus insinuates and suggests that these issues have something to do with the failures, he simply writes nonsense. As well might he say that in some occult way the rate of interest has been the cause of failure ; for in Nova Scotia, where no bank has ever failed, the rate of interest was constant, until recently ; whereas, in Canada, where some failures have taken place, it was regulated by the supply of loanable funds and the demand for them.

Mr. Wilmot seems to think that banks can augment their issues and loans to any extent, but in this he is quite mistaken. Banks do not, and cannot, regulate the quantity of notes in circulation. Notes are used mainly to facilitate the exchange of commodities, and it is the number of transactions in which they are required that regulates the quantity in circulation. As these transactions are numerous or few, so is the circulation large or small, and thus it is that in some countries there is a regular ebb and flow in the amount of notes afloat. In Canada, for instance, when the crops have to be moved to market, a much larger quantity of notes is required than at other times ; so also in Scotland during harvest. After the crops have reached a market, and harvest is over, the notes are returned to the banks. It is not the banks, however, which thus regulate the issues, but the parties who purchase the notes to facilitate these operations. Beyond the quantity necessary to effect those exchanges of property in which notes are employed, it is absolutely impossible for banks to increase their issue when redeemable in specie on demand. To this extent banks will issue them, for it is their interest to have as large an amount in circulation as possible. When they have been in existence for some time they can very well estimate this quantity, and will regulate their loans accordingly.

There is a current opinion that banks may lend to an indefinite amount, and that when they refuse to make loans by the issue of their notes it is from caprice, as Mr. Wilmot says, or for some other equally unworthy reason. It might be thought self-evident that banks can only lend what they have, and nothing more. Their resources consist of their capital and what they are enabled to borrow by deposits and their notes in circulation. The first of these—their capital—they can loan altogether; but the latter—what they have borrowed—can only be loaned to that extent which will leave a sufficient reserve to meet probable demands. When this has been done, all that banks can afterwards do in the way of discounts is to make their daily or weekly receipts and loans balance each other. When the notes in circulation are, from any cause, returned for payment, the available resources of the banks are reduced to that extent, and they must curtail their discounts. This, however, is what Mr. Wilmot cannot perceive. He imagines that banks wilfully intensify the evils resulting from a revulsion in trade, or an adverse foreign exchange, by capriciously reducing their discounts; whereas they cannot help themselves if they would remain solvent. They suffer with the trading community, and whatever injuriously affects the latter is felt by the banks in diminished resources. The same results would follow from like causes, although the banks did not issue notes. In this case, when the foreign exchanges are adverse—that is, when the imports exceed the exports of commodities—the balance must be paid for in coin, or in that which is equivalent to coin—bills of exchange. The amounts at credit of the mercantile community in the banks would be withdrawn, either to purchase bills of exchange, or in gold for exportation, whereby the available resources for discount would be diminished. They must then, as their loans mature, decline to make as large advances as before. When the deposits are diminished, the advances to merchants must be curtailed.

Again, if the notes in circulation were issued by the Government, and were payable in gold on demand, they would be brought in for coin to be exported, or to purchase bills of exchange. The amount in circulation would thus be reduced by an adverse foreign exchange, and whatever evils might exist would be intensified by a scarcity of money even under a system of Government note issues. Neither the Government, however, nor the banks are the agents in restricting the circulation; this is done by the holders of notes, who return them for payment. Of course, if the notes were not redeemable in specie on demand, as Mr. Wilmot desires, specie could not be obtained for them; but far worse evils than any he imagines would result. The notes would fall to a discount; gold would be at a premium. Holders would be defrauded to the extent of the discount, and the loss to the community would very soon be considerably more than has ever resulted from the failure of any bank.

It will now be apparent that, whether the note circulation is a Government or bank one, and so long as it is based on specie, it will be, to some extent—though to a far less degree than Mr. Wilmot imagines—dependent on the state of the foreign trade. And so far as any argument in favor of Government depriving the banks of their circulation is sought for in this fact, it falls to the ground.

But the note circulation of any country is even more dependent upon the state of its domestic than upon that of its foreign trade. Whenever there is great activity in the home trade—whenever numerous quantities of goods are changing hands, there will be more purchasers of notes, and the circulation will be increased. On the other hand, when the home trade becomes dull, when purchasers of goods are few, when what is called a revulsion in trade takes place, then it will be found that there are more notes in circulation than are required for the diminished number of transactions in which they are employed, and they will be returned to the banks. This would again diminish their available means for discount, and must reduce their loans. The same result would follow if the notes in circulation were a Government one, redeemable in specie. Not being required, they would be sent in for redemption, and fewer of them would be kept afloat. For this result neither the banks nor the Government would be to blame. It is a natural consequence of the state of the domestic trade. And here again Mr. Wilmot's reason for governmental interference is fallacious. But if the circulation were furnished by the Government, we would be liable to a very serious evil. For if the notes sent in for redemption were of considerable amount, Government might not be able, or might be afraid of their ability, to redeem them, and an Order in Council could be easily issued, and would be, suspending specie payments. Then would revulsions in trade be intensified, and property sacrificed. From these evils hitherto the bank note circulation has kept us, and this is one of the strongest reasons why the Government should not be allowed to tamper with the currency.

LETTER III.

In my last letter I endeavored to show that banks cannot augment or diminish the notes in circulation at will, and that they are not responsible for the expansions and contractions which take place. I will now attempt briefly to exhibit what the present Banking system has done for these Provinces, in assisting their material development, and thus furnish a strong argument against unnecessary Government interference.

In any country where there are no banks, there are many persons who have surplus funds not required in their business, and others who have accumulated savings which they retain in their own possession. At the same time there are many who are without adequate means to carry on their business profitably, and who are unable to obtain them because they are unacquainted with those who might be able or willing to supply them. So long as this continues it is impossible for the country to prosper. But when a bank is organized with sufficient capital to give depositors assurance of its stability, it draws together into one centre the larger part of the surplus funds and savings of the district in which it is situated, and makes them available for loans to industrious persons whose business has been retarded for want of capital. Additional resources are also derived from the notes circulated. Thus banks become the medium by which the funds possessed by persons unable or unwilling to use them are transferred to those who desire to employ them in mercantile, mechanical and agricultural operations, and, in consequence, are very powerful instruments in advancing the national prosperity. Especially is this the case in a new country, where the want of capital is more felt than in older ones, where it has accumulated.

By reference to the Year Book of Canada for the present year, it will be found that on the 31st July last the total capital of the chartered banks in the Dominion was $31,735,095 ; the loans made to them by the public in deposits and circulations, $42,755,-595 ; and the amount loaned by them to the mercantile community in discounts, $52,737,517. As the notes under discount mature at least every three months, and new notes are then discounted, it follows that the accommodation granted by the banks yearly, by means of discounts alone, cannot be less than $210,000,000. Of this large sum, $26,500,000, or rather more than one-eighth, is furnished through the lending power which the banks obtain by means of their note circulation. But this does not exhibit the entire assistance given by the banks. Many of them advance money on cash credits and on bills of lading, while all of them purchase large amounts of exchange. When we consider the impetus thus given to trade and commerce, it will at once be seen that those who purchase stock in banks, and those who deposit money with them, are, as surely as those engaged in industrial pursuits, promoting the material improvement of the Provinces; and some idea may be formed of the importance of the present Banking system, including its note circulation.

The farmer, the miller, the lumberer, the mechanic, the merchant,—all have felt this beneficial influence. The domestic trade, no less than the foreign, has been stimulated into activity. There is a stage in the history of every young country when the foreign trade is of vital importance, its condition guaging and controlling that of the purely domestic. It is the source of most of the wealth which is first accumulated. As it flourishes, it calls into being and activity domestic industries. The great assistants and stimulants of all these are the banks. They may not have given as much assistance as was necessary. There have been occasions undoubtedly when the demand upon them has been greater than they were able to supply. But Mr. Wilmot's plan of increasing their efficiency, by diminishing their resources, is assuredly a very "Irish" one. He proposes to compel them to withdraw their circulation, and imagines that thus their power to give assistance would be increased. The very statement of his plan shews its absurdity, and were it not that it chimes in with the views of the Government, although on very different grounds, it would be unworthy of notice. He and the Government, however, seek the same end—the substitution of a note circulation issued by the Government, or one based on Government securities, for the present one. One-eighth part of the loans made by the banks, as already stated, is derived from their note circulation, and the Dominion Government aims at absorbing this amount in a loan to itself, and thus withdrawing it from the available working capital of the banks.

Now, it behoves those who wish to alter the present condition of things, to give very satisfactory reasons for so doing. A system which produces results such as have been experienced should not be rudely tampered with. It has been the growth of time, and has become interwoven with all the various material interests of the country. Any check, such as the withdrawal of the note circulation, must inevitably have a very injurious effect. Whatever losses may have resulted from the failure of one or two banks has been amply compensated for in the general benefit resulting from their operations. In Canada there has only been one bank failure of importance for many years. There was a stoppage of another last year, but within a very few weeks its notes were at par, and have since been paid in full. The failure of the Commercial Bank in New Brunswick will not cause any loss to the holders of its notes who continue to hold them, as it is estimated that its assets will be sufficient, not only to pay all its debts, but to realize something for the shareholders as well. In Nova Scotia there has never been a bank failure, and consequently note holders have always obtained payment of bank notes on demand. This is more than can be said for the Government notes issued in Nova Scotia. It has often been difficult to obtain specie for them, as they are not all redeemable in specie, and holders have sometimes found trouble in paying their debts with them.

It should also be borne in mind, in discussing this subject, that during the various crises and revulsions in trade which have occurred of late years, and when the banks in the United States suspended specie payments, the banks in the Provinces continued to meet all demands promptly in specie. They have thus proved their stability in the past, and the inference naturally is, that in the future, if Government does not interfere to cripple them, they will continue to maintain the same high position.

LETTER IV.

Question 3.—Do you favor the system of a direct issue of Government notes as a circulating medium for Canada, or that of having circulation based on Government securities, but issued to the public otherwise than directly by the Government?—State what plan or system would in your opinion be best adapted to the wants and interests of the Dominion, and give the outlines of the plan you would recommend. State particularly what percentage of specie, under any system, ought to be retained for purposes of redemption; and, if any, what in proportion to deposits?

It will be observed that in the above question one of two alternatives is proposed for adoption by the Government for the currency of the Dominion, leaving out of view a third which might be continued. The first two are "a direct issue of Government notes," or the "having circulation based on Government securities, but issued to the public otherwise than directly by the Government." The third, which has been overlooked, is that of the present circulation issued by the banks.

In considering the question, By whom should the circulating medium of the country be furnished? it ought not to be treated as a mere abstract one, as if the Government had now to determine for the first time on the circulation of the Dominion. Much injury may result if the present circumstances of the country are not taken into account. There is already a circulating medium provided with which the public are familiar, adapted to the wants of trade, and which has already done good service. It is issued by the banks, and is based on specie, into which it has always been convertible on demand. It has thus maintained the same value, and passed current as freely as gold. There have been panics and runs upon the banks, but specie payments have never been suspended. From the endeavor seemingly about to be made to change the currency, it might be supposed that much loss has been sustained from the one now in use; but I venture to affirm that there have been fewer losses to the holders of bank notes in these Colonies than in any other country which possesses a similar bank note circulation. or one based on Government securities. In this Colony, certainly, there has never been any loss, and there appears therefore to be no necessity for a change. The security for ultimate payment is found in the capital and assets of the banks, together with the double liability of the stockholders, and it must be a very rare case indeed when these are insufficient to prevent loss. Still, to prevent even the possibility of loss to holders of bank notes, and to ensure speedy payment when a bank has failed, there could be no difficulty in making the circulation a first lien on the assets, to be paid whenever sufficient funds are realized. If the Government is honestly desirous of securing note holders from loss by bank failures, and has no ulterior design in depriving the banks of their circulation, this plan would completely serve its purpose. And there is this advantage in it over any other—that it could be accomplished without disturbing existing arrangements or cramping business, as must be the case when the loanable capital of the bank is diminished.

In the development of new countries the want of sufficient capital is severely felt, and any plan which would tend to diminish what there is should be carefully examined before being adopted. The outcry in Nova Scotia, and I presume in the other Colonies as well, whenever trade is active, is that there is a deficiency of capital. The banks are generally accused of unworthy motives when they decline to make advances under these circumstances, although they may be reducing their reserves to the lowest point compatible with prudence, to give all the assistance possible. But if the Government, by its interference, were to diminish their power, the community would very speedily discover the difference in greater stringency and in an increased rate of discount.

Borrowing, says Mr. Gladstone, is the vice of European Governments, and it has extended to the American continent. We see it in its worst features in the United States, where the National Banking system is a gigantic mode of borrowing. The Government of the Dominion is not free from the vice, and seems desirous of indulging in it still more freely. Whatever desire there may be to give security to holders of notes, it is nevertheless the fact that when Governments issue notes, it is not for the encouragement of trade by making loans to those engaged in industrial pursuits, but as a means of borrowing by paying their debts with "promises to pay." And the necessity for this course generally grows, and the issues of notes not being regulated by the requirements of trade, but by the wants of the Government, are increased until the country blessed with the system is landed in all the evils of a suspension of specie payments. This has been the invariable result wherever Governments have assumed the control of the entire circulation.

Now I question the wisdom or the advisability of the Government of a comparatively undeveloped country, where capital is scarce, borrowing from its own people the funds required for public works, or for the payment of salaries and other debts. Prudent Governments can generally obtain loans abroad for all they gradually require, and by this means they introduce more capital instead of absorbing a portion of what is already insufficient. If the Dominion Government were to issue the entire circulating medium, it would borrow from the public, to pay its debts, that which the banks now borrow and circulate through the various channels of trade. Or, if it were to compel the banks to lodge Government bonds as security for their note issues, this would be to make them loan to the Government a large amount now available for mercantile purposes. In other words, by the adoption of either of the proposed alternatives, the loanable capital of the banks—which is confessedly not in excess of the wants of commerce—would be largely diminished. To prevent this, it has been suggested, in another of the questions of the committee, that the present capital stock of tne banks might be increased, but it does not follow that their loanable funds would thereby be augmented. For the money lying idle and available for the purchase of bank stock is, for the most part, if not altogether, deposited with the banks. Any simultaneous addition to the capital stock of all of them would be derived from their deposits, so that they would not be placed in any better position. There can be no doubt, then, that the loanable capital would be permanently diminished by the withdrawal of the bank note circulation.

Let us now consider what would be the effect in Nova Scotia of the adoption of either of the alternatives apparently favored by the Government.

The first one suggested is the issue of notes directly by the Government, instead of by the banks. The total circulation of the chartered banks on the 31st July last, as given in the Year Book, was $822,748, to which has to be added that of the two private banks and the Bank of British North America. This would bring it up to at least $1,000,000. If we assume that the banks hold 20 per cent. of this amount in specie (such being the proportion of specie to deposits and circulation), there remains $800,000 derived from the circulation employed in the encouragement of trade. Were the supposed policy of the Government carried into effect, and the circulation of the banks withdrawn, it would necessitate the curtailment of the discounts to the extent of $800,000, or one-fourth of the entire amount—that is, an amount equal to the united capital of the Union Bank and the People's Bank. In regard to our two country banks—the one in Yarmouth and the other in Windsor—the proportion would be still greater. The circulation of the Bank of Yarmouth on the 31st July was $154,820, and its discounts $289,511. The circulation of the Commercial Bank of Windsor was $63,000, and its discounts $190,613. From these figures it is evident that the former would require to reduce its discounts by more than one-half, and the latter by about one-third. It requires no prophet to fortell the effect likely to be produced on the trade and commerce of Nova Scotia by this arrangement.

The result of the second alternative, if adopted—that of a circulation based on Government securities, according to the National Banking system of the United States, which is referred to in several of the questions of the Committee—would be even more injurious than that of the first.

Under the National Banking system of the United States, the banks are required to lodge with Government, in Government securities, one-third of their paid-up capital; and as security for the ultimate payment of their note issues, they must deposit Government bonds to an amount equal to their circulation, and one-ninth more. Now the paid-up capital of the chartered banks in Nova Scotia on the 31st July last was $1,554,380, and if there is added for the other three banks $400,000 (a low estimate), it gives $1,954,380 as the total paid-up capital. Of this amount one-third, or $651,460, would be deposited with the Government to begin with. Then, as the circulation is $1,000,000, to which, if we add one-ninth, there would be $1,111,111 deposited in addition as security, making in all $1,762,571 to be deposited with the Government, or more than half the entire amount under discount of the chartered banks. To purchase these bonds it would be necessary for the banks to call in their loans to the same extent. Thus the accommodation given to the mercantile community would be reduced one-half. Could anything more disastrous to the interests of Nova Scotia be devised than such a scheme as this? The banks would not suffer, it is true, because they would receive interest on the bonds and also on the circulation, but the business of the Province would be entirely prostrated. If at times it is difficult for the banks with their circulation to supply the wants of trade, it would be utterly impossible for them to do it when deprived of the means derived from their notes in circulation.

The conclusion of the whole matter, so far as I can see it, is that "the plan or system best adapted to the wants and interests of the Dominion" is the one now in existence, which has been of immense service in the development of these Colonies; and that the Government cannot do anything better than to let it alone.

LETTER V.

"I think that the effect of the State having the complete control of the circulating medium in its own hands would be most mischievous."—Sir Robert Peel.

It has been recognized by eminent writers on Economical Science that if a Government takes the note circulation into its own hands, it should conform itself solely to the "iron principle" of an exchange of notes for gold and gold for notes; and that there should always be in its possession an amount of gold equal to the notes in circulation. On this principle, the only sound one for a Government to adopt, there could not be any doubt of the immediate or ultimate redeemability of the notes, and note holders would be perfectly secured from loss. This, however, does not appear to be in accordance with the policy of the Dominion Government. Judging by the tenor of the various questions, the design is to substitute a Government note circulation with only a partial reserve in specie for the present bank note circulation with a like reserve. And the conviction is forced upon us that it is not for the purpose of thoroughly securing the convertibility of the currency, but in order to borrow, that the Government desires to interfere with the present system. This being the case, the policy is a most dangerous one. There would not be the same security for the immediate nor for the ultimate redemption in specie of Government notes as there is for bank notes.

The money borrowed by Government by the issue of its notes would be expended on various Government works, in payment of salaries, and in other ways, and would be gone beyond recovery. In the event of a panic or a large demand for gold for exportation, all that the Government would have to meet its notes would be the specie reserve. There would not be, as with banks, the daily maturing of loans, nor any other reserve, such as money invested at call, or in the hands of agents abroad, by means of which gold comes in, or could be immediately obtained, to meet any extraordinary demand. The only way in which the Government could obtain the gold would be by effecting a loan. But at such a time this would be next to impossible, and Government would be compelled to suspend specie payments. Besides, as Government would thus be relieved from the necessity of paying its debts in anything but "promises to pay," which are not intended to be paid—and this is a much easier process than paying them in coin—there is a constant temptation to bring about this result, diminishing any desire there might be to maintain the convertibility of the note.

Even if there were no distrust or panic, nor any extraordinary demand for gold, there is still danger in another direction. It is not difficult to imagine a time when there are as many notes issued as can be kept in circulation, when the Government is in want of money and there is difficulty in raising a loan by the sale of bonds.

Under these circumstances there would be a strong temptation to supply the deficiency by simply issuing an order in Council suspending specie payments. When it is possible to borrow money at the expense of paper and printing merely, it is too much to expect a necessitous Government, having the control of the currency, not to do so. For a bank to suspend specie payments is ruin, but for a Government to do it is to obtain increased facilities for raising money. There is every inducement for banks to pay their notes in gold on demand, no matter what the cost may be, but with Governments it is just the reverse. The latter gain by that which would be destruction to the banks. Nothing but the fact that its notes were not payable in specie enabled the Government of the United States to borrow so largely by their issue. There thus appears to be a far greater risk run by the holders of Government notes when the reserve is only a partial one, than by those who are in possession of bank notes. For, as was remarked in a previous letter, suspension with all its accompanying evils, such as the depreciation of the value of all kinds of property through the inflation of the currency, has been the invariable result, sooner or later, in every country where the Government has usurped the control of the note circulation.

There are other evils besides that of a suspension of specie payments, although it is the worst; evils of a political nature, which may result from the Government taking the circulation into its own hands, which I shall only glance at. It would then possess a power which might at any moment be exerted for party and other illegitimate purposes. Whether justly or not the Government also would be continually liable to attack for the manner in which it might use its power of issuing notes. And if the power of issue were conferred on any one bank of discount, which would thus become the national bank, the evil would only be intensified. On this point Mr. McCulloch says that "a national bank for transacting ordinary banking business would be neither more nor less than a national nuisance that would very soon have to be abated. And no Government would choose to encounter the obloquy of being connected with such an establishment." Whether correctly or not it has already been asserted that the power conferred on the present Government bank of the Dominion has been used in a manner disadvantageous to the interests of the banks and the community at large, thus corroborating so far Mr. McCulloch's opinion. What may then be expected if the power for evil is increased by the destruction of the bank circulation and the substitution of that of the Government, and the whole confided to a single bank of issue?

The other alternative presented by the Government, that of the issue of notes based on Government bonds as security, does not add anything to the security of the note holders.

The present National Banking system in the United States is one which took its rise under a suspension of specie payments, and it is impossible to argue from what has taken place there as to the adaptability of the system to other countries where the notes are redeemable in coin. This, however, is very clear, that one of its effects in the United States has been to drive out of the country nearly all the coin that was in it. Prior to the passage of the Act which called the National Banking system into existence, the banks in the principal cities held large reserves in gold. The immediate effect of their coming under its provisions was the sale of their gold to purchase Government securities to lodge with the Government for notes. And since the inauguration of the system gold has been exported to even a larger amount than was in the country at the time when the Act was passed; so that if there had not been a constant supply of bullion from California and elsewhere, there would not be at the present time any gold coin in that country. Canadian bankers affirm that the result of the recent issue of legal tender notes in Canada, where they are partially held instead of specie, as a reserve, has been the same; and that there is not now nearly so much gold in the country as there was before the issue of legal tender notes. This also brings us nearer to a suspension of specie payments than before.

Again, by the sale of their specie reserves, the banks in the United States were enabled to adopt the new system without disturbing their general business; but this could not be done where specie must still be held as the reserve for the payment of deposits and circulation.

It will thus be seen that it is impossible to draw any conclusions from the results of the National Banking system of the United States to help us in our consideration of the matter. But a similar system to that which is proposed for our adoption, that of the State Banks, had been in existence in the United States for a considerable time prior to the late war. Under it the attempt was made to secure the note circulation by the deposit of State or United States bonds, with what result may be gathered from the testimony of competent witnesses. The sub-Secretary to the

Treasury of the United States, writing under date 27th of November, 1854, says: "The ultimate security is better than no security at all. The mischief is that it is least available when most wanted. The same causes which prevent the banks from redeeming their notes promptly, cause a fall in the value of stocks on the ultimate security of which these notes have been issued. The ultimate security may avail something to the broker who buys them at a discount, and can hold them for months and years, but the labouring man who has notes of the state security banks in his possession, finds, when they stop payment, that *the ultimate security for their redemption does not prevent his losing 25, 50, or even 75 cents in the dollar.*" The Superintendent of Banking for the State of New York, in his report for 1856, remarks that the securities held in trust for banks which failed in 1855 were disposed of, "but the sums realized from their sale did not, in any case, suffice to pay the notes at par, while a period varying from two to four years would have to elapse before the affairs of the insolvent banks will be finally settled." And Mr. Buchanan, in his Message to Congress, December, 1857, states that "however valuable these securities may be in themselves, they cannot be converted into gold and silver at the moment of pressure, as our experience teaches, in sufficient time to prevent bank suspensions, and the depreciation of bank notes." What was true then is true now. The plan of making Government bonds the security for bank notes, has many advocates, but it fails whenever trouble arises. The tendency of the system, and of that in which legal tender notes are held as a reserve, is to run down the gold reserves to the lowest point, so that when a crisis comes the gold is absent and cannot be procured, nor can the Government securities be sold except at a great sacrifice, if at all. Holders of notes want gold and not Government securities, and the inevitable result is suspension and loss, as has more than once occured in the neighboring republic.

Judging, then, by the past history of Banking in the United States, as compared with that of Banking in the British North American Provinces, it is evident that the risk of a suspension of specie payments, and of loss to holders of notes, is far greater under a system in which "promises to pay" are held to meet other "promises to pay," and one species of indebtedness—Government bonds or debentures, to retire another species of indebtedness—the note circulation, or the credit of the Government is substituted for the solid gold—than under one in which the reserves 'are held in specie.

On the right determination of this important subject the future welfare of these Provinces very much depends. Danger, distress and ruin lurk behind the policy of Government issues in any shape they may assume—immediately, in the disturbance and cramping of trade and commerce, through the withdrawal of discounts, to enable the banks to redeem their notes, and obtain gold to hand over to Government for its notes or bonds; remotely, but no less surely, in the ultimate suspension of specie payments whenever the necessities of Government demand it.

JAMES BARNES, PRINTER, HALIFAX, N. S.

Banking and Currency.

To the Editor of the Morning Chronicle:

SIR,—When I formerly addressed you on the important subject of Banking and Currency, nothing was positively known as to the intentions of the Government. Much was surmised, but it was quite uncertain how far they would attempt to interfere with the existing bank note circulation. This state of uncertainty was removed when the Resolutions of Mr. Rose were submitted to Parliament. Therein the policy of the Government was fully declared, and it was of a character so opposed to the best interests of the country that even staunch supporters of the Government felt compelled to oppose it. After the debate in which this opposition was so thoroughly and ably manifested, the Resolutions were allowed to lie over, and it was only towards the close of the session, and after considerable discussion and difference of opinion in the Cabinet, that they were finally withdrawn. While thus reluctantly withdrawing his Resolutions Mr. Rose gave it to be understood that they were not abandoned, but only postponed, and he expressed the hope that they would yet receive the assent of the country. There can be very little doubt but that they will be brought forward next session, and that every influence will be used to secure their passing into law.

As is well known, the representatives of the banking interests gave to the Resolutions of Mr. Rose their decided opposition. An attempt was made to shake their influence by endeavoring to create the impression that this was the result of entirely selfish motives, and that they were looking after their own interests alone, while quite indifferent to those of the public. On the other hand Mr. Rose repeatedly assured Parliament, in the course of his speech, that the measure of the Government "was framed solely with a regard to the great interests of the country," and that they had no ulterior object in view. Mr. Tilley endeavored to prove that the public, as evidenced by the petitions presented, were, to a considerable extent, indifferent. Another member of the Government told me that whenever he saw so many bankers in opposition to the scheme he was sure it was a good one for the country. Now I have no hesitation in asserting that it was because they thought the policy of the Government would be most injurious to our mercantile and industrial interests that the bankers were so unanimously opposed to it. True, there was a well grounded dislike to being compelled to invest a large portion of their capital in government securities of variable value, and which would not be available when required for the redemption of the notes. They also knew that whatever legislation might injuriously affect the mercantile community must react upon the banks. To this extent the bankers were selfish in their opposition. But it did not arise from any fear as regards their profits, as might be supposed, for these would be nearly, if not quite, as much under the Government scheme as they are at present, while some thought that if they had merely consulted their own interests they would have welcomed the proposed change.

The question in reality is one which mainly affects the merchant, the trader, the mechanic, the manufacturer, the lumberman, and the farmer, as it would be impossible for the banks under the proposed system to grant to them anything like the same accommodation as they at present receive. The object of this letter is to draw attention again to the subject, and to shew what the result would have been in Nova Scotia had the Resolutions of Mr. Rose passed, and what there is in store for us should the Government hereafter succeed in forcing their policy through parliament.

The plan of the Government, as explained by Mr. Rose, and embodied in his Resolutions, was to compel the banks to purchase government bonds to an amount equal to their circulation, and to maintain besides a reserve of gold equal to twenty per cent. of their circulation. The meaning of this is, that for every one hundred dollars of notes afloat the banks must originally possess one hundred and twenty dollars in gold, of which one hundred dollars were to be loaned to the government and twenty dollars held in their safe to meet any demand for specie payment. It will be seen at once that this was in reality, whatever it may have been in intention, a grand scheme for obtaining possession of a large amount of gold by a forced loan from the banks. The latter were also required to hold in gold, or legal tender notes, a further reserve equal to one-seventh of their call deposits. This was the entire reserve which Mr. Rose supposed to be necessary for safe banking; an opinion opposed to the views of most practical bankers. To shew that his scheme would not be very detrimental to the commercial interests of the country, it was necessary for him to put the reserve at the very lowest point; which he accordingly did. And even with this very small reserve, he was obliged to confess that his scheme would withdraw at least $5,700,000 from the available banking funds of the Dominion.

The following calculation will shew the effect on the banking funds of Nova Scotia. I have taken the figures as given in the returns of the chartered Banks on the 31st July last, which is the latest date to which I have access, and have added one-fourth for the two private Banks and the Bank of British North America. At that date the total circulation was $1,028,000, which, according to the Government proposal, was to be withdrawn, and other notes based on Government securities substituted. The Banks were required to hand over to the Government $1,028,000 in gold for their bonds. They were also to keep a reserve of 20 p. c. in gold, and a further reserve of one-seventh of their call deposits. The total amount of specie thus required would have been $1,358,000, to meet which the Banks held $703,000 in gold and Government bonds, the difference amounting to $655,000 they could only obtain by permanently reducing their discounts to this extent. This, be it remembered, is according to Mr. Rose's own method of calculation, and yet is equivalent to wiping out the capital of the Union Bank and half that of the People's Bank. But the calculations of Mr. Rose are defective in two particulars. He has not made provision for any reserve for deposits on interest, nor has he made any for the reserve of notes which Banks must always hold in their tills, or which may be passing between the head offices and branches, and which are not in circulation. He has taken the amount of notes in the hands of the public alone as it stood on a particular day, or on the average, but there may be, and are, many days when it is considerably higher than on the day on which the returns are made up. A much larger amount than is made to appear in his calculations must be invested in Government securities, and thus withdrawn from available banking funds. Adding to the $655,000 required to be withdrawn from discounts, according to Mr. Rose's mode of calculation, one-seventh say of the deposits on interest, or $225,000, and the very moderate allowance of one-seventh of the actual circulation for a reserve in the till or $147,000, and we have at the very lowest estimate consistent with necessity and prudence, $1,022,000, permanently withdrawn from the loanable banking funds in Nova Scotia, or more than the united capital of the Bank of Nova Scotia and the Union Bank. The following recapitulation will probably show the result more clearly :—

Total circulation to be covered by Government bonds		$1,028,000
Reserve of 20 p. c. to be maintained in gold		205,000
Reserve of 1-7th of $877,000 call deposits		125,000
Total amount of gold required for circulation and deposits		$1,358,000
To meet this amount the banks held in specie	$620,000	
in government debentures	83,000	
		703,000
Making a deficiency to be taken out of discounts of		$655,000
To which add—		
Reserve in specie of 1-7th of $1,545,000, deposits on interest		220,000
Reserve of notes in till, viz., 1-7th of $1,028,000 actual circulation		147,000
Showing the total amount to be withdrawn from discounts to be		$1,022,000

No scheme more injurious to the material interests of this Province could well be conceived than this with which we are still threatened. To conciliate the banks, if possible, and to prevent the damaging effects from being immediately felt, it was proposed to spread the operation over a period of five years. Although this would lessen the evil for a time, it would go on growing year by year, until at the end of the five years the full blighting influence would be experienced. And if trade were to revive and increase in the meantime, there would be a contraction of means continually going on side by side with a growing demand, which would necessarily cause embarrassment, tighten the money market, and raise the rate of discount.

The main object professedly of the Resolutions was to ensure the ultimate payment of bank notes after the suspension of a bank, and to make assurance doubly sure, Mr. Rose, in addition to compelling the banks to invest in government bonds, proposed to make the notes a first lien on the assets of the bank, which of itself is a full and sufficient protection to the note holder. But, as if this were not enough, he also proposed to render immediately available the clause in the charters by which the stockholders are liable for double the amount of their stock. For some reason or other, by the way, which might be guessed at, the Bank of British North America was to have been exempted from the double liability. By this means the holders of notes of the Bank of British North America would not have felt so secure as the holders of other notes. Still if it was considered desirable in the public interests to make the shareholders in the local banks liable for double the amount of their stock, there could be no valid reason why those of this foreign institution should not be equally liable. And if it were not considered necessary in the case of the latter, neither should it have been in regard to the local banks. However, these two provisions—the making the notes a first lien on the assets of the bank, and rendering the double liability of shareholders immediately available after suspension—give undoubted and ample security without in any way curtailing the power of the banks to assist trade and commerce. And if Mr. Rose had merely looked at the interest of the public, he would have stopped there. But he went very much further, and, in order to assure a certainty, proposed a plan by which the reserves of the banks would have been reduced far below what the bankers of the Dominion now consider necessary for their own stability and the safety of the noteholder,—a plan which would not only have deranged our present monetary system and largely curtailed banking accommodation, but would have absorbed those resources which, if held by the banks themselves in times of difficulty, would enable them to meet their liabilities, and prevent suspension from taking place.

PETER JACK.