

This PDF is a selection from an out-of-print volume from the National Bureau of Economic Research

Volume Title: Canada's Financial System in War

Volume Author/Editor: Benjamin H. Higgins

Volume Publisher: NBER

Volume ISBN: 0-87014-334-4

Volume URL: <http://www.nber.org/books/higg44-1>

Publication Date: 1944

Chapter Title: General Conclusions

Chapter Author: Benjamin H. Higgins

Chapter URL: <http://www.nber.org/chapters/c0661>

Chapter pages in book: (p. 79 - 87)

GENERAL CONCLUSIONS

At least four general conclusions emerge from the study of Canada's financial system in war. The first is that diverting money income from one channel to another through fiscal and monetary policy is startlingly difficult. Even with such heavy taxation and public borrowing as that in Canada, a more substantial rise in total consumption has developed than was expected or desired by the government. In each year since war began, personal outlays on goods and services have risen by 30 to 55 percent of the increase in personal incomes net of taxes. Effects of disproportionate increases in demand for particular commodities and particular kinds of labor have been only partly suppressed by direct controls of wages and prices. Money, it seems, clings persistently to peacetime pursuits long after the armed forces and war industry are in action.

In the immediate postwar period, one objective of financial policy will be to assist the speedy reconversion of plant and equipment, to assist replenishment of inventory, and at the same time to continue control of inflation. Investment may have to be stimulated while consumer spending is kept within the limits imposed by available stocks.⁶⁵ On the other hand, once the war is won, the motive for prompt reconversion and inventory accumulation will be strong, and competition for men and resources may be keen. Some people may then insist that those industries most "essential" to society should reconvert first, even though the criteria of "essentiality" will be still less clear-cut than in wartime. In view of the wartime difficulties of reallocating resources, the possibility of an allocation problem in the transition period suggests a need for careful advance study to determine the proper timing and technique for abandoning wartime controls.

The second conclusion is that money, which has been immobilized or diverted to war uses by loan campaigns and direct controls, will still need checks and guides to assure its orderly return to civilian channels. The stimulation of a large-scale war effort seems to involve an inevitable expansion of liquid assets. Much of these assets is in the hands of individuals and corporations who normally do not hold

⁶⁵ Some of the difficulties inherent in such a fiscal policy are discussed by the author in an article on "Postwar Tax Policy," *Canadian Journal of Economics and Political Science* (August and November 1943).

large liquid balances. Accordingly, the government may continue urging them to hold their war bonds for some time after the war, to dissuade them from spending too much during the transition when supplies of goods and services are inadequate and too little later when these supplies become relatively abundant. Timing the use of these liquid assets will be a matter of concern to government, industry, and individuals alike.

The third conclusion is that the resources of all financial institutions of an economy at war must be mobilized if the objectives of war finance are even to be approximated. In order to attain the relative success of Canada's financial effort in War II, the investment and spending of banks, insurance companies, business concerns, finance companies, provincial and local governments, and individuals have had to be meshed with the fiscal policy of the Federal government.

As we have seen, the banks have necessarily coordinated their activities with the operations of the Bank of Canada and the Ministry of Finance. Except for agricultural loans, which are closely tied up with government buying and price maintenance of wheat, war-time bank expansion has resulted almost entirely from government financing and has been made possible through provision of the necessary reserves by the Bank of Canada. The life insurance companies have bought government bonds to an extent exceeding their net receipts from Canadian business, liquidating other assets to procure them, and have become for the time being intermediaries between individual savers and the Treasury. Provincial and municipal governments have altered their fiscal policies to synchronize more effectively with Federal fiscal policy. Retail finance companies have of necessity turned to the financing of concerns working on government contracts. Individuals and non-financial corporations have made unprecedentedly large investments in government securities.

The outbreak of peace will present problems comparable in magnitude and complexity with problems arising from the outbreak of war. A good deal of labor and capital will have to be shifted, both occupationally and geographically. Until the peace emergency is clearly over, the government will require the assistance of financial institutions in dealing with the financial problems of transition from war to peace. So long as the government finds it advisable to go on mopping up excess purchasing power by taxes, loan campaigns and

direct price controls, the tasks of the private financial system will remain much the same as in wartime. If the government deems it necessary to embark on a program of public work and relief to counteract recession, the private financial system may be relieved of some of its wartime duties; but may still be called upon to buy government bonds in large quantities.

The fourth conclusion is that financial institutions have an increased concern with postwar financial policy because war finance brings about a concentration of their earning assets in government obligations. While most financial firms are in a strong position to ride out mild flurries in the bond market they have an understandable interest in relatively stable values for their assets. Mass liquidation would be highly disturbing for the financial system, whether motivated by a desire to offset falling incomes by dipping into savings, to hedge against inflation, or to finance replacement of durable goods. The best guarantee of a stable bond market would be a high level of economic activity, with enough savings to provide a firm market for securities and to keep demands for goods from outrunning supplies.

The Annual Report of the Bank of Canada for 1943 gave virtual assurance that the banking system would use its resources to maintain a low interest-rate structure after the war. Referring to the reduction in the rediscount rate from $2\frac{1}{2}$ to $1\frac{1}{2}$ percent, effective February 8, 1944, the Governor of the Bank stated:

"It therefore seems appropriate that the bank, by reducing its rate, signify its intention to continue the kind of monetary policy which has brought about the current level of interest rates. A policy aimed at higher interest rates would only become intelligible if, after war shortages are over, consumers' expenditure and capital development were to proceed at a rate which would overstrain our productive capacity. I see no prospect of such a situation arising in a form which would call for a policy of raising interest rates."

However, such complete optimism about the possibility of pursuing an easy money policy without danger of inflation has not been shared in all quarters. The Advisory Committee on Reconstruction, in its report to the Prime Minister, has taken the position that inflation is the gravest of immediate postwar dangers.

In closing, it might be suggested that as long as Canada remains at war and continues to pursue her stated aims of war finance — to

stimulate war production, avoid inflation, and minimize postwar complications — she will undoubtedly find it advisable to maintain her anti-inflationary forces as close to full strength as possible. There are indications that war expenditures have already passed their peak; budget estimates for fiscal 1945 show a slight decline from the previous year. Nevertheless, large loan campaigns, high taxes, extensive rationing, and substantial subsidies will probably still be necessary for the duration of the war emergency. If so, the tendencies in the financial field already noted will continue. Financial institutions will hold still more money and still more bonds, and their stake in postwar financial stability will be greater than ever.

National Bureau of Economic Research

Officers

N. I. STONE, Chairman
SHEPARD MORGAN, President
H. M. GROVES, Vice-President
GEORGE B. ROBERTS, Treasurer
W. J. CARSON, Executive Director
MARTHA ANDERSON, Editor

Directors at Large

CHESTER I. BARNARD, *President, New Jersey Bell Telephone Company*
DAVID FRIDAY, *Consulting Economist*
OSWALD W. KNAUTH, *New York City*
H. W. LAIDLER, *Executive Director, League for Industrial Democracy*
SHEPARD MORGAN, *Vice-President, Chase National Bank*
GEORGE B. ROBERTS, *Vice-President, National City Bank*
BEARDSLEY RUMMLER, *Treasurer, R. H. Macy and Company*
HARRY SCHERMAN, *President, Book-of-the-Month Club*
GEORGE SOULE, *Director, The Labor Bureau, Inc.*
N. I. STONE, *Consulting Economist*
J. RAYMOND WALSH, *Director, Department of Education and Research,
Congress of Industrial Organizations*
LEO WOLMAN, *Columbia University*

Directors by University Appointment

E. W. BAKKE, *Yale*
C. C. BALDERSTON, *Pennsylvania*
W. L. CRUM, *Harvard*
GUY STANTON FORD, *Minnesota*
H. M. GROVES, *Wisconsin*
CLARENCE HEER, *North Carolina*
WESLEY C. MITCHELL, *Columbia*
PAUL M. O'LEARY, *Cornell*
T. O. YNTEMA, *Chicago*

Directors Appointed by Other Organizations

PERCIVAL F. BRUNDAGE, *American Institute of Accountants*
FREDERICK C. MILLS, *American Statistical Association*
C. REINOLD NOYES, *American Economic Association*
BORIS SHISHKIN, *American Federation of Labor*
WARREN C. WAITE, *American Farm Economic Association*

Research Staff

WESLEY C. MITCHELL, *Director*
MOSES ABRAMOVITZ
ARTHUR F. BURNS
SOLOMON FABRICANT
MILTON FRIEDMAN
THOR HULTGREN
SIMON KUZNETS
FREDERICK C. MILLS
GEOFFREY H. MOORE
RAYMOND J. SAULNIER
GEORGE J. STIGLER
LEO WOLMAN
RALPH A. YOUNG

Relation of the Directors to the Work of the National Bureau of Economic Research

1. The object of the National Bureau of Economic Research is to ascertain and to present to the public important economic facts and their interpretation in a scientific and impartial manner. The Board of Directors is charged with the responsibility of ensuring that the work of the Bureau is carried on in strict conformity with this object.

2. To this end the Board of Directors shall appoint one or more Directors of Research.

3. The Director or Directors of Research shall submit to the members of the Board, or to its Executive Committee, for their formal adoption, all specific proposals concerning researches to be instituted.

4. No report shall be published until the Director or Directors of Research shall have submitted to the Board a summary drawing attention to the character of the data and their utilization in the report, the nature and treatment of the problems involved, the main conclusions and such other information as in their opinion would serve to determine the suitability of the report for publication in accordance with the principles of the Bureau.

5. A copy of any manuscript proposed for publication shall also be submitted to each member of the Board. For each manuscript to be so submitted a special committee shall be appointed by the President, or at his designation by the Executive Director, consisting of three Directors selected as nearly as may be one from each general division of the Board. The names of the special manuscript committee shall be stated to each Director when the summary and report described in paragraph (4) are sent him. It shall be the duty of each member of the committee to read the manuscript. If each member of the special committee signifies his approval within thirty days, the manuscript may be published. If each member of the special committee has not signified his approval within thirty days of the transmittal of the report and manuscript, the Director of Research shall then notify each member of the Board, requesting approval or disapproval of publication, and thirty additional days shall be granted for this purpose. The manuscript shall then not be published unless at least a majority of the entire Board and a two-thirds majority of those members of the Board who shall have voted on the proposal within the time fixed for the receipt of votes on the publication proposed shall have approved.

6. No manuscript may be published, though approved by each member of the special committee, until forty-five days have elapsed from the transmittal of the summary and report. The interval is allowed for the receipt of any memorandum of dissent or reservation, together with a brief statement of his reasons, that any member may wish to express; and such memorandum of dissent or reservation shall be published with the manuscript if he so desires. Publication does not, however, imply that each member of the Board has read the manuscript, or that either members of the Board in general, or of the special committee, have passed upon its validity in every detail.

7. A copy of this resolution shall, unless otherwise determined by the Board, be printed in each copy of every National Bureau book.

*(Resolution adopted October 25, 1926,
and revised February 6, 1933 and February 24, 1941)*

Financial Research Program: Committee

In the conduct of this and other studies under its program in finance the National Bureau has benefited from the advice and guidance of its Committee on Research in Finance. The functions of this committee are to review and supervise the specific research activities of the staff of the Financial Research Program.

RALPH A. YOUNG, *Chairman pro tempore* — University of Pennsylvania; Director, Financial Research Program

RAYMOND J. SAULNIER, *Secretary* — Barnard College, Columbia University; Research Staff, National Bureau of Economic Research

WILLIAM J. CARSON — University of Pennsylvania; Executive Director, National Bureau of Economic Research

DAVID FRIDAY — Consulting Economist; Director, National Bureau of Economic Research

E. A. GOLDENWEISER — Director, Division of Research and Statistics, Board of Governors of the Federal Reserve System

F. CYRIL JAMES — Principal and Vice-Chancellor, McGill University

WALTER L. MITCHELL, JR. — Director of Surveys, Research and Statistical Division, Dun & Bradstreet, Inc.

WESLEY C. MITCHELL — Columbia University; Director of Research, National Bureau of Economic Research

SHEPARD MORGAN — Vice-President, Chase National Bank; President, National Bureau of Economic Research

WOODLIEF THOMAS — Assistant Director, Division of Research and Statistics, Board of Governors of the Federal Reserve System

DONALD S. THOMPSON — Chief, Division of Research and Statistics, Federal Deposit Insurance Corporation

ROBERT B. WARREN — Institute for Advanced Study

JOHN H. WILLIAMS — Dean, Littauer School, Harvard University; Vice-President, Federal Reserve Bank of New York

LEO WOLMAN — Columbia University; Research Staff, National Bureau of Economic Research

DONALD B. WOODWARD — Research Assistant to the President, Mutual Life Insurance Company of New York

Papers Published by the National Bureau of Economic Research

Occasional Papers

1	MANUFACTURING OUTPUT, 1929-1937 (December 1940) <i>Solomon Fabricant</i> . . . . .	.25
2	NATIONAL INCOME, 1919-1938 (April 1941) <i>Simon Kuznets</i> . . . . .	.25
3	FINISHED COMMODITIES SINCE 1879, OUTPUT AND ITS COMPOSITION (August 1941) <i>William H. Shaw</i> . . . . .	.25
4	THE RELATION BETWEEN FACTORY EMPLOYMENT AND OUTPUT SINCE 1899 (December 1941) <i>Solomon Fabricant</i> . . . . .	.25
5	RAILWAY FREIGHT TRAFFIC IN PROSPERITY AND DEPRESSION (February 1942) <i>Thor Hultgren</i> . . . . .	.25
6	USES OF NATIONAL INCOME IN PEACE AND WAR (March 1942) <i>Simon Kuznets</i> . . . . .	.25
7	PRODUCTIVITY OF LABOR IN PEACE AND WAR (September 1942) <i>Solomon Fabricant</i> . . . . .	.25
8	THE BANKING SYSTEM AND WAR FINANCE (February 1943) <i>Charles R. Whittlesey</i> . . . . .	.25
9	WARTIME 'PROSPERITY' AND THE FUTURE (March 1943) <i>Wesley C. Mitchell</i> . . . . .	.35
10	THE EFFECT OF WAR ON BUSINESS FINANCING: Manufacturing and Trade, World War I (November 1943) <i>Charles H. Schmidt and Ralph A. Young</i> . . . . .	.50
11	THE EFFECT OF WAR ON CURRENCY AND DEPOSITS (September 1943) <i>Charles R. Whittlesey</i> . . . . .	.35
12	PRICES IN A WAR ECONOMY: Some Aspects of the Present Price Structure of the United States (October 1943) <i>Frederick C. Mills</i> . . . . .	.35
13	RAILROAD TRAVEL AND THE STATE OF BUSINESS (December 1943) <i>Thor Hultgren</i> . . . . .	.35
14	THE LABOR FORCE IN WARTIME AMERICA (December 1943) <i>Clarence D. Long</i> . . . . .	.50

15 RAILWAY TRAFFIC EXPANSION AND USE OF RESOURCES IN WORLD WAR II (February 1944) <i>Thor Hultgren</i> . . . . .	.35
16 BRITISH AND AMERICAN PLANS FOR INTERNATIONAL CURRENCY STABILIZATION (January 1944) <i>J. H. Riddle</i> . . . . .	.35
17 NATIONAL PRODUCT, WAR AND PREWAR (February 1944) <i>Simon Kuznets</i> . . . . .	.50
18 PRODUCTION OF INDUSTRIAL MATERIALS IN WORLD WARS I AND II (March 1944) <i>Geoffrey H. Moore</i> . . . . .	.50
19 CANADA'S FINANCIAL SYSTEM IN WAR (April 1944) <i>Benjamin H. Higgins</i> . . . . .	.50

Technical Papers

1 A SIGNIFICANCE TEST FOR TIME SERIES AND OTHER ORDERED OBSERVATIONS (September 1941) <i>W. Allen Wallis and Geoffrey H. Moore</i> . . . . .	.50
2 THE RELATION OF COST TO OUTPUT FOR A LEATHER BELT SHOP (December 1941) <i>Joel Dean</i> , with a Memorandum on Certain Problems in the Empirical Study of Costs by <i>C. Reinold Noyes</i> . . . . .	.50
3 BASIC YIELDS OF CORPORATE BONDS, 1900-1942 (June 1942) <i>David Durand</i> . . . . .	.50