REVIEW: CURRENCY AND EXCHANGES

INDIAN CURRENCY AND EXCHANGE, By H. L CHABLANI, M.A. (Oxford University Press, Bombay) 1925.
8 y 2 x 5 y 2 pp. 184 Rs. 4-8-0

THIS brochure is a poor production. Within the small compass of 180 pages devoted by the author to a hurried treatment of a somewhat complicated subject, there is neither sufficiency of information nor sufficiency of illumination. Methodology is conspicuous by its absence. There are so many contradictions and compromises in his book that it is difficult to know what is the exact position of the author. In one place he says gold cannot be circulated in India because India is poor. In another place he says gold does not circulate in India because there are rupees. After devoting one whole chapter to the discussion of the quantity theory of money—in itself the simplest and the most obvious proposition in Political Economy—he says the rise of the Rupee after 1893 was not altogether due to the limitation of its issue! Similar contradiction appears in his chapter on Foreign Exchanges. There he contrasts the two theories—namely, the Theory of Purchasing Power Parity and the theory of the Balance of Trade—and gives his judgement in favour of the former as being the true theory. Yet throughout the book he argues on the basis of the wrong theory, namely, the Balance of Trade. Again, in his opening chapter he says that there is nothing absurd in reverting back to the silver standard! Management of currency is according to the findings of the author, one of the greatest defects in our currency. Yet he recommends a convertible Rupee as the remedy for this evil! The compromises which the author makes are witnessed by the fact that he agrees with almost every proposal made for the reconstruction of Indian Currency. He sees good in Dr. Fisher's plan, in reverting back to the silver standard, and also in an universalised Gold Exchange Standard. Nevertheless, the author has his own pet plan and that is to have a ' Convertible Rupee ', convertible not in gold coins but in gold bullion only. The author does not disclose it, but it is the plan suggested by Ricardo in his"Proposals for an Economical and Secure Currency". Fortunately for England it was not adopted. The reasons were simple. To legislate that notes shall be converted into gold bars of certain weight meant that only those who had notes of the value of the gold bars, could convert. The rest could not. In other words, it was felt that such a system would considerably weaken the effect of convertibility and would thereby give an opening to inflation. The proposal was not therefore deemed to be secure enough. The point whether the proposal was economical was not debated upon at the time, and may here be conveniently dealt with ; since there are so many writers in India—and our author is one of them—who, in order to show themselves civilised, indulge in vituperations against what they call the barbarity of using gold as currency. All these civilised writers on currency spend their energy in demonstrating the self-evident proposition which no one disputes that to use paper as a medium of exchange is more economical than to use gold. But these same writers never care to prove that such a plan besides being economical will also be secure in the sense of ensuring stability of prices. A merely economical plan which does not guarantee security is of no use. The plan to be acceptable must be both economical and secure. It will do, if it is not economical; but it will certainly not do, if it is not secure. Now I submit that the proposition that to economise gold as a currency is to impair its utility as a standard of value is as self-evident as the proposition of the civilised writers that to use paper as a medium is more economical than to use gold. For what does this discarding of gold from currency use mean? It simply means this; that by economising the use of gold you thereby increase its supply, and by increasing its supply you lower its value i.e. gold by reason of this economy in its use becomes a depreciating commodity and therefore unfit to that extent to function as a standard of value. It cannot be denied that issues of paper money, or any other substitute for that matter, affect the demand for metallic money. There are no doubt some who make the reservation that the demand for metallic money will or will not be affected by a paper issue according as the paper money is convertible or inconvertible. But this is an error. The test is whether the paper issues are covered or uncovered by a metallic reserve. If they are covered then they will not affect the demand for metallic money. But if they are uncovered, then they will affect the demand for metallic money whether they are convertible or inconvertible. The reason is : covered notes merely represent metallic money ; but uncovered notes add to the stock of value. Therefore you cannot both economise gold and also use it as a standard. If you want to economise gold, you must abandon gold as a standard of value. Besides, in the present day there is no necessity to economise gold, because there is all over the world such a great plethora of money that the less we economise gold the better. From this point of view the Gold Exchange Standard, once a boon, is now a curse. It served a very useful purpose for some time. From 1873 the production of gold had fallen off and the economy effected by the Gold Exchange Standard was indeed very welcome; because it helped in a period of contraction to expand the money of the countries of the world and thereby maintain the stability of the international price system by preventing the rapid fall in prices, which would have been inevitable if all the countries which established the gold standard had also adopted gold as currency. But after 1910 conditions changed and the production of gold increased, with the result that the continuance of the Gold Exchange Standard thereafter not only did not help the countries to check the rise of prices but actually helped to raise them by causing as a result of the economy in its use a redundancy of the already over-produced gold. The author approvingly quotes Prof. Fisher and others who blame the Gold Standard for the rise of prices after 1911. But Prof. Fisher forgets to take note of the fact that gold became a bad standard of value because of continuance elsewhere of the Gold Exchange Standard. For if after 1911 the Gold Exchange Standard has been abandoned and countries had used gold instead of economising it, there would have been no redundancy of gold and the rise of prices consequent on it would have been arrested. The Gold Exchange Standard from this point of view has outlived its purpose and is now doing positive harm. In the light of these considerations it is not possible to have any sympathy with projects that economise the use of gold and yet maintain it as a standard of value.

These points must have entirely escaped the author when he conceived his project of a Rupee convertible into gold bullion. But convertibility into gold bars does not embody the whole plan of the author. Along with convertibility he says a limit must be placed on the issue of rupees and small notes, even when they are legally convertible into gold bullion. The currency in India should be allowed to expand annually by only a certain small percentage representing its normal rate of progress in business. Beyond that percentage Government should have no power to increase the currency...... In giving reasons for this fluctuating limit on the issue of rupees and small notes, the author says,"A 'convertible rupee 'being small in its denomination, is not adequate safeguard against inflation ; for, as the older economists clearly showed, the *de facto* suspended convertibility of the small notes makes it practically inconvertible, and its over-issue, is just as likely as that of inconvertible paper."All this is fantastic if not strange. It is strange because the author in one place says"convertibility is the best safety-valve for redundancy of currency: it provides the easiest automatic danger signal to Government which is inflating the currency."Now, if this is so, why is a convertible Rupee not sufficient for the purpose the author has in view? The author is quite wrong when he says that the older economists believed that convertibility of small notes was not a sufficient safeguard against over-issue. What the older economists feared was not that convertibility was not enough to maintain gold in circulation if the Banks were allowed to issue notes of small denomination— a view which is quite different from the one ascribed by the author to the older economists. Again to realise their aim the older economists did not urge, as our author represents them to have done, the placing of a limit on their issue. What they urged was a total prohibition of the notes of small denomination. That is why we find the Bank of England prevented by the Charter Act from issuing notes of lesser denomination than £5. To be consistent, the author should have recommended that the Government of India should not issue Rupees or silver notes of lesser denomination than Rs. 5. Instead of this he recommends a haphazard and an unworkable plan. Supposing it were possible to fix this percentage—the author has not told us how to do it—is the percentage to be maintained at all times? Or will it be sufficient if it were found at the end of the financial year that the percentage has not been exceeded? If the latter is all that the plan demands, then there may be no limits to the increase and decrease in the volume of currency that may be issued in the course of the year, provided care is taken that at the end of the year the balance errs on the side of an increase equal to the given percentage over the normal. Again, is the normal to be a figure fixed for ever or is it to be revised? If it is revisable then how is it to be revised and what authority is to revise that normal? These are some of the questions that have to be answered before the plan can be accepted. But one wonders whether instead of indulging in such in genuities it would not have been better if the author had played the common role and recommended either a convertible Rupee or an inconvertible Rupee with a fixed limit of issue.

The book consists of lectures delivered by the author in his capacity as a Professor to his students at the Elphinstone College, Bombay, and at the Central Hindu College, Benares, and is divided into two parts. Part I which is mostly informative, the author says, is"intended for candidates preparing for the pass degree in economics.''Part II''is mainly critical''and''is meant primarily for the candidates for the Hons. degree.''As an examiner in Economics I always wondered why the answers of most of the pass students in Political Economy read like children's recitation of nursery tales and those of the Hons. like garbled versions of borrowed comments. It is now evident that this is due, as the author naively suggests, to the fact that the two sets of students are fed on two different kinds of fare—neither of which is supplied to them in plentitude or certitude.