[Distributed to the Council and the Members of the League.]

Official No.: **C. 530. M. 264.** 1932. II. A.
[F. 1102.]

Geneva, July 6th, 1932.

LEAGUE OF NATIONS

FINANCIAL COMMITTEE

REPORT TO THE COUNCIL ON THE WORK OF THE FORTY-SIXTH SESSION OF THE COMMITTEE

(Geneva, June 27th to 30th, 1932.)

CONTENTS.

INTRODUCTION.

The Financial Committee has the honour to submit to the Council the following report on the various questions with which it has dealt during this session. The following members were present:

M. SUVICH *(Chairman)*;
Mr. Norman DAVIS;
M. DAYRAS;
M. JANSSEN;
M. KEMPNER;
M. TER MEULEN;
M. MLYNARSKI;
Sir Otto NIEMEYER.
M. TANAKA.

There were also present:

1. *For Austrian Questions:*
   M. ROST VAN TONNINGEN, Representative of the Financial Committee in Austria.
2. *For Bulgarian Questions:*
   M. WATTEAU, Adviser to the National Bank of Bulgaria.
3. *For Greek Questions:*
   Mr. FINLAYSON, Financial Adviser to the Bank of Greece.
4. *For Hungarian Questions:*
   Mr. TYLER, Representative of the Financial Committee in Hungary.

S.d.N. 1.380 (F.) 1.305 (A.) 7/32. Imp. Kundig.

Series of League of Nations Publications
II. ECONOMIC AND FINANCIAL
1932. II. A. 15.

1. GENERAL SECTION.

The Financial Committee held a short session (June 27th to 30th), its regular May meeting having been postponed. It discussed the situation in Austria, in Hungary and Bulgaria with the League of Nations representatives in Vienna and Budapest, and the Commissioner in Sofia, and heard a statement concerning conditions in Greece by the Adviser to the Bank of Greece. It discussed, in addition, the final report of the Gold Delegation, which has been published since the Committee last met.

At the moment of the Committee's meeting, the Austrian problem is being discussed at a meeting of a delegation of the Committee and representatives of certain Governments to which the Council referred the general part of the Committee's forty-fifth report on May 21st.

---

2. BULGARIA.

The Financial Committee noted the twenty-third report of the Commissioner of the League of Nations in Bulgaria and the additional explanations supplied to it verbally by the Commissioner.

The Committee took note of the budget situation as it appears immediately before the close of the financial year 1931-32. The budget year 1931-32 is likely to end with a deficit (800 million levas) somewhat larger than had been anticipated, and this deficit has in fact been met from receipts belonging to 1932-33. The budget 1932-33 shows an expenditure of 7,300 million levas and it is hardly likely that the receipts can reach this total (the current receipts were about 6,300 million in the previous year).

It seems improbable that the budget can be balanced even with the strictest control of expenditure by means of the monthly budgets in the absence of the fundamental reforms recommended by the Financial Committee.

The Committee considered the Decree, issued on April 20th, 1932, by the Bulgarian Government, provisionally suspending 50 per cent of the transfers for the foreign public debt service. The Committee pointed out to the Government that the terms of this Decree are not in conformity with the Committee's recommendations.

The Committee has been informed that owing to the difficulties of the Treasury the Finance Minister has asked the Commissioner to agree that the State should be exempted from paying as budgetary sinking fund for its debt to the National Bank, the sum of 100 million levas which fell due at the end of the financial year 1930-31. This payment has not been made, although the necessary funds are reserved for the National Bank out of the profit on the coining of subsidiary currency.

The failure to make this payment would be an infraction of the Protocol of March 10th, 1928, and the Financial Committee feel bound therefore to bring it to the attention of the Council. They feel, however, that, in the present abnormal circumstances, exception should not be taken to the temporary suspension of the debt redemption and that the amount in question may be released to the Bulgarian Treasury. They would recommend a similar waiver of the payment due for 1931-32.

The Committee also dealt with the question of the payment to the National Bank as sinking fund for the State debt, of the profit on the coining of subsidiary currency as under the terms of the Protocol.

The Committee, at its session in January 1932, agreed that, owing to Treasury difficulties, this payment might be in some measure postponed. It considered that by this postponement the payment in question might be put off until the 1933-34 budget. It now confirms this recommendation.

---

3. GREECE.

The Committee's attention was specially directed to the measures taken by the Greek Government with regard to its external debts.

In its previous report the Committee had recommended measures, as regards the redemption of external loans, particularly through the International Financial Commission, for a provisional suspension of transfers for a period of one year. The Committee added:

> " This recommendation is subject to the maintenance by the Greek Government of the full payment in drachmæ of the amortisation in question, a step which the Committee believes to be essential for the maintenance of proper order in the public finances ".

It suggested that the sums thus paid in drachmæ should be employed by the Bank of Greece in advances to the Greek Government for unavoidable expenditure on the irrigation schemes which are in process of execution. In order that Greece might enter in its budget the credits in drachmæ relating to the redemption of its external debt, the Committee suggested the readjustment of certain taxes and fresh reductions in expenditure.

At the Council's meeting on April 15th, M. Veniselos said, in the first place, that the Greek budget was incapable—if it was to be properly balanced—of bearing even in drachmæ the charge for the amortisation of the external debt. In the second place, he announced that Greece not having obtained the foreign loan which she was requesting—a request which had been partially supported by the Committee—would henceforward be unable, until this assistance had been granted to her, to make the transfers required for service of the interest on its foreign debt. The payment of coupons would therefore be suspended until further notice as from May 1st. M. Veniselos added that the sums in drachmæ corresponding to the interest service would be deposited at the Bank of Greece in a blocked account.

In noting M. Veniselos' statement, the Council observed that, in any case, " the bondholders or their representatives are alone competent to discuss these questions with the Greek Government and to consent to such waiver of their legal rights as may appear to them to be called for in the present emergency ".

The Greek Government suspended transfers (redemption and interest) as from May 1st. This unilateral measure led to strong protests at the Council meeting of May 21st by the United Kingdom representative, with whom the French representative associated himself. He expressed " his deep regret that the Greek Government should have failed to carry out the solemn obligations undertaken towards its creditors, the League and the Governments represented on the Financial Committee ". The Council drew the Greek Government's attention once more to " the necessity of making every effort to comply with its obligations ".

Since then, not only has the Government made no transfer in respect of its foreign debt, but in the budget which it submitted to Parliament for the financial year 1932-33, beginning on April 1st, it only provided for the interest service on its foreign debt a sum equivalent to about half the amount which was required for this service when the drachma was at a gold parity. Owing to the present depreciation of Greek currency, this sum represents hardly more than a quarter of that for which Greece is liable for interest on its foreign debt. Furthermore, no credit was provided for redemption.

The Greek Government therefore went much further than had been anticipated and, in particular, it did not pay full interest on its debt in the national currency, a principle to which the Committee has always attached the greatest importance. In the case of Greece, the Committee is obliged to note that the Government has demanded of its internal creditors a sacrifice of 25 per cent, but has reduced by about 75 per cent the payments intended for its foreign creditor.

The Financial Committee cannot but regard such a situation as gravely prejudicial to Greece's credit.

4. HUNGARY.

The Committee thinks that the situation in Hungary does not require a new general report. It refers to its report of the forty-fifth session, and limits itself for the moment to pointing out the most recent default of Hungary in its external debts. The Hungarian Government failed, on June 15th, to transfer the remittances due to the Trustees of the Hungarian Loan 1924, and has informed the Trustees that, while the amount in pengö calculated at the official rate of exchange to cover the service of the loan will be placed to the credit of the Trustees at the National Bank of Hungary, the proceeds of the pledged revenues will cease to pass through the hands of the Trustees.

Failure to maintain the service of the loan involves a breach both of obligations assumed towards the bondholders and of obligations assumed towards the Council.

The raising of the loan formed an essential part of the plan adopted in 1924 for the financial reconstruction of Hungary and the Council did not give its approval to the issue of the loan unless Hungary, in addition to accepting control by a representative of the Council over the execution of the measures to be taken to re-establish monetary and budgetary stability, entered into obligations towards the Council as regards the meeting of the service of the loan out of the revenues on which it was secured. These obligations are included in Protocol II of March 14th, 1924.

Under this Protocol, the yield of the hypothecated revenues, which to-day at the official rate of exchange cover the charge about six times, must be paid in to a special account under the sole control of Trustees appointed by the Council to represent the interests of the bondholders, and Hungary has undertaken to permit them to fulfil the functions assigned to them by the Protocol. The functions of the Trustees as set out in the Protocol, and laid down in the General Bond in execution of provisions, of the Protocol, are such that their full exercise is irreconcilable with even a temporary suspension of the service of the loan. They are obliged to transfer out of the special account on the first day of each month to each country in which the loan was issued in the currency of that issue at least one-twelfth of the annual service of the loan. The present default involves the complete suspension of such transfers.

Further, the Trustees are not entitled to release to the Government any moneys in the special account (which is, of course, an account in Hungarian currency), retainable by them for the purposes of the service of the loan, and the General Bond expressly provides that, if the Government defaults in its direct obligation in regard to the loan service, they shall still retain from the special account sufficient funds to make goods such default and provide against further default. The Trustees therefore possess powers which it is their duty to exercise, to retain the whole of the revenues flowing into the special account. It must be recognised that such action would, in the present circumstances, deprive the Hungarian Government of funds without which the government of the country could hardly be maintained; and it is for this reason that the Hungarian Government has now removed the revenues from the Trustees' control. Such interference with the powers of the Trustees over the special account, however, involves a further breach of the Protocol. In this respect Hungary has therefore fallen into the same position as Bulgaria.

The Committee think it right to add that the total exports of Hungary during the first five months of this year had fallen to 56 per cent of the exports during the same period last year (33 per cent for the same period 1930) and that, at present, less than 30 per cent of the export exchange received is in readily available currencies. The Committee hopes, however, that there will be a seasonal improvement in trade after the harvest which may enable Hungary to increase her transfer capacity.

But the Committee can see no lasting remedy for the steady decline of Hungarian trade other than general measures of financial and economic reconstruction to which they have drawn attention several times in previous reports.

The Committee is gravely concerned at these breaches of international undertakings, and, in general, by the successive defaults of Hungary on all its external debts.

---

5. ROUMANIA.

The Committee was informed of the letter that the Roumanian Government has addressed to the Secretary-General, in which it expressed the desire to obtain the technical assistance of the League of Nations in applying its plans of financial reform and in the economic reconstruction of the country.

The Committee requested its Chairman to follow the developments of this question.

---

6. REPORT OF THE GOLD DELEGATION.

The Committee has considered during the present session the final report of the Gold Delegation. It believes that this report will prove of real value for those responsible, both for monetary and general economic policy, and trusts that special attention will be drawn to it. Further, it desires to state that it is in general agreement with the constructive financial and economic proposals contained in the report of the Gold Delegation. Extracts of these proposals prepared by the Secretariat are appended to the present report.

The Committee had referred to it the resolution of the sixteenth Labour Conference advocating the establishment of a gold truce. The Committee think it enough in this connection to refer to the report of the Gold Delegation of June 1932.

---

7. BUDGETARY PROVISIONS.

The budget of the Financial Organisation for 1933 has been communicated to the Committee in accordance with Article 7 (3) of the Financial Regulations. The Committee has taken note of this budget, observing that, as in the budget for the current year, a sum of 250,000 Swiss francs has been inserted in Chapter I, Item 3 (*b*), Unforeseen (Financial) to be used, subject to the vote of the Council, for special calls for technical advice and assistance arising from the financial crisis.

Annex

EXTRACTS OF PROPOSALS CONTAINED IN THE REPORT OF THE GOLD DELEGATION (PREPARED BY THE SECRETARIAT).

I. Restoration of the Gold Standard.

" The Delegation records its belief that, at the present stage of world economic development, the gold standard ", [if properly managed as some emphasise], " remains the best available monetary mechanism ".

" It is impressed by the practical difficulties and dangers of regulating currencies which are not on a common world basis, and by the very great desirability of agreement upon an internationally accepted standard in order to facilitate the free flow of world trade. Whatever the theoretical advantages that may be urged in favour of other monetary systems, their universal adoption presents very grave, if not insuperable, practical difficulties at the present time. The Delegation is, moreover, of the opinion that, granted the general acceptance of certain guiding principles, the gold standard is capable of functioning in such a way as to achieve most of the advantages of stability and justice claimed for alternative standards more broadly based on commodities other than gold " (paragraph 78).

II. Price Problems.

(*a*) " If prices remain at their present low levels, or fall to still lower levels, the burden of debt will in many cases become unbearable " (paragraph 175).

" A rise from the present level of prices would make the payment of fixed charges considerably easier. The real burden of debts and other fixed money charges would be lessened. We regard such a rise of prices as desirable. We do not look, however, to monetary policy alone to adjust the price-level, which is influenced by many factors of a non-monetary character. But we recognise that monetary policy, expressed through the volume of credit, may, if the general situation permits, play a large part in determining the level of prices. Hence we feel that, where credit contraction for one reason or another has been carried to extremes, it is proper and, indeed, imperative for the Central Bank to take such action, as may be within its power, to check excessive contraction, and in some cases to take the initiative in encouraging a freer use of credit. There is, of course, a danger that measures taken to expand credit may be undertaken prematurely, thus encouraging the belief that it is unnecessary to seek further correction of fundamental economic maladjustments. They may in some cases even lay the basis for a new expansion of credit which it may prove difficult to control.

That a rise in the price-level will take place when business confidence returns and industry revives is scarcely to be doubted. Meantime, it cannot be too strongly emphasised that, whatever remedial action is undertaken in the monetary sphere needs to be supplemented by evidence of progress in the settlement of such perplexing and disturbing problems as reparations, international debts, disarmament and trade restrictions " (paragraph 176).

(*b*) Next, " we consider it highly desirable that monetary policy should be directed to an avoidance of violent fluctuations in purchasing power " (paragraph 184).

" While firmly convinced that the wide fluctuations in prices and the recurrence of periods of economic depression constitute the greatest threat to the whole economic organism to-day, we desire at the same time to emphasise (1) that we do not consider it possible to avoid all oscillations in the general level of prices, and (2) that we are fully aware that even that measure of stability, which we would all wish to achieve, cannot be secured by monetary policy alone. We do not envisage, as an objective, complete stability of any group of aggregate prices; we do not envisage identical movements in all countries or in all groups of commodities. Identity of movement between, for instance, the prices of intermediate products and those of consumption goods is incompatible with the growth of efficiency. Complete stabilisation and identity of group movements are, indeed, impossible in a dynamic Society, and Society must either develop or decay " (paragraph 185).

III. The Criteria.

(*a*) " The criterion of monetary and economic policies should be their success over a period of years in maintaining the average level of wholesale prices of important international commodities relatively stable. But this does not mean that wholesale price index-numbers should be used as a sole means of determining when action should be taken to correct economic and monetary maladjustments. On the contrary, we show below that other and more sensitive indicators should be used. As we have already suggested, for action to be effective it must be taken in time. To check a fall in prices after that fall has set in is, we believe, very much more difficult than to prevent it developing. It is obvious therefore that, to be effective, monetary policy must rely upon other guides than those which, after the event, may be used as a test of its success " (paragraph 193).

" Moreover, international phenomena are the outcome of a complex of national phenomena. It is necessary not only to maintain the various national price-levels in equilibrium with one another, but also to take account of the domestic economic situations affecting the various national price-levels. Any policy designed to maintain the world price-structure in equilibrium, therefore, must necessarily be of a dual character. Those responsible for monetary policy in each country must take account both of domestic and of international considerations, and these may not be easily reconcilable. It is for this reason that we attach particular importance to the development of methods of continuous consultation and co-operative effort to maintain the international equilibrium without sacrificing national interests " (paragraph 194).

(*b*) " The first indicator for national policy should therefore, in our opinion, be the gold reserves and the gold movements, and policy should, apart from quite exceptional circumstances, be directed to accelerating the effects which such movements create " (paragraph 195).

(*c*) Other indices which reflect business activity—*i.e.*, " the market rates of discount, the yield of bonds, the prices of different classes of shares, the value of building permits, the debits to individual deposit accounts, the production of various primary products, the international movements of capital, etc. The significance of these will vary from country to country and from epoch to epoch. No set rules for their interpretation can be laid down " (paragraph 196).

IV. International Measures.

(*a*) " Restoration of a reasonable degree of freedom in the movement of goods and services " (paragraph 81).

" If measures are to be sought in the domain of monetary policy designed to lessen the amplitude of the periodic fluctuations in business activity, they must be accompanied by appropriate measures of general economic policy. The trade cycle is to-day an international phenomenon. Countries cannot hope to escape its effects by self-isolation. They can only hope collectively to lessen them. To this end they must permit an adequate freedom in the flow, not of credit alone, but of goods. In our opinion it is imperative that the restrictive commercial policies adopted by Governments to-day should be radically changed. Adherence to an international monetary standard at once implies and necessitates adherence to an international economic system. To impose artificial restrictions on the movement of goods is the negation of such a system " (paragraph 227).

(*b*) " A satisfactory solution for the problem of reparation payments and war debts. "

(*c*) " The gradual and cautious resumption of international credit and capital movements. "

(*d*) The acceptance by Central Banks " of certain guiding principles in respect of the working of the gold-standard system " (paragraph 81).

V. National Measures.

(*a*) " To restore and to maintain equilibrium in the national economy. This means that the budgets of the State and other public bodies must be balanced on sound principles, and also that the national economic system as a whole, and especially costs of production and costs of living, should be adjusted to the international economic and financial position, so as to enable the country to restore or to maintain the equilibrium of its balance of international payments " (paragraph 82).

(*b*) " Gold movements should not be prevented from making their influence felt both in the country losing gold and in the country receiving gold " (paragraph 81). " Policy should, apart from quite exceptional circumstances, be directed to accelerating the effects which such movements create " (paragraph 195).

(*c*) " The official discount rate supplemented, in certain cases, by open-market operations " (paragraph 198). " Open-market operations may render a real aid to central bankingau thorities when, for one reason or another, difficulties arise in making the official discount rate effective. They should, in our opinion, be looked upon as a supplementary, not alternative, lever. They should be employed rather to intensify than to deaden the semi-automatic influence of gold movements " (paragraph 201). " While we attach considerable importance to the last point, we are aware that special circumstances may occur in which counteracting open-market operations may be advisable " (paragraph 202).

(*d*) In the great creditor countries pressure and persuasion, if occasion arises, upon the commercial banks and issuing houses in order to discourage excessive or injudicious loan transactions. And in borrowing countries a watch and control over the volume of their borrowings so as to assure that they are devoted to productive purposes (paragraph 203).

(*e*) But, on the other hand, " lending must not be impeded by artificial restrictions, such as discriminatory rates of taxation ". " Any measures designed to improve the mechanism for the issue of foreign loans or to promote international transactions in existing securities," such as " the improvement of facilities for foreign investments, the quotation of foreign securities on national Stock Exchanges, the equalisation of taxes on domestic and foreign investments " would contribute to the smooth working of the gold standard (paragraph 205).

VI. Use and Economy of Gold in the Monetary System.

(*a*) "Now that gold coin is in circulation only in a very few countries and an internal drain cannot take place (except in moments of violent panic for hoarding as bullion), the reserves are primarily required to meet possible deficits in the balance of payments. Each country, in determining the gold reserve required, should therefore consider in the first instance what the range of movement in its balance of payments is likely to be " (paragraph 211).

" We are of opinion that it would be advantageous, as we argued in our first Interim Report, to reduce the reserve ratios from their present high levels..... In our opinion, the lowering of the minimum reserve ratio could and should be accomplished in such a way as not to endanger the liquidity of the Central Banks " (paragraph 212).

(*b*) " We regard the gold-exchange standard in this form [*i.e.*, as it was practised before the war] as a useful system for many countries, for whom it still remains the most economical and efficient monetary mechanism available " (paragraph 221). In this connection " two possibilities have been suggested ". The first is that countries adopting it should "choose carefully among the principal financial centres those which offer the greatest promise of future stability. The other is that an endeavour should be made to spread the risks of losses by utilising such an international institution as the Bank for International Settlements as the agency through which the system shall be administered. In the latter case, the reserve assets of the gold-exchange standard country would be deposited with the International Bank, which would in turn spread its deposits among its constituent Central Banks " (paragraph 221).

(*c*) Other methods of economising gold.

(*i*) " In all countries where gold is in active circulation or kept in the vaults of commercial banks, it could be withdrawn into the reserves of the Central Banks and replaced by notes.

(*ii*) " That in all countries in which banknotes of small denominations are in circulation, these small notes should be withdrawn and replaced by subsidiary coin. The employment of such notes is in the main the accidental result of inflation in certain countries. Notes which were originally of relatively high value have been allowed to continue in circulation after their value diminished. The result has been to increase the strain on gold reserves and, since a gold backing to such notes is required, the cost of subsidiary currency to the community as a whole.

(*iii*) " That in countries in which notes are largely used for payments of taxes and salaries, large retail transactions, the transference of money from place to place, etc., the use of cheques, post office banking facilities, transfers, mechanism for clearings, etc., should be developed. Much could be done directly by Governments and municipal authorities in this connection without legislative action, were they to set the example of accepting cheques whether drawn on commercial banks or on post office savings banks in payment or taxes, public utility services, etc. " (paragraph 223).