

SECTION IX.—THE FUTURE OF NEW ZEALAND CURRENCY.*

83. The question of the future relationship of the New Zealand currency with sterling is a matter for consideration. It has always been recognized as a normal function of government to prescribe by law the basis of the unit of currency, and in fact every currency is so established. Thus under the gold standard a British pound-note was convertible into a sovereign containing about 123·27 grains of standard gold. The New Zealand pound-note was convertible into a British pound-note and thus indirectly into a sovereign of the same value. As long as the value of the British currency remained fairly stable, this arrangement had great merits, because it gave stability to New Zealand exchange, and sustained an internal price level free from major fluctuations. At a time when British prices have been subject to a violent fall, it is legitimate for New Zealand to consider whether parity with sterling should be restored, and, if so, when, though naturally no final decision on this question would be made without consultation with Great Britain. A return to parity would at present involve the Dominion in a general deflation of its internal wholesale-price level to at least the level of British wholesale prices. In Section III (paragraph 22) reasons have been given for the belief, that, with a reduced amount of overseas borrowing, the New Zealand wholesale price level might fall even further if parity of exchange is to become again the natural as well as the official rate.

**The Legal Basis of
Currency.**

84. In Section VIII the general economic effects of different rates of exchange with sterling were considered.† From the analysis given in that section it may reasonably be assumed that under present conditions a rate above parity has net economic advantages. If this rate were fixed at, say, 10 per cent., the question arises whether it should be revised downwards gradually until parity is restored, whether it should be raised, or whether the rate should be stabilized at this level. It is impossible to come to a definite conclusion at present upon these alternatives. The influences to be considered in arriving at an ultimate decision may, however, be considered. It is the purpose of this section to draw attention to these influences.

**The Future Legal
Basis.**

85. The heavy fall in export prices is the main reason for concluding that a rate above parity has economic advantages.† It may therefore be assumed that the future of export prices in relation to internal costs will determine the advantage or disadvantage to be derived from maintaining a rate above parity with sterling. At the present 10-per-cent. rate export prices are 40 per cent. below the 1929 level. Costs, whether measured by the index number of farm costs, wholesale prices, or the cost of living, have fallen about 10 per cent. Let us take an increase in the rate, say, 25 per cent., purely for the purpose of illustration. This rate would raise export prices in the proportion of 125 to 110. That is from 60 to 68. They would still be much below costs. If, however, the adjustments in fixed charges and wages (see Sections X and XI) and the fall in import prices brought costs down from 90 to 80, the disparity would be reduced to 18 per cent. It would not be necessary to bridge the whole of this gap because exporters must expect to suffer a loss of real income proportionate to the loss suffered by the community as a whole. In these circumstances a rise of 15 per cent. in export prices might be sufficient to restore a balanced economic structure. If this improvement in export prices did not take place, further reductions in money costs or an increase in the rate of exchange, or some movement in both these directions, would be necessary to restore economic equilibrium. If international prices rose by substantially more than 15 per cent., it would be possible to reduce the exchange rate without causing internal disturbance, unless world prices, and with them New Zealand export prices, fluctuated more violently than at present seems possible, the variations in the exchange rate around the assumed rate would in these circumstances be slight.

**Factors determining
the Exchange Rate.**

86. The question arises whether such a rate could be maintained. Bankers are dealers in exchange, and they would naturally be averse from accumulating funds in London if they thought a fall in the exchange rate was inevitable. Hence the normal seasonal accumulation of funds in London during the export season would tend to drive the rate down, though there might be an upward pressure later when the export season was over. These seasonal fluctuations in London credits did not exert a disturbing influence upon the exchange rate before the depression, because it was the practice to maintain stability with sterling. In these circumstances an accumulation of funds in London did not cause any difficulties. The sterling holdings of the banks had a relatively stable value in New Zealand currency, and could be sold off later as the demand for London funds increased for imports, interest payments, or other financial transactions. There was thus a stabilizing influence. This is absent when the exchange is substantially away from parity and there is a general presumption that it will return to parity. If a rise in the rate occurred, a temporary accumulation of funds in London would be likely, but with exports valued at £32 m. sterling and Government and local-body demands as low as £8·5 m. (the minimum that would be required, even though the floating debt can be funded in London), imports would have to settle at £23·5 m. to balance funds. Accumulation would then occur only to the extent that imports fell below the level or other loans were raised. In so far as accumulation took place, it

**Temporary
Stability.**

* See Addendum by Mr. Park.

† This is subject to Mr. Park's Addendum concerning effect on the Budget.