

(c) In the case of internal-debt charges, money costs are unaffected by the exchange-rate ; but the real costs are definitely influenced by it. A lowering of the rate of exchange would increase the weight of internal debt. A lower level of money incomes derived from exports sold under a lower exchange-rate would widen the gap between farming receipts and costs and would compel adjustments which would be reflected in a general reduction of money incomes. The fall in the internal price-level would increase the real burden of all fixed debt charges—national, local-body, and private. (See Report of Economic Committee, 1932, pages 30 to 32, for a fuller exposition.) The exchange-rate of £125 New Zealand to £100 sterling has supported internal prices above the level which would have prevailed under any substantially lower rate, and therefore has provided (nationally) some relief from the dead weight of debt. Summed up : The higher exchange adds to the money costs of the external debt but does not increase its real burden ; the higher exchange adds nothing to the money costs of internal debt but does decrease its real burden.

(d) A lowering of the rate of exchange would stimulate imports in the first instance, and this would swell the Budget. Whether the increased revenue would be maintained would depend, however, on the course of external prices. The cost-price structure of farming would immediately suffer by a lowering of the rate, and unless export prices rose by an amount at least equivalent to the loss of income sustained through exchange reduction the economic distress of farmers would rapidly spread to the rest of the community and prejudice their power to meet direct taxation as well as their power to purchase imported goods. Since there is no valid reason for assuming that lower exchange-rates would cause a rise in external prices, the result on the Budget is unpredictable. If no rise in export prices occurred, revenue from other than imports would be more difficult to collect, and imports would also decline once the loss in farming income began to express itself in diminished buying. My conclusion is that, in our circumstances where national income and therefore taxable capacity is so sensitively responsive to the course of external prices, a rise in prices should precede any lowering of the rate of exchange.

(e) The initial stimulus to imports under a lower exchange would set a limit to further accumulations of exchange funds purchaseable by the Government, but would involve a loss on the amount now held. This loss would be of little economic consequence if rising external prices restored farming and national prosperity ; but it would be serious if prices failed to rise and the cost has to be borne by a Budget weakened through the diminished revenue consequent upon a fall in money incomes.

(f) A consideration of these various factors convinces me that the Government would be unwise to lower the rate of exchange in the present depressed and obscure circumstances. It might conceivably be justified if it were certain that external prices would rise sufficiently to restore the profit structure of farming. But there is no such certainty. The risks of undermining still further our farming industries while they still remain our major source of income are too great to be assumed. The serious consideration of a proposal to lower the rate should be postponed until either higher external prices or lower internal costs (or both) have definitely restored the profit equilibrium between costs and receipts.

(g) It would be wise, I think, to go further than this and definitely devalue our currency at the present rate. I justify this on the grounds—

- (i) That it would be unwise to lower the rate :
- (ii) That it would be difficult or impossible (politically) to raise the rate :
- (iii) That gradual cost adjustments to the present rate have made it an appropriate rate :
- (iv) That devaluation would introduce a degree of certainty now lacking from the exchange situation.

In regard to the last point : it is probable that uncertainty as to the future of the rate, combined with an expectation on the part of importers and traders that the rate would fall, has done much to cause the accumulation of credits in London. It has been fully enough stated (but with what authority I cannot say) that a generally cautious policy of importation due to the fear of being caught with large stocks bought at a high rate has prevailed, and that British exporting firms have opened accounts with New Zealand banks rather than pay the costs of transferring money to Britain (see *National Opinion*, 12th April, 1934, p. 7). If this is so, the only apparent explanation would be the hope or expectation of currency appreciation. A definite act of devaluation would therefore remove the incentive to these practices. It would also have the broader effect of minimizing distrust in the future of the currency. I would point out that at present there is not only the distrust entertained by those who fear a further depreciation, but also the distrust entertained by those who fear appreciation. Farmers and many who trade in farming belong to the latter group. Many cases have been brought to my notice of potential purchasers of farm lands who refuse to conclude the deal until they are reasonably sure that the rate of exchange will not be lowered. This is quite rational, since they are not prepared to assume important exchange risks in addition to the ordinary risks of farming at the present time. Although the effect of this uncertainty both in limiting importations and in freezing land transfers is not measurable, it may be of considerable importance, and is certainly of some importance. My conclusion on this point, therefore, is that stabilization of the exchange is desirable as a measure to increase the fluidity of trade. Moreover, I think that stabilization should be effected through devaluation at the rate of £125 New Zealand to £100 sterling, since a lower rate is likely to have serious repercussions on our key industries, while a higher rate is, I believe, inexpedient at present.

(h) The stabilization I have in mind, however, must permit of some elasticity. It has been suggested that the margin of fluctuation round the par should not exceed 30s. per cent. either way, on the grounds that this represents the cost of gold transfer between New Zealand and London. This, as I have said, is not relevant, since gold transfers are not normally important in our exchange system. I admit, however, that initially at least the limits of fluctuation set by law will be largely