PROFESSOR JEVONS ON THE INDIAN EXCHANGE

The Future of Exchange and the Indian Currency. By PROFESSOR H. STANLEY JEVONS. (Oxford University Press, Indian Branch. 1922. Pp. xii+264+4. 18*s.* 6*d.* net.)

THIS book is most stimulating to thought, and contains within a small compass the chief data on which to form a judgment. Professor Jevons has inherited his father's gift of never writing a dull line. I recommend it to everyone who is interested in this perennially interesting question—subject only to the proviso that the price of the book in relation to its length is outrageously high.[1]

Professor Jevons admits, somewhere in the course of the book, that he was gradually thinking out his conclusions while he wrote, and had not arrived clearly in his own mind at the conclusions of the last chapter when he began the first one, with the inevitable result that the broad outline of his argument does not stand out as plainly as it might. But the stages of his main argument are as follows :—

(1) He accepts the view that the rate of exchange of the rupee with sterling will be determined by the ratio of the Indian rupee price level to the British sterling price level. Everything depends, therefore, upon what is going to happen to these two price levels respectively.

(2) The Indian price level will depend on the currency policy of the Government. For all practical purposes it is now on the basis of inconvertible paper, so that internal prices are not automatically adjusted to outside prices. Under the policy existing at present the volume of currency in India cannot fluctuate very much. The Government is not melting rupees or selling gold, or paying off at most more than a relatively small amount of the securities in the paper currency reserve. Unless, therefore, the Government changes its policy on one or other of these heads, the volume of currency cannot fall very much. On the other hand, the Government is not coining more rupees at present, and is not adding to the securities in the paper currency

[1] So high as to reflect discredit, *primâ facie*, on the justly celebrated house which publishes it.

reserve. So long as these conditions obtain, it is equally the case that the currency cannot increase very much. The Government is too high-minded to inflate and too impoverished to deflate, a happy combination of inhibitions which tends to keep prices steady. Not that prices must therefore remain absolutely steady; they can suffer a certain amount of fluctuation for reasons not arising out of monetary policy. For example, a certain number of rupees disappear from circulation every year. A good harvest might put prices down, for obvious reasons, and there are other minor influences. Nevertheless, the broad conclusion holds that if the Government goes on as at present prices are not likely to move sensationally. Only if the Government deliberately deflates by one or other of the methods open to it, will prices fall; and only if it inflates, will they rise.

(3) What about sterling prices? On this head Professor Jevons comes to two conclusions. He thinks that the trade cycle will cause a certain increase of sterling prices in the near future, but that this will not last very long or go very far, and that a big rise for trade cycle reasons is not due for some years yet. On the other hand, he thinks that the long period trend of world prices, as distinct from cyclical movements, is likely to be, on the whole, downwards during the next generation. He gives some reasons for this, but also nearly as many on the other side.

(4) Is there any factor tending to disturb the relation between internal prices and external prices as measured by the level of exchange hitherto? Professor Jevons thinks that the effect of the new and prospective import tariffs may be to raise internal prices relatively to external prices somewhat, perhaps 15 per cent., in the absence of any movement in the level of exchange; or alternatively, if internal and external prices both remain at their present level, to raise exchange by say 15 per cent.

Accordingly he sums up with the opinion that, unless the Indian Government do something to stabilise the exchange, the tendency of sterling prices to fall will, in the absence of any deflation in India itself, tend to drag down the exchange. He does not, however, look for this quite immediately, first because of the temporary upward movement of sterling prices which he foresees in the near future, and partly because the new tariff will have an initial influence in the opposite direction.

Assuming the correctness of this argument, what ought the Government of India to do? Professor Jevons sees no advantage in leaving matters alone, which would result, in his judgment, in a slow sagging of the exchange. On the other hand, he thinks that it would be perfectly feasible for the Government, with its present resources available for purposes of deflation, to carry through with success the very moderate deflation which might be required to stabilise the rupee at 1*s*. 4*d*.; because, although he expects a fall of world prices, he does not expect this to be so severe as to require heavy deflation in India. On the other hand, he is opposed to any attempt to raise the rupee up to the 2*s*. level, on the ground that the deflation required in India to effect this, since it would have to be sufficient both to counteract falling external prices and to raise the exchange, would involve a disastrous interference with the business life of India.

Therefore let the rupee be stabilised forthwith at 1*s*. 4*d*., and let the Government of India dismiss from their minds the bogey, which mainly influenced the Currency Committee of 1919, of silver rising in price so much that the bullion value of the rupee would exceed its currency value.

This is a powerful argument, which takes account of the main factors of the case, and proceeds, in my opinion, in accordance with a sound schematism.

Nevertheless, I have two important reservations to make, and do not altogether endorse Professor Jevons' conclusions.

In the first place, I do not accept his conclusion that the trend of sterling prices is likely to be downwards. This is too long an argument to enter upon here. But I believe that the general tendencies towards a rise of prices, the existence of which Professor Jevons admits, are likely to overbalance causes operating in the other direction. In any case, prophecy is almost impossible, because many unknown factors will come into play; but if I had to guess, I should make the opposite guess to Professor Jevons, and should say that prices are more likely to rise than to fall. In addition, I think he under-estimates the rise of prices which is likely to come about during the impending trade revival, if he is right, as I think he is, that such a revival is due to take place. The price level reached during the depth of the depression was so much below what was really justified by world currency conditions that a substantial rebound may easily occur.

If I am right about this, exchange, if it is left to itself under present conditions, is likely to tend gradually upwards rather than downwards as Professor Jevons predicts. How far it will go up, whether to 1*s*. 5*d*., to 1*s*. 6*d*., or a good deal higher, it is impossible to say, but I should expect the trend to be in that direction rather than towards 1*s*. 3*d*. or 1*s*. 2*d*.

My other point is of a different kind. I think that Professor Jevons over-estimates the advantages of stability in exchange as against stability in internal price level in the case of such a country as India. Indeed, it is not obvious anywhere in the course of his book that he is clearly aware of the important antithesis between these two aims, although the latter aim much influenced the recommendations of the Indian Currency Committee of 1919. As he points out, the price level in India has remained during the recent sensational years very much steadier than anywhere else in the world. He shows on page 212, that if we consider the fall in prices from the highest monthly figure in 1920 to June 1921 the drop was in England 41 per cent., in the United States 47 per cent. and in India 12 per cent. But he does not draw the conclusion that the much-abused exchange policy actually pursued deserves a large part of the credit for this phenomenon. By allowing exchange to rise somewhat precipitately during the time when sterling prices were rising furiously, India was spared the extremity of rise which took place elsewhere; and by allowing exchange to fall during the acute period of the depression from April 1920 to April 1921 India was also spared the full fury of the collapse of prices. If the rupee exchange against sterling had been stabilised through the whole of the last three years at any level you choose to mention, India would presumably have felt the full fury of the price fluctuation in Great Britain. Stability in the internal price level is so superlatively desirable in such a country as India, that the fact of her having got through the recent cycle with so small a fluctuation of internal prices is a great deal to be set against the inconvenience to merchants engaged in foreign trade from the fluctuations in exchange.

The most just criticism of the Government of India's action, in the light of after-events, is that, from every point of view, they were overdoing it in attempting to raise the rupee so high as 2*s*. 8*d*.—a rate not contemplated by the Currency Committee. Prices outside India never rose so high as to justify a higher exchange than 2*s*. 3*d*. on the criterion of keeping Indian prices stable at the 1919 level.

The following table of approximate values, which I have compiled, exhibits: first, the remarkable stability of Indian prices during 1919–20; second, the hopelessness of the attempt to maintain the rupee at the highest 1920 figure, namely 2*s*. 8*d*., unless the Government were prepared to deflate internal prices some 20 per cent.; and third, the accuracy with which the purchasing power parity theory has worked, apart from the temporary and unsuccessful aberration of the 2*s*. 8*d*. rupee for a brief period in 1920, as between India and England, indicating considerable stability in the real ratio of exchange between the two countries.

	Indian Prices.	English Prices.[1]	Value of Rupee in Sterling.	
			Purchasing Power Parity.	Actual Exchange.
Average, 1919 .	100	100	100	100
Highest, 1920. .	112	129	115	152
Lowest, 1921 . .	95	65	69	72
Average, 1922[2] .	90	64	71	74

In the light of this experience I should be disposed, at the present juncture, to aim at sparing India some part of the rise in prices which is likely to occur in England by leaving matters as they are a bit longer, and letting movements outside India pull the exchange just as they like, in the hope that internal rupee prices would tend in that case to maintain their present relative stability. When the English index number had risen say to 200 or a little above as compared with 1913, then I might be inclined to stabilise the exchange, for the time being, without giving pledges for the future, at whatever level it had attained of its own motion by that time. For I fully accept Professor Jevons' arguments as to the feasibility of fixing exchange, within reason, at whatever level the Government of India think fit; and I also accept his view as to the general presumption in favour of fixing exchange more or less where you find it at the moment of stabilisation, rather than of trying to force it to some fancy figure.

I have not elaborated the arguments against Professor Jevons' view as to the future of world prices; but the passages which he interpolates about the harvest cycle and its effect on the trade cycle are no longer quite up to date, and are somewhat crude, having regard to recent more elaborate developments of credit cycle theories in general.

Since the publication of Professor Jevons' book, the rupee has moved moderately but appreciably upwards, until, as I write, it stands above 1*s*. 4*d*. Meanwhile the Indian authorities have modified their policy to the extent of recommencing the

[1] Statist. [2] First 10 months.

sale of Council Bills by tender. This has retarded but not prevented the rising tendency and appears to be due to the usual desire on the part of the India Office to strengthen its sterling balances (although it appears from Professor Jevons' figures that replenishment can hardly, as yet, be essential), rather than to any definite decision about future policy. Moderate sales of Councils in accordance with cash requirements would be quite compatible with the general policy I suggest above. Sir Basil Blackett, the new Finance Member of the Viceroy's Council, has gone to a problem not quite so thrilling as some of those he has left behind him, but of purer *intellectual* quality perhaps.

J. M. KEYNES