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The Story
of
Canada's
War Finance

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THE STORY
OF
CANADA'S
WAR FINANCE

BY

RIGHT HON. SIR THOMAS WHITE, K.C.M.G.
MINISTER OF FINANCE, 1911-1919

MONTREAL: -

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IT is my intention in the following pages to deal in a general way with the subject of Canada's financial administration during the war period. The war is by far the most profound event in our history, and it is, I think, desirable that its principal transactions in the several departments of administration should be made the theme of timely review by those most intimately associated with them. By this means, events will be seen in the light of contemporary knowledge, motive, colour and circumstance, and with clearer understanding than is possible from a bare historical recital of outstanding facts.

THE STORY OF CANADA'S WAR FINANCE

CHAPTER I

Outbreak of War—Demand upon Banks for Gold—Conference with the Bankers—Measures taken by the Government—The Financial Panic Ended.

IN July, 1914, I was on vacation at Rye Beach, a summer resort on the Atlantic Coast in the State of New Hampshire. During the last week of the month the press was filled with alarming reports of the critical European situation, which had developed with startling rapidity following the ultimatum served by Austria upon Serbia. The conflagration so much dreaded for years past was about to burst forth and the world was appalled and stunned at the prospect. During the first days of consternation the stock exchanges and bourses of the great financial centres, unable to withstand the flood of securities with which they were deluged, closed their doors one by one. It was thought in United States that the New York Stock Exchange would be able to continue business, but with the closing of the London Stock Exchange it became clear that this was impossible and New York closed with the others. On the part of creditors everywhere a demand at once arose for gold, and the international exchanges became speedily demoralized. On Friday, the last day of July, I grew exceedingly anxious about the Canadian situation. No advices of an alarming character had reached me from Canada, but the closing of the stock exchanges and the general disturbance of the world finance caused me much apprehension as to possible panic in Canada. I became so uneasy in mind that I decided to return at once to Ottawa, which I did, arriving on Sunday, August 2nd. I at once communicated by telephone with

Sir Vincent Meredith, president of the Bank of Montreal. He informed me that while he did not as yet regard conditions in Canada as alarming, there had been considerable demands upon the banks for gold. Heavy withdrawals had occurred in various parts of the Dominion, and particularly in Montreal and Toronto. We discussed over the telephone the probability of "runs" upon the several banks, and I suggested a meeting with the Executive Committee of The Canadian Bankers' Association for the purpose of discussing the whole situation and taking such measures as might be necessary to meet any crisis that should arise. He stated that a meeting of the Committee had been arranged for the following day at Montreal. I requested that after their meeting the bankers would come to Ottawa and make such recommendations as they deemed proper in the emergency.

By the next morning it became apparent that the situation was very grave. Many "runs" upon the banks took place throughout the country, and some particularly heavy withdrawals were made in Toronto and Montreal, gold being demanded in every case. It was clear that the public was becoming panicky. In both Montreal and Toronto there was an active demand for safe deposit boxes from the trust companies for the purpose of hoarding gold withdrawn from the banks. One case was reported to me from a Toronto bank. One of its best customers, a prominent citizen of Toronto, who has a deposit of over a quarter million dollars, called upon the general manager and informed him that he felt he must, in justice to himself and his family, withdraw the full amount in gold, as he believed that there would be a financial panic in which all the banks would have to close their doors. It was in vain that it was pointed out to him that if depositors throughout the country would exercise coolness the situation would be tided over and that upon the other hand if they, like himself, should demand gold the catastrophe which he apprehended would most certainly be speedily brought

about. The man insisted and received his gold which he locked up in his safe deposit vault. Several similar instances were reported to me on that Monday morning from Montreal.

At noon on Monday, August 3rd, the leading members of The Canadian Bankers' Association, headed by its president, the late Mr. D. R. Wilkie, arrived in Ottawa on a special train from Montreal. They were quite disturbed at the spread of the financial panic throughout Canada and the "runs" which were taking place throughout the Dominion and of which they were continually receiving word. They had numerous and by no means unanimous suggestions to make as to what should be done. During Monday afternoon we discussed the whole situation very fully and finally reached certain conclusions which I embodied in a memorandum which I wrote out during the conference. Neither in the Bank Act nor in any other Dominion legislation had provision been made for meeting conditions of financial panic in Canada. The law was that if a bank was unable to meet its demand liabilities as called upon by its creditors, it must close its doors. The lack of legislation providing for the contingency of panic was one of the grave defects in our banking system. It was obvious that a banking institution, however strong, could not be expected to be in a position to pay all its liabilities upon demand. Deposits received from the public were loaned, in the ordinary course of business, to the commercial community, a sufficient liquid reserve being maintained for the purpose of meeting contingencies such as occur from time to time in the course of the banking business. Cash reserves of banks extended to an amount of from ten to twenty per cent. of liabilities, and in addition to these our banks had large available liquid reserves in the form of call loans in New York. It was clear that these reserves which were more than ample for peace-time requirements would be quite inadequate to meet nation-wide withdrawals by the great body of the public acting under the influence of

panic and demanding gold. Under the law the banks were obligated to pay depositors either in gold or Dominion notes. Dominion notes represented and were convertible into gold, so that Canada was truly upon a gold basis. The first point to be considered therefore was how to put the banks in a position to meet all demands made upon them. It was clear that this could not be done if payment had to be made in gold or Dominion notes. The solution of the problem was to empower the banks to make payment in their own notes, although they were not legal tender under existing law. Bank notes, however, could only be lawfully issued by a bank to the amount of its paid-up capital and the amount of gold and Dominion notes deposited by it in the Central Gold Reserve. In order to provide that the banks should have sufficient bank note circulation to meet all withdrawals, it was proposed that the Dominion Government should make advances in Dominion notes to the chartered banks (charging interest therefor), against the pledge of securities deposited by the banks with the Department of Finance. The banks were also authorized to issue what was known as "excess circulation" during the period from March 1st to August 31st. This privilege had been hitherto confined to the crop-moving period, which was that part of the year from September 1st to the end of February. It was also thought advisable that redemption in gold of Dominion notes should be suspended. A moratorium was suggested by some, but I was unwilling to have one declared in Canada, as I feared its effect upon our credit. I am happy to say that, although authority was, as a precautionary measure, obtained from Parliament to do so, it did not become necessary for the Government during the war to declare a moratorium.

After reducing to writing the above-mentioned proposals, I telephoned the Prime Minister, who kindly came to my rooms where the conference with the bankers was being held. We explained to him the situation which had arisen and the need for immediate action. We also explained to

him the measures which we thought necessary to meet the emergency. An Order-in-Council was necessary to give them effect and I asked the Prime Minister to call a meeting of Council for eight o'clock that evening. Sir Robert readily grasped the situation and concurred in the conclusions reached. A Cabinet meeting was accordingly called in the evening and the various measures which I have mentioned embodied in an Order, which was signed immediately by the Governor-General. I had arranged in advance with the King's Printer to have a special Gazette containing the Order-in-Council issued before midnight. A full statement was given to the press setting forth to the Canadian people that, owing to the necessity of conserving gold, the banks were authorized by the Government to make payment of their liabilities in their own notes. It was further announced that the Government would, to whatever extent was necessary, make advances in Dominion notes to Canadian banks upon securities pledged by them with the Minister of Finance. The public were also informed that the Government was "prepared to give other possible assistance in order to prevent any avoidable interruption of stable business conditions" and for this purpose would "not hesitate to use to the fullest extent all existing powers and, if necessary, to ask further powers from Parliament." This announcement was made to the public on the morning of August 4th, the day upon which war was declared by Britain upon Germany.

It is to be noted that all the measures adopted were directly contrary to law. The provisions of the Bank Act and other Dominion financial legislation were deliberately over-ridden. The justification was the emergency which existed and the national interests at stake. The Order-in-Council embodying the measures decided upon was legally of no validity. It was, however, accepted by the Canadian people, and, when the official announcement appeared the next morning in the Canadian press "runs" upon Canadian banks were at an end. The placing of

the resources of the Government behind the banks by the provision for making loans to them in Dominion notes against securities at once restored confidence, and throughout the entire war period there was never again a sign of financial panic or of any "runs" upon Canadian banks. The plan adopted to meet the crisis was decided upon and carried into effect during one afternoon and evening. The last proceeding of the day was the signature, at my request, by the bankers present of a memorandum signifying their approval of what had been done. No one could foresee what the effect of such measures would be. It was possible that they might aggravate the situation, as notice would be given to all parts of the country that an acute condition had arisen. As it turned out, however, the Canadian financial panic was ended, the public patriotically acquiescing in what had been done. At the August session of the House the Finance Act, 1914, was enacted embodying the provisions of the Order-in-Council in legislation. It is now one of the permanent statutes of the Dominion, available at any time of national emergency to meet conditions of panic as they were met at the opening of the great war.

CHAPTER II

Business Conditions in Canada—Early War Financing—Borrowings from the British Treasury—Views as to the Duration of the War—Organization of the First Contingent—Gold Shipments to Ottawa.

WHEN the war broke out Canada was experiencing a business reaction which had been in evidence for some months. The Balkan struggle of 1913, which was the forerunner of the world-war, had most seriously affected the London money market, and loans for Canadian railway and industrial enterprises were not forthcoming as they had been for years past. It was just as well that the check came when it did, as expansion had been carried far beyond the bounds of prudence. With the slowing

down of the influx of British capital, our imports had shown monthly declines and our customs revenue had suffered rather severely in consequence. This condition was much aggravated by the outbreak of war. The cessation of intercourse with enemy countries, the interruption of trade with Great Britain and her allies, the demoralization of exchange, the requisitioning of shipping for war purposes, the restrictions placed by the Allies upon imports and exports, the closing of the London money market—all these and many other factors threw our external trade into confusion during the first months of the war and greatly embarrassed the Government's finances. From April 1st, 1914, to the end of the following January, our customs revenue showed a falling-off to the extent of nearly thirty million dollars. It is not generally remembered that the first effect of the war upon Canada was to bring about unsettlement in business, industrial slackness, and unemployment. The latter was much in evidence during the winter of 1914-15. To meet it, the Government, notwithstanding the heavy expense incurred in organizing, equipping, despatching overseas, and maintaining the first contingent, pressed forward as rapidly as possible its programme of public works, including much railway, canal and other construction. It has been suggested that we should have levied heavier taxation at the outbreak of the war. The effect of this would undoubtedly have been to increase the business depression and probably, through public discontent, materially affect the extent of our participation in the war. There was at that time no adequate realization of the duration and severity of the struggle which was to test the Empire to the limit of its courage and resources.

With public revenues declining and the London financial market closed, the question of how to raise money for our capital expenditures, and above all for our military effort, was a most anxious one. In a letter to Sir George Perley, Acting Canadian High Commissioner in London, upon the

matter of our finances, dated August 31st, 1914, I find I wrote: "These are terrible times and we cannot tell what lies ahead of us. All we can do is to take matters up from day to day and accomplish what is possible to us." I find also letters of about the same period to the Prime Minister, the Minister of Railways and Canals, and the Minister of Public Works, urging that only the programme of public works which was already under way should be proceeded with, and pointing out the serious financial condition with which we were confronted, with the London market closed, in having to provide in addition to our other expenditures a war expenditure of fifty million dollars for the remainder of the fiscal year.

It is to be borne in mind that in those days the sum of fifty million dollars was regarded as a very large amount even in terms of national finance. The largest loan which had previously been issued by the Dominion Government in the London market was for six million pounds and it was, in substantial part, a refunding operation. An issue of seven million pounds of Canadian Northern Railway securities guaranteed by the Government of Canada had almost thrown the London investment market into a panic in the fall of 1911.

As our military expenditure was to be mainly abroad, it would not have been wise to attempt at that time to raise a loan in Canada. Our bank deposits were fully employed in meeting commercial requirements. The large Canadian war loans which were floated during the last years of the war were made possible by the increased production of the country, for which high prices were obtained and from which large national profits were made. These profits were available for the war loans, the proceeds of which were all expended in Canada in the financing of further production. It would have been a mistake at the outset of the war, with exchange adverse to us, to raise money in Canada to finance military expenditures in Great Britain and on the continent. The policy followed was

the sound one, namely, to borrow for our military expenditure abroad from the British Government. During the first months of the war our principal outlay was in England and it was met from the proceeds of a loan from the British Government. For the period from September to the end of March, 1915, we arranged with the British Treasury for advances aggregating twelve million pounds sterling.

It is interesting now to recall the views which were held at Ottawa at the beginning of the war with respect to its duration and the extent of Canada's participation. There were few who thought that the war would last more than a year. Lord Kitchener's dictum that he had enlisted for a period of three years was not assumed to reflect his considered opinion as to the length of the conflict. Hints from the Imperial Government indicated an opinion on their part that events were about to transpire in Europe which would have an important influence in materially shortening hostilities. This, I think, must have related to the entry of Italy into the war, which was expected at an earlier date than it occurred. One of my colleagues bet me fifty dollars that there would be peace in Europe before February. Others were not so sanguine, but I am within the mark in saying that not one of them had the slightest notion that it was to be a four years' life-and-death struggle.

With regard to Canada's contribution in men, it was thought that twenty-five thousand would be the maximum in the first contingent. I distinctly remember thinking that this number might ultimately increase to fifty thousand. Anyone who had predicted that Canada's contribution would finally exceed half a million men would have met with derision. It must be kept in mind that Canada's only experience in war during living memory had been the South African conflict to which we had contributed a small contingent. In the light of existing knowledge, it seemed to most Canadians that the sending of twenty-five thousand men, in the first instance, with an additional twenty-five

thousand later on, would be a mighty achievement on the part of the Dominion and more than would likely be necessary on our part. It was felt that with Britain in the war the Central Empires must speedily be crushed.

From the financial standpoint such an effort on the part of Canada would involve, as we then regarded money, an enormous expenditure. There was a rough time-honoured official method of allowing one thousand dollars per man per annum as the cost of military operations. This would involve expenditure at the rate of twenty-five million dollars a year for the first twenty-five thousand, and fifty millions yearly for the maximum force. Such an estimate was of course wholly inadequate in the changed conditions of warfare. It was the intention, as I have said, to send in the first instance twenty-five thousand men. Owing to the martial spirit of Canadian youth coupled with the enthusiastic patriotism of the Canadian people and the untiring energy and brilliant organizing power of Col. the Honourable Sam Hughes, Minister of Militia, there was speedily assembled at Valcartier Camp a much larger force than had been expected, with the result that the first contingent consisted of thirty-three thousand fully-equipped Canadian soldiers. The recruiting, organization, and training of this force, with its quick despatch overseas, was to my mind one of the most outstanding of Canada's achievements during the war.

The leading financial features of the first stage of the war in Canada were the borrowing, which I have mentioned, from the Imperial Government, and an increase in the authorized Dominion note issue of twenty-five million dollars. There were many minor matters of interest. Arrangements were made with the Canadian banks to maintain liberal credits to their customers in order that general business might not be checked. It was also arranged that commercial discount rates should not be increased.

London had been the money centre and Britain the

great creditor nation of the world. Following the outbreak of war, Britain at once began to withdraw balances from foreign banks and to collect foreign indebtedness. The result was that the pound sterling went to a premium and a tide of gold began to flow to London. On account of the danger of ocean navigation, exposed as it was to hostile cruisers, it became impossible for United States firms to ship gold to London in payment of maturing indebtedness there. As exchange had been so seriously affected, they were not able to buy drafts upon London except at rates involving heavy loss. In the circumstances, the Bank of England, in order to meet the difficulty, announced that deposits of gold by American firms with the Receiver-General at Ottawa would be regarded as if received by the Bank in London for payment of creditors there. Many million dollars of American gold were shipped to Ottawa during the autumn of 1914 under this arrangement. It was received by officers of the Finance Department, who cabled advice to the Bank of England as to receipt of shipments, with particulars as to parties from whom received and instructions as to payment of accounts in London. Months later this gold began to return to the United States, as British exchange became unfavourable, and as Britain required money for the huge purchases which she was making for herself and her allies in the United States. There was a good deal of uneasiness in Canadian commercial circles during these days. I received a great number of telegrams and urgent letters from prominent business men advocating and in some cases demanding, that a moratorium should be declared postponing the payment of indebtedness in Canada and in London. The Government resisted considerable pressure in this regard. Fortunately it was not found necessary to take any action.

An incident of this period connected with the Finance Department may be specially noted. For weeks the City of Victoria was apprehensive of attack from Von Spee's Pacific squadron. It was thought that the German

Admiral might bombard the city from the sea, take possession and loot it of all its valuables. So impressed were we with this possibility that the gold in the vaults of the Receiver-General was removed inland. I believe the banks took similar action. The late Sir Richard McBride was then Prime Minister of British Columbia. During a visit to Ottawa on the matter of providing submarine defence for Victoria and Vancouver, I asked him whether there were not coast-defence guns at Esquimalt. He replied, "Yes, and they are very good guns, too. Their only drawback is that the breech block of one has been lost and six inches have been broken off the muzzle of the other. But for these defects they are in excellent condition." No doubt this was a humorous exaggeration of the facts, but the story is eloquent of the state of Canada's coast defences at the beginning of the war.

CHAPTER III

Financial Problems—The Problem of Finding Money—Effect of Raising the Tariff—Our First New York Loan—London and New York as Markets.

THE opening of the year 1915 found us with the first contingent overseas and with 50,000 men under training in Canada. While there was no longer talk of early victory, great expectation was built upon the spring campaign, especially of Russia. In fact, throughout the whole war it was always the next spring campaign which was to accomplish victory. At the period of which I am writing, the stern nature of the contest and adequate realization of the severity of the test which lay before them had not yet dawned upon the Canadian people. The entry of Italy on the side of the Allies in April, 1915, raised high hopes of an early victorious termination of hostilities.

On the financial side, it was clear that we must raise large additional revenue. Industry and general business were still suffering from the initial shock of the war, and our customs returns, which had always been the mainstay

of Canada's federal income, were showing heavy declines. We were leaning upon the British Treasury, not only for our war expenditure in England, but also in Canada, and for part of our public works and railway expenditure as well. The latter had been maintained for the purpose of affording employment during the winter months of 1914-15. The pound sterling was still king in the world of international finance and London exchange was at a premium. So long as this continued, the British Treasury was quite willing to lend us money, even for expenditure other than for war purposes in Canada. The situation in this respect was, however, gradually changing, owing to the immense expenditure by Great Britain in the United States for munitions, foodstuffs, steel and other manufactured products. By June of 1915 exchange had become unfavourable to London, and the problem of how to find funds to continue to purchase in constantly increasing amount in the United States and Canada became a very vital one for the British Treasury. It was this which led later on to the many issues of British loans in New York and, in large degree, to the successive war loans in Canada. So far as Canada's finance was concerned, what really happened throughout the war was this: Britain lent us the money in London to pay all our military expenses overseas. We repaid Britain by moneys placed to her credit in Canada. She used these credits to purchase munitions, wheat, flour and other Canadian products. The sale of these products enabled Canadians to subscribe the war loans. In a word, we paid the cost of our military operations by our production during the war. Canadian goods and services constituted the exchange which Canada made to Britain for providing for our expenditure overseas. We were to see before the end of the war all our borrowings for this purpose from the British Treasury repaid and an indebtedness to Canada by the British Treasury, of four hundred million dollars, owed half to the Dominion Government and half to Canadian banks.

To raise additional revenue, the Budget of 1915 levied special taxes upon banks, trust, loan and insurance companies, upon railway sleeping car and steamboat tickets, upon cheques and bills of exchange, express and post-office money orders, and increased the postal rates upon letters and post cards. Wines, patent medicines and perfumery were also taxed. Liquors, cigars, cigarettes and tobacco had been dealt with at the special session of August, 1914.

The main fiscal measure, however, was the uniform increase in general customs duties of $7\frac{1}{2}$ per cent. and in British Preferential rates of 5 per cent. Wheat, flour, tea, anthracite coal, and several other items were excepted from the increase. The justification for this unusual mode of raising tariff rates was that revenue was imperatively needed, and it was no time in the midst of war to deliberately revise the tariff, item by item. Canadian industry derived some advantage at a period when it was greatly needed because, although the tariff applied to raw material as well as finished product, the former represented only a part of manufacturing cost, and the net result was thus to raise the tariff advantage on finished products over what it had been before. The result of this customs increase was to almost immediately increase the national revenue and greatly stimulate business throughout Canada. It made us more self-contained, encouraged production both on farm and in factory, and assisted in conserving our gold reserves and the maintenance of our exchange with foreign nations by tending to reduce importation of many articles and foodstuffs which we ourselves could produce. My own view is that this increase in customs duties at the beginning of the war was of the utmost value to Canada in maintaining general prosperity and financial stability during the war and the period succeeding the armistice. In the Budget Speech of 1916, I was able to say, referring to this increase, "From the date of the introduction of the Budget (of 1915) the sharp monthly declines which had been experienced in our customs duties were at once arrested

and our revenues until August restored to the basis of the corresponding months of the year preceding the outbreak of the war. Since August a marked and continually progressive increase has characterized our monthly revenues."

In mid-summer of 1915 we determined to float as large a loan as possible in New York. We had thought of this at an earlier date, but it was not clear that either the Government or public opinion in the United States would favour a public offering there by one of the belligerent nations. The American people had, however, gradually come to realize the real issues of the struggle, and sympathy with the Allied cause was widespread in business and financial circles, especially in the East. The Allies were vast purchasers of American products of every kind. In order to continue their purchases it was known in financial circles that Britain and France would be obliged later to raise a loan in the United States. The suggestion that Canada should pave the way was therefore regarded with favour. The American public generally was more friendly towards Canada than to Great Britain, and it was not thought that serious objection would be raised in any quarter towards our borrowing in New York. Nevertheless, so sensitive was the situation that we decided to borrow not for war purposes but for public works and other capital expenditure. This would take the loan out of the category of a war issue, and would serve our purpose just as well, because the proceeds of the loan would liberate for war purposes just that amount of our own revenues which could then be applied for the purposes of war. It was as broad as it was long.

In July of 1915 we made an issue through Messrs. J. P. Morgan & Company and associates of \$45,000,000 in one and two-year notes, to yield five and five and a quarter per cent. interest respectively. The loan was a great success and was regarded with much satisfaction in Great Britain and in Canada. The only criticism came from some who failed to realize the effect of the war upon

interest rates, and from some investment dealers who were carrying municipal securities at pre-war prices and took a loss upon the change in value which the issue was thought to have brought about, but which it, in fact, interpreted because it had already occurred. Prior to the loan the securities market in Canada had been dead. The new loan cleared the air, declared the real interest rate upon high-class securities, and gave the market the fresh start and impetus which it needed. Those who shook their heads at five and five and a quarter per cent. interest rates were to see before the end of the war securities backed by the joint credit of Britain and France selling to yield nine per cent. in the New York market. The market for securities at any given time always reflects expert opinion as to the future. If the outlook is for tight money or uncertain conditions, the rate of interest which must be paid by those issuing securities is affected accordingly in advance. The price obtainable reflects the future as well as the present.

Borrowing in New York is very different from borrowing in London. London has been for generations an international money market. The British public will freely subscribe to issues of foreign securities. The public in the United States before the war had no such experience. They found all the investments they needed in their own country and had little knowledge of foreign investments. Canada they knew because we were their next-door neighbour, and our cities, municipalities and industrial companies had sold them debentures. They had practically no acquaintance with large loans by foreign Governments, and it took the experience of the war to broaden them in this respect. Even now, after that experience, it cannot be said that New York is an international market in the sense that London is. Only the wide extension of American foreign trade throughout the world, as that of England has extended, will make New York a financial clearing house like London, because commerce and finance go hand in hand and are intimately dependent one upon the other.

As to the mode of making issues, underwriting is essential in both markets where the amount required is so large that tenders cannot be invited with good result. But there is this vital difference: In London it is quite customary for underwriters to take a portion of the issue which has not been subscribed by the public. A loan in London which is only partly subscribed by the public is not regarded as a failure. The underwriters assume the balance and gradually market it. It is to ensure this that an underwriting commission is paid. In New York, on the other hand, an issue is not regarded as a success unless the public take it all and the underwriters obtain their full commission. The result is that the price fixed by the syndicate which floats a loan in New York is usually such as to absolutely ensure success. They wish to take no chances, and this attitude of mind inclines them to insist upon an attractive issue price. It is, however, to the advantage of high-class investment houses, both in London and New York, that issues should be made at the proper market price, because each issue has its influence upon the price of all other securities in which they are interested. My belief is that the difference in methods in London and New York is due to difference in temperament in the two peoples and that reputable issuing houses in both cities strive to do the best they can for their clients, having regard to the conditions which prevail at the time of issue. As illustrating the state of American opinion in 1915 respecting British securities, I recall an incident at the conference held in New York between British, French and American financial representatives, for the purpose of negotiating the five hundred million dollar Anglo-French loan of the Autumn of 1915. One of the most prominent New York bankers, who was strongly pro-British, said to me: "It is going to be pretty difficult to float this loan at a time when some financiers in New York are asking what would happen to British securities if the Germans should take London." Some western American bankers were afraid to take active

participation in this flotation because German depositors and customers had threatened to withdraw from their banks.

The Anglo-French loan was finally floated for \$500,000,000, which was much less than Great Britain and France desired to obtain. It was a five-year loan, with certain conversion privileges, bore interest at five per cent. and was underwritten at 96. The issue price to the public was 98. Its amount staggered the financial markets of the United States for a considerable period, and it was always heavy on the New York Exchange. Before the end of the war Canada was to show that, in a nation of only eight million people, loans of more than five hundred millions could be floated and their issue price maintained.

CHAPTER IV

Domestic War Loans—Canada's Favourable Trade Balance—
Doubts as to Success of Loan—Attitude of Investors—
Striking Success of the Issue—Establishing the First British
Credit—Educational Value of War Loans.

The first Canadian domestic war loan was floated in November, 1915. For many months it had been under consideration and was regarded as a somewhat doubtful experiment. No loan of even five million dollars had ever before been subscribed in Canada and a war issue of less than twenty-five millions would have been hardly worth while. There was, however, the clear necessity of discontinuing borrowing from the Imperial Treasury for our war expenditure in Canada. Exchange with America was unfavourable to Britain. Her purchases in United States and Canada of clothing, munitions, and other equipment and war material were on a constantly growing scale. Every withdrawal from London by the Canadian Government of funds advanced there by the Imperial Treasury aggravated the exchange situation and added to the cost of the British Government for New York funds with which to make its trans-Atlantic purchases. We

assuredly did not desire to lean upon the Imperial Treasury more than was absolutely necessary, but up to the spring of 1915 conditions in Canada, owing to the dislocation of business brought about by the war, were far from favourable for domestic financing on any considerable scale. A decided change had taken place by autumn. In the Budget Speech of the following February, I referred to this change in the following terms:

"Business has adjusted itself in a remarkable way to the altered conditions. We have been blessed with a most bountiful harvest, the greatest by far in the history of the Dominion, and this, coupled with the demand for war material, supplies and munitions, has given such stimulation and impetus to trade and industry that notwithstanding the war we are experiencing a high degree of prosperity."

It was the year of the great wheat crop in the Canadian Northwest and the year in which Canada began to manufacture munitions. This latter industry, destined to attain such large dimensions and to play such a part in enabling us to finance the war, will be made the subject of special comment later. For the present it will suffice to say that it owed its inception to the faith in Canadian industrial skill and enterprise of General Sam Hughes, Minister of Militia. Probably the most significant sign of the changed conditions was the alteration in Canada's trade balance. This had for years past been continuously adverse. For 1912-13 it had been adverse to the amount of three hundred million dollars; for 1913-14, one hundred and eighty millions, and for 1914-15, thirty-six million dollars. For the year 1915-16 it became favourable to an amount exceeding two hundred millions, with a total trade of twelve hundred millions, the largest in the history of the Dominion up to that time.

The prospects for a Canadian war loan seemed quite promising. Public utterances respecting the subject had been warmly received. Nevertheless, so great is the effect

of past experience upon the mind, the consensus of opinion in the financial world was that it would be exceedingly unlikely that we should be able to raise so large a sum as fifty million dollars. The general Canadian public were not investors. Before the war those who saved money in their business or from their salaries or wages for the most part deposited their savings with the banks. A small percentage bought bonds and stocks as investments. But farmers, mechanics, small tradesmen, and the salaried class generally had but little knowledge of securities. Large manufacturing and commercial concerns required all their liquid resources as working capital. The mass of the people did not know what a bond was. It seemed, therefore, that for the early stages of our war borrowing in Canada we should have to rely upon financial institutions, such as banks, insurance and trust and loan companies, and upon that comparatively small body of investors who had been accustomed to buy stocks and bonds for the investment of their money. The idea of endeavouring to organize so vast a country as Canada, with its scattered population, for the purposes of a nation-wide popular loan to which all citizens would be expected to contribute, had not yet dawned upon anyone. It was to come in due course, but only when the way had been prepared and necessity made it imperative.

The opinion among the leading financial men of Canada was that we might hope to obtain twenty-five million dollars. As we decided to make the issue fifty millions, it seemed certain that a very large portion would remain unsubscribed by the general public. To meet the situation the Canadian banks very generously offered to subscribe twenty-five million dollars upon the understanding that all subscriptions from the public in excess of twenty-five million dollars should be taken in abatement of their subscription. That is to say, they agreed without remuneration to underwrite the issue to the extent of twenty-five millions to ensure its success. Banks do not desire to

lock up their resources in securities and it is not in the national interest that they should do so. Their funds should be employed to as great an extent as possible in meeting the requirements of the agricultural, commercial, and industrial community for short loans for the purpose of production and marketing of commodities. I was most anxious in connection with all our war finance that the banks should not become burdened to the detriment of Canadian business and industry, with an undue amount of public securities and temporary loans. In respect of this, Canada undoubtedly came through the war in better case than any other belligerent nation, not excepting the United States. The result of this policy was that after the armistice the liquid resources of Canadian banks were available for the business of Canada. They were not locked up to a large extent in Government bonds as in the United States, or engaged in carrying the burden of an immense unfunded public debt as in Britain.

A great deal of consideration was given to the question of the terms of the first war loan. That so large an issue should be made attractive to investors was apparent. The investment community was still in a discriminating mood. The war had not advanced so far nor patriotism aroused as yet to such a pitch that rate of interest and other features of a loan became of secondary importance. Although a war loan, it was regarded by most of the investing community as an investment issue to be critically examined and compared with other investments available on the Canadian and New York markets. I do not mean to say that investing interests would not have subscribed to the first war loans if these had not been made financially attractive. But undoubtedly the amount of such subscriptions would have been smaller than they were. Life insurance and other investment companies desired and, indeed, felt it their duty to invest the trust funds in their hands to the best advantage. Private investors at that stage of the war, when Canada was upon a voluntary

enlistment basis and danger to the Empire did not yet appear acute, naturally sought to obtain as high a rate of return upon their investments as possible. Just as those engaged in agriculture, industry, and trade required the market price for their products and commodities, so those having money thought themselves entitled to rates of interest justified by market conditions. Throughout our early war financing the successive loans issued by the British Government in New York proved embarrassing to us. The Anglo-French Loan of 1915 could be bought in New York to yield six, seven, eight and even nine per cent. at different periods from 1915 to 1919, and proved a great rival attraction to Canadian investors who never doubted the ability of the British Treasury to pay interest and principal according to the letter of its obligations. On the New York and Canadian markets there were readily obtainable numerous other high-class securities with similarly attractive interest return.

The first Canadian war loan was of the maturity of ten years. It bore interest at five per cent. and was sold at 97½. This gave a yield rate of between five and five and a quarter per cent. As this was a low rate in comparison with what could be obtained upon other high-grade securities, it was issued free of taxation. This had been insisted upon by the New York interests which floated our earlier loan there and was regarded as a specially attractive feature by Canadian financial experts. It was also thought necessary that the privilege should be given to holders of the bonds to convert at issue price into the bonds of any succeeding Canadian domestic issue. The reason for this was that many investing interests were disposed to hold off until the next loan, believing that it must soon be made, and that, with advancing interest rates, it would be offered at a more favourable yield rate.

The loan was well received by the Canadian public. The best endeavours of the press and of the banks at all their branches throughout Canada were specially enlisted.

The bond dealers and stock brokers co-operated most effectually with their selling organizations. All other available agencies, including the churches, lent their aid, and when the last returns came in it was found that, instead of fifty millions asked for, more than one hundred millions had been subscribed by the Canadian people. This notable and striking success created a sensation both at home and abroad. That Canada, which had always been a borrowing country, and had no developed investment market of its own, should raise a hundred million dollars by popular subscription from its own people was hardly credible in London and New York. The success of the loan created almost as great an impression abroad as the news of the organization and quick despatch overseas of the first contingent of the Canadian Expeditionary Force. Canada as a military power surprised the world scarcely more than Canada as a financial power, able and willing to use her great financial resources towards the winning of the war.

Having received twice the sum asked for, the problem arose what to do with the surplus. It was clear it could be used to good purpose. Great Britain had made us huge advances for our war expenditure to date. She was labouring with the heavy task of finding money to purchase supplies in United States and Canada. The idea occurred to us that it would not only be the best use to which we could put the money, but also that it would afford a most striking illustration of Empire solidarity and Empire strength if we should devote this extra fifty millions as a credit in Canada to the British Government. Such a loan, the first of its kind to be made by any Overseas Dominion to the Mother Country, could not fail to be of striking effect throughout the world. The only difficulty in the way was the fact that we had by the prospectus confined the issue to fifty millions. This was overcome by issuing a notice to all subscribers that the amount of allotment would be one hundred millions instead of fifty millions and

giving anyone who so desired the right to withdraw his subscription. Only a very few withdrew or asked to have their subscriptions reduced and the thing was done. The news that Canada had been able to loan fifty million dollars to Britain to enable her to purchase munitions, foodstuffs, and other supplies in the Dominion came as a tremendous surprise to the outside world and undoubtedly had a heartening effect throughout the whole Empire. The gracious congratulations of His Majesty, the warm thanks of the Imperial Government, and the notable tributes of the British press all contributed to set in high relief Canada's first war loan as one of the most outstanding of the great achievements of the Dominion. Two other war loans were floated during the years 1916 and 1917. The securities and mode of issue were in the main similar to what I have described. In the second loan we asked for \$100,000,000 and were offered \$200,000,000. In the next we asked for \$150,000,000 and were offered \$250,000,000. In each case we took only the amount asked for by the prospectus. This policy kept the market firm and enabled us to obtain better prices for succeeding issues than would have been possible had we accepted all subscriptions and left no residue of buying power on the market.

One of the benefits of these early war loans was that they paved the way for the great Victory Loans which were to follow at the critical period of the war when the resources of both Britain and Canada were strained to the utmost. They educated the Canadian public to understand the nature of investment securities. They taught us to rely upon ourselves financially and greatly promoted thrift and saving among the people. They made us understand more clearly than could have been done in any other way the dependence of production and commerce upon credit, that is to say upon national savings. As illustrating the lack of knowledge in these early days as to the precise nature of a Government loan, I conclude with the story of a staunch Conservative yeoman, who had

attained to the dignity of a reeveship, who wrote me somewhat as follows: "I notice that the Government is going to make a public loan of fifty million dollars. In my opinion this is the best move the Government has yet made. The people here will take all the money you can lend us and if you choose me to do the distributing I will guarantee that no Grit will ever be elected in this constituency." This deluded man was under the impression that the Government intended to lend not borrow money.

CHAPTER V

Military Effort—An Army of Half a Million—Further Loans and Taxation—Suggestions for Raising Revenue—Business Profits War Tax—Criticism of Business Profits Tax—Profits of Munition Makers.

IT was not until the close of the year 1915 that the Canadian people fully realized the life-and-death character of the struggle in which the Empire was engaged. Up to that time it was generally believed that if Germany could be held upon the western front the Russians with their unlimited man-power would speedily pierce to the heart of Austria or even to Berlin and compel capitulation. That hope was doomed to early frustration. During the campaign of 1915 the Germans proved able with diminished forces to hold securely their western line, and, with augmented strength in the East, to drive the Russians out of Galicia and Poland as well. It was the beginning of a period of grave anxiety to the Allies.

Speaking of the war in the Budget of February, 1916, I used the following language: "The conflict has developed and extended upon a scale and to an extent far beyond our expectations or imaginings at its inception. Looking backward over its tragic course and reflecting upon its varied fortunes, there has grown in the hearts and minds of all an ever-deepening sense of its increasing gravity and menace to the Empire's safety."

In view of the gravity of the situation and with the

object also of producing a heartening effect throughout the Empire; Sir Robert Borden announced on New Year's day, 1916, that Canada's authorized enlistment would be extended to a total of half a million men. This momentous decision, which undoubtedly was of the greatest value by reason of its encouragement to Britain and her Allies, and which must have surprised and dismayed an enemy who had openly proclaimed that the Overseas Dominions of the British Empire were negligible from a military standpoint, was reached at a meeting of the Cabinet held at Sir Robert Borden's house. Up to that time 120,000 men had been sent overseas. An equal number were being trained and equipped in Canada. To more than double this establishment was a most formidable undertaking for a country which less than a year and a half before had considered 50,000 men the maximum force which it would be able to raise. After full deliberation, however, the decision was taken and announced. On the whole, it was favourably received by the Canadian people, although much doubt was expressed in many quarters as to Canada's ability to contribute, or to raise the money for, so large a force. Here I should like to say what I thought frequently during the early years of the war, namely, that the Government of Canada, in the matter of raising men and in its attitude as to the extent of Canada's participation in the struggle, stood always decidedly in advance of public sentiment throughout the Dominion. It is true that, in certain parts of Canada, and particularly in cities, there was criticism that the Government was not sufficiently energetic in pushing recruiting. But having regard to the whole country and its various sections and classes, the Government, in its action respecting the war and Canada's contribution towards it, was always the leader and not the follower of public opinion. If praise should be accorded to the Prime Minister for seeing clearly the nature of the issue and for determination to place the full power and resources of Canada at the service of the cause of the

Empire and of civilization, then decidedly Sir Robert Borden merits that praise. When the decision was reached increasing enlistment to five hundred thousand men, not one of us had any clear view as to how so many additional men could be raised or where the necessary money would come from. We simply went on faith, feeling instinctively that what we decided upon was right and that means would be found to enable us to carry it out. In other words, we believed in the cause for which Canada was fighting and in the patriotism and capability of the Canadian people.

In March, 1916, a loan of seventy-five million dollars was raised in New York. There were three maturities of five, ten and fifteen years, each for \$25,000,000. With regard to the first two maturities, the issue price was right. With regard to the last, it was too low, as was shown by that part of the issue being over-subscribed many times and going, immediately after allotment, to a premium of four or five points. This mistake was caused by a sudden change in market sentiment in favour of long-date as opposed to short-date investments. New York is particularly subject to such reversals of sentiment. In all our issues there it was a nice question to determine whether a long or short maturity would best suit the market at the time of issue. As it turned out, the quotation for the fifteen-year securities to which I have referred went afterwards much lower than the issue price, so we had no ground for serious complaint. Although satisfied that I had acted upon the best advice as to the right price for this issue, the failure to hit more closely upon it worried me considerably at the time. One undoubtedly good result of the over-subscription and of the securities going to a premium was to maintain the high credit of Canada in the New York market. This is an aspect of public finance which must never be overlooked. Getting the last fraction of value for an issue, or a little more than its value, while it may seem a matter of congratulation at the time, usually

brings its penalty at the time of the next issue when the public recall that the previous one went to a discount after flotation.

During this period, on account of the rapidly-mounting war expenditure, I received many suggestions as to means of raising revenue. They were for the most part quite impracticable. Towards the end of the war I had become quite accustomed to letters and telegrams intimating that for a substantial consideration the writer would place before me a plan for wiping out the national debt and raising without difficulty the further moneys required for the war expenditure. Not to be mentioned in this class was a very worthy citizen of Canada, a business man well known and respected in his community, who travelled at his own expense three hundred miles to lay before me a scheme of taxation which he said "would completely restore the finances of the Dominion." The plan was not feasible, but not wishing to offend one who was so sincere and well-meaning I asked him how much it would raise in the way of revenue. "It will," he said, "completely restore your finances. It will raise three-quarters of a million dollars a year." He was surprised beyond measure when I informed him that we paid out more than that sum every morning in the Finance Department. My experience with the public has been that most of them do not appreciate the magnitude of sums beyond a million. That is the reason why expenditures of tens of millions of dollars are looked upon so frequently with complacency by the taxpayer. So large an amount of money seems to be beyond the average comprehension and to be indistinguishable from a considerably less or greater amount.

The feature of the Budget of February, 1916, was the Business Profits War Tax Act, which provided for the taking off a percentage of profits of companies, firms and persons carrying on business in Canada. During the year and a half preceding this Budget many concerns had made large

profits in business. This was due in the case of some to the rise which had taken place in the price of commodities which they had on hand or which they had bought early in the war. Grain was a case in point. The milling companies and other dealers in grain had made large profits on their purchases of grain of the crop of 1914.

It must be borne in mind that all through the war business men stood to lose if it had suddenly come to an end. But, lasting as it did, they had for many years the benefits of a rising market, and their profits became in many instances abnormal and such as to invite public criticism. The Business Profits War Tax Act was made retroactive so as to apply to profits made from the beginning of the war. When first imposed it provided for taxation to the amount of one-fourth of all profits in excess of 7 per cent. upon the actual capital of corporations and in excess of 10 per cent. upon the capital of persons and partnerships. It applied only to those who had a capital of \$50,000 and over, except manufacturers of munitions, who were taxed under it no matter what their capital. The reason for this was that we desired the small business concerns to keep themselves strong so as to be able to meet the inevitable depression which must follow the war. The Act did not apply to agriculture or stock-raising. Thus only large industries and business concerns were made subject to it. It was to cover a three-year period, at the end of which we expected the war would be over. My estimate was that it would yield thirty million dollars. In 1917 the taxation under it was greatly increased in severity so that it became one of the most drastic measures of taxation adopted during the war by any nation. Its period of duration was extended from time to time by legislation and it has to date realized over one hundred and fifty million dollars. It is not improbable that when its final returns are made a sum in excess of two hundred million dollars will have been realized from this tax.

[During the war and since there has been considerable

criticism to the effect that the Business Profits Tax was not sufficiently heavy. In my view this criticism is not sound and fails to take into consideration many vital aspects of the subject. A Business Profits Tax is justifiable during a prolonged war, because money is urgently needed and it is a ready method of obtaining it in large amounts. There is also a justification in the fact that public opinion is offended at the sight of abnormal profits in a period of great suffering and privation. On principle, however, the tax is not sound and tends to produce much economic evil in the State. It is really a tax upon business success, and consequently tends to discourage enterprise and administrative efficiency. It also leads to waste and extravagance in business, because many business concerns strive to keep down their showing of net profits and to this end will enormously increase the advertising of their products and make unwarranted plant extensions. They take the view that it is better to do this with surplus profits than pay them over to the Government. There is no doubt in my mind that the taxation of business profits in England, United States and Canada has had much to do with increased prices of commodities. Taxation always tends to transfer itself to the consuming public, no matter what its immediate incidence may be. Another and perhaps the gravest objection to this tax, is that it depletes the liquid resources or working capital of business and in consequence leads to inevitable bank credit inflation. The annual profits of the average business firm or company are not usually represented by cash on hand. They are represented principally in plant extensions made during the year and stocks of goods on hand. The tax, however, is payable in cash, and most firms have to borrow from their bankers in order to pay. If, as has happened during the past year, there occurs a severe decline in prices and a slowing down of business, these concerns find themselves saddled with such heavy losses on the goods they are carrying as to wipe out the profits they had made previously

and upon which they have paid and are still called upon to pay taxation. The result is not only great hardship and injustice to themselves at the time, but a severe and permanent handicap to their business for the future. It is not difficult to see the national disadvantage of such a tax continued beyond the abnormal war period.)

A word as to manufacturers of munitions, many of whom made large profits during the war. It was with the greatest difficulty that manufacturers were, during the early period of the war, induced to go into this business, which afterwards reached such gigantic proportions and became of such vital consequence to the prosperity of the Dominion. The reason was uncertainty as to the duration of the war and the large amount of capital expenditure for expensive machinery required before manufacture could be begun. A manufacturer had to consider the loss he would sustain if, after purchasing many thousands (in some cases hundreds of thousands) of dollars' worth of machinery the war should come to an end before he had earned enough from his contracts to pay for it. Generally speaking, it was quite worthless for purposes other than the making of munitions. This was the reason why the price paid for munitions was so high. It had to be sufficient to ensure profits and amortization of capital for machinery and special plant. With less favourable prices or with existing legislation providing for the taking away of all profits beyond a normal interest yield upon capital invested, Canadian industrial enterprise would not have taken to munition making or achieved the notable results it did in this line. I remember another feature which greatly impressed me at the time. A manufacturer would obtain a contract for munitions and make a substantial profit. Another manufacturer would obtain at the same time an identical contract and lose as much as the former made. The difference lay in the superior resources or organizing and administrative ability of the successful manufacturer. It was by no means the fact that all engaged in munition

manufacture made large sums of money. Many, undoubtedly did, but many others were only moderately successful in a business way. Many lost money and some were ruined. It is never safe to generalize with regard to industrial or commercial success.

CHAPTER VI

**Gold and Securities—Britain's Huge Purchasing in America—
The First Flow of Gold—Mobilizing Britain's Securities—A
Wondrous Stream of Gold—The Handling of the Gold—
Where the Money Went.**

THIS is an opportune place to deal with the subject of gold movements through the Finance Department during the war. They constituted by far the largest transactions of the kind in the history of the world. They began shortly after the outbreak of the war, the movement then being from the United States to Britain, and reached their culmination during 1916 and 1917 when Great Britain was drawing upon all available gold resources in Europe, Africa and Asia for the purpose of meeting her colossal commitments for munitions, foodstuffs, and other supplies purchased in the United States. In all, more than twelve hundred million dollars of gold was dealt with. It is impossible for the public to adequately realize the magnitude of this sum, but some idea of it may be obtained by reflecting that it would provide one hundred and fifty dollars in gold in the hands of every man, woman and child in Canada at the time it was with us. It represented in weight over two thousand tons. It filled the vaults in the Department of Finance. The interior of the large vault, stored as it was with hundreds of bags of glittering gold coin and with tiers of bars of solid gold reaching to the ceiling on all sides, was the most dazzling vision of wealth ever spread before the eyes of man. Croesus never dreamt of such a treasure. I believe that the gross amount of gold represented in our vaults at Ottawa during the war

was almost twice the total amount of all the gold held by all British financial institutions, including the Bank of England, in the year immediately preceding the war.

In this chapter I propose to explain how this gold came to be stored temporarily at Ottawa, how it was handled there, and what ultimately became of it. To understand why it came to us it is necessary to know something of the gigantic financial effort which was made by Great Britain on this side of the Atlantic before the entry of the United States into the war on the side of the Allies.

Immediately the war broke out Great Britain and her European Allies began to buy munitions, steel, explosives, and other war material together with wheat, flour, meats and food supplies generally in the United States and, to a limited extent at that time, in Canada. The volume of these purchases can only be described as prodigious, and with high and rising prices owing to the demand, the sums of money required to meet the obligations incurred were very large and indeed staggering in the total. Payment could not be made in pounds sterling or in francs. It had to be made, as to the United States, in American money. In order to provide the funds which she required for these gigantic commercial operations, Great Britain first purchased all American exchange available. Without going into technical details, this means that she first called in all balances owing by United States manufacturers, merchants, bankers, and others to British interests and persons. The effect of this was to cause a scramble on the part of Americans to obtain sterling exchange with which to pay their debts in Britain. In consequence, the pound sterling, shortly after the outbreak of the war, became worth seven dollars in American money. As the demand for sterling exchange could not be satisfied without driving its price to a prohibitive point, the Bank of England agreed, for the convenience of American debtors, to accept gold deposited in the Finance Department, Ottawa, as the equivalent of gold deposited with the Bank of England

in London. This was a great concession to American interests and was eagerly availed of.

During the late summer and fall of 1914 two hundred and eighty-eight consignments of gold were received from merchants and others in the United States and Canada having bills and accounts maturing in Great Britain, which they were thus enabled to pay in gold instead of by purchasing exchange at a heavy premium. The first of these consignments was received on August 12, 1914, from Messrs. Kidder, Peabody & Company, Boston. The last was received on December 16. The gold embraced in these consignments consisted of United States gold coin, sovereigns, Japanese yen, and fine gold bars. Consignments were received from Boston, New York, San Francisco, Philadelphia, and several other points in United States. A shipment of \$505,000 was received from the Secretary of the Treasury of the United States for credit of the Secretary of the United States Treasury, London, and \$800,000 from the United States Post Office for credit of the British Post Office. A few consignments were also received from Canadian banks in Toronto and Ottawa. The gold received from United States at this period was contained in oak casks or in wooden boxes containing \$50,000 each. The Japanese coin, which came direct from Japan through Japanese branch banks in San Francisco, was packed in tin boxes, hermetically sealed, placed inside wooden boxes.

Early in 1915, on account of the enormous purchases in America, to which I have referred, the rate of exchange turned and the gold which had been received during the preceding autumn was forwarded to New York for account of the Imperial Government and the Bank of England.

During the first period of the war, Great Britain, in addition to calling in her foreign credit balances, compelled her people to surrender to the Imperial Government all securities amounting to billions of dollars, which they held, representing investments made for generations past

of British savings in American railroad, industrial, State, and municipal securities. The British Government gathered these up from the British public giving them in exchange British Government Bonds. The American investments were thus made available for sale or as collateral to loans issued in New York. Of these securities an amount variously estimated at from three to five billions were sold on the New York Stock Exchange and through American financial houses. The remainder were pledged as collateral to the successive loans, aggregating many hundreds of millions of dollars, which Great Britain floated during the year 1916 and early in 1917 in New York. It must be pointed out that, after the Anglo-French loan of 1915, Great Britain was not able to float any loans in the United States upon her credit solely. Each loan had to be secured by collateral known and acceptable to American investors, and the amount of collateral had to be a substantial percentage in excess of the amount of money borrowed. The American investor would not part with his money except upon absolute security. France was able to raise comparatively little money in the United States and the other Allies practically none, as Continental European credit had disappeared early in the struggle, and Italy did not enter until the war had been in progress for many months. The brunt of finding money for the Allies' purchases in America, therefore, fell upon Great Britain alone and unassisted. The extent to which she pledged her credit at this time, and the magnitude of the obligations to which she committed herself, illustrates her unconquerable fortitude of character as clearly as her gigantic efforts on sea and land. After the United States entered the war in the spring of 1917, the American Government became the banker of and loaned immense sums to the Allies for the purpose of their purchases in the United States. The result of all these operations had been the piling up of an immense indebtedness by Great Britain to the United States, which may take generations to pay, but which

will be paid to the last cent of interest and principal. It may be of interest to Canadians to know that Great Britain now owes the Treasury of the United States more than twice the amount of the entire national debt of Canada to-day.

At the time that Great Britain was commandeering the American investments of the British public she was requisitioning gold in all parts of the world for the same purpose, namely, making payments for the purchases of herself and her allies in United States. This gold came principally from Great Britain, South Africa and Russia, although small consignments were received from Brazil and Borneo. It consisted of a miscellaneous assortment of British sovereigns, American, Russian, German, Austrian, Japanese and French coin, together with fine gold bars. It came packed in boxes of \$10,000 and \$50,000. Of the total of \$1,200,000,000 of gold handled by the Department of Finance from the beginning, \$546,000,000 was for account of the Bank of England and \$658,000,000 for account of the Imperial Government. From United States \$104,000,000 was received on the first movement; on the reverse movement \$491,000,000 came to hand from Great Britain, \$353,000,000 from South Africa, \$253,000,000 from Russia, \$692,000 from Borneo, and \$172,000 from Brazil. More than three-quarters of the entire amount was represented by bullion. It will be of interest to learn that \$253,000,000 was received from the Imperial Russian Government. This gold was shipped from Petrograd and Moscow to Vladivostok, thence to Vancouver or Esquimalt via Japan in Japanese warships. These ships were met at the port of discharge by a representative of the Finance Department, who received the gold and transferred it to the Dominion Express Company for transportation to Ottawa. In all, four consignments of this gold were received, over the period from February, 1916, to May, 1917. The gold was contained in more than six thousand boxes, the largest consignment being that of February,

1917, amounting to \$97,000,000, undoubtedly the largest shipment of gold ever made. This principal shipment was transported to Esquimalt by three Japanese warships. It required twelve express cars to transfer it to Ottawa. Fourteen thousand bars of bullion were contained in this shipment. It had to be weighed to the one-thousandth part of an ounce, and fourteen thousand individual calculations had to be made to determine the number of fine ounces in this huge consignment. Three representatives of the Imperial Russian Government accompanied each shipment. They remained in Ottawa and witnessed the opening of the boxes and the weighing of the gold. It is satisfactory to be able to relate that the Department's method of control during the opening of the boxes and the weighing of the gold, as well as the extreme care in weighing, was eminently satisfactory to them. When the first consignments were received from New York and other points in United States, representatives of the shippers accompanied the gold. They found that the system of the Finance Department as to handling and weighing was so satisfactory that they advised their firms that it was not necessary that future shipments should be personally accompanied. Thereafter, treasure was shipped to the Department direct and the Department's statement of weight was accepted without question. The gold which came from Britain and South Africa was brought to Halifax by British cruisers.

I feel I should say a word as to the handling of this gold at Ottawa and the laborious and painstaking service, extending over many months, tendered in connection with the work by the officials of the Department of Finance. Part of the gold received was what is known as raw gold. It had to be transferred to the Mint at Ottawa for refining. So great was the demand upon the Mint in this regard that a new refinery had to be erected. It was built in eight weeks and had a refining capacity of one million ounces of fine gold per month. It will be a cause of pride to

Canadians to know that the Mint at Ottawa during the war refined gold on a larger scale than any other Mint or gold refinery in the world. After the raw gold was refined at the Mint it was returned to the Department of Finance, and before it could be placed to the credit of the Bank of England or the Imperial Treasury accounts it was necessary to check and weigh each bar. With respect to gold coin, each bag had to be emptied and the contents weighed to the one-hundredth part of an ounce. Each bar of gold had to be weighed to the one-thousandth part of an ounce. In the weighing in and out of nearly forty million ounces of gold the difference in weight between the weighing in and out was a very small fraction over one ounce, which testifies to the extreme accuracy of the work performed by the officials of the Department. It is impossible to convey an adequate idea of the excessive and wearying character of the work of handling this vast treasure. Only a small portion of gold either in the form of coin or bullion can be weighed at once, and extreme care, with double personal check, was required in emptying and refilling the bags and receiving and storing the bullion. At the same time all possible haste was necessary. The speed with which the work was performed may be illustrated by the following: At half-past four on Saturday, November 11, 1914, the Department received thirteen million dollars in gold coin from New York. This gold was contained in twenty-six hundred bags, all of which had to be emptied and weighed and a tabulation made of each bag, amounting in the total to more than six hundred thousand standard ounces. Notwithstanding the tremendous amount of work involved, at one o'clock on Monday morning cables were fyled stating officially the total number of ounces in each consignment, and the American shippers received credit in London on Monday morning.

As illustrating the work involved in receiving the shipments, it may be mentioned that in all fifty-five trips were

made to Halifax and four to the Pacific Coast to meet vessels bringing the consignments.

The transactions in gold which I have been describing were carried out by a few members of the staff of the Department of Finance, without outside assistance, with the exception of two labourers occasionally engaged. It was performed without cost to the Imperial Government, with the exception of a few hundred dollars for labour and cartage. The members of the staff immediately engaged in the operation were required to work day and night, Sunday and Saturday, for months at a time.

I feel I should not be doing justice to my predecessor in office, Hon. Mr. Fielding, if I did not say that it would hardly have been possible to have carried out transactions of such magnitude save for the fact that during his régime as Minister of Finance he established vault accommodation of the most modern and commodious character in the Eastern Departmental Block, immediately adjoining the executive offices of the Department of Finance. These vaults had the time-lock system and were guarded day and night by the Dominion Police. It was during Mr. Fielding's period of office also that the Royal Mint was established at Ottawa.

A humorous incident connected with the holding of the gold in the vaults at Ottawa comes to my mind. A member of Parliament had brought in a constituent from the back country to show him the treasure. After he had feasted his eyes upon it for some time, he exclaimed to the member: "Heavens, what a hold-out the Minister of Finance must have on all this money!"

It will be asked where did all this vast treasure go? It went to the United States in payment for the purposes I have mentioned. It helped to purchase the foodstuffs, ammunition and other supplies needed by the Allies during the war. It constituted an impressive part of that tide of wealth which from the beginning of the war flowed in ever-increasing stream into the coffers of the Great Republic.

The money made by the people of that nation during the war is beyond calculation. Their bank deposits alone increased by ten billions. The Allies owe them ten billions more. In addition, they subscribed their own war loans. They brought back from Great Britain and the Continent five billions of their own securities. From the standpoint of money, they almost hold the world in fee.

CHAPTER VII

Imperial Loans—Invitation to Visit England—Collateral for British Loans—Visit to England, 1916—Problem of American Finance.

IN my last chapter I described the prodigious effort of Great Britain in mobilizing her immense resources in foreign credits, American securities held by her own people, and gold drawn from all parts of the globe to meet her commitments for war material and food supplies purchased on this side of the Atlantic. Towards the middle of 1916 the burden of this financing became exceedingly heavy. The Titan was beginning to bow beneath the load. Expenditure in the United States had become a monster into whose insatiate maw flowed an ever-increasing stream of gold from the Treasury of Britain. In Canada also British commitments for munitions were running at the rate of twenty-five millions a month, of which we were furnishing by way of credits about fifteen millions. In addition to these mighty obligations, Britain was maintaining the value of sterling exchange by buying it in the New York market. This was done because a break-down in the value of the pound sterling would have been seriously detrimental to the Imperial credit and would have had the effect of raising the price of food and other necessities in the United Kingdom. At the close of 1916 it was estimated that Britain was expending money in New York at the rate of a billion dollars a year to sustain sterling exchange. I never could get our shippers to understand

why they were not permitted by the British and French authorities to sell certain of their products to private buyers in Britain and France who were willing to pay cash upon delivery. They failed to realize that bills drawn upon such buyers and sold in New York were to a large extent purchased by Britain who had to find money for the purpose, in support of exchange, and that if such support had been withdrawn the pound sterling and the franc would both have gone so low that commercial transactions with Europe would have been almost impossible. This exchange question lay at the very root of control by Britain of her imports during the war. As she was obliged to support exchange, it was sound policy that only necessities should be permitted to be imported and that the amount of even these should be under restriction. The Government at Ottawa was constantly urged to obtain in Britain or France a free market for Canadian products at a time when Britain was staggering under the burden of supporting sterling exchange, whereby alone the sale of these products could be financed. There is no question so difficult to explain as that of exchange and its effects upon trade, and I can only hope that those who during the war were prevented from selling their produce freely abroad will by this time have appreciated that there was the best of reasons why the regulations forbade them.

On July 28th, 1916, I received a cable despatch from Right Honourable Bonar Law, Colonial Secretary, stating that "it would be of the greatest assistance to His Majesty's Government" if I "could arrange to come to London at the earliest possible date to give an opportunity of discussing the question of Canadian and American purchases personally" with me. The despatch expressed appreciation of the financial help already given by Canada and stated that arrangements for future finance would be greatly facilitated "by such a survey of the whole question as a visit would alone render possible." It was not possible for me to go overseas at that time as I was fully engaged at Ottawa

with business of an urgent character, and I was also preparing for the issue of the second domestic war loan early in the Autumn. On August 12th I received a further cable, stating that it was considered most important that I should come over and "give the benefit of my advice with regard to the whole situation at the earliest possible moment."

I may here explain that at this time Britain was using every endeavour to obtain collateral satisfactory to American investors for her New York issues by which she was then principally financing her United States requirements. It was at this stage that we settled our balance of indebtedness to Great Britain by issuing to her Canadian Government securities to an amount exceeding one hundred million dollars to be used as the principal collateral to a large loan then being made in New York. In the eyes of American investors the Canadian securities were regarded most favourably and this transaction was a real service to Britain at a critical time. A cable was received expressing the warm appreciation of the Chancellor of the Exchequer. We provided that the Treasury should hold the bonds after the loan was repaid so that the market for our securities might not be injuriously affected by their sale. As a matter of fact, these securities were returned to us under a later arrangement and have now, I believe, been cancelled. In September, 1916, our domestic war loan was successfully floated and I received from the Colonial Secretary a cable of congratulations, which expressed the hope that now the loan was out of the way, I would go to London. It also contained the following sentence: "There are several questions on which personal conference between us would be of the greatest assistance to the British Government." A further cable from Sir George Perley, stating the desire of the Chancellor that I should go to London for the purpose of discussing the whole financial situation seemed to make it undesirable that I should further delay, and, after consultation with the Prime Minister and my colleagues,

I decided to go. I had been reluctant because of the situation in Canada, the amount of pressing work I had on hand, and the loss of time which would result. On the other hand, I felt that I should not disregard the repeated urgent requests made at so critical a time by the Imperial Government.

This is not the place to narrate incidents of my trip to England, except in so far as they relate to the matter of Canadian and British finance on this side of the Atlantic. I may mention, however, that I went over on the "Mauretania" with two thousand Canadian troops and that during my stay abroad I was privileged to visit the Front and the British Fleet at its base in the Orkney Islands. My principal business was with the Chancellor of the Exchequer, Right Hon. Reginald McKenna, and the officers of the Treasury. It would not be proper for me to go into details as to our discussions, but I may say that at numerous conferences we considered fully the extent of the commitments of the Imperial Government in the United States and in Canada and the programme of expenditure which they had in view, and canvassed exhaustively the possibilities of providing by the issue of loans or otherwise the immense amount of money required for these purposes. I found Right Hon. Mr. McKenna not only a man of most delightful personal qualities, but also a financier of high ability and indomitable courage. I think it was this latter quality which impressed me most. His plucky optimism and buoyancy of spirit in the midst of responsibilities and duties, which might well have been described as crushing in character, were most inspiring to all coming in contact with him.

I had discussions also with Right Hon. Bonar Law, who in a few weeks' time became Chancellor of the Exchequer in succession to Mr. McKenna. Being himself a Canadian, he has always had a deep interest in the welfare of the Dominion, and is a statesman of great sagacity and unusual practical ability. I met also Mr. Asquith, then Prime

Minister, and most of the members of the Cabinet. Without exception they were wholeheartedly appreciative of Canada's achievements in the war and filled with pride at the valour of our men in the field. To assist Canada's industry, trade and finance by placing orders for war material and foodstuffs of all kinds with us, they were most willing and anxious to do what lay in their power. The great battles of the Somme which had raged all summer and autumn had consumed ammunition on an undreamt-of scale, and the cry from the Front was ever for more shells. The vast industrial resources of Canada—our great steel plants and other manufacturing establishments—were almost unknown to Britain before the war. Our achievements in all fields were surprising to the outside world and our industrial achievement not less so than the others. That Canada was rich in coal, iron-ore (Belle Isle), copper, nickel, and timber was a revelation to many men of affairs in Great Britain who, one would think, should have known all about it. That we had many huge industrial plants and hundreds of smaller ones of high efficiency, capable of turning out explosives, shells and other war munitions, ships and airplanes on such a scale of production as we actually accomplished came as a complete surprise to British officialdom. The extraordinary resources and capabilities of Canada in this regard were being placed most forcefully before the British authorities by Sir Joseph Flavelle, chairman of the Imperial Munitions Board for Canada, who was in London for the purpose at this time. As a result of his representations and our undertaking to provide twenty-five million dollars monthly as a Canadian credit to the Imperial Government, Sir Joseph returned with orders for Canada for munitions to the amount of over forty million dollars per month. He obtained permission also to let contracts in Canada to the amount of ten million dollars for ships, for which we lent the money to the Imperial Government, and for a twenty-five million dollar airplane programme

which we started by advancing one million dollars for the purchase of a plant. Among other prominent Canadians also there was Lord Shaughnessy, probably the best known and most influential Canadian in London official and business circles. Needless to say, he, too, was doing his best in the interests of Canadian trade and industry and also in the way of assisting British finance. To this period belongs the episode of the Canadian Pacific Railway Company, through Lord Shaughnessy, offering to issue in substitution for its sterling debenture-stock outstanding in Britain and requisitioned by the British Government, bonds payable as to principal and interest in Canada and the United States which could be used as collateral for further Imperial loans to be floated in United States. From first to last, throughout the entire war period, the Canadian Pacific Railway Company aided to the limit of its great financial power the British Government, and the Canadian Government in finding money for the vast purchases made by the former in the Dominion.

There was no question as to the need to Great Britain of continuing to purchase in America to the utmost extent. The German submarine campaign was developing with frightful rapidity and effectiveness. Daily, the papers contained reports of sinkings of merchant vessels. Daily, Britain and her allies were being bled white by the tremendous drain upon their resources. The policy was to strain every nerve and bring to bear every power to bring to an end the war which threatened to destroy the world by exhaustion before a final decision could be obtained. Britain needed for herself and her allies American and Canadian iron, steel, copper, nickel, timber, shipping, rolling stock, wheat, flour, meats and all manner of other supplies necessary at the Front or required to feed the civilian population at home. The continent of America had these supplies in unlimited quantity. The seas were kept open by the British fleet. The sole problem was that of obtaining the money on this side of the Atlantic. The

credit of France, Italy and Russia had long since been exhausted. On Great Britain alone fell this titanic burden. During the previous part of 1916 Britain had been raising money in the United States for her heavy commitments there by issuing successive loans fully secured by collateral acceptable to American investors. The market would not take loans upon her credit only. The time was approaching when collateral in sufficient amount would be no longer available and when, if Britain could make no other arrangements for money, she would be obliged to greatly restrict or discontinue her purchases in the United States. There, of course, was another side to the question. If Britain could not purchase from United States, United States could not sell to Britain. The consequence of discontinuance to American industry would be appalling and was fully realized by America's business men. The question was: Would the American people, after Britain's collateral had become exhausted, subscribe Britain's loans offered in United States to anything like the immense sums required for the year 1917? My belief was that, if the American people became fully aware of the dependence of their export trade upon their subscribing loans to Britain upon her unsupported credit, a considerable amount of money would have been forthcoming for the purpose. But having regard to the mixed opinions upon the war prevailing in United States at this time, the unfamiliarity of American investors with foreign securities, and the uncertainty as to the outcome of the conflict, it was not probable that Britain could obtain in this way more than a fraction of the aggregate (running into billions of dollars) which she required. One suggestion which had been put forward in New York was that British short-date bills, for say five hundred million dollars, could be issued and kept afloat in that market. My view as to this was that such bills should not be floated to an amount materially beyond the ability of Britain to meet at maturity from gold or funds available for the purpose. The New York market

is peculiarly subject to panic and there is no certainty that money required to meet maturing bills can be raised by fresh issues. It is a most dangerous market in which to have afloat large liabilities in the form of short-date securities.

All the matters I have here touched upon were discussed fully with the Treasury authorities, with the Governor of the Bank of England, and with Lord Reading, whose extraordinary financial knowledge and diplomatic ability were to prove so useful to Britain at a later stage, when he became Ambassador at Washington. Mr. J. P. Morgan, of New York, whose firm was the fiscal agent of the British Government for the United States, was in London at this time discussing with the Treasury this all-important subject of American finance. The upshot of the conference was to proceed with the issue of American loans, but to watch the situation carefully with a view to curtailing commitments should the prospects for money become unfavourable. Subsequent events justified my apprehensions as to further American loans. Only one British loan was floated in New York after the close of 1916. It became clear that United States investors could not be depended upon to supply Great Britain, upon her credit solely, with the money required for her purchases in America. What would have happened had conditions continued as they were I do not attempt to conjecture. In April of 1917, the United States entered the war as an associate of the Allies, and the American Treasury became their bankers. The people of the United States would eagerly subscribe their own Liberty Loan issues, whose proceeds to the amount of twenty-five billion dollars were used for the purpose of the war expenditure of the United States and for making loans to the Allies to enable them to continue purchasing in America. If the entry of the United States into the war provided the Allies with money on this side of the Atlantic, it also saved the export business of the United States, which otherwise must have experienced collapse.

An incident occurred at the close of my London visit, of which I should like to tell. Mr. McKenna, Chancellor of the Exchequer, gave a farewell dinner in our honour. Among others were present Lord Shaughnessy, Mr. J. P. Morgan, Sir Joseph Flavelle, Lord Cunliffe, Governor of the Bank of England; Lord Reading and myself. At the close I asked Mr. McKenna playfully if he had provided for an escort of destroyers for the "Finland" which was an American vessel, upon which we were to sail the next evening. He replied in the negative, and someone pointed out that American ships were sensitive about British escorts, as German feeling was growing more bitter against the United States, and an escort might make for danger rather than protection. I remarked to Mr. McKenna that if a German submarine captain should sink a ship having on board Lord Shaughnessy and Mr. J. P. Morgan, to say nothing of the rest of the passengers, he would probably get at least half a dozen iron crosses for so meritorious a performance. Nothing further was said about the matter at the time. We embarked the next evening at Liverpool, and during the night sailed down St. George's Channel. In the morning, when we went out on deck, the first sight to greet our eyes was two British destroyers one on either bow of the "Finland," shepherding the American liner through the submarine-infested waters off the southern coast of Ireland.

CHAPTER VIII

**Taxation—Dominion Income Taxation—Taxation of Luxuries—
Financial Effort of United States—British Finance in Canada.**

THE year 1917 was probably the most trying period of the war. It was a time of deep anxiety and uncertainty as to the outcome. While it marked the entry of United States on the side of the Allies, it was also the year of Russia's revolution and subsequent collapse. The German submarine campaign was at the height of its power

and destructiveness. It was directed at enemy and neutral shipping alike in the desperate endeavour to starve Britain into submission and bring the war to an immediate end. In order to conserve food and make the most compact kinds available for shipment overseas, control was established in Canada and the nation placed upon rations. It was during this year that the stress of the conflict and the strength of public opinion in favour of "equality of sacrifice" brought about conscription. The loss of Canadian lives at the Front had been heavy and there was widespread and poignant grief throughout the Dominion. The strain, horror, and suffering of the war had produced a strong religious feeling among the Canadian people. Patriotic women were working heroically day and night in connection with the Red Cross and kindred associations. For the first time the Canadian people were upon a war basis, instinct with the spirit of sacrifice and self-denial which must be evoked before the full power of a democracy can be brought to bear. In the realm of finance, with which I am dealing, the sentiment of the public was reflected in a desire for heavier taxation. This was partly caused by the failure of some well-to-do people to contribute as generously as they should have to the patriotic and other war funds. At one time during the year there was an agitation for what was called the "conscription of wealth." This was taken by some to mean the confiscation of deposits in our chartered banks, and in consequence of the publicity given to the expression there were "runs" in certain parts of Canada. So serious did the matter become that I was obliged to make a statement in the House of Commons that so far from intending to confiscate deposits, the Government's policy was to promote and foster national savings. In fiscal legislation, the prevailing sentiment of the public was given expression in two important measures. By the first, the Business Profits War Tax was made much more drastic. Prior to this time it had taken one-quarter of all net profits in excess of

seven per cent. upon the capital of corporations, and ten per cent. upon that of individuals and partnerships. The new taxation took one-quarter of such excess profits up to fifteen per cent., one-half between fifteen and twenty per cent., and three-quarters of all beyond twenty per cent. I have already written of the revenue derived from this tax and of the objections against continuance beyond the period of war conditions.

The Income War Tax Act, which was passed by Parliament in 1917, had been drafted the year before. I had hesitated long before introducing it, because, among other reasons which were given at the time, we did not desire direct taxation to be heavier in Canada than in the United States. This is a maxim which, on account of Canada being a country inviting immigration and business enterprise, I think should be observed as nearly as may be. The scale of income taxation which prevailed in the United States before her entry into the war would, if applied to Canada, have given us a comparatively small aggregate return. The Dominion with its great geographical area and sparse population, was most difficult to organize for the collection of taxation upon individual incomes. Moreover, we have in some of our provinces income taxation by municipalities and provincial governments. The imposition in addition of a federal tax makes three in all, with an exceedingly heavy aggregate. My view was that the income tax should, if possible, be left to provinces for their own purposes and those of municipal governments. The rapidly mounting expenditures of the war and the necessities for revenue made it at last imperative that the Dominion Government should resort to this form of taxation. Shortly after the entry of the United States into the war, Congress adopted a heavily increased income tax, and ours, since its first imposition, has been kept on almost precisely the same basis. The present Commissioner of Taxation pointed out to me when the legislation was under consideration, that it would undoubtedly take three

or four years to complete the organization for its administration and make it efficient. In Great Britain, income tax legislation has been under administration for seventy years and their methods of collection have been continuously improving. It was not until many years after the establishment of federal income taxation in the United States that its administration became even fairly effectual. I give one instance of the difficulties with which our Federal Taxation Department has to contend. An inspector of an important district in the northern part of Western Canada told me, when I censured him for his slowness in making returns, that the people in his community spoke more than fifteen different languages and that only by a personal visit in each case could he get any information whatever as to their incomes. With every desire to pay his proper income taxation, the average farmer who keeps no accounts and whose farm provides food for his family, would find it most difficult to make out an accurate return. I shall not enlarge further upon the well-known difficulties of administering a system of income taxation, except to say that the burden falls with most certainty upon those having fixed salaries, information as to which is furnished by their employers. Without a strict investigation, which is not practicable in every case, it is impossible to be assured that income returns are even reasonably accurate. That there always will be evasion on a large scale is inevitable.

It has been asked why we did not resort to a greater extent to the taxation of luxuries during the war. The principal reason was that nearly all articles of luxury were covered by fixed rates of customs duties in our treaty with France. The tariff could not, therefore, be raised in respect of these without our first cancelling the treaty. This we did not feel we should do during the war period, as France needed the advantage of her sales on this side of the Atlantic in order to assist her in paying for purchases made in Canada and the United States. To have adopted

a heavier duty against her importations would have been an ungenerous act towards our great Ally. This view was shared by the British Government, with whom we discussed the question.

At the stage of the war of which I am now writing, the demand upon the Dominion Treasury for money was becoming exceedingly heavy. We had to provide not only for our rapidly mounting war expenditure in Canada but also the ever-increasing credits required by Great Britain for her purchases of Canadian munitions and other supplies. For this last purpose we were lending her twenty-five million dollars a month, and, in addition, the sum of ten million dollars for a shipbuilding programme which she was carrying out in Canadian yards. We floated our third domestic war loan in March of 1917, and in the summer placed an issue of one hundred million dollars of two-year notes in New York. This last-named issue was the least successful of the public flotations made by the Government during the war. We had to arrange to have a part of it specially subscribed and it immediately fell to a discount after allotment. The reason for its non-success was that the United States had declared war in April, and American investors were conserving their resources for the purposes of their own national finances. Hon. Mr. McAdoo, Secretary of the Treasury, whose permission I had to obtain before making the issue, was well-disposed towards Canada and desirous of doing what he could to facilitate our financing. This friendly attitude I found among all members of the administration at Washington during my visits there.

The task of Hon. Mr. McAdoo was a heavy one. The United States had to put forth a mighty effort very suddenly. Not having been in the war from the beginning, she had not, so to speak, "got under way" gradually, as in the case of the other Allies. Moreover, she had at once to provide loans of vast amount to Britain and the other Allies to enable them to take care of their American com-

mitments. All this meant that the American Treasury had to quickly organize a campaign to raise an immense sum of money. In the circumstances, it was only natural that Americans should desire to conserve their money for these purposes. These facts must be kept in mind when considering the attitude of the United States during 1917 and 1918 towards the expenditure by Great Britain in Canada of funds borrowed from the American Treasury. Up to this period the money which Britain had borrowed from the American public by flotations of loans had been available, in part, for the purpose of making payment for munitions and food supplies purchased in Canada. When the American Treasury began to make advances to Great Britain, money to pay for expenditures by Britain in Canada was not available to the same extent as it had been before. As, however, a great deal of American raw material was being purchased by Canadians for the manufacture of munitions, an arrangement was come to whereby Great Britain was allowed to expend out of the money borrowed from the United States Treasury from ten to fifteen million dollars per month in payment for munitions manufactured here. Funds were also provided with which to purchase part of our exportable surplus of wheat which was required by the Allies. Our banks loaned the Imperial Government the balance needed for this purpose. We pointed out, of course, as strongly as we could, Canada's huge adverse trade balance with the United States as a reason why the latter should not object to an equal expenditure in Canada by the British Government of funds borrowed at Washington. Looking backward at all these transactions, I think it only fair to say that in my view the Secretary of the Treasury and his colleagues at Washington adopted as generous a policy towards purchases by Britain in Canada from monies borrowed from the American Government as we could have reasonably expected in view of all the conditions at the time.

About the mid-summer of 1917, the pressure upon Great

Britain for funds to meet her Canadian purchases became exceedingly heavy. In June, I had made an arrangement with the banks for three monthly advances of twenty-five million dollars each, which with other funds available I expected would carry us over until we could float a further domestic loan in the autumn. In July, however, we received the most urgent despatches from the British Government, pointing out that it would not be possible for them to continue purchasing our cheese, hay, oats, and flour unless Canada could provide the credits. For the purchase of our cheese alone, forty million dollars was required. Twenty millions more than we had counted upon for July and August was needed for munitions. This sudden intimation completely upset our financial plans and made it imperative for us to not only provide at once a very large sum of money but also to organize a loan campaign on a national scale, with the object of raising at least three hundred million dollars to carry us until the spring. We found part of the money immediately required by issuing fifty million dollars in Dominion notes secured by approved collateral lodged by the British Treasury to our credit with the Bank of Montreal in London. Later, we called together the leaders in the investment world of Canada and discussed with them the making of a nationwide appeal through the medium of an organization which would cover every section of Canada. This was the origin of the first Victory Loan which, with its successors and the national purpose which they accomplished, I shall discuss in the next chapter.

CHAPTER IX

Victory Loans—Purpose of the Victory Loans—Victory Loans Organization—Savings Greatly Increased—Banks' Resources Free for Trade.

THE three Victory Loans were the greatest financial achievement of Canada during the war. They were floated in 1917, 1918 and 1919 respectively and raised

an aggregate of more than seventeen hundred million dollars. That this astounding sum, which was almost twice the amount of all the deposits in all the chartered banks before the war, should have been made available for the purposes of the Government from the savings of the people of Canada was probably as surprising to ourselves as to the outside world. Suggestions have not been wanting that Canada could have raised as large sums through public issues made to her own people before the war, but that we never suspected our ability to do it, and consequently always did our national borrowing in London and New York. This view overlooks the fact that our war loans were really subscribed by the public from the savings made during the war itself. There is real truth in the statement which was made frequently by economists that nations pay for wars as they go along. Productive enterprise is of necessity greatly stimulated. This, coupled with the constantly increasing rise in wages and in the prices of commodities, produces an enormous amount of credit, or money so-called, which finds its way into the pockets and the savings accounts of the public. This money is available for subscriptions to Government loans. On the other side of the national account is the vastly increased public debt representing the money expended for the equipment of the nation's military forces, the food consumed by them during the course of the war, and the immense amount of ammunition used in the field. The burden of the debt created is passed on to future generations as a legacy and reminder of the waste of war.

The outstanding features of our Victory Loan campaigns are well known to the Canadian people, who, without exception as to class or party, gave them the devoted and patriotic support, lacking which no such measure of success could have been achieved. Some of the factors which entered into that success may be specially noted. The first Victory Loan organization was created in the autumn of 1917. We had an unprecedented, and

even staggering, financial situation to deal with. There were hundreds of munition factories in Canada actively engaged in the production of shells urgently needed at the Front. These plants, with auxiliaries providing them with raw and partly finished material, had under employment more than two hundred thousand men and women. The British Government was buying the munitions produced at a cost of from forty to fifty million dollars per month. That Government required also our wheat, flour, meats, butter, cheese, salmon and other food products, together with the ships which they were building in Canadian yards, and the airplanes under construction for them in Canadian factories. Their finance in Canada had in a sense broken down because they were not allowed to use in Canada, beyond a closely restricted amount, monies which they were borrowing from the American Treasury. This condition prevailed from mid-summer of 1917 until the end of the war. Unless during that time the Canadian Government had been able to provide the British Government with about five hundred million dollars a year in Canada, by way of loan, the latter would have been obliged to greatly curtail their programme of expenditure in the Dominion for the purposes mentioned. About the time of the first Victory Loan they had under consideration a far-reaching cancellation of munition orders, which would have had the effect of closing down the greater part of our munition factories with consequent loss of the output for use in the field and to the Canadian people of the amount of business involved. They would also have been obliged to discontinue in large part the purchase of our agricultural products. For example, in June, 1917, they ceased buying for a time Canadian cheese, and would not have been able to resume had not the Government of Canada undertaken to furnish the forty million dollars necessary for the purpose. The situation could not be met by loans such as we had hitherto been issuing through public offering in the press and through financial houses. Nothing short

of a nation-wide movement in which appeal would be made to all members of the community to save their money and subscribe to a national loan, would at all meet the condition with which we were confronted. The business of Canada literally depended upon her ability to finance the greater part of our external trade. If we could finance it, the national gain would be sufficient to pay for the expenses of our army overseas and leave a large surplus beside. The people of Canada met the situation by their subscriptions to the three Victory Loans. These loans were the foundation of the enormous volume of business done by Canada during the last three years of the war. They kept the Dominion Treasury in funds for the purpose of our war expenditure in Canada, and provision of credits for Great Britain's purchases here. They enabled us to conclude the war with practically no floating debt and with the Government of Great Britain owing Canada four hundred million dollars, half to our Government and half to our banks, over and above the vast sums which we had borrowed from Great Britain to pay for our expenditures in the maintenance of our army abroad. While the credits which we furnished to Great Britain were used for the purchase of particular products such as munitions, ships, airplanes, and foodstuffs, the money was distributed among all classes of the community in the form of wages, rents, purchases of commodities, and in other ways. In a word, the entire Canadian public derived the business benefit of this expenditure. If Canada had not had the benefit of this business and had sent overseas an army which she did, we should have finished the war with an indebtedness to the British Government of a billion dollars or more. In view of this, it is not too much to say that we should not have been able to make such an effort. The business which Canada obtained through the financing afforded by the Victory Loans enabled us to pay our war expenditure abroad as we went along and finish with a large balance to our credit.

One of the most difficult features of the Victory Loans was the creation of the organization by which they were carried out. That organization was formed in 1917 and perfected during the next two years. It was, I believe, one of the most efficient in operation anywhere in the world. It combined professional and lay ability. Those engaged in the securities business in Canada understood thoroughly the most modern methods of marketing bonds. Associated with them was a body of most earnest men and women in every part of Canada patriotically devoting their thought and energy to the service of these loans. The publicity campaign was organized most efficiently by the Canadian Press which probably more than any other single factor, except the patriotism of the people, had to do with the success of these great flotations. The work of the chartered banks in receiving and handling subscriptions was invaluable. The co-operation of all fraternal and other societies, loan, trust and life insurance companies, the schools and churches of Canada, was actively enlisted, and with all these agencies at work the impetus of a Victory Loan movement, once it got under way, was irresistible. I had a great deal of heavy work at the outset in getting the organization extended over the whole Dominion and in smoothing out difficulties which continually arose. I am happy to say that no question of politics ever entered into these campaigns. I do not recall hearing a single complaint as to discrimination on this ground. Most assuredly, the Government had the wholehearted support of the entire community in its war finance.

Apart from the other business considerations which I have mentioned, these loans undoubtedly greatly stimulated saving on the part of the Canadian people. If we had not had them I am positive that the great mass of the Canadian people would not have been nearly so well off as they are to-day. They would have spent a great deal more money upon themselves that they did. At the end of the war tens of thousands of the Canadian public had

Victory Bonds which have stood them in good stead since. Hundreds of thousands of others have these bonds as permanent investments, from which they derive a regular income. They have acquired also the habit of saving and investment, which, like any other habit, grows by cultivation. From the national standpoint, it is of the utmost advantage that so large a proportion of our war debt is held by the Canadian people themselves. I hesitate to think of what our position would be if we had borrowed, and were still owing, externally, even half the amount of our war debt. We should be kept in economic servitude through adverse exchange for a generation to come.

Another important aspect of our Victory Loans is the fact that our national debt, great as it is, was funded during the war. Maturities were fixed at various dates extending to 1937. This gives ample opportunity for the country to recuperate from the effects of the war before the first heavy maturity has to be met. It should not be difficult to refund the principal as it becomes payable. This should be done well in advance and on an attractive basis, so as to ensure conversion of their existing holdings by those who may wish to continue investment in Dominion securities.

The proceeds of the second Victory Loan, which was floated about the time of the armistice in 1918, gave the Government funds with which to meet the trying period following upon the war. They were thus enabled to provide, among other things, a gratuity of more than one hundred and thirty million dollars to Canada's returned soldiers for their maintenance during the unsettled conditions which then ensued. It also enabled us to continue shipbuilding and provide credits for the purchase of Canadian products, all of which was of the highest consequence to Canadian industry at that critical time. The third Victory Loan, which was floated by my successor in office, Sir Henry Drayton, enabled him to finish the reconstruction programme and announce the policy of no further public borrowing.

The fact that the Victory Loans were subscribed by the Canadian people and that our banks were not called upon, as they were in the United States and in England, to take part of them or extend to the Government large floating credits, has been of the utmost importance to Canada during the past two years. It has meant that our banking resources have been available for the purposes of agriculture, commerce, and industry. In the United States, the banks were compelled, in order to make the Liberty Loan successful, to subscribe billions of dollars for the purpose. In England, the British Government, whose effort was of course much greater even relatively than our own, have a floating debt of about seven billion dollars, which has been a most serious burden upon their credit facilities.

The policy which we adopted as to the terms of our War and Victory Loans was to be absolutely fair with the Canadian public. Market conditions were under close study and issues were made conformably with these conditions. We believed that if we asked the Canadian people to save they should be given full value for their money. As a result, practically all have been satisfied in this important regard. At the end of the war all our Victory Loans stood above their issue price. This was accomplished partly by the operations of the Victory Loan Stabilization Committee which we created, and which enlisted the co-operation of all the investment dealers and stock brokers of Canada. To maintain the market they purchased, from funds furnished by the Government, all offerings of bonds at fixed prices. Through their organization, which covered the whole of the Dominion, they carried on a campaign for their re-sale at a higher price, which was also fixed. This gave a much wider distribution to the bonds than could have been accomplished during the brief duration of the Victory Loan campaigns and got them into the hands of those most likely to hold them as investments. The best tribute to the work done by this committee and to the financial strength of the Canadian people is the

present quotations of this immense body of securities upon the Canadian market, which, before the war, would have been staggered by a five-million dollar loan. The securities of no other Government in the world stand so close to-day to issue price as those of Canada.

It can be said with confidence that Canada found herself financially, as in many other ways, during the war. I have mentioned no names in connection with these Victory Loans, because it would be invidious to do so. The Government throughout had the loyal and devoted service of thousands of patriotic Canadians whose co-operative effort thoroughly covered the whole Canadian field. The patriotism of the people did the rest. The campaigns were not without their pathetic side. Bonds were unknown to the greater part of the Canadian public when these campaigns began. Some worthy women believed that in subscribing to a Victory Loan they were giving their money gratis to the Government as a patriotic contribution towards the expenditure of the war. I had touching letters from some of these good souls. They had saved a few hundred or a few thousand dollars and had finally reached the conclusion that it was their duty to respond to the appeal of the Government and give the money, which practically represented their all. I had some difficulty in convincing them that they were purchasing an obligation of the Government which would give them an income and was worth the purchase price. I remember the case of a woman who subscribed for and received a one-thousand dollar Victory Bond with coupons attached. She did not know it had any value but looked upon it as an official receipt for her contribution of one thousand dollars to the Government for war purposes. She had it framed and hung up in her parlour and was surprised beyond measure when she found out it was one thousand dollars and would yield her fifty-five dollars a year in interest. Another case which came to my attention was that of a man who wrote the Department asking for a cheque for interest due

upon his bond. He said that he understood it could not be paid until the appropriate coupon was destroyed and that he had destroyed it by burning in his stove.

CHAPTER X

Personal Observations—Negotiations at Washington—Money for Canada's Wheat—The Peace Conference Period—Final Solution of the Problem.

IN this, my last chapter on Canada's war finance, I trust I may be allowed a personal word. The work and strain of the year 1917 had impaired my health. In addition to the duties and responsibility of official day-to-day administration we had a session of Parliament lasting from the middle of January to the end of September. As a dissolution was in prospect it was a fighting session from the beginning. As Minister of Finance I had necessarily a heavy part in the legislation which came before the House, particularly the Budget, the Income War Tax Act, and that connected with the taking over of the Canadian Northern Railway System. It was the year of the Military Service Act, of the formation of Union Government, and of the last general election. These are all inviting subjects of comment, but I am here dealing with finance and not with politics. Immediately succeeding the organization and successful flotation of the first Victory Loan the election came on and, after that, steps had to be taken to enable the marketing of some sixty million dollars of provincial and municipal issues, which had been held up pending the issue of the first Victory Loan. Provision had also to be made to stabilize the price of its bonds. We had at an earlier date taken control of the Canadian investment market and forbidden, except by consent of the Finance Department, any provincial, municipal or other offering of securities. This having been done, and having been ordered by my physician to take a six months' rest, I tendered Sir Robert Borden my resignation as Minister

of Finance, as I did not think it proper that the holder of this vitally important office should, at so critical a period in the war, be absent so long from his post. Sir Robert, however, declined at the time to accept my resignation and appointed as Acting Minister Hon. A. K. Maclean, who, when in Opposition, had been the principal critic of the financial administration of the Conservative Government, and who carried on most capably during my absence. The main features of his Budget, which received warm commendation, were the application of the Business Profits War Tax, with slight modification, to business firms and companies having a capital between twenty-five thousand dollars and fifty thousand dollars, below which latter figure it had not previously applied; a substantial increase in income taxation; and the imposition of customs and excise duties upon a considerable range of articles of luxurious use or consumption.

After I had been absent in California for four months, the Prime Minister requested me to go to Washington to take up some urgent matters relating to Canadian exchange with the United States and credits for the purchase by Great Britain of Canada's wheat and other products. I was at Washington at other times during the year 1918 upon this mission and was in more or less constant touch with Lord Reading, the special British Ambassador there, and Sir Hardman Lever, who most ably represented the British Treasury in its American finance. I doubt if Britain could have found more capable men than these for the delicate, responsible and immensely important work which they had to perform. Canada, I feel, owes them special thanks for their active efforts to support her trade and assist her finance at this most trying time. Our exchange was aided greatly by the large orders obtained for Canada from the American Government for munitions and war supplies by the Canadian War Mission, with Mr. Lloyd Harris at its head, and through the influence and exertions of Sir Joseph Flavelle, chairman of the Imperial

Munitions Board in Canada. Sir Charles Gordon, of Montreal, head of the British Purchasing Mission to the United States, who had his headquarters at Washington, was also of much service to Canada in this connection. Altogether, Canada had a most capable representation of wide-awake business men at Washington during the closing year of the war. With regard to our exchange, which was two or three per cent. unfavourable to Canada, I soon discovered that the United States was so engrossed with her own financial problems that the question of her commercial exports to Canada had become of entirely subordinate importance. Her own exchange was at one time at a thirty per cent. discount with Spain. Our people were in reality unreasonably disturbed over the trifling discount on the Canadian dollar. We helped to maintain its value by keeping a large New York cash balance, from which we sold a million or so of exchange from time to time as the market required steadying. The exchange market is always a narrow one and peculiarly sensitive to unexpected offerings. We accomplished something also by prohibiting the importation of a considerable range of non-essential commodities.

The big problem for the British and ourselves was to obtain money for the purchase of Canada's wheat crop of 1918. The loans made by the American Government to Britain were restricted in their use to purchases made in United States. On the other hand, our wheat and flour were a necessity to the Allies in carrying on the war. The question of provision of two hundred and fifty million dollars from American funds for this purpose was the subject of frequent discussion with the American Treasury by Lord Reading and ourselves. Personally, I preferred that Britain should do the borrowing from the United States, but we were prepared to borrow if the money had been available. There was a technical difficulty also in the fact that Canada was not a complete sovereignty, and so not strictly within the terms of the American legislation

authorizing loans to foreign nations. Whether if the war had gone on Lord Reading would have obtained money from this source for the purchase of our wheat crop, I do not know. It had not been obtained by November when the armistice came. Fortunately, thrown upon our own resources, the great Victory Loan of that time gave us nearly seven hundred million dollars, which enabled us to supply Britain with Canadian money for the purchase of Canada's wheat. It also enabled us to provide against industrial collapse in the winter of 1919, when munition factories had dismissed their employees and our soldiers were returning home. For months the chief theme of discussion in Canada was as to what would happen industrially when the war ended. Almost everyone was obsessed with the idea that we should have a terrible situation on our hands with unemployment and discontent. Thanks largely to the second Victory Loan and the measures taken by the Government in distributing one hundred and thirty million dollars as gratuity to the soldiers, in making available credits for the purchase of Canadian products by Britain and other European countries, in carrying on shipbuilding, in giving large orders for rolling stock and making extensions to the national railway system, the transition period from war to peace was bridged with no serious trouble in the industrial world and no sign of business or financial panic. Of all the nations engaged in the war from the beginning, Canada, I truly believe, emerged in the best economic condition. Even with the United States, which was a belligerent for less than two years, we do not suffer in comparison.

Upon my return to Ottawa in May of 1918, I engaged with the Prime Minister that I would continue as Minister of Finance, if my health would at all permit, until the close of the war. Immediately after the armistice at the urgent and repeated request of Rt. Hon. Lloyd George, the British Prime Minister, Sir Robert Borden went overseas to attend the deliberations of the Peace Conference. It was expected

that he would not be absent more than three months. How the discussions at Paris continued until the following summer is known to all. Upon leaving for the Conference, he did me the great honour of appointing me Acting Prime Minister during his absence. I served in this capacity as well as that of Minister of Finance from November, 1918, to June, 1919, when Sir Robert returned and resumed his duties as Prime Minister. On August 1st, 1919, I resigned my portfolio and was succeeded by Sir Henry Drayton, the present capable Minister of Finance. I feel it a great honour and privilege to have had the opportunity of serving the Canadian people in the important post with which I was entrusted during the war, and desire to return to them all, without exception, my warmest thanks for the generous patriotic support which they gave Canada's war finance, without which the best efforts of the Government would have been in vain.
