

A BRIEF HISTORY OF THE AUSTRALIAN NOTES ISSUE BOARD, 1920–24

William Coleman

In 1920 Australia transferred control of the note issue from the Treasury to a newly created authority, the Notes Issue Board. This paper recounts the background to the Board's establishment, the powers and responsibilities with which it was endowed, the policies it pursued, and the difficulties it experienced that led to its abolition in 1924.¹ This history records an attempt to vest discretionary control of the monetary base in an independent body that was neither a central bank nor a currency board.

The Origins and Constitution of the Notes Issue Board

The Notes Issue Board became a legal entity on December 14, 1920, and was a delayed response to the creation of the Australian Notes Issue in 1910. The Australian Notes Act and the Bank Notes Tax Act—both passed in 1910—eliminated private bank notes in Australia that had largely satisfied the demand for notes. Under those acts, the issuance and control of the new Australian Note Issue was to be vested in the Treasurer. The two principal constraints on this power of issue was that the new government notes were to be convertible into gold and the Treasury was required to keep a gold reserve no smaller than a third of the note issue. Another constraint was that the note issue not exceed £7 million in total—a limit that was repealed in 1911 (Polden, 1977: 146).

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William Coleman is a Professor of Economics at the University of Tasmania. He thanks Gary Swain for research assistance and Selwyn Cornish, Mac Boot, Erol Middleman, and an anonymous referee for helpful comments on earlier drafts of the paper.

¹Polden (1977) and Cornish (1988) are excellent unpublished narratives of the life of the Board. More summary treatments of the Board may be found in Giblin (1951: 10–15), Butlin (1961), Blainey (1983), and Schedvin (1992).

By the eve of the First World War the new Australian notes had effectively displaced the old private bank notes. The First World War effectively ended the convertibility of these Australian notes into gold. The War also saw the rapid expansion of the note issue, from £6,346 million in August 1914 to £59,057 million by November 1918.

In the process of postwar reconstruction, following November 1918, there were two pressures to remove control of the note issue from the Treasury. The first was the sentiment that an inconvertible currency was a dangerous power for political authority to possess. That conviction was inherited from the canons of sound finance of the preceding century. But it was also doubtless reinforced by the massive expansion of the note issue that Australia experienced during the First World War. Joseph Cook, the Treasurer in 1920, favored the removal of the note issue from Treasury on these grounds (Polden 1977: 222). However, Cook also had a less public-spirited motive in proposing an independent note issue: he believed that the management of the note issue inevitably led to controversy and unpopularity, and the government would be better off unburdened of this unenviable responsibility (Polden 1977: 214).

The second pressure might be called “Central Bank Creationism.” This was the widespread sentiment that part of the development of Australia would consist of the creation of an Australian central bank with note issue power. It was, for example, the explicit intention of the original creators of the Australian Note Issue in 1910 that the Issue would reside with Treasury only until its transfer to a central bank could be secured (Polden 1977: 203). This aspiration to create a central bank with note issue power corresponded perfectly with the institutional empire building of the first governor of the Commonwealth Bank, Sir Denison Miller, who wished to augment what was then merely a government-owned savings and trading bank.

The outcome of these two impulses was the creation of the Notes Issue Board. In 1920 the Commonwealth Bank Act transferred control of the note issue from the Treasury to a new Notes Issue Department in the Commonwealth Bank. The act decreed that the new Notes Issue Department “shall be kept distinct from all other Departments of the Bank.” The act deemed that the Commonwealth Bank was to be regarded by the Board as no different from any other bank with respect to the issuance of notes.²

²There was therefore a resemblance between the structure of the Commonwealth Bank after the Act of 1920 and the structure of the Bank of England after the Act of 1844. Both banks conducted banking and note issue operations, and in both those operations were separated into distinct and supposedly autonomous divisions.

The Department would be managed by a Notes Issue Board composed of the Governor of the Commonwealth Bank, an officer of the Commonwealth Treasury, and two persons unconnected with the Bank or the Treasury. In the case of a tied vote, the Governor would have a casting vote. Thus, although notes were issued by a Department of the Commonwealth Bank, only one of the four persons who managed the Department was of the Commonwealth Bank (see Polden 1977: 206). This peculiar management structure was the result of a power struggle between the Treasury and the Commonwealth Bank. Prior to the Act of 1920 Miller had pressed for the complete transfer of control of the note issue to the Commonwealth Bank. In this he was resisted by the Treasury. The outcome was the hybrid management structure of the Board.³

The Board faced no real constraint on the issue of notes. Notes were allowed to be issued by the purchase of government securities and “trade bills.” The note issue of the Department was required not to exceed four times the Department’s gold assets, but that constraint was never binding.

There was in theory a constraint placed on the issue by Australia’s nominal adherence to the gold standard. All notes issued by the Notes Issue Department bore the promise of the Australian Treasury that they would be redeemable in gold coin at the Commonwealth Bank’s Head Office. However, the Australian note issue was not a genuine gold standard issue. First, in legal terms, the Board argued that the promise on the notes was made by the Treasury, not the Commonwealth Bank. So in the Board’s interpretation, the notes were essentially checks drawn by the Treasury on its account at the Commonwealth Bank, “made out to gold.” Hence, it was concluded that the Bank had “no obligation to presenters” (Reserve Bank of Australia [RBA] Archives, N-f-21-6).⁴ Second, and more substantively, the private banks had (at the request of the government) refused to redeem any notes in gold since the outbreak of World War I, and the Commonwealth Bank “discouraged” any redemption. Market participants understood that Australia’s supposed adherence to the gold standard was a fiction.⁵

³Miller originally wanted the Board to be only an advisory board. The Treasury successfully insisted that it be a managing board.

⁴The correspondence, papers, and minutes of the Board are held in the archives of the Reserve Bank of Australia, at its head office in Sydney. There seems to be little other direct primary evidence on the conduct of the Board. The annual reports of the Commonwealth Bank are not informative, and the archives of the Australian Treasury yielded little to this researcher. *Documents on Australian Monetary and Financial History, 1901–1951* (Reserve Bank of Australia 1993) provide some material on the abolition of the Board.

⁵“Scrutineer” of the Melbourne *Argus* expostulated thus: “The promise to pay sovereigns

The Powers of the Board

The Notes Issue Board did not have the extensive powers and instruments of a modern central bank. It had no discount window, no discount rate, and no supervisory or regulatory powers over banks' liabilities or assets. But it would be a misunderstanding to assume that the Board was only an example of the currency boards which were so common in the British colonies of the time. The currency boards of the Empire were created to ensure a strict parity between the local currency and pound sterling. By contrast, the Notes Issue Board happily allowed the Australian pound to float against the pound sterling. The currency boards were forbidden from issuing currency through the purchase of domestic securities. By contrast, there was no such restriction on the Notes Issue Board: a balance sheet shows that holdings of government securities amounted to about one-half of the Board's issue of notes.

The currency boards were essentially shop fronts for the Bank of England (Sayers 1952: 423–27). The Notes Issue Board, by contrast, had no connection, formal or informal, with the Bank of England. Indeed, it did not hold the policies of the Bank of England in high esteem. As will be seen, the determination of the Notes Issue Board to go its own way, regardless of sterling, was one of the reasons for its demise.

The Independence of the Board

In accordance with the goal of removing the note issue from politics, the Notes Issue Board was deemed independent of the government. Reinforcing that legal independence was the fact that the Board was composed of persons not inclined to take directions from the government. The Board was comprised of Sir Denison Miller (1860–1923), George Swinburne (1861–1928), Sir John Garvan (1873–1927), and James Richard Collins (1869–1934), the Secretary to the Commonwealth Treasury. All three of the non-Treasury members of the Board (Miller, Swinburne, and Garvan) were defensive of the Board's independence. Sir Denison Miller was the strong, ambitious founding Governor of the Commonwealth Bank of Australia, and wished to have the Treasury removed completely from the management of the note issue. George Swinburne was possessed by “a conviction from which he never swerved, the necessity of removing

on demand on the Australian note is an absolute falsehood. Sir Joseph Cook describes this as a 'reckless and mischievous' statement. It is a literal and absolute fact, perfectly well known to every Australian citizen, including Sr Joseph Cook.” (*Argus*, 8 August 1923: 9)

questions concerning finance and currency beyond the reach of political influence” (Cornish 1988: 23). In 1904, as Victorian Minister for Water Supply, he had “placed all State water-supplies under the control of a new statutory authority—publicly funded and in principle independent of political control” (Ritchie 1990: 151). Sir John Garvan was to prove his independence in repeated clashes with the government over monetary policy.

The Board’s Policy Goals and Strategies

The Commonwealth Bank Act did not impose any policy goals on the Board. The Board appears to have given itself two policy goals: the avoidance of inflation and the restoration of a genuine gold standard.⁶ The Board’s strategy to achieve these goals was determined by the quantity theory of money, which the Board adhered to in its most elementary form. Garvan, for example, once tersely telegraphed the Board regarding a proposed issue expansion: “All credit inflation dangerous particularly in peacetime; purchasing power of money automatically less” (RBA Archives, N-f-22-16, 20 October 1922).⁷ This adherence to the quantity theory of money, in conjunction with an implicit acceptance of purchasing power parity, implied a single strategy: control of the money supply. Controlling the money supply would control inflation and thereby facilitate the return to a genuine gold standard.

The Board’s commitment to controlling the supply of money had two concomitants. First, the supply of currency would not be elastic to demand, since such a policy implies “validating” inflationary shocks. There was a qualification here. The quantity theory allows that an autonomous increase in the demand for money, all other things being equal, would destabilize prices and thereby warrant an increase in the money supply. But a reliable indicator of such an increase in demand would be a downward pressure on prices in the absence of a change in the supply of money. Thus, as long as there was no downward pressure on prices in an environment of a stable money

⁶This wish to void inflation was undoubtedly heightened by the postwar European inflations. Between 1921 and 1922, in the early years of the Board’s existence, prices rose 1,022 percent in Germany and 2,544 percent in Austria (Mitchell 1992: 848). Garvan commented: “Germany is an object lesson for any banker who favours currency inflation” (Polden 1977: 242). H.T. Armitage, the Secretary to the Board, on his return from a tour of Europe voiced his opinion: “One cannot but be impressed with the tremendous potential for harm inherent in a note issue” (RBA Archives, N-N-3, 23 November 1922).

⁷Sir Henry Braddon (1863–1955) (who replaced Swinburne in 1922) was of the same view. His *Essays and Addresses, Historical, Economic, Social* included an account of the assignat episode of the French Revolution.

supply, there was no reason to suppose that the demand for money had genuinely increased, and no justification for an increase in the money supply. This position was clearly stated by the Board to the commercial banks (RBA Archives, N-N-1, letter from the Board to the Chairman of the Associated Banks).

Second, the Board's commitment to controlling the size of the note issue meant it had little commitment to the maintenance of the long-established parity of the Australian pound with the pound sterling. The Board felt such a policy meant that the Australian price level would be governed by monetary policy in Britain, and it appears to have had no particular confidence in British monetary policy. An historian of the Commonwealth Bank has analyzed the sentiment of the Board on this point in this way: "England was off the gold standard and there was no definite prospect of a return to it. To follow England in these unholy revels was to compromise 'the good Australian pound.' What should be done was to allow sterling to go to a greater discount" (Giblin 1951: 11).

And sterling did go at a discount. In December 1920, when the Notes Issue Board commenced operations, the rate of exchange was 101 pounds Australian to 100 pounds sterling. By the time of its demise in October 1924, it was 96 pounds and 10 shillings Australian per 100 pounds sterling.

Opposition to the Board

The Board's policy of controlling the note issue at the cost of parity with pound sterling provoked the opposition of primary producers and commercial banks.

Primary Producers

The upward pressure on the Australian pound provoked the resentment of primary producers. Primary exporters complained that sterling balances were accumulating to their credit in London but could not be converted into deposits in Australia owing to the excess demand for Australian pounds. Whether there were in fact these sterling balances has been questioned. Later researchers have had "substantial agreement that there was no piling up of London funds in 1924" (Giblin 1951: 8). It seems that the appreciation of the sterling value of the Australian pound was sufficient within a short period of time to eliminate any significant excess demand for Australian pounds.

But this appreciation of the Australian pound itself was unpopular. Since the prices of primary producers were generally fixed in pounds sterling, every appreciation of the Australian pound meant reduced

incomes in terms of Australian pounds. And although the appreciation was never more than 4 percent, it was virtually without precedent: not since 1853 had Australian pound notes risen so much against the pound sterling. And in the 1920s there was a lack of recognition of the existence of an Australian currency distinct from the British pound.⁸ As a consequence, exporters felt they were getting 4 percent less than they deserved, and that sentiment was not challenged. As a historian of the Commonwealth Bank wrote, “It was generally recognized as a legitimate grievance of the export producer that he should get only, say, 97 pounds for wool or wheat which sold for 100 pounds in London” (Giblin 1951: 7).⁹

The Banks

The Banks also opposed the policies of the Board. A recurrent complaint of the commercial banks throughout the period of the Notes Issue Board was that the Board was not allowing the supply of currency to be elastic with respect to its demand. The *Australasian and Insurance Banking Record* (1924: 271), for example, declared, “The plan followed by the Notes Issue Board has been virtually to impose a rigid limit upon the total amount of cash available for business.” But the Board was unsympathetic to those complaints. It told the banks that “a genuine shortage of currency would have been accompanied by a decrease in prices,” and there had not been such a decrease (RBA Archives, N-N-1, letter from the Board to the Chairman of the Associated Banks).

The Imperial Connection

One final source of antagonism to the Board might be found in the lack of concordance of its actions with the imperial attitudes of the prime minister, Stanley Melbourne Bruce (later Viscount Bruce of Melbourne). Clearly the Board’s interest in an independent monetary standard, its indifference to the parity between the Australian pound and sterling, and its gaze toward New York sat awkwardly with the imperial orientation of Bruce. At the Imperial Economic Conference in London, in October 1923, Bruce faulted freely floating exchange

⁸“Until the depression, the Australian pound and the English pound were generally regarded as identical” (Report of the Royal Commission on Banking 1937: 41).

⁹Using the exporters’ premise that “a pound is a pound,” one might have sought to console exporters with the observation that what sold for 97 (Australian) pounds in Australia sold for 100 (UK) pounds abroad. In selling abroad they were, therefore, receiving a “premium” over selling at home. But since primary producers markets were overwhelmingly export markets, and since their costs were in Australian pounds, I doubt they would have been consoled.

rates for putting at risk the economic links between England and Australia that he was seeking to nurture.

The End of the Board

By the end of 1923 the Board's actions had antagonized primary producers and commercial banks. These interests sought redress by appealing to the prime minister. Bruce was a sympathetic listener and urged the Board to increase the note issue.

Perhaps the Board could have survived these political and commercial pressures. It was unfortunate for the Board that at this time it no longer had the benefit of the leadership of Sir Marcus Miller, owing to his sudden death in June 1923. Miller's replacement as Board chairman, James Kell (1864–1933), appears to have made little impression on his contemporaries. None of the *Who's Who* of the period record his existence. The semiofficial history of the Commonwealth Bank barely mentions him (Giblin 1951). The absence of a strong and prominent Board chairman after mid-1923 meant that the Board's policies lacked a strong defender. It also meant that its policies were dominated by the inflexible quantity theory precepts of John Garvan, which implied a rejection of the prime minister's requests. The upshot was that the Commonwealth government, finding the Board impervious to its imprecations but without an effective defender, decided to abolish the Board. This would be done as part of the reform of the Commonwealth Bank, contained in the Commonwealth Bank Act of 1924.

The new act eliminated the Board. The note issue was now to be controlled by the newly created Board of the Commonwealth Bank. This new Board was to have eight members. The governor was to be one and the secretary to the Treasury another. The remainder were to consist of persons "actively involved in agriculture, industry and finance." Decisions concerning the note issue were to require the assent of six Board members if eight were present, and five Board members if fewer than eight were present. Reflecting the imperial themes of Bruce, a London Board of Advice was enacted, but no appointments were ever made. The Commonwealth Bank was also permitted to issue notes on the basis of funds deposited at the Bank's London Branch. The Notes Issue Board ceased to exist on October 10, 1924.

Conclusion

This paper has presented a brief history of the Australian Notes Issue Board. It has told how for four years Australia experimented

with vesting discretionary control of the monetary base in a body without the extensive array of instruments of a modern central bank, but with the power to issue notes by purchase of government securities. This history has shown that the results of this experiment disappointed sectional interests, the Board was subsequently abolished, and the control of the note issue was transferred to the Commonwealth Bank. The end of the Board marks the beginning of orthodox central banking institutions in Australia.

The end of the Board also marked the end of an experiment to apply simple quantity theory precepts in Australia, an experiment that has never since been reattempted. That attempt earned the Board the harsh judgments of later commentators. One critic writing in 1951, for example, faulted the Board for its “haunting” fear of inflation, its “facile” application of the purchasing power parity theory of exchange rates, and its “fine careless rapture” over the quantity theory of money, “which more mature experience has not wholly justified” (Giblin 1951: 12). The revival of the quantity theory since 1951 may lead commentators today to be not as harsh. In 1951 the Australian dollar was worth \$US1.12. By 1998 it was worth only \$US 0.55. This decline is in accord with simple quantity theory, since currency per unit of real GDP has grown much more slowly in the United States than in Australia. Consider an index of U.S. currency per U.S. real GDP expressed as a ratio to Australian currency per Australian real GDP. If the index is given a value 100 in 1950, then by early 1998 it stood at 50.5. It would seem, therefore, that “more mature experience” goes some way to vindicating the Board’s belief that a tight control of the Australian money supply was required to preserve the value of Australian currency.

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