

Conversions; Sterling Balances

The rising balances of the Dominions and India (as of other members of the Sterling Area) were a constant pre-occupation of H.M. Government; and means by which they were kept at levels more or less consonant with the requirements of these territories are described in adjacent chapters. In India, where sterling piled up rapidly, a large proportion of pre-war sterling debt was disposed of by means of vesting and repatriation of securities, but balances at the end of the war were still very high. South African accumulations were on a smaller scale; *nominaly* in the Sterling Area, South Africa tried to maintain gold standard practices, and though selling anything up to £80 million a year of her surplus gold for sterling she nevertheless financed large imports from the Western Hemisphere in gold. Two repatriations of sterling securities amounting to about £74 million South Africa likewise covered in gold. Late in the war she agreed to pay about £33 million towards her war expenditure.

In Australia and New Zealand things took a different course. There was no question of either Dominion contributing a substantial amount of gold to sterling area finances. New Zealand, whose sterling had suffered a rapid decline in the immediate pre-war years, was able, with the help of the British banking system led by the Bank of England, first to convert with success and later to pay off a substantial part of loans due. She only agreed, with some reluctance, to extend Reverse Lend-Lease in September 1943.

The first war-time Australian conversion operation began to be discussed, between the Governor, H.M. Treasury, the Australian High Commissioner in London (Lord Bruce*) and Lord Glendyne (Nivisons), in the autumn of 1940, about a year before ^a £13½ million Commonwealth Loan was due for repayment. Sinking Fund arrangements under the Act to consolidate the debts of the Commonwealth and States were complex, but there were optional repayments (at 3 months' notice) amounting in all to £45 million in 1941.

It was

* Rt. Hon. S. H. Bruce, created Visct. Bruce of Melbourne, 1947.

It was suggested that Australian repayments might be financed, so far as loans were not converted, by using the Commonwealth Bank as a reservoir much as the Local Loans Fund was intended to be used for similar repayments of the obligations of British Local Authorities, if they bore a rate of interest of 4% or over.

~~When the Commonwealth Bank is used as a reservoir for the purpose of financing the repayments of the obligations of British Local Authorities, it is necessary to provide for the possibility of a reduction in the rate of interest on the loans which are to be repaid.~~

An objection to this proposal was that in such a case Australia might be tempted to ^{expand sterling resources} ~~expand resources~~ on optional conversions in order to secure at an earlier date a slight reduction in annual interest charges. This would make it more difficult for H.M.Treasury to obtain repayment of Australian war costs*.

An early decision (March 1941) was, however, made that the money to repay non-converting holders would be provided out of Vote of Credit** in exchange for stock of the new issue(s). The Bank agreed to registration of the stock "in the names of the usual nominees of the Bank of England", though it would in fact be a Treasury holding.

An offer of renewal of £13½ million Commonwealth of Australia 3% Registered Stock 1939/41 was accordingly made on the 17th April 1941 - renewal was for 3 years, repayable on 1st October 1944, with optional redemption a year earlier on giving 3 months' notice.

On 21st May notice was also given that the Commonwealth Government's offer to convert a further £30 million would be exercised. The announcement was made by question and answer

*c.f. similar objections to full repayment by the New Zealand Government.

**This did not require special legislation.

in the House of Commons. The Chancellor's reply stated that ".... I am glad to be able to announce that an offer of conversion in respect of those stocks carrying a higher rate of interest than 4% will be made forthwith. In order to facilitate this operation without interference with the Government's borrowing operations, I have agreed to advance from the Vote of Credit to the Commonwealth of Australia such sums as may be necessary to repay any unconverted stock."

A note by Mr.Kershaw to the Governor (6th April 1942) begins "..... My broad view is that the Australian Government debt is far too large for safety, and that we should, therefore, welcome any opportunities (such as approaching maturity^{ies}) for its reduction to a more manageable level. But I fear that in present circumstances the question of purchases, whether in New York or London, is largely academic". He went on to point out the fall, rather than rise, in Australia's London funds: on 30th March the Commonwealth Bank held just over £40 million. Australia's sterling position would probably be more favourable in six or nine months' time, she would spend less on imports, and for some of her exports (wool, butter, meat) she would receive sterling whether they were shipped or not.

To the end of 1945 there were, including a small amount of Municipal debt, £35 million due for repayment, nearly half (£16½ million) on 1st January 1943. In addition options amounting to £108 million ~~were~~ could be repaid by December 1945 on giving three months' notice*.

Correspondence with the Treasury on what proved eventually to be the largest conversion operation ever undertaken by Australia began with a letter (Governor to Sir R.Hopkins 1.7.42). The Governor's final paragraph read "..... I have the idea that rather than pay for the Commonwealth Bonds at maturity it would be better, if necessary, to go through the form of renewing them with the Treasury

*Commonwealth and State Loans maturing in or before 1975 amounted to well over £400 million.

Treasury as underwriter. Although cash is likely to be claimed on practically all the maturing bonds, you, nevertheless, would receive a marketable security which we could try and sell later, and this £16½ million would therefore not be included in the money which you will eventually be forced to forgive and forget!" On the 3rd November ^{Lord} Bruce visited the Bank to discuss the £16½ million 2½% Stock maturing on 1st January 1946. The Governor advised him to issue a 3% Stock, maturing in ^{mid-}1946, at 98, which would yield £3:12:6 to redemption. Notice was issued on the 20th November 1942 to convert the £16½ million into Commonwealth of Australia 3% Registered Stock 1944/46.

^{Lord} Bruce's visit was followed by discussions between the Governor, Lord Glendyne and Mr. Lewis (London Manager of the Commonwealth Bank) early in January 1943, and again in March, on the prospects of selling the large blocks (£14½ million in all) of Australia 3½% 1961/66 and Australia 3% 1944/46 held by the Bank as security against loans to the Commonwealth Bank. Lord Glendyne was asked ~~by Mr. Lewis and Mr. Lewis~~ to impress on both the Commonwealth Bank and the Australian Government "the favourable treatment which the Dominion had received by having their conversion loans underwritten by the Treasury" "also to remind them of the very large maturities of Australian loans running at high rates of interest over the next few years and to suggest that they could not expect these to be underwritten in the same way unless they in turn would agree to the sale of such stocks as they might be left with as soon as possible, even if they showed a loss."

On the 30th September 1944 (reporting date) Australian sterling balances amounted to £145 mn. and opinion was already formed ^{was} on the possibility and desirability of paying off £87 mn. due on the 1st July 1945 in one operation, leaving £21 mn. to be dealt with in one further operation.

At the end

At the end of October Mr. Kershaw wrote "The procedure to be followed - apart from dates and size of operations - depends mainly on one basic factor.....i.e., the size of Australia's London funds at the time of negotiations, and the view they take as to the amount they can spare for possible redemptions....."

"In my view Australia would be ill advised to let her sterling fall below £100 mn. until the post-war contraction begins; and I should feel happier about her prospects if she kept to a minimum of £120 mn."

It seems to have taken a long time for the Australians (and their British advisers) to come to the conclusion that it would be possible to deal with all the 5% loans with options in 1945 in one operation. The Governor (Lord Catto) used a bolder tone in his note of 11th December 1944....."Why not take first things first and offer conversion of the £68 mn. into a ?% stock; say, possibly $3\frac{1}{2}\%$, depending upon the length of loan, to be underwritten by the Australian Government and paying £34 mn. or thereabouts or anything in excess of that by H.M.T. If this succeeded then plainly every redemption could be dealt with; indeed consideration might be given as to whether all the 5% loan^s on which there are options in 1945 should not be dealt with at the same time."

A tentative proposal for a large-scale operation from *Lord* Bruce (4th January 1945) seems to have revived doubts even in Lord Catto's mind....."I said he seem^{ed} to me to be suggesting a very complicated transaction and one that I very much doubted could be worked in the way he wanted. Any borrowing from H.M.T. would, of course, have to be shown and it would seem very curious that H.M.T. should be lending money to Australia when her sterling balances were at such a high peak as they are now and would be even if £30 mn. were deducted. Apparently this had not occurred to him: he thought the suggested borrowing would be arranged privately between H.M.T. and the Australian Government. I replied that however private it might be it would certainly have to be shown in the figures both here and in Australia."

On the

On the 10th January it was agreed that the Treasury would underwrite £60 mn. of the repayment of five issues maturing in July and August and amounting to £94.3 mn., the Australian Government to provide £34.3 mn. out of their sterling balances, leaving £14.1 mn. New South Wales 5% stock to be dealt with later. On the 1st February the Bank put forward a suggestion that this should be met by the issue of a short, which it was thought would be successful as there was a scarcity of short-term ^{bonds} on the London market at the time. The matter did not arise urgently until August and the Treasury were in any case averse from asking the Chancellor ^{to agree to} ~~to agree to~~ a loan. ~~to agree to~~

On the 24th August the terms of the ^{New South Wales} conversion were fixed. An issue of Australian 3% stock 1952/60 at 98% was made. £9,750,000 (nearly 70%) was converted. The Australian Government made no repayment and the Commonwealth Bank took up the unconverted balance with a view to selling at their discretion as and when market conditions allowed.

On the 4th March ^{Lord} Bruce wrote to confirm that Australia would repay £34.3 mn. out of their sterling balances and that "any part of the £60 mn. not converted will be taken up by the Commonwealth Bank with a view to reselling. Should the amount not converted exceed £15 mn. it is understood between us that such amount will be financed by the Bank of England, if it is desired, in the same way as unconverted stocks have been handled in previous operations."

Notice of conversion of the five stocks^x was issued on 27th March. Nearly £57 mn. out of the possible £60 mn. was converted.

^x £68,419,293 Commonwealth of Australia 5% Regd. Stock 1945/75
 £7,217,819 South Australia 5% Regd. Stock 1945/75
 £11,717,984 Victoria 5% Inscribed Stock 1945/75

(of which Stocks notice of redemption had already been given)

£599,000 Tasmania 5% Regd. Stock 1945/75
 £6,357,771 Western Australia 5% Inscribed Stock 1945/75

The Bank, two Clearing Banks and two of the Australian banks*, assisted in carrying out the necessary work, a task far beyond the Commonwealth Bank's staff's capacity. The Bank of England's charge for their assistance, based on their own out of pocket expenses, was £7,500.

*Westminster, Glyn Mills, Bank of Australasia and Commercial Bank of Australia.

U.K. Sterling Liabilities to Australia

(comprising deposits, advances, bills, and if held for banking offices in Australia, British Government securities)

£ millions

	Total	Commonwealth Bank Holdings	Other Official Holdings and Funds with Commercial Banks (net)
At 31st December 1941	52.6	46.4	6.2
" 31st March 1942	45	37.3	8
" 30th June "	50	47.5	2.5
" 30th September "	60	58.3	2
" 31st December "	66.6	62.4	4.2
" 31st March 1943	60	56.7	3
" 30th June "	60	57.6	2
" 30th September "	65	64.3	1
" 31st December "	83.9	78.3	5.6
" 31st March 1944	105	95.4	10
" 30th June "	140	125.0	15
" 30th September "	145	138.9	6
" 31st December "	146.5	141.2	5.3
" 31st March 1945	147.5	146.4	1
" 30th June "	145	141.8	3
" 30th September "	120	113.2	7
" 31st December "	134.3	125.2	9.1
" 31st March 1946	145	131.1	14
" 30th June "	150	138.6	11
" 30th September "	160	150.0	10
" 31st December "	160.3	153.2	7.1

Note End-year figures have been revised but those for end-quarters are estimates obtained by an approximate correction of the unrevised figures.

Statistics Office,
15th May 1950.
R.H.J./565.