The Problem of War Debts and Bankruptcy

Montgomery Bell, Esq., Writing in the Journal of the American Bankers' Association for July, Says No Nation Will Be in Bankruptcy After the War—Capital Taxation Will Solve the Domestic Situation.

At the outbreak of the war in 1914, not only laymen but trained financial and economic experts believed and asserted with what was then considered sufficient reason, that the financial burdens consequent upon a war of the present magnitude would make the continuance of the conflict impossible even for a year. With the passing of time the war continued, and more nations joined in the fray; each month the expenditure on both sides has been increasing at an alarming ratio; the only explanation that the self-same experts were able to offer has been that the nations would be unable to avoid eventual bankruptcy.

At first this argument was used by the pacifists in support of immediate peace. Later, however, the fight-to-the-finishers took it up to show that the side that is defeated will be bankrupt. At present, the experts steer a middle course; they assert that bankruptcy is unavoidable for the enemy; but our position, while not serious, would only be relatively better—at the conclusion of peace. Nevertheless, the bogey of bankruptcy plays a very large part in shaping the course of our political and economic conduct—at least for the present.

Bankruptcy, as it is known in law and commerce, arises out of the inability of an individual or corporation to meet his or their obligations, in whole or in part, at the stipulated date and in accordance with the contracts entered into. The gravamen of bankruptcy is that the obligation must be due to a party other than the party which is a debtor. Further, the enforcement of the contract and the declaration of insolvency must be made by a properly constituted legal authority. Now the warring nations—at least, the chief belligerents—are debtors to their own people—except for comparatively small amounts due to other countries. How can a nation become bankrupt for owing money to itself? Even if they should, one and all, repudiate their indebtedness, there will surely be hardships for individuals, but the financial condition of the nation will remain unaltered. Capital, property and all other forms of wealth will remain intact; there will be only changes in the titles of ownership of individuals.

Next, how can the state enforce a contract against itself? In practice, one department of the state acts as a check on the other; in the United States, for instance, the judiciary or the Supreme Court decides upon the constitutionality of the legislative acts of the Congress, and the latter acts as a check on the executive, or the President and the Cabinet. If the governments of the different nations should find no means of paying their obligations, the governments may be forced to quit, but the nation or the state will be as sound as ever. This, however, does not apply to foreign obligations, non-payment of which destroys the credit of nations. Even in this respect, the only remedies are military expedition and refusal to do business in the future. If the state is a powerful state, the former alternative is out of the question—as, for instance, in the case of Russia, in the past. As for refusing to do business with a defaulting state, competition for the world's markets among powerful nations has practically nullified any such relief for the creditors—except in cases where they acted in concert, as, for instance, in China, up to 1913.

There are three categories of the belligerents financially affected by the war. The first is the nation that has borrowed only of its people and has had no credit from any other nations. The only examples of it are the United States and Japan. Most of the belligerants belong to the second category, i.e., those that have borrowed mostly of their own people, but have obtained not inconsiderable amounts from outside. Great Britain, Russia, France, Italy, Germany, Austria and Turkey belong to this class. The third category comprises nations that have borrowed from other countries in order to fight and carry on the government; Servia, Belgium, Montenegro, Bulgaria, Roumania and, to a certain extent, Greece and Brazil, belong to this class.

Without exception, all neutrals and some belligerant states have improved their financial positions as a result of the war—in spite of the fact that European neutrals are suffering from want of food products, as a result of the operations of the submarine, and have had to incur expenditures in order to be able to maintain neutrality. The South American neutrals have one and all profited by the high prices they have obtained for the produce they exported, while the volume of imports has been measurably reduced. Even some of the belligerant states, like Siam, China and India, have profited by the reduction in the volume of their imports.

There is a very general impression that after-war finance will prove a serious problem to every country in the world; there is nothing more erroneous than this belief. The great majority of the world's states would have benefited by the turn of events during the past four years. Almost every South American state, with the possible exception of Brazil, has reduced its debt to Europe, and has repurchased a considerable part of European holdings of its stocks and bonds. The latest example is the purchase made by Uruguay of its railway from British interests. Mexico has received higher prices for its silver, metals and petroleum, and is immensely better off financially than it has been during the past ten years. Of the Central American states, Nicaragua has been reaping large benefits, while others have done as well as they could under the circumstances. There is no country in Asia, independent or dependent, that has not benefited by the conflict—from the economic point of view. Japan has had the largest advantage. She has increased her annual trade from $600,000,000 before the war to $1,200,000,000 in 1917. She has reduced her debts in Europe; doubled her gold holdings and stands as a creditor not only to China and Russia, but also to England. China has had the supreme advantage of the rise of 100 per cent. in the value of silver, which is the national money; and, as with other countries, the war has prevented the market from being dumped with European goods. India has had similar advantages; in addition, there has been a very marked industrial revival. The colonial possessions of the different powers in Africa have had little to complain of; in any case, they have had no burden of debt to shoulder. The conclusion of peace will find the European neutrals no worse off than before the war; in any case, they have had returned to them during the first three years of the war all foreign holdings of their own stocks and bonds, and have invested in British, French, German and Russian war loans and treasury bills besides. Of the belligerants, Roumania will come out with practically no change in her economic position. Servia, Montenegro, Austria, Turkey, Greece and Italy were never noted for their sound financial position; they were borowers at all times. Russia is now in an anomalous situation, but it was ever thus; the country of the Czars has had numerous financial crises in the past. Hence, problems of the future resolve themselves into readjustment of conditions in Great Britain, Germany, France and the United States. Even in these countries, the problems would have been much simpler but for the fact that they have held economic sway over the world in the past—apart from political domination—and they are anxious to reassert such sway unimpaired.

A consideration of facts as recorded by history proves conclusively that nations at no time suffer the effects of