## TRADE BALANCES.

### What They Are and How They Work—Influence of Capital Investments—Demands of New Countries.

(Written by George Paish for the National Monetary Commission).

The term "trade balance" is generally used for the purpose of indicating the excess value of a country's exports of merchandise over the value of its imports of merchandise or the excess value of a country's imports of merchandise over the value of its exports of merchandise. In monetary circles the term is employed to denote the ability of a country to import supplies of the precious metals. If the rate of exchange of one country upon other countries is at the level which permits of gold imports, it is said that the balance of trade is in favor of the country importing the gold. On the other hand, if the rate of exchange of any country is at a level which admits of gold exports, the balance of trade is said to be against the country exporting the gold. In the sixteenth, seventeenth, and eighteenth centuries a favorable trade balance was a matter of great concern to statesmen and to financiers. At that time it was supposed that any country which imported goods of greater value than the goods it exported would be seriously injured by having to make payment in the precious metals for the difference between the value of the goods imported and the value of the goods exported, and that any country which persisted in purchasing goods of greater value than the goods it exported would be totally drained of its stock of the precious metals and would be ruined. The theory of the supreme importance of a balance of exports over imports was known as the "Mercantile system." Exports to secure favorable trade balances led to the passage of many laws for restricting imports and for stimulating exports. As commerce developed and international banking advanced it was recognized that a nation could under certain circumstances purchase goods of a greater aggregate value than it exported without sustaining any drain upon its stock of the precious metals or suffering any inconvenience whatsoever, and in recent time no one has paid any great amount of attention to the question of the trade balance other than for the purpose of ascertaining the factors which caused the imports of certain countries largely to exceed their exports, or of discovering the reason for the exports of certain countries largely exceeding their imports.

The great change in the theory of commerce that has taken place in modern times is due to the recognition of the fact that the volume of trade which any country enjoys quickly adjusts itself to the needs of that country, and that the effect of a sudden disturbing influence to trade—such as a crop failure, labor troubles, etc., which temporarily reduce a nation's exporting power—can be got over by financial operations in the great international money markets, and that excessive drains of the precious metals are not now to be apprehended. Experience has shown that apart from sudden catastrophes the foreign trade of every country is of a very elastic character, that the volume of imports or of exports quickly responds to the necessities of the case, and that no country can have an adverse balance of trade except for a short time and as a consequence of some unexpected disaster which temporarily diminishes its power to make payment for goods imported. Even at such times countries in good credit have no difficulty in borrowing temporarily or permanently the sums required to settle the balance due to other countries for commodities purchased or obligations incurred prior to the disturbing event—a process which averts any excessive denudation of the stock of the precious metals possessed by the country experiencing the disaster.

### II.—Capital Investments and Trade Balances.

The nations of the world may roughly be divided into two classes. In Class I are the countries whose imports exceed their exports, and in Class II are the countries whose exports exceed their imports. Generally speaking, the nations in Class I are the lending countries; those in Class II are the borrowing countries. The lending country has to receive payment for two things, (1) for the goods it exports and (2) for the interest upon the capital which it has in former years supplied to other countries. Excluding all other considerations the imports of a country which has placed capital in other lands must necessarily exceed the value of its exports to the extent of the produce it receives from other countries in payment of the interest upon its capital. On the other hand, the country that has borrowed capital from other countries, other factors being excluded, must export a larger amount of produce than it imports in order to pay, first, for the produce imported and, second, for the interest upon the capital it has previously borrowed from other nations. Hence the exports of the borrowing countries exceed their imports and the imports of the lending countries exceed their exports.

The situation is not usually confined to the mere receipt by a lending country of interest upon capital previously lent or the mere payment of interest by a borrowing country upon capital previously borrowed, and it will be worth while briefly to indicate the normal course of the trade balance, first, of a country which invests capital in other lands, and, secondly, of a country which borrows capital from other countries. Were there no interfering conditions the value of the goods, in which I include the precious metals, imported by a country must exactly balance the value of the goods exported in exchange. But when a country commences to invest capital in other lands its exports begin to exceed its imports. Capital investment by one country in other lands means that that country is willing to sell goods to other lands and to take payment in securities of one class or another. Should the capital investments extend over only one year the exports of the lending country in the year in which the loan is made would exceed its imports to the extent of the sum invested. Should no additional investments be made, the imports of the lending country in the following years would exceed its exports to the extent of the interest or dividends it received upon the capital invested. As time goes on, and the total amount of capital invested by it in other lands attains to larger and larger figures, the annual sum received as interest upon the capital embarked rises correspondingly. In this case the balance of exports over imports resulting from the investment of capital becomes smaller and smaller in consequence of the increasing sums received per annum from the interest upon the capital previously invested. After a time the annual sums which a lending country receives for interest exceed the additional sums it lends in each year, and in spite of its continued investment of capital in other lands its imports exceed its exports. For the clearer understanding of the matter I set out suppositious statements to show how investments of capital and the receipt of interest affect the trade balance of a country—

1. That neither lends nor borrows capital.
2. That is beginning to invest capital in other lands.
3. That has in the past invested capital in other lands but has temporarily ceased to make new investments.
4. That has both invested capital in other lands in the past and is still investing annual sums equal to the interest received on former investments.
5. That has in the past invested capital in other lands and is investing fresh amounts equal to less than the interest received.

1. A country that neither lends nor borrows and which has an exchange trade of $500,000,000:—

| | |
|---|---|
| Exports | $500,000,000 |
| Imports | 500,000,000 |
| Balance | Nil. |

2. A country beginning to invest capital in other lands and which places $100,000,000 of capital abroad in a year:—

| | |
|---|---|
| Exports | $600,000,000 |
| Imports | 500,000,000 |
| Balance of exports over imports....a | $100,000,000 |

3. A country that has invested abroad in the past a sufficient amount of capital to yield an income of $100,000,000 per annum from interest and which temporarily ceases to make fresh investments of capital:—

| | |
|---|---|
| Exports | $500,000,000 |
| Imports | 600,000,000 |
| Balance of imports over exports....b | $100,000,000 |

4. A country that has in the past invested capital in other lands, is receiving an income of $100,000,000 a year from interest upon that capital, and is investing an additional amount equal to the interest received:—

| | |
|---|---|
| Exports ....c | $600,000,000 |
| Imports ....d | 600,000,000 |
| Balance | Nil. |

5. A country that having invested a large amount of capital in other lands, is receiving an income of $150,000,000 per annum from interest upon that capital, and is investing $100,000,000 of additional capital in a year:—

| | |
|---|---|
| Exports ....e | $600,000,000 |
| Imports ....f | 650,000,000 |
| Balance of imports over exports... | 50,000,000 |

a Sum invested by exporting country.
b Received as interest on capital previously invested.
c Of this sum, $100,000,000 is for new capital investment.
d Of this sum, $100,000,000 is interest on capital previously invested.
e Of this sum, $100,000,000 is new capital investment.
f $150,000,000 is interest on capital previously invested.