

MONEY AND WAR PRICES

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by borrowing abroad, which was made immediately available by advances from the Canadian banks on the security of the foreign drafts, and partly from advances from the banks to be repaid from future loans, domestic or foreign, and future increases of revenue from new sources, thus putting into operation all three processes of financing the war already referred to.

"The first national sacrifice made in the economic line was the loss of the product of the labor and services of the troops enlisted and sent overseas. The second and much greater loss, was the cost of the special equipment of these troops for service at the front, the transportation, clothing, storing, etc. The second loss involved the setting aside of another large body of citizens with extensive plants and vast quantities of raw materials and other goods for the production of equipment, munitions, etc., destined to complete destruction without the return of anything to replace it. What we imported in connection with this process had to be paid for in the export of additional food, raw materials, etc. Thus, while our production was limited, the competition for it was greatly increased, and credit furnishing funds to the purchasers, prices continued to advance.

"The purchases and expenditures of the government naturally dominated the whole situation, determining prices for all others. It was no longer a question of finding a market for goods, but for finding goods for the market. The expansion of the credit documents which carried on the exchange processes dominated by the government occurred partly through the extra issues of Dominion notes. We need not take account of the notes issued for regular circulation—viz., the ones and twos and the few fives. We are concerned with the larger notes, chiefly of \$1,000 and upwards, which are not intended or used for circulation, but which were issued to meet government payments, and passing into the hands of the banks, become one of the lines of security on which they extend their issues and credits. The credit expansion came mainly, however, through the advances made by the banks, especially the advances of credit to the government—largely in anticipation of future loans. Under the suspension of specie payment and taking the banking system as a whole, the indefinite continuance of this process is quite practicable because a credit once granted and poured by the issue of cheques into the general money volume of the country never passes out of that circle until it is retired, usually by conversion into another form, as when the bank advances are paid off from the further government loans. Thus a credit of \$5,000,000, granted to the government is merely an entry in the bank's books, and when drawn upon by the government in favor of munition industries, transportation companies, and supply purveyors of all kinds, much of it may not leave the books of the individual bank involving nothing more than debit and credit entries in its ledgers. Even when the parties to whom the credits are transferred, keep their accounts with different banks, the interchange of such credits between the banks through the clearing house, practically offset each other in the long run. Thus a credit of even \$5,000,000 on government account makes little or no drain on the individual bank, and none at all on the general circle of banks, unless it comes to a matter of foreign exchange. Here the matter first takes the form of corresponding offsets in the shape of exchanges against exports, or against funds of the government, or corporations borrowed abroad. During the war, in particular, our financial engineers arranged carefully for the balancing of our international exchanges, so that there should be no serious embarrassment on that score. To be sure the continuation of the advancement of bank credits must lead in the end to an adverse balance of exchange through the stimulus thereby given to purchasing abroad. This we see in the case of Canada at the present time, where there is no special object to be gained by the government coming to the rescue.

"In the meantime, the bank account of our more prosperous citizens and those corporations and individuals chiefly profiting by the extensive war expenditures, were accumulating much of the extensive profits advanced by the banks. They were thus in a position to subscribe heavily to the new loans issued by the government. These, when successfully floated, enabled it to wipe out the bank advances and thus prepare the way for new and larger advances on the next turn. Even between the subscription to the loan and the payment of the final instalments, many subscribers obtained from the disbursements of that very loan sufficient to make their later payment upon it. The laborer, of course, takes care that he shares with his employer in the extra profit of war industries or trade, but is always disappointed to find that his latest wage increase is soon overtaken by the steady increase in prices.

"When the credit and advances made by the banks come in competition with each other in the purchase of supplies, alike for export and for home consumption, it is found that the volume of purchasing credit has increased much more rapidly than the volume of supplies, which is the cause of the constant rise in prices. This is quite inevitable and quite independently of any manipulation by the middlemen, though, of course, the constancy and urgency of the demand is a guarantee to them of ready sales at good prices.

"Some of the bankers, it is true, attempt to hedge on this rapid increase of credits. They admit a certain proportional advance of pure credit, when it is made to the first party, as to the government in anticipation of loans, but when once the government has drawn a cheque against these advances for the purchase of goods or services, and that cheque is deposited by the second party, it is treated as a deposit of actual wealth, as distinguished from a credit advance, and becomes at once a basis for a further advance. Much the same is true of advances to foreign governments to assist in the purchase of Canadian supplies. These advances are made in return for the securities of these foreign governments which are placed in the vaults of the bank and counted among its most liquid assets, although it is well known that, however sound the permanent credit of the government issuing them, they are certainly only paper credits at the present time, and as far as their effect upon Canadian finance is concerned, are solely expansion of credits without an ounce of good behind them. They, too, increase the competition for our necessities of life, thereby increasing prices and raising the cost of living, contributing, at the same time, statistical evidence of increasing prosperity.

"Reference has been made to the stage at which the inflation of credit in increasing prices, and thus fostering imports, develops an adverse balance of exchange. The net effect of an adverse balance of exchange in the main lines of a country's trade, as between Canada and the United States; is, first, to check imports and, secondly, to stimulate exports. It checks imports by adding its own rate, say 2 or 3 per cent. to the tariff barrier which already exists. It thus favors the domestic producer and increases the price of these goods to the consumer. It stimulates exports by adding the rate of exchange to the price received for them, and, by diminishing the supply at home, tends to raise the price for the domestic consumer. Thus inflation of credit is not baulked of its prey through the influx of foreign supply.

"We have seen, then, how subtle, effective and far reaching are the effect of the expansion of credits, and how useful, indeed indispensable, was this process to the financing of the war on the part of a country so little prepared for such operations as Canada. While, therefore, we cannot criticize the process as a war measure, it is plain that it assisted our country in making those huge sacrifices incidental to the war. It is now our task to reverse the process, to reduce the inflation, and this can only be done by the extra production of wealth. In a word, we must once more replace the water with milk, we must enable the people to receive for their labor the full value of it in goods and not merely in money."