THE CANADIAN CLUB
OF TORONTO
1933-34

(May 9, 1933)

Problems of the World Economic Conference

By Sir Walter Layton.

President Sifton:—This is the first meeting of the Canadian Club since I have been elected President and I want particularly to welcome you and express the hope that the present interest shown in the Club will continue during the year and that the Club will be worthy of the support you have given today.

I am not going to say anything of my own elevation to the Presidency except that on the day upon which the committee met I was very ill, as some will remember, and it may have occurred to the committee an opportunity was given for a graceful gesture which might not have to be implemented. But in any event I will here and now accept the honor and take it as a serious responsibility which I will seek to carry out.

Our head table is laden with a galaxy of interesting people. The young forward-looking people are the new members of the executive committee. Their names may not be very familiar to you or their faces as yet but they are setting out to start off the new year. Of course this is banker's day in honour of Sir Walter Layton and the other older faces you will all know. They will be somewhat familiar—perhaps all too familiar—to the borrowing

and debtor classes so well represented. We have them all here in any event.

We have the great honor of having Sir Walter Layton to address the Club today. He is the Editor of the *London Economist*. I think that is all the introduction necessary because, once you say that, there isn't much else to be said. We are deeply grateful to him for coming to the Club. We appreciate the trouble he has taken and we will listen with great interest to his remarks.

In order that his time will not be cut short there will be no remarks from the Chairman after his address is completed and he will be free to continue until two o'clock.

SIR WALTER LAYTON: — Mr. Sifton and Gentlemen, may I say first it is a great delight to be back once more among what one instinctively feels is one's own people.

The last question that was asked me before crossing over from the United States was whether I thought the World Economic Conference was going to be a success or not. Well, that is a pretty difficult question to answer, but my actual answer was something like this. The difficulties in the way of that Conference are immense, perhaps even greater than we probably understand, but, on the other hand, the penalties of failure for everybody are so great that none of us can afford to allow that Conference to fail. I shall only give one illustration of the immensity of the problem, and I give it because it happens to have been in my mind in going through the various parts of the United States. It is just the factor of the national income of the United States of America. It was estimated that in 1929 the combined income of the people of the United States, that is to say the total wages and salaries, income of people who received interest and so on, amounted to eighty-five billion dollars. It is estimated that last year, 1932, combined income amounted to forty billion dollars; that is to say, it had fallen to less than one half, partly through the fall of prices and partly through the shrinkage of production. When you imagine what is involved in that enormously diminished figure, with a national budget which was increasing for various reasons, you will see the difficulty and the problem which is facing the United States. It is

only the same problem that every one of us is facing. I merely give the figures because it throws into sharp relief this scale of the adjustment that has to be made, that is in fact being made, in trying to adapt our economic life to the appalling condition of the prices.

I have been following, as everyone has, the conversations in Washington, as they have been preliminary to the conference. I think it may be truly said that the visit of MacDonald and Herriot and various other foreign statesmen has had one very important effect, and personally I rate it as the most important result of those conversations. There is, of course, as everyone realizes in the United States, a division in the forces of unseen public opinion on economic affairs. There is the trend toward isolation, as there is in almost every country in the world to-day, and there is the current of opinion which understands that it may be necessary to contemplate an international and internation co-operation. I think that the visit of Mr. MacDonald and those who followed him has had very definitely this effect; that it has tended, for the time being, and this direction may be maintained by wise statesmanship, to emphasize in the public mind of America that this is an international problem with which we are faced, and to strengthen the hands of the administration and the hand of the President in attempting to move along lines of co-operation. Watching the situation for the last three weeks, it seems to me these visits have definitely had that effect.

When you come to consider what are these specific, these detailed, lines of co-operation, then it becomes more complicated and more difficult, and in particular the situation has been radically changed in the last few weeks by the action of the United States in regard to currency and the gold standard. That action has been so recent that it has made it very difficult to formulate precisely a basis of co-operation for the simple reason that nobody knows—it is not lèse majesté to say that even the President himself does not know—how he is going to use the powers he has obtained from Congress in regard to monetary legislation; but I would only make two comments in passing, and I make these comments here because I have ventured to

make them when I was addressing equally American audiences. They are these: I think there exist definitely certain great illusions in the United States as to what can be done by monetary action to raise prices. The simplest form of the appeal that is made to public opinion is that it suggests the devaluation of the dollar. It is assumed offhand that if you halve the gold content of the American dollar, you will double prices either next morning or within a comparatively short time. That I believe to be a complete illusion. There is no economic reason to suppose that if you halve the gold content of the dollar you will double prices, no economic reason whatever. What will happen is that, if the United States does that while it remains on a gold basis, it will halve its exchange with any country which also remains on a gold basis. If France remains on a gold basis and America allows gold to move freely and devalues the dollar, it follows that the dollar exchange against the franc must halve, but the effect of that may be to push down gold prices and the franc—not necessarily to double them in the United States, and there is every reason to think that it would certainly not have that effect. What it would do is: it would free a certain amount of circulating media. Notes might be issued against free gold by somebody, it might be the Government, it might be—well, if it were the banks, it probably would not be spent there, but if the Government took the surplus in the form of an excess profit on the currency and used it to redeem debt, that money would be spent once, precisely as if the Government had printed that amount of paper money; and as we have seen again and again in times of credit inflation, in periods of deflation, that expenditure might create an upward movement which would go around and around with its own momentum, but equally that currency might come back and lie idle once more, and, if it does that, prices will not be raised more than this one act of spending. I mention that because it is the simplest form which the illusion takes, and I am not going to touch upon the other suggestions that have been made in the United States, but I have merely illustrated that, to show it is not as easy as it looks.

The other point I want to make in connection with

what is going on in the United States is this, that if you are going to try to control and manage currency there is only one machine through which you can do it, and that is the banking system. The control of currency, the putting out of currency, and the giving of credit are matters that are carried out day by day by the bankers. There is no other way of doing it, and at the present moment in the United States there is no liaison between the Government and the banking system. For reasons which everybody understands, there is a political feeling that the bankers are largely responsible for the depression, that they have acted unwisely, and so on. I am not defending the bankers. I dare say it is true. It is not for me to judge. Many of these feelings may have grounds of justification, but you cannot ground a currency system except through the banks. The position when Mr. MacDonald was in Washington was that there was under discussion a currency problem perhaps more far-reaching than any that had been considered in the whole of recent history, and it was being considered with the Secretary of the Treasury in bed, with no governer of the Federal Reserve Board, the previous governor having resigned, and no successor having been appointed, and with no bankers in consultation. Now if there is to be management, one of the steps that has to be taken must be to recreate adequate contact between the civil authority, legislative and administrative authority, and the apparatus through which this monetary policy must be put into effect.

Now I mention that because I want to make this last point, that you can play havoc with prices by unwise action, but the wise action is to secure a rise in prices, which every economist, every public man, believes to be essential if the present crisis is to be ended. That rise of prices can only be obtained by careful and co-operative and international action, and what has got to be done is to establish first of all the basis of a monetary policy, and then to set up the machinery for co-operation between the banking apparatus of the chief countries of the world.

Now that apparatus is not functioning in the United States at the present moment and therefore it is difficult,

and will be difficult until that is remedied, to plan an international monetary scheme. I said just now that all economists and public people, and indeed one might say the whole world, realize that we must try and get an upward movement of prices, and that international action is necessary if that is to be achieved. It is further realized everywhere that fluctuations of exchange create uncertainty and stop trade. They don't merely postpone it, because if the trade of this month is not done it will probably not be done at all or the great part of it. Every month that you create inactivity in the business world, you are losing ground and one of the conditions that creates that inactivity is an unstable exchange.

Well, that being the case, why is it that Great Britain has hesitated to return straight away to the gold standard, and to accept, so to speak, the invitation that has been held out, indeed the pressure that has been put upon us, from the United States and from almost every other country of the world, to return to the gold standard on a new basis? I should like to spend the remaining time that I have in trying to explain a little bit to this audience why that is the case, as I see it. I am not speaking officially; I am speaking in purely individual capacity, and I hope that will be borne in mind in listening to what I have to say. I think it is particularly desirable and important to give this viewpoint, and that you in Canada understand it, because, as I have always conceived it, Canada must always be in a sense a link, a liaison, a go-between between Great Britain and the United States, both of whom you understand so intimately.

To understand why Great Britain hesitates, and has hesitated, I will venture for a moment to go back very shortly over the history of the last few years. In the past decade, Great Britain made a great effort to restore the gold standard, believing that it was the surest basis of reconstruction after the War. You will recall the loans floated under the aegis of the Bank of England, largely to reconstruct Austria, to put Hungary on its legs, to help later on in collaboration with America to stabilize the mark; always laying down one or two propositions—one, that the budget must be balanced, and, two, that the currency must be stabilized in relation to gold, and usually in return for these concessions a loan was granted.

We had worked the gold standard before the War, and Great Britain was largely responsible for working it. London before the War was the world's monetary centre, and the system worked largely because we maintained a free open market for goods, which enabled debtor countries to pay in goods. We took them. We accepted the balance of imports, and that meant the system worked because Britain at that time was so enormously an important market in relation to the whole world. Her imports were in the neighborhood of thirty or forty percent of everything that sailed the seas, and it came freely into Great Britain. The system worked smoothly and without friction, and we thought that after the War we could reconstruct it, and, as I say, the gold standard was re-established. It didn't work according to plan for a number of reasons. These currencies were stabilized on an unstable basis. France, for example, stabilized her currency on gold, but at a level which meant that her competitive prices were below those of other countries. Now, in economic theory, the natural result of that should have been that her prices would quickly rise. She would continue to export, her imports would diminish, gold would flow in, and prices would rise. That did not happen, however, because France's economy is an old economy and changes very slowly, with the result that gold continued to flow into France for an unduly long period of time and contributed to the mal-distribution of gold.

Another factor, we found tariffs rising against British goods all over the world, not only in Europe but in the British Dominions. You will recall that the Balfour investigation pointed out that the increase in tariffs against British goods was greater in the case of the Dominions than in the case of European goods, and finally the American booms began to reverse what had been the case for several years—instead of American capital flowing out of the United States capital was drawn into America in connection with the vast stock exchange boom, and that

still further dislocated the gold situation. Up until 1929 the international monetary situation, based upon the gold standard, was kept going by the export of capital from the United States and Great Britain, but as soon as that stopped it was realized the balance of payments of many countries of the world was not in equilibrium. The creditor countries were not ready to accept goods in payment of debt, and those debts had piled up mountain high, even in connection with private undertakings Finally, on top of that mountain of debt, there were war debts which had not, in fact, been paid during that period because of the lending that had been going on. After the crash in 1929 the whole of that structure began to topple, and finally we were driven off the gold standard.

We were driven off the gold standard because of the run of foreign depositors on Great Britain. I needn't go over the story of that period, and I don't want to give details at all, but I just want to make this point in connection with us going off the gold standard, that although we were forced off the gold standard because of the run on foreign capital deposits in London, there was a more deep-seated reason. That deep-seated reason was that our trade had been growing more and more out of balance, that while we had been maintaining our imports, increasing our imports indeed, our exports were unable to overcome the tariff and obstacles that were placed in the way. With the crisis, the makeshift arrangement that had kept the whole of this apparatus in equilibrium for five or six years ceased to function and we were brought up against hard realities, and one of the most outstanding of these hard realities is that when people are not lending, when capital is not flowing from country to country, countries must pay their way, and unless they have an unlimited supply of gold to do it with, they must pay their way by exchanging goods and services for goods and services. There is no option to that iron law. We were not doing that, and when you are in that situation, there is only one of two things you can do—one, deflation of prices and wages and everything in the country, and when the German prices broke in June 1931, we had no time to organize a revaluation of prices, wages and salaries and deflate, even if we could have done it politically. If you don't do that, there is only one option, and that is to depreciate the currency, which automatically begins to put you right.

We had fought very hard to maintain the gold standard after we had operated it all these years; we had persuaded countries in Europe to put their deposits in the Bank of England, and persuaded them it was as good as gold. It was felt our honor was involved, but the moment we were driven off, there was an immense feeling of relief that we were no longer trying to maintain the position which had strained our resources for six or seven years and involved us in a position where we had a million and a half unemployed.

The level to which the British pound fell was, speaking very broadly, a level which sufficed to establish very nearly, though not quite, equilibrium of our balance of payments, and it was that which is the underlying force determining what at the time we spoke of, and still speak of, as the natural level of the pound, and that natural level is a function any time of world conditions, including Paris. If the tariffs of America, the Dominions and Europe and all the rest of them had been lowered and our exports had found readier markets, the pound would not have dropped to $3.40 but would have stopped perhaps at $4.00, and if those obstacles were increased it is as certain as anything could be that the pound would drop further and stop our imports or increase our exports, or both. There is nothing mysterious about it. It is absolutely an inevitable result of the economic conjuncture with which our country was faced.

Now may I pass on to a corollary of that period? We established an Exchange Equalization Fund. People said abroad, and we have heard a great deal of it the last few weeks, that this was devised to maintain a permanent competitive advantage. Believe me, or believe me not, that was not the origin or purpose of the Exchange Equalization Fund, but being off gold and having had the depreciation of the pound, everybody turned on us and said, "Your action has been deflation. It is making depression worse

than before," and with some justice, because every change of that kind creates the uncertainty I have just been speaking of. We had created uncertainty. We had made it uncertain what the future level of prices was to be. We had been partly responsible for the continued fall of gold prices. Until we got our natural equilibrium, and everyone in Britain was conscious of the fact, it was highly desirable that the pound should not have unreasonable unnecessary fluctuations, we were not prepared to guess, and we are not at present prepared to guess, what is the proper price to stabilize the pound at in relation to the dollar. If for some political reason or for some other reason, the investors or speculators of the world suddenly get into their heads that for the time being the pound is a good currency to hold, and a wave of capital moves into London, and, if you do nothing about it, the pound will rise and when the waves recede the pound will fall again, and in the meantime they will have had their calculations disturbed. They will have had other currencies fluctuating and all the evils of uncertainty with their accumulative repercussions. The purpose of the Exchange Equalization Fund, as you read it in the speech of Mr. Chamberlain when he set it up, was to neutralize the abnormal movements upon the pound, to pinch and punish the speculator and discourage him from going on speculation in pounds, but it was not to modify or drive or push the pound to a set figure worked out and calculated in advance. Obviously, this is not a specious argument, it is a perfectly natural policy because we, at all events, in Great Britain realize fully enough that we shall never succeed in maintaining the pound at an international level; and if we tried, and if, let us say, the natural level was $3.40 and we tried, by means of an Exchange Equalization Fund, to hold it at $3.00, the tax-payer will in the end incur a stupendous loss. There is no known way of maintaining indefinitely exchange at an international level, and I am certain the governor of the Bank of England is the last man in the world to attempt it, but we have thought that in maintaining the Equalization Fund and preventing undue fluctuation, having regard for the international importance of

the pound sterling and its exchange, we were performing an international service.

Now may I say a word as to what the position was when the United States went off gold. Britain went off gold after external pressure. America went off gold after internal pressure and tremendous desire to secure an internal rise in prices. We fought against an internal rise in prices. We fought against inflation, balanced the budget before we left gold, and watched very, very carefully so we would not incur the fate which we thought at that time would befall almost any country that was off gold, namely complete collapse of the currency as it occurred in Germany. Other nations have learned from our experience that it is possible to be off gold without such a fate, and with our experience before them the United States have gone off gold with a view to securing an internal rise of prices under control to prevent it from going to extreme lengths.

But what was the position of the dollar? When America went off gold, America's balance of payments was in her favor. More money was owed to the United States than the United States owed abroad. There was, therefore, no reason why the dollar should fall. Nothing in the economic situation has changed the relative value of the dollar and the pound sterling, and no reason has yet been put forward why any such change should take place. It is still as imperative as ever for Britain to balance her payments as for every other country, and sooner or later, if the dollar is depressed, the pound will be depressed with it, subject only to one consideration, and that is the possibility that inflation may succeed in the United States without corresponding movement anywhere else. I already have given reasons for thinking that that is not as simple or easy as appears at first sight. I think, too, that what we can contemplate is some movement arising, and it has already begun, that the belief that prices are going to rise will help to start the movement and that foreign countries, particularly Great Britain, will co-operate in a similar movement to encourage an upward movement of prices, and the situation in Britain is set for an expansion of

credit. We have only to study the bank figures to see that, but if you get a movement of the currencies there is no reason why the exchange should not remain as it was a few months ago or return to that position.

I am afraid that I have taken rather a long time discussing that, but it is a matter which is certainly in everybody's mind in the United States, and I have very little doubt that it is in the minds of everybody in this country. I want to try and answer my question why we hesitate to act quickly in regard to the stabilization of the pound. I said just now, we have had a long strain in trying to maintain the gold standard and there is almost the feeling in Great Britain that gold is the villain of the piece, that that long strain was due to gold. You must accept that as a fact. It may be right or wrong, but accept it as a fact with certain knowledge, that in the labor movement and among members of Parliament and in industry, there is the feeling that we tried more than we could. We were strained beyond our strength. It was a great relief when we went off gold, and we are not going back until we are sure that the same thing will not happen again, and the conditions that it shall not happen again are something as follows—First of all, there must be a new parity for the pound sterling. We have our ideas of what it should be. I have given my reasons for thinking that there is some justification in the level of the pound which was obtained in recent times. Obviously, there is room for controversy that that argument is not accepted, and if every other country thinks it would like to get down to some other level, it must be brought to a test as to what level of currency will enable countries to balance their international payments and pay their way. There is no other basis for adjustment of parities between the countries. We must get this somehow. Some wise man must settle the new parity. We must get common agreement among the banking systems of the world. That means not particularly the central bank, but also it required the collaboration on a monetary policy which will aim at raising prices through abundant credit, though not indefinitely. We have got to try and get to an agreed monetary policy; and finally we

must have a rule as to the way in which the gold standard is to work in future. It is no good having a banking system under which gold flows in freely but never flows out, otherwise again you get the situation which brought the whole system collapsing down before; and, it is not an effective rule that any one nation should take the line that we need all the gold we have for the basis of our own currency. After all, the function of gold in an international system is as an indicator to indicate that the balance of trade has got out of gear and to increase the imports of the country which is importing too little, and increase the exports of the country which is exporting too little, and restore a balance, and there is no other function for it. There is not enough gold in the world to use as a commodity by way of trade. There must be new rules, new understanding perhaps, as to the functioning of the bank systems of the world.

So much for money matters; but there are also economic conditions and those economic conditions are chiefly concerned with trade and tariff. I have given some indication of the trend of opinion in England about the gold standard. The international system which we established failed because we thought if we established an international monetary system everything else would follow. We have discovered that you cannot run an international monetary system unless the economic background is right, and that requires that there must be a reasonable freedom in the movement of goods between one country and another. Unless that condition is satisfied, you cannot work an international monetary system. It is bound to break down, and if the influences tend in the direction of self-sufficiency or autarchy, a word at present so popular, you cannot have an international system. The two are incompatible.

How we are to get the tariffs removed is another matter, and I cannot, obviously, at the end of the speech, begin to talk of that subject, but I would only say that it requires that certain illusions here again need to be removed. One is that a creditor country can continue to be a creditor country without accepting goods. All experience and all theory show that that is not the case, and that a creditor country

must, if it is not to drive its debtors into default, accept a surplus of imports. But there is something else, and that is that there exist many other illusions regarding tariffs. One is that high tariffs mean high standards of living. The highest tariffs in the world are the tariffs in the United States, which certainly have a high standard; of Brazil, which hasn't quite so high a standard; and of Spain, which is one of the low ones in Europe. In Europe the high standard of living goes with the lowest tariff, and if you take Europe as a group of countries you will find the standard of living is almost in inverse ratio to the height of the tariff, or again that there is a naturally scientific tariff which would solve the problem if everybody would adopt it. The tariff should represent the difference between the cost of production at home and abroad. That, fortunately, has never been carried to its logical conclusion by any country, but it has been made the basis of the highest tariffs in the world, and naturally so, because if you put a tariff equal to the difference between the cost of production at home and abroad, you abolish precisely the benefit that foreign trade would otherwise produce. A country exchanges with another because the other country can produce more cheaply. If we put on tariff equal to the difference in the cost of production, there will be no trade, since we have reduced our people to starvation level. The proper application of that doctrine is to be found on the difference in production between the Prairie Provinces and the home counties in England, and it leads to absolute stagnation of trade. There are other illusions, but I have not time, and I have just time to say that when you have dealt with monetary and with economic matters, there remain a whole series of political obstacles, and that is a subject not for a few minutes of remarks, but for years of discussion, but they must be dealt with because they all tie up together.

If what I have said is right, you cannot establish an international monetary system unless you get the movement of goods which enables it to work, but a movement of goods from country to country implies that the nations are willing to be inter-dependent. When nations will not

be inter-dependent, if they expect to go to war the day after to-morrow, you have the whole circle of problems with which we are faced, and it is a desperately difficult situation. It is enough to baffle the wisdom of the wisest of our statesmen, but it has got to be faced, and I come back to the answer with which I started. If it is not faced, if we move in the direction of autarchy, of self-sufficiency, there is no room in such a world for such a country as Canada or the Argentine. Autarchy is the negation of a whole economic structure on which this great Dominion has been built up, but if it is destructive, if it is suicidal, for a country such as this, it is equal destructive for the great industrial countries of the world, for the great industrial countries which want to export goods to buy your natural products and the natural products of other countries of the world. If these threefold groups of difficulties are problems the most complex that any statesmen have had to tackle, the reason that they must fight on and try to solve them is that none of us dare face the consequences of failure. It means that if they fail all countries, whether the agricultural countries of America or the countries of the old world must face a disastrous fall in the standard of their material civilization.