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Source: *Proceedings of the Academy of Political Science,* Vol. 19, No. 1, Economic Nationalism, Trade Barriers and the War (May, 1940), pp. 80-87
Published by: The Academy of Political Science
Stable URL: https://www.jstor.org/stable/1172518

THE AMERICAN GOLD PROBLEM AND WORLD TRADE

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THIS gold problem is full of complications and can hardly be handled adequately or comprehensively in any short period of time.

Perhaps I might better begin by mentioning a few aspects of the subject about which I suppose there will be no disagreement. The first of these is that we already have a stock of monetary gold in the United States far in excess of what is needed to support any desirable increase in the present volume of currency and credit. The second proposition is that this already superabundant gold stock is certain to be considerably enlarged during the course of the war, and presumably during the months of readjustment following its conclusion. Some billions of additional gold, we may reasonably presume, will come into the country during these next few years, thus increasing the aggregate monetary gold stock from the present eighteen billions to perhaps twenty-two or even twenty-five billions of dollars.

I think it may also be agreed that this additional amount of gold does not in and of itself greatly increase the danger of inflation. We could have inflation on a very solid gold foundation with our present stock of gold; consequently, adding a few billions of unwanted gold to the stock does not very greatly change the picture so far as the danger of inflation is concerned. Inflation does not result from the possession of a large stock of gold. Such a stock merely permits inflation on a gold foundation. In order to have inflation, you must have a condition of persistent demand for all available labor, and also for all available capital; and that is a situation which does not, unfortunately, appear to be in the offing at the present time. Therefore, I rule out inflation as a present danger arising out of the presence of this superabundant gold stock.

With twenty-five billions of gold rather than eighteen billions, it will be a more difficult job for our monetary authorities to check inflation when and if an inflationary tendency develops, but it can be done if the will to do it is present. Reserve requirements of the commercial banks can be increased, and the federal reserve banks can reduce the total holdings of earning assets, and, by these means, two or three billions of gold might be neutralized, but that would not turn the trick. It would not be enough with our present eighteen billions, much less with the prospective twenty to twenty-five billions.

It will be necessary, if inflationary tendencies develop, and the will to control them is here, for the Treasury to sterilize large amounts of gold by issuing additional government securities for the purpose of absorbing excess bank reserves. I assume that that will be the policy of our government. You can, therefore, see that I am not particularly disturbed, from a danger of inflation standpoint, by the continued inflow of gold; but there is another danger that has, perhaps, more reality. We, at present, hold something like two thirds of the total monetary gold stock of the world and will doubtless hold a still higher percentage before the present war is ended. It has been suggested in many quarters that the rest of the world may elect to conduct its monetary affairs without any gold whatever, and may be unwilling in the future to accept gold as an international means of making payment, leaving the United States with a great stock of gold which will be quite without value for any exchange purpose whatever.

Certainly, if gold were no longer to perform any monetary purpose, its value would decline to a very small fraction of the present price. Since there are few industrial uses for gold, that would develop merely because gold were available at twenty dollars an ounce, or ten dollars an ounce, or even one dollar an ounce, we might find ourselves possessed of twenty to twenty-five billions of gold having no appreciable exchange value. I think that this is a possible danger but I doubt very much whether it is a serious danger and I will venture to give you four reasons for this view, a view which to some of you may seem unduly optimistic.

In the first place, it should be borne in mind that there is a widespread interest in gold mining in various parts of the world — particularly in South Africa, Canada, Australia and

Russia. In addition to the producing areas directly concerned, there is also the influential financial interest in gold mining properties, particularly in Great Britain. A policy calculated to destroy the gold mining industry will, therefore, be certain to encounter strenuous opposition.

In the second place, and this is of very fundamental significance, monetary authorities in no country seem to be willing to acquire indefinitely large balances in the currencies of other countries. This is an attitude which, I believe, will persist in the future. Everyone concerned practically with monetary matters recognizes the need of some asset which will be readily accepted as a means of making settlements in foreign countries. In spite of the monetary disturbances of the last ten years, gold has held its position as an acceptable means of making settlements. Nothing has appeared to take its place—certainly not the paper pound and not even the paper dollar. Experience during the last few years does not indicate that any country that has enjoyed a favorable balance of payments has been unwilling to acquire gold. On the contrary, such countries as Switzerland, Belgium, Holland, Sweden, to say nothing of Great Britain, whenever payments have been favorable to them, have acquired gold. Now this, I think, is a condition which will presumably continue. I hope for a far more peaceful world, of course, than we have been living in in recent years—in fact, all my analysis is on the supposition of a more peaceful world. I should think, however, that it was unreasonable to anticipate such a complete community of interest and such complete confidence as to lead different countries to be prepared to build up indefinitely large balances in foreign countries. They will wish to take something which they feel reasonably certain will prove acceptable as a means of payment anywhere throughout the world. Gold has continued to hold that position and no other commodity has anything like that acceptability throughout the world, and I do not observe that the acceptability of gold has in the slightest degree diminished during these recent years of disordered currencies.

In the third place, in the absence of some acceptable means of making settlements, the universal adoption of bilateral compensatory trade and financial arrangements between countries would, in my judgment, probably be unavoidable. There has, of course, for other reasons, been a strong tendency in this direction in recent years. It is certainly not a development calculated to increase the total volume of world trade. It has been a natural consequence of disordered economic and financial international relationships. If we are to move toward a more peaceful world, it may be presumed that bilateral trade arrangements will gradually disappear; but if gold should no longer be acceptable as a means of settlement, I very much fear that bilateral arrangements will become even more general than at present, and with little hope of their ultimate disappearance.

A fourth and final reason for my belief that gold will continue is related particularly to the functioning of a managed currency, and here I address myself to monetary theorists. Much criticism has been leveled at the gold standard on the ground that a rigid, fixed price for gold and rigid exchange rates frequently impede or prevent the adoption of desirable monetary policies, desirable within particular countries. That is the basis for the proposal that in the future we establish managed currencies. Now, it is not necessary that there be a permanent fixed price for gold and fixed exchange rates in order to secure the continued use of gold. Gold can play a part in a managed currency even though the currency system is one which permits a very considerable degree of elasticity, as regards the price of gold and as regards exchange rates.

I shall not undertake to discuss whether it will be desirable in the long run to establish an elastic price for gold, and elastic exchange rates. Merely for the purpose of this discussion, I shall assume that such a course is desirable; but then, I venture to suggest that without gold as a foundation or as a cushion, currencies cannot be controlled by the currency managers, that they will find in periods of stress that they are unable to give their currencies just the desired degree of elasticity that they think desirable from the point of view of their domestic situation.

In the entire absence of anything that the foreigner would be certainly willing to accept, I should imagine that, in a period of strain, speculation would develop against a currency, and in the course of time confidence in that currency would be so weakened that the currency managers would find that their currency was fluctuating within wider limits than in their opinion was desirable. The possession of a considerable amount of gold would serve as a cushion, and give them the means, I believe, of adopting that currency policy which they happen to think is desirable, and in the absence of that cushion I should question their ability so to do. This seems to me to be a reasonable ground for my opinion that monetary authorities are likely to agree that gold should continue to play some part in the working of the international monetary mechanisms.

Now, let us turn to the question of the circumstances in which it is reasonable to anticipate a somewhat better distribution of gold than that which obtains at the present time, and particularly a better distribution of gold than the even more unsatisfactory distribution which may be anticipated at the close of the present war. Let me say, first, that I do not envisage any considerable reduction in the aggregate amount of gold held in the United States. If that figure is twenty-five billions of dollars at the end of the present war, it would be my guess that it will be twenty-five billions, ten or twenty years hence.

The best that we can look for in my judgment is that in the years following the war, if gold continues to hold its place as a part of the international monetary mechanism, the rest of the world will acquire future gold production. Now, the present annual output of gold is in the neighborhood of forty million ounces, and the total value is between twelve and fourteen hundred millions a year. If the rest of the world over a period of ten years were to acquire the present annual output, assuming it to be maintained as I think one may reasonably presume it will be, at the end of ten years the rest of the world would have ten to fifteen billions of gold (scattered among the various countries) more than it will have at the end of the war. That would give a not too bad distribution of the total gold stock as it then will be.

I do not anticipate an outflow of gold from the United States, because even to change the inflow involves so very considerable a change in the balance of payments of this country. We have received this gold partly because of an excess of exports over imports, and in part because of funds sent to this country either for investment or safekeeping. Had this war not occurred, it is at least possible that conditions would have so developed that a considerable part of the foreign funds that have come to this country in recent years would have been withdrawn for employment at home; but, a major part of these funds will doubtless be expended in this country for the purchase of war products of one sort or another. Consequently, at the end of the war I think we may reasonably presume that not only shall we have more gold than now, but also that foreign investment and foreign funds in this country will have been quite materially reduced.

Whether there continues to be an inflow of additional funds from abroad, seeking investment and safekeeping, will depend, of course, upon conditions abroad relative to those here, obviously a matter over which we ourselves have no direct control. However, on the supposition of a satisfactory peace with a promise of a peaceful world, I should imagine that European funds would find employment at home for the work of reconstruction of their capital resources. There is, therefore, it seems to me, a fair probability that, in so far as gold has come to this country in recent years for investment reasons, the inflow may decline.

We now come to exports and imports. In this matter I am afraid that there is very, very little that the United States will do. It seems to me quite unlikely that the United States will change its tariff policy in a period of business inactivity in such fashion as to permit a large volume of goods to come in from the outside in competition with inactive American industries. That exports will shrink, owing to the inability of the rest of the world to find dollars, is perhaps a probability. We may get a more normal relationship between exports and imports through a shrinkage in exports; but I should not imagine that that would be a satisfactory solution from the point of view of the rest of the world; a mere reduction in exports, accompanied by a reduction of imports, does not look very satisfactory or promising.

I therefore wish to present what I believe to be the greatest single contribution which the United States can possibly make to a more satisfactory condition all around the world and so to a solution of the gold problem. It is a contribution that has no direct relationship to exports and imports. The United States is so large a country that we cannot expect a trade recovery on a broad front to be brought about here through an expansion of exports. We are already exporting an excessive amount relative to imports, and the billions of additional exports that would be required really to bring about a broad recovery certainly cannot be developed beyond the temporary increase that may accompany this war.

If we are going to have a broad recovery in the United States we must produce more goods and services for home consumption. It was observed this morning that at one time we exported something like seven hundred thousand motor units to foreign countries. Well, you cannot imagine exporting a million and a half units to foreign countries; it would simply smother the foreign countries with cars when account is taken of their purchasing power, but an increase of a half a million cars in the United States per year is almost a normal kind of thing. We vary all the way from two million and a fraction to five.

This is a great consuming market of one hundred and forty millions of people, and full employment of labor and utilization of current savings in capital expansion must be directed primarily toward producing more goods and services for home consumption, whether that be in reconstruction of our railroads, improvement of our utilities, or in what seems to be the major possibility in this country—a transformation of housing conditions for the great mass of people.

The way to secure a broad recovery is to utilize our technological knowledge so that the man with the income of two thousand dollars shall, in the course of not too many years hence, be able to buy what the man with twenty-five hundred dollars is now able to buy, on the basis of the same general level of prices. If we advance in that direction, then we can really adjust our position to the rest of the world without any difficulty to ourselves, and to the great advantage of the rest of the world. For, given full employment, mainly concerned with the production of goods for home consumption, we should, as an incident of that widespread prosperity, buy more from abroad, and without inconveniencing any of our existing industrial groups. We should import more tea and coffee and cocoa and rubber and tin, and so on, in those circumstances. That is the basic means within our own control of bringing about a change which would lessen the inflow of gold, but until that comes about, I fancy that we shall continue to take in gold. Obviously we are not going to refuse to acquire gold when the refusal to do so would abruptly eliminate at least a billion dollars' worth of purchasing power for our exported commodities. We could refuse to take in gold, but there would at once be an inevitable contraction in our exports. That we are unlikely to face in a period of widespread unemployment and business inactivity.

I feel that we shall probably continue to import gold until somehow or other we have succeeded in developing a sufficient demand for labor and capital in this country to yield widespread business activity, general prosperity and a higher standard of living, and when that time comes, the gold, I am confident, will cease to come in, and I am at the same time confident that the rest of the world, now one country and now another, as it develops a favorable balance of payments, will acquire some portion, large or small, of the current gold output of future years.

Remarks by the Chairman

Chairman Wadsworth: I think all of us here who have been worrying about the appraised value of that pile of gold that is accumulating in Fort Knox must take a good deal of encouragement from what we have heard from Professor Sprague in his estimate of the future of gold as a measure of values in this country and throughout the world.

One element discussed in part of Professor Sprague's general thesis on gold is the importance of foreign lending, and we are very fortunate to have the President of the Export-Import Bank of Washington, who will speak to us now on "Foreign Lending". I take great pleasure in introducing Mr. Warren Lee Pierson, President of the Export-Import Bank. Mr. Pierson!