THE FALL IN FOREIGN EXCHANGE

BY STUYVESANT FISH

THE fall in foreign exchange is merely the outward and visible manifestation or the symptom of a very serious disease prevailing in the money situation in Europe. No one over there does, nor here in America should, question that the monetary situation of each of the European nations engaged in the late war is one of weakness, not to say collapse, which calls for careful diagnosis, fearless and thorough probing, drastic remedies, and I fear in some cases "capital operations," to use a surgical term.

The autumn of 1914 found the nations of Europe doing business with currencies consisting of gold and silver coins, and of bank notes supported by not over-abundant reserves of bullion and metallic money. The war had been preceded by many years of preparation therefor by all of the leading nations of Europe. Germany was prepared in every respect, military, naval, financial and commercial. Great Britain had for many years been maintaining as a matter of settled public policy a navy equal to those of any two other Powers. France had recently increased the term of compulsory service in her standing army.

Immediately on the mobilization, all of the belligerent nations of Europe declared moratoria in respect to obligations of their own people payable within their own jurisdiction, forbade the customary renewals of credits to foreign borrowers, closed their stock exchanges, (thereby preventing foreigners from selling therein) and at the same time moved heaven and earth to collect in gold the obligations of foreign debtors. Of this fact we have an instance in the unfortunate City of New York, which was forced in one way or another to pay premiums amounting to near seven million dollars in order to liquidate in gold or its equivalent a debt of eighty millions held in France and England. The season chosen for the beginning of hostilities was an unfortunate one for our bankers and merchants, in that they had, as usual, drawn very liberally against European credits, expecting to renew the drafts, or to pay them with shipments of wheat and cotton later in the autumn. Exchange on London rose to $7 per £1, a price exceeding 143 per cent of the theoretic, metallic par of $4.8665.

The various warring nations also cast aside all the restrictions of prudence and of law governing the issue of bank notes, and put forth irredeemable paper, carrying no promise to pay, simply the governmental fiat that it had been made legal tender for all purposes. There followed the inevitable result, under the law which Sir Thomas Gresham had laid down in the reign of Queen Elizabeth, that "Bad money drives out good": and gold disappeared from circulation. The first issues (specimens of the English and French reached here early in October, 1914) were of course followed by other and vastly larger ones, till we now have in Europe a situation absolutely unheard of in all history, indeed undreamed of. A number of publications[1] give the fabulous figures to which these issues have grown.

The effect of these issues on foreign exchange was soon seen in the fall thereof below the gold shipping point, that is to say, the price at which gold would naturally flow from the debtor country to the creditor country. Needless to say the export of gold except on Government account was strictly forbidden. In Germany at least, private stores of gold and silver plate were expropriated. In other countries the premium on gold as reflected in the exchanges, and the growing burden of taxation, accompanied by increased cost of living when paid for in depreciated paper, must have effected considerable melting-up of private stocks of plate. Many doubtless did this from patriotic motives. Toward the close of 1915 the price in New York of exchange on European countries at war, clearly showed the existence in them of a premium for gold when paid for in the paper money therein current. At first we were told that this was due to the war rates for marine insurance preventing shipments of gold, but when the depreciation exceeded those war rates, as it speedily did, the fact of the depreciation of the currency became obvious to all thinking persons at all versed in the business. Individually I became so much im-

---

[1] *Financial Status of Belligerents. Debt, Revenues and Expenditures, and Note Circulation of the Principal Belligerents in the World War.* By Louis Ross Gottlieb. With an Introduction by Prof. Edwin R. A. Seligman of Columbia University. 1920.

pressed with these facts and with the world-wide struggle for gold which was certain to follow peace, that in the spring of 1916, I wrote the then Secretary of the Treasury, Mr. McAdoo, pointing out the necessity of preparing for that inevitable struggle, closing my letter thus:

> My purpose in thus addressing you, is to bring to your attention the necessity for monetary and financial preparedness to meet a contest which is both imminent and unavoidable and in which we will have to combat the combined financial skill, experience and power of all Europe for the first time. Their struggle will then indeed be one for monetary and financial life or death—a thing worth fighting for.

In August 1914 the nations of Europe generally, and particularly Great Britain, France and Germany, were vastly creditors to the rest of the world and especially to the United States. That situation has, so far as we are concerned, been reversed, in that most of the European holdings of American securities have been sold in this country for one purpose or another, and in that, while we were at war, Congress, as a war measure, saw fit to lend the various European Governments, at the exceedingly low rate of five per cent. per annum, nearly ten billions of dollars. I say low rate, because at the time those loans were made, the well-secured obligations of the best of those Governments, England and France, could be bought in this market to yield over seven per cent.

The struggle for gold foreshadowed in my letter of 1916 to Secretary McAdoo is now on. Two years ago, that is in January 1918, when Mr. Wilson began developing his ideas about a League of Nations, the British Government with their usual intelligence and forehandedness appointed a committee, at the head of which was Lord Cunliffe, the Chairman of the Bank of England, " to consider the various problems which will arise in connection with currency and the foreign exchanges during the period of reconstruction and report upon the steps required to bring about the restoration of normal conditions in due course." Having made interim reports, that Committee rendered a final one on December 3, 1919, in which they criticised adversely the maintenance in England of rates of interest lower than those prevailing in gold-paying countries, and recommended as follows:

> That preference should be given to exports to countries which are able to make payment in the ordinary course of trade.
>
> Increased production, cessation of Government borrowings and de-

creased expenditure both by the Government and by each individual member of the nation are the first essentials to recovery. These must be associated with the restoration of the pre-war methods of controlling the currency and credit system of the country for the purpose of re-establishing at an early date a free market for gold in London.

Meanwhile, so far as I have been able to discover, the Government of the United States has done nothing, except that Mr. Glass toward the end of his term as Secretary of the Treasury, recommended to Congress the unheard-of proposition that the United States shall, in advance, fund the interest to accrue for a term of years on the debts due by European nations, among which Great Britain and France, the strongest of them, are our largest debtors. The measure is now before Congress, and it is to be presumed that the rate of interest will be as before, five per cent. Should this monumental folly be enacted, it will shift from the shoulders of the debtor nations to ours a present burden of some four hundred and forty million dollars per annum of added taxes, and will result in enabling the merchants of Europe the better to compete with those of the United States for the trade of the world in the meanwhile. In view of the fact that during the twenty months in which the United States were at war (April 1917 to November 1918) they did not enter into any form of alliance with any of the European Powers, how can this unheard of proposition of voluntarily making of ourselves what might be called "deferred creditors," and now entering into a financial alliance with more or less bankrupt Europe, be advocated?

There is nothing novel in the present condition of the foreign exchanges, nor in the attempt to disguise under that title the premium on gold which exists when paid for in irredeemable legal tender paper. The same thing happened in Great Britain during the Napoleonic Wars. Then, however, the paper was better, in that it was in the form of notes of the Bank of England, a solvent, going concern, and bank notes were not at that time legal tender. This occurred in the so-called period of "Bank Restriction" after the Chancellor of the Exchequer had, in 1797, ordered the bank to cease paying gold. In 1810, a Select Committee of Parliament on the High Price of Gold Bullion, brought in the "Bullion Report," which was then ordered printed, but by Parliament rejected as the war was still pending. Four years after Waterloo, in 1819, Parliament took the matter up again, accepted the verities of the "Bullion Report," ordered and enabled the Bank of England to reduce its over-issues of paper money, and effected the resumption of specie payments in 1821. In 1810 as now, the representative of "High Finance" maintained that there was no depreciation in the paper money, but only "adverse" exchanges. The Committee, looking further into the matter, found on the testimony of those who traded with gold paying points, Amsterdam, Hamburg and Paris, that there was a premium of fifteen and a half per cent above the mint price of gold. The premium increased in later years to approximately the figure now prevailing in England, say thirty-five or forty per cent. Professor William G. Sumner of Yale, writing in 1874, said, "So much in regard to the laws which govern paper issues, as was laid down in the Bullion Report, is established beyond dispute. Its doctrines are the alphabet of modern finance." A later English writer, Henry Dunning MacLeod, A. M., speaks of it as "a most masterly report, probably the most able ever drawn up by a Parliamentary committee. It is one of the great landmarks in economics, as containing the infallible principles upon which a paper currency must be regulated." To which I add that those laws operate today as then, and are as incapable of change as Sir Thomas Gresham's law about bad money driving out good.

In a recent English publication, *The Paper Pound of 1797-1821*, A Reprint of the Bullion Report with an introduction by Edwin Cannan, LL.D., Professor of Political Economy in the University of London, Professor Cannan says of the present situation:

> When the scales at last fall from the eyes of the people of Europe, groaning under the rise of prices, they will no longer cry to their Governments "Hang the profiteers!" but "Burn your paper money, and go on burning it till it will buy as much gold as it used to do!"

So likewise we, during and after the Civil War, had our troubles with our depreciated currency, which for eighteen months throughout the year 1864 and the first half of 1865, averaged, in gold, a value of less than fifty cents on the dollar. Indeed our price for gold rose to 284. But as English writers of that period did not fail to say, "the American Government acts wisely in forcing gold by timely arrangements to pass through its treasury." This was effected through our Act of February 25, 1862, authorizing the issue of the " Greenbacks," in providing that they should not be received in payment for duties on imports nor paid out as interest on the public debt. Those two things were currently and constantly paid in gold through our whole period of suspended specie payments from 1862 to 1878 inclusive.

This resulted in an open market for gold in New York, in which there were wild fluctuations, but as foreign exchange continued to be bought and sold in gold the fluctuations therein were not abnormal. That is to say, the United States faced the situation honestly and frankly, confessing a premium for gold, and a depreciation in our irredeemable legal tender money. Had the European nations, or any of them, in 1914 followed our example they would have had a like experience and be today much better off.

I trust I have made it clear that there is nothing whatever the matter with the fall in exchange except in that it represents a premium which has to be paid in countries afflicted with over-issues of irredeemable fiat money, when they seek with such money to buy gold,—the one thing accepted of all men everywhere, at all times, in international exchange operations. Do not understand me as favoring the putting of any restriction whatever upon the export of gold from the United States for commercial purposes, nor as being opposed to our merchants, bankers, financiers and capitalists making loans, or investments abroad, further than this, that payment must be exacted in American gold dollars, and at rates of interest enough higher than those here prevailing to justify the investing of money outside of the jurisdiction of our Government. On the contrary such loans and such investments by individuals should be encouraged. We should begin now to act as the banker of the world, but must do so prudently, in full appreciation of our responsibility to ourselves and to the rest of the world. But our Government must not be allowed to fritter away another dollar in altruistic nonsense. Each of the nations of Europe is fully alive to the situation, and in its struggle for gold will leave no stone unturned, each playing its own hand for its own sake against the others and against us. Meanwhile we must protect ourselves, if we are to continue to remain able to protect them against the results of their own monetary and economic blunders.

There are among us those well versed in the business, who contend that the fall in foreign exchange is not solely due to the over-issue of irredeemable paper money. Of them I would ask, what is there in the course of trade or the balance thereof, or in anything whatever except the depreciation of the currency, to account for the following facts: That on January 1, 1920, it took the nominal equivalent of one hundred and twenty-nine dollars of English money to buy one hundred dollars of American, and that a month later, on the first of February, it took one hundred and thirty-nine; that in France on the first of January it took two hundred and sixteen, and on the first of February two hundred and fifty-eight; in Italy on the first of January two hundred and fifty, and on the first of February three hundred and one; while in Germany it took on the first of January one thousand and twenty-five, and on the first of February nineteen hundred and four. Let me also ask, what can there be in the state of trade in Europe or the balances thereof, which makes such discrepancies as between the various countries named, and above all why at the same time the exchanges of those countries were similarly affected toward the gold-paying countries of Europe,—Norway, Sweden, Holland, Switzerland, and Spain, as well as toward the rest of the gold-paying world, including the United States, South America, parts of Africa, and the Orient.

I have given their theory such thought as I am capable of, but cannot see the solution except in the single fact that the paper money of Europe is discredited in the minds of the people who are forced to accept it. What the depreciation in paper or the premium for gold, call it what you will, shall be next month I am unable to guess.

Another fallacy which has been so assiduously circulated among us by interested parties as to be somewhat generally believed, is that the fall in foreign exchange is "almost as detrimental for us as exporters as it is for the unfortunate peoples of Europe." The facts are that during the Napoleonic wars, from 1801 to 1821 inclusive, the *volume* of imports into Great Britain increased; that in our period of depreciated paper money the gold value of imports of merchandise into the United States for consumption therein doubled; that during the late war, imports into Great Britain, exclusive of those for the purposes of the Government, increased by more than one-half and that in Italy imports rose in a still higher ratio. All of which was of course accomplished by borrowing.

Those of us who are, as I am, old enough to remember our period of strain and suffering under depreciated legal tender paper money, which lasted through the years 1862 to 1878 inclusive, and the train of other difficulties, more or less political,—"Greenbackism," "Bryanite Silverism at Sixteen to one," etc.,—which continued to afflict us down to the end of the nineteenth century, can appreciate as younger men cannot, the gravity of the situation now confronting the nations of Europe. Do not think of it at all as a matter of foreign exchange, but rather as one of financial and monetary blundering committed by the nations to which we have always been accustomed to look for sound conservative example on such subjects, based on their long experience and vast accumulations of capital. Out of the slough in which they are now involved, there are three possible ways:—

First: To resume specie payments, as Great Britain did in 1821 after more than twenty years of suspension, and as the United States did on January 1, 1879, after seventeen years of like experience.

Second: To flounder along for indefinite years with a depreciated currency, constantly varying in value in respect to gold, as Spain, Austria and Russia have done.

Third: To repudiate the paper currency as was done by the United States during our Revolutionary War in 1780, when the stuff fell to such a price that it is recorded of a barber in Philadelphia that he papered the walls of his shop with notes of the Continental Congress; and as the French Republic did a few years later with their *assignats*.

Where paper money has fallen to a very great discount (our Continental money became worth only two cents on the dollar, before it was absolutely discarded) the best outcome probably will be to let the stuff become valuable and interesting solely as a memento of past bad times, as soon as possible. After all this would involve merely an internal tax, and one of no very great amount, on any one individual holder, and would fall upon all in proportion to their holdings. Let us hope that the gold-paying countries of the world, among which the United States must take the lead, will work out some solution, by carefully husbanding their resources of gold and of credit based thereon, and intelligently, profitably and liberally using them for the common good of the whole world. If this be done we shall in due time see the nations of Europe, one by one, get back on a gold-paying basis. Meanwhile we have nothing to fear except the possible folly of our own Government and our own people in frittering away for maudlin sentiment an opportunity such as does not come to any nation once in a century. Such an opportunity Great Britain seized in 1821 and held until 1914, by making of London a free market for gold, and a safe place for the investment of foreign capital, with the absolute assurance that the owners of it could at all times get it back in kind, that is to say, in gold.

STUYVESANT FISH.