A B C OF FOREIGN EXCHANGE

Most Important Crisis in History of International Trade Has Caused Dramatic Upset in Financial Capitals of World

By EDWARD A. BRADFORD

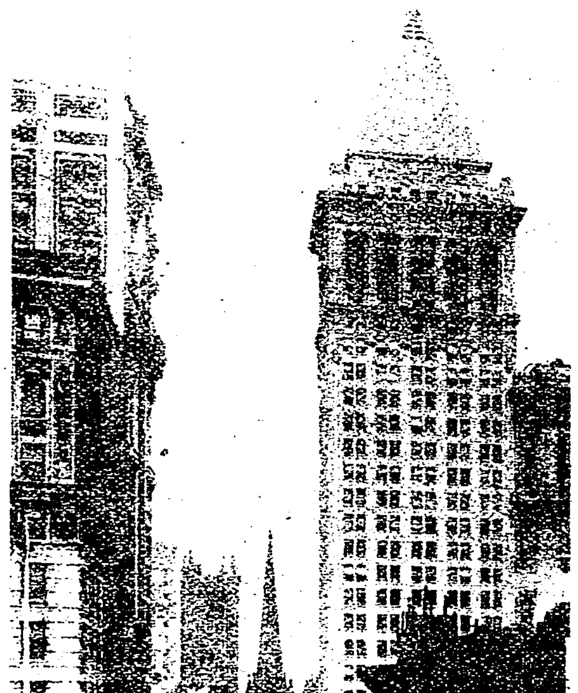
Money Talks in So Many Languages That Only Gold Can Act As Interpreter, and Its Disuse Has Made the World a Tower of Babel

NO reader of newspapers can escape seeing references to the confusion and losses caused by the use in international trade of as many sorts of money as there are countries concerned. A country makes its currency almost as much a point of honor as its flag, and would not dream of using the money of any other country or allowing any other country to interfere even by suggestion regarding the merits of its currency, its basis, or manner of use. And, truly, in domestic trade, within the limits of any one country, there is little practical objection to indulging such preferences or prejudices. They even have their uses, just as patriotism profits by pride in the flag, whatever its colors, and even whatever crimes it may cover or errors it may condone.

It is different in trade between nations. Imagine the bookkeeper of a man in international trade keeping his accounts in pounds, marks, francs, dollars, krone, rubles, guilders, drachmas, pesetas, yen, milreis, and so on through the list, always too long and much lengthened by the addition to the roster of nations of a dozen or two created by the Treaty of Versailles. Each of the list must have its own currency, of course, for currency has always been thought—erroneously—to have something essential to do with sovereignty, and not as being primarily a matter of trade. In each of these countries wages can be paid and spent and goods can be exchanged with little difficulty, but it is constantly harder for the keeper of international accounts to balance his books.

Even in the primary school one of the first lessons is that apples and oranges cannot be added or subtracted. In the next grade it is taught that fractions can be added only by being reduced to a common denominator. International traders and their bookkeepers have just that sum to do under conditions more difficult than trouble school children. Fractions do not change while the sum is being done, but the value of the money of one country in the money of another country is as changeable as April weather. Last week the value of pounds in dollars or of dollars in pounds changed while the international bookkeepers were telegraphing or even telephoning about it. Dollars or pounds or any other currency change their value according as goods are plentier or scarcer, but that occurs only over considerable periods of time and by changes so small that they pass unnoticed from day to day or sometimes from year to year. But last week the most expert valuers of the money of one country in the money of another country stopped trading, the alterations of values were so swift and large. If that is the case with the money changers—they call themselves cambists when they are calculators and when they trade arbitrageurs—imagine the troubles of merchants, exporting or importing, trading over thousands of miles of distance and over weeks of time, with little or no knowledge of the technique of the money market. Whether the bargains are done in the money of the seller or the money of the buyer, whether the contract is for payment when the goods are put on board cars or steamships, or when the goods are delivered—f. o. b. or c. o. d. —it is all the same, the profits of the trade may be turned into a loss by the change in the value of the currency during the time necessary to do the business.

It is plain that merchants trading in that manner cannot be sure whether or not they are solvent. Few businesses are managed on a margin as great as the fluctuations in the "exchanges" (of one currency for another) more than once in a single day of the last week or so. The confusion was greatest where the depreciation was greatest, but it was universal, except in Russia. Nobody will take Russian currency for goods, or exchange any other currency for Russia's. The Bolsheviki set out to make money worthless, and succeeded. Russia printed currency until it was so worthless that it was thought a waste of paper and labor to print any more, and it passed by weight instead of by count. Notes of large denominations when used at all were used in strips or sheets, like our postage stamps.



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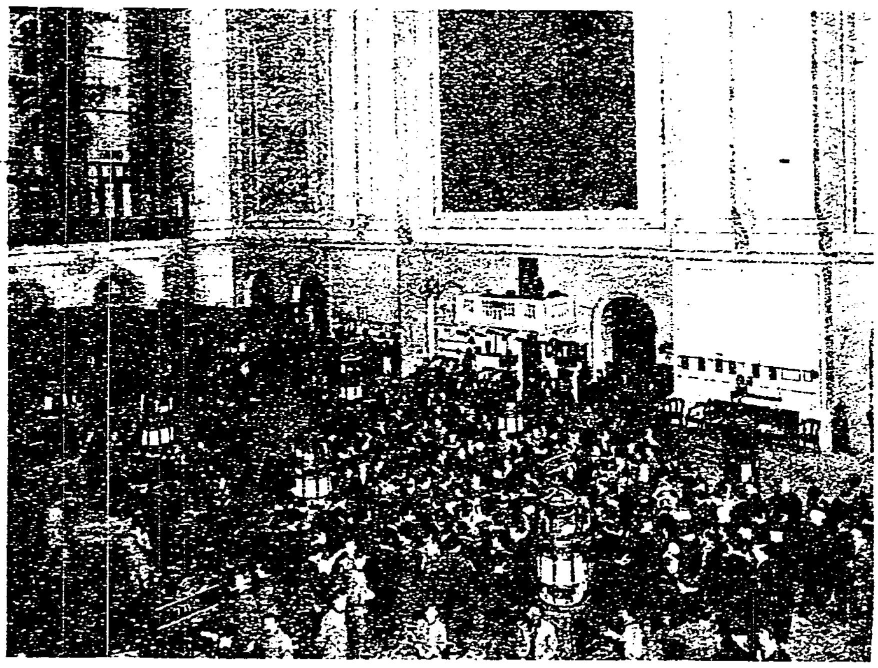
This is less so in other continental countries, but in all in some degree it is true. As the cable quoted Professor Jastrow of the University of Berlin, an authority for Germans at least: "Our money trading machine has broken down. We no longer have a standard of value. It must be stated frankly and ruthlessly that we no longer have a functioning monetary system."

That is a calamity, for under our industrial system of production all goods are produced and exchanged for money. The Socialist theory is that goods should be produced only for use, for consumption, and that production should stop when the need for goods was satisfied. The Socialists complain that when goods are produced for money they are produced for profit, and that the greed for profit is illimitable, and is the root of the exploitation of labor. It is apart from the point to discuss the Socialist notion that the invention of money was the ruin of the working class. The point here is the confusion of the exchange of currencies produced by the breakdown of the monetary system, as Professor Jastrow said last week.

Why is that greater just now than at any other time? It is because of the difficulties of the keepers of international accounts who have to deal with fractions without a common denominator. Exchanges of currencies used to be managed by the use of gold. When different currencies would buy equal amounts of gold the currencies were of equal value in the same place, and of different values in different places only according to the cost of moving the metal from one place to the other. But gold can now be got for currency at par only in the United States. In other countries gold is at a premium, and if the gold is at a premium the currency given for it must be at a discount. The discount may be of any degree. In London the discount last week was the greatest ever known, 35 per cent., while the premium on gold was 47 per cent.

Why was there a difference between the premium on gold and the discount on currency? Chiefly because the gold was wanted to spend outside of England, particularly in New York, and the currency had value only in England. If Americans were as eager to buy in England as Englishmen are to buy in the United States, the two currencies would be in equal demand, and therefore of equal worth. But when other nations are buying in the United States on a scale of four billions of dollars more than they sell to the United States it is proved that there is a greater demand for dollars than for other currencies. In other words, other currencies are at a discount—compared with dollars.

There are two reasons for the premium on dollars, compared with other countries. One is that the dollars can be spent in New York to greater advantage than anywhere else, for the world's greatest stocks of the most wanted goods are here. The other reason is that the



Floor of the New York Stock Exchange

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The Royal Exchange in London

dollars can be taken from New York to buy anywhere whatever the world wants and cannot buy here. In one day last week $17,500,000 was sent from the United States to Argentina, which is willing to take dollars now, although ordinarily Argentina prefers pounds.

More correctly speaking, Argentina prefers neither dollars, nor pounds, nor any other particular currency, but wants its bills paid, and the United States owes Argentina, having bought there more than it sold there. In just that manner all countries which buy or sell outside themselves want the balances due them in their own currencies. The old notion was that the balances were wanted in gold because gold was wealth in itself, but that theory has been exploded. The balance of a nation's trade represents profits, and the only way to reduce profits to possession is to bring them home. Argentina would be compelled to take its own currency if we could supply it, but, having no way to get Argentine currency, we send gold. That brings out the point that there is no international money. When gold is sent from one nation to another it goes as bullion, as a commodity, not as currency. It is universally acceptable, because gold will buy anything anywhere, but it is not international currency of legal tender.

How does it happen that there is no international money when every year there are scores of billions of international trade? Why is the lack of an international money more grievous this year than in other years? The reason is that world trade is on a commodity basis rather than a currency basis or even a gold basis. It is customary to speak and think of the exchanges of currencies, although the fact is that the exchanges are of goods. Nations are not traders, although the world war has produced among its many marvels some cases in which nations have traded directly with each other in a manner contrary to all prior experience. The exchanges between different countries are exchanges between their private traders, and their private negotiable paper has been hitherto an acceptable substitute for international money. It is not unknown in domestic trade that one man pays his debts with another man's check. That has been the settled custom of international exchange of goods. The "exchanges" might be used almost synonymously for either goods or currencies, but the exchanges of goods are the substance, although the exchanges of currencies are usually thought and spoken of.

By long use foreign traders are accustomed to paying and receiving payment in other men's checks, in foreign trade called bills of exchange, even when the business is done through banks. England may be buying American cotton and Americans may be buying British cotton cloth. The exchanges of the staple for the fabric will balance, including the profits, but the business will not be done with the bills of exchange (or checks) of the buyer of either commodity. Each will pay with the bills of entire strangers, and their own bills of exchange will pay other traders' debts. Money will in normal times seldom cross the ocean, not in a tithe or 1 per cent. of cases. Those not familiar with the well-settled customs and wonderfully refined methods of foreign exchange may well be puzzled that buyers and sellers do not pay their own bills and that each receives payment through banks, but really from strangers who owe them nothing. If any one were to suggest such a method as a new proposition it would be rejected as unworkable or even as insulting to intelligence. Nevertheless, that is the way of the world, and on the whole it works very well.

The object is to send the goods abroad and to get the payment home. Americans may sell to Englishmen and sell in sterling pounds, but they want dollars for their costs and profits because their accounts are in dollars. The reverse is just as true of British sales to America and of any country's sales to any other country. Books are kept in domestic currencies and there is no international currency or money of account. It makes no difference that foreign trade is usually on credit and for a longer maturity than is customary in domestic trade. All that is arranged through banks of discount. It is their business to turn future debts into present cash for a banker's profit which is fairly earned.

Last week there were cabled here protests at the profiteering implied in the discounts mentioned above, as though American traders or bankers profited by the discount on the British currency or the premium on gold. That is nonsense. If our bankers were making money like that they would not have suspended business as they did at times, refusing to take the bills of exchange which were offered except for collection. Usually the bankers of all nations will buy or sell on a narrow margin the bills of exchange arising from the exchanges of goods. Seldom do the banks buy or sell with their own money or even with their depositors' money. The exchange business almost finances itself. Approximately there are as many buyers as sellers of exchange. The one pays the other with the assistance of the bank, although both are strangers to each other or perhaps to the bank. The American sellers in pounds to British buyers want dollars. The British buyers in pounds must pay dollars. One hand washes the other. The bankers are merely honest brokers bringing strangers together to do services to other strangers, for the entire business is impersonal and without a trace of nationality, despite the national pride in currency and obstinate loyalty to inconvenient forms of it.

There are several reasons why this system has broken down. It never before has happened that there was such an accumulation on the same side of the ocean of such eager demand for everything, and on the other side of the ocean such accumulation of supplies of both the wanted goods and the credit necessary to move the goods. Usually there is an approach to balance of wants and credits, of buyers and sellers' checks. Under such normal conditions there is a free movement of gold to even the balances when they are uneven. Now the trade is unbalanced by billions, and there is little gold free except here to move. There is no question which is the world's primary market for both money and goods just now. But our primacy is troublesome. There are dangers in selling more than the buyers can pay for, or in consuming ourselves the excess above our wants which we fear to sell. The fabric of prices is so intricately woven that no thread can be unraveled without spoiling the entire pattern. There can be no stoppage of production and profits without stoppage of wages and disturbance of security markets, as well as goods markets. The front pages attest this beyond the escape of the man in the street. It is a question of bread and butter to him, even though he may think that he has nothing to do with the foreign exchanges, and cares nothing for the outlandish currencies which the newspapers persist in putting before his unwilling eyes. It is a serious mistake for him to make, and it would be well if it were made easier for him to understand a matter made unnecessarily puzzling, because no man or nation invented the methods, which just happened out of the adaptation of the methods of domestic to international trade. It is apparent that they are a misfit, a Babel of foreign currency languages, with only a few professional interpreters, the bankers.

How much simpler it would be if there were a financial international Esperanto, or universal money of account, useful in either domestic or international bookkeeping! That has been a dream of currency reformers for a generation, and was the actual practice of ages so long ago that the nations which practiced it are dead, and the art has been forgotten. It may be revived now that the need is greater than ever before. In the common phrase, "money talks." Unhappily, it talks too many languages, and never so many as since the Treaty of Versailles.