

Foreign Trade

and the

International Balance of Payments

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MOST of the new problems affecting Canada's foreign trade have an origin in the wide unbalance in Canadian trade with different countries and areas. This has taken on a new significance because of the deterioration in the exchange position of many of Canada's overseas customers. While basic elements in Canada's trading position as a whole have been strengthened with the development of the nation's industries and resources the structure upon which this trade rests has some insecure features arising out of the direction of trade and the wide disequilibrium which exists in Canada's trade with individual countries.

The general nature of this disequilibrium is well known. It springs from the predominance of the United States as a source of Canadian supply and the importance of markets overseas for many Canadian products. As a result Canada has characteristically had export balances in trade with overseas countries and chronic import balances in trade with the United States. The two kinds of disequilibrium, arising out of the predominant character of trade, are offsetting types and as long as foreign currencies were freely convertible there were no major obstacles to carrying on international trade

in these directions. The balances which arose out of this trade could be settled through multilateral settlements, claims on some countries being used to pay debts in other countries.

But the international background which permitted international commerce to be carried on under conditions of this kind was seriously altered during the war. Furthermore this bilateral disequilibrium has been augmented in the post-war period by the abnormal international conditions affecting both supply and demand. International efforts of an unprecedented character have been directed during the post-war years towards restoring more salutary conditions of trade and creating a better balance in future trade between nations. The objectives of cooperative undertakings like those under the European Recovery Program and the new international institutions have been directed towards this general end. Nevertheless the pressing exchange problems which continue despite these efforts have led to the introduction of widespread restrictions upon international trade by countries experiencing balance of payments difficulties. The Canadian dollar, like the United States dollar, has been among the scarce currencies in most overseas countries. The

balance of payments problem of the United Kingdom and the other countries of the sterling area has attracted special attention in recent months by the Tripartite Conferences in Washington and the devaluation of sterling. Problems of a comparable and related kind have also limited the ability of other countries throughout the world to carry on trade in a normal manner. There has grown up an intricate network of bilateral agreements and restrictive practices working against the efforts of Canadian exporters to sell abroad.

The bilateral disequilibrium in Canada's trade which has been so prominent in recent years is not a new development. It has been the unprecedented extent of the unbalanced gap and the lack of free convertibility of exchanges which have accentuated the problems of the Canadian balance of payments in the post-war world. These developments are well illustrated in the balance of payments between the United Kingdom and Canada.

An export balance was characteristic of Canadian trade with the United Kingdom before the recent war. This was increasing in the immediate pre-war years following the Ottawa agreements in 1932. It was also affected by British prosperity in the decade of the 1930's at a time when Canadian demands were subnormal. The export balance with the United Kingdom was \$237 million in 1937 compared with only \$36 million in 1929 if wheat shipped to continental Europe is deducted from recorded Canadian exports to the United Kingdom. The level of exports in that earlier period was less diversified than in 1937 and Canadian imports were higher. In contrast the Canadian export balance with the United Kingdom had increased to \$567 million in 1947, the highest surplus shown in post-war statements, on the balance of payments, exports being at a post-war peak and the volume of import shipments being still retarded.

Other current transactions than the merchandise trade between Canada and the United Kingdom had the effect of offsetting part of this export balance on commodity account in the pre-war period, whereas in the post-war period

this group of current transactions has acted to widen the gap in the British accounts with Canada. Before the war Canada had deficits on freight and shipping account, and income payments to the United Kingdom were greater than they have become recently as a result of war-time repatriations of Canadian securities held in the United Kingdom. Consequently the total current account with the United Kingdom, including all exchanges of goods and services which showed a Canadian deficit of about \$99 million in 1929, changed into a surplus of \$135 million in 1937 and has grown to a record post-war surplus of \$633 million in 1947. Since then the surplus has been reduced to \$488 million in 1948 with prospects of a much smaller balance in the future with reduced British purchases in Canada and increased Canadian imports from the United Kingdom. The dollar problems of the United Kingdom which led to the necessity of reducing this gap in that country's accounts with Canada need not be reviewed here. The Canadian loan of \$1,250 million to the United Kingdom was a major measure designed to cover part of this gap in the balance of payments. By the end of 1949 \$1,135 million of this had been drawn, most of it in the years 1946 and 1947. The high degree of disequilibrium which continues is a reflection of the British dependence upon Canadian sources of supply for some important foods and raw materials even following numerous British curtailments in expenditures in Canada. (The problems of increasing British shipments of goods to Canada are considered at greater length elsewhere in this symposium.)

The patterns of trade with other Commonwealth countries and with other overseas countries also both give rise to a similar type of disequilibrium as has been characteristic of trade with the United Kingdom in recent decades. Although the disequilibrium is not as great as with the United Kingdom the export balance has likewise been many times the size of those typical of the years before the war. In 1948 the excess of exports over imports in Canada's trade with coun-

tries of the sterling area other than the United Kingdom was \$101 million compared with an export balance of \$21 million with much the same group of countries in 1937. In the peak post-war year of 1947 the corresponding balance was \$206 million in trade with this area. The other current transactions including freight and shipping receipts also give rise to net receipts by Canada, further augmenting the gap in the current account of all exchanges of goods and services which in 1947 was \$241 million and in 1948 was \$129 million. Canada became a more important source of supply for this group of countries in the early post-war years than had ever been the case before. The rapid growth in the export balance has been influenced chiefly by this expansion in Canadian exports to this currency area which is the more variable element in the accounts. The increases in Canadian imports from other Commonwealth countries have been retarded by insufficient supplies of many commodities which Canada normally imports. In other cases where supply was not a deterrent Canadian purchases were limited by the level of requirements.

Because of the financial relations of this group of sterling area countries with the United Kingdom the gap in their trade with Canada has materially increased the needs of the United Kingdom for Canadian dollars. Consequently changes in Britain's financial position have had direct effects upon the extent to which this group of countries could make expenditures in Canada. Following the rapid use of the Canadian and American loans in 1947 and the general deterioration in Britain's dollar resources which became acute in the summer of that year, this group of countries was obliged to reimpose or extend restrictions upon expenditures in Canada as well as in the United States. As a result purchases of Canadian goods in 1948 by these countries were sharply reduced. Further declines in purchases of most types of manufactured goods continued in 1949, only being offset by abnormal purchases of wheat and railway equipment by several of the Dominions.

II

IN the case of trade with overseas countries other than those belonging to the sterling area there has likewise been a very great growth in the balance of exports. While this has been declining from the peaks of 1945 and 1946 the balance of Canadian exports to this group of countries was still \$305 million in 1947 compared with \$39 million in 1937. But in 1948 the balance was sharply reduced to \$204 million followed by further declines in 1949. Other current transactions with these countries also increased Canada's credit balance which was \$346 million in 1947 and \$256 million in 1948 when all exchanges of goods and services are taken into account. Most of this great post-war expansion has occurred in exports to Europe. Influencing the unprecedented level of these have been shipments of UNRRA and post-UNRRA relief contributed by Canada as well as goods paid for by Canadian export credit loans. In the post-war period the contributions of official relief have amounted to some \$150 million. Net drawings on export credit loans extended during the transitional period to assist and develop Canadian exports amounted to \$528 million. Most of this assistance was extended to European countries with minor amounts to countries in Asia.

It is apparent, however, that the exceptionally high level of exports to regions like Europe and Asia were swollen by abnormal demands arising out of exceptional shortages and reconstruction needs of the early post-war years. The level of Canadian trade continuing in the last few years has been affected by the dollar shortages of these countries which in many respects are comparable to those of the United Kingdom. Purchases in Canada have consequently been curtailed because of currency and other balance of payments problems abroad as the gap in the accounts has not yet been materially reduced by increases in commodity shipments by these countries to Canada. The Canadian export credit loans had expired by the end of 1948 and subsequent

balances of trade have had to be met by transfers to Canada of convertible exchange. Trade with this area has customarily been a significant source of convertible exchange which Canada needed in meeting current deficits with the United States. This trade yielded substantial amounts of convertible exchange even during the earlier post-war years when a large part of exports was financed by export credits and in many years before the recent war the export balances with other foreign countries were greater than Canada's deficit with the United States. As a group these countries have been a traditional outlet for many of the surplus commodities produced in Canada.

Canada's United States dollar problem has arisen from the reduced amounts of receipts of convertible exchange from all overseas countries in comparison with the enlarged size of Canada's current deficit with the United States. The potential amount of these receipts was materially reduced in years like 1946 and 1947 when large amounts of Canadian exports were financed by Canadian loans, export credits, and contributions of relief. Although Canada had a substantial export balance in those years, and somewhat smaller balances from all current exchanges of goods and services, there were sharp reductions in Canada's official reserves of gold and United States dollars from current transactions. This situation arose from the short fall of receipts of convertible exchange (which were reduced by the loans and contributions) and the enlarged Canadian deficit with the United States. While Canada's over-all current account with all countries showed a surplus a substantial part of the exports producing this surplus was financed by the Canadian Government and consequently did not produce convertible exchange.

While the amount of exports financed by loans has been greatly reduced, being the \$120 million drawn by the United Kingdom in 1949, the size of Canada's current account surplus has fallen sharply from the level of \$453 million to which it had recovered in 1948. A further reduction in the current account balance in 1949 has been influenced particularly by

the decline in the size of the export surplus. In the early part of the year appreciable gains in the volume of imports were shown at a time when the volume of exports was declining. In addition there has been a sharp decline in the balance of receipts on tourist account due to the rapid growth in Canadian travel expenditures abroad and the trend in all other current transactions has also been unfavourable. The size of the current account surplus with all countries is of vital significance for Canada's exchange problem since this is a measure of the potential current receipts of convertible exchange when the amount of exports financed by loans is also taken into account. The declining trends in Canada's current account surpluses with overseas areas have already been pointed out. These trends have been due to increased Canadian purchases overseas as well as to reduced expenditures by overseas countries in Canada. The rising trend in Canada's current account deficit with the United States has also been a major contributor to the Canadian exchange problem.

III

CANADA'S balance of payments with the United States is influenced by a great variety of interrelationships between the two nations. The relative trends in economic activity in the two countries have decisive effects upon the current balance. But even with comparable conditions of prosperity in the two countries the volume of trade in both directions is normally large with an excess of Canadian imports over exports, a condition which seems almost chronic and expands with the volume of activity. This traditional unbalance is influenced by the distribution of resources in the two countries and their relative stages of development. Even with high incomes in the United States there are distinct limits to the commodities which that country buys in Canada, as the types of goods normally bought are not as widely distributed as is the case with Canadian imports from the United States. Canadian exports to that

country are highly concentrated in certain groups of primary products and special commodities like newsprint. Imports from the United States by Canada, on the other hand, cover almost all classes of a wide range of commodities produced in the United States. Basic requirements, like fuel and raw materials, make up important parts of Canadian imports. But imports are also distributed over all types of manufactured goods, both consumers' goods and producers' goods, and many of the imports are in the form of components for further manufacture in Canada. This customary deficit on commodity account is enlarged when Canadian prosperity continues at a time when readjustments occur in United States activity as has been the case in 1949. The extent of the disequilibrium has also been widened abnormally in the post-war years by the scarcities which exist overseas for many commodities usually purchased from those areas by Canada.

Other current transactions with the United States also contribute substantial amounts to the current deficit. The chief of these making for larger payments are the large income payments by Canada servicing investments of United States capital in Canada. Interest payments on bonds have been large and in times of prosperity dividend remittances expand. Heavy payments are also made for inland and freight and for shipping services, a large part of which arises out of the movement of bulk commodities like fuel to Canada. Other interchanges of services likewise contribute to the deficit. The only major source of net income from services is the tourist trade. But while the expenditures of United States tourists in Canada are higher than in any other country the net travel account between the two countries does not yield a balance of receipts anything like equal to the heavy expenditures in Canada. This is because of the very large amount of Canadian travel expenditures in the United States which on a per capita basis are much larger than those arising from the opposite movement of Americans to Canada. The remaining source of receipts is Canada's production of gold which

has been relatively less important in the current account in recent years in comparison with the pre-war period.

During each of the last four years Canada's current deficit with the United States has been much larger than in any other earlier period and the fluctuations from one year to another have been very sharp. In 1947 the deficit was almost twice as large as in 1946, rising from \$607 million to \$1,135 million in comparison with a deficit of \$149 million in 1938. Influenced by the effects of restrictions introduced in the Emergency Exchange Conservation programme late in 1947 and by the sharp growth in exports to the United States, the current deficit in 1948 declined to \$401 million. But a considerable expansion again occurred in 1949 due to a combination of factors. The volume of imports rose while that of exports declined, reflecting opposite economic trends in the two countries in the earlier part of the year as well as some reduction in import restrictions and some improvements in the supply of commodities in the United States, particularly metal products. Further augmenting the current deficit in 1949 has been a growth in Canadian payments on income account and for other services, and a sharp decline in net receipts from travel expenditures due to the new high level of Canadian expenditures in the United States on travel. This dynamic character of the current account between Canada and the United States, even under the still extensive restriction programme introduced late in 1947, demonstrates the variable nature of this account and its contributions to the vulnerability of Canada's exchange position.

The broad characteristics of the Canadian balance of payments have been described above—the financial problems associated with the unusually large surpluses from trade with overseas countries and the uncontrollable nature of much of the disequilibrium which arises with the United States, combined with the basic strength exhibited by the Canadian balance of payments when transactions with all countries are taken into account. It is the special dependence upon an

international environment in which foreign balances may be settled which creates the paradox of the Canadian balance of payments in recent years. Despite the basic strength indicated by the continued existence of a current account surplus with all countries there is this vulnerability to the international environment and the importance to Canada of the international financial position of overseas customers. Efforts being made to reduce the opposite kinds of bilateral disequilibrium without impairing the volume of trade point to one of the chief means of overcoming the disadvantages of Canada's position. Related to these

are favourable effects to be anticipated from the basic developments in the natural resources of the country now under way which will do much to reduce the disequilibrium with the United States. Any international progress towards improving international financial relations which might be made in the future would also act towards reducing the vulnerability. A combination of the two trends, the reduction in bilateral disequilibrium and the restoration of a more salutary international environment, could greatly reduce the uncertainties which have been present in conditions existing in recent years.

