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The Fallacy of a Balanced Budget

By Major C. H. Douglas

A common cause of confusion to those unfamiliar with the technique of finance can be found in the excusable assumption that a statement which is true and obvious in regard to individual experience of money matters is equally true in regard to the money matters of a nation.

There are at least two assumptions made by those who argue in this way. The first is that the process by which a community obtains money is fundamentally similar to the process by which an individual obtains money. The second is the idea, alternatively, that money is limited in quantity by the laws of nature, or that it is always exactly equal in amount to the price values of the goods which it is supposed to represent.

Now, as a matter of fact, no one of these common assumptions is justified, as can easily be seen by anyone who will take the trouble to give the matter a little thought. All individuals obtain money by getting it from somebody else, i.e., so far as individuals are concerned, money is quite correctly defined as *a* medium of exchange (although not an invariable medium of exchange). But in the case of a sovereign community, this never is and never has been the case. Whether the power be delegated, as in the case of Great Britain to the Bank of England, or not, a sovereign community has the power of actually creating money--it is self-financing, a situation which in fact places the community and the individual in a position of technical opposition, the community and the individual always being on opposite sides of the ledger.

The first alternative of the second assumption is quite obviously not true if it be granted that a sovereign community has the power of creating money, and the second alternative assumption can, I think, be disproved with very little additional difficulty. Before attempting this disproof, however, it may be desirable to point out that the statement that the first essential of sound finance is that a country's budget must be balanced, that is to say, that all the expenditures made by government departments must be recovered from the public *in the same period of time,* i.e., at the same rate, that they are disbursed, depends absolutely for its soundness on the failure to disprove this contention.

A balanced national budget means, and can mean nothing else, than that all national expenditure is financed with what we may call "old money." A portion of this expenditure is distributed in government wages and salaries, much of which goes to the production of what we may call "intangibles," such as defence, organisation, education, and so forth, and a further portion in payment of the interest on outstanding loans. In regard to that portion which goes to the production of public works, the position would hardly seem to require argument.

Now in regard to the first portion of this, if the whole of it is recovered at the same rate at which it is distributed, it must be quite obvious that the assumption is made that there is an absolute equilibrium between production and consumption, and such an assumption is never justified. Leaving out of account the physical assets, many of them having many years of life, which are produced by a portion of government expenditure, it is undeniable that there is a constant increase in the real value of intangibles, such as better organization, better education, increased scope of intercommunication, utilisation of the possibilities of modern science, and many other bases of real credit, which means that every year's working carries forward into the succeeding year a considerable body of real values which would be quite correctly represented in a business by an increase of good will. In regard to the portion of the national budget commonly called the "consolidated fund," and the service of various loans, any examination of the destination of the greater part of this must make it obvious that it is re-invested and not spent upon the purchase of consumable goods. Any portion of it paid by industry, as such, must appear in the prices of consumable goods, since the producer-taxpayer must charge his taxation into the cost of his product if he is to remain in business. The portion of the taxation paid directly by the consumer means a correspondingly less body of effective demand against the goods for sale, or it means an increasing body of sales below cost, resulting inevitably in the bankruptcy of the producer. That all these causes operate to produce a lack of effective demand is obvious to anyone who will observe the "To Let" and "For Sale" notices which are our chief national exhibit.

To put the matter another way, a balanced national budget and a balanced budget of all the country is an arithmetical impossibility, even if every business disposed of its product at cost, but as the current theory of business is that it should be carried on at a profit, the proposition can only be made to function by each balanced business budget being paralleled by a corresponding loss in some other business. This loss is approximately the difference between price values produced and purchasing-power available to meet these values. This purchasing power includes not merely that relating to goods for sale but also payment for exports and other monies not distributed in respect of goods for sale in the home market; and these payments go some way to reduce the apparent loss.

The position disclosed by this examination is, in fact, similar to that disclosed by an examination of the price values which are produced in a manufacturing business in comparison with the amount of money available *at any moment* as a demand against these price values. There is always a body of price values against which there is no existing effective demand, but upon which those institutions which are in a position actually to create money [those comprising the banking system] are generally willing to do so *upon terms sufficiently satisfactory to themselves* [emphasis added]. As, however, this money is always loaned, and a price is charged for the loan, it is clear that the unbalancing process is cumulative. In periods of excessive capital production, financed by large creations of new money, this situation is not so noticeable, and is precisely similar to that produced by a budget balanced by loans instead of taxation.

The issue involved in this question of the balanced budget is precisely the same as that involved in the maintenance of the present price system, and can be clearly enough stated. It is that all improvements of process, together with the potential benefits of machine production, shall go to form a reserve of security against loans created by the financial system, and the public at large shall pay an increasing tribute to the financial system for their use. It is not a highly ethical situation, even if it could be made to work, but it cannot be made to work for reasons for which I have dealt with at some length elsewhere [***The Monopoly of Credit,*** etc.]. This is, perhaps, unfortunate, since it seems unlikely that our financial rulers can be made to appreciate that they are themselves the greatest, if not the only danger to the social system they control. Being, as apparently they are, determined upon suicide, we shall probably have to endure a reorganisation of a productive system which is quite satisfactory, in order to demonstrate that it is not the same thing as an immoral distribution system which its controllers do not even understand.

The above position was concisely summarized by Major Clifford Hugh Douglas in the following brief excerpt from a letter of advice (see ***The Alberta Experiment***) written from London to the Premier of Alberta and the Executive Council on the 24th of February, 1936:

THE HONOURABLE WILLIAM ABERHART, M.L.A., B.A.
Premier of Alberta, Edmonton, Alberta, Canada.

Strictly Confidential to Executive Council of Alberta

DEAR MR. ABERHART,

This seems to be a suitable occasion on which to emphasise the proposition that a Balanced Budget is quite inconsistent with the use of Social Credit [i.e., *Real* Credit--the ability to deliver goods and services "as, when and where required"] in the modern world, and is simply a statement in accounting figures that the progress of the country is stationary, i.e., that it consumes exactly what it produces, including capital assets. The result of the acceptance of this proposition is that all capital appreciation becomes quite automatically the property of those who create an issue of money [i.e., the banking system] and the necessary unbalancing of the Budget is covered by Debts.

C. H. Douglas
London, England

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