Available online at www.sciencedirect.com
ScienceDirect
Explorations in Economic History xx (2013) xxx–xxx
www.elsevier.com/locate/eeh

Defying Gravity: The 1932 Imperial Economic Conference and the Reorientation of Canadian Trade☆

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Received 6 August 2013

Abstract

In the wake of the Great Depression, the Canadian government embarked on a stunning reversal in its commercial policy. A key element of its response was the promotion of intra-imperial trade at the Imperial Economic Conference of 1932. This paper addresses whether or not Canada was able to defy gravity and divert trade flows towards other signatories at Ottawa. The results suggest that the conference was a failure from this perspective. Potential sources of this failure include unreasonable expectations about the likely reductions in trade costs and a neglect of key considerations related to certainty and credibility.

Keywords: Imperial Economic Conference; Interwar trade; Preferential trade agreements

1. Introduction

The collapse of international trade in the wake of the Global Financial Crisis has led to fundamental reconsiderations of the structure and sustainability of the global economy. Although the sources of this trade bust are still debated, changes in the composition of output and trade, the role of inventories, and issues related to trade credit and the spread of cross-border supply chains are all clearly implicated (cf. Alessandria et al., 2010; Bems et al., 2010; Chor and Manova, 2012; Eaton et al., 2010; Levchenko et al., 2010). What has been less contentious is the appropriate response of policymakers with respect to commercial policy. In part, a firm and long-standing commitment to the cause of free trade ensured the quick recovery of international trade volumes to pre-crisis highs. This recent experience, of course, comes in marked contrast to that of the interwar period.

In this paper, Canada's engagement with international markets during the interwar period is explored.

☆ This paper was written while the author was a visitor at UCLA, and he thanks the Department of Economics for its hospitality. He also thanks the paper's editor and referees along with Jeremy Atack, Jen Baggs, Mario Crucini, Krishna Pendakur, Leah Platt Boustan, and Almos Tassonyi for suggestions and appreciates the comments from seminars at Arizona, ANU, Caltech, Carleton, La Trobe, LSE, New South Wales, Queen's, Toronto, UC Merced, Vanderbilt, Waterloo, and Western Ontario as well as from the 2011 All-UC Group/Caltech/Huntington Conference, the 2011 Canadian Network in Economic History meetings, the 2011 European Historical Economics Society meetings, the 2011 NBER DAE Summer Institute, and the 2011 Rocky Mountain Empirical Trade meetings. Finally, the author gratefully acknowledges the Social Science and Humanities Research Council of Canada for research support.

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0014-4983/$ - see front matter
http://dx.doi.org/10.1016/j.eeh.2013.12.002

In particular, the implications of the Canadian policy response in the wake of the Great Depression and the erection of foreign trade barriers, most notably in the form of Smoot-Hawley in the United States, are considered. Apart from home-grown tariff legislation, a key element of the Canadian response was the promotion of intra-imperial trade at the Imperial Economic (or Ottawa) Conference of 1932. This represented a stunning reversal in Canadian commercial policy which had previously emphasized maintaining continued access to US goods and markets. Thus, drawing on a well-established literature in international trade, the primary question which this paper seeks to address is whether or not Canadian trade was able to defy gravity–that is, defy the attractive force for Canadian exports and imports exerted by the economic mass and geographic proximity of the US–and divert trade flows towards other signatories at Ottawa in 1932.

The choice of Canada as the observational unit is motivated by a number of reasons. First is the sheer size of the Canadian–US border trade and its long-running preeminence. By 1927, Canada had surpassed the United Kingdom as the United State's largest trading partner (Jacks et al., 2011), a position it holds into the present day and which represents the largest bilateral trading relationship over the past 80 years.[1] What is more, this single border registered roughly 5% of all world trade in the interwar period. At the same time, the Canadian response to the combined pressures of the Great Depression in general and Smoot–Hawley in particular was to embark on its most pronounced reversal in commercial policy to date. Documenting the evolution of this vital trading relationship is, thus, important not only for our understanding of history, but also of the context of commercial policy in the present.

Second, Canada provides insight into the dilemma facing small- and medium-sized economies which are dominated by a few–generally large and proximate–trading partners. Historically, we can place areas like Australasia, the Low and Nordic Countries, and Latin America in this category. In the contemporary setting, this may become more binding for the East Asian Tigers, Japan, and–again–Australasia with the rise of China as a dominant player in international trade. The particularly Canadian experience explored here serves to highlight the tension between the benefits of integration which are often hard to identify and the more readily felt costs which are borne in the face of significant reversals in a dominant trading partner's commercial policy and economic fortunes. Such costs may come in the form of the loss of electoral support for political parties which have previously championed the cause of further integration or in the form of the loss of output and productivity attendant on the misallocation of capital in the presence of intermediate inputs and integrated economies (Bond et al., 2013). In any case, the topic of diversifying trade partners uncannily emerges any time progress along these lines falters. Unfortunately, little of the debate surrounding this decades-long issue addresses the feasibility–as opposed to the desirability–of such a re-orientation of trade flows. This paper represents a step forward in this direction.

Finally and more generally, the experience of commercial policy in the interwar period has proven to be one of the few decisive lessons learned from economic history. A consensus has emerged within the economics profession, across the political spectrum, and more haltingly–but more surprisingly–throughout the electorate. This consensus holds that while broad-based protectionism may perhaps bolster the domestic macroeconomy in its direct effects, indirectly it will almost certainly raise the counter-protectionist ire of other nations, suggesting little is likely to be won in following this path. Additionally, the experience of the interwar with respect to unilateral changes in commercial policy initiated the pronounced move towards multilateralism in the post-World War II period (Baldwin, 2009; Snyder, 1940). Therefore, a further consideration of the policy disaster of the interwar may contribute to a wider appreciation of this consensus view.

Section 2 below sets the scene leading up to the events surrounding the period from 1929 to 1932. It reveals that the Canadian economy was highly exposed to changes in commercial and economic conditions in the United States and, thus, unprepared for the Great Depression. This fact might help explain why the Canadian economy had not regained the economic ground lost during the depression even as late as 1939. Sections 3 through 5 represent the main contribution of the paper. Canadian trade statistics are particularly rich for this period and allow us to explore the effects of

[1] This blanket statement has a few notable exceptions when the United Kingdom–United States bilateral trading relationship reasserted itself. These came in 1933 when Canadian–US commercial and diplomatic relations where close to their nadir and the war years of 1940 through 1944 when the US engaged in an unusually large and highly unrepresentative export trade with the UK. Putting things in further perspective, the volume of Canadian–US trade still held a commanding 15% lead on the runner-up, namely China and the US, in 2012.

Please cite this article as: Jacks, D.S., Defying Gravity: The 1932 Imperial Economic Conference and the Reorientation of Canadian Trade, Explor. Econ. Hist. (2013), http://dx.doi.org/10.1016/j.eeh.2013.12.002