A two page brief summary of 14 page essay: **"How Imbalanced Domestic Trade" disrupts a closed economy."**: www.questioneconomics.com/fmpc/#beginfmc

Ralph Hiesey, August 12, 2025

What money is supposed to do: In every human culture people make things and services that they want to share with others. This is much more efficient, compared with having everyone "flying solo" where everyone produces stuff, but doing all the work only for themselves.

I believe the most important task of economics is to define fair rules for exchanging goods/services in an economy. There are different ways to allocate this division of labor. In a small group of people, like a family, a common way is the communist method: from each according to his ability, and to each according to his need. This usually works well only when a few people live together and know each other. When people share work with many others they usually use money to keep track of equitable exchange.

Money works well for trading in (even a closed) economy when each agent consistently purchases goods/services of about equal value to what that same agent produces in goods/services during a similar monthly period. However a serious monetary balance problem can develop in a modern economy when, because of greatly increasing productivity, some agents ("over-producers") produce much more value than they purchase over time, thus increasing their savings. That's how trade imbalance can occur in a closed economy. In an economy with fixed amount of money, to consume the extra product they produced requires that there be other agents, over-consumers, that do the opposite: to consume the extra goods made by the over-producers. The effect of this imbalance is to reduce income to over-consumers. Reduced income for over-consumers reduces their ability to consume, which reduces GDP for the entire economy, and reduces the ability to distribute all produced goods/services. This also increases income inequality among agents.

The purpose of this essay is to study the problem that occurs when highly productive, highly capitalized economies require fewer production workers, leaving less demand for workers who need jobs to earn money to maintain aggregate demand for products/services. Since at least 1980, higher productivity has reduced incomes for the bottom 60% compared to those at the top 10%.

Frequently past economies that used money exchange experienced recessions, crashes, or depressions. These periodic events puzzled economists because they occurred even with plenty of goods for sale. Macroeconomics was a part of economics that came into prominence in the 1930's to try to understand why these happened, and if possible to correct this. By far the event most influential to explain this was a textbook called "Economics" by Paul Samuelson that was based on British economist J. M. Keynes' ideas. Its first edition was published in 1948. This influential textbook was revised many times for over four decades afterwords.

This essay does not take anything away from the insight of Samuelson or Keynes. However it suggests the importance of knowing what I have defined *Internal trade imbalance* for a *closed* economy and have added that to Keynes' argument, which gives important additional economic insight. The argument is virtually the same as the explanation for how *international trade imbalance* causes money to shift from net importers to net exporters.

In the 16th-18th centuries some countries with international trade deliberately caused "trade imbalance" by exporting more value than they imported to capture a greater quantity of reserves of gold and silver from other countries. Money/gold/silver was transferred from net importing countries into net exporting countries. Eventually this reduced trade as money/reserves moved away from importing countries. It resulted in much war and conflict when countries wanted to increase their stash of silver and gold. This practice was eventually discouraged by economists, as it became understood as a zero sum game for obtaining money wealth.

Perhaps surprisingly, this essay shows that a closed economy can also be damaged by *trade imbalance*. Agents who are *net over-producers*—(like net exporters) accumulate money when selling to *net over-consumers* (net importers). Net over-producers accumulate savings but *over-consumers* must spend down savings—or go into debt. This generates inequality of income and wealth that has been increasingly evident in today's highly productive economies.

To compensate trade imbalance in a closed economy, methods are needed to recycle money back to importers from exporters. This is recognized for international trade through its *capital account*. But its importance is not now explicitly recognized for national economies. Such compensating institutions have necessarily evolved because otherwise a capitalistic economy could not work

S**ection 5 of this essay describes domestic economic institutions** that have historically developed to rebalance—analogous to those in international trade that are tracked by a country's *capital account*. Examples of domestic institutions that recycle money from *exporters* to *importers*: taxes taken from *exporters* to provide government services for citizens some of whom are *importers*. Social Security transfers money from *exporters* to *importers*. Credit cards that loan money from *exporters* to *importers*. Legislated minimum wages for *importers*. Government deficit spending using Treasury bonds sold to *exporters*. Earned income tax credits. Unemployment benefits. Monetary and fiscal policy also has an important role.

Such institutions must adequately compensate *internal trade imbalance*—but not over balance, to recycle money to purchase produced goods. Over balance could produce inflation. Trade balance benefits not only *importers* but also *exporters* who will find more demand for their products.

Although it took economists a few hundred years to recognize the problem of trade imbalance for **international trade**, this insight for a **non international trading** economy has not yet been understood as an important cause of increasing income and wealth inequality.

This awareness of trade balance could Improve much government economic and tax policy. It shows the foolishness of cutting taxes for the rich who already spend much less than they save. It demonstrates the need to tax those with high wealth who hold high amounts of precautionary money at low monetary velocity that has been effectively taken out of circulation. A correct amount of socialism can help balance an economy to improve goods distribution and increase GDP, but overdoing it could cause excessive inflation. Moderate inflation can be beneficial by reducing burden of interest payments to taxpayers from long past government debt.

Government deficit spending and t**ransfer payments such as Social Security** can be quite helpful to an economy. **Unlike what is popularly believed,** both can result in **raising** real GDP for everyone **if not done to excess**—more effectively recycling money by putting an economy into better trade balance.   Shows why the German *Schuldenbremse* "debt brake" has unwisely limited helpful government borrowing.