BANK FOR INTERNATIONAL SETTLEMENTS

NINETEENTH ANNUAL REPORT

1st APRIL 1948 — 31st MARCH 1949

BASLE

13th June 1949

BANK FOR INTERNATIONAL SETTLEMENTS, BASLE

NINETEENTH ANNUAL REPORT

ERRATA:

Page 17: in the table, a footnote reference (²) should be added to the heading "Direct aid";
in the column "Countries", instead of: Germany (²), read: Germany (³).

Page 60: in the table,
instead of: Raw materials and imported products,
read: Raw materials and semi-finished goods.

Page 66: table – "United Kingdom: Gross national product", under "Resources",
instead of: Provision for depreciation and maintenance of buildings,
read: Provision for depreciation and maintenance

paragraph 2, line 2,
instead of: ... personal consumption rose only by about £320 million and government consumption is found to have declined by £165 million ...
read: ... personal consumption rose only by about £540 million and government consumption is found to have declined by £155 million ...

paragraph 2, line 5,
instead of: Economic Survey for 1948 ...
read: Economic Survey for 1949 ...

Page 107: table – "Wage increases", add to "France", as footnote (¹),
(¹) Figures for 1947.

table – "Amount of wheat covered by the Wheat Agreement",
United States, in millions of bushels,
instead of: 68, read: 168.

Page 108: line 4,
instead of: ... delivered as follows by the exporting countries,
read: ... delivered by the exporting countries as shown in the table on the preceding page.

Page 110: in the table – "Terms of trade", the heading should be corrected as follows:

Year	Average Values of		Terms of Trade
	Imports	U.K. Exports	

Page 124: paragraph 5, line 1,
instead of: DM 3.33 = $ 1,
read: RM 3.33 = $ 1.

Page 127: paragraph 1, line 5, and } instead of: Economic Survey for 1948,
Page 149: line 4, } read: Economic Survey for 1949.

Page 135: paragraph 3, line 1,
instead of: While with E.R.P. countries ...
read: As regards E.R.P. countries, ...

Page 156: last paragraph, line 5,
instead of: ... in unrefined gold which was not covered ...
read: ... in unrefined gold which was covered by the regulation ...

Page 162: table – "Discount rates of central banks", footnote (4),
instead of: In effect since 18th March 1949,
read: In effect since 22nd March 1949.

Page 166: table – "United States: Annual rate of turnover of total deposits", delete the sub-heading "in percentages".

Page 169: table – "France: Notes in circulation", for 1948,
instead of: 933, read: 988.
table – "Bank of France: Balance sheet", footnote,
instead of: Including over Fr. fcs 400 million ...
read: ... Fr. fcs 400 milliard ...

Page 177: paragraph 1, line 9,
instead of: 15 to 10 per cent ...
read: 15 to 12 per cent ...

Page 183: table – "Danish National Bank": item "Gold",
instead of: 82,729, read: 82.7;
70,568, 70.6;
70,438, 70.4;

Page 184: paragraph 2, line 2,
instead of: ... Sw.fcs 407 million ...
read: ... Sw.fcs 507 million ...

Page 214: paragraph 3, line 3,
instead of: ... 43.6 million ...
read: .... 210.3 million ...

Page 252: heading,
instead of: ... International Payments ...
read: ... Intra-European Payments ...

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ANNEXES

NINETEENTH ANNUAL REPORT

submitted to the

ANNUAL GENERAL MEETING

of the

BANK FOR INTERNATIONAL SETTLEMENTS

held at

Basle, 13th June 1949.

Gentlemen,

I have the honour to submit herewith the Annual Report of the Bank for International Settlements for the nineteenth financial year, which began on 1st April 1948 and ended 31st March 1949. The results of the year's business operations are set out in detail in the section from page 214 to page 222 together with a general review of the current activities of the Bank and an analysis of the balance sheet as at 31st March 1949.

The financial year closed with a surplus of 5,101,855.91 Swiss gold francs, of which 300,000 Swiss gold francs have been transferred to the account for exceptional costs of administration and the remaining 4,801,855.91 Swiss gold francs to the provision for contingencies. At the end of the previous financial year (on 31st March 1948), the greater part of the surplus for that year was transferred to a Special Suspense Account, which thus reached 13,547,201.77 Swiss gold francs. The amount on this account has now been amalgamated with other amounts set aside in earlier years to meet contingencies and, in the balance sheet as at 31st March 1949, the consolidated account is included in a new item, "Provision for Contingencies", which shows a total of 101,448,567.70 Swiss gold francs.

It was expressly stated in the Annual Report for the previous financial year that "wider fluctuations must be expected in the financial results of the Bank than in the years prior to the war, as a much smaller proportion of income is now derived from interest on investments". Had it not been for the fact that the Bank for International Settlements was able to develop its business relations with the various central banks and thus succeeded in increasing the volume of its individual transactions, it would have found it difficult, with rising costs, to arrive at the comparatively satisfactory results attained in the financial year under review. As it was, between the end of March 1948 and the end of March 1949, the total of the Bank's balance sheet rose from 555.8 to 722.5 million Swiss gold francs — mainly owing to an increase of 162.6 million Swiss gold francs in deposits received in currencies from central banks. This increase in the funds entrusted to the Bank for International Settlements is in itself a sign of a return to more normal conditions; and, in that way, it may be said to reflect the need here in Europe for an institution serving the various monetary authorities as a depository for funds and a source of short-term financing.

I. International Capital Movements and Grants in Aid.

With exchange control in force in almost all countries of the world (the United States and Switzerland being the outstanding exceptions) and with some control of capital issues imposed in almost every market, one of the shortcomings of the post-war monetary situation has been that, between the different countries, transfers of capital other than those officially arranged have been restricted in volume and limited to particular fields. As will be seen from the figures in the following pages, private investments abroad have been of real importance only when undertaken for special purposes (e. g. to develop valuable oil resources) or within special monetary areas (strengthening the ties between a European country and its overseas territories).

It should be remembered that, not only in the decade following the first world war, when exchange control, as we now conceive it, was unknown, but also in the latter half of the inter-war period, capital funds moved from one centre to another, in search of security (i. e. really to avoid a loss) or for the sake of speculative gains; the movements in question had at times a distinctly disturbing effect on the currency situation (even though their responsibility for currency changes has often been exaggerated, since the real causes — heavy budget deficits, too high costs — were largely of a more fundamental nature). One of the reasons advanced for the maintenance of exchange control after the second world war has been the plea that control was necessary to prevent a recurrence of unmanageable capital movements. Officially, the need for a control of transfers on capital account has been recognised: in the Articles of Agreement of the International Monetary Fund it is stipulated that, subject to certain temporary exceptions, "no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transactions", the emphasis on the world "current" signifying that there is no prohibition against control as regards capital transfers, another article specifically stating that "members may exercise such controls as are necessary to regulate international capital movements".

In practice, it has so far proved difficult to frame and apply a system of exchange control that does not stand in the way of desirable capital movements, one reason being that it is no easy matter to distinguish clearly, in the daily run of business, between capital movements, on the one hand, and current transactions, on the other. Sometimes one finds a tendency to overestimate the amounts involved in capital movements: it often happens that all purchases of foreign exchange outside the regular channels of the Control are referred to as flight of capital (see page 132), whereas, when foreign currencies are bought in parallel markets in order to import commodities for which no licence has been granted, this is obviously a transaction relating to foreign trade and thus falling within the current account of the balance of payments (there being no question of a transfer of capital). The somewhat arbitrary character of many of the interventions and prohibitions imposed by the Foreign Exchange Control cannot fail to have a cramping effect on such capital movements as are undoubtedly desirable. For the fact is that hindrance to ordinary capital movements is largely to be found in the circumstance that funds will not readily flow to a country which does not offer sufficient guarantees of monetary stability and from which the funds cannot be legally repatriated when required. Control encounters the same difficulty here as in other fields: at best, exchange control secures what it can actually manage to lay its hands on but, operating by prohibitions, it does not attract funds and there will, therefore, be few voluntary movements by which it can benefit. Between most markets there has been a failure to revive both the so-called equilibrating movements of a short-term character (which used to ease the strain of seasonal and other fluctuations in the supply of foreign exchange) and the long-term capital investments which have in the past been such an important aid in the economic development of the world as a whole.

There is, however, a growing realisation of the part that foreign investments and some of the other types of capital movements might play; and the various signs of activity in this field must be carefully watched.

United States government aid to foreign countries.

Period	Net unilateral transfers	Net outflow of long-term loans and investment	Net total
	in millions of U. S. dollars		
1945	6,640	841	7,481
1946	2,279	3,230	5,509
1947	1,812	6,891	8,703
1948	4,308	687	4,995
Total	15,039	11,649	26,688

Only two of the countries for which sufficiently comprehensive data are as yet available, viz. the United States and Canada, had in 1948 a surplus on the current account of their balances of payments permitting a net outflow of capital or a net reduction of foreign liabilities or a strengthening of monetary reserves. Even in the case of the United States capital transactions on private account did not correspond, either in 1947 or in 1948, to more than a fraction of the amounts going abroad through government grants and credits. On the whole, it may be said that U. S. aid makes up for the insufficiency of private movements of capital which for a number of reasons has characterised the post-war period. The table gives a comprehensive picture of all the assistance extended by the U. S. Government to foreign countries in the form of gifts (or "unilateral transfers") as well as long-term loans and investments from public funds.

All the four years 1945–48 were characterised by a heavy export surplus for the United States. In 1945 and the first half of 1946 this was financed mainly by unilateral transfers (lend-lease, UNRRA aid, etc.). In the latter year, however, the bulk of the financing began to be done in the form of foreign loans granted by the U.S. Government, and this mode of financing was even more widely used in 1947. But the funds thus made available proved insufficient (partly because of special difficulties — poor harvests, etc.), and in 1948 the United States again gave its assistance through unilateral transfers — in the first place, the E.R.P.

In the table below the U. S. government subscriptions to the capital resources of the International Bank for Reconstruction and Development and of the International Monetary Fund are shown as part of the "long-term loans and investments" for 1947; but the total thus received by the Bank and the Fund was not at the disposal of other countries in that year. If allowance is made for this circumstance, it will be found that the net U. S. government aid (grants and loans) was about $1 milliard less in 1948 than in 1947; moreover, the net dollar disbursements by the International Bank for Reconstruction and Development and the International Monetary Fund declined by about $400 million from 1947 to 1948.

United States government aid to foreign countries.

A. Unilateral transfers. (1)

Period	Straight lend-lease	UNRRA and post-UNRRA aid	Civilian supplies for occupied territories	Greek-Turkish aid	E. R. P.	Other government transfers (2)	Gross unilateral aid	Less reverse transfers (3)	Net unilateral transfers
	in millions of U.S. dollars								
1945	7,613	589	871	—	—	442	9,515	2,875	6,640
1946	209	1,524	539	—	—	245	2,517	238	2,279
1947	—	788	980	74	—	430	2,272	460	1,812
1948	—	84	1,263	349	1,867	1,073	4,636	328	4,308
Total . . .	7,822	2,985	3,653	423	1,867	2,190	18,940	3,901	15,039

B. Long-term loans and investments. (4)

Period	Lend-lease credits	Surplus property (5)	Export-Import Bank	Subscriptions to the International Bank	Subscriptions to the Monetary Fund	Loan to United Kingdom	Other	Total outflow	Inflow	Net outflow
	in millions of U.S. dollars									
1945	830	63	35	—	—	—	12	940	99	841
1946	600	841	945	317	5	600	12	3,320	90	3,230
1947	2	274	796	318	2,745	2,850	80	7,065	174	6,891
1948	—	249	453	—	—	300	21	1,023	336	687
Total . . .	1,432	1,427	2,229	635	2,750	3,750	125	12,348	699	11,649

(1) Not including net private payments: viz. 1945: $ 473 million; 1946: $ 598 million; 1947: $ 568 million; 1948: $ 603 million.
(2) Including interim aid to France, Italy and Austria, the Chinese aid program, war damage payments, grants to the International Refugee Organisation and other transfers.
(3) Including lend-lease settlements.
(4) Not including net private outflow; viz. 1945: $ 454 million; 1946: $ 26 million; 1947: $ 744 million; 1948: $ 761 million.
(5) Including ship sales.

But this was not the only decline in the dollar resources available to other countries. During 1947, the countries in question financed about $4.5 milliard of their purchases in the United States from their own monetary reserves; in 1948, purchases financed from these sources shrank to about $860 million.

To meet the resulting total decline of about \$5 milliard in their dollar supplies, the other countries increased their exports to the United States by about \$2 milliard and reduced their purchases in the United States by about \$3 milliard — which represents a considerable reduction in the trade deficit of the rest of the world in relation to the United States. In commenting on these figures, the Survey of Current Business (for March 1949) issued by the U. S. Department of Commerce expressed the opinion that such a "result could not have been achieved without considerable progress in foreign economic recovery and the continued high level of business activity in this country" (i.e. the United States).

If attention is concentrated on the movements of capital (as distinct from grants and other unilateral transfers), the following table shows the results of such movements during the years 1947–48.

Movements of long-term capital to and from the United States.

Items	1947	1948
	in millions of U. S. dollars	
Movement of U.S.-owned capital:		
Government funds:		
Outflow	7,065	1,023
Inflow	174	336
Net outflow of government long-term capital	6,891	687
Private funds:		
Outflow	1,600	1,300
Inflow	856	539
Net outflow of private long-term capital	744	761
Movement of foreign capital invested in the United States:		
Outflow	164	215
Inflow	58	70
Net outflow of foreign capital invested in the United States	106	145
Total net outflow of capital	7,741	1,593

Note: As shown in the table, net foreign investments in the United States were reduced by \$ 106 million in 1947 and \$145 million in 1948. It is true that for most countries the existing control of foreign exchange prevents capital movements to the United States; but, even in relation to countries where movements are free (e. g. Switzerland), withdrawals have exceeded new investments in the United States.

As compared with the effective outflow, in grants and loans, of government funds from the United States (about \$6 milliard in 1947 and \$5 milliard in 1948), the net outflow of private long-term capital (at about \$750 million for each of these years) represents less than 15 per cent. of the total outward movement of funds. Nevertheless, the net outflow of private long-term capital in 1947 and 1948 compares favourably with the magnitude of such capital investments in the period before the second world war (when first the great depression and then fears of war had a cramping effect), but it was exceeded by the volume in 1922 and in the years 1926–28.

In 1947 not less than 70 per cent. of the net outflow of private long-term capital from the United States represented direct investments in the petroleum industry in Latin America and the Middle East. In that year direct private investments by the United States were primarily in the following areas: Latin America (\$408 million); the Middle East and Africa (\$115 million); the Far East (\$57.5 million); Europe (\$54 million) and Canada and Newfoundland (\$2 million).

The net outflow of private long-term capital in 1948 included a Canadian Government loan of $150 million taken up by a group of insurance companies in the United States.

For Canada this loan subscribed in the United States was not the only credit item on the country's capital account with other countries in 1948; during the year there was an inflow of capital to an estimated amount of Can.$152 million, mainly from the United States.* To the extent of Can.$68 million this represented direct investments in Canadian property and businesses (as distinct from portfolio investments in public issues of Canadian securities and various forms of short-term capital movements). It may, moreover, be mentioned that the book value of U. S. direct investments already existing in Canada is estimated to have risen in recent years by some Can.$115–125 million a year. The Foreign Exchange Control Board of Canada in its annual report for 1948 explains that

"inflows for direct investment arise out of the decisions of non-resident investors to build factories or open mines or drill oil wells, etc. in Canada. Such inflows therefore contribute directly to, and are reflections of, the physical development of Canada's natural resources. They generally involve, moreover, the provision of experience and 'know-how' by the non-resident investors. In this way, foreign skills and techniques supplement foreign risk-capital in the direct investment field.

Decisions by non-residents to undertake direct investments in Canada are generally based on long-term expectations. The physical assets produced or acquired by the capital inflow are likely to be much less liquid than marketable securities. Direct investments are therefore customarily not undertaken unless they are viewed as more or less permanent. Those who are in search of liquidity or who are influenced by speculative considerations choose some other form of investment."

Canada: Balance of payments.

Items	1947	1948
	in millions of Can. dollars	
Current Account in relation to:		
United States	— 1,135	— 401
Sterling area	+ 874	+ 617
Other countries	+ 346	+ 256
Balance	+ 85	+ 472
Adjust: Contributions of official relief	— 38	— 19
Balance on current account	+ 47	+ 453
Capital Account:		
Loans to the United Kingdom and other governments	— 570	— 142
Subscription to International Monetary Fund	— 74	—
Government of Canada — borrowing in the United States	—	+ 150
Other net capital movements (1)	— 146	+ 35
Balance on capital account	— 790	+ 43
Balance on current and capital accounts	— 743	+ 496
corresponding to the change in: Canada's official holdings of gold and U.S. dollars (2)	— 743	+ 496

(1) Excluding change in Canada's official holdings of gold and U.S. dollars.

(2) The total of Canada's holdings of gold and U.S. dollars was:

End of year	Gold	U.S. dollars	Total
	in millions of U.S. dollars		
1945	354	1,154	1,508
1946	536	709	1,245
1947	287	215	502
1948	401	597	998

* This inflow of capital and various other capital movements mentioned in the text are not specified in the table, where they are included in the item "other net capital movements".

The proceeds of the loan subscribed in the United States and the inflow of capital were sufficient to meet the amounts needed for retirements of Canadian securities held abroad (about Can.\$130 million) and for new loans and credits to the amount of Can.\$126 million (net) granted to the United Kingdom and other governments.

As shown by the table, Canada's official reserves in gold and U.S. dollars increased in 1948 by slightly more than the surplus on the current account of the balance of payments. This would not have been possible had it not been for "the important and helpful part played by the European Recovery Program, which went into effect in April 1948, in preventing a severe contraction in the level of our exports to countries participating in this Program and in maintaining our receipts of convertible exchange from our European trade", to quote the report of the Foreign Exchange Control Board.

Where a net outflow of funds has occurred, it naturally shows itself as a surplus on the current account of the balances of payments of the capital-exporting countries; capital funds may have left other countries too, but such outflows must then have been counterbalanced by foreign grants and credits or the use of the country's own gold and foreign exchange reserves. There have been large-scale movements within the sterling area and some of these movements have been essentially of a speculative character in that they have been unconnected with the financing of any particular business activity. The movement of funds to South Africa would seem to have been largely of this character: the net inflow of capital in the years 1946 and 1947 and the first quarter of 1948 is estimated at £SA150 million (a sum equal to two-fifths of the total amount of capital imported between 1870 and 1936; but commodity prices were then lower than in recent years). Much of the capital thus imported was exported again in the three last quarters of 1948.

It is well to remember that, when capital movements are said to be "of a speculative character" in the sense indicated in the text, they may simply reflect a desire on the part of the owner to diversify his capital investments. But, if there are many who want to make the same change in their investments, the resulting flow may, in the aggregate, create difficulties of a monetary character. And transfers of funds not followed by actual investments may appear definitely undesirable if they exceed certain limits. Inside the sterling area various steps have been taken to put a brake on untrammelled movements, in particular of so-called "hot money". In March 1948 an exchange control order was issued in the Union of South Africa banning the acceptance of deposits from other countries in the sterling area unless the depositor in question could prove that the money was needed for productive purposes within the Union. As a further step, South Africans were directed to invest at once any money received from abroad or to return it within thirty days; and on 5th November 1948 new exchange and import control regulations were issued by the Union Government to preserve the country's foreign exchange resources and gold reserves.

In Australia, no special regulations were enforced with regard to capital movements, but in April 1948 the Prime Minister issued a warning against the use of the Commonwealth as a refuge for "hot money", pointing out that, according to provisions already in force, such money could not be withdrawn from Australia without official permit; the Minister for Post-war Reconstruction estimated in the autumn of 1948 that amounts equal to some £A 50 million had either entered the Australian market or were seeking to do so.

The somewhat speculative transfers of funds to and from South Africa and Australia have attracted a great deal of attention but they constituted only a part of the transfers of funds from and to the United Kingdom — a country which, both in 1947 and in 1948, increased its external capital assets and reduced its sterling liabilities (the main figures being given in the "Economic Survey for 1949", which was published in London in March 1949). Since there was in both 1947 and 1948 a deficit on the current account of the British balance of payments, the overseas investments and the reduction of sterling liabilities were met by utilisation of gold and dollar resources obtained from credits, grants, monetary reserves, etc. (Some of the data for 1948 are still provisional.)

Thus the United Kingdom increased its external capital assets and reduced its sterling liabilities to the tune of about £400 million in 1947 and £300 million in 1948. The following table shows how these amounts, as well as the deficit on current account in the balance of payments, were covered by available resources in gold and dollars.

United Kingdom: Changes in external capital assets and in sterling liabilities.
Increases (+) and decreases (—).

Items	1947	1948
	in millions of £ sterling	
Changes in external capital assets* of the United Kingdom:		
in the non-sterling area	+ 73	— 100
in the sterling area	+ 179	+ 192
Net change	+ 252	+ 92
Changes in sterling liabilities:		
in relation to the non-sterling area	+ 3	— 246
in relation to the sterling area	— 145	+ 35
Net change	— 142	— 211
Increase in external assets *plus* decrease in liabilities	394	303

* Assets other than holdings of gold and dollars.

Of the gold and dollars obtained from foreign credits, monetary reserves, etc., over 60 per cent. was required in 1947 to cover the current deficit in the balance of payments, which meant that less than 40 per cent. went to build up external capital assets and reduce the amount of sterling liabilities. In 1948, however, the percentages were more than reversed: less than 30 per cent. of the available resources in gold and dollars was absorbed by the current

United Kingdom:
Settlement of the gold and dollar deficit.

Items	1947	1948
	In millions of £ sterling	
Increase in external capital assets plus decrease in sterling liabilities (as in the preceding table)	394	303
Deficit on current account in the balance of payments of the United Kingdom	630	120
Total deficit to be covered in gold and dollars	1,024	423
These deficits were covered by:		
Drawing on United States and Canadian credits	812	87
Drawing on International Monetary Fund	60	32
South African gold loan	—	80
Marshall aid	—	169
Use of gold and dollar holdings	152	55
Total resources used to cover the above deficits	1,024	423

Note: This table includes the net figures for the whole sterling area and, inter alia, £17 million drawn by India on the International Monetary Fund. Since, however, the net transactions in gold and dollars are generally reflected in the amount of sterling liabilities of the United Kingdom, the figures in the table give an approximately correct impression of the changes in the position of the United Kingdom itself.

deficit, over 70 per cent. being devoted to strengthening the external capital position. The increase in external capital assets is mostly made up of investments in British colonies and other parts of the Commonwealth, the Economic Survey stressing that "this is an indispensable element in the programme for developing new sources of supply upon which our ultimate hope of solving the dollar problem is largely based"; and, as a result of the strengthening of the financial position in relation to countries which hold balances of sterling, the Survey thinks it will be less likely that in future these countries "will be able to draw gold and dollars from us; indeed, the significant improvement which has taken place in the position of sterling in the world's financial centres has been one of the most striking developments of the last year".

The Survey does not differentiate between the transfers of capital on government and on private account. It is known, however, that a considerable part of the overseas investments took the form of establishing subsidiary companies or expanding already established firms, mostly in sterling-area countries, the financial development going together with an emigration of manual workers and other staff.

France, too, has in recent years made substantial investments in its overseas territories, although the amounts involved cannot be exactly stated. Whereas in 1913 commodity exports from Metropolitan France to these territories were only one-eighth of the country's total exports, in 1948 they amounted to nearly one-half, while French imports from overseas territories rose during the same period from one-tenth to over one-quarter of total imports. Exports have thus risen more than imports, partly as a result of the contribution made by the mother country to the post-war reconstruction of the various territories. In the French balance of payments the current deficit of the French overseas territories (for which Metropolitan France is liable) was equivalent to $162 million in 1947 and $190 million in 1948, but this did not all correspond to capital investment in the territories in question, a part being, for instance, attributable to special requirements in Indo-China.

Fairly substantial capital movements of a private nature would seem to have occurred in the form of repatriation of funds to the Swiss market in amounts sufficient to cover, for the years 1947 and 1948, deficits of perhaps Sw.fcs 200–400 million on the current account of Switzerland's balance of payments and still enable the Swiss National Bank to increase its reserves of gold and foreign exchange. Swiss investors have subscribed to two Belgian loans of Sw.fcs 50 million each (one in 1947 and the other in 1948) but, otherwise, private foreign lending, both on short and on long-term account, has been at a low ebb, there having been a general tightening of the Swiss capital market in the course of 1948. Early in 1949, however, a marked change occurred, reflected in a fall in interest rates coincident with the reappearance of a surplus on the current account of the balance of payments. It is becoming increasingly realised that the Swiss market has, from current savings, a surplus of funds available for investment abroad (but only if suitable forms can be found; for people have not forgotten the heavy losses incurred on their previous foreign investments). It may be recalled that in the more favourable years in the nineteen-twenties the Swiss market used to export some Sw.fcs 400 million a year.

The loans issued for Belgian account on the Swiss market constitute an operation almost unique in the post-war period, since other issues of bonds have, practically without exception, been limited to transactions between countries belonging to the same monetary area — and then they have mostly been for the purpose of converting old loans. The preponderance of direct investments, after the war, in the movements of long-term capital between different countries (quite one-half of the net outflow of private capital from the United States being of this nature) reflects the investors' distrust (caused by defaults and depreciations) in the soundness of bond issues — a form of lending which accounted for the major part of the international long-term investments after the first world war. In 1947 the failure of the attempt to re-establish convertibility of sterling meant a further setback for the revival of private lending, and this, together with other circumstances, contributed to a most critical situation in the autumn of that year. Most governments in Europe had already drawn heavily on such foreign loans and credits as they had obtained and, more often than not, used up the greater part of their monetary reserves — and that at a time when they had to face the consequences of an exceptionally poor harvest (some 30 per cent. below normal), which rendered them all dependent on imports of foodstuffs.

Had it been necessary to reserve the available resources in gold and dollars to pay for priority imports of food, many countries would have been forced to make drastic cuts in their imports of raw materials, although such a curtailment might have led to a serious breakdown in the economic life of more than one country. These were the circumstances in which Marshall aid was made available, first in the form of Interim aid to France, Italy and Austria and then, in the course of 1948, as assistance to the various countries participating in the European Recovery Program. The United States had adopted a new formula for the granting of aid, in view of the fact that the Export-Import Bank had well-nigh exhausted its resources and little remained of the British loan, while the task in hand obviously went beyond the purposes of such institutions as the International Monetary Fund and the International Bank for Reconstruction and Development, since, in accordance with the provisions of their statutes regarding the conditions under which funds could be made available to borrowers and the repayment of such funds, they would have had to give full consideration to the economic situation of the countries concerned.

Much has been written about Marshall aid and the facts and figures are well known also in circles other than those directly concerned with its administration, but it is essential to keep the main data firmly in mind because of their importance for the financing of trade as well as from a general point of view.

The principle of stop-gap aid to France, Italy and Austria, for the purchase of essential commodities in the first quarter of 1948, was approved by Congress through the adoption of the "Foreign Aid Act" on 17th December 1947 and, a few days later, Congress appropriated $540 million, including $522 million for Interim aid and $18 million for assistance to China. The Interim aid was divided as follows:

France	$ 284	million
Italy	$ 181	,,
Austria	$ 57	,,
Total	$ 522	million

By the end of March a further $55 million was appropriated as Interim aid for France, Italy and Austria, to enable those countries to hold out until the European Recovery Program would become operative.

The European Recovery Program itself was enacted when the President of the United States affixed his signature on 3rd April 1948 to the "Foreign Assistance Act of 1948", of which Title I (under the name of "Economic Co-operation Act of 1948") laid down that assistance should be extended to the sixteen European countries having signed, on 22nd September 1947, the report of the Committee of European Economic Co-operation, to their Overseas Dependencies, to the Allied Zones of Occupation in Germany and to the Free Territory of Trieste.

By various decisions, Congress appropriated an amount of $5,000 million plus the transfer to the European Recovery Program (usually referred to as E.R.P.) of a carry-over of $10 million from the $55 million formerly allocated as a supplement to Interim aid. In addition, $1,300 million was appropriated for relief and recovery in occupied areas (including Japan);

$225 million for military assistance to Greece and Turkey; $35 million for the Emergency Children's Fund; $71 million for the International Refugee Organisation and $400 million for aid to China.

The $5,010 million of E.R.P. aid was made available for a period of fifteen months (from 1st April 1948 to 30th June 1949) but the "Foreign Assistance Act of 1948" empowered the President to ask for authority to use the whole amount by the end of March 1949 and to demand from Congress new appropriations for the second quarter of 1949. Upon the recommendation of the E.R.P. Administrator, the President determined that the entire sum would be required for the first twelve months of the Program and that he would ask for further appropriations covering the second quarter of 1949. The programme for the first year was, in fact, prepared on the supposition that $6,160 million would become available for the fifteen months up to the end of June 1949, the difference between that amount and $5,010 million — i.e. $1,150 million — being appropriated by Congress in April 1949.

The distribution of E.R.P. aid has passed through two different stages.

At first, when the Economic Co-operation Administration, "E.C.A." (the U. S. organisation set up to administer E.R.P. aid, with central offices in Washington and Paris and American Missions in each of the participating countries), started working in April 1948, there was no time to prepare a detailed programme, nor was the Organisation for European Economic Co-operation, "O.E.E.C." (the organisation of the participating countries, with an office in Paris), yet in a position to do so. But the need for aid was urgent and, in view of this, E.C.A. made a direct distribution of $1,337 million for the April–June quarter of 1948.

In the meantime O.E.E.C. was preparing its first annual programme for the fiscal year July 1948 to June 1949 and by mid-October 1948 it was able to submit a preliminary programme together with a suggested allocation of aid which, but for some minor changes, was accepted by E.C.A. The amount for the twelve months beginning 1st July 1948 was fixed at $4,756 million plus $67 million for administrative and other expenses. The primary distribution of E.R.P. aid was made on the basis of the estimated deficits on the current accounts of the balances of payments of the participating countries in relation to the western hemisphere, i.e. the dollar area. While the amounts thus made available would enable the participating countries to pay for their imports from the dollar area, there remained the problem of intra-European trade. Such trade had been kept up since the end of the war largely by the granting of reciprocal credit margins as part of bilateral payment agreements, but such credits, together with the existing monetary reserves, had for many countries reached exhaustion point and intra-European trade threatened to contract sharply and thus to counteract the intended effect of the United States aid.

In order to relieve the situation, an intra-European payments plan was worked out and the "Agreement for Intra-European Payments and Compensations" was signed in Paris on 16th October 1948 by the governments of the sixteen participating countries and representatives of the Bizone as well as the French Zone of Germany and also of the Free Territory of Trieste (see Chapter VIII). Under this arrangement the individual countries, in those cases where it was estimated that they would be "creditors" on current account of their balance of payments with any other participating country, received part of their allotments in dollars as "conditional aid", this part corresponding to the (estimated) surplus on current account. Each country thus had to establish "drawing rights" in its own currency in favour of other countries (according to a schedule included in the Agreement), so that a part of the E.R.P. aid received in dollars was passed on, via the national currency, to the final recipients.

The following table shows the distribution of the amount of direct aid, as well as the amounts of net indirect aid received or granted by the individual countries and, as the result of these two sets of figures, the distribution among the various countries of the net total aid

First fifteen months of E.R.P. aid.(1)

Countries	April 1948 to June 1948	July 1948 to June 1949			Total net aid: April 1948 to June 1949
		Direct aid	Net indirect aid granted (—) received (+)	Net total aid	
	in millions of dollars				
Austria	62	215	+ 64	279	341
Belgium-Luxemburg*	20	248	— 208	40	60
Denmark	20	109	+ 7	116	136
France*	335	981	+ 323	1,304	1,639
Germany: (3)					
Bizone	109	411	— 10	401	510
French Zone	20	99	+ 1	100	120
Greece	50	145	+ 67	212	262
Iceland	2	5	—	5	7
Ireland	10	78	—	78	88
Italy	158	555	— 20	535	693
Netherlands*	115	470	+ 72	541	656
Norway	20	83	+ 32	115	135
Sweden	—	47	— 25	22	22
Trieste	4	18	—	18	22
Turkey	10	40	— 12	28	38
United Kingdom*	400	1,239	— 290	949	1,349
Commodity reserve	—	13	—	13	13
Total programme	1,335	4,756	± 565	4,756	6,091
Administrative and other outside expenses	2	67	—	67	69
Total E.C.A. funds	1,337	4,823	—	4,823	6,160

* Including overseas territories. (1) For various modifications in the figures, see chapter VIII.
(2) Portugal and Switzerland did not receive E.R.P. aid.
(3) The direct aid to Germany remains a charge against the country, pending eventual settlement, and is, therefore, not necessarily in the nature of a grant.

allotted for the period 1st July 1948 to 30th June 1949. While leaving aside the Interim aid, the table shows separately the aid allocated by E.C.A. for the second quarter of 1948 and the aid for the first fiscal year July 1948 to June 1949, the final column setting out the net E.R.P. aid for the whole period of the first fifteen months of the European Recovery Program.

Between the Government of the United States and each recipient country a bilateral agreement has been concluded, in accordance with which a sum equal to the amount of aid received as a grant from E.C.A. is being currently deposited in the local currency of each country. A deposit is made as soon as the United States notifies the government of the recipient country of the amount of aid utilised. The release of any funds thus deposited (the so-called "counterpart funds") requires the agreement of E.C.A. and is granted usually for certain specific purposes (to provide for the development of productive capacity or for other investment, or for a reduction of public debt — cf. chapter VII). Apart from such aid as is received in the form of grants, $1,000 million (of the $5,010 million made available between April 1948 and March 1949) has been set aside for loans and investment guarantees. Of the $1,000 million, $27.7 million was earmarked for investment guarantees, and as regards the balance — amounting to $972.3 million — E.C.A. has entered into loan negotiations with the participating countries, loans being arranged for a period not exceeding thirty-five years at a rate of interest of 2½ per cent., no interest being charged before 1st July 1952 and no repayment being demanded in any case before that date (and in some cases not before 1st July 1956). The loan agreements further include a provision for the discussion of postponement of payments and for alteration of terms in the event of "adverse economic conditions or for any other reasons".

On 14th April 1949 the U. S. Senate and House of Representatives approved a $5,430 million authorisation for the operation of E.R.P., comprising $1,150 million for the three-month period April to June 1949 and $4,280 for the year 1st July 1949 to 30th June 1950.

The President of the United States, however, on the strength of the recent price decline, requested Congress for a total appropriation of only $5,272 million, of which $4,198 million should be for the year beginning 1st July 1949. The House Appropriation Committee voted a 15 per cent. cut in the latter amount. At the time of writing, a compromise had been reached, the House accepting the 15 per cent. cut but stating that the funds thus reduced for 1948–49 could be expended during 10½ months, i.e. up to 15th May 1950.

In view of the fact that, as originally intended, a somewhat smaller amount is made available for the second than for the first fiscal year of E.R.P., it is possible that the quotas allotted as "drawing rights" will be somewhat reduced. In the "Report on Recovery Progress and the United States Aid", submitted in February 1949 by E.C.A. for the use of the members of Congress, it is explained that the Agreement for Intra-European Payments and Compensations was designed "to prevent a stagnation of intra-European trade caused by payment difficulties". This agreement is, indeed, said to have constituted "the first step towards mutual aid among the participating countries and multilateral balancing of payments among themselves". The total amount of drawing rights arranged for the first fiscal year of E.R.P. aid was $818 million; since, however, countries both give and receive drawing rights, the net amounts of drawing rights came to $565 million.

At the request of the Council of O.E.E.C. in the autumn of 1948, the Bank for International Settlements agreed to act as technical Agent under the Agreement for Intra-European Payments and Compensations, this being in a measure a continuation of the rôle the Bank had played as Agent under the First Agreement on Multilateral Monetary Compensations, which was signed in Paris on 18th November 1947 by the Governments of Belgium (acting also for Luxemburg), France, Italy and the Netherlands (and which was described on pages 142–153 of the eighteenth Annual Report). As explained more fully in chapter VIII, the intra-European payments scheme adopted as part of the E.R.P. operates through a monthly compensation of balances held under European payments agreements plus the utilisation of drawing rights. The Bank for International Settlements, acting in a strictly technical capacity, is responsible for carrying out the monthly operations and is thus entrusted with the administration of an essential element in the working of the European Recovery Program.

The countries participating in the Marshall Plan have together a population of about 270 million, out of the 400 million which make up the population of Europe — apart from the U.S.S.R. Estimates of national income are, especially in times of inflationary movements, necessarily subject to a fairly wide margin of error and must, therefore, be taken as indicating mainly "orders of magnitude"; but, even so, a comparison between the Marshall aid allotted to the individual countries and the corresponding national income throws some light, from another point of view than the purely "balance of payments" aspect, on the importance of the aid received in each case. In the table on the following page the actual amount of aid allotted to each particular country for the year July 1948 to June 1949 — the first "fiscal year" of the European Recovery Program — is shown as a percentage of the national income (converted into U.S. dollars, it being recognised, however, that this introduces another source of possible error).

While the indirect aid facilitates trade within Europe, it is really the amount of net aid received which represents what is available to each country for the covering of its own expenditure for various purposes. As the table shows, Switzerland and Portugal had no direct or indirect aid allotted to them; Sweden and Belgium receive the lowest percentages of net aid in relation to the national income while the highest percentages go to Greece, Austria and the Netherlands.

Relation of E.R.P. aid to the national income of the participating countries and the United States: July 1948 to June 1949.

Countries	National income	Aid allotted: July 1948 to June 1949			
		Direct aid	Net total aid (1)	Percentage of national income represented by	
				Direct aid %	Net aid %
	in millions of dollars (2)				
Austria	2,000	215	279	10.8	14.0
Belgium-Luxemburg (3)	7,000	248	40	3.5	0.6
Denmark	3,500	109	116	3.1	3.3
France (3)	20,000	981	1,304	4.9	6.5
Germany (Trizone) (4)	17,000	510	501	3.0	2.9
Greece	1,500	145	212	9.7	14.1
Iceland	100	5	5	5.0	5.0
Ireland	1,000	78	78	7.8	7.8
Italy	10,000	555	535	5.6	5.3
Netherlands (3)	5,000	470	541	9.4	10.8
Norway	2,000	83	115	4.2	5.8
Sweden	6,500	47	22	0.7	0.3
Trieste	200	18	18	9.0	9.0
Turkey	2,000	40	28	2.0	1.4
United Kingdom (3)	40,000	1,239	949	3.1	2.4
Total	117,800	4,743	4,743	4.0	4.0
Portugal	1,400	—	—	—	—
Switzerland	4,500	—	—	—	—
Total E.R.P. countries	123,700	4,743	4,743	—	—
United States	230,000	4,743	4,743	2.1	2.1

(1) The amount of aid allotted, account being taken of the operation of drawing rights as shown in the tables in chapter VIII. (2) Round figures. (3) Including overseas territories.
(4) The total for *Germany* is made up of the combined figures for the Bizone and the French Zone.

The aggregate "national income" of the participating countries comes to about $120 milliard (for a population of 270 million) as compared with a national income of $230 milliard in the United States (with a population of 148 million). Thus the United States has a national income which is about twice as large as the aggregate money income (in dollars) of the participating countries in Europe and, per head, three and a half times as large. As everyone who has visited the United States knows, the cost of many articles and services is greater in that country than in Europe, but the bulk of the staple commodities (wheat, meat, petrol, etc.), as well as many mass-produced goods, are cheaper in the United States than in Europe. It is the size of the real income per head which enables the United States to extend aid to so many other countries. Thus, the total aid for the first fiscal year of the E.R.P. came to little more than 2 per cent. of the national income in the United States, while the amount of current private savings in the United States is estimated to have been equal to 15 per cent. of the national income.

For the recipient countries in Europe the aid allotted for the period July 1948 to June 1949 corresponds to about 4 per cent. of their aggregate national income. The significance of this figure may be judged from the fact that before the first world war a proportion of 10 to 15 per cent. of the national income was saved in the richer countries and invested at home and abroad — which permitted a fairly regular growth of nearly 3 per cent. in world production. Thus in 1948–49 Marshall aid, on an average, corresponded to about a third of the proportion of savings required for normal economic growth; here as elsewhere it is, of course, the marginal contribution that counts most, making all the difference, in this case, between a slow and painful increase in production (even assuming that social and political disasters could have been avoided) and the fairly rapid recovery which actually took place, almost without exception, in the E.R.P. countries in the course of 1948. One of the principal problems to be solved as Marshall aid draws to its close will be how to ensure sufficient savings in the participating countries to enable them to continue investments at not too low a rate.

While the aim of Interim aid made available for the first three months of 1948 was primarily to help France, Italy and Austria to extricate themselves from a critical situation, the application of the full European Recovery Program soon had a profound effect in the recipient countries and in the world at large. As the first and most signal result it must be mentioned that the external aid helped to keep up the volume of international trade — not only in relation to the dollar area but, through the operation of the payments scheme, within Europe as well; if the aid had not been forthcoming, several countries which could not afford to dip more deeply into their already badly depleted monetary reserves would have had no choice but to cut down their imports still further, even though that would have meant a recurrence of unemployment and would in many cases have impaired the chances of continued recovery; for they could not very well have suddenly given free rein to the price and foreign-exchange mechanism since that would have involved too brusque a change from the previous system of rigid control, and the adjustments in such a case might very likely have become intolerable from a social point of view. A second very important result was that inside each individual country Marshall aid helped to arrest inflation by making more goods available (thus increasing "supply") and by exerting, to the extent that "counterpart funds" were effectively accumulated, a certain restraining influence on spending and lending (thus curtailing "demand"). In that way, time was afforded for "reorganisation" — and an essential point is, of course, that the time thus gained should be utilised in a way which really makes the help received "help towards self-help". The time must also be wisely used to further the co-operative aspects of the Program — the strengthening of the ties between the participating countries, so that joint consideration can be given to problems concerning them all and, when occasion arises, common or at least coordinated action can be taken. The provision of an impetus to think along new lines — overcoming settled habits as well as old antagonisms — and the recognition of the necessity for setting up new institutions for concerted action may one day prove to have been the lasting achievements of Marshall aid.

Now that a low rate of production is no longer the bottleneck of world recovery, other problems — and in the first place monetary problems — can receive increasing attention. Depleted monetary reserves form a very unreliable basis for recovery — thence the necessity for their replenishment. Strengthening of monetary reserves should be regarded not only as a step towards the general re-establishment of confidence in national currencies but also as a means of enabling the various countries to apply, in relation to one another and to the world in general, a less arbitrary commercial policy, which is possible only if they do not live in constant fear of a further shrinkage of their too scanty holdings of gold and foreign exchange. But a replenishment of monetary reserves will bring little lasting benefit if it is not accompanied by the establishment of those internal and external conditions upon which the maintenance of balance in the economies of the individual countries depends and without which no monetary standard can work smoothly; moreover, the measures required to bring about the necessary adjustments will have to be taken well before the time appointed for the termination of external aid.

The provision of Marshall aid has been the generator of the main transfers of funds since the beginning of 1948 but other movements have also occurred.

In eastern Europe a number of trade and payment agreements have been concluded in the course of 1948, providing for an increased volume of trade, generally over periods of five years and also, as a rule, for some extension of credit. The U.S.S.R. has undertaken to deliver, partly on credit, certain types of capital goods and also raw materials to Czechoslovakia, Poland and Yugoslavia. Moreover, the U.S.S.R. has made two middle-term loans to Poland: in March 1947 one of $28 million in gold for thirteen years and in January 1948 a ten-year loan of $450 million at 3 per cent. to finance Polish imports of capital equipment.* In December 1948, a loan in gold and foreign exchange was granted by the U.S.S.R. to Czechoslovakia, but the amount has not been published.

In the trade agreements between the U.S.S.R. and countries in eastern Europe arrangements are usually made for deliveries of particular commodities (sometimes involving an extension of credit); but when a loan in gold has been granted there does not seem to have been any condition attached limiting the purchase of goods to a particular country or group of countries. In the more recent agreements in which the U.S.S.R. has been one of the partners, that country has increasingly accepted consumption goods — a natural consequence of the industrialisation in eastern Europe, which is a line of development obviously furthered by the government in Moscow.

The countries in eastern Europe are, however, still largely agricultural, with a relatively low income per head of the population. It would seem

* See "Major Economic Changes in 1948" (page 22), published by the United Nations, January 1949.

on the basis of recent estimates (confirmed by a comparison with data for the pre-1939 period, when complications caused by the inconvertibility of currencies, etc. were somewhat less acute than at present) that, on an average, the national income per head of the population in eastern European countries works out at about 60 to 65 per cent. of the average for the other countries in Europe.

Before Marshall aid became available, several European countries had been the recipients of U. S. government funds through the lending operations of the Export-Import Bank in Washington. Between the summer of 1945 and the end of 1948 this bank extended credits for a total of $2,350 million, of which more than two-thirds went to European countries. In 1948 the credits newly authorised were as follows:

Europe — United Kingdom	$ 22.5 million	
Finland	$ 10.7 ,,	
Germany	$ 4.6 ,,	
Sweden	$ 2.2 ,,	
Norway	$ 0.3 ,,	
Total for Europe		$ 40.3 million
Egypt		$ 1.5 ,,
Canada		$ 5.0 ,,
Japan		$ 29.0 ,,
Central and South America		$ 62.4 ,,
Total		$138.2 million

In the second half of 1948 the new credits of the Export-Import Bank were mostly for projects in the other American republics, a loan of $10 million to Finland being the only credit to a European country in that period.

While the Export-Import Bank has practically exhausted its lending capacity on the basis of funds allotted to it by Congress, it should be noted that during the years 1949–1952 the bank is due to receive some $120 to 140 million in principal and, in addition, some $50 to 60 million in interest each calendar year (from which, however, the operating expenses have to be paid, at the rate of about $13–14 million a year, including some $12 million paid to the U. S. Treasury as interest on notes).

As E.C.A. completes its loan negotiations with participating countries, funds corresponding to the loans granted are (after consultation with the National Advisory Council) being allocated to the Export-Import Bank, which acts as an agent for the E.R.P. loans. At the same time, the availability of Marshall aid has made it possible for the Export-Import Bank to limit its own activity. In its sixth report to Congress, for the period January to June 1948, it stated that, as far as its own lending was concerned, its directors thought that "credits to the participating European countries should not be authorised save in exceptional circumstances".

A similar attitude has been adopted by the International Bank for Reconstruction and Development and by the International Monetary

International Monetary Fund:[1] Summary of transactions.

Currency	Exchange transactions: for the fourteen months ending 30th April 1948	Exchange transactions: for the fiscal year ending 30th April 1949
	U. S. dollar equivalent in millions	
Currency sold:		
U.S. dollars	600.0	108.0
Belgian francs	—	11.4
Pounds sterling	6.0	—
Total currency sold	606.0	119.4
Currency bought:		
Belgian francs	33.0	—
Brazilian cruzeiros	—	15.0
Chilean pesos	8.8	—
Costa Rican colones	—	1.3
Czechoslovakian koruny	—	6.0
Danish kroner	10.2	—
Egyptian pounds	—	3.0
Ethiopian dollars	—	0.3
French francs	125.0 [2]	—
Indian rupees	28.0	72.0
Mexican pesos	22.5	—
Netherlands guilders	68.5	6.8
Nicaraguan cordobas	—	0.5
Norwegian kroner	5.0	4.5
South African pounds	—	10.0
Turkish liras	5.0	—
Pounds sterling	300.0	—
Total currency bought	606.0	119.4

(1) Up to the end of April 1948, the I.M.F. sold 24,000 U.S. dollars against gold and during the fiscal year ending April 1949 $ 6,136,000.

(2) Represents the U.S. dollar equivalent calculated at the agreed par value in force at the time the transactions were effected.

Fund. The latter institution pointed out in April 1948 that, in the case of E.R.P. member countries, recourse to the Fund should be had "only in exceptional and unforeseen cases" so as "to maintain the resources of the Fund at a safe and reasonable level during the E.R.P. period in order that at the end of the period such members will have unencumbered access to the resources of the Fund".

During the calendar year 1948 the International Monetary Fund increased the amount of currencies bought from member countries (more than 97 per cent. of the purchases being against sales of U.S. dollars) by $208 million.

But besides selling and purchasing currencies (which is in some respects equivalent to an extension of credit) the International Monetary Fund is concerned with problems relating to exchange rates, and in its annual report submitted to the Board of Governors at their meeting in September 1948 it took the opportunity to make it clear that its task "to promote exchange stability" does not

> "impose upon the Fund the duty of perpetuating in the name of stability exchange rates which have lost touch with economic realities. Stability and rigidity are different concepts... The Fund has never insisted on the maintenance of an exchange rate which was not suited to a country's economy. On the contrary, it has always recognised that an adjustment of exchange rates may be an essential element in the measures necessary to enable a country to pay for the goods and services it needs from abroad without undue pressure upon its international reserves. Stability implies that when exchange rate adjustments are necessary they should be made in an orderly manner and that competitive exchange depreciation should be avoided."

In the report it was further explained that "when the Fund was set up a major preoccupation of those who were concerned with international exchange policy was the avoidance of competitive exchange depreciation" as a measure of protection against the effects of deflation. But in recent years the basic conditions had been virtually the reverse of those existing in the latter half of the inter-war period. Since there was now general "anxiety about the effect of rising living costs", the tendency in all countries had been "to maintain exchange rates rather than to depreciate them". In this connection the Fund stressed the view that

> "so long as an exchange rate does not hamper a country's exports, there is little to be said in present world conditions for altering it. There are indications, however, that in some countries the exchange rate is becoming a restraining factor on exports and that it is adding to the difficulty of earning convertible currencies."

But it will also be necessary to take "internal financial problems and policies" into account, and with them "the necessity of restraining inflationary forces, particularly by achieving a balance or surplus in the national budget and bridging the gap between the volume of investment which is undertaken and the amount of its income the community is willing or able to save".

The International Bank for Reconstruction and Development had, up to the end of 1947, granted loans for an amount of $497 million, distributed as follows:

France	$ 250 million
Netherlands	$ 195 ,,
Denmark	$ 40 ,,
Luxemburg	$ 12 ,,
Total	$ 497 million

During 1948 two new loans were arranged: $16 million to Chile and $12 million to various Dutch shipping companies, these loans being guaranteed by the government of the Netherlands.

The Bank for International Settlements participated by the provision of Sw.fcs 17 million as part of the financing accorded by the International Bank for Reconstruction and Development to the Netherlands, as described in the eighteenth Annual Report of the Bank, page 8. In the first quarter of 1949 the International Bank for Reconstruction and Development arranged three further loans:

Mexico	$ 34 million
Brazil	$ 75 ,,
Belgium	$ 16 ,,

The total amount of loans granted by the Bank for Reconstruction and Development up to the end of March 1949 was thus brought up to $650 million. As regards the loan to Belgium, $16 million of Kingdom of Belgium bonds were sold privately by the International Bank for Reconstruction and Development to New York insurance companies; these bonds, which had the unconditional guarantee of the International Bank for Reconstruction and

Development as to principal, interest and sinking-fund payments, bear 3 per cent. interest and mature in twenty years. Belgium as a borrower pays 4 ¼ per cent. for the funds, which are being used to provide capital for purchases of steel-mill and power-plant equipment.

In the third annual report of the International Bank for Reconstruction and Development, submitted on 29th September 1948 to the Board of Governors, the main lines of the Bank's lending policy were set out:

> Since it was clear that United States assistance to Europe would for the time being greatly exceed any amount which the Bank might lend, it seemed desirable that the Bank should "... *reserve its not unlimited resources to* finance productive projects in other areas of the world and to supplement the E.R.P. by helping the participating countries in their long-term investment programs". Thus in Europe "negotiations have been conducted with respect to a number of small loans for specific productive purposes which seem clearly desirable irrespective of the ultimate form of the E.R.P.". But "the Bank's continued interest in assisting European recovery has not prevented a definite increase in its activities in other parts of the world during the past year; in fact, the problems of the Bank's underdeveloped member countries are more and more occupying the major proportion of the Bank's attention and, in the long run, they will undoubtedly constitute the Bank's primary concern". The Bank is "... convinced that sound development is best promoted, not by sporadic injections of large amounts of capital, but rather by a steady flow of capital in moderate amounts". The Bank finds it desirable "... that a considerable part of the foreign capital employed for development purposes be in a form of equity investments in order to avoid an undue burden of fixed charges which might impair the credit of the borrowing country or intensify its balance of payments problems during a period of declining trade or falling prices". Direct investment by foreign business enterprises, moreover, has "the special advantage of supplying technical and managerial skills as well as capital". For these various reasons it is one of the principal objectives of the Bank "to help to create conditions which will encourage a steady and substantial stream of private investment, particularly equity investment, flowing into its underdeveloped member countries". It is pointed out that "through the use of its guarantee powers the Bank can itself assume the risk of loans made from private funds" and that "the Bank is examining the possibilities of granting limited guarantees — for example, a guarantee of transfer of interest — to reduce the special risks involved in international financing without eliminating the private character of the investment".

* * *

Marshall aid is by intention and by its very nature a temporary form of financing on the basis of government funds. Just as there was a period after the war during which provision for "reciprocal credit margins" in bilateral trade agreements was justified as a means of giving an initial impetus to trade so, on a larger scale, Marshall aid has its justification as a comprehensive measure which will afford strength for recovery and time for reorganisation. Already minds are beginning to busy themselves with the problems of further financing after basic recovery has been attained — being well aware of the fact that many tasks remain to be tackled. The Bank for International Settlements has, during the past few years, gained some experience with regard to short-term financing, having granted credits mostly of an equilibrating nature; and it can see further needs arising, as the official financing through E.R.P. gradually decreases. The International Monetary Fund and the International Bank for Reconstruction and Development will continue to devote their attention to their own particular functions of international financing. But the financing of international trade and foreign investments cannot for long rely principally on the provision of government funds or on the activities of a few specialised international institutions of an essentially official character. It will obviously be necessary to create the proper conditions for increased international financing from the resources of private capital. The attraction of such capital was, indeed, clearly envisaged in "Point Four" of President Truman's Inaugural Address (delivered on 20th January 1949), dealing with "the improvement and growth of underdeveloped areas". The following extracts from the Address show some of the main lines of the President's thoughts on this subject:

> "Fourth, we must embark on a bold new program for making the benefits of our scientific advances and industrial progress available for the improvement and growth of underdeveloped areas.
>
> . . . .
>
> I believe that we should make available to peace-loving peoples the benefits of our store of technical knowledge in order to help them realise their aspirations for a better life. And, in co-operation with other nations, we should foster capital investment in areas needing development.
>
> Our aim should be to help the free peoples of the world, through their own efforts, to produce more food, more clothing, more materials for housing, and more mechanical power to lighten their burdens.
>
> We invite other countries to pool their technological resources in this undertaking. Their contributions will be warmly welcomed. This should be a co-operative enterprise in which all nations work together through the United Nations and its specialised agencies whenever practicable. It must be a world-wide effort for the achievement of peace, plenty and freedom.
>
> With the co-operation of business, private capital, agriculture, and labor in this country, this program can greatly increase the industrial activity in other nations and can raise substantially their standards of living.
>
> Such new economic developments must be devised and controlled to the benefit of the peoples of the areas in which they are established. Guarantees to the investor must be balanced by guarantees in the interest of the people whose resources and whose labor go into these developments.
>
> . . . .
>
> All countries, including our own, will greatly benefit from a constructive program for the better use of the world's human and natural resources. Experience shows that our commerce with other countries expands as they progress industrially and economically."

Investment in underdeveloped areas necessarily means, at the outset, a fairly lengthy period of waiting for the expected goods to be produced, and the first effect is, therefore, to reduce the resources available for other purposes — e.g. an increase in consumption or in the volume of investments of the home country. Thus concern with the growth of production in underdeveloped areas brings no immediate relief to the European countries, and obviously not in their struggle for an early re-establishment of proper equilibrium in their own balances of payments. But even if it is a fact that in some respects a programme of helping underdeveloped territories (which — it should be remembered — are not all situated outside Europe) involves a momentary burden, there are — as the President emphasised in his Inaugural Address — a number of reasons why an effort should be made to proceed with well-thought-out development schemes.

Such a course of action is undoubtedly to the advantage of the territories themselves, since in that way their productivity can be increased and their standard of living raised at a rate which they could not achieve unaided, especially since modern methods of production and social welfare can do much for the workers in the underdeveloped areas, where the income per head of the population is generally less than one-tenth of the income per head in the United States. But little would be gained if the development of local industries were simply to be in the direction of autarky behind high protective walls. The U.S. Secretary of State, Mr Dean Acheson, in a press conference* on 26th January 1949 explained that the President in his Inaugural Address had

> "pointed out that in so far as his program is successful and in so far as peoples in less developed areas acquire skills, they may also create the conditions under which capital may flow into those countries. He [the President] did not say this was to be governmental capital and, indeed, if the proper conditions are created, the reservoirs of private capital are very great indeed. He pointed out that these must be two-way operations. There is abroad in the world an idea that there is a magic in investment. There is an idea that if every country can only have a steel mill, then all is well. There is a failure to understand that it is a long and difficult process to develop the skills which are necessary to operate many of these plants. There is sometimes failure to understand that plants should be located where the natural resources exist and not on purely nationalistic bases. There is also in many places a failure to understand that unless the conditions are created by which investors may fairly put their money into that country, then there is a great impediment to development."

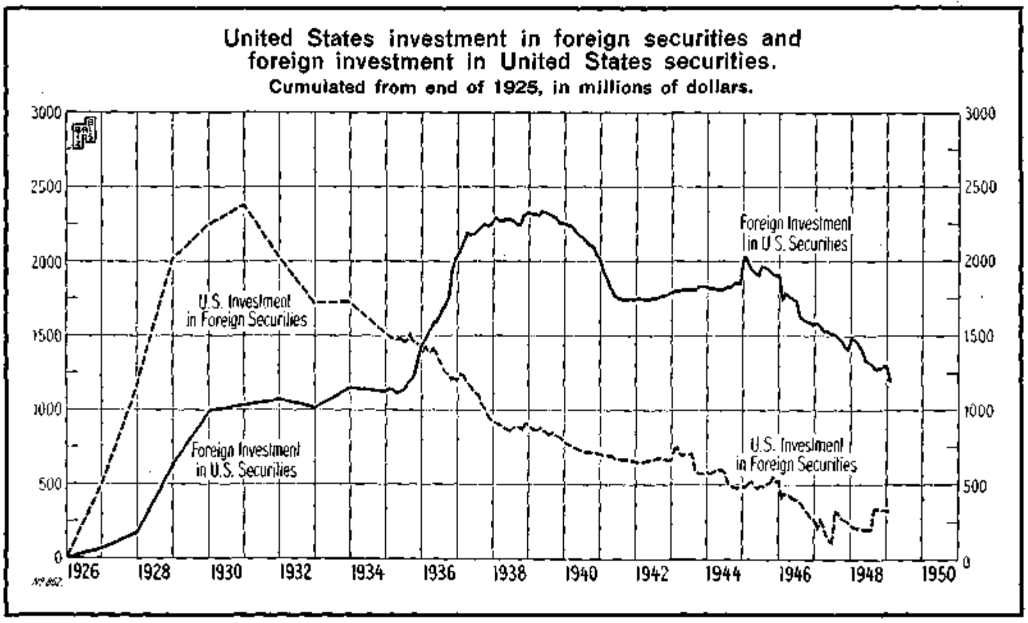
These warnings did not seek to belittle the importance of the idea expressed in "Point Four" of the President's address but to ensure that efforts should be directed along practical lines.

This is the more important since — as past experience shows — an expansion of production in underdeveloped areas can at the same time be of great benefit to countries which are already developed. Full use must be made of recent technological progress, and possibilities must be provided for investment of capital; but, if this happens, such areas should gradually become important sources of supply of raw materials; and, as their earning power increases, they should be in a position to buy more and more from

* Reproduced from the Department of State Bulletin for 6th February 1949.

abroad. The effort of getting new schemes adopted and properly executed may have in it "a vitalizing force" which can help to overcome any tendency to stagnation in the older countries, while bringing modern technique into underdeveloped areas. But a revival of private foreign investment by the United States means the reversal of a tendency which has prevailed almost uninterruptedly since the middle of the nineteen-thirties.

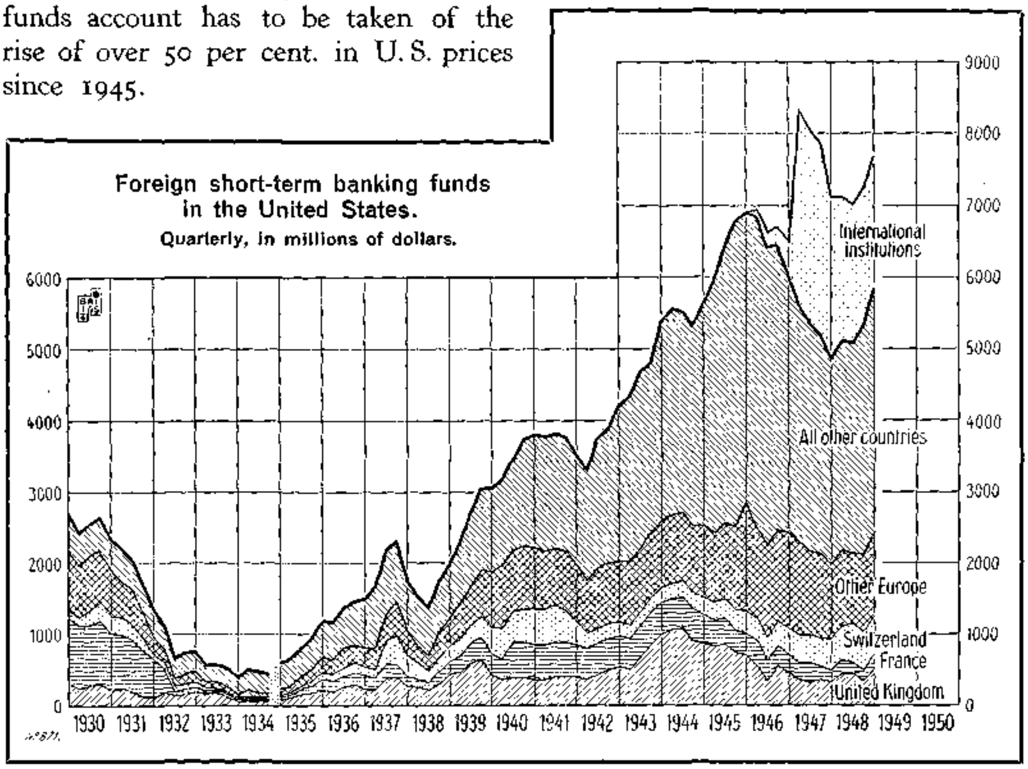
It should be noted that investments recorded in the graph below represent investments in securities (bonds and shares), thus excluding holdings of short-term balances and direct investments. As the graph shows, there has been an almost uninterrupted decline in American investments in foreign securities ever since 1934.



There had been two great waves in the foreign acquisition of American securities: nearly $1,000 million (net) was bought in the two years 1928–29 and over $1,000 million between the middle of 1935 and the early part of 1937. Experience after the stock-market declines in the autumn of 1929 and the spring of 1937 indicates that, while non-American investors (considered as a whole) bought American securities during the bull markets, they did not, on balance, sell during the subsequent decline in prices.

But there were sales of securities, together with a withdrawal of funds, early in the war (to a large extent connected with the requisitioning of securities by the British Government) and then an appreciable decline in holdings after the war, partly owing to requisitioning by a number of governments but partly also to voluntary withdrawals.

The following graph shows the changes in foreign short-term banking funds in the United States, most of these being demand deposits with American banks. In the Federal Reserve Bulletin for February 1939 it was stated that "an analysis of the capital movement itself suggests that, while this movement has been influenced to an important degree by disturbed conditions abroad, only a limited amount now represents nervous foreign money ready to leave this country as soon as conditions abroad become more stable". In fact, the war years saw another increase in the holdings of foreign countries in the United States, the foremost depositors being Latin American countries. The proportion of the short-term banking funds now held by European countries is much less than it was in 1930. In judging the real significance of these funds account has to be taken of the rise of over 50 per cent. in U. S. prices since 1945.



Important though investments in securities and holdings of bank balances are, the largest single item among U. S. foreign investments was for years the total of direct investments, *exceeded only in 1947 by the* U. S. Government's own investments abroad (i.e. its loans to foreign countries). The table on the next page shows the changes which took place during the war in the international investment position of the United States, according to the computations of the U. S. Department of Commerce.

It will be seen that the development of a U. S. creditor position on capital account corresponds to the amount of foreign loans and other investments abroad by the U. S. Government.

If the criterion is the net amount of income received from investments abroad, the United States comes out more clearly as a creditor country, since

United States: International investment position.

Items	End of 1939	End of 1946	End of 1947
	in milliards of dollars		
U.S. investments abroad:			
Private long-term			
Direct	7.3	8.5	9.4
Portfolio	4.1	5.8	5.7
Private short-term	1.1	1.3	1.6
Total private investments	12.5	15.6	16.7
U.S. government investments	—	5.1	12.1
Total U.S. investments abroad	12.5	20.7	28.8
Foreign investments in the United States:			
Private long-term			
Direct	2.9	2.6	2.6
Portfolio	5.8	5.1	4.8
Private short-term	3.8	5.2	5.2
Total private investments	12.5	12.9	12.6
U.S. government obligations held abroad	0.3	3.5	3.9
Total foreign investments in the United States	12.8	16.4	16.5
Net debtor (—) or creditor (+) position of the United States	— 0.3	+ 4.3	+ 12.3

in 1948 such income is estimated to have been equal to $983 million — the difference between $1,257 million received from abroad and $274 million paid to foreigners as their return on investments in the United States (a large part of these latter investments being in the form of bank balances on which a low rate of interest, if any, has been paid).

An expansion of the volume of trade almost always represents a gain in itself; but triangular trade, in which overseas countries sell raw materials to the United States while buying a variety of machinery and manufactured articles from Europe or in which part of the earnings of such countries is spent by their nationals visiting Europe, has the further advantage of helping to solve the dollar problem; for trade of this kind makes it possible, so to say, to get round the U. S. tariff, since most raw materials are duty-free, in contrast to manufactured articles, which are usually subject to fairly heavy duties on entering the United States, so that the shipment from Europe of manufactured goods involves, as a rule, the necessity of climbing over the American tariff.*

Encouragement of triangular trade is not, of course, a short cut to solving the dollar problem, but it helps up to a point, and in this field, as so often in human affairs, a solution must be sought along many different lines.

On this there is probably general agreement, and the same consequently applies to the desirability of improving production in underdeveloped areas: the real question is how to translate more or less vague aspirations into practical

* It is well to remember that, since the middle of the nineteen-thirties, the U. S. tariff has been greatly reduced through reciprocal trade agreements, the rise in prices (which has lessened the burden of specific duties) and further steps taken in connection with the International Trade Organisation. According to the results given by the usual methods of measuring the weight of protective duties, the U. S. tariff level is now about one-half of what it was in 1932 and it is even lower than it was after the fairly sharp cut in protection brought about in 1913-14 under President Woodrow Wilson's leadership. But, as mentioned in an article on "Europe after 1952" by Professor John Williams, in "Foreign Affairs" for April 1949, it seems to be a fact that the U. S. tariff "still accords effective protection in just the range of goods in which Western Europe might otherwise compete".

modes of action. In some respects this is part of the wider problem of restoring capital movements, in general, between countries; for even between the older countries technical progress occasions questions of give and take in the matter of up-to-date processes, there being many cases in which the use of such processes cannot easily spread from country to country in the absence of some possibility of capital investments. Moreover, it is dawning upon the world that multilateral trade will not prove possible without a revival of multilateral capital movements.

Obviously one of the reasons why trade has recovered so well between members of the same monetary area (as, for instance, between the countries within the sterling area) is that, in the relations between such countries, capital has been free to move whenever it was needed for genuine investments and financing of trade. A recognition of this fact points to the true solution of the problem: progress must be made in the monetary field so that, on the one hand, payments can be carried out freely on current account and, on the other hand, capital transfers required for genuine economic purposes will meet with fewer and less serious obstacles. But such progress will not be possible without the fulfilment of certain conditions, which can only be briefly indicated here:

(i) there must be no inflationary creation of purchasing power for budget purposes or through the credit system — which means that the so-called "inflationary gap" must be closed;

(ii) there must, where necessary, be a return to realistic exchange rates; and

(iii) there must be a minimum of political stability, internally and internationally, for otherwise it will not seem worth while to launch out on ventures which will take years to bear any real fruits.

But there is obviously one further condition which must be fulfilled, namely that the older countries will have the resources to invest in the areas needing help in the expansion of their production. The real resources which are needed must be generated by means of genuine current savings, as they were in the past, when European countries invested their surplus savings for the building of railways and the establishment of industrial and commercial enterprises in overseas countries — including the United States. For many years now, the United States has been almost the only country with a surplus of savings available for investment abroad. The world is suffering today from a scarcity of current savings; those who feared that monetary difficulties would arise from a superfluity of savings after this last war have clearly, but not unexpectedly, been wrong. It is not enough to increase production: it is necessary that resources should be set free for the formation of real capital at home and abroad. This is obviously a problem which goes far beyond the particular field of investment in underdeveloped areas; it reaches the core of the fundamental problem of how to establish a true balance within each individual country and in the relations of the various economies one with the other. There will be occasion to return to that problem in almost every part of this Report.

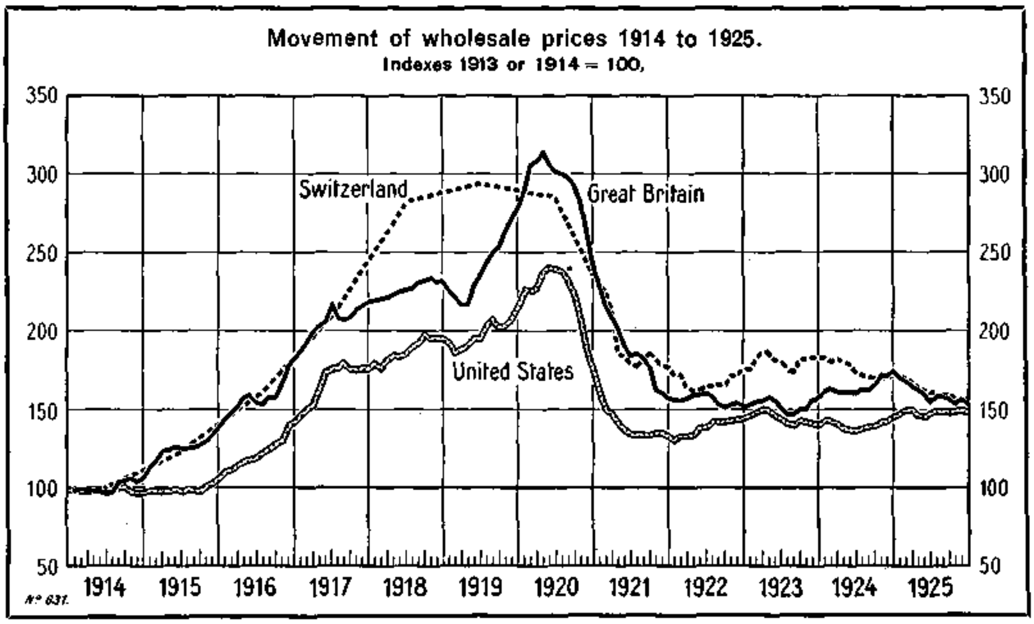
II. The End of the Post-war Inflation.

Five years will soon have passed since France and Belgium were liberated in the late summer of 1944 and four years since the war came to an end on the continent of Europe. It is thus becoming possible to see the situation in longer perspective: notwithstanding many difficulties of a technical and political nature and some regrettable setbacks, much progress has undoubtedly been made; in most cases, production has attained or even surpassed peacetime proportions, and commodity prices have ceased to increase as they had been doing under the influence of inflationary issues of money for meeting government expenditure and (but to a much lesser extent) private demands for credit.

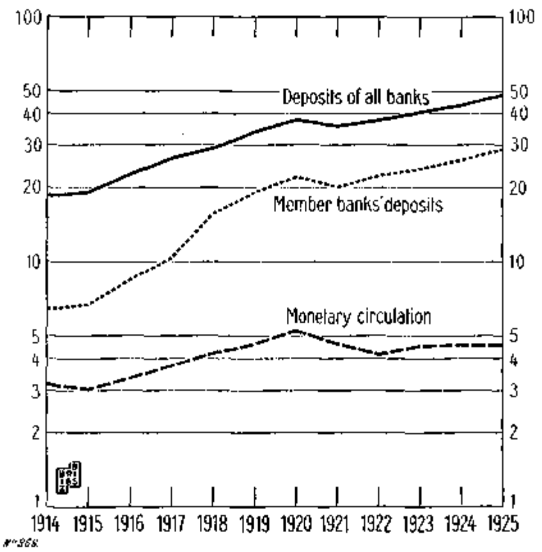
Comparison with the business trend during the four to five years following the first world war brings out the absence of anything corresponding to the post-war depression which began to make itself felt in the latter half of 1920 and, after bringing a short but sharp fall in prices, had already run its course by the autumn of 1922.

The following graph shows the movement of wholesale prices between 1914 and 1925 in the United States, Great Britain and Switzerland.

Wholesale prices are subject to strong international influences and, in the main, the actual movements after the first world war display common characteristics for the three countries included in the graph; but, on closer examination, the available data indicate that the driving force emanated from the United States, where the wartime shortages were most easily overcome.



United States: Volume of deposits and monetary circulation 1914 to 1925.
End-of-June figures, in milliards of dollars.*



* Logarithmic scale.

It seems sometimes to be taken for granted that the fall in the American price level after the first world war was mainly due to a contraction of credit. Facts do not bear out such an assumption, however. The volume of deposits and the note circulation had expanded rapidly up to 1920; in the following year there was a certain shrinkage in both; but the remarkable thing is that the decline from the top figure was slight indeed in comparison with the previous rise and, moreover, of really short duration. By 1922 the volume of deposits had already regained the 1920 level and an expansion then set in, which continued without a break up to 1930.

In terms of money, the national income also kept up well — another indication that aggregate monetary demand in the United States remained practically undiminished all through the first post-war depression in 1920–22.

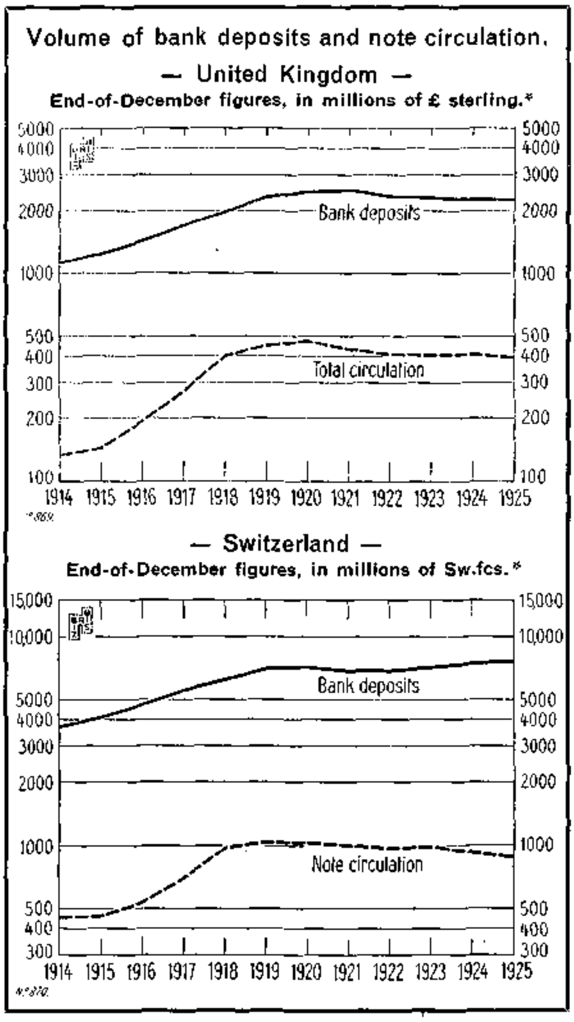
That being the case, the decline in prices must rather be attributed to changes in the supply situation. During the war, sudden shortages had sent prices and profits soaring and an intense demand for labour had made it possible for numbers of industrial and agricultural workers to obtain an increase in wages (while large groups of salary-earners and others had found their real incomes lessened by the rise in prices).

But a reaction followed: as soon as the normal peacetime supplies reappeared, the abnormally high prices had to come down — and once the decline had started the fall was swift indeed. It took not quite two years before a new balance was struck between the volume of monetary purchasing power left by the war and the reconstituted supply of goods and services; but a level of prices was then reached which remained practically stable for some six or seven years.

Decline in wholesale prices 1920–1922.

Country	Yearly average 1920	Yearly average 1922	*Percentage change*
	1913 = 100		
United States . .	221	139	— 37
Denmark	341	179	— 47
France	509	327	— 36
Great Britain . .	307	159	— 48
Netherlands . .	292	160	— 45
Norway	382	233	— 39
Sweden	359	173	— 52
Switzerland . . .	285	168	— 41

The price fall which started in the middle of 1920 made



* Logarithmic scale.

itself felt everywhere. In countries other than the United States, however, it was mostly accompanied or followed by further complications.

During the war and up to 1920, prices in Great Britain and Switzerland rose more sharply than prices in the United States but, after the reaction came, their relative decline was ultimately greater (as shown by the graphs — and a similar fall occurred in a number of other European countries, e. g., Denmark, the Netherlands, Norway and Sweden). An obvious reason for the fall in prices in Europe, as in the United States, was the overcoming of wartime shortages. For many European countries, however, another factor came into operation: the exchange rates of a number of European currencies had become depreciated in terms of dollars in the course of 1919 but the countries concerned were soon credited with the settled policy of re-establishing exchange relations at the pre-war gold parities; and this belief was sufficiently strong to bring the actual market rates close to the old par rates. Those rates, however, meant that the commodity prices of the countries in question had to fall precipitously and the volume of credit had also to be somewhat reduced. That actually happened, and it was an interesting case of prices' becoming adjusted to the pre-war partities instead of the exchange rates' being determined by relative price levels, in accordance with the theory of purchasing-power parities.

The corresponding graphs for the period of the second world war and for the years 1945–49 reveal a very different picture:

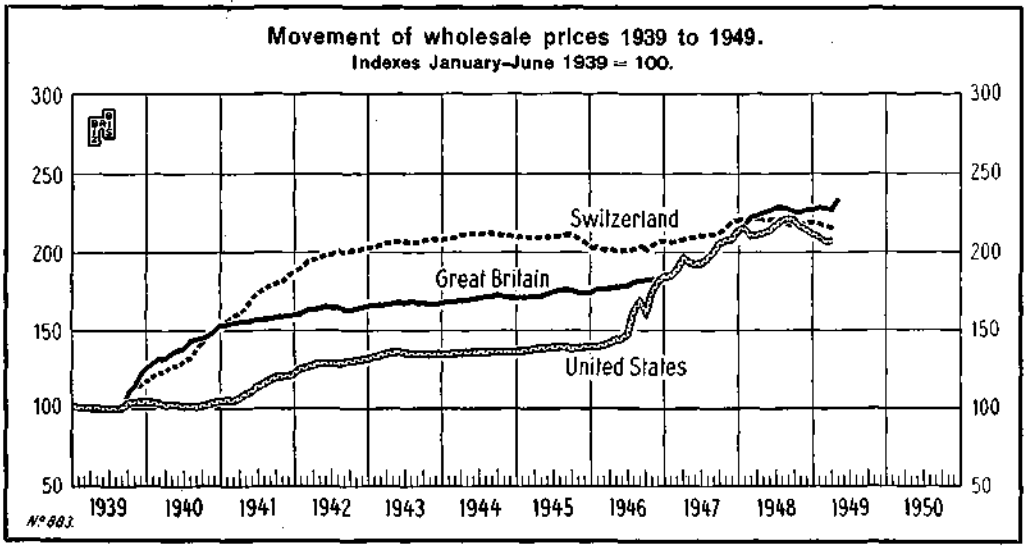
(i) During the actual war period, prices at first rose some 30–50 per cent., after which they were as a rule kept more or less stable for about three years (a very different state of affairs from the doubling and trebling of prices at the time of the first world war).

(ii) Once hostilities had ceased, in 1945, an insistent demand (previously repressed) set in, with the result that prices began to go up, and between the middle of 1945 and the end of 1946, i.e. during the first eighteen months after the war, the price level, in many countries, rose to about the same extent as during the corresponding length of time after the first world war.

(iii) But no such reaction set in as had happened in the middle of 1920. The rise went on until, by the end of 1948 (i.e. when the war had been over some three and a half years), prices in the United States and in a number of other countries had reached a level more than twice as high as before the war. Thus, although the wartime increase had been less pronounced, the ultimate price increase seems to be higher in the present instance than after the first world war.

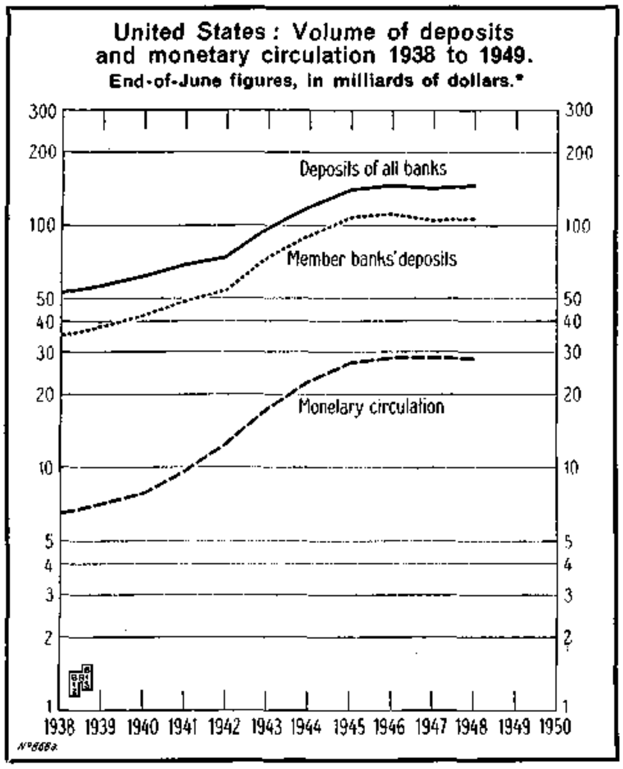
It is of some interest to consider the main reasons for the difference in the respective price movements after the first and the second world wars:

(i) One of the reasons is undoubtedly the fact that during the second world war the resolute application of a comprehensive wage and price control *not only went a long way towards neutralising fresh issues of* monetary purchasing power but also, with the aid of rationing and other measures, prevented shortages from being reflected in higher prices. In the fourteenth Annual Report (published at the end of 1944) it was pointed out (in a footnote to page 19), that, had it not been for price control, wartime shortages might have had a greater influence on the price level than is generally realised. If — without price control — the supply of goods and services in a certain country had been reduced



Movement of wholesale prices 1939 to 1949.
Indexes January-June 1939 = 100.

Note: With regard to any comparison of the relative purchasing power of the pound sterling, the dollar and the Swiss franc, it should be remembered that in the late summer of 1939 the exchange value of the pound was reduced by 14 per cent. — a reduction of which no account is taken in the above graph.

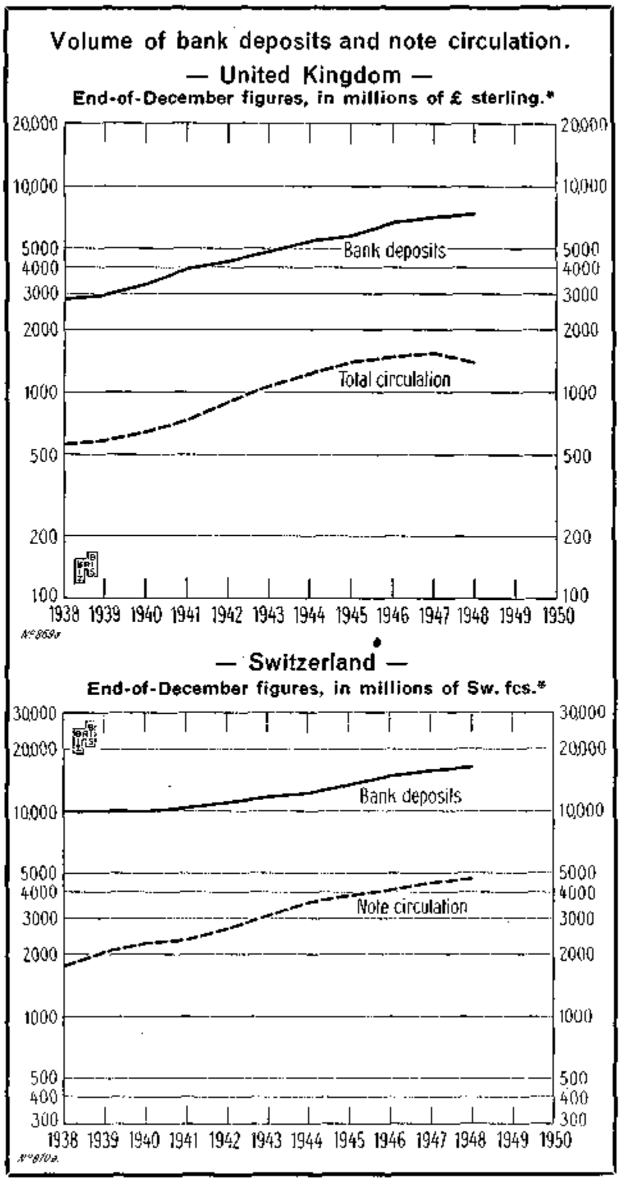


* Logarithmic scale.

by 20 per cent., the price index would have risen from 100 to 125. If, at the same time, an inflationary expansion of purchasing power had doubled the volume of effective monetary demand, the price level would have been raised to 250. Of the increase, 50 points (i.e. one-third) would have been due to the exceptional shortages; to this extent the rise would have disappeared when the shortages were overcome, if the increase in the volume of money and credit remained. If, on the other hand, as actually happened in the second world war, the control had been successful in preventing the shortages from raising prices, there would be no compelling reason why increased supplies of goods and services, after the end of the war, should lead to any pronounced fall in prices.

In the second world war, moreover, it was part of the policy of the United States, Great Britain, Switzerland, Sweden and a number of other countries to keep down the cost of living through the payment of subsidies, in order to prevent wages from rising too steeply. By the end of the war, wages in the countries mentioned had in fact risen much less than between 1914 and 1920; and, since the general price level did not fall even when supplies became more normal, no disequilibrium emerged between wage costs and prices and, consequently, there was no reason for a general reduction in wages. On the contrary, as prices went on increasing, wages also were generally raised. But the whole of this development must be seen in relation to the general trend of business, as determined not merely by the evident need for a large amount of work to be done after a destructive war but also by the combination of such a need with a redundant volume of purchasing power left over from the war and often dilated by current financial policy.

(ii) Attention must, indeed, be specifically directed in the second place to the working of the money and credit system. *Since throughout the*



* Logarithmic scale.

period between 1914 and 1920 prices rose as much as was warranted by the combination of wartime shortages and the inflationary expansion of purchasing power, it was inevitable that, when normal supplies became available, prices were too high in relation to the volume of notes and deposits and, therefore, had to come down. But, at the end of the second world war, the controlled prices were clearly too low in relation to the volume of notes and deposits then in the hands of the public; the monetary cloak was in most cases too big for current prices to be able to grow into it, so to say, by means of greater production. That being the case, it was open to the authorities either to cut the cloak down (by the blocking or even cancellation of part of the notes and deposits) or to leave the economy to grope its way towards a new equilibrium, which would then be at a higher level of prices; the United States chose the second alternative, with the result that the level of wholesale prices in that country rose more in the three and a half years after the war than during the war itself. Since the U. S. budget was more or less balanced from the beginning of 1946 (in some years with quite impressive surpluses), there was no inflation due to current deficit spending by the government, but past creation of money continued to have its effect, and the cheap-money policy was, on the whole, maintained — which made it possible to sell government securities at par when funds were required for new capital investments.

United States:
War and post-war changes in wholesale prices and Federal debt.

Period	Changes in wholesale prices	Changes in the total gross Federal debt
	as a percentage	in milliards of dollars
September 1939 to September 1945	+ 33	+ 221
September 1945 to December 1948	+ 54	— 9

As prices rose, demands were made for higher wages and, with relatively ample profit margins at their disposal and the feeling that even higher prices could be charged without reducing sales, employers generally put up relatively little resistance to requests for increased pay. It happened from time to time that signs on the horizon were interpreted as foreboding a recession; but up to the spring of 1949 the volume of business and industrial activity has been well maintained, although the "super-boom" seems to have come to an end in the course of 1948.

Economic conditions in the United States have set the tune for the business trend in the world at large and, now that western European countries are able to import food and raw materials in sufficient quantities, thanks largely to American aid and credits, the keynote generally has been one of profitable business and a high degree of employment. Apart from all social considerations, it was clearly desirable that, with so much work to be taken in hand after a devastating war, valuable time should not be wasted through unemployment; and the absence of any depression has, therefore, been a blessing. But it must at the same time be remembered that the sharp but short setback in 1920–22 had at least the advantage (which has been missed this time) of permitting price and exchange controls to be swept away at one go and almost all subsidies to be abolished, since prices were coming down so precipitously of their own accord. In 1921 and 1923 wages were also reduced; but, as the reduction was not commensurate with the fall in prices, real hourly wages were often increased by some 20–30 per cent., notwithstanding the extra cost which the shortening of the legal working-week from about 60 hours in 1913 to 48 hours after the war had imposed on industrial enterprise in a number of countries. The disappearance of control and subsidies meant a relief for the budgets, which also benefited by a reduction in armaments, partly arrived at by international agreement (Washington Naval Treaty of 1922).

After the second world war, there has been no similar relief for the budgets. On the contrary, there has been an evident inclination to take on new tasks, although this has meant that there could be little or no relaxation of the heavy wartime taxation. In the boom that has prevailed it might have behoved the governments to reserve their own activity for a later date when the trend had turned. The Nederlandsche Bank in its report for 1947 says that:

> "It is one of the disappointing aspects of the present situation that, while the requirements of a correct and proper economic policy are, theoretically, fully recognised, and the government also has the power to act

in accordance with those demands, the government, just as the free entrepreneur of former times, cannot see their way to avoid excessive activity in times when economic activity is large and increasing."

As far as the Netherlands itself is concerned the report stresses that:

"Our country cannot possibly at the same time restore order and peace in the Indies, rebuild its own damaged territories, materialise an industrialisation programme, provide an increasing population with houses, schools and such-like and, nevertheless, in the face of disturbed economic relations with the hinterland, increase the consumption level of the mass of the population as well."

In the Netherlands,* however, steps had already been taken in the autumn of 1945 — following an example set by Belgium* a year earlier — to cope with the redundancy of purchasing power, left by the war, through an exchange of notes, a proportion of them being held as blocked balances, while existing deposits were also blocked to a certain extent. A number of other countries (including Denmark* and Norway*) took similar measures.

As the technical features of the measures differed from country to country, so did the repercussions. Nowhere does the volume of current incomes seem to have been curtailed, and the effect was, therefore, never directly deflationary. But the limitation placed upon the disposal of accumulated assets was of some importance (since spending need not be limited to current income but can also be made from capital); and there was a psychological factor which should not be overlooked in the possibility that workers and others might be more willing to refrain from demands for increased pay when they found that sacrifices were being imposed on all sections of the public.

Furthermore, in analysing the nature of price movements, it seems useful to make a distinction between such increases as are essentially due to an expansion of monetary purchasing power (and, in that sense, clearly "inflationary") and other increases which result from an abolition of subsidies, higher indirect taxation or an adjustment of exchange rates — the latter increases being the most effective means of absorbing an excessive volume of purchasing power (not eliminated by direct methods) and thus establishing a more realistic price level, at which stabilisation can more safely take place.

* * *

Germany and Austria provide interesting — in some respects almost unbelievable — illustrations of the decisive rôle which, under certain conditions, the rates of wages (as well as salaries) may play when it comes to safeguarding the intrinsic value of individual currencies. Wage and salary movements are always of importance, since

* As described in the fifteenth Annual Report of the Bank for International Settlements, pages 60–65.

(i) wages and salaries represent the most substantial element in the national income[1] and, consequently, in the composition of the demand for goods and services;

(ii) wages and salaries further represent, for the economy as a whole, the most important single element in the cost of production; and

(iii) wages and salaries — at any rate as regards a reduction of costs — are usually a most sticky element.

These considerations have been of particular weight since the war: in Austria and Germany, and especially in the latter country, the maintenance of existing wage and salary rates (in terms of money) made it possible to save the value of the national currency in the face of a pronounced wartime inflation.

In Austria money wages and officially controlled prices had been kept stable during the war (Austria being at that time incorporated in Germany) and for the first two years after the war; but a sharp increase of approximately 45 per cent. was agreed upon in August 1947, by which money wages[2] were lifted to a level about 160 per cent. higher than in 1938 and some 110 per cent. higher than in 1929. As described on pages 32–34 of

Austria: Note circulation, deposits and current accounts.

End of month	National Bank			Other credit institutions			
	Notes in circulation	Current accounts		Current accounts		Savings deposits	
		free	blocked	free	blocked	free	blocked
	In millions of schillings						
1947 October	6,219	2,818	3,407	4,544	1,878	2,614	6,067
1948 January	3,440 (1)	2,279 (1)	2,034 (1)	4,570*	.	976*	.
March	3,994	1,453	1,943	4,802*	.	1,119*	.
June	4,474	1,173	1,847	4,831*	.	1,223*	.
September	5,132	1,076	1,718	4,990*	.	1,228*	.
December	5,635	1,377	428	4,783	.	1,272	.
1949 March	5,833	963	1,136	4,930	.	1,461	.

* Including temporarily blocked accounts. (1) 23rd January 1948.

Note: The main change in the situation of the National Bank during 1948 was the increase in the total of the note circulation and the "free" sight liabilities. The total circulation increased by 23 per cent. between 23rd January and 31st December, this being largely due to payments on blocked current accounts to the amount of Sch. 1,606 million — mostly in consequence of the release of Sch. 1,360 million of temporarily blocked deposits.

(1) In the United States, for instance, wages and salaries together represent about 60 per cent. of the national income; a pre-war estimate for Germany put the share of wages and salaries at 55 per cent. of the national income, a further 12 per cent. being represented by old-age pensions and similar benefits.

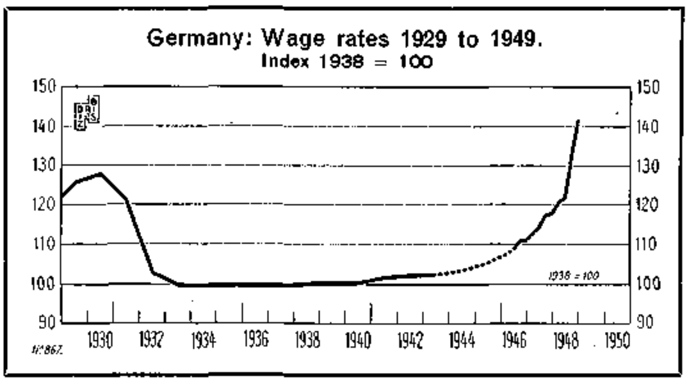
(2) If, during the difficult post-war years the wages of industrial workers in Vienna and some other urban centres have been kept reasonably stable without any social disturbances, one of the chief reasons has been the maintenance of regularity in the food supply, largely thanks to Allied assistance. At the time of the very difficult food situation in the autumn of 1947 (after the poor harvest of that year), workers in the towns were sure of about 1,700 calories (per day and per person), the purchase of which for a family would take about one-third of normal money wages. Actually, about 50 per cent. of the rationed foodstuffs representing the 1,700 calories were obtained from the Allies (in the first place from the United States).

the eighteenth Annual Report, a currency reform was put into effect in December 1947, under which notes were exchanged at the rate of one new for three old notes, but Sch. 150 per person could be exchanged at par; certain exceptions were also made for farmers; and deposits were treated in a different way. The final result was that the amount of notes in circulation was reduced by about one-third, while deposits previously blocked were definitively written off.

The effects of the currency reform were as swift as, on the whole, they were salutary. Black-market prices fell within a few months by 40–60 per cent. The price quoted for Austrian bank-notes in Switzerland rose gradually from Sw.fcs 1.50 for Sch. 100 in December 1947 to over Sw.fcs 15 for Sch. 100 in April 1949. In that month wholesale commodity prices stood at an index figure of 363 (December 1937 = 100), which means that they had risen not quite twice as much in Austria as in the United States. (This is not surprising considering all the vicissitudes through which Austria has passed since its incorporation in the German Reich in the spring of 1938.) The parity of the schilling (which early in 1938 stood at Sch. 5.35 to $1) had been fixed at Sch. 10 to $1 in October 1946; at that rate the official parity with the Swiss franc would be Sw.fcs 43.15 to Sch. 100, and this shows the gap still remaining between the official rate and the foreign price paid for (smuggled) schilling notes.

The following graph shows the movements of wage rates in Germany from 1929 onwards.

In the summer of 1948, wage rates in terms of money were 40 per cent. higher than in 1936 (when a "wage stop" had been imposed in Germany) and very little higher than in 1929–30, there having been no rise of significance in German money wages during the war and, after the war, a more limited rise in Germany than in other countries. This meant that a worker was still receiving only RM 0.95 per hour at a time when (in 1946–47) RM 7 or more would be paid for a single cigarette in the black market and a kilogramme of butter would fetch as much as RM 900.



Note: From 1929 to 1943 the data represent the yearly average of hourly wages for skilled and unskilled workers and as from 1946 onwards the quarterly average of hourly earnings in western Germany.

As long as the war lasted, strict discipline was still imposed by the totalitarian German government — without much difficulty, it might be added. And, even after the collapse of the German Reich in 1945, the local administrations carried on their task of control, their authority being soon reinforced by orders from the occupying powers. One factor which helped to ensure observance of the regulations was the obsession of the German workers, and the German public in general, with fear of an uncontrollable inflation; but this would have been ineffectual had it not been coupled with the fact that the worker continued to receive a certain supply of rations (approximately 1,800–2,000 calories per person per day) at controlled prices, which made him certain of a bare subsistence minimum. At RM 0.90–95 an hour, a worker would earn (say) RM 160 a month. Out of this income the rations would cost — for a family of four persons (parents plus two children) — about RM 60 per month and rent RM 20–30 per month, so that, in many cases, half the earnings would be left for other purposes, including a few supplementary purchases in the black markets (but up to 20 per cent. of this half would have to go in taxes and various social charges).

Exact figures of the amount of notes issued in Germany have not been available since 1944, but it has been estimated that (for the whole of Germany) the total note circulation (including Allied military marks) came to about 65 milliard in the spring of 1948, as compared with RM 8.6 milliard at the end of 1938 and RM 3.9 milliard at the beginning of 1933, when National Socialism came into power. As a result of the redundancy of circulating media after 1945, the currency became less and less useful as a medium of exchange; but it was still needed for the payment of money wages, taxes and rents as well as for the purchase of the meagre official rations — not to speak of the transactions in the black market — since it is almost impossible to do without money in a modern country. It must be said, however, that the currency in existence could no longer serve as a unit of account and, of course, even less as a store of value. The German economy was increasingly run by way of "barter"; private individuals and firms had to learn how to carry out so-called "compensation affairs", which were complicated, mostly illegal, and, therefore, costly. More and more workers and employers wanted to be at least partly paid in kind, willingly accepting whatever goods were available, since almost any commodities they received could be exchanged for others which they needed. There was less and less inducement to earn cash or to make careful calculations of the money costs of production. Although the industrial output continued to rise slowly, the economy began to show such signs of disorder that a currency reform was indispensable. Such a reform was agreed upon and put into effect in the three western zones on 20th June 1948.

The main features of the reform were, briefly, as follows:

1. The Reichsmark (RM) lost its quality as legal tender, with the result that notes and deposits in RM could no longer be used or drawn upon.

2. A new Deutsche Mark (DM) was created, the Bank deutscher Länder having the sole right to issue the new notes and coins up to a total of DM 10 milliard — a limit which might be exceeded only in very exceptional circumstances.

3. The first issues ("Erstausstattung") of DM were made as follows:

(a) Each person received in exchange for RM 60 in notes, a per-capita allocation of DM 40 in June 1948 and another instalment of DM 20 in September 1948. Thus, with a population of 47 million in the three western zones, the maximum that could be issued was 2.8 milliard. The per-capita allocation was charged against other claims to the new currency.

(b) Business and professional men, juridical persons and associations of persons had a right to DM 60 per employee against cancellation of RM 600 (and, if the full amount was not available, the new currency could be obtained at a correspondingly lower rate — even down to RM 1 = DM 1). In all, about DM 500 million was issued under this heading (so-called "business amounts").

(c) About DM 3.4 milliard was issued to the Länder and other local authorities, the railways, the post offices and the military governments.

4. In the week from 20th to 26th June everybody had to pay his RM notes into an account at a financial institution, and the credit balances thus constituted, as well as the old accounts in RM, were treated in the following way:

(a) All balances held by public authorities were cancelled but, in exchange, the said authorities received the special grants in new money indicated under 3 (c) above (the grants in question being equal to the average monthly receipts(1) of the authority concerned during the six-month period from 1st October 1947 to 31st March 1948).

(b) All balances of financial institutions inter se were cancelled.

(c) As regards other balances in RM, the owner was credited in DM with 10 per cent. of the total left after deduction of the per-capita allocations and the "business amounts", and he was able to dispose of 50 per cent. of this DM holding (this part being the so-called "free account") after the approval of the tax authorities. The other 50 per cent. was blocked; on 30th September 1948, however, it was decided that, of the balance which had been blocked, 70 per cent. should be cancelled, 20 per cent. released and 10 per cent. left for later investment in medium and long-term securities.(2)

If account is taken of the per-capita allocation and business amounts as well as of the cancellation of 70 per cent. of the originally blocked balances, it will be found that holdings of notes and deposits, etc. entitled to conversion were curtailed in a ratio of 12.6 : 1. The ratio works out at approximately the same figure if balances owned by public authorities and financial institutions — which were not entitled to conversion but received the above-mentioned "dotations" — are included in the calculation. The Bank deutscher Länder has estimated that, after deduction of the amounts paid or charged against the per-capita allocations and business amounts, there remained an

(1) The railways and the postal administration received amounts equal to their half-monthly takings only.

(2) The balances left on so-called "investment account" may be used for the acquisition of newly-issued securities, provided the securities in question have, by an official decision, been declared appropriate for such an investment. The first security which was thus authorised was a 6 per cent. loan (repayable at the latest in 1959) issued by the German Railways in the three western zones, subscriptions being received from the end of May 1949. Balances on investment account not used for acquisition of securities will receive interest at 2½ per cent., up to the end of 1953 and be converted into free sight balances from 1st January 1954.

amount of about RM 104 milliard subject to conversion in the ratio of 15.4 : 1, the result of which is expected to be less than DM 6.8 milliard. If, however, the total amount of notes and deposits actually in circulation just before the currency reform (probably RM 140–145 milliard) is compared not merely with the amount of the new currency resulting from conversion of old currency (about DM 6.8 milliard) but with that amount plus the amount of initial grants made irrespective of holdings of old currency (another DM 6.7 millard), i.e. with a total of DM 13.5 milliard, a conversion ratio of 1 : 10.5 to 10.7 emerges. It is probably this latter ratio which gives the most correct idea of the compression brought about in the volume of currency in the three western zones of Germany.

5. Claims in RM other than deposits with banks (and similar financial institutions) were scaled down in the relation of 10 : 1, with the exception of:

(a) the debt of the Reich and similar liabilities, which have remained untouched by the currency reform (it being expected that they will be largely cancelled);

(b) claims and liabilities in respect of wages, salaries, pensions, rents, etc., to which the ratio of 1:1 was applied.

6. It should further be mentioned that provisions are to be issued by the German authorities to ensure a more just distribution of the financial burden entailed by damage of different kinds, and especially that suffered during the war or as a result of the currency reform or of reparation removals.

The amount of the new currency brought into being, in the form of notes or free deposits, is shown in the table.

Volume of free Deutsche Mark created by initial grants and conversions of RM balances.

Item	End of July 1948	End of February 1949
	in millions of DM	
Allocation per head ("Kopfgeld")	1,922	2,782
Grants to:		
"Länder" and municipalities	2,266	2,350
Business firms	269	472
Railways and post office	312	315
Military governments	772	772
Total	5,541	6,691
Add: Free accounts (due to conversion of RM balances)	3,066	5,771*
Total	8,607	12,462

* Including the 20 per cent. released in October 1948 in respect of the blocked balances. At the end of April 1949, the total of initial grants was DM 6,693 million while the total on free accounts (due to conversion of RM balances) had risen to DM 5,909 million, making together DM 12,602 million.

Substantial amounts of the new currency having been issued during the early days of the reform as allocation per head of the population and grants to "Länder" and municipalities, business firms, etc., there was not much room for the extension of fresh credits by the banking system. Certain new credits were unavoidable, but the limit of what was permissible was soon reached and in the autumn of 1948 credit restrictions had to be applied, which sharply reduced the rate of credit expansion during the winter months 1948–49.

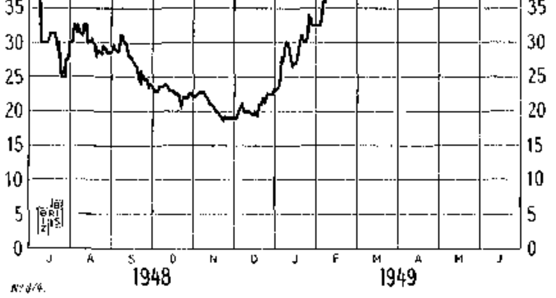
Of the grand total of about DM 19.2 milliard for the end of April 1949, an amount of DM 6.3 milliard was held in the form of notes and the remaining DM 12.8 milliard consisted of deposits. In addition about DM 500 million remained on accounts which were still blocked.

Germany: Source of the "free" amounts of notes and deposits.

End of	Official allocation: Initial grants	Official allocation: Conversion of RM balances	Official allocation: Total	Extension of credits: By the central banks	Extension of credits: By the commercial banks	Extension of credits: Total	Grand total
	in millions of DM						
1948 July	5,541	3,066	8,607	4	1,351	1,355	9,962
August. . .	5,719	3,756	9,475	— 32	2,400	2,368	11,843
September.	6,743	4,161	10,904	— 76	3,226	3,150	14,054
October . .	6,702	4,625	11,327	102	3,852	3,954	15,281
November .	6,691	5,086	11,777	270	4,368	4,638	16,415
December .	6,689	5,413	12,102	282	4,724	5,006	17,108
1949 January . .	6,689	5,508	12,197	242	4,928	5,170	17,367
February. .	6,691	5,771	12,462	222	5,299	5,521	17,983
March . . .	6,690	6,748	12,438	383	5,582	5,965	18,403
April	6,693	5,909	12,602	618	5,941	6,559	19,161

The change brought about by the currency reform seemed miraculous in more than one respect: one week the German economy was still characterised by a scarcity of goods (as great as in wartime, or even worse) and by a general withholding of stocks from the market; a week later every producer and business man seemed anxious to sell all he could, the supplies being, in a surprisingly large number of cases, more than adequate to satisfy the current demand. Most controls were soon lifted, wholesale prices establishing themselves at an index figure of about 160 (1936 = 100). The index of production rose from 51 in June 1948 (1936 = 100) to 79 by the end of the year and to 89 in March and April 1949. At first, DM notes were quoted on the Swiss market at about Sw.fcs 55 to DM 100; the quotation dropped to Sw.fcs 19 at the end of November but rose again and reached Sw.fcs 65 in April 1949 (the par via the dollar being Sw.fcs 129 = 100 DM). The essence of the change was that money had again become scarce and was therefore sought after: in place of the flight from the RM, there was a willingness on the part of the average German to sell his goods against DM, to work for payment in DM and to save in terms of DM. If anybody had ever believed that "money did not matter as a guide to the economy", the experience of western Germany after 20th June 1948 would have provided a striking object-lesson to the contrary.

Rates of D.Mark notes in Switzerland.
Daily, in Swiss francs for 100 D.Mark.



A few days after the announcement of the currency reform in the three western zones, new currency measures were put into effect in the eastern zone of Germany also. In some respects these measures resembled those adopted in the west (which was only to be expected considering that the occupying powers had previously been discussing the basic principles of a currency reform applicable to all four zones). While in the west the provisions adopted were based on essentially monetary considerations, those adopted for the eastern zone clearly show that privileges in the matter of conversion have been determined by political and social considerations; moreover, in the eastern zone the general economic policy remained unchanged — in contrast to the western zones, where controls were generally lifted and more economic freedom was thus introduced.

The main provisions of the currency reform in the eastern zone were as follows:

1. It was prohibited to import notes or coins made invalid in the western zone or the new currency issued in that zone.

2. At first the old notes were kept in circulation but with special coupons attached to them; all fractional currency retained its full value.

3. The rates for conversion of notes were:

   (a) 1 : 1 for a per-capita allocation of 70 marks;

   (b) 10 : 1 for further notes, with a maximum of RM 5,000 for a family, excess amounts being placed in a blocked account to be available for disposal only after it had been proved that the money had been rightfully earned, i. e. not through war deliveries, speculation, black marketing or illegal price increases;

   (c) 10 : 1, without limitation, for notes held by business enterprises, institutions, etc.

4. Savings deposits were converted at privileged rates: the first RM 100 in the ratio 1 : 1, a further amount up to RM 1,000 in the ratio 5 : 1 and the remainder at 10 : 1 — with a reservation (as in (b) above) for amounts exceeding RM 5,000.

5. Other deposits with financial institutions were in principle converted in the ratio 10 : 1 — with the same reservation for amounts above RM 5,000.

   There were, however, certain privileged bodies whose funds obtained conversion in the ratio 1 : 1, namely:

   (a) balances held by the political party and trade-union organisations as on 1st May 1948;

   (b) balances held by public bodies and publicy-owned enterprises;

   (c) balances held by other industrial enterprises to the extent that wages were due and also amounts corresponding to a week's turnover. Firms other than industrial enterprises received only amounts corresponding to a week's pay.

   (d) bank's own funds in the form of capital and reserves.

6. Social-insurance institutions had all their funds converted at 2 : 1 and other insurance institutions at 5 : 1.

7. Blocked deposits from the time before the capitulation were generally converted at 10 : 1 and, when they belonged to Germans, were transformed into a 3 per cent. loan.

8. Certain amounts were not converted: inter alia, the loans issued by the Länder in 1946 and the debt of the Reich.

9. No change applied to prices, wages, salaries, pensions, taxes, etc.

New notes expressed in Deutsche Mark of the newly-established Deutsche Notenbank were issued in July 1948 against the notes to which coupons had been attached. Only DM 70 were exchanged in cash, amounts in excess of that limit being credited to temporarily blocked accounts. Further, special provisions were issued with regard to accounts with financial institutions.

No detailed figures have been published concerning the amounts converted but, according to a statement by the Soviet Military Administration, an amount of 28 milliard Reichsmark (and Allied military marks) was affected, against which 4,112 million was issued in new notes of the Deutsche Notenbank in July 1948. It was estimated that, at the end of January 1949, 814 million "Ostmark" was held by credit institutions and about 3,300 million was in circulation (the latter amount is reported to have fallen to 2,750 million in April 1949). At the same time the amount of deposits was estimated at 7–8 milliard — making altogether a "money volume" of 10–11 milliard Ostmark (as compared with DM 19.5 milliard in the three western zones).

Special difficulties arose in Berlin, where the Deutsche Mark of the Bank deutscher Länder (the "Westmark") was made legal tender in the western sectors while the "Coupon mark", and later on the Deutsche Mark of the Deutsche Notenbank (the "Ostmark"), was the currency of the eastern sector of Berlin, as in the eastern zone. The "Westmark" is not valid in the eastern sector, but the "Ostmark" was allowed to circulate in the western sectors even after 20th March 1949, when the "Westmark" was made the sole legal tender in the western sectors. These sectors were at the same time given their own "Berliner Zentralbank" for the issue of currency, etc. Including an advance from the Bank deutscher Länder and about DM 145 million for conversion into Westmark of certain further amounts in Ostmark, the total issue for the western sectors of Berlin would come to DM 690 million. The money issued for these sectors is legal tender of the same standing as the Deutsche Mark current in the three western zones, but the Berliner Zentralbank is not attached to the central-bank system of western Germany, nor is there a system of free payments from the western sectors of Berlin to the western zones of Germany but transfers in the reverse direction are allowed. In the western sectors of Berlin nearly 40 exchange offices have been opened for the interchange of the two currencies. The rate is fixed every day according to the supply of, and demand for, Ostmark; at the beginning of June 1949 the rate was 4.50–4.70 Ostmark for one Westmark. There are no exchange offices established in the eastern zone of Berlin nor in the eastern zone of Germany, but at the frontier between the eastern and the western zones amounts in Westmark, which is a currency not admitted in the eastern zone, may be exchanged at a rate of one Ostmark for 1.25 Westmark.

* * *

Some eight weeks of actual fighting took place between the Allied crossing of the Rhine on 8th March 1945 and the conclusion of the war on German soil, but twenty-two months elapsed in Italy between the Allies' landing in Sicily (on 10th July 1943) and the final liberation of the north (on 25th April 1945); and most of these months were taken up by an inch-by-inch fight, with almost complete disorganisation of all administrative services and, in monetary matters, the issue of notes by two rival Italian governments as well as by the Allied commands.

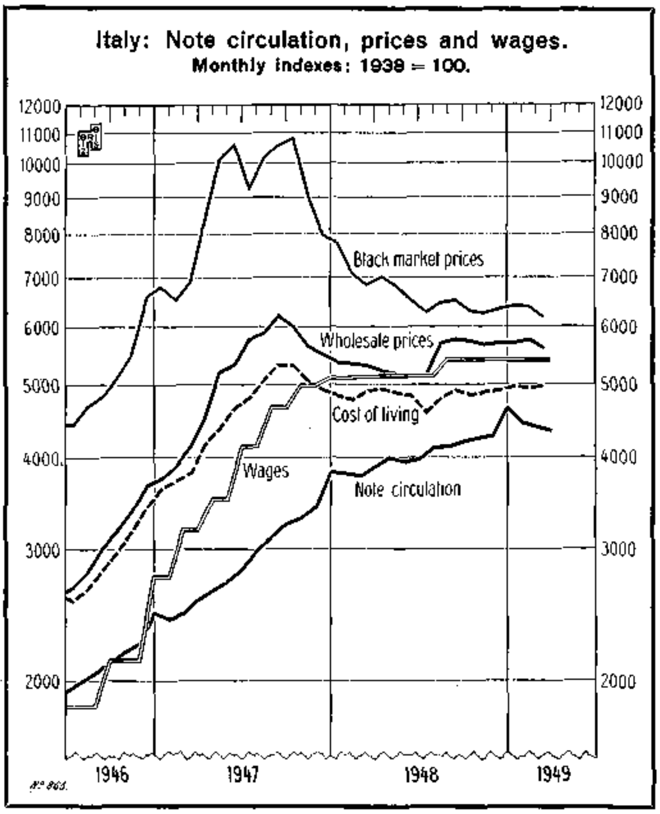
By September 1947 effective prices in the black markets were more than 100 times above the pre-war level, although the note circulation had risen by only 30 times (the very high velocity of circulation which this indicates reflecting distrust in the currency), while the budget deficits were still overwhelming and production was at a low rate. But the government and other services soon began to cope with the problem and, in August 1947, a shock was administered to the Italian economy by the enforcement of severe credit restrictions, which applied a brake to the credit expansion. To obtain funds to meet their expenses, firms were generally compelled to reduce their inventories, and such reductions, in conjunction with good crops and post-UNRRA aid from the United States, brought about a sudden reversal of the price trend. The official index for wholesale prices (1938 = 1) fell from 62 in September 1947 to 51 in July 1948, returning to 57 in December 1948 after food subsidies had been largely abolished and the tariffs of many public services increased; the free prices (legal or illegal) fell more precipitously — in some cases by over 40 per cent.

The official cost-of-living index remained unchanged, except for the effects of the abolition of the food subsidies, which were reflected in a rise of 7 per cent. in the index figure. It must not be forgotten that, although money wages were kept stable, individual households benefited by the improvement in the supply position and the fall in all kinds of "free" prices.

Wholesale prices for Milan.

Groups of commodities	Official prices		Free prices	
	October 1947	May 1949	October 1947	May 1949
	Index: 1938 = 1			
Raw materials	54	58	122	64
Semi-finished products	49	49	67	50
Finished products . . .	52	54	113	56
General index	52	55	108	58

Increased confidence led to a slowing-up of the velocity of circulation, and more notes were soon required by the public. In fact, the note circulation rose from Lit. 687 milliard in October 1947 to Lit. 970 milliard in December 1948, i.e. by more than 40 per cent. in fifteen months, but declined afterwards to Lit. 900 milliard at the end of March 1949.



It is a remarkable thing that in Italy, notwithstanding the war and post-war inflation, the farmers and certain other sections of the population never ceased to save in forms of the national currency; coupled with the increase in the amount of notes held by the public, these savings, mostly represented by deposits in local banks together with subscriptions to Treasury bills (partly out of the deposits), made it possible to finance a budget deficit which was still fairly large without prejudicing the purchasing power or the foreign exchange value of the lira.

In France, up to the time of the Liberation, disobedience to the occupying power was felt to be the duty of a patriotic people; but the result was that rationing and control over prices and wages came to be largely regarded as alien to French ways, i.e. as part of a totalitarian system. As early as the autumn of 1944, the French authorities had to abandon the system of obligatory deliveries of agricultural products, in so far as the bulk of small producers were concerned. No price control applied under such circumstances could become effective; regulations remained legally in force but it is highly debatable whether a mistaken belief, held in some circles, in the adequacy of the existing control did not for a time delay the taking of really effective measures. As long as budget expenditure continued to be covered by inflationary methods, large profits were made and prices rose. The workers demanded higher pay, and again and again the government had to authorise increases by 15, 20 or 30 per cent. in money wages; but, since such increases were generally too large to be met from existing profit margins, France: Indexes of prices and note circulation.

Month	Average of wholesale and retail prices	Note circulation
	Index: 1938 = 1	
1938 December	1	1
1944 September	3	5.7
1945 December	5	5.1
1946 "	8¼	6.5
1947 "	13	8.3
1948 "	19½	8.9
1949 February	18¾	9.2
March	18½	9.4
April	18	9.4

they were necessarily followed by general price increases. Knowing that the Control would accept increases in costs as justification for immediate and corresponding increases in prices, and counting upon obtaining a sufficiency of credit facilities from the banks whenever prices and wages rose, manufacturers did not as a rule find it necessary or opportune to oppose increases in money wages, most of them being anyhow in a position to dispose of their output on the domestic market without having to trouble about exports. As prices rose, the French people began to use their notes more quickly and to bring them out of hoards — which was tantamount to an increase in the velocity of circulation.

By the end of 1948 prices had risen twice as much as the note circulation; but such a situation naturally afforded an opportunity for action with good prospects of success, and the beginning of 1949 saw a reversal of the price trend. By that time the root cause of the rise in prices — the inflationary expansion of monetary demand as a result of budget deficits — had been eliminated; and further abrupt increases in money wages had been avoided. The price decline which began to characterise the markets had not been decreed by the Control but was the combined effect of two sets of factors: on the one hand, increased supplies (attributable to a better harvest, higher industrial output and the goods and services received as Marshall aid) and, on the other hand, the check on the issue of new purchasing power (by a better balancing of the budget, the application of credit restrictions and some accumulation of balances on the account representing the counterpart of Marshall aid). It was thus realised that price policy must not be thought of as sufficient in itself but as something related to the policies pursued in the domain of public finance and the credit system, in the field of foreign trade and in the system of foreign exchanges.

* * *

The four countries dealt with above — Austria, Germany, Italy and France — have each had a different price history during the last few years. In the course of 1948, however, they all arrived at a point of price stability signifying for them — one may hope — the end of the inflation engendered by the second world war. But these four countries are not alone in having reached such a point. A state of affairs in which the price rise has been checked

Percentage change in wholesale prices.

Countries	Percentage change in 1946	in 1947	in 1948	between October 1948 and March 1949
Belgium	+ 21	+ 12	+ 5	— 4½
Denmark	+ 9½	+ 9	+ 9	+ 1
France	+ 80½	+ 44	+ 62	— 1
Italy	+ 38	+ 50	+ 3	— 3
Netherlands . .	+ 22½	+ 5½	+ 4	+ 3½
Norway	+ 4	+ 3	+ 2	+ 3
Sweden	+ 1	+ 7	+ 6	0
Switzerland . .	+ 2½	+ 6	— ½	— 1½
United Kingdom	+ 6	+ 13	+ 8½	+ ½
United States .	+ 31½	+ 16	— ½	— 4

is becoming the rule rather than the exception, and in some countries the trend has even been clearly reversed.

It was only in France that the price rise in 1948 was as sharp as in the previous three years but, as may be seen from the table, a reversal of the price trend occurred in that country between October 1948 and March 1949.

Before indicating the changes in the general supply-and-demand position and their effect on price movements, it may be useful to make certain observations of a more general character.

(i) During the past few years there has been a distinct change in the atmosphere of economic thinking: while the war was still going on and for some time after it had come to an end, it was, for instance, widely believed that before long a post-war depression would set in, especially in the United States, and that it would consequently be justifiable to bolster up the volume of monetary demand either by budgeting for a deficit or by financing investments through an extension of bank credits. Quite apart from any wish to influence a particular business trend, it would seem as if the opinion had gained ground that a fairly abundant volume of monetary demand would be all to the good in that it would secure the continuance of a high level of employment, the system of controls being relied upon to prevent an inflationary rise in prices and the emergence of a deficit in the balance of payments. But, during the first four years after the war, instead of a depression in the United States, boom conditions continued, on the whole, to prevail; those who practised inflationary financing, moreover, found that, despite all their measures of control, they could not avoid a disquieting gap in the balance of payments. It was soon discovered that freshly created credits could not serve as a substitute for genuine savings or make good a shortage of capital, and it became evident that not even a controlled economy could dispense with a sound currency; for, without it, income and savings could not bear witness to the availability of real resources. 1947 was an important year in the history of European economic thinking, for it was then that, under the influence of a number of setbacks and disappointments (continuing deficits in the balances of payments, a gradual exhaustion of monetary reserves, the failure of the convertibility of sterling and, on top of it all, poor harvests), many a man in a responsible position — to say nothing of the public in general — had to discard economic dreams for economic realities. It became increasingly realised that the supply of money had to be brought into relation with the supply of goods and that, by and large, the ordinary physical controls would not work satisfactorily without financial order. The Interim Report of O.E.E.C., published in Paris on 30th December 1948 and approved by the nineteen governments participating in the European Recovery Program, lays down the principle that "the budget must be balanced. For there is universal agreement that inflation cannot be prevented, in the face of an inappropriate fiscal policy, by mere multiplication of specific controls over particular prices and the use of particular resources".

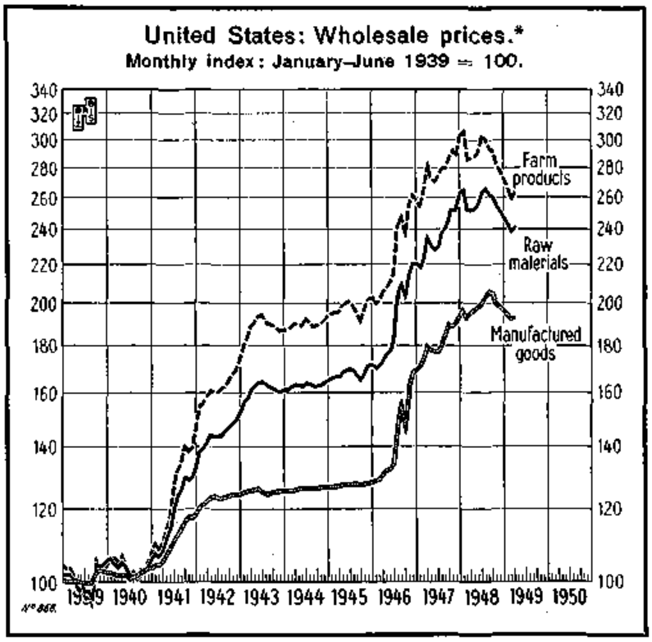
(ii) Those who had expected a depression had primarily the United States in mind, for they assumed that in that country the current demand for either consumption or investment goods would not be large enough to provide outlets for the mounting peacetime output of goods and services. But, for reasons already explained, no disequilibrium arose between costs and prices, the demand being so well sustained that prices continued to rise.* Those who had expected a depression were, however, right in forecasting a very high level of output in the United States and also in assuming that the trend of American business conditions would be of particular importance for the rest of the world. Europe had had to bear the effects of the second world war before the disorganisation caused by its predecessor had been really overcome; it suffered, indeed, very great losses in capital (within its own continent and on its investments overseas) as well as in current production, and it thus emerged very much poorer from the war. The experience of the United States had been just the contrary: whereas in the years before the outbreak of war the United States had been harassed with the problem of about 9 million unemployed and a national income which per head of the population was in real terms some 10 per cent. less than in 1929, the great activity after the second world war provided over "60 million jobs" and the national income per head of the population rose, in real terms, to about 40 per cent. above the 1929 figure.

While it cannot be denied that the almost uninterrupted rise in the American price level from the summer of 1945 up to the first quarter of 1948 helped a number of European countries to maintain the exchange value of their currencies, it is equally certain that, as long as prices continued to rise by over 10 per cent. a year in the United States, it was well-nigh impossible for other countries to achieve

* It may be pointed out that it is not the granting of assistance to Europe which accounts for the difference in the business trend in the periods following the first and the second world war respectively, since in relation to the national income foreign aid granted by the United States was no greater in the years 1945–49 than after the first world war (in neither case did it exceed 2½ per cent. of the current national income).

price stability (unless they were prepared to give up the exchange link with the U. S. dollar).

Early in 1948 it was agricultural prices in the United States which were the first to feel the downward pull; since they had risen more than others, however, that particular decline could be looked upon more as a natural adjustment of an extreme and untenable position. In the course of 1948 industrial raw materials were also affected, but here again the prices in question had previously risen more than the general run of manufactured products, the prices of which have so far not fallen very much (and it is still doubtful whether they will do so in the near future). It is only natural that price movements in the United States should be closely watched; up to the spring of 1949 all that can really be said is that the cessation of the price rise in a number of European countries could not have happened without the reversal which has occurred in the price trend in the United States.



* Logarithmic scale.

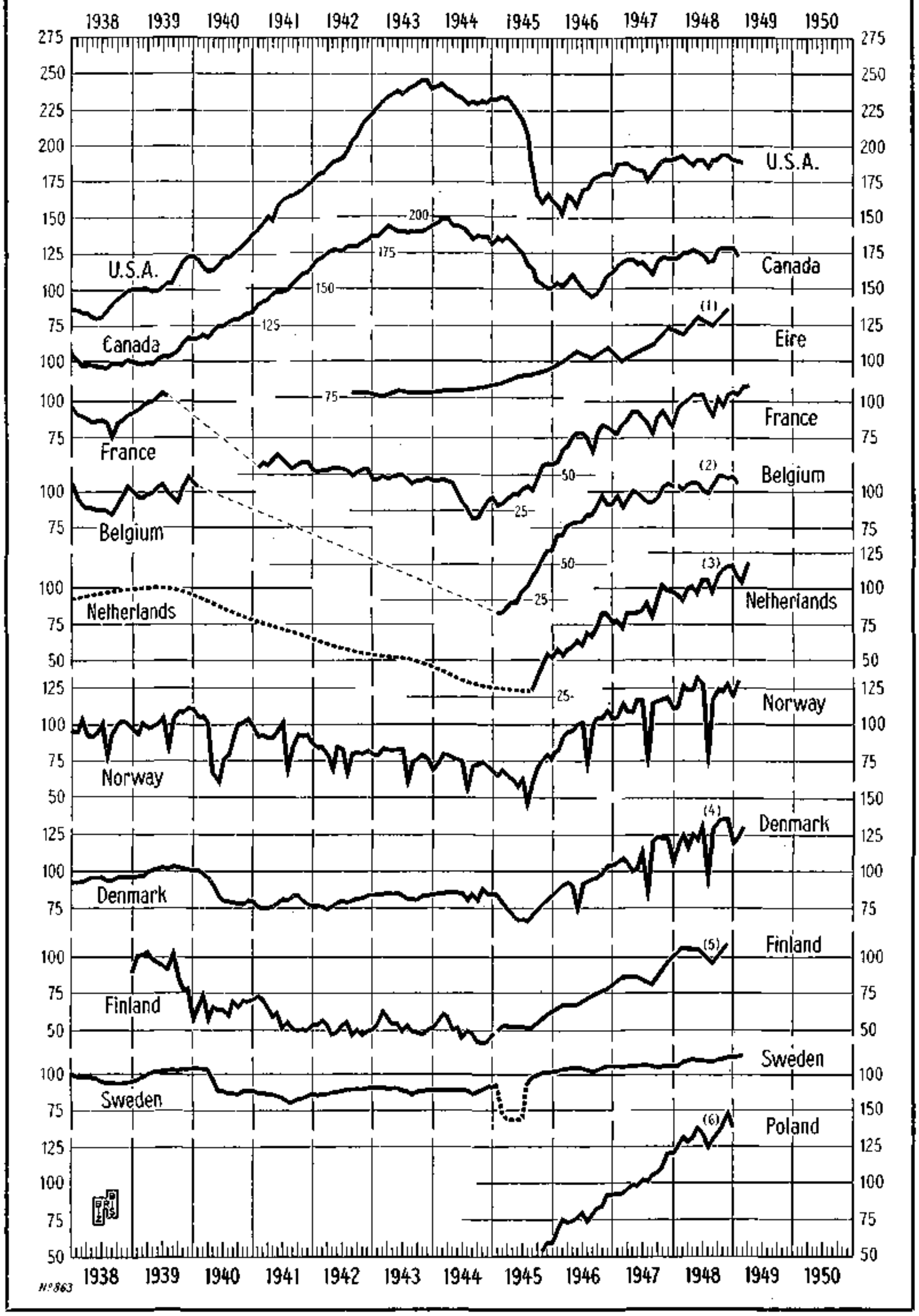
(iii) Although the motive force in the post-war price rise has been an abundance of monetary demand in relation to supplies, the strategic position held by movements of money wages and other personal incomes must not be forgotten. It could clearly not be expected that workers in general would be satisfied with an unchanged money income while an expansion of monetary purchasing power was sending up prices and swelling the earnings of many other income groups. The workers themselves soon found, however, that increases in money wages which were followed by corresponding increases in prices did not benefit them but, by the disorganisation caused to the general economy, led rather to a deterioration of the position of most people (a typical and unwanted exception being the black-market operators). Without some respite from continuous increases in the level of money wages, it was obviously difficult — if not impossible — to establish a balance in the general economic situation and reverse the inflationary trend. The methods adopted to gain the necessary respite have varied from country to country, a solution being in some cases arrived at through agreements with representatives of the workers and other interests involved — sometimes only after prolonged conflicts. But, whatever the method adopted, a position would seem to have been reached early in 1949 in which such increases as may be made in future in personal money incomes need not occasion a general rise in prices. If that should prove to be the case, the increases in money wages would amount to a real improvement in the workers' position; indeed, an improvement all round would result from an increase in supplies combined with a downward adjustment in prices (even if the reduction were not so pronounced generally as with regard to certain foodstuffs in France, where prices of potatoes and vegetables fell by some 30–40 per cent. in the late autumn of 1948).

In a "Statement on personal incomes, costs and prices", presented to Parliament in February 1948, the British Government emphasised that "the danger of inflation is ever present" and how "experience has shown that, when it comes to a race between rising prices and personal incomes, prices will always win in the long run, so that conditions become progressively worse for the holders of all personal incomes but particularly for wage-earners. It is essential, therefore, that there should be no further general increase in the level of personal incomes without at least a corresponding increase in the volume of production."

The reversal of the price trend means the disappearance of the super-boom and, at the same time, of the pronounced sellers' markets which still prevailed in most countries in 1948. It may well be that in a boom period production and trade reap, for a while, some real advantages from an unusual state of animation — in the past four years, for instance, there has been a high degree of investment activity, especially by means of profits ploughed back into industry. But the danger is that at such a time many projects are started without due discrimination — that, indeed, there is a temptation to do too much in too many fields, with the result that too great a strain is imposed upon the economy, and a serious lack of balance emerges before long.

A reversal of the trend may then administer a salutary shock, in which case the sobering effect would lead to the elimination of inefficient traders and producers and the resumption of proper business calculations. The consumer would once more be served with efficiency and consideration, and quality would again count. Each phase of business has, however, its own difficulties; producers faced with falling quotations begin to ask for price support to be given them by the government, and other new problems arise. It must be remembered that many maladjustments (including, for instance, the maintenance of unrealistic exchange rates) may have only slight adverse effects so long as the boom lasts, since sales are then easy, but that such maladjustments will make themselves increasingly felt when a buyers' market prevails once more. The gradual return to a normal structure of demand will necessarily call for a return to the normal structure of production, and this

Volume of industrial production.
Indexes: January-June 1939 = 100.



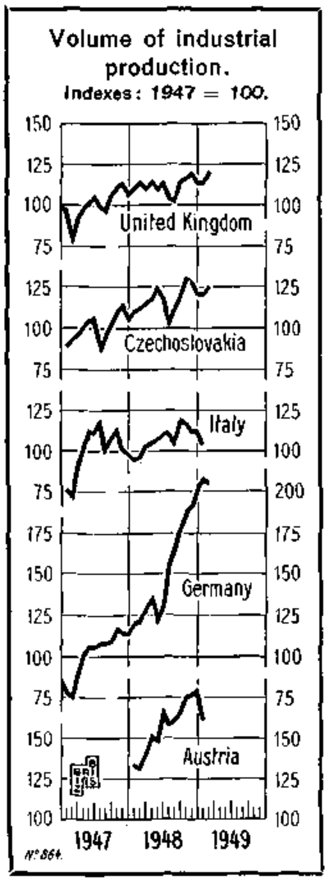
(1) Quarterly indexes: 1939 = 100.
(2) New index since 1948.
(3) Index 1939 = 100.
(4) New index since January 1947.
(5) New quarterly index since 1945.
(6) Index 1938 = 100.

will often involve a new relation between the output of capital and consumers' goods and an adaptation of agricultural production to the general rate of recovery.

There are more and more indications that the world economy is passing through a period of transition from concern with the problem of insufficient supplies to mindfulness of the problem of maintaining sufficient demand. Typically enough, measures are already being taken in the United States for a relaxation of the cash requirements of banks and of the restrictions which generally apply to the granting of instalment credits. But the new phase is only in its infancy and has not yet become characteristic for all countries. In reviewing the past year the essential task is to analyse the changes in supply and demand which have brought the post-war inflation to an end.

* * *

1947 had been a year of vicissitudes in Europe: it had started with a severe winter and a fuel crisis; it went on to a rainless summer resulting in a bad harvest. 1948 fared better; production could proceed normally, shortages were gradually overcome and the weather happened to be unusually favourable — all of which helped the supply position.



1. For the world as a whole, the volume of industrial production would seem to have been 5 to 10 per cent. higher in 1948 than in 1947. World figures are necessarily somewhat unsure, since estimates have to be made for vast territories regarding which the information available is rather scanty.

In the United States, the most important industrial country in the world, the physical output of the factories and mines, as measured by the Federal Reserve index of industrial production, was 3 per cent. larger in 1948 than in 1947, while the corresponding increase had been at the rate of 10 per cent. from 1946 to 1947. The slower pace in 1948 was mainly due to the fact that reconversion had been completed; but — especially towards the end of the year — it seems also to have been a sign of something like a turn in the business trend.

In 1948 the industrial output in the United States was 92 per cent. above the 1935-39 average, but in most of those years there were some 9 million unemployed and an average volume of production 10 per cent. below the 1929 level. 1940 was a year of rearmament, with production 13 to

14 per cent. higher than in 1929. It is interesting to note that, even so, the volume of industrial production in 1948 was fully 50 per cent. above 1940.

After the first world war it was in almost every respect appropriate to take the year 1913 as a starting-point and basis for comparisons, that year (although not conspicuously a boom year) marking the peak of a rapid industrial expansion at the beginning of which the various currencies had already been in substantial equilibrium with one another for a long time. No year immediately preceding the second world war possesses these characteristics. In the first post-war years it was usual to take 1938 as a basis; while in that year the harvest was definitely above the average, industrial production in most countries had suffered a severe setback in comparison with the previous year. Recently, a number of institutions have adopted 1937 as the basic year and in some respects it undoubtedly provides a better basis. But, for certain countries greatly dependent upon the trend of the world "Konjunktur" (e.g. Belgium), a period of rapid fluctuations cannot offer any single year which is a satisfactory basis. To bring out the difference it makes if 1937 is chosen as the basic year instead of 1938, the following table shows for some countries the index of industrial production calculated on the one basis and then on the other. As regards international comparisons, moreover, it must be remembered that in 1937, as in 1938, the exchange value of a number of currencies was subject to fluctuations.

Industrial production in 1948
with 1937 and with 1938 as base.

Country	1937 = 100	1938 = 100
Belgium	93	115
Canada	168	177
France	98	111
Italy	92	98
Netherlands . .	114	113
Sweden	144	143
United Kingdom	109	116
United States . .	170	216

In the graphs on the two preceding pages, showing the volume of industrial production, the period January–June 1939 is taken as base (= 100). In that half-year production had in most countries recovered somewhat as compared with the level in 1938.

In Europe as a whole — excluding the U.S.S.R. but including Germany and eastern Europe — the volume of production in 1948 did not reach the 1938 level and was probably some 10 per cent. below the 1937 level. But the drag was mainly Germany: without that country, the production level of 1938 is estimated to have been passed by 13 per cent. and it follows that the 1937 level was probably exceeded by 5 per cent.

Western Germany recovered very quickly after the currency reform (see page 43) and elsewhere in western Europe good, though less spectacular, progress was made. With one or two exceptions, the industrial production in this group is above the level for the best pre-war year. But, as the United States will serve to show, once conversion to peacetime purposes has been achieved and most enterprises are working at full capacity, it is no longer possible to count on such a rapid expansion as in the first post-war years.

2. As regards agricultural production, the 1947 harvest in Europe was 20 to 25 per cent. below the average for the years 1937–38; in 1948 the shortage had been reduced to between 10 and 15 per cent. But, if it

were possible to count all that is obtained from the more intensive use of gardens, small plots of land, etc. or simply escapes the statistics (since it is disposed of in a clandestine way), the margin between the actual present production and the normal pre-war output would probably prove to be very small. When in any country relatively free trading in foodstuffs has been restored, prices in unofficial markets have often fallen and, in more than one case, the supplies then appearing have been almost as large as before the war. Still, Europe remains vulnerable as regards food: its population has risen by 10 per cent. since 1938; in some places the soil has become exhausted; and structural changes of diverse kinds and difficulties of trading between different parts of Europe have not helped to bring supplies to the markets. In this respect, the receipt of Marshall aid has supplied vitally necessary assistance for some of the countries in western Europe.

3. The transport system of Europe has also been put into working order, including the reconstitution of ocean-going ships, owned and operated by European companies, up to the pre-war tonnage. This is improving Europe's earning power; and other invisible items (tourist traffic on a scale exceeding pre-war records) are also making their contribution. Neither individual European countries nor Europe as a whole can forget what trading in a wide sense (including banking, insurance, etc.) contributed to their earning power. Close contact in commercial and financial relations often forms a basis for the rapid adaptation of production to what is effectively demanded in different parts of the world.

4. Finally, Europe's own resources in 1948, as in the previous post-war years, were supplemented by assistance from abroad. Full information is not available regarding the loans and other forms of assistance received by the eastern European countries from the U.S.S.R. but some indications are given on page 22. As regards the western European countries, the deficit in Europe's balance of payments shown in the table in chapter III was practically all on their behalf, so that they accounted for about \$5½ milliard in 1948. In the previous year Europe's deficit had been about \$2 milliard higher but then a certain part was in the form of UNRRA aid, etc. connected with eastern European countries. If the difference of \$2 milliard had all been a reduction suffered by the countries in receipt of Marshall aid, this reduction would have been equal to less than 2 per cent. of the aggregate of their present national incomes. Thanks to the better harvest and the rise in industrial production, western Europe increased its current income of domestic origin by more than 2 per cent. from 1947 to 1948 and, by the end of the latter year, it had a much better supply of goods and services than a year earlier (as could be perceived without the aid of statistics by anyone having visited western Europe during the years in question). The assistance received from abroad represents a very valuable addition to the recipient countries' own resources and it is well understood, and agreed, that the aid must not be used for current expenditure but for the building-up

Commodity aspect of Marshall aid.

Commodity groups	Procurement authorisations
	millions of dollars
Food, feed and fertilisers	1,384
Fuel	562
Raw materials and imported products	1,039
Machinery and vehicles	577
Miscellaneous and unclassified . . .	145
Total	3,707

of net capital assets. The accompanying table shows the main categories of commodities for which procurement authorisations had been issued by E.C.A. up to the end of December, 1948.

The fact that, apart from capital goods (such as machinery) and industrial prerequisites in the form of fuel or raw materials, Europe has received a considerable proportion of the aid in the form of consumable goods (mostly food but also some others) does not in any way mean that this part of the aid has not been used for capital purposes. A country may, of course, import food to be consumed by workers who produce capital goods and a similar use may be made of other kinds of imports. For purposes of comparison it may be mentioned that in the past many a country borrowing abroad for the construction of railways has imported the wheat, lard and coffee which the railway workers consumed while engaged on the building of the railway.

But, if it is not the nature of the commodities imported which determines whether the aid is for current or for capital purposes, attention must be directed towards the really decisive circumstances, which are intimately connected with the whole economic and financial situation of the country concerned (as referred to more fully in chapter VII).

Hand in hand with the rise in output, the authorities in most countries have made more intense and largely successful efforts to curb every expansion of monetary purchasing power not warranted by increased production, their object being to arrive at a proper **limitation of effective demand**. For such a result to be achieved different methods have had to be employed.

1. In some countries measures were obviously required to do away with a redundancy of money inherited from the war and, as shown previously, a **direct curtailment of the volume of money** has been effected since the autumn of 1947 in Austria, in the U.S.S.R. and in the eastern as well as the western part of Germany.

The rise in the level of wholesale prices in the United States by more than 50 per cent. since 1945 caught up an increase in prices which had already occurred in some countries, while in others it gave rise to a "sympathetic" price increase. In both cases an adaptation to the redundant volume of monetary purchasing power was facilitated. It remains a moot point whether in certain countries liquidity is not even now too great — in some markets there is still a possibility of monetising part of the heavy national debts.

2. The most important measures for the curtailment of excessive demand, however, have been those taken for the purpose of putting the budgets in order and it cannot be denied that in this field great progress has been achieved. Let it be said in passing that international comparisons of government revenue and expenditure present great difficulties, since the distinctions between ordinary and extraordinary, current and capital, over-the-line and under-the-line, expenditure vary considerably from country to country. Outlay is, moreover, sometimes charged to Treasury accounts without being shown as part of the budget expenditure. Finally, social contributions outside the budget often represent a heavy charge, which can no longer be neglected in comparisons of this kind; and here a particular difficulty arises from the fact that some countries include the greater part of the expenditure for social benefits in the budget and thus cover such expenditure by taxation, while other countries keep it outside the budget and meet it through special contributions from employers and employed.

Whatever the system adopted, however, it is necessary to stress the great progress which has been made in establishing a true equilibrium between current expenditure and current revenue; most countries go even further and aim at paying at least part of their capital expenditure from the yield of taxation. And a few countries in Europe (Switzerland and the United Kingdom) have managed to produce a surplus of revenue over all current and capital expenditure and have in that way been able to reduce their national debts, while Sweden has budgeted for a small over-all surplus for the year 1949–50. Outside Europe, the United States had in 1947–48 a budget surplus of over $8 milliard, which was helpful in re-establishing balance in the credit system; but it would seem as if, with a reduction in taxation and somewhat higher expenditure, there will be a slight deficit in the fiscal year ending 30th June 1949.

Budgeting for a surplus has come to be regarded as an anti-inflationary measure by which a kind of forced savings can be procured as an offset against heavy investments; and, although a budget surplus alone (without an appropriate credit policy) may not produce all the desired results, the realisation of a surplus is no doubt a very potent factor. But, at the same time, it must be remembered that heavy taxation required to bring about an over-all budget surplus can hardly avoid taking toll of already existing capital assets (and not only through the collection of death duties) and it will also very likely diminish the current flow of private savings. Thus the surplus in the budget will not, in its entirety, constitute a net addition to the volume of genuine savings. To what extent a budget surplus really generates savings in an economy becomes a question of fact rather than of principle.

When all current and some, or all, capital expenditure is paid for by current revenue the burden of taxation then begins to be severely felt; it will at the same time be brought home to people that heavy taxation makes for rigidity in economic life and in that way represents an obstacle to economic enterprise and progress as well as to individual liberty. Demands for retrenchment of government expenditure have recently become insistent; the question arises not only of eliminating waste in each branch of the administration but also of overhauling the scope of government functions, including those assumed during and after the last war. The problem is not merely one of equilibrium in the public finances; it is also a question of the level of government expenditure on all counts.

3. The example of several countries (the most typical being that of Italy in 1947) has shown that even with a moderate budget deficit it may be possible to reverse an inflationary trend by the application of credit restrictions; and it is a fact that, whatever the outcome of its budget accounts, each country has to frame an appropriate credit policy.

Immediately after a devastating war, when the main task is to get the economy into working order again, even an inflationary resort to credit creation may be temporarily justified; but such methods of financing must not on any account be maintained for long. Bitter experience has taught more than one people that the use of the banking system to cover budget deficits involves inflationary spending and steps have been taken nearly everywhere in Europe to guard against such a danger; but it has not been so clearly understood that what is sometimes called "pre-financing", i.e. the extension of credit while the work of producing capital assets is still in full swing, may be equally dangerous. For when it is a question of capital assets, e.g. the building of a factory, the amounts invested will only gradually be returned by slow amortisation over many years. Indeed, the producer, if he is to keep up the construction of capital assets, is likely to need more and more credits. That is how "pre-financing" differs from borrowing for the provision of working capital: nowadays the construction of a factory may take no more time than the manufacture of many types of consumption goods (especially certain woollen fabrics — not to mention "durable consumers' goods" such as automobiles, radios, refrigerators, etc.); but, when consumers' goods are sold to a customer and paid for in the normal way, the working capital of the producer is reconstituted, so that he is under no compulsion to make new demands on the banks for more funds to maintain his production. The producer may not be able to repay the bank immediately, since he may have continued need of his working capital; but, granted relatively stable prices, he should not require more. In the case of long-term investments in fixed capital, the same thing will happen provided that, after the pre-financing by the banks has been running for three or six months or (say) even longer, the firm that acquired the capital goods is able to repay the producer (and the producer the bank) from current savings, i.e. from the proceeds of an issue of bonds and shares or from savings within the particular firm ("self-financing"). But the trouble with many markets in recent years has been that savings have not been forthcoming for the "unloading" of the bank credits extended for the purpose of "pre-financing". When no such unloading takes place, freshly created bank credits used for the reconstruction of fixed assets or new equipment are just as inflationary in their effects as the financing of a government deficit.

To keep the demands on the credit system within safe limits and at the same time to encourage savings, rates of interest have been raised in a number of countries — and in some quite considerably (see chapter VII). As a rule, an increase in interest rates has not been the only means employed: it has usually been combined with the application of qualitative and quantitative credit restrictions. There is, of course, no necessary contrariety between using methods of direct control and resorting to price changes in order to establish equilibrium, since the one method can be employed to strengthen the effect of the other. For examples of such combinations see chapter VII.

4. Reference must finally be made to another way of generating monetary purchasing power, namely, the one which comes into operation through the agency of the public itself when the velocity of circulation increases. In the past the velocity of circulation both of notes and of deposits has often, with relatively slight cyclical variations, been extraordinarily constant over long periods. But in recent years there have been important changes in a number of countries. When confidence is upset, people may reduce the amount they habitually hold as cash in notes and such a reduction is tantamount to the production of a larger effective demand by the same quantity of money in circulation. That happened in France from the middle of 1946 up to the end of 1948 — but after that there was a manifest reversal of the trend. And in Germany the first eight to nine months after the introduction of the currency reform witnessed several changes — and even rather abrupt ones — in the velocity of circulation (see chapter VII).

As monetary confidence is restored, however, there will be a return to greater steadiness in regard to the velocity of circulation; and it may even be that a

"Real value" of note circulation.*

Note circulation of	End of 1945	End of 1946	End of 1947	End of 1948
	Indexes January–June 1939 = 100			
Austria	.	333	160	173
Bulgaria	363	341	318	.
Czechoslovakia	95	133	183	216
Denmark	211	210	198	193
Finland	132	150	142	141
France	106	76	63	45
Hungary	.	24	41	61
Italy	.	70	73	88
Netherlands . .	68	114	120	119
Norway	198	249	268	274
Portugal	180	184	187	178
Spain	105	98	100	98
Sweden	171	175	164	171
Switzerland . .	126	131	133	140
Turkey	111	120	112	111
United Kingdom	184	184	160	143
United States .	306	249	220	214

* Index of circulation as divided by the average of the wholesale-price index and the cost-of-living (or retail-price) index (in each case, January–June 1939 = 100).

Note. The index figure of 100 means that the note circulation has risen to the same extent as prices (as was, for instance, the case in Spain at the end of 1947, according to the above table). In most countries the note circulation has risen more than prices: in the United States, for instance, 114 per cent. more than prices by the end of 1948 — an extra rise largely explainable by the increase in production. In France, Hungary and Italy, on the other hand, there was a greater rise in prices than in the note circulation.

propensity among the public to hold more notes (simply for reasons of expediency) will actively help the authorities to regain control of the monetary situation (as was the case in Italy in 1947 and 1948).

What such control means is not "deflation" but an adaptation of the volume of money and credit to the flow of production and the growth of the real earning power of the country through its internal and external activities.

* * *

It is evidently necessary to think of "supply" and "demand" as aggregate items and thus relate them to the total *available resources* (whether of domestic origin or obtained from abroad) and to the *use made of those resources*. A general view of this sort is gained by compiling estimates after the manner of "national accounting", as is now done in an increasing number of countries. There are, however, some dangers involved in such a form of presentation. The circumstance that, in the tables giving the comprehensive data, both sides of the accounts necessarily add up to the same total (although often with the help of some balancing item) may convey a false assurance that everything is in order. Another danger is that attention is too exclusively directed to the broad problems; consequently it may be forgotten that production capable of meeting competition at home and abroad depends largely on the efficiency of the individual firm and that the balancing of the economy as a whole presupposes that not only the separate sectors of the economy but also the great majority of individual enterprises will be in equilibrium as regards costs and prices and thus be working on a remunerative basis. There is, of course, also the danger that the estimates (often based on incomplete material) are not sufficiently reliable. But, after all these reservations have been made, it is still a fact that a review taking the form of national accounts brings out some useful relations. Among them must specially be mentioned

United States: Gross national product and its uses.

Gross national product	1947	1948	Uses	1947	1948
	in milliards of dollars			in milliards of dollars	
National income at factor cost:			**Expenditure:**		
Wages and salaries	128	140	Personal consumption	165	178
Proprietors' and rental income	46	51	Government purchase of goods and services	28	36
Corporate profits	25	29	Gross private domestic investment	30	40
Interest	4	5	Net foreign investment	9	1½
Total national income at factor cost	203	225			
Add: Indirect taxes less subsidies	16	16			
National income at market prices	219	241			
Add: Capital-depreciation allowances	13	14			
Gross national product	232	255	Gross national expenditure	232	255

the link between the volume of internal expenditure and resources, on the one hand, and the deficit or surplus on the current account of the balance of payments, on the other (although the existing compilations do not always bring out the relationship as clearly as might be desired).

In the United States estimates of the national product and of its uses are compiled concurrently and published with great promptitude: those for 1948 appeared in the number for February 1949 of the Survey of Current Business issued by the U. S. Department of Commerce.

The national income (and the same applies to the gross national product) rose by about 10 per cent. from 1947 to 1948 but most of this increase was due to higher prices rather than to a larger physical volume of production (cf. page 57). As the table shows, there were some important changes in the use made of the national product.

United States: Percentage distribution of the gross national product according to use.

Items	1929	1948
	percentages	
Personal consumption .	75.9	69.7
Gross private domestic investment	15.2	15.6
Net foreign investment .	0.7	0.6
Government purchases of goods and services	8.2	14.1
Total . . .	100.0	100.0

The share of personal consumption has fallen from about 76 per cent. in 1929 to less than 70 per cent. in 1948. The primary explanation of this fall is a reduction in consumers' disposable income, which in its turn (as pointed out by the Survey of Current Business) was not due to any extraordinarily large gross retained business earnings (since total business savings had gone down from 11 per cent. of the national product in 1929 to 9 per cent. in 1948) but to the increased tax revenue collected by the government.

The volume of gross private investment rose from 1947 to 1948 but the most pronounced change during the same period is the fall in the item "net foreign investment". To appreciate the exact nature of this decline it should be borne in mind that the "net foreign investment" includes loans granted by the U. S. Government but excludes all "unilateral transfers" of U. S. government funds (cf. the table on page 8). The change-over from loans to the granting of Marshall aid thus largely explains the shift in expenditure from "net foreign investment" in 1947 to "government purchases of goods and services" in 1948.

In this connection it should be noted that in the balance-of-payments statistics of the United States the "unilateral transfers" of U. S. government funds are shown as a separate item and not as part of the U. S. government expenditure abroad (in the latter case it would be included under service items). Account has to be taken of this fact in relating the analysis of the gross national product to the current surplus in the balance of payments as usually presented (see chapter III).

In the United Kingdom, estimates of the total available resources, their origin and the use to which they are put are presented to Parliament, as a White Paper, each year at about the time of the budget speech (i.e. in the course of April).

United Kingdom:
Gross national product and its uses at market prices.

Resources	1947	1948	Cost of	1947	1948
	in millions of £ sterling			in millions of £ sterling	
National income	8,725	9,675	Personal consumption . . .	7,465	8,004
Provision for depreciation and maintenance of buildings	750	825	Government consumption . .	2,069	1,914
Gross national product . . .	9,475	10,500	Gross capital formation at home	2,040	2,352
Indirect taxes less subsidises	1,469	1,650			
Borrowing from abroad, sale of assets to foreigners, foreign gifts	630	120			
Total available resources . .	11,574	12,270	Gross national expenditure .	11,574	12,270

While the national income is estimated to have increased by £950 million from 1947 to 1948, personal consumption rose only by about £320 million and government consumption is found to have declined by £165 million (owing largely to less expenditure in Germany and elsewhere abroad). As the Economic Survey for 1948 points out, it was the restraint upon consumption (which, if account is taken of the price rise, remained almost unchanged in aggregate quantity) that permitted practically the entire expansion in national output to go to increase exports and investment. The following table gives details of the capital formation and of the resources by which it has been made possible.

United Kingdom: Investments and savings at market prices.

Capital formation	1947	1948	*Covered by*	1947	1948
	in millions of £ sterling			in millions of £ sterling	
			Savings:		
Gross fixed investments (construction and plants) .	1,800	1,990	Personal, including addition to tax reserve	225	96
Other investments (stocks, etc.)	240	362	Corporate undistributed profits including addition to tax reserve	470	705
Gross capital formation . . .	2,040	2,352	**Public:**		
Provision for depreciation and maintenance	— 750	— 825	(a) current surplus of public authorities . .	— 341	427
			(b) transfers to private capital account* . . .	306	179
			Total net savings	660	1,407
			Resources obtained from abroad	630	120
Net capital formation	1,290	1,527	Resources available for net investment	1,290	1,527

* Refund of taxes, war-damage indemnification, etc.

The most important changes in the flow of savings have been, on the one hand, a further decline in personal savings and, on the other, a more than compensatory increase in corporate savings and an even greater offset in the fact that a deficit of £341 million in 1947 in the budgets of public authorities was turned into a surplus of £427 million in 1948.

The difference between the amount of capital formation and the yield of domestic savings had in each year to be covered by "resources obtained from abroad", corresponding to the deficit on the current account of the balance of payments. It is noteworthy that when equilibrium was restored internally between savings and investments in the latter half of 1948 equilibrium was also reached in the over-all balance of payments, and aid from abroad could thus be used for a reduction of debts (as explained in chapter VII).

In the accounts for the United Kingdom the difference between the total national expenditure (for consumption and investment), on the one hand, and the total available resources of domestic origin, on the other (or what comes to the same: the difference between investments and savings), corresponds, as it should, to the deficit (or surplus, as the case may be) in the current account of the balance of payments; and similar correspondence is found in the national accounts for the Netherlands, Denmark, Norway and Sweden, and others, too. When, as in France, commodity prices have been fluctuating wildly and the balance-of-payments statistics are even established in dollars to render them more comparable with the aid received, while the statistics of national resources and expenditure are naturally compiled in the national currency, there is almost bound to be some divergence between the estimates. But in France, also, the difference between the national resources and expenditure appears as a deficit in the balance of payments.

France: National resources and their uses.

National resources	1938	1948	Expenditure	1938	1948 *
	in milliards of 1938 francs			in milliards of 1938 francs	
National income	353	360	Private consumption	331	314
Add maintenance and renewal	50	50	Government consumption . .	22	21
Gross national product . . .	403	410	Gross public and private investments	58	85
Add deficit in the current account of the balance of payments	8	10			
Total . . .	411	420	Total . . .	411	420

* Yearly figures on the basis of estimates for the second half of 1948.

It will be seen that in the second half of 1948 the national income was slightly higher than before the war but that more resources were devoted to investment, so that consumption was not up to the pre-war rate. Investments are also helped by resources derived from abroad — obtained, before 1948, in a variety of ways, including the use of the French monetary reserves (see table on page 80), but now accruing mostly through the Marshall aid. In 1947 the situation was more critical since, on the basis of the decisions which had been taken up to November of that year with regard to the budget, investments, etc., it was estimated by a special "Commission du Bilan" that, considering the amount of genuine savings to be expected, there would be an "inflationary gap" of Fr.fcs 365 milliard in 1948 (i.e. an excess of demand, at existing prices, over and above the available supplies). The Commission in question further pointed out that, if no new measures were adopted (e.g. the imposition of higher taxes), the gap would exert an influence conducive to a rise in prices.

In other countries also similar calculations have been made in order to find an expression in figures for the tension between projected expenditure and the resources which are likely to be forthcoming. The "gap" is not, of course, synonymous with the "budget deficit", being affected by utilisation of credit for private as well as for public purposes — even though a deficit on government account is usually the main contributor to the gap.

During the war, the "inflationary gap" had been essentially a result of uncovered expenditure in connection with the national effort, which was centred in the government. But at that time a rationing system which embraced almost all types of goods and services made it well-nigh impossible for the public to spend the whole of the money income coming into its hands; and, since private investments were strictly limited (often even ruled out altogether) by the system of allocation of materials, etc., a considerable part of the new money distributed through budget deficits came back via the banking system to the Treasuries as a kind of more or less forced savings. In the midst of a terrible struggle, the aim was to reduce private consumption almost to the subsistence minimum in order that the largest possible proportion of the available resources should be set free for the all-eclipsing task of winning the war.

In peacetime, on the contrary, the aim of economic policy is to raise the standard of living of the people and to stimulate private investments in order to improve productivity. An inflationary increase in monetary purchasing power (i.e. in effective demand) will then find its expression in increased spending, with consequent increases in prices, which is what has happened in so many countries in recent years.

The mere desire to acquire goods or to build houses has, of course, in itself no direct economic influence; for an effect to be produced, those who entertain the desire must possess the monetary purchasing power which will turn volition into "effective demand". Generally, people obtain monetary purchasing power by contributing to production (as wage-earners, owners of capital goods, etc.) and, if the amount of money earned (including payments via the budget) is not more than the counterpart of the contributions thus made, the likelihood is that balance between demand and supplies will be preserved.* For an inflationary gap to arise in the domestic economy, it is necessary that additional monetary purchasing power should come into existence and be injected into the domestic economy, and the three main ways in which this may happen are as follows:

(i) a budget deficit may be financed through recourse by the government to the banking system and, in particular, through the creation of new money by the bank of issue;

(ii) investments in excess of real savings may be financed in a similar way by creation of new money via the banking system; and,

(iii) in connection with investments but also for other purposes a part of the public debt may be monetised through the transformation of government bonds into monetary purchasing power available for current expenditure.

If no new money were provided by the banking system, the desire to buy goods would be ineffective in practice and no inflationary gap would arise.

As regards the emergence of a deficit in the balance of payments, it is likewise necessary that, failing current supplies from the exchange market, some institution should be ready to provide importers with the foreign exchange required to pay for their purchases; otherwise excess imports would soon have to cease. Since the second world war, the central-bank reserves of the respective countries have been drawn upon to provide importers (including the government) with foreign exchange at fixed rates, and funds for the same purpose have also been obtained through payments agreements and foreign loans and grants.

Thus the emergence of an inflationary gap at home and of a deficit in the current account of the balance of payments presupposes that:

(i) fresh monetary purchasing power is being created by the central bank (or else via the banking system) in addition to income really earned; and that

(ii) foreign exchange, in excess of the market's own deliveries, is being supplied to importers at fixed rates of exchange by the central bank or some other institution.

It is generally agreed that at home every effort should be made to put a stop to the artificial creation of monetary purchasing power, by the balancing of the budget and the adoption of a suitable credit policy. This does not mean, of course, that no foreign assistance is needed by the European countries still feeling the after-effects of the war. But it makes a great difference both internally and as regards the foreign exchange policy whether the assistance is *obtained in time, so that it* can be appropriated to specific purposes and be drawn upon when the need arises, or whether money is

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* During a severe depression, the creation of new money may be justified as a means of keeping up demand in relation to the available or potential supply of resources; but that is very far from having been the case in the sellers' markets of the last few years, with a shortage of goods in most lines and no lack of employment.

simply being spent on the basis of an excessive extension of credit without any provision having been made for the resulting deficit in the balance of payments, which will then most likely make itself felt as a dollar shortage.

The two aims — the internal: to establish balance between the effective demand and the available supplies in the domestic economy; and the external: to achieve a balance in relation to other economies through a suitable exchange policy, etc. — are closely interrelated and must be pursued together.

After the first world war, it was the merit of the Financial Committee of the League of Nations that, when it undertook the task of reconstruction in Austria, Hungary, Greece, etc., it paid attention both to the internal and to the external aspects of the situation to be put in order. Here it may be of interest to recall that the reconstruction in question was in each case carried out with the aid of comparatively moderate foreign loans and that the proceeds of the loans were generally employed (with the possibility of switching according to the circumstance) for three purposes:

(i) one part of the proceeds was used to meet budget deficits; these had to be compressed by a rationalisation of the administration (including a reduction in the number of officials) and, in addition, an increase in revenue, the latter being facilitated by stabilisation of the currency (usually a relatively small fraction of the loan proceeds sufficed for the purpose of meeting the current deficit);

(ii) a substantial part was employed for productive investments (electrification of railways, the draining of swamps, etc.); and

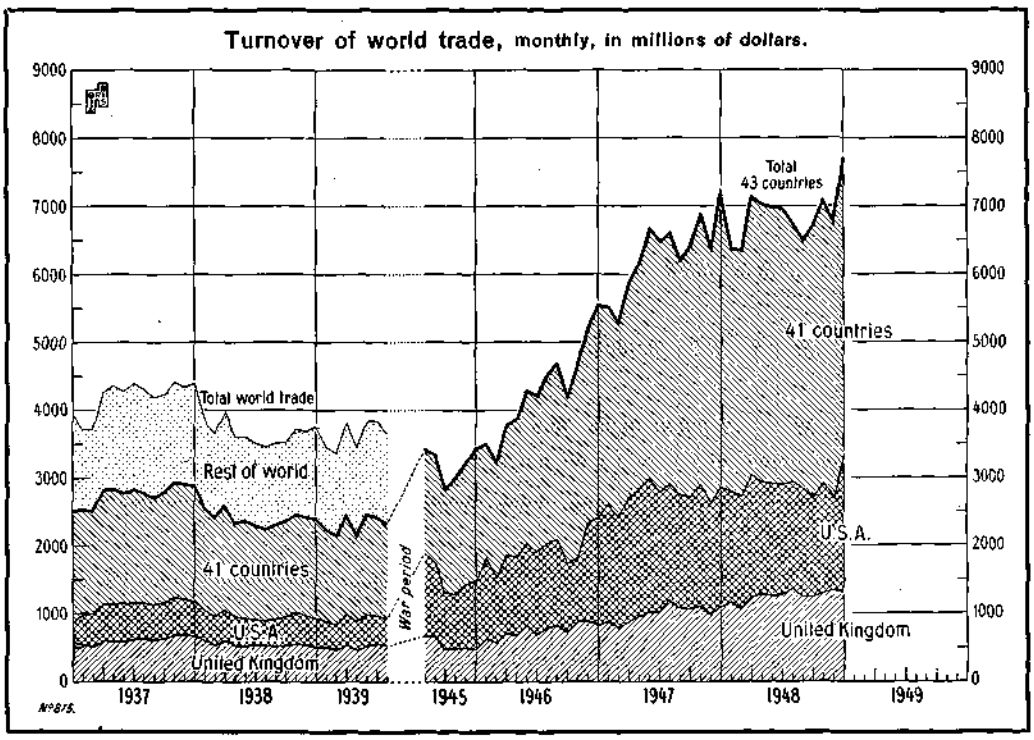
(iii) a third part was used in connection with an immediate reorganisation of the central bank, particular attention being paid to the need of strengthening its reserves in gold and foreign exchange and, inter alia, to ensuring convertibility of its currency.

It is obvious that similar needs must be attended to at the present time. It was only natural that for the first period of Marshall aid, when foreign trade was threatened with a breakdown, the foremost objective should be to meet deficits in the balances of payments in relation to the western hemisphere. But it seems equally natural, now that the post-war inflation appears to have come to an end and pre-war levels of production have been generally surpassed, that the aid should be adjusted more directly to the urgent tasks which remain to be carried out before a country can gain its economic independence of foreign assistance. The difficulties and problems are not the same for all countries but one obvious requisite is to render each country's currency more invulnerable to pressure from abroad. Side by side with repayment of debt and the promotion of productive investment there is in many countries the need of replenishing monetary reserves — which is also a form of investment.

III. Towards a more balanced position in Foreign Trade.

In these post-war years, governments as well as the public in almost every country have been much concerned about the state of the balance of payments — and no wonder: it was in most cases palpably clear that the standard of consumption and the general welfare of the people could only be kept up by the receipt of food and other commodities from abroad and that, without surplus imports of raw materials and machinery, industrial recovery would have to be slowed down; but while, in the domestic sphere, governments could prescribe price control and obtain fresh purchasing power from the banks even if that meant inflation, and could, at a pinch, requisition whatever goods were available, at the frontier their sovereign powers ceased: they were dependent on whether their own countries had sufficient goods to export and whether those goods could be sold at competitive prices, whether their own reserves of gold and foreign exchange were in danger of exhaustion or whether they could obtain loans and credits or other assistance from abroad. It is true that they could impose a stringent control on foreign trade and curtail imports of non-essential goods; but experience soon taught them that when imports were cut down exports also declined. As long as expenditure for consumption and investment was kept up beyond the limit set by the national output, there remained a problem of restoring equilibrium on foreign account and especially in relation to the United States.

In examining the various aspects of the problem of the balances of payments some useful purpose may no doubt be served by adding together the



figures of visible and invisible trade for certain groups of countries, e. g. all the countries in Europe or, more particularly, those belonging to O.E.E.C., and by studying the more comprehensive figures thus obtained in relation to the trade of other groups of countries, e. g. the dollar area. Certain general trends may then be discovered and an idea gained of the order of magnitude of imports and exports inside Europe and in relation to other continents or of the net amounts paid in dollars over different periods. But the general statistics thus compiled must not be allowed to obscure the paramount importance of the problems of each separate country. For it is still largely the particular conditions with regard to budgets, investments, etc. inside each country which determine the state of its balance of payments. In these respects, conditions in Europe are still very varied. One country — Switzerland — has continued to receive an influx of dollars, despite its attempt to stave off receipts of funds in that currency by means of a fluctuating rate for financial dollars; a few countries, e. g. Belgium and Italy, have begun to add to their gold and dollar holdings, thanks, inter alia, to a domestic policy of credit restrictions and to Marshall aid (operating both as direct assistance and as a helpful factor in the general improvement in Europe); a few other countries — Denmark and the United Kingdom — have been in a position to reduce their foreign liabilities, while some of the rest — the Netherlands, Norway and Sweden — had to draw on their monetary reserves in 1948 and were still doing so in the early months of 1949. In view of these important differences, it is obviously necessary that the main facts about individual countries should be presented and examined in addition to any general tables.

In recent years there has been a juxtaposition of unstable price conditions on the one hand and officially fixed exchange rates on the other, fluctuating prices in fact coexisting with inconvertible currencies of fixed official value. In these circumstances special difficulties in valuation have unavoidably arisen with regard to imports and exports and, as a consequence, the actual flow of trade has often been less reliably reflected by the ordinary trade statistics of individual countries than is the case in normal times. Not infrequently a marked discrepancy has been found between the import and export figures in the returns compiled by the customs administrations (that is, the ordinary trade statistics) and the foreign trade figures based on receipts and allocations of foreign currencies by the Exchange Controls. As a rule, the exchange-control figures (duly adjusted) are regarded as the more correct ones and are, therefore, preferred for the compilation of the estimates of balances of payments; but these figures are generally rather late in appearing and, since they are not classified in the same detail according to commodities and with regard to the distribution of trade between different countries, it is as a rule necessary, for these purposes, to fall back on the ordinary trade statistics.*

* Another complication arises from the fact that the customs statistics refer to f.o.b. prices for exports and to c.i.f. prices for imports, while the compilers of the estimates of balances of payments are increasingly adopting the use of f.o.b. prices not only for exports but also for imports

World trade turnover.

Trade of:	Pre-war			Post-war		
	1929	1937	1938	1946	1947	1948
	in milliards of current U.S. dollars					
United Kingdom	15.2	7.3	6.5	9.1	12.0	15.1
United States	16.1	6.3	5.0	14.3	21.1	19.7
41 countries	42.1	19.7	17.2	28.3	42.5	47.6
Total for 43 countries . . .	73.4	33.3	28.7	51.7	75.6	82.4
Estimate for rest of world	42.8	20.5	18.3	21.1	27.8	32.7
Total(1).	116.2	53.8	47.0	72.8	103.4	115.1

(1) Pre-war according to League of Nations tables of world trade.
Post-war according to an estimate of the International Monetary Fund.

It would seem that the ordinary trade statistics are used for the computation of such comprehensive statistics as exist with regard to world trade; since this involves, in addition, the conversion of national data into some common currency (e.g. the U. S. dollar), another possibility of error is introduced. But even if the available estimates of movements of world trade or of the aggregate trade of certain groups of countries can only be regarded as rough approximations, they are probably sufficiently reliable to indicate the general tendencies of world trade.

In the publication of the United Nations called "Major Economic Changes in 1948" it is pointed out that the quantum indexes, i.e. the indexes which measure the volume, as distinct from the value, of trade, "are likely to be more reliable but they are not perfect since they fail to reflect changes in the average quality, or degree of processing, of goods belonging to each statistical item".

*   *
*

The main facts brought out by the figures for world trade up to the end of 1948 may be summarised as follows:

(i) Measured in U. S. dollars, the turnover of world trade (exports plus imports) has continued to increase without interruption since 1945.

(ii) The increase from 1947 to 1948 in the dollar turnover of world trade comes to about 10 per cent., which is rather more than the rise in prices. There was thus a slight increase in the volume of world trade in 1948. The Department of Economic Affairs of the United Nations gives figures as regards exports only (since export figures are considered a more reliable measure of the changes in world trade than import figures).

(and consequently, in making the estimates, have to reckon with other figures for the income and expenditure from shipping and insurance). One result of this practice is that the currently available statistics of monthly imports and exports as published by the customs administration are not directly comparable with the trade figures in the estimates of balances of payments, this making it more difficult to form an idea of the real significance of the currently published figures. It would be well if those who compiled the yearly estimates would establish and make known some relatively simple formula for fitting the current (monthly) figures into the over-all picture of the balances of payments where this is possible.

(iii) The fact that for the world as a whole the volume of trade did not increase appreciably in 1948 has been due almost exclusively to the continuous decline in exports from the United States since the middle of 1947.

There has thus been a 40 per cent. contraction in the export surplus, due partly to a smaller volume of exports and partly to a larger volume of imports. The increase in the imports of the United States corresponds, of course, to an increase in the exports of other countries to the United States.

(iv) The quantum of exports of all countries other than the United States increased in 1948 by about 10 per cent. but was nevertheless only three-quarters of what it had been in 1937, the failure to attain the pre-war figure being due mainly to the low level of exports from Germany and Japan. If these two countries are excluded, the quantum of exports is found to have been within 10 per cent. of the 1937 figure and almost as large as in 1938.

Quantum of world exports.

Period	Unit dollar value (price movement)	Dollar value of exports	Quantum
	Base : 1937 = 100		
1937	100	100	100
1938	95	86	91
1946	167	127	76
*1947	200	182	91
1948 (first half) .	215	194	90 *

* To judge from preliminary material, there seems to have been an increase in the volume of trade for the full year 1948, and it may be that even for the first half of 1948 the estimate in the table will be found to have been too low when more complete data are available.

It will be seen from the following table that in 1948 most countries were able to cover a greater part of their imports by current exports than had been the case in 1947.

This improvement has been due to the following main causes (which are clearly interconnected):

(i) the general increase in production (in industry as well as agriculture), partly in consequence of progress in reconstruction and partly thanks to favourable weather for the harvest;

(ii) the brake put on inflationary financing by better balancing of budgets and by increasingly effective credit restrictions, which are somewhat easier to apply now that much imperative investment has been completed;

(iii) the special arrangements which, thanks to the Marshall aid (including the European payments scheme), it has been possible to make for the financing of foreign trade. It should be remembered that, without this aid, exports from a number of other extra-European countries besides the United States would have been severely handicapped.

While it was at first natural to look at Marshall aid primarily as a means of financing trade with the western hemisphere and — through the payments scheme — also inside Europe, the related internal effects have not to be forgotten: obviously, western European production as a whole could not possibly have increased as much as it did without the receipt of foreign assistance nor could inflationary financing have been so effectively arrested. But it must also be observed that, in so far as the resources provided by

Exports as percentage of imports
(special trade).

Country	1938	1946	1947	1948	1949 1st quarter
	percentages				
Western European Countries					
Belgium (1)	94	52	72	85	105
Denmark	95	57	75	80	76
France (1)	66	43	61	66	83
Italy	93	54	47	71	72
Netherlands (1)	74	33	44	55	63
Norway	66	55	48	56	57
Sweden	89	75	62	80	80
Switzerland	82	78	68	69	77
United Kingdom (1)	61	70	63	76	85
North America					
U.S.A. (2)	157	198	268	178	183
Canada	124	120	108	117	103 (4)
South America					
Argentina	99	170	100	.	.
Brazil	100	140	93	103	.
Chile (3)	136	110	105	120 (5)	.
Peru	132	123	92	97	.

(1) Including trade with overseas territories.
(2) General imports and exports including re-exports.
(3) Proceeds of copper and nitrates not available for payment for imports. If these items were excluded, the proportion of imports covered by exports would be as follows: 1938 – 40 per cent.; 1946 – 39 per cent.; 1947 – 27 per cent.
(4) January and February. (5) 11 months.

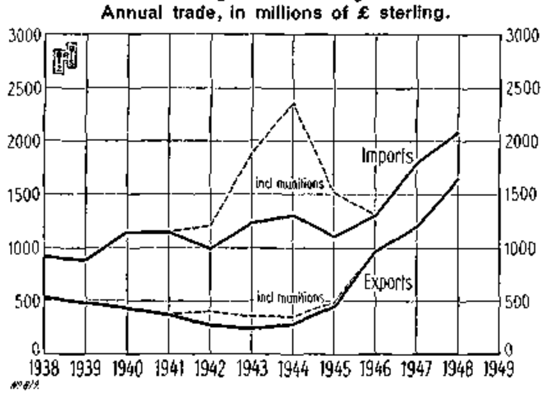
Marshall aid have been used in the separate countries as cover for internal expenditure — mostly of an investment character — and thus led to a maintenance of exports to Europe, Europe was at the same time freed from the obligation of paying through its own exports for the surplus of goods and services which it received.

Whether import restrictions have contributed appreciably to a reduction in the trade deficits is very doubtful, since a cut in imports affects the flow of exports, including those of the country which applies the restrictions (see final section of this chapter).

* * *

For Europe as a whole the deficit on the current account of the balance of payments fell from the equivalent of about $7,600 million in 1947 to about $5,600 million (according to estimates made by the International Monetary Fund); three-fourths of this is due to a reduction in the adverse balance of the United Kingdom.

United Kingdom: Foreign trade.
Annual trade, in millions of £ sterling.



For the United Kingdom, total imports rose from £1,795 million in 1947 to £2,080 million in 1948 but exports (including re-exports) rose more sharply, from £1,198 million to £1,648 million, which meant that the trade deficit was reduced from £597 million in 1947 to £432 million in 1948. This improvement in the foreign trade position must (as in the case of some other countries) be seen primarily in connection with the internal policy of "disinflation";

United Kingdom: Foreign trade.

Period	Total imports	Exports U.K. goods	Re-exports	Total exports	Balance
	in millions of £ sterling				
1938 yearly total . . .	920	471	62	533	— 387
1946 „ „ . . .	1,301	915	50	965	— 336
1947 „ „ . . .	1,795	1,138	60	1,198	— 597
1948 „ „ . . .	2,080	1,583	65	1,648	— 432
1946 monthly average .	108	76	4	80	— 28
1947 „ „ .	150	95	5	100	— 50
1948 „ „ .	173	132	5	137	— 36
1949 January	187	159	5	164	— 23
February	162	141	4	145	— 17
March	190	160	6	166	— 24
April	188	137	6	143	— 45

but in this particular case the improvement was greatly helped by the application of "export quotas", which made it obligatory for manufacturers to sell abroad a certain (often quite high) proportion of their output. In that way a large part oj the country's production was deliberately diverted to export markets, even when the home market was characterised by a grave shortage of many of the goods thus exported. As a result, exports rose more than current production: in 1948 the volume of exports was 36 per cent. larger than in 1938, while, for instance, the production index of manufacturing registered a rise of 24 per cent. over the 1938 level. The accompanying table shows impressive increases in the export values of particular commodities (it being necessary to remember that export prices for the United Kingdom rose, on an average, by 147 per cent. from 1938 to 1948).

United Kingdom:
Exports of manufactured articles.

Groups	1938	1947	1948
	in millions of £ sterling		
Cotton yarns and manufactures . . .	50	78	131
Woollen and worsted yarns and manufactures	27	58	95
Electrical goods and apparatus . . .	14	49	73
Vehicles *	44	168	244
Machinery	58	181	254
Silk and artificial silk	6	30	39
Pottery and glass	10	33	45
Non-ferrous metals and manufactures	12	40	55
Iron and steel manufactures	42	84	106
Chemicals, drugs and dyes	22	67	84
Others	80	212	252
Total . . .	365	1,000	1,378

* Including locomotives, ships and aircraft.

In the first quarter of 1949 the volume of exports was as much as 56 per cent. above the 1938 level.

Apart from Switzerland, whose productive capacity was unhurt by the war, the United Kingdom is the only European country which has raised its export volume above the 1938 level. Great as this achievement is, it has to be remembered that in 1938 the United Kingdom had a deficit of £70 million on the current account of its balance of payments and that its

United Kingdom: Balance of payments.

Items	1938	1946	1947	1948
	in millions of £ sterling			
Visible trade				
Imports (f.o.b.)	835	1,097	1,541	1,768
Exports and re-exports (f.o.b.)	533	889	1,100	1,550
Balance of visible trade	— 302	— 208	— 441	— 218
Government expenditure overseas (net)	— 16	— 295	— 207	— 109
Other invisible items (net)				
Interest, profits and dividends	+ 175	+ 73	+ 47	+ 50
Shipping	+ 20	+ 17	+ 24	+ 60
Travel	— 12	— 33	— 59	— 35
Films	— 7	— 17	— 14	— 10
Other items	+ 72	+ 83	+ 20	+ 142
Net total of other **invisible income**	+ 248	+ 123	+ 18	+ 207
Total balance on current account	— 70	— 380	— 630	— 120

exports in that pre-war year only covered 51 per cent. of its imports, while the ratio of 85 per cent. attained in the spring of 1949 corresponds more closely to the "normal" average for the countries in western Europe.

In addition to the halving of the trade deficit, expenditure abroad by the British Government was reduced in 1948 by about £100 million, while the net balance of other invisible items improved by nearly £190 million, so that the total deficit on the current account of the balance of payments came down from £630 million in 1947 to £120 million in 1948.

With the reconstitution of the mercantile marine, the net income from shipping has risen, and for 1948 it exceeded, in real terms, the corresponding income for 1938, while the net income from foreign investments represented, *in real terms*, only between one-sixth and one-seventh of what it had been in 1938 (with the possibility, however, that the ploughing-back of retained profits may have increased the aggregate value of British-owned direct investments abroad).

The division of the total balance of payments into separate balances with four main areas of the world reveals a varied and complex pattern of commercial and financial relationships.

United Kingdom:
Regional distribution of the current account of the balance of payments.

Region	1947	1948
	in millions of £ sterling	
Sterling area	+ 55	+ 225
O.E.E.C. countries	— 25	+ 80
Western hemisphere	— 655	— 340
Other countries (mainly Middle East and eastern Europe)	— 5	— 85
Total	— 630	— 120

The deficit in relation to the western hemisphere (indicative of the "hard currency" problem) has been reduced but is still substantial, while the deficit in relation to the Middle East and the east of Europe has grown from 1947 to 1948. But, at the same time, the surplus with the sterling area has increased and a deficit with the O.E.E.C. countries in 1947 was turned into a surplus in 1948. The Economic Survey for 1949 states the opinion that "as long as the non-dollar world remains critically short of dollars, it is not possible for us in general to earn from the countries with which we have surpluses the dollars which we need to finance our dollar deficit". It is further explained why the surpluses in relation to the sterling area and the O.E.E.C. countries are considered inevitable for the time being. The surpluses consist of:

(i) a part which reflects the establishment of drawing rights in favour of some O.E.E.C. countries under the intra-European payments scheme, since this has enabled the countries in question to buy from the United Kingdom and the rest of the sterling area more than they could send in return;

(ii) another part which represents investments made in various parts of the Commonwealth (cf. page 12); and

(iii) a further part which serves directly to strengthen the British financial position by reducing sterling liabilities.

This analysis shows the, in any case self-evident, connection between the distribution and pull of financial resources and the flow of trade in goods and services in response to effective demand.

The way in which the current deficit was covered and other items on capital account of the balance of payments were met has been shown on page 13. It might be added that for the first four months of 1949 the trade deficit (with imports counted c. i. f.) was about £109 million, at which figure it was probably covered by net income from invisible items, so that Marshall aid could be devoted to capital purposes of a nature to strengthen the long-term British position on foreign account.

In France rapidly rising prices in the years after the war caused great difficulties in the valuation of both imports and exports. For any comparison of the figures from year to year, account must always be taken of the price factor, and some guidance can also be obtained from the statistics of foreign trade in metric tons.

It is estimated that in 1948 the foreign-trade turnover of France had practically regained the pre-war level. But in this connection it must not be forgotten that in 1938 the volume of French exports was insufficient to ensure equilibrium in the balance of payments, being some 40 per cent. below the level reached in 1929.

As regards imports, the level reached in 1947 and 1948 represents almost the same volume as in 1929, i.e. what France imported in a prosperous year. In view of the loss of invisible income, the maintenance of such a volume of imports will require a considerable expansion of exports (to more than twice the average 1948 level) if there is to be equilibrium in the balance of payments. After the war, there was a particularly marked expansion in exports to the French overseas territories, the proportion rising from over one-eighth of the country's total exports in 1913

France: Foreign trade.*

Period	Index of wholesale prices	Value			Weight	
		Imports	Exports	Balance	Imports	Exports
		in milliards of current French francs			in millions of metric tons	
1938 yearly total	1	46	31	— 15	47	27
1946 „ „	6½	234	101	— 133	30	10
1947 „ „	10	347	213	— 134	37	14
1948 „ „	17	654	431	— 223	42	19
1946 monthly average	6½	19	8	— 11	2.5	0.8
1947 „ „	10	29	18	— 11	3.1	1.1
1948 „ „	17	55	36	— 19	3.5	1.5
1949 January	19½	73	57	— 16	4.0	1.9
February	19	74	65	— 9	4.5	2.3
March	18¾	77	63	— 14	4.3	2.2
April	18½	85	69	— 16	4.3	2.5

* Including trade with overseas territories.

to not far short of one-half in 1948 and the corresponding imports from one-tenth to over one-quarter. Between metropolitan France and these territories the balance of trade has, moreover, remained in substantial equilibrium. In commercial relations with foreign countries (other than France) the French overseas territories had substantial trade deficits only partly covered by invisible income, with the result that the current deficit of these territories came to the equivalent of $162 million in 1947 and $190 million in 1948 — the liability resting on France itself.*

In the inter-war period the United States and Canada habitually furnished France with 14 per cent. of its imports — a proportion which rose to 29 per cent. in 1947 but fell back to 18 per cent. in 1948. In its direct relations with these two countries (i.e. the bulk of the dollar area) France had a trade deficit of about $100 million in 1938 and about $800 million in 1947, reduced to $400 million in 1948. This reduction in the trade deficit with the dollar area was, however, followed by an increase of an approximately equal amount ($400 million) in the deficit in other directions — chiefly towards the sterling area. As a result the credit margins available to France under payments agreements began to be exceeded, and this often entailed payments in gold and dollars. A kind of indirect dollar crisis ensued, and it was to avoid the necessity of a drastic curtailment of imports by France (and by some other European countries in a similar position) that the intra-European payments scheme was instituted, through which France was allocated net drawing rights amounting to $323 million.

Estimates of the French balance of payments have been made in current dollars, a mode of presentation which permits a readier comparison with the figures for foreign aid.

* France's net payments on account of the overseas territories represent, in part, a contribution made to post-war reconstruction by the supplying of industrial and agricultural equipment; in part, exceptional expenditure in Indo-China and elsewhere; and, in part, a seepage of funds, the overseas territories affording opportunities for export of capital.

France:
Current account of the balance of payments.

Items	1945	1946	1947	1948*
	in millions of current U.S. $			
Trade balance				
Imports	904	1,980	2,492	2,404
Exports	43	453	1,040	1,060
Balance of trade	— 861	— 1,527	— 1,452	— 1,344
Invisible items (net)				
Freight	— 26	— 246	— 311	— 220
Interest and dividends	— 26	— 21	— 61	— 84
Transfer of wages	— 15	— 45	— 69	— 100
Other items	— 188	+ 87	+ 380	+ 196
Balance of invisible items	— 255	— 225	— 61	— 208
Deficit of French overseas territories	— 375	— 297	— 162	— 190
Balance on current account	— 1,491	— 2,049	— 1,675	— 1,742

* Estimates.

France: Cover for current deficits in the balance of payments.

Methods of financing	1945	1946	1947	1948*
	in millions of current U.S. $			
Requisitioning and voluntary private repatriation of assets	—	200	184	90
Use of official reserves of gold and foreign exchange	628	938	346	291
Credits utilised under payments agreements and counterpart of foreigners' franc accounts	53	167	22	138
Credits and grants from the United States	211	849	1,101	1,074
Credits and grants from other countries	638	131	136	187
Total	1,530	2,285	1,789	1,780

* Estimates.

In 1948, the proportion of French imports covered by exports being still less than 50 per cent. (with foreign countries) and 66 per cent. if French overseas territories are included, a deficit equivalent to about $1,300 million remained on visible trade; invisible items, together with the deficit of French overseas territories, added another $400 million to the adverse balance.

The rapid exhaustion of France's own resources in gold and foreign exchange was followed by increased reliance on foreign credits and other foreign aid, obtained chiefly from the United States. Fortunately in the first quarter of 1949 exports covered 83 per cent. of imports* — indicating a decisive improvement in the trade situation; moreover, it is expected that the tourist traffic may yield $200 million in 1949 against (net) $90 million in 1948.

In Italy the improvement in the foreign-trade position was very rapid once effective credit restrictions, together with other measures, had been imposed (in September 1947) as safeguards against a continuance of inflation and at the same time the official exchange rates had been brought relatively close to the free-market rates — this adjustment being accompanied by a certain

* Including trade with French overseas territories.

Italy: Foreign trade.

Period	Index of wholesale prices	Value			Weight	
		Imports	Exports	Balance	Imports	Exports
		in milliards of lire			in millions of metric tons	
1938 yearly total	1	11	10	— 1	20.6	4.5
1946 ,, ,,	29	92	65	— 27	10.0	1.1
1947 ,, ,,	52	930	339	— 591	18.5	1.9
1948 ,, ,,	54	821	571	— 250	17.8	3.8
1946 monthly average	29	8	5	— 2	0.8	0.1
1947 ,, ,,	52	77	28	— 49	1.5	0.2
1948 ,, ,,	54	68	47	— 21	1.5	0.3
1948 October	57	62	54	— 8	1.5	0.3
November	57	66	65	— 1	1.4	0.4
December	57	65	68	+ 3	1.3	0.4
1949 January	57	62	52	— 10	1.2	0.4

fall in prices. Roughly speaking, the weight (in tons) of exports in 1948 was twice as great as in 1947 while, in stable-money values, the increase was about 60 per cent.

Value figures of Italy's foreign trade in U. S. dollars show that imports increased by perhaps 5 per cent. from 1947 to 1948 and that, in 1948, they were paid for to the extent of fully 70 per cent. by exports (as compared with less than 50 per cent. in the previous year). In November and December 1948, for the first time since the war, the monthly trade statistics (expressed in dollars) showed export surpluses, the dollar equivalents of which were \$0.1 million and \$6.7 million respectively.

In terms of U. S. dollars, the current account of the Italian balance of payments shows the following figures for 1948.

Italy: Balance of payments 1948.

Items	In millions of U.S. dollars
Balance of visible trade	— 320
Invisible items:	
Freights and insurance	— 107
Tourist traffic	+ 24
Emigrants' remittances	+ 85
Miscellaneous	+ 46
Balance of invisible items	+ 48
Total balance on current account	— 272
This deficit was more than covered by:	
Post-UNRRA aid, Interim aid, E.R.P.	+ 340
Gift parcels, International Children's Fund, etc.	+ 40
Total cover	+ 380
Surplus	+ 108

During 1948 the Italian monetary reserves rose by the equivalent of \$175 million and the credit balances on payments agreements accounts by some \$100 million, making together \$275 million. This increase is explained (in the table) by the surplus of \$108 million, together with some \$90 million of foreign assets repatriated through the franco-valuta import system and some \$100 million representing the net utilisation of foreign credits (from the Argentine, etc.). Thus, Italy is a country which has reserved a considerable part of the proceeds of foreign loans and credits for the particular type of investment consisting in the reconstitution of its almost depleted monetary reserves with a view to strengthening confidence in the national currency and regaining more freedom in shaping its commercial policy.

Switzerland had, in each of the years 1947 and 1948 an import surplus of about Sw.fcs 1,550 million, which would seem to have been covered to the extent of Sw.fcs 1,100 to 1,300 million by net income from tourist traffic and other invisible items. The large amount of imports in the two years in question (in volume exceeding pre-war imports) reflects a process of restocking, undertaken on a considerable scale as soon as supplies became available. It would seem that towards the end of 1948 sufficient stocks had been accumulated, and in the first quarter of 1949 imports fell, while exports were relatively well maintained.

With the fall in the trade deficit there must have been a surplus in the current account of the balance of payments during the first three months of 1949, reflected, it might be added, by an increase of Sw.fcs 90 million in the gold holdings of the Swiss National Bank during the same period.

Swiss exports consist almost exclusively of manufactured articles, largely of a non-essential character, the sale of which is often hampered by trade and exchange controls in other countries. It has been the objective of Swiss negotiations to secure the granting of licences for non-essential as well as essential exports, so that the consumers in foreign countries should be free to buy Swiss goods of this type if they wished to do so. At the same time Switzerland has wanted to make sure that the Swiss franc balances accumulated by other countries should, apart from a certain margin, be used for the purchase of Swiss goods and for other payments in Switzerland. It has not always been easy to arrive at an agreement on these matters — and with France there was at the end of April 1949 a break in the negotiations, which led to the suspension of the payments agreement and an interruption in the normal settlements between the two countries. Fortunately this was only of a most temporary nature, for normal relations were re-established from 1st June 1949.

Switzerland: Foreign trade.

Period	Imports	Exports	Import Surplus
	in millions of Swiss francs		
1938 yearly total	1,607	1,317	— 290
1946 „ „	3,423	2,676	— 747
1947 „ „	4,820	3,268	— 1,552
1948 „ „	4,999	3,435	— 1,564
1947 monthly average	402	272	— 130
1948 „ „	416	286	— 130
1949 January	363	252	— 111
February	324	268	— 56
March	364	290	— 74
April	306	270	— 36

Belgium: Foreign trade.

Period	Imports	Exports	Balance
	in millions of Belgian francs		
1938 yearly total	23,069	21,670	— 1,399
1946 „ „	52,562	29,654	— 22,908
1947 „ „	85,559	61,655	— 23,904
1948 „ „	87,418	74,020	— 13,398
1947 monthly average .	7,130	5,138	— 1,992
1948 „ „ .	7,285	6,168	— 1,117
1949 January	6,580	6,138	— 442
February	6,503	6,725	+ 222
March	7,160	7,613	+ 453
April	6,669	7,012	+ 343

Belgium:
Foreign trade with the United States.

Items	1947	1948
	in milliards of B.fcs	
Belgian exports to United States .	2.71	4.45
Belgian imports from United States	22.66	15.65
Balance	— 19.95	— 11.20

Belgium has also progressed towards a better foreign-trade position, the import surplus falling from B.fcs 23.9 milliard in 1947 to B.fcs 13.4 milliard in 1948. There was in particular an improvement in the balance with the United States.

In recent months the Belgian trade returns have registered an export surplus — the first of its kind since the second half of 1939.

Official estimates of the balance of payments of the Belgo-Luxemburg Union give for 1947 a deficit of B.fcs 13,334 million on current account. Together with B.fcs 1,860 million of Belgian net long-term investments abroad, the current deficit was covered by net repatriations of private capital to the extent of B.fcs 10,755 million and by a net reduction in the amount held in the form of gold and foreign balances by official and banking institutions.

There is no official estimate of the balance of payments for 1948 but, according to a private estimate,* the current deficit was reduced to B.fcs 1,898 million for that year, which has been more than covered by the proceeds of various capital transactions and Marshall aid as well as continued repatriation of funds, permitting an increase in the gold reserves by B.fcs 1,218 million in 1948.

Netherlands: Foreign trade.

Period	Imports	Exports	Import surplus
	in millions of florins		
1938 yearly total	1,459	1,074	— 385
1946 „ „	2,363	815	— 1,548
1947 „ „	4,278	1,892	— 2,386
1948 „ „	4,965	2,718	— 2,247
1947 monthly average .	356	158	— 198
1948 „ „ .	414	227	— 187
1949 January	465	318	— 147
February	401	245	— 156
March	476	283	— 193

The Netherlands has also seen some improvement in the balance of payments, although the foreign-trade deficit remained substantial in 1948.

Of the Fl. 1,474 million for which cover had to be found in 1948, the dollar charge came to the equivalent of Fl. 1,133 million or $427 million. Under the heading of Marshall aid, $112 million was received in

* By Prof. F. Baudhuin of the University of Louvain.

Netherlands: Balance of payments.

Items	1947	1948
	in millions of florins	
Current Account:		
Trade balance	— 1,823	— 1,426
Interest and dividends, etc.	+ 79	+ 125
Other services (net)	+ 178	+ 350
Balance on current account	— 1,566	— 951
Account must also be taken of the following items on capital account which are in some respects similar to current expenditure:		
Amortisation of government credits	— 640	— 154
Credits granted (mostly to Indonesia)	— 355	— 369
Total charges	— 2,561	— 1,474

actual dollars and the equivalent of $15 million as drawing rights, etc. A further $130 million was obtained through government credits and an almost equal amount through net reduction in foreign investments (essentially repatriation).

While in 1946 exports had only amounted to 33 per cent. of imports, the corresponding figure was 65 per cent. in the last quarter of 1948, as compared with 74 per cent. for the whole year 1938. But the Netherlands will presumably have to cover a larger percentage of its imports with exports than before the war, in view of the decline in invisible income owing to the loss of foreign investments (including the uncertainty of Indonesia) and the reduction — at any rate for the time being — in transit trade in relation to Germany.

Denmark: Foreign trade.

Period	Imports	Exports	Balance
	in millions of D. Kroner		
1938 yearly total	1,626	1,535	— 90
1946 „ „	2,848	1,618	— 1,230
1947 „ „	3,090	2,313	— 777
1948 „ „	3,424	2,731	— 693
1946 monthly average	238	135	— 103
1947 „ „	258	193	— 65
1948 „ „	285	228	— 57
1949 January	325	252	— 73
February	342	240	— 102
March	409	276	— 133

In the group of northern countries, Denmark has been able to reduce the deficit on the current account of the balance of payments, from D.Kr. 413 million in 1947 to D.Kr. 270 million in 1948, thanks to a fall of D.Kr. 63 million in the adverse trade balance and an increase of D.Kr. 80 million in the income from invisibles (mainly shipping). Marshall aid payments made it possible to reduce the (net) foreign liabilities of the National Bank from D.Kr. 667 million at the end of 1947 to D.Kr. 553 million at the end of the following year.

Norway: Foreign trade.

Period	Imports	Exports	Balance
	in millions of N. Kroner		
1938 yearly total	1,193	787	— 406
1946 „ „	2,197	1,202	— 995
1947 „ „	3,620	1,620	— 2,000
1948 „ „	3,708	2,063	— 1,645
1946 monthly average	183	100	— 83
1947 „ „	318	152	— 166
1948 „ „	309	172	— 137
1949 January	283	169	— 114
February	376	173	— 203
March	343	228	— 115

In Norway, the current deficit in the balance of payments was reduced from N.Kr. 1,365 million in 1947 to N.Kr. 890 million in 1948 but, notwithstanding Marshall aid to the equivalent of N.Kr. 285 million and various credit operations, Norway had to draw upon the accumulated foreign currency reserves of the Norges Bank, other banks and certain shipping concerns to the extent of N.Kr. 267 million. The freights earned by Norwegian shipping furnished a net amount of N.Kr. 790 million in 1948, covering practically half the trade deficit in that year.

Sweden, too, had to draw on its monetary reserves in foreign exchange in 1948, the combined losses of the Riksbank and the commercial banks amounting to S.Kr. 275 million. In the previous year, the trade deficit had reached the all-time peak of S.Kr. 1,980 million, with a current deficit of S.Kr. 1,440 million in the balance of payments. This led to the reimposition of a stringent control over foreign trade; at the same time, taxation was increased to secure a budget surplus, and investments were cut down (in the building trade by 10 per cent.). A "plan" for the country's foreign trade was worked out and adopted as a guide but, as shown by the following table, actual trade has exceeded the figures anticipated.

Sweden: Foreign trade.

Items	1947	1948		1949
		Plan	Actual trade	Plan
	in millions of S.Kr.			
Imports. . .	5,220	4,345	4,877	4,200
Exports. . .	3,240	3,675	3,965	3,750
Balance . .	– 1,980	– 670	– 912	– 450

Sweden: Trade with United States and United Kingdom.

Items	1947	1948	Difference
	in millions of S.Kr.		
Swedish imports from:			
United States.	1,640	688	– 952
United Kingdom . . .	444	839	+ 395
Swedish exports to:			
United States.	349	295	– 54
United Kingdom . . .	491	673	+ 182

The import surplus was thus about S.Kr. 240 million larger than had been "planned" and the result was a current deficit of S.Kr. 450 million for 1948 in the balance of payments. Imports from the United States had been severely cut down but exports to that country could not be kept up, the sales of pulp and paper, in particular, lagging behind expectations.

Swedish export prices rose from 1947 to 1948 by about 12 per cent., which to some extent explains the increase in the value figures for Swedish exports over and above the estimates in the plan.

In 1945 the volume of Finland's foreign trade reached barely 18 per cent. of the 1935 level, but by 1948 imports came to 121 per cent. of 1935 and the volume of exports to 67 per cent. without the reparation deliveries, and 79 per cent. including those deliveries. The terms of trade had, however, moved strongly in favour of Finland: with 1935 equal to 100, c. i. f. prices of imports stood at 996 in 1948, while f. o. b. prices of exports had risen to 1,278.

If account is taken of invisible income (mainly freights earned abroad by the Finnish merchant fleet), it would seem as if the current deficit in the balance of payments has been considerably reduced if not wholly wiped out.

By a decision of the Soviet Union the war-reparation debt remaining on 1st July 1948 was reduced by one-half, which meant that of the original total of $300 million (at 1938 prices) an amount of $73.5 million, or 24.5 per cent., was cancelled. It has been calculated that, after the cutting of the yearly instalments by half of their original amount, their charge upon the national income will be reduced to less than 4 per cent.

Finland: Foreign trade.

Period	Index of whole-sale prices	Imports	Exports	Balance	Reparations exports*
		in milliards of Finnish markkas			
1935 yearly total . .	1	5.3	6.2	+ 0.9	—
1938 „ „ . .	1	8.6	8.4	— 0.2	—
1945 „ „ . .	4	6.8	5.2	— 1.6	8.2
1946 „ „ . .	6	24.3	23.1	— 1.2	8.8
1947 „ „ . .	7	47.0	45.2	— 1.7	10.4
1948 „ „ . .	9 ½	66.4	56.5	— 9.9	11.5
1947 monthly average	6	3.9	3.8	— 0.1	0.9
1948 „ „	9 ½	5.5	4.7	— 0.8	1.0
1949 January . . .	9 ½	4.1	3.1	— 1.0	0.8
February . . .	9 ½	4.2	3.7	— 0.5	0.7
March	9 ½	4.8	3.9	— 0.9	0.6

* Not included under "Exports".

For 1948 as a whole, 0.8 per cent. of Finnish exports went to Germany but virtually no imports were obtained from the latter country, while in 1938, on an average for imports and exports, 17.5 per cent. of Finland's foreign trade was with Germany.

This is an extreme case but it illustrates the complete dropping-out of Germany as an active trade partner over a vast area in Europe. The aggregate volume of exports of the various zones in Germany to other countries in 1948 would seem to have been barely one-fifth of Germany's exports in 1936, while the volume of imports (kept up thanks to assistance from the western countries) was between 35 and 40 per cent. of the pre-war figure, and Germany's domestic production was perhaps 50 per cent. of normal (it being difficult to give any exact figures owing to much "clandestine" output and trade). But as far as the three western zones were concerned there was an appreciable improvement after the monetary reform in June 1948.

For the Bizone, i. e. the combined American and British zone, the accompanying trade figures have been published.

The adverse trade balance of 1,347 million marks in 1948 (RM up to the monetary reform, afterwards DM), as well as the net outflow for other foreign-exchange purposes, was (like the

Bizone of Germany: Foreign trade.

Items	January to June 1948	July to December 1948	Whole year 1948
	in millions of RM or DM		
Imports			
Food	747	1,078	1,825
Other goods	424	915	1,339
Total imports . . .	1,171	1,993	3,164
Exports			
Staple goods*	239	620	859
Other goods	246	712	958
Total exports . . .	485	1,332	1,817
Import surplus	686	661	1,347

* Coal, coke, timber and scrap iron.

Bizone of Germany: Balance of payments.

Items	1945-46 (1)	1947	1948
	In millions of U.S. dollars		
Current account			
Foreign trade: (2)			
Exports	163 (3)	200	540
Imports	739 (3)	705	1,404
Balance of foreign trade	— 576 (3)	— 505	— 864
Services: (4)			
Income	. (3)	25	59
Expenditure	. (3)	3	11
Balance of services	(3)	+ 22	+ 48
Balance on current account	— 576	— 483	— 816
On capital account the following amounts were available:			
G.A.R.I.O.A. (5)	—	600	899
E.R.P.	—	—	99
Not specified	576	—	—
Total available on capital account	+ 576	+ 600	+ 998
Difference between total available on capital account and the deficit on current account: foreign exchange available for import payments (+)	—	117	182

French Zone of Germany: Balance of payments.

Items	1945-46 (1)	1947	1948
	In millions of U. S. dollars		
Current account			
Foreign trade: (6)			
Exports	64	120	106
Imports	46	120	179
Balance of foreign trade	+ 18	—	— 73
Services:			
Income	(7)	4	3
Expenditure	(7)	15	9
Balance of services	(7)	— 11	— 6
Capital account			
E.C.A.	—	—	+ 37
Assets in Sweden (8)	—	—	+ 4
Not specified	— 18	+ 11	+ 38
Total	— 18	+ 11	+ 79

trade deficits of the previous years) offset to some extent by an income surplus from "services" and, for the rest, by assistance from abroad. The table shows the figures (converted into dollars) of the balance of payments for the Bizone from 1945–46 up to 1948.

Fairly reliable data have gradually become available for the estimates of trade in goods and of services, the compilation being made on the basis of the J.E.I.A. (Joint Export-Import Agency) statistics; but it must be clearly stated that, especially for the period before 1947, the figures are incomplete. For the distribution of the Bizone's foreign trade in 1948, the Economic Commission for Europe gives a series of figures which, as to the totals, tally fairly well with the trade figures for the same year in the table.

(1) Covering the period from 1st August 1945 to 31st December 1946.

(2) The item "Foreign trade" includes export and import of electric current.

(3) For 1945-46 the export and import figures include the service items.

(4) The service items include the usual items of invisible income but no payments of interest and dividends.

(5) G.A.R.I.O.A. stands for "Government Appropriations and Relief for Imports in Occupied Areas" (as granted by the U.S. Congress to prevent disease and unrest in these areas, viz. Germany, Austria, Japan, Korea and Trieste).

(6) Including export and import of electric current.

(7) Included in export and import figures.

(8) Mobilised from previous German assets, payment for imports into the French Zone being made subject to the reservation that a settlement is ultimately reached with France.

The Economic Survey of Europe in 1948 (published Geneva, May 1949) notes three striking features of the foreign trade of the Bizone:

Germany: Foreign trade in 1948.

Regions	Imports	Exports	Balance
	in millions of U. S. dollars		
Bizone's trade with:			
the United States	840	28	— 812
other overseas countries	285	43	— 242
western European countries	357	538	+ 181
eastern European countries	26	16	— 10
Total	1,508	625	— 883
Other zones*	278	258	— 20
Whole of Germany . .	1,786	883	— 903
Compare: whole of Germany: 1938	1,836	2,033	+ 197

* Excluding trade between the USSR and the Soviet zone of Germany.

(i) abnormal dependence on imports from the United States — even, to a certain extent, as regards products which might be obtainable in Europe;

(ii) large export surplus with western Europe; and since the exports of the Bizone consisted largely of essential goods (coal, timber and machinery), the receiving countries could generally be forced to pay in dollars for surplus imports; and

(iii) the virtual absence of trade with eastern Europe; while in 1938 about one-fifth of total German exports went to the eastern European area, only 2½ per cent. of the exports of the Bizone went there in 1948; and it is iron and steel products, tools and machines, chemical products and some other specialities of western Germany that the eastern European countries need most to import.

It may be recalled that before the war western Germany obtained what it needed in the way of grain and several other foodstuffs largely from the domestic production of the eastern parts of the Germany of that day;* but this generally meant that relatively high prices had to be paid, since German agriculture was heavily protected. It is not impossible that western Germany might be able to obtain its food more cheaply through imports from the west, provided that German exports can count on not meeting with too great obstacles in the form of tariffs, etc. Less exporting to the east and more to the west will mean that Germany will have increasingly to compete with highly industrialised countries, which will in their turn feel the impact of the added German competition. It is not that competition in itself is to be feared, but there will be a loss all round if trade is not allowed to develop in directions where natural outlets exist and where an exchange of goods and services would be of most benefit to all parties.

For the eastern zone of Germany, Poland was the second trade partner in 1948. In that year reparations payable to the U.S.S.R. were officially fixed at 10 per cent. of the gross industrial production and deliveries to the Soviet occupation troops at 5 per cent., but no return is available as to the value of actual deliveries, while for 1949 a total of 12.4 per cent. of the gross production is to go to reparations and the occupation troops in the east.

* In 1936, the whole of Germany imported 350,000 tons of cereals, potatoes and sugar, while, in 1948, the Bizone alone imported 5.6 million tons of these commodities.

UNRRA aid as of 30th September 1947.

Countries	In millions of U.S.$	Percentage of total for	
		Europe	World
Albania	26	*1.1*	*1.0*
Czechoslovakia	261	*11.2*	*9.2*
Hungary	4	*0.2*	*0.1*
Poland	471	*20.3*	*16.7*
Yugoslavia	407	*17.5*	*14.4*
U.S.S.R.:	249	*10.7*	*8.8*
Byelo-Russia	61	*2.6*	*2.1*
Ukraine	188	*8.1*	*6.7*
Total for eastern Europe	1,418	*61.0*	*50.2*
Rest of Europe	906	*39.0*	*32.0*
Total for Europe	2,324	*100*	*82.2*
World Total	2,826	—	*100*

In the immediate post-war period it seemed as if the countries in eastern Europe, after having been cut off from the general circuit of world trade, were being brought back into it by the movement of goods and services through which UNRRA aid was made available (with these countries as its chief beneficiaries).

But UNRRA aid came finally to an end in the first half of 1947 and in that and the following years certain new circumstances had the effect of adding to the distance, in matters of commerce, between eastern and western Europe:

(i) The non-participation of the eastern European countries in the Marshall aid co-operation which was inaugurated in the summer of 1947.

(ii) The fact that a very poor harvest, due to the prolonged drought, not only deprived these countries of a large part of the supplies usually exported to the west but made them dependent upon obtaining food from the U.S.S.R., which led to increased trade in the eastern direction.

(iii) Difficulties and delays in arriving at commercial agreements — one reason for the protracted negotiations being differences of opinion with regard to compensation of foreign shareholders in enterprises which had been nationalised.

(iv) Announcements by the United States (the first one in March 1948) of a list of goods (including tools and machinery) which for strategic reasons would not be sold to the countries in eastern Europe; and similar announcements later on by a number of other countries.

(v) The controversy regarding Berlin, which in June 1948 led to the discontinuance of land traffic (replaced in a large measure by the air bridge) and then the prohibition of trade between the western zones and the Soviet zone of Germany — these measures having repercussions on the volume of trade even outside Germany (e. g. transit trade).

So it happened that, when production in Europe began to recover (apart from the exceptionally bad harvest of the single year 1947), east-west trade did not recover to the same extent; and no large-scale arrangement of credit or other form of assistance proved possible. In 1947 exports from eastern Europe to O.E.E.C. countries came to less than the equivalent of \$1 milliard and in 1948 they increased only to \$1¼ milliard. It has been calculated that the corresponding imports in 1938 were equivalent to \$3¼ milliard (at the prices prevailing early in 1949). Thus in 1948 trade between western and eastern Europe barely reached 40 per cent. of pre-war.

Poland, Czechoslovakia, Hungary and Bulgaria: Foreign trade equivalents in dollars.

Countries	Imports	Exports	Balance
	in millions of U.S. dollars		
Poland:			
1947	318	248	— 70
1948	540	480	— 60
Czechoslovakia:			
1947	578	571	— 7
1948	754	753	— 1
Hungary:			
1947	124	89	— 35
1948	168	165	— 3
Bulgaria:			
1947	75	86	+ 11
1948	112	92	— 20

Czechoslovakia: Foreign trade.

Distribution of trade	1947	1948	Difference
	in millions of U.S. dollars		
Eastern Europe:			
Imports	114	268	+ 154
Exports	109	287	+ 178
Total trade with eastern Europe	223	555	+ 332
Other trade:			
Imports	464	486	+ 22
Exports	462	466	+ 4
Total trade with other countries	926	952	+ 26

For Czechoslovakia, Hungary and Bulgaria foreign trade statistics are available in national currencies, while for Poland figures converted into current dollars are the only ones published. It has been the practice in several of these countries to convert trade statistics into dollars.

In 1948 there was an increase of about 50 per cent. in the turnover for the four countries, with a reduction in the deficit for Poland and its practical disappearance for Czechoslovakia and Hungary, while Bulgaria saw a surplus change to a moderate deficit.

As is shown by the figures in the accompanying table, a larger exchange of goods with other countries in eastern Europe was responsible for the whole increase in Czechoslovakian imports, as well as exports, in 1948.

As regards Hungary, 46 per cent. of the imports and 41 per cent. of the exports were in relation to the eastern European countries. For Poland it is reported that 46 per cent. of the total turnover (in both directions) was with the east of Europe, including 22 per cent. with the U.S.S.R. as partner.

New trade agreements concluded between various eastern European countries for 1949 or for longer periods seem to indicate an intention to increase intra-eastern European trade — in some cases by only 30 per cent., in others up to 150 per cent. At the same time there is, however, a reduction in the trade with Yugoslavia, which has seen a severance of its commercial relations with a number of the countries in the eastern European area.

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*

The turnover of foreign trade of the countries in eastern Europe represents about one-eighth of the total trade turnover in Europe. Moreover, the aggregate balance of payments of these countries as a bloc seems to have been in equilibrium in 1948. For this reason, the deficit on current account, as well as the other figures in the following table on Europe's balance of payments, reflects in the main the developments in relation to visible and invisible trade of western Europe (the O.E.E.C. countries).

The current deficit of $5.6 milliard in 1948 was covered mainly by $3.6 milliard in U.S. Government grants, $0.7 milliard in U.S. Government credits, $0.3 milliard in loans from the International Bank for Reconstruction and Development and amounts drawn on the International Monetary Fund, $0.3 milliard through a South African gold loan to the United Kingdom, $0.5 milliard through drawings on sterling balances, Canadian and Latin American credits, and $0.2 milliard through the net use of gold and dollar assets.

Europe: Current account of the balance of payments.

Item	1938			1947			1948 *		
	United States	Other non-European countries	Total	United States	Other non-European countries	Total	United States	Other non-European countries	Total
	in milliards of current dollars								
Europe's imports (f.o.b.)	1.3	4.2	5.5	6.1	7.8	13.9	4.8	10.0	14.8
Europe's exports (f.o.b.)	0.6	3.1	3.7	0.9	5.5	6.4	1.1	7.5	8.6
Balance on trade account	— 0.7	— 1.1	— 1.8	— 5.2	— 2.3	— 7.5	— 3.7	— 2.5	— 6.2
Income from investments (net)	+ 0.1	+ 1.1	+ 1.2	—	+ 0.6	+ 0.6	—	+ 0.5	+ 0.5
Transport (net) . . . }	+ 0.2	+ 0.4	+ 0.6	— 0.7	+ 0.3	— 0.4	— 0.2	+ 0.5	+ 0.3
Other invisibles (net) . }				+ 0.2	— 0.5	— 0.3	+ 0.3	— 0.5	— 0.2
Balance on invisibles account	+ 0.3	+ 1.5	+ 1.8	— 0.5	+ 0.4	— 0.1	+ 0.1	+ 0.5	+ 0.6
Balance on goods and services	— 0.4	+ 0.4	—	— 5.7	— 1.9	— 7.6	— 3.6	— 2.0	— 5.6

Note: The estimates for 1947 and 1948 were prepared by the Research Department of the International Monetary Fund. More detailed data on national balances of payments are found in the Fund's publication "Balance of Payments Yearbook", published in Washington, 1949. * Provisional.

As may be seen from the above table, the improvement in Europe's balance of payments from 1947 to 1948 was all in relation to the United States and was achieved through a reduction of $1.3 milliard in Europe's imports from that country and an increase of $0.2 milliard in Europe's exports to that country plus a change-over from a deficit (of $0.5 milliard) to a surplus of $0.1 milliard on invisible items (mainly on account of shipping and tourists). According to the table, Europe had in 1948 a current deficit equivalent to $2 milliard in relation to non-European countries other than the United States. A small part of this was paid for by sales of capital assets but most of it would seem to have been settled in dollars. In fact, the International Monetary Fund estimates that Europe as a region (and thus excluding all intra-European settlements in gold and dollars) paid $1.9 milliard to non-European countries other than the United States out of the dollar receipts obtained in the continent's relations with the United States. These payments were thus instances of multilateral settlements and, although the estimate is subject to many reservations (since it assumes that the item for errors and omissions in Europe's balance of payments was entirely attributable to Europe's transactions with countries other than the United States), it seems that most of the multilateral settlements have been official in character and that the transfers of funds covered by the estimate are broadly in accordance with the known course of payments.

Balance of trade of the O.E.E.C. countries with other countries.

Period	North and Central America	South America	Total western hemisphere	Sterling area*	Eastern Europe	Others	Total
	Annual rates, in milliards of current dollars						
1947: 1st half	— 4.9	— 0.8	— 5.7	+ 0.1	+ 0.1	— 0.1	— 5.6
2nd half	— 5.7	— 0.8	— 6.5	— 0.1	— 0.2	+ 0.1	— 6.7
1948: 1st half	— 4.0	— 0.9	— 4.9	— 0.2	— 0.3	— 0.4	— 5.7
2nd half	— 3.5	— 0.4	— 3.9	+ 0.2	— 0.3	— 0.2	— 4.2

* Excluding the United Kingdom, Iceland and Ireland, which are in the group of O.E.E.C. countries.

The difficulties which beset Europe in the course of 1947 are reflected in the increase in the trade deficit from the first to the second half of that year. The figures for 1948 show a distinct improvement — and it may be added that the first quarter of 1949 confirms the continuance of the improvement. It is interesting to note the restoration of a traditional pattern: the O.E.E.C. countries have developed a trade deficit (of some $650 million on a yearly basis) in relation to eastern Europe which, indeed, through its surplus sales to western Europe obtained purchasing power to pay for imports from overseas countries (largely the sterling area). On the other hand, it should be noted that the O.E.E.C. countries achieved a surplus in relation to the sterling area.

The foreign-trade figures just quoted reveal no mean improvement in the course of 1948. An adjustment has been taking place and is continuing in 1949. Sometimes the obstacles in the way of the restoration of a satisfactory balance may seem formidable and there may be impatience with the difficulties involved in removing the obstacles. Obviously, things are far from being in perfect order in Europe; but it is sometimes hard to tell whether, for instance, existing exchange rates are in general a great drag upon recovery in trade. Rarely is the statistical evidence of relative costs and prices conclusive, especially as regards prices of finished goods, where quality plays a considerable rôle. But it is important not to exaggerate the extent of such disequilibria as no doubt remain. Generally speaking, costs, prices and exchange rates in western Europe cannot have been very much out of line with intrinsic currency values; otherwise the improvement which has taken place, and is still going on, would hardly have been possible.

* * *

The complementary aspect of the improvement of European and other trade balances (Canada's, for instance) is a reduction in the export surplus of the United States from \$9.6 milliard in 1947 to \$5.5 milliard in 1948, or by 40 per cent. The reduction is due to a decrease of \$2.7 milliard in exports and an increase of \$1.3 milliard in imports; if account is taken of the

United States: Foreign trade.

Period	Total Imports	Exports			Export surplus	
		Total	Cash	Aid and relief	Total	Cash
	in millions of dollars					
	1	2	3	4	1—2	1—3
1938 Yearly total	1,960	3,094	3,094	—	+ 1,134	+ 1,134
1946 „ „	4,909	9,739	7,964	1,775	+ 4,830	+ 3,055
1947 „ „	5,733	15,340	13,682	1,658	+ 9,607	+ 7,949
1948 „ „	7,070	12,614	11,056	1,558	+ 5,544	+ 3,986
1946 Monthly average	409	812	664	148	+ 403	+ 255
1947 „ „	478	1,278	1,140	138	+ 800	+ 662
1948 „ „	589	1,051	921	130	+ 462	+ 332
1949 January	589	1,086	*	*	+ 497	*
1949 February	568	1,028	*	*	+ 460	*
1949 March	632	1,152	*	*	+ 520	*

* Not yet available separately.

rise in prices, it would seem that, in real terms, the export surplus fell by one-half from 1947 to 1948. It is not only in relation to Europe that the United States has a smaller export surplus; the same applies to almost all its trade partners.

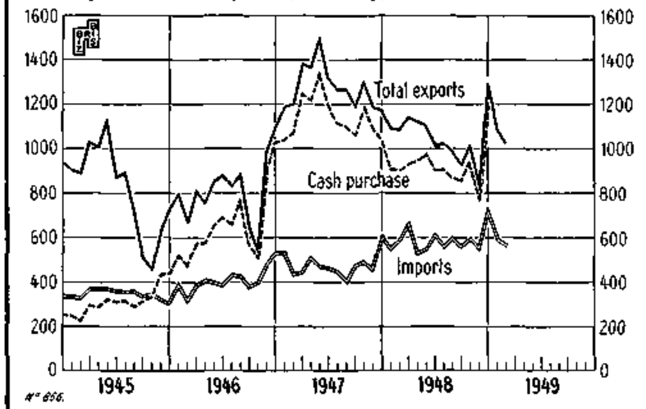
Geographical distribution of U. S. foreign trade.

Items and Years	O.E.E.C. countries	Rest of Europe	Total for Europe	Canada	Latin America	Africa and Near East	Oceania and Far East	Total (1)
	in millions of dollars							
Exports and re-exports (2)								
1936-38 (3)	1,129	125	1,254	454	486	149	557	2,967
1946	3,279(4)	866	4,145	1,442	2,100	583	1,328	9,739
1947	5,296	472	5,768	2,074	3,858	1,043	2,346	15,340
1948	4,183	196	4,379	1,914	3,161	1,043	1,888	12,614
General imports								
1936-38 (3)	606	119	725	345	542	81	757	2,489
1946	679	191	870	883	1,760	422	880	4,909
1947	695	182	877	1,095	2,150	377	1,098	5,733
1948	955	186	1,141	1,553	2,329	526	1,327	7,070
Balance of Trade								
1936-38 (3)	+ 523	+ 6	+ 529	+ 109	— 57	+ 68	— 200	+ 478
1946	+ 2,600	+ 675	+ 3,275	+ 559	+ 340	+ 161	+ 448	+ 4,830
1947	+ 4,601	+ 290	+ 4,891	+ 979	+ 1,708	+ 666	+ 1,248	+ 9,607
1948	+ 3,228	+ 10	+ 3,238	+ 361	+ 832	+ 517	+ 561	+ 5,544

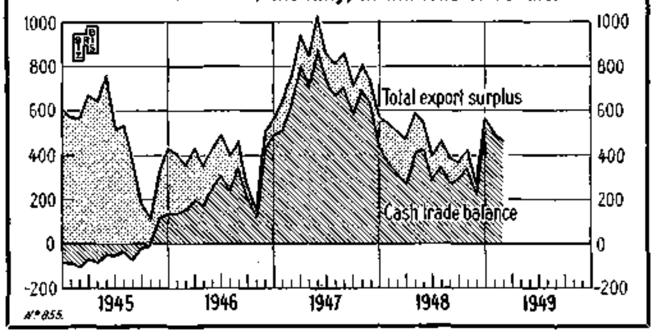
(1) Including areas other than those specified. (2) Including lend-lease and various kinds of relief. (3) Average.
(4) Excluding, in 1946, civilian supplies to Germany, which — it should be noted — are included in the figures for the following years.

United States: Foreign Trade.

Imports and exports, monthly, in millions of dollars.



Trade balance, monthly, in millions of dollars.



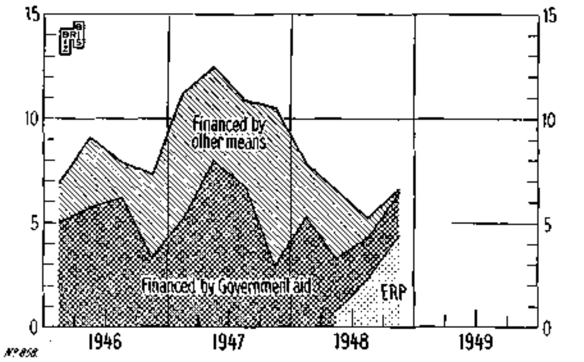
The United States had in 1947 and 1948 a surplus with all the separate areas shown in the table, although in the latter year the surplus had shrunk to a very small one in relation to European countries other than those participating in O.E.E.C. The percentage changes in foreign trade from 1947 to 1948 reveal even more clearly the shift which has been taking place.

United States:
Percentage changes in geographical distribution of foreign trade from 1947 to 1948.

Trade with	Exports from the United States	Imports into the United States	Export surplus of the United States
	1948 as percentage of 1947		
O.E.E.C. countries	— 21	+ 37	— 30
Rest of Europe	— 58	+ 2	— 97
Total for Europe	— 24	+ 30	— 34
Canada	— 8	+ 42	— 63
Latin America	— 18	+ 8	— 51
Africa and the Near East	— 0	+ 40	— 22
Oceania and the Far East	— 20	+ 21	— 55
Total for the world	— 18	+ 23	— 42

It seems somewhat paradoxical that in the first year of Marshall aid the United States should have exported less to Europe than in 1947. For one thing, not all of the Marshall aid went to pay for exports from the United States, about one-third being used in settlement of "off-shore purchases", i.e. purchases in countries other than the United States. (In 1948 total procurement authorisations for the purchase of commodities amounted to $3,707 million, of which $2,299 million were on account of the United States.) In addition to commodity purchases, authorisations included $ 1.2 million for technical services and $337 million for ocean freights. Secondly, it is important to remember that by the end of 1947 a large number of the countries in Europe had depleted their dollar reserves to such an extent that they became almost wholly dependent upon foreign aid for the payment of surplus imports and, therefore, simply had to cut down their purchases in the United States. Thirdly, the year 1947 saw the disposal (generally on credit terms) of the

United States: Export surplus of goods and services.
Annual rates, in milliards of dollars.*



* Department of Commerce data.

bulk of the American war stocks left behind in the recipient countries. Fourthly, there is the more satisfactory circumstance that the recovery in European production made some American exports unnecessary; this explains the decline in European imports of $200 million in coal and of $500 million in machinery, in rolling stock and ships — to mention only some of the most important items.

On the other hand, the increase in imports by the United States is encouraging, although it has not as yet gone very far. In 1948 total imports corresponded to 3.2 per cent. of the national income — a proportion no larger than in 1932, i.e. in the very depth of the depression.

United States:
Imports and tourist expenditure
as percentage of the national income.

Year	National Income	Imports		Tourist expenditure	
		Amount	as percentage of national income	Amount in millions of dollars	as percentage of national income
	in millions of dollars				
1929	87,400	4,400	5.0	480	0.55
1932	41,700	1,320	3.2	260	0.62
1937	73,600	3,080	4.2	350	0.48
1947	202,500	5,730	2.8	540	0.27
1948	224,400	7,070	3.2	600	0.27

Were the percentage rates for the boom year 1929 applied to the national income of 1948, total imports would have been $11,200 million and tourist expenditure $1,230 million, which seems to indicate the possibility of a greater power of absorption of European goods by the American market than is usually assumed — and in 1929 the American tariff stood higher than it does now (see footnote page 31).

Both in 1947 and in 1948 the United States had a net income from invisibles, which thus had to be added to the surplus of exports in the current account of the balance of payments.

While among the invisible items the income from investments rose slightly, the income from "other services" gave place to a net out-payment in 1948. This was due principally to a decline in the net foreign demand for transport from more than $1 milliard to $440 million, the reduction in the volume of American exports having been accompanied by an increase in the share carried by foreign vessels.

United States: Current account of the balance of payments.

Items	1947	1948
	in millions of $	
Export surplus	+ 9,985	+ 5,687
Net income from investments .	+ 847	+ 983
Net income from other services	+ 446	— 335
Balance of goods and services.	+ 11,278	+ 6,335

The main movements on the capital account of the balance of payments have already been referred to on page 9. In 1948 net U.S. Government gifts and other unilateral transfers came to $4,308 million, the net amount of long-term loans and investments by the United States Government to $687 million and the net outflow of other, i.e. private, capital to $906 million. These figures show the overwhelming part still played by transfers on government account — in itself a measure of the exceptional conditions which still prevail.

* * *

Among the countries which in 1948 managed to establish a better balance with the United States there is, in the first place, Canada. As can be seen from the table on page 10, 1948 brought a shifting of Canadian exports towards the United States in comparison both with 1947 and with pre-war years. Thus, the triangular pattern of a heavy trade deficit with the United States compensated by a surplus with the United Kingdom (and some other countries) has been tending to be replaced by a relationship of more direct equilibrium in both directions — an achievement in its way, no doubt, but nevertheless a sign of the regrettable necessity of developing trade at the present time according to the dictates of bilateral equilibrium.

The countries in the sterling area,* on the other hand, have been able both to improve their balance with the United States and to develop their trade with western Europe, whose imports from that source increased by more than $1,100 million in 1948 as compared with 1947. A certain connection can, no doubt, be seen between this advance and the state of freedom from hampering monetary restrictions between countries using transferable sterling. With more general application, a similar reason provides an explanation of the improvement noticeable in trade between countries within the same monetary area (e.g. the relations between metropolitan France and the French overseas territories) and this constitutes indirect evidence that at the present time the most formidable obstacles in the way of foreign trade may be found in monetary — as distinct from merely commercial — restrictions.

To a considerable extent, however, the increase in European exports to the sterling-area countries reflects a flow of goods in settlement of past liabilities (so-called "unrequited exports"), paid for with sterling balances which originated in relations with the United Kingdom during the war (see page 77).

* Excluding in this context the United Kingdom, Ireland and Iceland, since these are participants in O.E.E.C.

How far a shift in the availability of financial resources affects trade currents is also illustrated in a general way by the countries in Latin America, which in 1945 had at their disposal nearly $4,000 million in gold and U.S. dollars accumulated during the war. A considerable part of these holdings were soon used up to pay for restocking purposes, and some of the Latin American countries also began to execute ambitious investment programmes which required surplus imports. The result has been that several of the countries in question have run into payment difficulties and are trying to regain their balance under conditions which do not yet allow a resumption of all-round multilateral trading. A continued recovery in the European economy should facilitate the task for the Latin American countries — but increased trade with Europe necessarily implies readiness to accept manufactured goods and, in general, to use European services in the sphere of transport, banking, insurance, etc.

Re-establishment of multilateral trade is certainly a very important matter as far as Europe's internal relations are concerned. But such a re-establishment must in no way be limited to Europe: a more far-reaching success in the return to multilateralism, with a recovery in triangular trade, requires the adoption of appropriate commercial and monetary policies in countries and areas outside the continent of Europe itself.

* * *

The restoration of sufficient balance in international trade, after the losses brought about by the biggest of all wars and the consequent displacements of wealth, could never have been a simple task. New lines of trade, with all that they involve, are not easily developed. There are undoubtedly some strong forces which tend to re-establish traditional currents of trade according to deep-seated differences in basic resources, technique and output. But old ways may have to be altered: the flow of goods and services cannot but take account of major changes in the distribution of effective purchasing power between the various nations and continents.

The inter-war period already taught the world how difficult it is to rearrange the pattern of commerce so that it corresponds to the shift in purchasing power. In the first place, certain conditions must be fulfilled in the exporting country, including an adaptation (if necessary by credit restrictions) of domestic purchasing power to the actual production of goods and services, so that goods which should be exported are not used for consumption or equipment at home; there must also be a sufficient degree of flexibility to enable labour and other factors of production to be transferred to the requisite export industries from other modes of employment.

But certain important conditions must also be fulfilled in the importing country, which — in the world as we know it — means, in the first place, the United States. If, as may be expected, the flow of grants and other

Visible and invisible trade of a number of countries.

Countries	Years	Currencies	Exports	Imports	Surplus of exports (+) or imports (—)	Surplus (+) or deficit (—) of service items	Surplus (+) or deficit (—) on current account
			In millions of (national) currency units				
United States . . .	1938	Dollars	3,243	2,173	+ 1,070	+ 210	+ 1,280
	1946		12,140	5,264	+ 6,876	+ 1,257	+ 8,133
	1947		16,056	6,071	+ 9,985	+ 1,293	+ 11,278
	1948		13,398	7,711	+ 5,687	+ 648	+ 6,335
Canada	1938	Can. $	844	649	+ 195	— 95	+ 100
	1946 (1)		2,393	1,822	+ 571	— 214	+ 357
	1947 (1)		2,723	2,535	+ 188	— 141	+ 47
	1948 (1)		3,030	2,598	+ 432	+ 21	+ 453
Belgium	1938	B. fcs	21,670	23,069	— 1,399	.	.
	1946		29,694	52,562	— 22,908	.	.
	1947		61,609	85,528	— 23,919	+ 18,419	— 5,500
	1948		74,020	87,418	— 13,398	+ 11,500	— 1,898
Bulgaria	1938	Leva	5,580	4,930	+ 650	.	.
	1946		14,940	17,510	— 2,570	.	.
	1947		24,530	21,420	+ 3,110	.	.
	1948		26,200	32,000	— 5,800	.	.
Czechoslovakia . .	1937	Kčs	11,972	10,989	+ 983	— 583	+ 400
	1946		14,283	10,308	+ 3,975	.	.
	1947		27,980	33,480 (2)	— 5,500	+ 2,250	— 3,250
	1948		37,648	37,716	— 68	.	.
Denmark	1938	D. Kr.	1,582	1,665	— 83	+ 194	+ 111
	1946		1,633	2,864	— 1,231	+ 301	— 950
	1947		2,371	3,144	— 773	+ 360	— 413
	1948		2,740	3,450	— 710	+ 440	— 270
Finland	1938	FM	8,425	8,590	— 165	+ 575	+ 410
	1946 (3)		23,050	24,270	— 1,220	+ 1,850	+ 630
	1947 (3)		46,250	46,970	— 720	+ 1,925	+ 1,205
	1948 (3)		56,505	66,369	— 9,864	.	.
France (4)	1938	U.S.$	386	625	— 239	+ 234	— 5
	1946		453	1,980	— 1,527	— 225	— 1,752
	1947		1,040	2,492	— 1,452	— 61	— 1,513
	1948		1,060	2,404	— 1,344	— 208	— 1,552
Hungary	1938	Pengő	522	411	+ 111	.	.
	1946	Forint	420	371	+ 49	.	.
	1947		1,042	1,453	— 411	.	.
	1948		1,933	1,975	— 42	.	.
Italy	1938 (5)	U.S.$	515	708	— 193	+ 171	— 22
	1946		489	903	— 414	+ 46	— 368
	1947		666	1,566	— 900	+ 78	— 822
	1948		1,070	1,390	— 320	+ 48	— 272
Netherlands. . . .	1938	Fl.	1,086	1,245	— 159	+ 176	+ 17
	1946		815	2,143	— 1,328	+ 236	— 1,092
	1947		1,772	3,595	— 1,823	+ 257	— 1,566
	1948		2,738	4,164	— 1,426	+ 475	— 951

(1) Excluding official relief but including, in 1946 and 1947, receipts by War Supplies Ltd. (2) Including UNRRA imports.
(3) Excluding exports for reparation payments and commodities surrendered in compensation for German assets.
(4) Excluding overseas territories; but in 1938 including estimated import surplus of overseas countries.
(5) At June 1946 purchasing power.

assistance should come to an end and private lending and other forms of investment should not immediately assume any considerable proportions, then the purchasing power which, through the loans and grants, used to be put at the disposal of the other countries will be retained in the United States. The question then arises under what conditions that purchasing power will best be able to attract goods and services as imports into the United States.

(i) The purchasing power retained in the United States should be effectively used and not allowed to run to waste, as happened in the depression of the nineteen-thirties. Since a part of that purchasing power will presumably be saved and, if it is not to languish in idleness, will have to be invested, it is imperative that the United States should be able to achieve a fairly high level of economic activity — which means that it will require substantial imports.

(ii) The United States should not, by its tariff, put too great obstacles in the way of imports. The fact that the United States has in most lines a very high productive capacity is not in itself a hindrance to trade: highly developed industrial countries — e.g. Great Britain and Germany — have in the past often been each other's best customers, since it is a question of comparative costs between different lines of production. But suppose a high tariff is maintained for the very goods which foreign countries are relatively most capable of producing. These countries may nevertheless have no choice but to export the goods in question to the United States. In technique, however, American production in those lines may also be first-rate and, therefore, the differential advantage in costs which the other countries must have in order to surmount the tariff may have to be obtained through the payment of

Visible and invisible trade of a number of countries (contd.)

Countries	Years	Currencies	Exports	Imports	Surplus of exports (+) or imports (—)	Surplus (+) or deficit (—) of service items	Surplus (+) or deficit (—) on current account
			in millions of (national) currency units				
Norway	1938	N. Kr.	824	1,116	— 292	+ 391	+ 99
	1946		1,239	2,428	— 1,189	+ 602	— 587
	1947		1,898	3,800	— 1,902	+ 537	— 1,365
	1948		2,140	3,666	— 1,526	+ 636	— 890
Poland	1938	U.S.$	224	245	— 21	.	.
	1946		127	146	— 19	.	.
	1947		248	317	— 69	.	.
	1948		480	540	— 60	.	.
Sweden	1938	S. Kr.	1,843	2,082	— 239	+ 263	+ 27
	1946		2,550	3,390	— 840	+ 750	— 390
	1947		3,240	5,220	— 1,980	+ 540	— 1,440
	1948		3,960	4,870	— 910	+ 460	— 450
Switzerland	1938	Sw. fcs	1,317	1,607	— 290	.	.
	1946		2,676	3,423	— 747	.	.
	1947		3,268	4,820	— 1,552	.	.
	1948		3,435	4,999	— 1,564	.	.
United Kingdom .	1938	£ stg	533	835	— 302	+ 232	— 70
	1946		889	1,097	— 203	— 172	— 380
	1947		1,100	1,541	— 441	— 189	— 630
	1948		1,550	1,768	— 218	+ 98	— 120

low wages — a necessity which may have serious social consequences. Thus the problem is not purely an economic one: limits of a more social and political character may be reached if, through tariffs and in other ways, a great strain of readjustment is placed on countries already struggling with their own post-war difficulties. This is beginning to be well understood and, though it would be a mistake to draw the conclusion that certain — even painful — adjustments will not be necessary, it is equally important that an attempt should be made to alleviate the hardships of these adjustments by, for instance, a suitable tariff (or licensing) policy in the stronger countries.

If the United States absorbs imports on a sufficient scale, other countries may be able to continue to purchase American goods without having to impose heavy restrictions. But if, for one reason or another, this condition fails to materialise, and if the loans and grants to other countries taper off, then the United States will naturally be under the necessity of changing its own export pattern — and the question then arises whether it has the requisite flexibility to effect the change, and whether political resistance to such a change will not make itself strongly felt. Thus the strain of adjusting the mechanism may have its political repercussions not only in Europe, and it is therefore a matter of common interest to make the passage to a new balance as smooth as possible; and in any case not to cause unnecessary difficulties.

Thus, certain measures designed to facilitate the entry of goods need to be taken by those countries which have to increase their imports — and among them predominantly the United States — but it is, of course, vain to expect satisfactory results unless the financial and economic policy of the exporting countries (as regards budgets, investments, etc.) is such that, over and above the domestic expenditure for consumption and investment, it leaves a sufficient supply of goods for export at competitive prices.

Since the war, most European countries and several others outside Europe have tried to restore balance in their foreign trade by way of a curtailment rather than an expansion, the main feature of their control of foreign trade being a cutting-down of imports. Considering that for almost every country in Europe the deficit in the balance of payments still persists, there must surely be some particular reason why the cutting of imports does not eliminate the trade deficit as had been hoped. As a matter of fact, most countries find that the curtailment of imports leads to a reduction in exports. An example (from actual life) may be cited to show the connection between imports and exports: in a country whose monetary reserves were almost exhausted a licence was refused for the import of a machine costing about \$50,000; since the would-be importer could not do without the machine in question (fortunately not a very complicated one), he managed to get it made in his own country at a cost equivalent to about \$70,000. But what effect did this have on the home market at a time when full employment already prevailed? It is not likely that the making of the machine led to a reduction in domestic demand; on the contrary, the probability is that such demand was increased because of the additional spending at home to which the manufacture of the machine gave rise. More money being spent internally, production for domestic purposes would surely not be reduced; and, that being the case, the workers and others factors of production required to produce the machine must have been taken from the export industries — with the net result that exports were reduced and, maybe, by a larger amount than it would have "cost" to allow the importation of the machine.

Again and again, instances of a similar process will arise as long as imports are being curtailed. What looked like an "economy" designed to "save" foreign exchange thus turns out to be an indirect way of reducing exports, and often to a larger extent, a vicious spiral being set in motion which can only be arrested by the adoption of a wholly different policy.

Thus it comes about that refusal to import more of non-essentials than certain minimum quotas can easily result in a more than proportionate reduction in exports and to a consequent aggravation of the trade deficit. The exclusion of non-essentials of foreign origin does not, as experience shows, induce people to save more; other goods are demanded in their place; it is usually found that a host of small new industries spring up to satisfy the need for the goods which cannot be imported; many of these new industries involve a sheer waste of effort, since the domestic production is generally on too small a scale to be economic and is unduly expensive in other ways. While in foreign trade the attitude is to look askance at the importation of anything but essentials, an exaggerated stimulus is given to the domestic production of luxuries, which are generally not subject to regulation in the same way as necessities, the price of which is often kept down — an example of the preposterous contradictions to which controls may lead. And little knowledge is needed about European economies to realise that for many of them it is of paramount importance that the distinction between "essential" and "non-essential" should disappear from the tenets of current trade policy.

But is it not a fact that, as regards a large number of products, a more equal distribution of income after this second world war has greatly reduced demand? That may be so in the case of a few luxuries perhaps, but it surely does not apply to the great mass of goods often styled non-essentials. And it would seem to be for the consumer himself to decide how he wishes to dispose of the income left to him after payment of all dues and taxes. Curiously enough, it is apparently sometimes assumed that even in the "free-enterprise countries" — and that means practically the whole western world — it is the governments which always decide what should be bought from abroad. But, with the exception of particular instances of "bulk buying" (strictly limited to a few necessities), it is the consumer who, in the last instance, decides whether a thing can be sold; governments may refuse to grant import quotas, but even the granting of quotas does not mean that actual trade takes place; whether the goods will actually be imported and ultimately sold to the consumers will depend on the consumers themselves.

It is important to remember this now that, with the return of the buyers' market, success in the sale of goods will depend more and more on the extent to which their quality and price meet the views of the consumers. Foreign sales generally demand more effort and cost more than sales on the home market. As a rule, it is only when the producers cannot sell any more at home that they apply themselves seriously to a search for foreign markets. There is a link between what is imported and what must be exported. Imports always absorb a part of the domestic purchasing power and, in a country where there is no inflation (*i.e.* no addition to the volume of purchasing power beyond what the current increase in production requires), this absorption sets free a corresponding part of the national production for export. (The same applies, of course, to invisible trade: when nationals of a particular country go abroad for holidays they reduce the amount spent at home and that helps, inter alia, to set productive power free for exports and, to some extent, helps to diminish imports.) In fact, the home producers will be once more under compulsion to export. The important thing is, on the one hand, to arrest internal inflation and, on the other, to reinstate the stabilising mechanism which resides in the fact that, once this full monetary balance has been established internally, imports lead to exports — and that is the case not only because imports put purchasing power at the disposal of the seller countries but also because the importing country must needs export in its turn if goods are not to remain unsold. The adjustment of production and the building-up of appropriate sales organisations may be no easy task; but, if the necessary adjustments are shirked, foreign trade will continue to languish at a low level and the gain obtained from it will be lost, to the detriment of the standard of living over the whole world.

To permit imports of non-essentials as well as essentials must, therefore, be an integral part of a rational export policy (because an exchange of goods and services is an advantage in itself and the volume of imports and exports affect each other); but it has also to be remembered that no export policy can be isolated from questions of price and exchange rates. A policy of promotion of exports must never be limited to such matters as the study of foreign markets or the granting of special credit facilities, etc. but must be framed more widely, account being taken of balance in the cost and price structure as influenced by the credit policy and related to foreign economies, the maintenance of appropriate exchange rates, etc. It is not through the control of foreign trade or through the negotiation of commercial agreements, however helpful they may be, that the balance of trade is ultimately assured, but through the budgetary credit and exchange policy of the respective countries as affecting prices and the flow of trade.

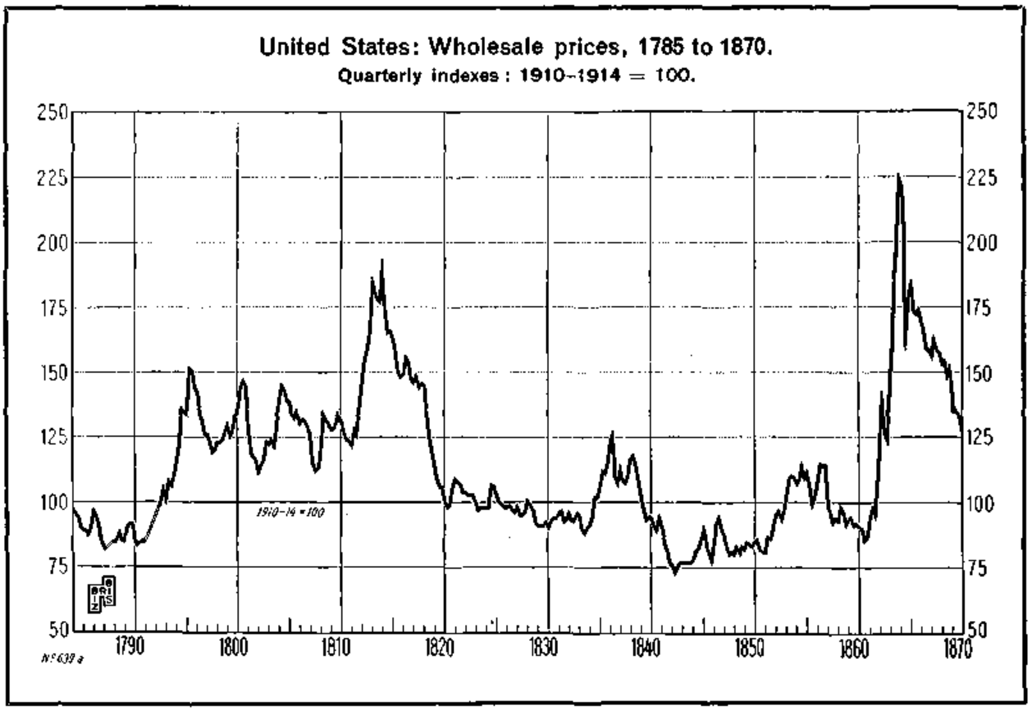
IV. Period of Price Adjustments.

One of the worst features of continuing inflation is (as we know well by now) that it destroys the mechanism of economic adjustment and is, therefore, the cause of many distortions. When any kind of enterprise — small or big, commercial or industrial — can, however badly managed, become a paying proposition, there is no elimination of mistaken ventures, no need for particular skill or efficiency, no special attention to the wishes and requirements of the customers and no striving for intimate knowledge of commodities and markets, since the rise in prices usually wipes out the consequences of any business error. Profits are often made without justification — that is part of the trouble in an inflation, although it is sometimes a question of profits which are large in appearance rather than in reality, the provision for depreciation charges being often unduly small for a period in which rising prices demand ever-increasing sums for the replacement of fixed and working capital. At the beginning of an inflationary period, issues of new purchasing power may, under certain circumstances, produce "forced savings" but, as the inflation proceeds, people become increasingly aware that saving in terms of the national currency (e.g. in the form of bank deposits or government bonds) exposes them to a loss of substance; and a more general awareness of this fact, in combination with easy profits easily spent, is likely to lead to a dissipation of resources.

Where an overdose of monetary purchasing power on the home market is ready to absorb almost all the current output, there is no inducement to export — a situation which can only result in a deficit in the balance of payments.

When the authorities at last manage to master the inflation and a period of price adjustment returns, the process will put an end to many unhealthy practices but it will not be painless. For the community it is, however, imperative that inefficient firms and black-market profiteers (many of whom posed as "business men") should disappear and that, for adequate profits to be made, it should once more be necessary to look to exports markets. Indeed, such a process of readjustment is obviously unavoidable if balance is ever to be restored. From a more human point of view, it must be added that an end to the rise in prices is required to restore the calm necessary for better work. Only then will husbands no longer hear tales of woe from harassed wives who, in times of rapidly rising prices, cannot possibly feed their families without using more and more cash for the daily household expenses. And when workers of all grades realise that they cannot simply step into another job round the corner they will give more attention to their current tasks.

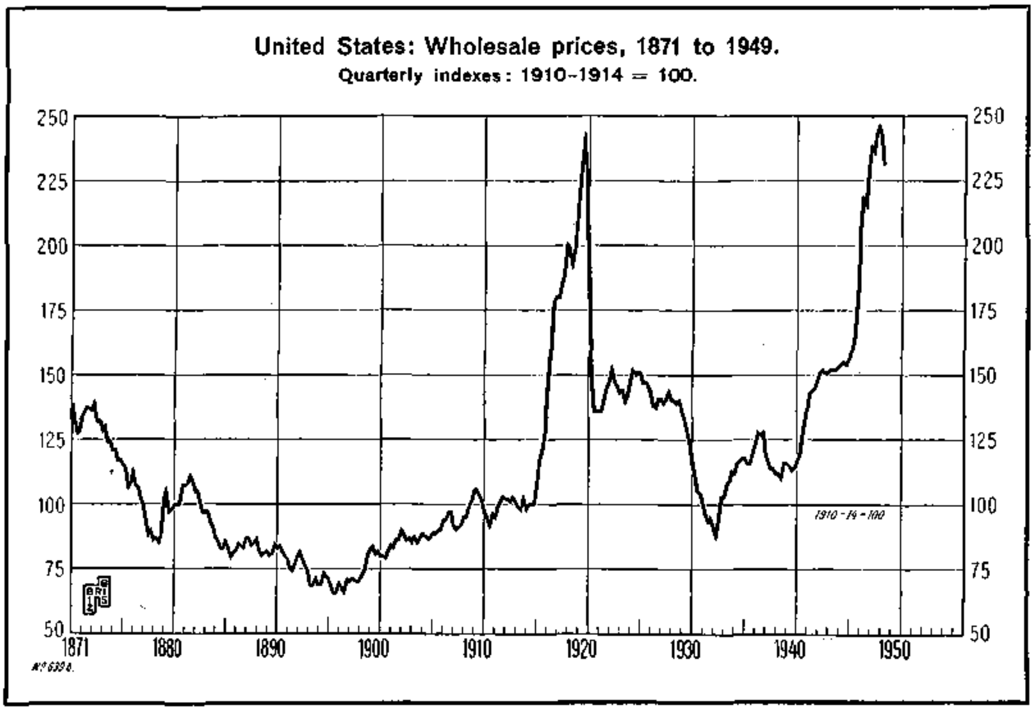
All this is well known from experience in recent years: quite apart from the injustice caused by inflation as between creditors and debtors — a matter of no little gravity in itself, since it tends to undermine the foundations of



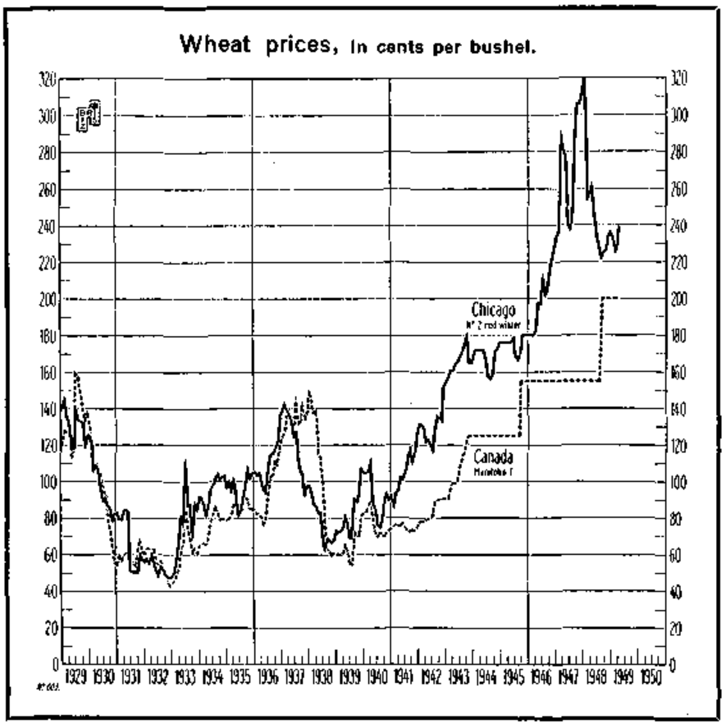
society — there are the direct economic losses and disturbances brought by continuing inflation. It is, therefore, satisfactory to find that over a large part of the world the signals are now no longer set for a continuous rise in prices.

It has already been shown in the second chapter of this Report that the price movements of the year 1948 and the early months of 1949 furnish every indication of a new phase in the world's price history in that the various countries are now at the end of the post-war inflation. In some instances they have already reached what it has become customary to call "disinflation" — a rather apt term, since it denotes a stage when a brake has been put on undue issues of monetary purchasing power, and increased supplies of goods and services can consequently make themselves felt. The process of curbing inflation has been far from uniform in every country and it is instructive to compare recent developments in some typical instances — as has been done in chapter II for Austria, Germany, Italy and France.

Important — one may even say decisive — as the steps taken in these individual countries have been in their fight against inflation, it would clearly not have been possible in 1948 to arrest the widespread rise in prices if it had not been for the downward turn in the United States. That country, which has 7 per cent. of the world's population, is responsible for more than 40 per cent. of the world's industrial output and is, therefore, the main purchaser of most raw materials as well as of a number of other important

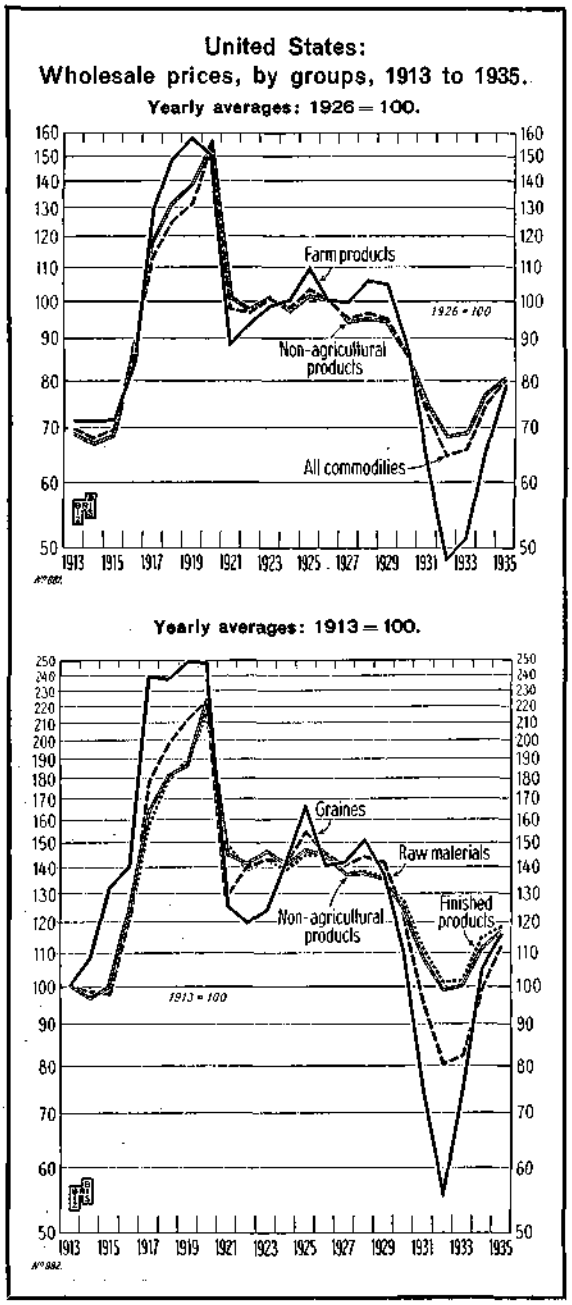


commodities. The result is that, in so far as it is possible to speak of "world prices", such prices are largely determined by the supply-and-demand position in the United States.



Wholesale prices in the United States reached their post-war peak in August 1948, when they stood 120 per cent. above the 1938–39 level. In February 1948 the price of wheat had come down from $3.20 per bushel to $2.20 but it had afterwards recovered to about $2.40 per bushel. The decline from the top figures did not affect the general level of the prices of "farm products" and "foods", which both reached their post-war high in the course of the summer of 1948. In August a fairly rapid decline set in, however, bringing the average price for farm products down by 14 per cent. in half a year.

Commodities other than "farm products" and "foods" did not reach their post-war high until the autumn of 1948, and the subsequent fall remained moderate up to April 1949, when the prices of these products were, on an average, about the same as a year earlier.



United States:
Wholesale prices, by groups, 1913 to 1935.

Since 1914 the price of grain has been subject to wide fluctuations; during the emergency period comprised by the 1914–18 war and its aftermath, when foodstuffs were all-important, the price of wheat rose above the average level of prices and in 1921–23, as well as in 1930–34, it fell more sharply than the average price level. The particular reason why the price of wheat drops heavily in periods of depression is not difficult to find: in such a period industry does not absorb any manpower from agriculture; those working on the land carry on, as a matter of fact, without curtailment of effort or output when prices are falling and little is earned, and even when losses are being incurred — sometimes it would even seem as if the people remaining on the farms put in more work during the depression. In industry, on the other hand, a disequilibrium between costs and prices soon leads to a distinct decline in activity, with increased unemployment and a consequent reduction in output. Thus, while the supply of manufactured goods is reduced, the supply of agricultural products will be kept up and will lead to a greater fall in the prices of such products than in those of manufactured goods.

It is interesting to find from the graphs that in 1929 the prices of wheat and other kinds of grain (and still more the average prices of farm products) were well sustained in comparison with the general price level. Animal products (in contrast to grains in general) were, as a matter of fact, among the commodities which in 1930 continued to stand up best against the general fall in prices during that year.

In discussions of special measures designed to maintain prices of farm products at a reasonable level the fact should not be lost sight of that it has been only in periods of deep depression that farmers have failed to secure a price equivalent to that of other producers (in relation to 1913 as basic year). That seems to teach a lesson for the future: it does not seem necessary for farmers to be much concerned about the prices their products will fetch in normal times. In all countries recent years have seen a greater percentage increase in the pay of farm workers than in that of other workers; and, with the increase in world population and the fact that there is no longer so much virgin soil to be exploited, there seems no reason to expect any particular disadvantages for those who work in agriculture, at least as long as severe depressions can be avoided.

Consequently, farmers have every reason to continue to be concerned about the maintenance of a fairly stable general price level and an absence of sharp economic fluctuations, and they will thus have an interest in the pursuit of such monetary and financial policy as may contribute to the attainment of that goal.

It would seem, however, as if, in deliberations about agricultural prices, the problem of general price stability had been relatively little touched upon, attention being devoted almost exclusively to the obtaining of immediate guarantees of sufficient sales and adequate prices for agricultural goods.

In the international field, after two abortive attempts in 1947 and 1948, a new wheat agreement (accepted by the representatives of 42 governments — in 5 exporting and 37 importing areas) is up for ratification before the end of June 1949. The price has been fixed at a maximum of $1.80 per bushel for the duration of the agreement; a minimum price of $1.50 is fixed for the 1949–50 season, the latter price to be reduced by 10 cents per year for

Wage increases from pre-war to 1948.*

Country	Agricultural workers	Industrial workers
	Indexes: pre-war = 100	
Denmark	350	200
Finland	1,300	1,130
France	1,070	580
Netherlands	270	180
Sweden	230	170
Switzerland	230	190
United Kingdom	260	190
United States	320	220

* Latest figures available.

Amount of wheat covered by the Wheat Agreement.

Exporting countries	In millions of bushels	Equivalent in millions of tons
Canada	203	5.53
United States	68	4.57
Australia	80	2.18
France	3	0.09
Uruguay	2	0.05
Total	456	12.42

the remainder of the agreement's lifetime, thus sinking to $1.20 per bushel in the fourth and final year. Provision is made for agreed wheat exports to the amount of 456.28 million bushels (= about 12½ million tons) to be delivered as follows by the exporting countries.

The Argentine and the U.S.S.R. withdrew from the negotiations, the latter country because it did not obtain a quota of 75 million bushels (about 2 million tons). According to an estimate in the "Corn Trade News", the import needs of the whole world may be estimated at about 720 million bushels* (not quite 20 million tons), this representing about 12 per cent. of the world's total wheat consumption. Assuming that the new wheat agreement will be duly ratified and come into operation, the volume of wheat trade outside the scope of the agreement would work out at 720–455 = 265 million bushels or about 7 million tons.

A most important change in the world supply of foodstuffs is the result of the increased production of wheat in the United States.

The impressive increase in the agricultural output in the United States above the pre-war level is attributable not merely to a surprisingly long run of favourable weather but also to a higher standard of technique (increased mechanisation, sowing of hybrid seeds with a heavier yield, and the use of more fertilisers); as the number of persons employed in agriculture has

World wheat production.

Production in	1935–39 average	1947	1948	1935–39 average	1947	1948
	in millions of bushels			equivalent in millions of tons		
United States	759	1,367	1,288	20.7	37.2	35.1
Canada	312	337	393	8.5	9.2	10.7
Australia	170	220	200	4.6	6.0	5.4
Argentina	222	245	170	6.0	6.7	4.6
Total for the "Big Four"	1,463	2,169	2,051	39.8	59.1	55.8
Total for Europe not including U.S.S.R.	1,593	1,020	1,465	43.4	27.8	39.9
Estimated world total including U.S.S.R.	6,010	5,790	6,415	163.6	157.6	174.6

Note: Wheat is, of course, the most important but it is not the only bread grain. In central and eastern Europe (mainly east of the Weser) as well as in northern Europe, rye is a good second and in some areas there is a larger consumption of rye bread than of any other kind. The world's wheat harvest in 1948 is estimated to have yielded about 6,400 million bushels (= 174 million tons), while rye came to about 1,700 million bushels (= 43 million tons). Thus the rye crop was equal to nearly a quarter of the wheat crop. While the figure for wheat includes estimates (of perhaps 1,000 million bushels) for China, etc., it should be noted that practically the whole of the "world" supply of rye is harvested in Europe and in the U.S.S.R., the rye crop for the combined area corresponding to more than one-half of its wheat crop.

* Of the 720 million bushels, 520 million are for Europe as a whole, including 200 million for the United Kingdom (whose quota under the new wheat agreement is put at 177 million bushels) and 120 million bushels for Germany.

actually declined, the increase in production since 1938 is due to a 60 per cent. increase in output per man and a 30 per cent. increase in the yield per acre.

In 1933, for the first time, the American farmers obtained price support through the Agricultural Adjustment Act and, in 1938, a more developed system with "parity prices" was introduced. Under that system the farmer has been assured of getting, for an average assortment of his products, the same stable amount of goods and services as he was able to buy with the income obtained from such an assortment in the years 1909–14. The price level for agricultural products has to be maintained at this parity (or just below it), since government agencies must be prepared to pay (on an average) 90 per cent. of the parity price in the form of loans, to give effect to the so-called "support prices" for the products concerned.

Spot and support prices for selected agricultural commodities (28th February 1949).

Commodity	Unit	Support price	Spot price
		in U.S. dollars	
Wheat	bushel	2.23	2.26
Corn	bushel	1.58	1.38
Oats	bushel	0.70*	0.79
Flax seed	bushel	6.00	6.00
Soya beans	bushel	2.18*	2.39
Hogs	cwt	16.75	22.25
Eggs	doz.	0.35	0.45
Butter	lb.	0.59	0.63
Cotton	cwt	30.87	32.56

* National average on farm — no market support price calculated.

Note: At the beginning of 1948 the prices paid for agricultural products were regularly well above the "support" prices, so that the parity calculation remained of merely theoretical interest. Through the price fall (by 13 per cent.) during 1948 the situation changed — but, as the commodities farmers buy also fell somewhat in price, the situation early in 1949 was simply that the discrepancy between market prices and support prices had become narrower. As will be seen from the above table, it is really only the price of corn which is well below the support-price level.

This "parity" legislation lapses at the end of 1949 and, as regards the support to be given from the beginning of 1950, the government has proposed the adoption of a new system, based on the guarantee of a "minimum income" to the farmer, who in case of falling prices would receive specially calculated "subsidies"; the consumers would get the benefit of a fall in prices but any difference which arose would have to be shouldered by the taxpayer as a charge in the budget.

Through such measures, the farmers are anxious to obtain a price guarantee for the future rather than any immediate benefits. Notwithstanding the decline in 1948, agricultural prices have on the whole kept up well — the price of wheat having recovered to $2.22 per bushel in the middle of May 1949, while other farm products have shown a decline over the year. It is the memory of the terrible price fall in the years 1929–33 that lends fuel to present fears, notwithstanding much current concern about a "world shortage of food" and the certainty that, in any case, increased food production will require a considerable economic effort.

* * *

It is not difficult to pick out, in the non-agricultural field, several important commodities the prices of which have even slightly risen over the year, e.g. coal, steel billets, iron, tin and quicksilver. But, even so, a predominant downward pull has been noticeable; and among industrial raw materials a sudden decline occurred in the spring of 1949, affecting, in particular, lead, zinc, copper, scrap iron, rubber, hides and crude oil. Production of metal ore and metals has risen side by side with a slackness of demand by commercial consumers and a forced inactivity, for lack of funds, on the part of the United States stockpile.* This has resulted in the accumulation of stocks in the hands of custom smelters, who are cutting their prices in the hope of reviving demand.

It is not yet possible to tell whether this downward movement is likely to be accentuated. But one result is clear: through this decline prices of raw materials and of manufactured goods have been brought nearer to each other. From a European point of view, this is a movement of great importance, since Europe is, by and large, an importer of raw materials and an exporter of manufactured products. The same "favourable" terms of trade for Europe as in the nineteen-thirties may well be out of the question, since the relatively low prices then paid for most raw materials reflected the low level of industrial activity, with 9 million unemployed in the United States at the time.

United Kingdom: Terms of trade.

Year	Average imports	values of U.K. exports	*Terms of trade*
	Indexes: 1938 = 100		
1913	97	68	142
1919	233	189	123
1920	277	245	113
1921	185	184	101
1922	148	136	109
1923	145	130	112
1924	150	129	116
1925	151	126	120
1926	138	118	116
1927	132	112	118
1928	133	111	120
1929	130	109	119
1930	114	104	110
1931	92	93	98
1932	86	87	98
1933	83	87	95
1934	86	88	98
1935	89	89	100
1936	93	91	103
1937	107	98	109
1938	100	100	100
1946	211	196	108
1947	258	222	116
1948	288	246	117

Note: The figures under the heading "Terms of trade" above show the changes in the volume of exports required to pay for a fixed volume of imports, i.e. a rise in the index indicates an adverse movement in the terms of trade. But, mainly owing to variations in the make-up of imports and exports and to uneven fluctuations in the prices of particular commodities, these figures can only give an approximate measure of the fluctuations in the terms of trade.

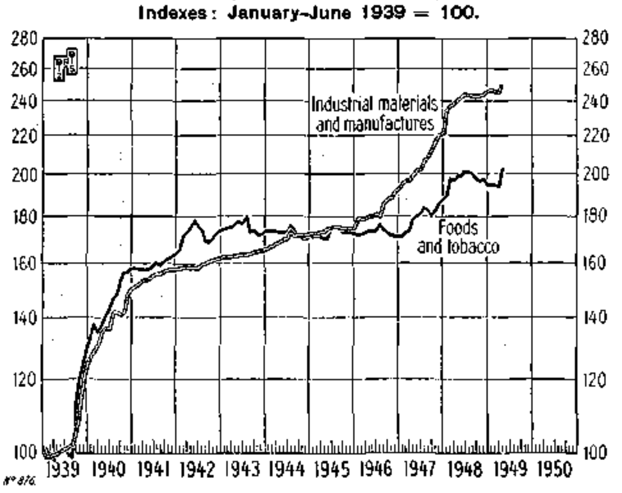
Neither in 1913 nor in 1928–29 were the terms of trade for the United Kingdom as favourable as in 1938 but in both the earlier periods the state of British industrial activity was a healthy one, with a current surplus in the balance of payments. When producers of primary products can no longer meet their costs, trade with many areas is bound to suffer. For the countries in Europe a loss resulting from relatively unfavourable terms of trade may quite possibly be compensated by the gain resulting from more active business all round.

* Under the "Strategic and Critical Materials Stockpiling Act of 1946" materials had actually been accumulated by the end of 1948 to the value of $821 million ($66 million being the residue of the pre-war stockpile, $584 million having been transferred from war surpluses and $171 million representing new materials acquired). It is reported that at the prices ruling early in 1949 the final goal of the United States stockpile would work out at something like $3,700 million.

It may, in fact, be only too easy to overrate the importance of shifts in the terms of trade since, in the production of many modern commodities (radios, automobiles, tools, machinery, watches, etc.), "value added in manufacture" is of far greater importance than the cost of the raw materials. When, with a rise in the standard of living, more and more of the national income is being spent on "services", the personal element is bound to be increasingly important. Human skill and training are again coming into their own, playing a greater rôle than the possession of natural resources. But, for the human element to have free play, it seems necessary that peace should reign, as has been the case in Switzerland — a prosperous country with a high average standard of living, although lacking all important raw materials. It is interesting to note that in April 1949 the index figure for import prices (1938 = 100) stood at 236 while the figure for export prices had reached 250 — a price constellation in Switzerland's favour.

An examination of the price indexes of a number of other European countries shows that export prices have, indeed, often risen more than import prices. In some instances, Finland being one (cf. page 85), the relation thus revealed signifies a genuine improvement in earning power vis-à-vis other countries. But that is not always the case. In France, an official enquiry has found that in the autumn of 1948 it was possible to get 19 per cent. more goods than in 1938 for the same volume of goods exported; but it should be remembered, on the one hand, that in 1938 French internal prices were exceptionally low at the rates of exchange prevailing at the time and, on the other hand, that in the autumn of 1948 many French prices were rather too high at the rates of exchange then in force. The "favourable" terms of trade in the winter of 1948–49 were, therefore, purchased at the cost of an overvaluation of the currency at the official exchange rates and too small a volume of exports — being thus a source of weakness rather than of strength.

United Kingdom: Wholesale prices.
Indexes: January-June 1939 = 100.



For many countries in Europe the ups and downs of world-market prices have made themselves felt with a considerable time-lag. Thus in the United Kingdom the effect of the post-war rise in prices was delayed for some years by the institution of official "bulk buying" (or sometimes only "centralised buying") of many foodstuffs and raw materials, and the same practices seem also to have

Price movements in Europe.

Percentage price increase (+) or decrease (—).

Countries	1945	1946	1947	1948	Dec. 1948 Index: Pre-war = 100
Austria					
Wholesale prices	—	—	—	+ 20	357
Cost of living	—	+ 44 (1)	+ 148	+ 22	370
Belgium					
Wholesale prices	—	—	+ 12	+ 5	384
Cost of living	—	—	+ 9	+ 9	383
Czechoslovakia					
Wholesale prices	+ 36	+ 49	+ 2	+ 6	317
Cost of living	+ 29	+ 48	— 7	+ 2	294
Denmark					
Wholesale prices	— 7	+ 9	+ 9	+ 9	239
Cost of living	0	+ 1	+ 3	+ 3	169
Finland					
Wholesale prices	+ 93	+ 19	+ 39	+ 9	960
Cost of living	+ 99	+ 16	+ 54	+ 11	805
France					
Wholesale prices	+ 71	+ 80	+ 44	+ 62	1,917
Cost of living	+ 62	+ 74	+ 57	+ 42	1,802
Greece					
Cost of living	+ 1,781 (2)	+ 96	+ 49	+ 23	27,075
Hungary					
Wholesale prices	—	—	+ 18 (3)	— 3	642
Cost of living	—	—	+ 19	— 9	455
Iceland					
Cost of living	+ 4	+ 7	+ 7	— 1	326
Ireland					
Wholesale prices	0	+ 2	+ 11	+ 3	229
Cost of living	+ 1	— 2	+ 5	+ 2	184
Italy					
Wholesale prices	—	+ 38 (3)	+ 50	+ 3	5,697
Cost of living	—	+ 23 (3)	+ 44	0	4,917
Netherlands					
Wholesale prices	+ 31	+ 23	+ 5	+ 4	267
Cost of living	+ 15 (4)	+ 11	+ 3	+ 6	214
Norway					
Wholesale prices	— 6	+ 4	+ 3	+ 2	186
Cost of living	+ 2	+ 3	— 2	0	157
Poland					
Cost of living	— 18 (5)	+ 46	— 2	— 2	13,000
Portugal					
Wholesale prices	— 3	— 5	+ 4	+ 7	256
Cost of living	+ 10	+ 6	— 1	+ 3	215
Spain					
Wholesale prices	+ 13	+ 23	+ 12	+ 5	324
Cost of living	+ 18	+ 36	+ 10	+ 4	303
Sweden					
Wholesale prices	— 3	+ 1	+ 7	+ 6	199
Cost of living	0	+ 2	+ 7	0	156
Switzerland					
Wholesale prices	— 3	+ 2	+ 6	— 0.5	219
Cost of living	— 0.5	+ 2	+ 5	+ 0.6	164
Turkey					
Wholesale prices	+ 1	— 2	+ 3	+ 6	469
Cost of living	+ 3	— 3	— 1	+ 5	352
United Kingdom					
Wholesale prices	+ 1	+ 6	+ 13	+ 9	225
Cost of living	+ 1	+ 0.5	+ 3	+ 5	142

(1) Compared with April 1945
(2) „ „ November 1944
(3) Compared with January 1946
(4) „ „ July 1944
(5) Compared with March 1945

somewhat delayed the moment when the full downward turn in world prices, which began in 1948, would make itself felt in the British economy. Thus the prices of imported raw materials reached their highest index figure in March 1949, when they stood 27 per cent. above the 1947 level (this representing an index figure of 358 with 1938 = 100, while export prices, on the same basis, were at an index figure of only 249).

The variety of the price movements in the different European countries has been so great that any classification under precise headings becomes somewhat artificial, but it is helpful to review the countries with reference to the degree of the price rise:

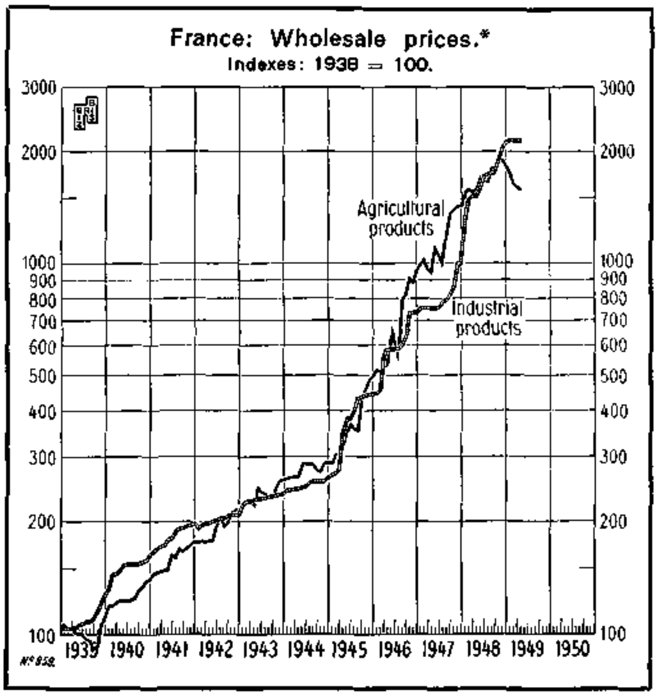
1. In Hungary and Greece prices in 1945–46 rose to such a pitch that the national currency lost all value: a new basis was established and on that basis prices in Hungary have risen about six times but in Greece as much as 260–290 times. In Hungary the price rise seems to have received a check in 1948, to judge from the cost-of-living index.

2. In Poland the point reached by prices is at 130–140 times the pre-war level, with a distinct tendency to stabilisation in 1948. No statistics are available for Roumania but there the rise would seem to have been more pronounced than in Poland.

3. In Italy the price level in 1948 had reached about 55 times the pre-war level — but showed a distinct decline in the late autumn (the fall in prices affecting the cost of living also). Rationing having been abolished and black markets having no longer a raison d'être, it may now be said that the official price index adequately reflects the real price movement.

4. In France prices registered their maximum at nearly 20 times the pre-war level. This point was reached in November 1948, but between then and April 1949 agricultural prices fell by some 17 per cent. while industrial prices increased by 3 per cent. With the gradual disappearance of black markets (more and more commodities being decontrolled), the official index may be said to give a reliable picture of the real price movements.

5. Prices in Finland rose sharply up to the end of 1947 but since then it has been possible to moderate the rise and



* Logarithmic scale.

a decline set in during the winter of 1948–49, when wholesale prices were 9 to 10 times as high as pre-war.

6. In Austria prices rose again about 20 per cent. in 1948 (cf. page 51) to a level about three and a half times as high as in 1938. Some difficulties were experienced in the spring of 1949 in mastering the price movements, although the supply of goods had greatly improved. Less stress was being laid on a direct control of prices and more on the taking of financial measures (increased taxation, credit restriction, etc.) designed to check the expansion of monetary purchasing power.

7. In Belgium and Turkey prices have risen by about four times the pre-war level. The rise continued in 1948 but in Belgium a downward turn set in during the first quarter of 1949. In that country wages would seem to have risen as much as the cost of living and, since most direct controls were abandoned in 1945, the consumer was, at an early stage, free to arrange his purchases according to his preferences — an advantage which, as a rule, was not enjoyed in other countries in Europe before 1948. Although highly industrialised, Belgium used to be a "cheap-wage" country; it is true that the Belgian franc was devalued by 34 per cent. after the Liberation, but, even so, it is in Belgium that wages seem to have risen more in terms of dollars (or gold, which comes to the same thing) than anywhere else. For such a position to be tenable in an economy so dependent on exports, it is necessary that industrial and other enterprises should have the capital and other prerequisites for carrying through effective measures of rationalisation without delay.

Increase in wages from 1937 to 1948.

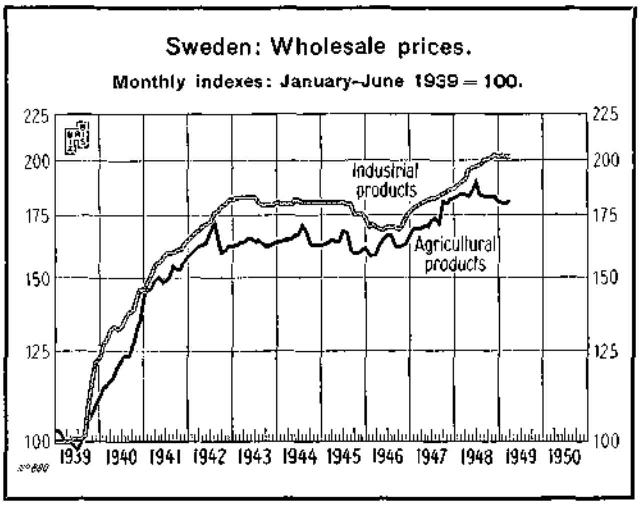
Countries	Money wages in national currency	Money wages converted into dollars
	Indexes: 1937 = 100	
Belgium	420	284
Czechoslovakia	259	148
France	1,140	131
Italy	5,280	175
Netherlands	182	125
Sweden	197	215
Switzerland	187	187
United Kingdom	183	149
United States	213	213

8. In the Netherlands, where prices have risen by about three times, the amount paid as subsidies from the budget was reduced in November 1948 by approximately Fl. 330 million from the level of about Fl. 570 million reached under the system up to then in force. Of the amount by which the subsidies were reduced, about Fl. 70 million reflected a reduction in import prices; Fl. 90 million was saved on fuel (coal and oil), and Fl. 240 million on foodstuffs. To compensate for the consequent rise in the cost of living, all employed persons more than 23 years old and with a yearly income not exceeding Fl. 3,700 were to receive one guilder more per week (there being also an increase in the allowances for children). Industry and trade agreed to shoulder the cost of the higher pay without making any increase in the prices asked for their own products. One reason why such a course was possible seems to have been that the wage increase was kept within limits set by what can be regarded as the normal increase in efficiency and output per worker.

9. As regards Portugal, Ireland, Switzerland and Sweden, which were neutral in the war, wholesale prices have about doubled in Sweden (this being the lowest price rise within the group) and have gone up one and a half times in Portugal (where the rise has been highest). Sweden has also the lowest increase in the cost of living (with an index figure of 156), the appreciation of the Swedish crown by 16.6 per cent. in 1946 having helped

to moderate the rise in prices, although causing difficulties in other ways.

10. Among the countries involved in the war, the lowest price rise is found in Norway, Denmark and the United Kingdom. The two first-mentioned countries introduced monetary reforms after the war; in all three, budgetary inflation has been avoided and comparatively strict price control was enforced while shortages still remained.



* * *

The flattening-out of the price curves in most European countries has gone hand in hand with a marked relaxation of controls.* In the United Kingdom, for instance, rationing of potatoes, bread and preserves was discontinued during 1948 and confectionery in May 1949, the one outstanding difficulty as regards foodstuffs being the strict rationing of meat. On the other hand, footwear and clothing were progressively released during the summer and winter of 1948 and taken completely off the ration in March 1949. In the Netherlands also progress was made in 1948, footwear, milk, furniture, bread, flour and petrol being among the articles no longer rationed. In Belgium food rationing was largely discontinued in 1947 and finally abolished at the beginning of 1949; in Switzerland it had already been completely abolished in 1948, while in France and Italy practically all restrictions pertaining to food have now been lifted. And in the Bizone in Germany, the currency reform was accompanied by far-reaching decontrol, restrictions being retained only as regards certain foodstuffs and fuel and as regards clothing and footwear in the retail trade.

The return to a more or less normal supply position with freedom from rationing brings, in itself, an improvement in real income, since the individual householder is again able to lay out his money as suits his own particular needs and preferences; and the very fact that the black markets, with their high prices, have disappeared is also of importance. Account of such improvements has to be taken in comparing the trend of real wages in different countries. But in such a comparison account has further to be taken of the increasingly important benefits received and contributions levied under social-security régimes, since in many cases the operation of these régimes means a substantial increase for wage-earners (in France, for instance, an addition

* Information regarding the relaxation of control in different countries has been largely obtained from the Secretariat of the O.E.E.C. in Paris.

of about 25 per cent. to the average money wage received). The systems by which social benefits are provided and their cost met vary considerably, however, from country to country: in France, the greater part of the cost is covered by direct contributions from employers and employed, paid in relation to current wages, and those contributions would seem to enter into the cost of production. In some other countries, including the United Kingdom, the greater part of the social-security outlay is a charge on the budget, and the incidence of the cost is then more difficult to determine.

Most countries in Europe have not as yet seen their way to restore freedom as regards the *movement of wages*. In some countries, such as France, Denmark, Belgium and Norway, direct control has been maintained, while in others — the United Kingdom, Switzerland, Sweden and Austria — reliance has been placed mainly on voluntary agreements, between governments and the representatives of workers and employers, to limit wage increases. In this field, there seem to be two — partly contradictory — tendencies, connected with the abolition of control over the sale of goods and the consequent reappearance of competition (intensified by the return of the buyers' markets): on the one hand, the fear of rising costs makes for a greater resistance to wage increases; on the other hand, the need to adjust production more closely to variations in demand calls for a greater flexibility all round, including the field of wages. As long as imports are kept down and price rises therefore escape the moderating influence of foreign competition, it can hardly be possible to abolish all price and wage control. For this and other reasons, many governments are finding it difficult at the moment to adopt any clear line of policy, but there seems little doubt that the trend will be towards greater freedom and flexibility.

The removal of rationing and the lifting of other controls have the effect of restoring a freer market at home, with the volume of sales depending on effective demand, for which producers and traders will compete. Once that is the case, output in excess of what the home market absorbs has to seek an outlet through sales abroad (cf. page 100). In that way, balance is restored between sales on the home market and sales abroad. It is difficult to see in what other way trade can be established on healthy foundations.

Producers and traders who have to contend with competition on their own domestic market will be steeled to endure the still harder test of competition on foreign markets. For the various countries in Europe, *freedom of trade*, acting as a check to excessive prices and as a spur to rationalisation, *constitutes a wholesome corrective to economic rigidity*.

It has been one of the dangers of the post-war situation that through bilateral arrangements and various forms of protection within areas with special affiliations (the advantages being not infrequently of a monetary character), it has often been possible to sell goods at higher prices than they would fetch in markets where competition is freer. It has even happened that in some countries two prices have been quoted for the same product: one for customers whose choice of markets is limited (e.g. customers who cannot procure the whole range of foreign currencies against their own money); and another price when it becomes necessary to compete on world markets. If such differences are long-lived and numerous the result will soon be equivalent to a currency depreciation. And, in the meantime, trade will take a lopsided course; exports will most likely be diverted from the dollar markets for sale under softer conditions.

Countries which have been under the direct strain of a terrible war may not exactly rejoice in the necessity of encountering all-round competition. For them the years of sellers' markets have afforded a period of respite, with relatively easy sales whenever goods were available; but, when it is a question of restoring the economic and financial position, with equilibrium in the balance of payments and independence of extraordinary financial assistance from abroad, there is no choice but to become capable of selling in competition with producers and traders of other countries. For the authorities in each country the task will then be one of establishing, through suitable commercial and monetary policy, those general conditions (as regards tariffs, exchange rates, etc.) which will enable the producers and exporters of that country to face the inevitable competition without having to labour under any particular handicaps.

V. Foreign Exchange Rates.

After the first world war, it took more than five years before any European currency was formally "stabilised", which at that time meant linked to gold again at the par rate. Before stabilisation took place, the various currencies were subject to sometimes rather wild, sometimes quite moderate, fluctuations; but for each currency there was not more than one rate quoted (apart from a slight spread between buying and selling rates) and the various currencies could be bought and sold freely for all purposes at the rates thus quoted in the respective exchange markets. In order to steady quotations, central banks (and sometimes governments also) had at times to support their currencies by entering the market as purchasers or had to buy up any offer of foreign currencies which might threaten to raise the value of the national currency more than was desired, those being the early days of the gold exchange standard. Furthermore, there was always the possibility of obtaining gold via sterling (gold being dealt in freely on the London market) or via the dollar, which remained convertible into gold, as it had been before the entry of the United States into the war.

Since the second world war, the exchange system has been of a different kind. "Par rates" have been fixed for most currencies and at those rates current commercial and other transactions have to be settled, the settlements taking place largely through clearing and other bilateral accounts without any specific transactions in the open exchange markets. Not only capital transfers but current operations, whether commercial or financial, are, in most countries, dependent upon an "allotment of foreign exchange" by the official Control. This being so, there are normally no fluctuations in the official rates. Any alterations (beyond such minor modifications of a fractional nature as the authorities may decide upon from time to time) are, under the new system, made on the basis of official decisions applicable from certain definite dates (as was the case in July 1946 when the Canadian dollar was appreciated by 10 per cent. and the Swedish crown by 16.6 per cent.). Thus, the official par rates are in no immediate way dependent upon quotations in actual exchange markets; that being the case, any foreign currencies required in excess of what the control authorities obtain from exporters, etc. must be supplied from monetary reserves or from the proceeds of foreign loans or grants.

The fact that some dealings not within the official range of transactions actually take place accounts for the existence of other quotations, dependent upon the supply and demand in the particular market in which the dealings are carried out. There is a great variety of such outside markets, some being entirely legal, others rather in the nature of black markets even though they may be officially more or less "tolerated". At the moment there is not one currency in the world which has only a single quotation. Even for the relations between the dollar and the Swiss franc — two of the strongest currencies nowadays — quotations different from the official "par" apply to certain transfers, especially of a financial character. A great diversity of rates has come into being: particular rates for notes — and sometimes different rates for different denominations; official rates which are not the same for imports as for exports, and so on. A whole new vocabulary has been formed, rates being variously described as official, free, black-market, parallel, or grey, or classified as security rates, compensation rates, etc. There are rigidly fixed rates — in or out of touch with reality — fluctuating rates, orderly or disorderly cross rates, multiple rates, tourist rates, etc. There are countries which, though members of the International Monetary Fund, have not yet had "par rates" established — Austria, China, Finland, Greece, Italy, Poland, Uruguay and Indonesia — while no clear agreement has so far been reached between France and the Fund as regards the present French franc régime.

To some extent the situation in France and Italy differs from the general picture, though in their case also it is true that the official rates are not established through the interplay of supply and demand in markets where currencies can be bought and sold irrespective of the purpose of the transaction. It would, indeed, be difficult — not to say impossible — for those two countries to contract out of the general system of payments agreements, etc. as applied in Europe. In France, for instance, the "official free rate" quoted is not a rate at which anybody whatsoever can sell francs and buy other currencies but a rate which, in contrast to the "par rate", can be altered from day to day by the Control, thus possessing an element of flexibility that other official rates lack; through such alterations it may be possible to maintain contact with freely quoted rates, e.g. the quotations in Switzerland and New York of French bank-notes.

The exchange system introduced in France after 26th January 1948, i.e. after the franc had been devalued for the third time since the war, was described in the eighteenth Annual Report (page 91). As the system was developed in the spring of that year, "free rates", applicable mainly to tourist expenditure and financial transactions, were quoted for three currencies (the U. S. dollar, the Swiss franc and the escudo). The free rates were kept around Fr.fcs 305 = \$1 (with equivalent quotations for the other two currencies). Commercial transactions were settled at the mean rate which, being the middle rate between the free and the official rates of Fr.fcs 214.39 = \$1, worked out at about Fr.fcs 260 = \$1. For all other currencies than the three mentioned, rates applicable to commercial and financial transactions, tourist expenditure, etc. were calculated on the basis of the official rate: Fr.fcs 214.39 = \$1 (the rate of the pound sterling, for instance, being fixed at Fr.fcs 864 = £1, which, for commercial transactions, made the cross rate between the pound and the dollar equal to about £1 = \$3.30).

As domestic prices rose in the course of 1948, France had a growing trade deficit with the sterling area and for this and some other reasons the decision was taken to effect the so-called "alignment of the exchanges", which took place on 17th October 1948. The purpose was to equate the cross rates for all currencies (other than the dollar, the Swiss franc and the escudo) to the mean rate of the dollar (at the time still about Fr.fcs 260 = \$1), which meant, for instance, that the sterling-dollar cross rate for commercial transactions would be £1 = \$4.03 again. For all currencies except the three quoted on the free market, official rates are fixed at the end of each month on the basis of the mean rate of the dollar multiplied by the dollar parity of the currency in question.

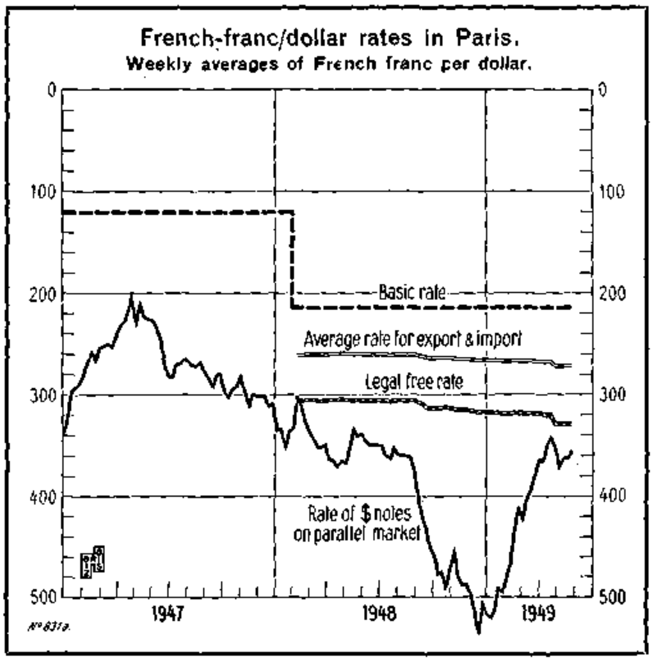
Furthermore, it was decided that payments for *all imports and exports* were to be settled at the mean rate, which meant that preferential treatment previously granted to certain "essential imports" was abolished. As regards freight and insurance, the mean rate was to replace the free rate, which remained applicable to financial transactions and to tourist expenditure.

Prices paid for gold and dollars in Paris and price in French francs of one dollar on the Swiss and American markets.

Date	Price in French francs in Paris of			Price in French francs of one dollar on the bank-note market in Zurich and New York
	one napoleon	one dollar on the official free market	one dollar on the parallel market	
	in French francs			
1947 April	2,736	119.10*	220	214
October	3,834	119.10*	296	308
December	3,584	119.1C*	307	311
1948 January	3,853	119.10*	338	339
February	3,999	306.52	312	337
March	4,181	305.65	345	358
April	4,123	305.10	366	364
May	3,939	305.60	346	348
June	4,019	305.97	350	349
July	4,367	306.23	360	354
August	4,379	305.95	365	372
September	5,388	311.02	427	430
October	5,983	313.09	475	465
November	5,745	314.57	475	471
December	5,898	317.00	512	497
1949 January	5,918	318.29	503	491
February	5,388	318.61	449	437
March	4,646	318.76	394	386
April	4,240	322.14	352	347
May	4,283	329.04	363	359
June 1st	4,180	329.40	351	353

* Official rate before the establishment of the *official free* market.

In the spring of 1948 the free rate was within 10 per cent. of the rates quoted for French bank-notes in the United States and Switzerland and on the so-called parallel or black markets in Paris, and experience has shown that, when the margin is no greater, tourists and others may generally be expected to sell their notes and travellers' cheques to the Control. But in the autumn and winter of 1948–49 the gap between the free rate and the quotations for the French franc on the foreign markets became much wider (at one time corresponding to more than 60 per cent. of the official free rate) and tourists and others then ceased to convert their currencies through the agencies of the official Control. It was obviously in the interest of the authorities to reduce the gap, and they did so both by allowing the official free rate to rise and by trying to improve the quotation of the French franc on the foreign markets. Thus, the amount of French bank-notes which a foreigner (or a Frenchman permanently resident abroad) could bring into France each month was raised from Fr.fcs 4,000 to Fr.fcs 10,000 at first, then to Fr.fcs 20,000 and then again to Fr.fcs 40,000, which considerably increased the demand for French notes in Switzerland. Meanwhile the official free rate had been going up: within a few weeks the increase in the quotation amounted to some 5 per cent., a quotation of Fr.fcs 329.80 = $1 being reached on 26th April 1949.



Thus, after having reached Fr.fcs 500–550 to the dollar at the end of 1948 and in January 1949, the dollar/French-franc rate resulting from quotations of notes in Switzerland and in the United States (and roughly corresponding to the "parallel" rates quoted in Paris) was reduced to less than Fr.fcs 400 in March and, after a further fall to 335 in the middle of April, it has remained more or less stable at Fr.fcs 350 to 370 since then. The disparity of about 10 per cent. still found between this rate and the official free rate (now about Fr.fcs 329) is essentially due to the fact that there are still a lot of imports and current transactions which, being refused import licences and foreign exchange allocations, are paid for via the "parallel" market; thus the closing of the gap between the rates on the "parallel" market and the official free rates can only proceed pari passu with the extension of the range of current transactions for which licences are granted.

Nevertheless, the improvement in the quotation of the French franc on foreign markets has had this important consequence:

(a) for sterling and all the controlled currencies purchased by the authorities at the mean rate, the free or "parallel" rate is, at most, equal to the official rate, if not below it;

(b) for the dollar, the Swiss franc and the Belgian franc, the premium which they still enjoy has been compressed, in relation to the official free rate (or, in the case of the Belgian franc, the travellers'-cheque rate), within a margin of about 10 per cent., which means that for a number of transactions the black market is no longer a paying proposition.

If this rate structure persists (and, even more, if there is a further improvement) there should be a prompt normalisation of the intake of foreign currencies through the official circuit.

In Italy, where the foreign exchange value of the currency was adjusted in the autumn of 1947 and early in 1948, the official rate for the dollar has been kept practically stable since May at Lit. 575 = $1, while the rate for the Swiss franc has varied between Lit. 140 and 145 = Sw.fc 1 (fluctuating in sympathy with the quotations for "financial dollars" in Switzerland).

Italy: Quotation of some currencies.

Monthly averages	Official price in lire of			Parallel-market price in lire of		
	one dollar	one Swiss franc	one £ sterling	one dollar	one Swiss franc	one £ sterling
1948 January	576	141	1,637	592	141	1,425
February	573	135	1,756	612	148	1,501
March	573	137	1,838	663	161	1,533
April	574	139	1,840	618	151	1,484
May	575	140	1,851	587	146	1,572
June	575	142	1,947	582	146	1,619
July	575	143	1,963	583	148	1,648
August	575	144	1,936	582	148	1,640
September	575	145	1,937	615	159	1,666
October	575	145	1,944	656	167	1,726
November	575	145	2,038	642	164	1,813
December	575	144	2,317*	656	164	1,937
1949 January	575	141	2,317	672	171	1,993
February	575	141	2,317	689	175	2,036
March	575	141	2,317	670	170	2,073
April	575	141	2,317	633	161	2,027
May	575	141	2,317	632	162	1,970

* Since 28th November 1948 the £ sterling has been pegged to the dollar.

Italy, since the currency reform of November 1947, has been able to limit the disparity between the official free rate of the dollar and the rate for the lira on foreign markets (to which the quotation for the dollar on the "parallel" market in Italy more or less corresponds) to about 10 per cent. The rate for the lira on the Swiss market, after a slight decline in 1948 from Sw.fcs 0.70 to 0.60 for Lit. 100, has remained steady at a little over Sw.fcs 0.60 since the beginning of 1949.

The main alteration in the Italian exchange system during the year occurred as a consequence of the agreement entered into with the United Kingdom in November 1948, by which the fixed cross rate of $4.03 = £1 was adopted (bringing the rate to £1 = Lit. 2,317.25) and Italy returned to the group of countries holding transferable accounts within the British exchange system. The balance of trade being already in Italy's favour, the alteration had the effect of increasing the accumulation of sterling by the Italian Exchange Control, which has also increased its holdings of dollars since the beginning of 1948 (see page 80).

On the other hand, the same consideration for the system of cross rates was not shown when in April 1949 the Italian-French rate was altered from Lit. 220 = Fr.fcs 100 (corresponding to the ratio between the official dollar rate in Italy — $1 = Lit. 575 — and the current mean rate for the dollar in France — about Fr.fcs 260 = $1) to Lit. 180 = Fr.fcs 100 (corresponding to the ratio between the above-mentioned official rate and the "free rate" of about Fr.fcs 320 = $1 in France), the alteration being justified as the only means of balancing the foreign trade relations between Italy and France.

Special mention may also be made of the exchange situation in Belgium, which is the only European country that has effected a considerable reduction in the disparity between the official rate and the free rate for its currency without changing the official rate (fixed after the Liberation), since the reduction was brought about exclusively by an improvement in the quotations of the Belgian franc on free foreign markets.

The quotation for Belgian notes in Switzerland, which stood at about Sw.fcs 6 to B.fcs 100 at the beginning of 1947, rose to about Sw.fcs 8 at the beginning of 1948 and then declined slightly to about Sw.fcs 7.50 at the end of the year, only to rise to Sw.fcs 8.50–8.68 in April and May 1949 (the parity with the free rate for the dollar as quoted in Switzerland being Sw.fcs 8.90).

This result was obtained thanks to a number of measures which were put into effect by the Belgian authorities. As regards current operations there has for some time been no difficulty in procuring the necessary allotments of foreign exchange (many imports even benefit by the system of "a simple declaration is equivalent to a licence"). Moreover, permission was given in 1948 for Belgian notes purchased abroad to be repatriated without limitation by tourists and for investments. In March 1949 the permission was extended, in that notes sent by foreign banks to Belgian banks could be credited to accounts utilisable for various specified payments, including payment for goods exported from Belgium. In that way the rates quoted for Belgian notes outside the country have now become closely linked with the official rate, since any appreciable divergence from, for instance, the official dollar rate would make it advantageous to buy notes for the settlement of commercial transactions. In May 1949 the Belgian franc note rate in the United States was, as a matter of fact, close to the official rate for bank transfers (B. fcs 100 = about $2.22 being quoted for notes as compared with $2.28 for transfers).

Spain had not changed its official parity since 1941 but only introduced, in August 1946, a preferential tourist rate equal to Pesetas 16.40 = $1 instead of the usual official buying rate of Pesetas 10.95 = $1. In order to compensate for an actual "overvaluation" of the peseta at the official rate, the export of a number of products was subsidised and a surtax imposed on imported goods, varying between 30 and 70 per cent. of the c.i.f. value of the goods in question.

In December 1948, however, a rather radical change was made by the introduction of a whole set of new rates, forming a "multiple-rate" system somewhat similar to those existing in many Latin American republics.

While the old official selling rate of Pesetas 11.22 = $1 remains in force for the import of goods not specially listed (in general, "essential" goods), all other goods (i.e. goods not considered essential) have been classified in different categories, to which other selling rates apply, varying from Pesetas 13.14 to 27.375 = $1. A differentiation has also been made with regard to buying rates. For goods not specially listed the old official rate of Pesetas 10.95 = $1 remains in force, while a scale of rates varying from Pesetas 12.59 to 21.90 = $1 applies to the proceeds of different categories of export goods. And in January 1949 the preferential tourist rate was increased to Pesetas 25 = $1. It is obvious that, in future, the average rate for the peseta can be altered by transferring goods from one category to another in the import and export classifications.

No change in the external value of its currency was announced by any country in eastern Europe during 1948 or the early months of 1949.

The currency reforms which were introduced in the two parts of Germany in the summer of 1948, and have been described on pages 43 and 124, affected the rates of exchange of the mark. At the outbreak of war in 1939, the official rate was RM 2.49 = $1. At the beginning of the occupation, in 1945, the Allies fixed a rate of RM 10 = $1; but this rate was chiefly used for dealings with the occupation authorities and not as a means of price-fixing in foreign trade, since the Joint Export-Import Agency (JEIA) bought imported goods at world prices and generally sold them at lower prices in Germany, while it paid German exporters the relatively low domestic prices, selling the goods abroad at world prices.

In May 1948, a rate of DM 3.33 = $1 was fixed for Reichsmark payments relating to imports and exports, and after the monetary reform in June this rate was applied to the new "Deutsche Mark" — which meant a devaluation of 25 per cent. as compared with the pre-war rate of the Reichsmark. With the lifting of price control over almost all industrial products, there was a price rise in Germany which at one time seemed to threaten the country's export possibilities. As a transitional measure, exporters received a kind of premium (conversion factor) from various counterpart funds, which temporarily brought the rate for the export of finished articles to about DM 4 = $1; but this practice is being gradually discontinued and will presumably cease to operate in the middle of 1949.

German wages do not appear high in comparison with those in other countries but then efficiency is, for many reasons, relatively low (enterprises working for civilian purposes having for many years had little chance to rationalise their processes). The gradual liquidation of the system of export premiums has not prevented a steady increase in German exports, these being stimulated by the disappearance of all inflationary tendencies on the home market.

The difficulties caused by the practice of stipulating for settlement in dollars for German exports of some "essentials" (coal, coke, potash, etc.) to European countries have been to some extent lessened by the participation of the Bizone and the French zone in the intra-European payments scheme. There is no doubt that in 1948 settlements in sterling were on the up grade in Europe, one reason being the increase in exports from the sterling area.

In current parlance the term "sterling area" is still used, but the official designation of the area within which, broadly speaking, transfers are freely permitted is "Scheduled Territories" as defined by the Exchange Control Act which came into operation in the United Kingdom on 1st October 1947. In the eighteenth Annual Report (pages 95–97 and 149–151) an outline was given of the British exchange-control system, under which countries having trading and financial relations with the United Kingdom could be classified in five groups, mainly according to the degree of transferability of sterling. In the "Midland Bank Review" for February 1949 the following account has been given of the relations between the different groups (here reproduced by kind permission of the Midland Bank).

During 1948 two South American republics — Chile and Peru — left "American Account Countries", the former joining "Transferable Account Countries" and the latter "Bilateral Countries". In the same year the Argentine and Brazil moved from "Transferable Account Countries" to "Bilateral Countries", while Italy (as a result of the Anglo-Italian Agreement of November 1948) moved in the opposite direction. "Bilateral Countries" now also include Tangier, Syria and Germany, the Bizone as well as the French and the eastern zones.

Sterling balances accruing to a country thus assume a different degree of transferability according to the group to which that country belongs. Since it is possible for merchants in a country belonging, say, to the bilateral-account group to buy goods in the sterling area and resell them (with or without some minor transformations) to, say, a customer in a country belonging to the dollar area, arrangements may be made between individual merchants for roundabout exchange transactions combined with movements of goods. Since sterling of the bilateral-account type may only be used for direct purchases of sterling-area goods, its quotation in this particular kind of "market" between individual merchants varies according to the state of the balance on current accounts of each of the bilateral countries in relation to the sterling area and also according to the availability of dollars within each of the said countries.

The existence of such quotations in fact gives rise to arbitrage dealings, in connection with trading in commodities. One example of such trading is cited in the report of the National Bank of Egypt dated March 1949:

UNITED KINGDOM EXCHANGE CONTROL REGULATIONS
OUTLINE OF PERMISSIBLE TRANSFERS, JANUARY 1949

→ The arrow indicates direction of transfers, permitted without the necessity of individual approval by the U.K. Control, between different categories of sterling accounts. All other transfers require separate approval.

AMERICAN ACCOUNT COUNTRIES

Inter-transfers permitted.

Bolivia
Colombia
Costa Rica
Cuba
Dominican Republic
Ecuador
Guatemala
Haiti
Honduras
Mexico
Nicaragua
Panama
Philippine Islands
Salvador
U.S.A. and its Dependencies
Venezuela

TRANSFERABLE ACCOUNT COUNTRIES

Inter-transfers permitted, provided payment is made from an account designated as a "Transferable Account".

Anglo-Egyptian Sudan
Chile
Czechoslovakia
Dutch Monetary Area
Egypt
Ethiopia
Finland
Iran
Italy
Norway
Poland
Siam
Spanish Monetary Area
Sweden
U.S.S.R.

"OTHER COUNTRIES"

Inter-transfers permitted.

Albania, Arabia, Afghanistan, Ex-Italian Colonies, Liberia, Nepal, Southern Korea

SCHEDULED TERRITORIES ("Sterling Area")

Broadly speaking, inter-transfers are freely permitted; but some limitations are imposed by local controls, e.g. South Africa, Fiji, Hongkong, India and Australia.

British Commonwealth and Empire except Canada and Newfoundland
British Mandated Territories of Cameroons
Nauru
New Guinea
South West Africa
Tanganyika
Togoland and Western Samoa
British Protectorates and Protected States
Burma, Iceland, Iraq

"BILATERAL" COUNTRIES

Inter-transfers *not* permitted unless specifically authorized by U.K. Control.

Argentina
Austria
Belgian Monetary Area
Brazil
Bulgaria
Canada and Newfoundland
China
Denmark (including Faröe Islands and Greenland)
France and French Monetary Area
Germany (Bizonia; French and Russian Zones)
Greece
Hungary
Japan
Palestine
Paraguay
Peru
Portuguese Monetary Area
Roumania
Switzerland
Syria
Tangier
Transjordan
Turkey
Uruguay
Vatican City
Yugoslavia

Note: This diagram was originally designed, in the Overseas Branch of the Midland Bank, in September 1947 and has been revised from time to time.

"... cases occurred where cotton bought from us in sterling was resold in hard-currency countries at prices a good deal lower than those corresponding to the official exchange parities."

Measures have been taken to avoid the loss of dollars which (as in the case of Egypt) results for the official control from such trading. It is difficult to tell the extent to which dealings of the type just described take place in transferable and other sterling; but they are of some importance and it was presumably with reference to them that the "Economic Survey for 1948" noted "the significant improvement which has taken place in the position of sterling in the world's financial centres" (cf. page 13). Similarly, in Switzerland the quotation for pound notes has improved by about 20 per cent. from May 1948 to May 1949.

Within the sterling area, the rate of the New Zealand pound was altered in August 1948 from the old rate of £NZ 1.25 = £1 to the new rate of £NZ 1 = £1. New Zealand, not being a member of the International Monetary Fund, could make the change without prior consultation. At the time of the revaluation of the currency by 20 per cent., it was emphasised that prices in New Zealand had risen between 10 and 20 per cent. less than in Great Britain. And in relation to the United States the following comparison was made: in 1937 the average rate between the New Zealand pound and the dollar had been £NZ = $3.97; since 1937 prices in New Zealand had risen 5–6 per cent. less than in the United States; thus there seemed nothing against returning to a rate around four dollars for one New Zealand pound.

Canada, which had appreciated its currency by 10 per cent. in July 1946, had some difficulties in its balance of payments for a year or two but was able to replenish its monetary reserves in the course of 1948.

In the United States there is an unofficial market in "inconvertible" Canadian dollars, with an average price of Can. $1 = U.S. $0.917 in 1948. The market is a relatively small one, with a turnover of probably less than $200 million as compared with an aggregate figure of several milliards for Canada's international transactions in 1948. The "Foreign Exchange Control Board" mentions in its annual report for 1948 that the market is essentially

"... comprised of the professional exchange traders in the United States who provide facilities for residents of the United States who receive capital payments in Canadian dollars which are not convertible at the official rate of exchange, to dispose of these Canadian dollars to other residents of the United States, if they wish to do so, at a price in United States dollars agreed between the buyer and seller ..."

"'Inconvertible' dollars are not acceptable payment for exports from Canada nor for most types of services performed by residents; consequently they are purchased mainly to pay for investments or tourist expenses in Canada. When they are used to purchase Canadian investments there is no net withdrawal of non-resident capital from Canada ..."

"When, on the other hand, 'inconvertible' dollars are used by residents of the United States dollar area to meet travel expenses in Canada there is a net withdrawal of capital from Canada ..."

Outside Europe some rather important alterations have been made in existing exchange systems, to which only brief reference will be made here:

In Japan, a new official rate of Yen 360 = \$1 has been applied as from 25th April 1949 to all permitted foreign trade and exchange transactions. In 1938 the dollar rate was Yen 3.50 = \$1 and at the beginning of 1949 Japanese prices would seem to have been 160 times as high as in 1937–38, and thus to have risen 85–90 times more than in the United States. But Japanese prices have probably not yet been completely stabilised and, furthermore, Japanese exports in 1948 paid for only 40 per cent. of imports.

In China, monetary disorder has continued to prevail. In August 1948 an attempt was made by the National Government to introduce a new currency: a new gold yuan, with a parity of Gold Yuan 4 = \$1 and Gold Yuan 12 = £1, was issued at the rate of one new gold yuan for 3 million old yuans. New notes issued amounted to Gold Yuan 2 milliard and a monetary reserve was built up by the requisition of foreign exchange in the possession of private individuals and enterprises and by earmarking for this purpose part of the American aid.

At first, the reform seemed to show some success but already in November 1948 the new yuan had to be officially devalued by 80 per cent. Then in February 1949 the Chinese Government, in order to safeguard the real value of at least part of its fiscal revenue, created for special purposes a new currency, the Customs Yuan, one unit being equal to \$0.40.

In Mexico a rate of Pesos 4.86 = \$1 had been ensured by the intervention of the Bank of Mexico but in July 1948 this bank suspended its operations in the foreign exchange market in view of the heavy losses in gold and foreign exchange that its support of the rate involved. The market's immediate reaction was a rise in the dollar rate to Pesos 6.85–6.95, which held until February 1949, when the quotation went to about Pesos 7.30 for the dollar, while for fiscal purposes a provisional rate of Pesos 6.50 = \$1 was maintained.

In June 1948 the rates of exchange at which the monetary authorities buy the proceeds of exports were altered in the Argentine, the alteration amounting to an average depreciation of about 20 per cent. Three different buying rates and five different selling rates are quoted (ranging between Pesos 3.35 to 5.00 = \$1), besides black-market quotations rising as high as Pesos 10.30 = \$1 at the end of April 1949.

In July 1948 the International Monetary Fund accepted the declaration of the par value for the Brazilian currency as Cruzeiros 18.50 = \$1. This rate applies to all imports and exports of essential goods, while a free-market rate (which stood at Cruzeiros 28.75 = \$1 at the end of March 1949) applies to financial transactions and to the import of non-essential products. Since the beginning of 1948 the official selling rate has been increased by a 5 per cent. exchange tax for some special remittances.

By decisions taken respectively in February and December 1948, Chile and Colombia maintained their existing multiple-rate exchange systems with some alterations, the rates ranging in the one case between Chilean Pesos 19.37 and 61.95 = \$1 and in the other case between Colombian Pesos 1.95 and 2.75 = \$1. In Peru also, multiple rates are in force, the system involving the use of exchange certificates, which in March 1949 sold at Soles 17.79 = \$1, as compared with an official rate of Soles 6.50 = \$1. Uruguay also has a system of multiple rates, varying from an official buying rate of Pesos 1.519 = \$1 to an official "free" rate for non-trade transactions, which in December 1948 was fixed at Pesos 2.25 = \$1. Venezuela also has several rates, the lowest of which (Bs. 3.09 = \$1) is applicable to the proceeds of the export of petrol and the highest (Bs. 4.80 = \$1) to the proceeds of the export of coffee (this being in the nature of an indirect subsidy).

In its Annual Report for the fiscal year ended 30th April 1948, the International Monetary Fund explained that

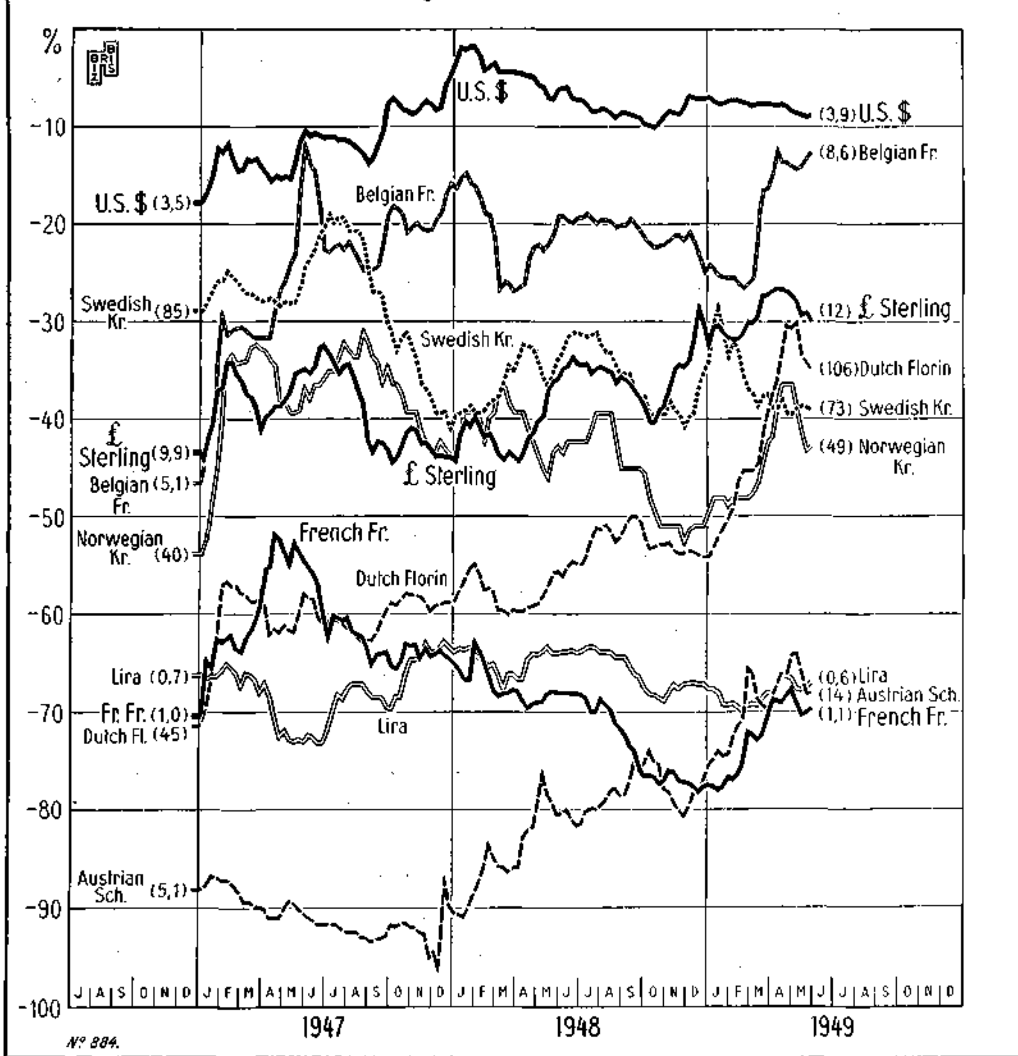
> "certain countries, particularly in Latin America, have used multiple currency practices as a means of restricting imports without resort to complicated administrative machinery and without giving the recipients of import licences opportunities for large windfall profits. They have also had fiscal significance in some countries in which governmental revenue is derived in large part from indirect taxes ...
>
> The Fund has advised those of its members which engage in multiple currency practices of its interest in the unification of exchange rates structures ...
>
> At present, the most important consideration is the termination in the countries concerned of domestic inflation. Until the abnormal demand for imports can be checked by other means, some countries may have to use penalty rates of exchange for this purpose ...
>
> In view of their special circumstances the Fund did not take exception to proposals by some member countries to introduce multiple currency practices or to adapt existing ones to changing circumstances."

* * *

Returning to exchange conditions in Europe, it is of interest to examine the trend of quotations on the Swiss and American markets for foreign bank-notes. Under the Swiss legislation, this is a completely free market, as is the free market for notes and currencies in New York. The discount at which notes are traded in depends partly on the ban (still existing in many cases) on reintroducing more than a limited amount of notes into the country of origin; but the quotations do not, as a matter of fact, diverge appreciably from those registered on the market for remittances, which is in operation and would seem to be dealing in funds of a much greater usability.

The general impression received from the quotations of notes in Switzerland as in the United States is one of improvement in the value of the

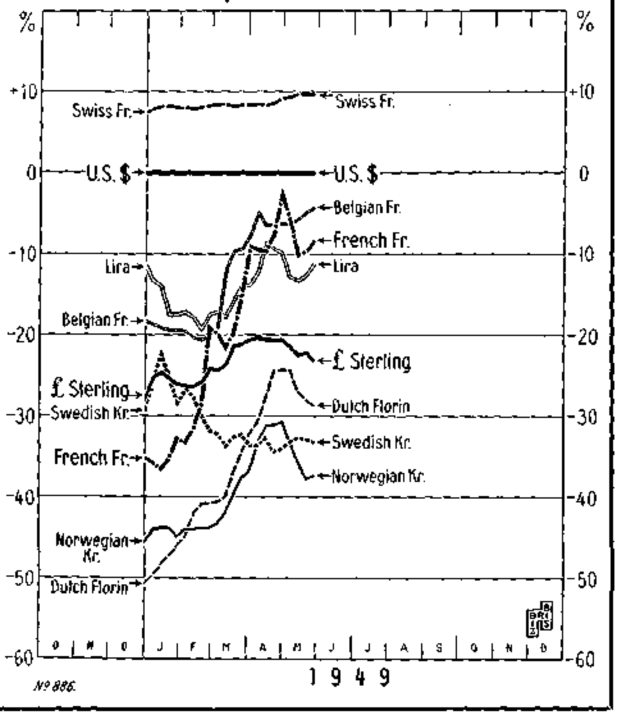
Price of foreign bank-notes in Switzerland.*



* Weekly averages.

Note. The initial rates in the above graph were established as discounts in relation to the official rates in force for each currency at the end of 1946 and thus show the depreciation which at that time the free-market quotations for the notes involved in relation to the then official rates. Since for some currencies the official rates were altered in the following years, the curves do not generally retain the same significance but represent the fluctuations of the price in Swiss francs paid for the foreign bank-notes.

Free-market rates for notes in Switzerland shown in relation to the official rates for the purchase of dollars.*



* Weekly averages.

Note. The quotations for notes in Switzerland correspond closely to free-market quotations of bank-notes on the New York market and the graph shows the value of the various currencies (according to the free-market quotations) in relation to the dollar.

The purpose of the graph is thus to show the disparity between the official rates at which the monetary authorities of the countries concerned purchase dollars, i.e. the official dollar rates in 1949, and the rates which correspond to the prices paid for bank-notes on the Swiss (and American) markets, these prices corresponding at the same time to the rates generally used for so-called "private compensations". The exact significance of the different dollar rates varies somewhat from country to country. The free rate for the Swiss franc in the United States is not applicable, under Swiss regulations, to the settlement of commercial transactions. The official free rate for the dollar in Paris is applicable to commercial transactions as to 50 per cent. only (see page 119).

different currencies. The price for 100 Dutch florins has risen from Sw.fcs 45 at the end of 1946 to Sw.fcs 106 at the end of May 1949; the value of the Austrian schilling shows an even higher percentage rate of improvement (but the level from which it started was very "low"). The quotation of the pound note was Sw.fcs 9.90 at the end of 1946 and it stood at Sw.fcs 12 at the beginning of 1949. It should be added that the "value" of the Danish crown (not included in the graph) has improved by nearly two-thirds — approximately the same proportion as for the guilder.

The second graph is interesting because it shows how relatively slight the disparity for the Belgian franc, the French franc and the lira now is in relation to the actual dollar par rate.

There has, however, been no improvement in the quotation of the Swedish crown (following the intensification of the control over Swedish trade and foreign exchange in the course of 1948). The disparity between the official rate and the market rate for the financial dollar (or the dollar note in Switzerland) is due to the restrictions placed by the Swiss authorities on the purchase of gold and foreign currencies (including the dollar) as a defence against too great an influx of capital. There have been fluctuations during the year in the price paid for financial dollars or dollar notes but no great change on balance.

The market for notes in Switzerland may at times have been rather narrow, but for many currencies the quotations have been the only really free quotations and it would seem as if increased importance had been attached to them for several reasons:

(i) It has already been mentioned (page 120) that as long as the discount between the rates quoted abroad (corresponding to "parallel" rates at home) and the official rates is less than 10–15 per cent., the Exchange Control in the country in question can usually count on collecting most of the exchange brought in by tourists, etc., but that, once the disparity becomes more pronounced, this source of foreign exchange will begin to run dry as far as the legal channel is concerned.

(ii) Secondly, there is often a variety of "private compensation" transactions, which are settled more or less according to the rates quoted for notes on the foreign market. When such rates move sharply against a country, the economy of that country is generally a loser, since the foreign partners in the transactions are then, as a rule, able to obtain very favourable terms of trade. Furthermore, exporters have then an interest in under-invoicing and importers in over-invoicing goods, so that the legal circuit is in danger of losing part of the foreign exchange; and the greater the discount at which the home currency is quoted on foreign markets, the greater the incentive to adopt such practices and the greater the consequent loss of exchange.

(iii) Thirdly, considerable attention seems to be paid, not only by the general public but also in many well-informed financial circles, to the ups and downs of the quotations of foreign bank-notes, which (being outside the domestic, controlled sector) influence the degree of confidence (or lack of confidence) felt in each of the particular currencies concerned. Thus, when an improvement occurs in the quotation for the notes of a country, this is often seized upon as a sign that confidence in that particular currency is growing stronger.

There is an increasing number of countries which have deliberately set out to lessen the difference between the free rates quoted in Switzerland and the United States and their official rates. As mentioned above, Belgium has taken measures to induce a progressive rise in the quotation of the Belgian franc outside the country and to bring it into immediate proximity to the official parity of the dollar.

The adoption of the system of official free rates in Italy and France has permitted a great reduction in the margin between the official and the "parallel" rates.

As dealings in notes on the foreign markets have generally a counterpart on the black or "parallel" market inside the country, it is sometimes assumed that all such transactions amount to so much f l i g h t o f c a p i t a l. But transactions not infrequently represent mere changes in ownership of dollar and other notes already in the country; moreover, the bulk of the remaining transactions have not been on capital but rather on current account — French people have, for instance, bought Swiss francs to be spent during a visit to Switzerland or in order to import commodities for which foreign exchange is not allocated by the Control.

As regards genuine flight of capital, this can also be contrived, as mentioned above, through under-invoicing exports and over-invoicing imports. In both cases, some active outside help is required — plus belief in the foreign currency concerned. If an export of capital has to be carried out in a clandestine way, it is not always so easy to stage it successfully as is sometimes suggested — and it should be remembered that, at times when credit is severely restricted, there are not so many firms which have excess funds to export.*

Fear of flight of capital is the reason why it is often thought necessary to maintain a control over capital movements, even when it is intended that exchange shall be freely available for current transactions. But in the process of deciding what should constitute "current transactions", some new distinctions have gradually developed. In the Articles of Agreement of the International Monetary Fund, adopted at Bretton Woods in July 1944, current payments were defined as comprising "normal short-term banking and credit facilities" and "payments of moderate amount for amortization of loans or for depreciation of direct investments". The next step would be to conclude that genuine foreign investments should be permitted and even stimulated. That is the rule applied, for instance, within the sterling area but, at the same time, measures have been taken within that area to prevent what may be regarded as more or less speculative transfers. Difficulties no doubt arise when it comes to applying such distinctions in practice, but recently greater emphasis has been laid on the fact that certain types of capital movements are essential for the rebuilding of economic life as well as for the restoration of a workable exchange system.

* * *

During the heyday of the gold standard before the beginning of the first world war, exchange rates were kept stable (with movements only within the gold points) and, if a country happened to get out of line as regards its costs and prices, it had to take suitable steps (through an increase in its rates of interest or otherwise) to eliminate the disequilibrium which had arisen. It may, therefore, be said that, at that time, prices had to be

* In the first half of 1948 the weight of French exports in tons (according to the Customs statistics) increased by 16 per cent., while the dollar equivalent of the value received (according to the Exchange Control statistics) fell by 15 per cent. as compared with the previous year. But in themselves these figures in no way prove a widespread export of capital through under-invoicing. A large part of the disparity is explained by the increase in exports of heavier products (especially coal, including deliveries of Saar coal from 1st April 1948). Moreover, the French franc was devalued by 65 per cent. in 1948 in relation to the dollar, the Swiss franc and the escudo, and when such a thing suddenly happens it is likely that the dollar equivalent of the value figures of foreign trade will rise more slowly than would otherwise be the case — partly because there are always some sales which were originally expressed in the domestic currency and partly because the amounts expressed in currencies other than the three just mentioned are also reduced in terms of dollars. This shows with what circumspection statistics have to be interpreted in times of rapidly changing prices and exchange rates. It is, indeed, probable that in actual fact the flight of French capital in 1948 did not amount to more than at most one-third of the equivalent of $500 million — the figure which has frequently been mentioned. (In any case, the standard argument quoted as evidence for that figure is not valid, being based on comparison between the Customs and the Exchange Control statistics, as mentioned above.)

adapted to exchange rates and not vice versa. But it should be added that, in the twenty years before 1914, price adjustments did not, as a rule, subject countries to any painful process of adaptation, since world prices were gradually rising under the influence of the mounting output of the South African gold mines. It was a different story in the previous twenty-year period when, with world prices gradually falling, it had now and then been difficult for countries to align their economies to the general price movements on the world markets. The "single-rate" regime followed after the first world war is discussed on the first page of this chapter.

In the years since the second world war, the exchange rates of most countries have been kept at officially stable parities. There have been those who thought it premature to adopt a régime of official exchange stability, since cost and price relations could not possibly have reached a state of balance after the wartime upheavals and severances. But it must be pointed out that adjustment was facilitated by the persistent price rise in the United States, which lifted the wholesale price level by more than 50 per cent. between the summer of 1945 and the end of 1948; this rise undoubtedly helped to restore balance to currencies in Europe (and elsewhere) which would otherwise have remained overvalued. Now that prices are beginning to fall in the United States, a different situation may take shape; but so far the state of affairs is that prices of foodstuffs and raw materials have been reduced in relation to those of manufactured goods, the prices of the latter having kept up fairly well. If such tendencies continue, the result will, on the whole, turn out to the advantage of Europe, which is an importer of raw materials and foodstuffs and an exporter of manufactured goods.*

Even more than the movements of the general price index in the United States, the variations in the different sections of that index should be closely watched; in addition, each country in Europe would be well advised to examine — on the basis of all the material it can collect — the competitive price position of its own manufactured goods in relation to the corresponding price structure in the United States. Should such an examination reveal disequilibria which seem likely to be of a permanent character, the need will arise of restoring equilibrium either by an adjustment in the domestic costs and prices or, if that proves impossible, in the exchange position.

A lively discussion is in progress at present regarding the principles which ought to guide the authorities in determining appropriate exchange rates. Considering the structural changes which have occurred during and since the war, it is not easy to lay down precise rules; but some general observations may perhaps be usefully made with regard to the influence exerted by changes in rates on the volume of imports and exports; also with

* It has been calculated that for the three western zones in Germany the fall which has already (May 1949) taken place in world market prices for foodstuffs and raw materials means a saving of foreign exchange to the amount of DM 300 to 400 million a year for these zones.

regard to the need for adjusting rates to the respective levels of costs and prices; further, with regard to the effect produced by the internal credit and investment policy; and, finally, as to the chances of collecting a sufficiency of foreign exchange under the difficult conditions now prevailing.

1. Often a downward adjustment in the exchange value of a currency is thought of primarily as a device to stimulate exports and reduce imports and in that way to restore equilibrium in the balance of payments. In exchange policy this is no doubt a consideration of real importance but the experience of many countries has shown conclusively that devaluation in itself is not enough: if internal conditions (with regard to budget equilibrium, etc.) are not in order, the relief resulting from an adjustment in the exchange rates may be no more than ephemeral in character.

If as a result of a budget deficit or excessive investment a deficit emerges in the balance of payments, there is no reason to expect that resort to devaluation will bring in from abroad the amounts required to establish internal and external balance while national investment programmes remain the same, etc. The net result may sometimes be the reverse, since devaluation, if it goes too far, may in effect reduce the amount of foreign exchange actually realised as payment for exports. Much depends on the starting-point: if the national currency has been overvalued, devaluation is likely to mean that many products which could not previously be exported will move into the category of possible exports and thus help to restore equilibrium fairly quickly. If a devaluation had been feared, the very fact that it is undertaken ("over and done with", as the phrase goes) may just reverse the preceding movement and bring funds to the country whose currency has been devalued.

While with E.R.P. countries it should be possible to arrange for the requirements of foreign capital without upsetting for their sake the balance in the foreign-exchange market. And, having eliminated this particular source of disturbance, the countries should be able to establish rates providing for the greatest possible degree of harmony between the various economies.

2. The search for harmony is the fundamental idea behind the theory of purchasing-power parities, which assumed that the actual exchange rates in the market would be determined by relative cost and price levels. This assumption obviously presupposed that goods could move freely and in sufficient quantities from one country to another. Experience showed that, when that condition was not fulfilled, the rates might fluctuate wildly, especially since, under such circumstances, little help could be expected from equilibrating capital movements. But, even when trade flows freely, it may happen that a country, having lost a considerable part of its foreign investments or failed to keep pace with technical progress, has to accept a lower exchange value of its currency than would otherwise be necessary. In such cases, however, a very wide margin would not seem to be called for. The experience of the inter-war period was that on the few occasions when

relative currency values had been more or less re-established (as in 1929 and again, for most currencies, in 1938), the relative price levels stood to one another (with comparatively slight deviations) as in the basic year 1913 although in the intervening period many shifts must have taken place in the structural strength of the various economies. A deviation of as much as ten per cent. could then be regarded as exceptional.

But the current price level is not always relevant for determining the true value of a country's currency; it has to be a price level at which the economy of the country in question is reasonably in equilibrium and thus has sufficient resilience to be able to stand the strain of, for instance, a moderate depression with a return to buyers' markets.

It is clearly to nobody's advantage that the exchange level of a currency should be pressed down more than is necessary to find, without undue delay, a self-sustaining level.

3. There have been a number of countries, however, whose exchange rates seem to have been at a fairly correct level from a purchasing-power point of view (account being also taken of controlled prices) but whose exports have covered (say) only one-half of their imports, the result being a marked "penury of foreign exchange". It is then necessary to enquire why exports have been at such a low ebb. Immediately after the war, most countries suffered from a scarcity of goods, which made it difficult to increase exports; but by the latter half of 1948 production in most western European countries was back at or above the pre-war level. The reason for a deficit in the balance of payments can then only have been that total spending (for consumption and investment by the government and the general public) was greater than the available resources of domestic origin and thus on a larger scale than the pre-war total.

Admittedly there are circumstances — as just after a war — when, in order to restore the transport system to working order or to undertake badly needed industrial repairs and provide new plant and equipment, it is appropriate to spend, and especially to invest, more than the domestic resources would warrant. In this connection, an important question of timing arises, however. If large investments are undertaken without being matched by sufficient domestic savings and if — no foreign resources being available at the time — the funds required are obtained through a domestic credit expansion, the effect will generally be inflationary in character, leading to a deficit in the balance of payments. Since this will cut into monetary reserves, the country will be exposed to a drain on its foreign-exchange holdings, including, in the first place, its dollars; and then the public will talk about a "dollar shortage".

The proper way of proceeding is clearly to ensure that the foreign resources required as cover for investments (i.e. as additional capital from abroad to supplement a country's own insufficient savings) are available in time. If that is the case, amounts received from abroad will be applied to the purposes for which they have been obtained; and there will then be neither an inflationary effect on the domestic market nor a demand for foreign exchange in excess of the foreign resources specifically provided for the purposes intended.

But it is necessary that the remaining expenditure — either in the budget or for other investments — should be covered by genuine domestic resources. It is also necessary that the exchange rate should be at a proper level; but experience proves that in a changing world a proper level depends not so much on calculations of purchasing-power parities as on the harmony attained in the whole economic and financial policy which a country pursues. It is interesting to record that when, as in Belgium, internal financial equilibrium is ensured by a careful investment policy, even a relatively pronounced rise in the domestic price and wage level may be compatible with a strengthening of the exchange position (for Belgium added to its gold and dollar reserves in 1948).

4. When in a particular country foreign exchange is sold to importers by the central bank (or some other monetary authority) and the imported goods are sold to the public, those latter sales absorb part of the existing purchasing power and (assuming that inflation has been completely arrested) the effect should be — as shown on page 100 — to set free other goods and services for export. From those exports the central bank should be able to replace the foreign exchange it had previously sold. But all this will happen only under certain conditions, one of them being that the exporters really hand over the foreign exchange to the central bank. There is, in fact, a separate problem, viz. that of collecting the foreign exchange. If exporters cannot obtain fresh and easy credits from the banks, they will be compelled to repatriate most of the proceeds of their foreign sales, since otherwise they cannot carry on their business at home — the example of Italy in 1947 and of France in the spring of 1949 provides evidence of how effective credit restrictions may be in this respect (it would be possible to mention other instances, too). One consideration is, no doubt, the price paid for the foreign currencies. Reference has already been made to the fact that a reduction in the margin between, on the one hand, rates quoted for notes on the foreign markets (or on black or parallel markets at home) and the official rates, on the other hand, is of real importance (see pages 131–132). It seems essential that the countries should not be deceived by an illusory security in the form of rigid rates of exchange (as fixed by the Control) but that they should look squarely at the situation and ask themselves what proportion of foreign exchange is really being collected — and then they might remember that the difference between soundness and failure of an enterprise is often determined by a margin of ten per cent.

In the years 1932–34 Austria made a successful adjustment of its exchange rate by a gradual process in which permission to apply so-called "compensation rates" was granted more and more frequently until it was possible to gauge the true level of the newly-restored equilibrium.

In a somewhat similar way, a number of countries in Europe — and notably Italy and France — have operated along the lines of flexibility of exchange rates, but a flexibility practised with a view to stabilisation. Their action in this respect has been more or less in conformity with the time-honoured methods of the past. But it is by no means out of the question that a successful result can also be achieved in other ways such as, for instance, a sudden alteration affecting the whole exchange-rate structure, i.e. a modification of the par rate by a definite percentage, the new rate being introduced (so to say) with one stroke. In that way, a new equilibrium may become established if the judgement of those who decree the change is sufficiently reliable. In either case also, the foreign exchange control may be retained, but the success of the adjustment — as of any set of rates in force — will ultimately have to be judged by the extent to which foreign exchange is freely made available for all current transactions and all normal capital transactions (the control being retained as a safeguard against excessive capital movements). Success, however, will only come if the exchange policy is sufficiently coordinated with appropriate policies in other fields, and especially as regards budget and credit conditions. When a country lowers the exchange value of its currency an expansionist element is pro tanto introduced into its economy and the country is then likely to be successful in improving its balance of payments if, at the same time, it applies a relatively restrictive credit policy and shows moderation in the extent to which its costs and prices are allowed to be adapted.

Considering that the history of prices, costs and all the other phenomena of an inflation has been a very different one for the various countries in Europe, it is not to be expected that such exchange adjustments as prove necessary will be applicable in the same way to all of them. But, even if the problems are not the same, there are certain minimum requirements to be fulfilled before a country ceases to be vulnerable as far as its supplies of foreign exchange are concerned. One of those requirements is that it should be free to shape its commercial policy not chiefly with an eye to day-to-day receipts and outgoings of its foreign-exchange till but in a broader way. For that to be feasible it must have adequate monetary reserves, otherwise the management of its whole policy will be on too precarious a basis; and, without sufficient backing, it will be impossible when some trouble arises (as it always does) to maintain the confidence in the currency which is indispensable for the regular collection of the foreign exchange that should flow, day in, day out, into the monetary reserves.

Now that rehabilitation has gone so far that wartime shortages are being overcome and, consequently, control can be lifted in one sector after the other, the material conditions are beginning to be established for a freer movement of goods and services internationally. That being so, it may once more be possible to put greater reliance upon the cost and price levels of the different countries as the factor determining the rates of exchange. When monetary reserves are sufficient to provide for temporary deficiencies without forfeiting confidence, the exchange values of different currencies may soon be expected to correspond, according to the valuation of the market, to the buying power of the currencies in question.

Though foreign-exchange control may have to be maintained as a safeguard against abnormal movements of capital, it would be dangerous to allow fear of such undesirable movements to prevent a return to adequate

Official alterations in exchange rates 1939–1949.

Countries	National currency units	U.S. dollar middle rate				Percentage change	
		24th August 1939	December 1945	End of March 1948	End of March 1949	24th August 1939 to March 1949	December 1945 to March 1949
Austria	Sch. . .	5.34 (1)	10.00	10.00	10.00	— 47	0
Belgium	B.fcs . .	29.58	43.83	43.83	43.83	— 33	0
Bulgaria	Leva . .	83.90	286.56(2)	286.56(2)	286.56(2)	— 71	0
Czechoslovakia.	Kčs . . .	29.235	50.00	50.00	50.00	— 42	0
Denmark	D.Kr. . .	4.795*	4.80	4.80	4.80	— 0.1	0
Finland	FM . . .	48.40	135.70	135.70	135.70	— 64	0
France	Fr.fcs . .	37.755	119.10	259.89½(3)	266.79½(3)	— 86	— 55
Germany	RM/DM .	2.493	10.00	10.00	3.33(4)	— 25	+300
Greece	Dr. . . .	117.60	500.00	5,000.00(5)	5,000.00(5)	— 98	— 90
Hungary	P/Frt . .	5.20	104,000.00	11.74(6)	11.74(6)	— 56	—
Italy	Lit. . . .	19.00	100.00	573.00(7)	575.00(7)	— 97	— 83
Netherlands . .	Fl. . . .	1.86	2.65	2.653	2.653	— 30	— 0.1
Norway	N.Kr. . .	4.27	4.96½	4.96½	4.96½	— 14	0
Poland	Zl.. . . .	5.325	—	100.00(8)	100.00(8)	— 95	—
Portugal	Esc. . . .	23.36	24.815	24.91½	24.91½	— 6	— 0.4
Roumania . . .	Lei . . .	143.59	3,635.00(9)	151.50(10)	151.50(10)	— 5	—
Spain	Pts . . .	9.05	11.085	11.085	11.085(11)	— 18	0
Sweden	S.Kr. . .	4.15*	4.19	3.59½(12)	3.59½	+ 15	+ 17
Switzerland . .	Sw.fcs .	4.435	4.30	4.30	4.30	+ 3	0
Turkey	Liras. . .	1.267*	1.305(13)	2.8126	2.8126	— 55	— 54
United Kingdom	£stg . . .	4/3¼ d	4/11½ d	4/11½ d	4/11½ d	— 14	0
Yugoslavia . . .	Dinars . .	44.05	50.00	50.00	50.00	— 12	0
Canada	Can.$ . .	1.0047	1.1025	1.0025	1.0025	+ 0.2	+ 10
New Zealand. .	£NZ . . .	3.56	3.20	3.23	4.00	— 11	— 20
Argentina (14). .	Pesos . .	4.325	4.0675	4.01	4.80½	— 10	— 15
Brazil (14). . . .	Cruz. . .	19.93	19.50	18.72	18.72	+ 6	+ 4
Peru *	Soles . .	5.36	6.50	6.50	6.50	— 18	0
Iran *	Rials . .	17.41	32.50	32.50	32.50	— 46	0
China	Chinese$ Gold Yuan	3.33	20.00	12,000.00	20.00(15)	— 83	0

* Official selling rate. (1) January 1938. (2) Official rate plus premium of 250 per cent.
(3) Mean rate between basic and free official rate. Devaluation on 26th January 1948.
(4) Export-import rate.
(5) Without exchange certificates. With certificates the rate would be about Dr. 10,000 for one U.S. dollar.
(6) The forint was introduced on 1st August 1946 and was equal to 400,000 quadrillion pengö.
(7) Rate fixed monthly by decree of 28th November 1947.
(8) Without premium surcharge of Zl. 300 in practically all financial transfers abroad.
(9) Including the supplementary premiums.
(10) The new leu was introduced on 15th August 1947 and was equal to 20,000 old lei.
(11) In addition a sliding scale of rates, ranging from Pts 12.59 to Pts 21.90 for specified export goods and from Pts 13.14 to Pts 27.375 for specified import goods, has been applied since 3rd December 1948.
(12) Revaluation in July 1946. (13) Official rates, excluding premiums. (14) Free-market selling rate.
(15) Official rate. On 19th August 1948 the gold yuan was introduced and was equal to 3,000,000 old yuan. Its initial exchange value was 4 gold yuan for one U.S. dollar. This rate was lowered to 20 gold yuan for one U.S. dollar on 11th November 1948.

liberty for normal transactions and then to let whatever control is necessary over capital movements interfere unduly with freedom in the field of current transactions. What is clearly called for is the re-establishment, with the least possible delay, of a normal régime in which commercial transactions and other current operations can be effected without excessive formalities and with the certainty that for all current operations the necessary foreign currencies will be obtainable when required. To fulfil such a condition the exchange régime must obviously aim at being "self-sustaining", which means that it will obtain the necessary exchange from the market itself — and a market freed from artificial limitations as regards all current-account operations.

The trend should clearly be towards greater freedom as regards foreign exchange transactions. It has to be remembered that the real cost of exchange control is not to be measured simply by the expenses of the administration, a heavier item being the loss of time and effort — not to speak of the actual loss of trade — through the cumbersome formalities, the delays and uncertainties which seem to be inseparably connected with such a vast undertaking as the application of effective exchange control.

VI. Production and Movements of Gold.

No precise information is available with regard to the output of gold in the U.S.S.R. but if, for statistical purposes a figure of 4 million ounces is again adopted (and maybe it is not very far from the truth) total world production of gold in 1948 would be equal to 27.8 million ounces, as compared with 27.3 million ounces in 1947. There has thus been a slight increase in the yearly output, but this is still one-third below the peak figure, which was reached in 1940. A few producers — in particular, the Union of South Africa, Canada and British West Africa — have seen an increase in their production, while most of the others (although still with a question-mark for the U.S.S.R.) have shown a decline.

Gold production (annual).

Country	1940	1947	1948
	In thousands of ounces		
South Africa	14,038	11,198	11,574
Canada	5,311	3,070	3,528
British West Africa	939	560	668
Total for three producers	20,288	14,828	15,770
All other producers	20,712	12,472	12,030
Total production	41,000	27,300	27,800

Valued in dollars at $35 an ounce, the world's gold production was equal to $975 million in 1948 but it should be observed that an increasing part of the output was being sold at prices above those officially fixed in the various countries. Of the newly-produced gold, about two-thirds went into monetary reserves and this was, in general, paid for at official prices, i.e. at about $35 an ounce for fine gold or its equivalent in other currencies.

In 1948, the gold stock of the United States increased by $1,490 million i.e. by the total output of gold and half as much again. But countries other than the United States were able to increase their gold stocks too, including Canada (by $115 million), Venezuela (by $108 million), Italy (by $38 million), Switzerland (by $31 million) and Belgium (by $27 million), and there were also additions to the reserves of Cuba and Hungary. Two international institutions, the International Monetary Fund and the Bank for International Settlements, increased their holdings by $80 million and $6 million respectively. These various amounts together came to $400 million, so that, with the increase in the gold stock of the United States, the total increases registered were about $1,900 million.

Only about one-third of this increase was derived from the part of the annual production that was available for monetary purposes, the other two-thirds being a draft on the reserves of other countries, which fell by an aggregate reported total of $1,450 million. The greatest loser was South Africa, which (in addition to its own annual output at the rate of about $400 million) drew on its reserves to the extent of $579 million. For the United Kingdom the decline was equivalent to $420 million and for the Argentine to $190 million, while some ten other countries incurred a loss of about $260 million together.

Since in 1948 the United States was no longer the only recipient of any importance, the gold movements in that year were somewhat less one-sided than in earlier years — a small but welcome sign of some progress towards equilibrium under the influence of anti-inflationary measures taken in the countries concerned, many of which have profited by the respite afforded by Marshall aid.

During the year, gold went increasingly into private hoards in the East and elsewhere. The industrial consumption of gold has been rising steadily but there is often only a pretence of working it up, since semi-manufactured or finished articles (e. g. simple statuettes) represent only another method of furnishing the metal in a form suitable for private hoards; as a result, the line of demarcation between industrial uses and downright hoarding is becoming more and more blurred. In all, it would seem as if in 1948 the amount of gold taken by the industry or going into hoards had been of the order of magnitude of 10 million ounces, i.e. around $350 million's worth.

Higher prices — often the equivalent of more than $40–50 an ounce — have been paid for gold by open or concealed hoarders. At the same time, the world's gold producers, harassed by the inflationary pressure of high costs of production (which affect marginal mines), the scarcity of labour and the difficulty of finding funds for new investments, have looked longingly at such higher prices. In 1948, the gold-mining industries in nearly all gold-producing countries did, in fact, appeal to their governments either for tax reductions or subsidies or for permission to sell gold on the free market above the official price. The International Monetary Fund in Washington has again and again had to investigate and take decisions with regard to the payment of subsidies in member countries and the prices at which gold might be sold in domestic markets. There is no indication of any early abatement of the discussions and controversies regarding these matters.

Output of Gold.

Reference has already been made to the fact — more fully revealed in the following table — that in 1948 the development of gold production was not uniform throughout the world.

In South Africa, the decline in the output of gold which had begun in 1942 was interrupted for the first time in 1948, when output rose by 376,000 ounces, or 3.4 per cent. This greater yield did not, however, represent any real expansion in production but rather a recovery from the low level of 1947, when demands for higher wages in view of the rise in prices had led to bitter conflicts, together with strikes in February and March of that year. These strikes accounted for the loss in output of about 500,000 ounces and also for an increase in costs of production. Consequently, the increase in output in 1948 was more or less accidental and the same may be said of the stabilisation of costs in that year — with the result that these data offer no firm basis for conclusions as to future trends.

World gold production.

Gold-producing countries	1929	1940	1945	1946	1947	1948
	Weight, in thousands of fine ounces					
Union of South Africa	10,412	14,038	12,214	11,918	11,198	11,574
Canada	1,928	5,311	2,697	2,833	3,070	3,528
United States (1)	2,208	5,920	997	1,625	2,321	2,099
Australia	426	1,644	657	824	937	889
British West Africa	208	939	548	590	560	668
Rhodesia	562	833	568	552	523	515
Mexico	652	883	499	421	465	450*
Colombia	137	632	507	437	383	335
Belgian Congo	173	555	347	331	308	316
Nicaragua (2)	12	155	200	182	212	223
Chile	26	343	179	231	169	164
India	364	289	168	132	173	185
Peru	121	281	173	158	116	160*
Brazil	107	264	195	140	134	133
New Zealand	120	186	128	119	110	100*
Other countries (3)	1,744	8,727	6,423	6,507	6,621	6,461
Estimated World production	19,200	41,000	26,500	27,000	27,300	27,800
	Value in millions of dollars (4)					
Value of estimated World production	672	1,435	930	945	955	975

* Provisional. (1) Including Philippine Islands production received in the United States through 1945.
(2) Gold exports representing about 90 per cent. of gold production.
(3) Estimated. The total for "other countries" includes for the years since 1940 a conjectural figure of 4 million ounces for the U.S.S.R. (4) At the rate of $35 per ounce of fine gold.

In South Africa, as elsewhere, development of the mining industry is dependent upon four principal interrelated factors: prices (of gold and other commodities), wages, taxation and the payment of dividends.

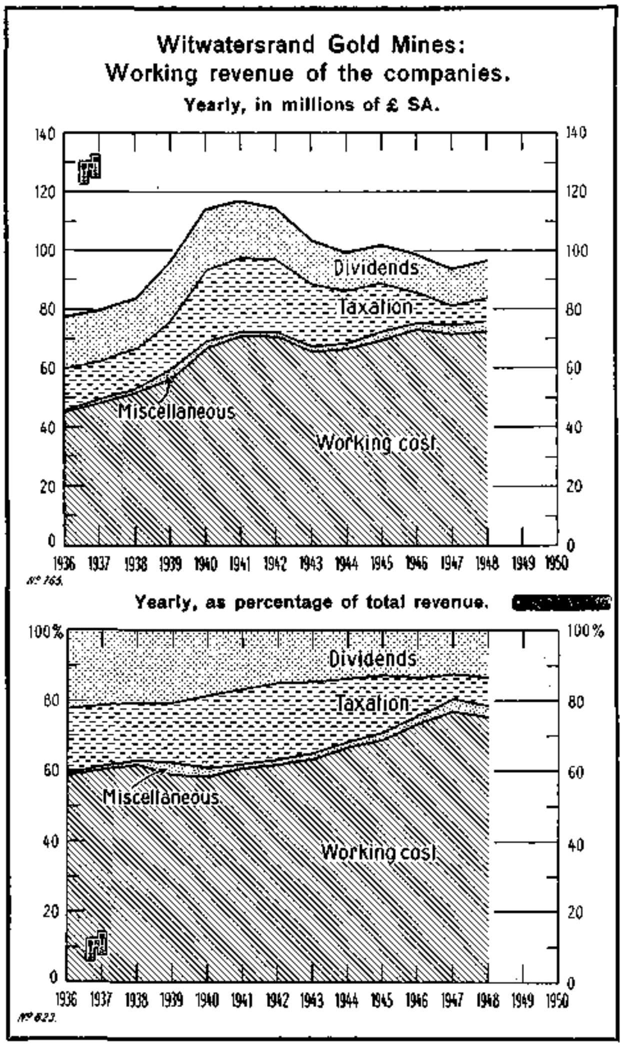
The official price of gold remained unchanged in the face of rising costs and prices.

Obviously working costs cannot be stabilised in the absence of a comparatively stable level of prices, since changes in money wages are largely bound up with the movement of retail prices. Only such branches of production as were in a position to counteract the increase in retail prices by an increase in money wages could enrol and maintain a sufficient volume of labour, and in that connection the possibilities of the gold-mining industry, subjected to an inflexible gold price, were clearly limited. The number of natives employed on the Witwatersrand fell from 280,000 in December 1946 to 276,000 in December 1947 and then again to 257,000 in December 1948.

Union of South Africa: Prices and cost of gold production.

Year	Working costs per oz. (1)	Commodity prices: Wholesale (2)	Commodity prices: Retail
	Indexes: 1938 = 100		
1938	100	100	100
1945	136	153	132
1946	144	156	134
1947	151	164	140
1948	148	175	148

(1) Witwatersrand and extensions.
(2) Including imported goods.



Indexes of share prices in South Africa.

Year	Producing gold mines	Industrial enterprises
	Base: 1938 = 100	
1938	100	100
1939	96	93
1940	94	93
1941	99	110
1942	92	128
1943	111	158
1944	121	170
1945	131	179
1946	137	219
1947	123	247
1948	123	252

Dividends, which reflect the profit-making ability of gold mining and are, therefore, of real importance for the attraction of capital, declined continuously from 6s. 10d. (per ton milled) in 1939 to 4s. 5d. in 1947, the real value diminishing even more because of the increase in prices. This reduction had its effect on the quotations of gold-mining shares as contrasted with those of other shares.

The quotations of shares in industrial enterprises as a whole have risen faster than prices, while the shares of gold mines lag behind the rise in prices.

Of the factors affecting costs of production, the only one which it was within the power of the South African Government to mitigate was taxation. To relieve the position of the mining industry, the tax formula was reduced and the amortisation allowance was raised from 22½ to 27½ per cent. in the autumn of 1948. The gains of the gold-mining industry resulting from this reduction were estimated at £900,000 for a full fiscal year. Already, as a result of earlier tax reductions, government revenue derived from the gold mines (comprising tax, lease and other payments) had declined from 8s. 3d. per ton of ore milled in 1942–43 to 2s. 4d. in 1947–48.

Helpful as this lowering of taxation was in protecting gold output from a sharp decline, it could not by itself solve the problem of further development of the mining industry as dependent on the purchasing power of gold in South Africa and on international markets. As to measures with this end in view, see page 156.

Canada, faced in 1947 with a heavy deficit in its balance of payments with the United States and unable to obtain sufficient dollars as payment for its surplus exports in other directions, began to pay more attention to the profitability of its gold-mining industry (affected, inter alia, by the appreciation of the Canadian dollar in July 1946) and, in the autumn of 1947, set on foot a subsidy scheme, which, after some modifications, was approved by the International Monetary Fund. It was probably the subsidy payments that helped to maintain the upward trend of gold production, which increased by 15 per cent. from 1947 to 1948 (even with this improvement, however, it only came to 66 per cent. of the gold output in 1940). Though the gold-mining industry is still hampered by a shortage of manpower, some easing of the position has already taken place in this respect and it is expected that more labour will become available in the event of a decline in the activity of the manufacturing industries.

After a temporary recovery in 1946 and 1947 in the gold-mining industry in the United States, there was a decline by 10 per cent. in the output in 1948, probably reflecting the relatively small profits to be made in gold mining as compared with the possibilities in other lines of production. But surprisingly little was heard about the difficulties encountered by the gold-mining industry; in view of the general prosperity, the decline in the output of gold could obviously not be presented as a serious drawback (the United States being in a different position from countries largely dependent on the export of gold and much of its gold output being extracted rather as a by-product).

In Australia, the gold-mining industry, feeling the strain of rising costs and prices, urged the Federal government to support mining activity by way of subsidies or to allow sales on Indian markets, where the demand for gold was quite strong at relatively high prices. The government did not agree to any form of general assistance but, after a thorough investigation by Treasury officials, it gave financial assistance in the autumn of 1948 to three mines (the claims of some others remaining under consideration); the companies in question were to be allowed to pay a dividend of 4 per cent. on their issued capital.

In British West Africa, output increased by nearly 20 per cent., which would seem to be the highest proportionate increase anywhere. In addition to the usual difficulties of rising costs, etc., the industry had had to contend with an export duty, which had been reduced in 1946 from 20s. 11d. to 17s. 5½d. per ounce but was still felt as a hindrance to production, especially for the marginal mines. In 1948, this duty was replaced by a new form of taxation based on the ratio of profit to recovery and involving a reduction in the tax burden by about 10 per cent.

In Southern Rhodesia, dependent on gold as a source of foreign exchange and especially of dollars, a maximum subsidy of 40s. per ounce was granted to certain low-grade mines as early as in 1946. Then in May 1948 the government announced its intention of paying a subsidy of 27s. 6d. per ounce for all gold produced in the Colony, the cost to be met by a special surcharge of 10 per cent. on all income-tax assessments. And, in connection with this subsidy scheme, the Minister of Finance announced that Southern Rhodesia could no longer accept, without question, the monetary policy of the United Kingdom.

It was at once clear that, through this scheme of uniform subsidy payments, the price of gold was increased in a way which the International Monetary Fund had refused to approve in the case of the original Canadian subsidy scheme (dating from the autumn of 1947). Since Southern Rhodesia was not itself a member of the International Monetary Fund but is closely linked with the United Kingdom, the question arose to what extent the mother country had any responsibility in the matter and what steps could be taken by the International Monetary Fund. It proved possible in the second half of 1948 to reach an agreement between the Fund, the British Government and the Government of Southern Rhodesia regarding a modification of the subsidy scheme which had been put forward. The new scheme of May 1949, which is more complicated, is based on the tonnage milled and the recovery grade for primary treatment, payments being made on a sliding scale ranging from 1s. to 5s. per ton of ore with a recovery grade not exceeding 4 dwts; thereafter, the subsidy will be reduced by 1d. per ton for each additional tenth of 1 dwt., until it finally fades out at a recovery grade of 10 dwts. Mines producing more than 3,000 ounces a month do not qualify for the new subsidy, which will be payable for the first time on the output of June 1949 and which is estimated to cost the taxpayers about £500,000 per annum.

In the Belgian Congo the decline in the output of gold which had begun during the war was reversed in 1948 for the first time, but the financial position of the mines was difficult. To help them, a scheme indicated on page 156 below was set on foot.

Elsewhere, too, the gold-mining industry was growing restive in face of rising costs and difficulties in recruitment of sufficient manpower. The question of subsidies often arose. The International Monetary Fund has asked members to consult with it prior to introducing any new measure to subsidise their gold production. In its annual report submitted in September 1948 it explained that it

"took the position that a subsidy in the form of a uniform payment per ounce for all or part of the gold produced would constitute an increase in price which would not be permissible if the total price paid by the member for gold were thereby raised to any amount in excess of parity plus the prescribed margin of one quarter of one per cent. The Fund emphasised that other types of subsidy may constitute an increase in the price of gold and that each proposal for subsidy must be examined on its merits with regard to its specific provisions and in the light of surrounding circumstances. The Fund stated that any subsidy on gold production, regardless of its form, is inconsistent with Article IV, Section 4 (a) of the Fund Agreement *if* it undermines or threatens to undermine exchange stability."

Movements of Gold.

The main recipient of gold in 1948 was again the United States, although not on the same scale as in the previous year. The following table analyses the changes in the country's gold stock according to the channels through which gold flowed in or out.

United States monetary gold stock:

Analysis of changes.

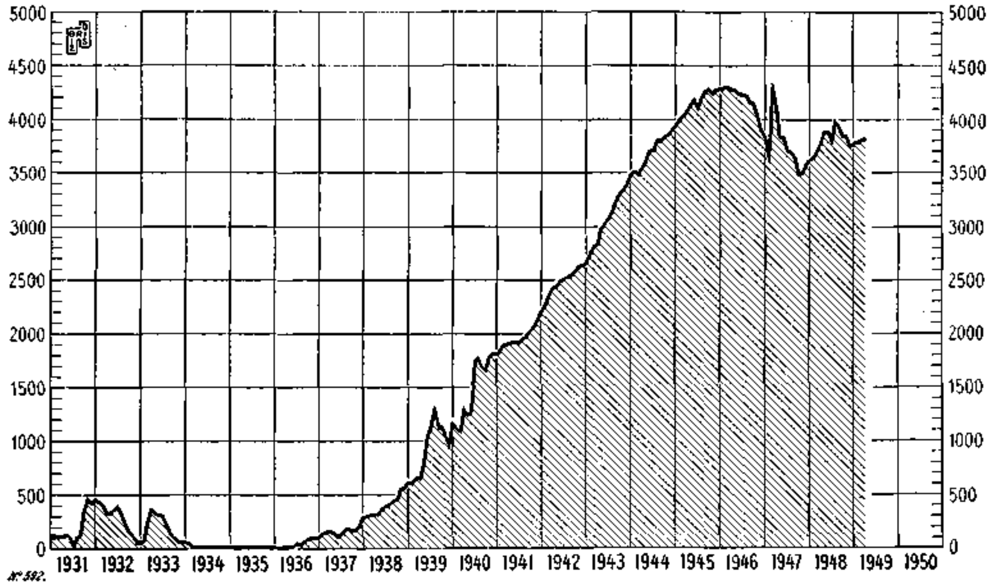
Items	1945	1946	1947	1948
	in millions of dollars			
Net imports (+) or exports (—)	— 106	+ 312	+ 1,866	+ 1,680
Earmarked gold increase (—) or decrease (+)	— 357	+ 465	+ 210	— 159
Total	— 463	+ 777	+ 2,076	+ 1,521
U.S. gold production	+ 32	+ 51	+ 76	+ 74
Other factors	— 123	— 364	+ 73	— 105
Increases (+) or decreases (—) in monetary gold stock	— 554	+ 464	+ 2,225*	+ 1,490
Gold stock at the end of the year	20,065	20,529	22,754	24,244

* This change allows for the transfer of $687.5 million in gold as subscription to the International Monetary Fund; if it had not been for this transfer the increase in the gold stock would have been even more considerable in 1947.

The amount of earmarked gold which other countries hold in the United States was somewhat increased again in 1948, evidently with a view to strengthening their liquid position on the New York market. The amount of gold held under earmark rose to $3,778 million at the end of 1948 but at this figure it was still below the record total — $4,312 million at the end of February 1946.

The main characteristic of the gold movements since the war is that they have not served for the settlement of seasonal deficits in the balance of payments but have been used to secure a transfer of capital required in the country losing the gold because a deficit in its balance of payments may have been caused by a deficit in the current budget or too large a volume of investments or heavy repayments of foreign liabilities. Since the United States

United States: Gold held under earmark
by Federal Reserve Banks for foreign account.*
Monthly, in millions of dollars.



* Including gold held for the account of international institutions. The change in February 1947 reflects primarily gold subscription to the International Monetary fund.

was, in these post-war years, the only country with sufficient resources to sustain a substantial export of capital, the gold would have a tendency to flow to the United States. And, at a time when the United States was furnishing aid (by government loans and grants and private investments) to other countries, it necessarily had a surplus in its balance of payments. This surplus was so large that even the large-scale influx of gold to the United States covered only a minor part of the active balance — less than one-tenth in 1946 and about one-quarter in 1947 and 1948.

In 1947, the U. S. surplus on the current account of the balance of payments was — at $11.3 milliard — greater than the value of all the gold held in reported monetary reserves outside the United States. Obviously, the value and volume of the excess flow of goods and services from the United States was such that a settlement was beyond the capacity and outside the sphere of monetary reserves and could only be effected by appropriate transactions on other accounts. Indeed, the running-down of monetary reserves

**United States:
Current surplus covered by receipt of gold.**

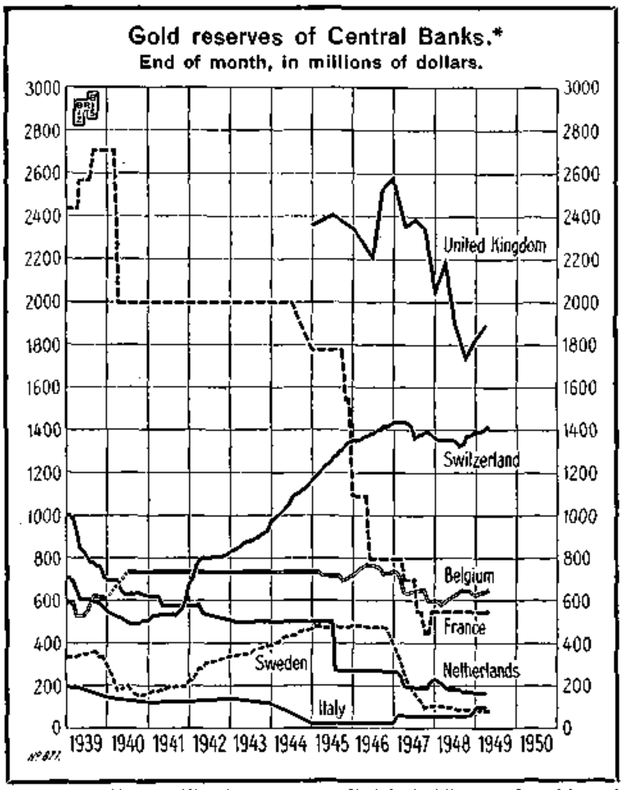
Items	1946	1947	1948
	in milliards of dollars		
U.S. exports of goods and services	15.0	19.7	16.8
U.S. imports of goods and services	7.2	8.4	10.5
Balance . . .	+ 7.8	+ 11.3	+ 6.3
Sale of gold to the United States	0.7	2.8	1.5
Percentage relation between the sale of gold and the active balance on current account	9 %	25 %	24 %

would only create difficult problems for the future, since a country can hardly be said to have regained its economic balance unless it has at its disposal adequate reserves of gold and foreign exchange. In its "Economic Survey for 1948", the British Government explained that

> "from the start of the E.R.P. the Government has been working on the principle that the reserves should be maintained throughout the E.R.P. period at their level at the beginning of the period (3rd April 1948) and thus that dollar outgoings should be limited to dollar income plus external aid."

In a speech of 5th July 1948 the Chancellor of the Exchequer said that on 31st March 1948 the reserves of the United Kingdom in gold, U. S. and Canadian dollars stood at £552 million. Throughout the E.R.P. period there would, he added, be some lag in reimbursement but it was hoped that, even so, it would be possible to keep the reserves at round about the £500 million mark.

In a sense the monetary reserves of the United Kingdom constitute the central reserve for the whole sterling area and, as pointed out in the footnote to the table on page 13, the settlement of the gold and dollar deficit of the United Kingdom takes account of the net position of the whole sterling area through the operation of the changes in external capital assets of the United Kingdom.



Gold reserves of Central Banks.*
End of month, in millions of dollars.

* For the United Kingdom gross official holdings of gold and U.S. dollars as reported by the British Government.

As shown in the same table, the United Kingdom used £152 million of its gold and dollar holdings in 1947 and £55 million in 1948 to cover a part (about one-seventh in each case) of its gold and dollar deficit. £55 million is equal to about $220 million, while the table on page 150 shows a decline by $420 million in the gold holdings of the United Kingdom. The difference is probably to be explained by an increase in the dollar holdings (which seems confirmed by the fact that the total liabilities of U.S. banks in relation to the United Kingdom rose from $326 million at the end of 1947 to $540 million by the end of 1948). In the "Economic Survey for 1949"

Gold reserves of Central Banks and Governments
(including International Institutions)

Reporting Countries	End of 1938	1944	1945	1946	1947	1948	Loss (—) or gain (+) during 1948	1938–1948
	in millions of U.S. dollars							
United States (1)	14,512	20,619	20,065	20,529	22,754	24,244	+1,490	+9,732(1)
Venezuela	54	130	202	215	215	323	+ 108	+ 269
Italy	193	24	24	28	28(2)	66(2)	+ 38	— 127(2)
Switzerland (3)	701	1,159	1,342	1,430	1,356	1,387	+ 31	+ 686
Belgium (4)	728	732	716	735	597	624	+ 27	— 104
Cuba	•	111	191	226	279	289	+ 10	+ 289
Hungary	37	24	24	24	34	35	+ 1	— 2
Canada (5)	192	6	7	7	7	8	+ 1(5)	— 184(5)
Austria	88	0	0	0	5	5	0	— 83
Egypt	55	52	52	53	53	53	0	— 2
Spain	525(6)	105	110	111	111	111	0	— 414
New Zealand	23	23	23	23	23	23	0	0
Peru	20	32	28	24	20	20	0	0
Denmark	53	44	38	38	32	32	0	— 21
France (7)	2,430	1,777	1,090	796	548	548	0	—1,882(7)
Iran	26	128	127	149	142	140	— 2	+ 114
Chile	30	79	82	65	45	43	— 2	+ 13
Turkey	29	221	241	237	170	162	— 8	+ 133
Uruguay	73	157	195	200	175	164	— 11	+ 91
India	274	274	274	274	274	256	— 18	— 18
Colombia	24	92	127	145	83	65(8)	— 18	+ 41
Norway	84	54	80	91	75	53	— 22	— 31
Sweden	321	463	482	381	105	81	— 24	— 240
Brazil	32	329	354	354	354	317	— 37	+ 285
Mexico	29	222	294	180	100	44(9)	— 56	+ 15
Netherlands	998	500	270	265	232	167	— 65	— 831
Argentina	431	992	1,197	1,072	322	131	— 191	— 300
United Kingdom (10)	2,690(11)	1,855	1,995	2,415	2,030	1,610	— 420	—1,080
South Africa	220	814	914	939	762	183	— 579	— 37
International Monetary Fund	—	—	—	15	1,356	1,436	+ 80	+1,436
Bank for International Settlements	14	37	39	32	30	36	+ 6	+ 22
Reserves: (12) Reported	25,700	32,000	32,100	32,500	33,500	34,000	+ 500	+8,300
Unreported	*	4,300	4,900	4,900	4,500	4,600	+ 100	*
Total	*	36,300	37,000	37,400	38,000	38,600	+ 600	*

(1) Not including gold held in the Exchange Stabilization Fund: $80 million end of 1938, $12 million end of 1944, $18 million end of 1945, $177 million end of 1946, $114 million end of 1947 and $154 million end of 1948.
(2) Not including $30 million gold kept in the U.S.A. for the purpose of the subscription to I.M.F.
(3) Including gold owned by the Swiss Government.
(4) Not including gold held by the Treasury: $44 million end of 1938 and $17 million end of 1944 and 1945.
(5) In May 1940, gold belonging to the Bank of Canada was transferred to the Foreign Exchange Control Board. Since then gold reported is gold held by the Ministry of Finance. Gold held by the Foreign Exchange Control Board amounted to $354 million end of 1945, to $536 million end of 1946, to $287 million end of 1947, and to $401 million end of 1948.
(6) End of April 1938.
(7) Not including gold held by the Exchange Stabilisation Fund and the Caisse Centrale de la France d'Outre-Mer: $331 million end of 1938, $214 million end of 1944, $457 million end of 1945, $77 million end of 1946, $8 million end of 1947 and $3 million end of 1948.
(8) End of June 1948.
(9) End of August 1948.
(10) Partly estimated.
(11) Not including gold held by Exchange Equalisation Account: $759 million end of September 1938.
(12) Partly estimated, and including other countries.

the gold and dollar holdings of the United Kingdom at the end of 1948 were given as £457 million (equal to $1,840 million, as compared with gold holdings on the same date amounting to $1,610 million).

In the first half of 1948 the United Kingdom received a gold loan of £80 million from the Union of South Africa which, with gold reserves exceeding £SA 187 million at the end of 1947 and its current gold production running at the rate of about £SA 100 million, still appeared to be in an excellent position; but heavy investment expenditure within the country was stimulating imports, while the exports of gold from current production, sold at the fixed price, covered a steadily falling percentage of imports at rising prices. *Excluding all gold shipments, the current deficit in 1948 in the* balance of payments was estimated at about £SA 260 million, of which £SA 81 million was in relation to the sterling area and £SA 179 million vis-à-vis other countries (chiefly the dollar area). It is estimated that the net capital inflow still amounted to £SA 75 million, while the current output of gold available for monetary purposes yielded, as mentioned above, £SA 99 million, after which there still remained a deficit of £SA 86 million. South Africa made good this deficit by drawing on its gold reserves to the extent of £SA 62 million and on its exchange reserves to the extent of £SA 24 million, while buying about $8 million (say, £SA 2 million) from the International Monetary Fund. In all, the combined gold and foreign exchange reserves of the South African Reserve Bank, the commercial banks and the Union High Commissioner in London declined by £SA 164 million during 1948.

To cope with the internal situation, the minimum reserve of gold which had to be kept against notes and other sight liabilities of the South African Reserve Bank was reduced from 30 to 25 per cent. in the autumn of 1948 and, for the purpose of calculating the percentage, the bank was permitted to deduct from its liabilities to the public an amount equal to its foreign assets. Furthermore, in March 1949 it was reported that the South African Government had requested the British Government to repay, in sterling, a part of the £80 million gold loan and that the United Kingdom had transferred sterling funds to the value of roughly £5 million to the Union Government as redemption payment. Repayment in sterling continued in April, when it was announced that further repayments would be dependent upon the state of the Union's trade balance with the sterling area. As mentioned on page 11, trade and exchange control had already been introduced in South Africa in November 1948.

How South Africa has been affected since 1940 by the fall in the output of gold, and the fact that it has to be sold at a constant price although the general level of commodity prices has doubled, may be illustrated by the following comparison; in 1940 the value of the gold exported from South Africa (in all, 10.7 million ounces) represented about two-thirds of the country's exports and financed 85 per cent. of all imports but in 1948 the export of gold derived from current production represented only 33 per cent.

of all exports and covered 28 per cent. of total imports. That is the obvious reason why the South African Government has sought to obtain higher prices for at least a part of the newly-produced gold.

Other gold-producing countries are exposed to similar difficulties resulting from the decline in the purchasing power of gold. Thus, in the Belgian Congo the percentage of gold exports fell from 24 per cent. of total exports in 1940 to 4 per cent. in 1948 and in the Gold Coast Colony from 53 per cent. in 1940 to 20 per cent. in 1947.

Among natural resources, petrol has clearly proved a more valuable asset than gold in recent years — witness the fact that, after the United States and Canada, Venezuela is the country which in 1948 added most to its gold reserves (viz. the equivalent of $108 million).

Cuba, with its sales of sugar to the U.S. market, had also a current surplus in its balance of payments and thus registered an increase of $10 million in its gold holdings. In fact, most of the republics in the Caribbean area have export surpluses in relation to the United States and also receive many American visitors, while trade with Europe has been sagging and is no longer of primary importance. These countries have generally been able to maintain their reserve position, an exception being Mexico. The gold reserves of that country, after reaching $294 million by the end of 1945, had been reduced to $100 million by the end of 1947 and the latest available figure is for August 1948, when they were down to $44 million. At that size they could no longer serve as a decisive factor in the management of the exchange, and in the course of 1948 and at the beginning of 1949 several adjustments were made in the rate of the Mexican peso (see page 128).

At the end of the war, all the Latin American republics together held about $4,000 million in gold and foreign exchange (at the time mostly dollars) but of this about $1,400 million had been used up by the end of 1948. Mexico's share in the amount thus used represented about $250 million but a much greater loss was suffered by the Argentine, whose reserve of gold alone went down from $1,197 million at the end of 1945 to $131 million at the end of 1948 — a reduction by 90 per cent. Chile has lost 50 per cent. — a drop from $82 million at the end of 1945 to $43 million at the end of 1948 — while Brazil and Uruguay have only lost between 5 and 10 per cent.

But for the Latin American countries in general the size and the composition of their exchange holdings are particularly important. Thus, at the end of June 1948, their total gold holdings came to about $1,600 million, while the exchange holdings were returned at the equivalent of $1,350 million. Besides amounts of U.S. dollars which were still substantial, the latter total included European currencies (not only sterling but others as well) and, while these currencies could not as a rule be converted into dollars, they served to maintain trade with the continent of Europe, this being especially so for the countries south of the Caribbean region. For Brazil the proportion of trade handled with the United States is still fairly high (sales of coffee); but, before the war, often less than 10 per cent of the export trade of the Argentine and Uruguay, consisting mostly of foodstuffs, was with the United States. For Europe and for these countries themselves it is of importance that Europe can once more furnish the goods they need; and the table on page 92 showed that in the second half of 1948 the O.E.E.C. countries were able to reduce by one-half their combined import surplus in relation to South America, as compared with the three previous half-yearly periods.

Outside the countries already mentioned, neither the losses nor the gains of gold were absolutely or relatively of any great importance in 1948. For one thing, the availability of Marshall aid made it less imperative to draw on reserves, and that not only because the aid paid for imports but also because it permitted the re-establishment of a better balance internally, gradually ensuring a cessation of inflationary tendencies. Two among the E.R.P. countries were even able to augment their gold reserves during the year — Italy, to the extent of $38 million, and Belgium, to the extent of $27 million. The movements in the balance of payments which led to this addition are set out for Italy on page 81 and for Belgium on page 83. Particular account should also be taken of the fact that in the two countries the governments have been chary in providing funds for reconstruction and that private investment has been kept back by a somewhat restrictive credit policy, including the application of higher interest rates. Without such a policy the monetary reserves would not have been replenished — and it may, indeed, be said that countries have, to some extent, had a choice between launching substantial programmes of internal investment and concentrating on a restoration of their monetary position. Those countries which have chosen the second alternative, however, will very likely, in years to come, experience the need of foreign capital to supplement domestic savings as they go ahead with reconstruction and modernise their economic equipment.

For Europe as a whole the monetary reserve position is, as yet, in no way assured. At the end of 1938 Europe (without the U.S.S.R.) had gold reserves amounting to about $10,400 million. Ten years later, by the end of 1948, the corresponding reserves were about half as high — not exceeding $5,300 million. The United Kingdom has a little more than halved its holdings (from $3,450 million at the end of September 1938 to $1,610 million at the end of 1948) while Switzerland has practically doubled its holdings (from $700 million at the end of 1938 to $1,390 million at the end of 1948). These two countries, together with Belgium, now hold $3,620 million or 70 per cent. of Europe's gold. The gold reserves of the Bank of France amount to $548 million. For some of the other countries also, the amount of gold held must be said to be offset by the existence of liabilities in clearing accounts and under similar arrangements.

The insistence of the British Government on the need of adequate gold reserves at the end of the Marshall aid period might be echoed by other countries and this circumstance may well become a consideration of growing importance in the framing of immediate financial and economic policy.

Gold outside monetary reserves.

When gold coins formed part of a country's circulation and were actually utilised as means of payment there could, of course, be no question but that such gold had to be counted as part of the monetary stock (originally it was the monetary stock). Now, an actual circulation of gold coins freely exchangeable at par with the paper currency is nowhere to be found but there are still places where gold coins of various kinds and denominations (often of foreign provenance) are not only widely held by the public but actually used to pay for goods and services as well as for the acquisition of capital assets. In such cases, the gold obviously performs monetary functions as a means of payment and a store of value. Hoarded gold is probably looked upon essentially as a store of value, but only because it is known or believed that there will always be somebody else willing to exchange assets against it — and there is even the additional consideration that it might prove especially useful as a means of payment in an emergency. It is probably a matter of fine distinctions whether such gold could be regarded as part of the monetary stock. In statistical analyses it is normally left out, since it is becoming increasingly the practice to exclude all gold outside the centralised monetary reserves, it being clearly impossible to specify any marks which can be used for distinguishing different kinds of gold held by the public. Refinements in those fields do not serve much purpose, since it is hard enough to obtain even approximate information about the total amounts involved.

Among the countries in western Europe, the propensity to hoard gold has probably been strongest in France; the French people, remembering the old gold franc introduced by Napoleon in 1803 (the so-called "franc germinal"), which maintained its value intact up to 1914 and thus withstood the strain of two lost wars — 1814 and 1871 — as well as a number of other vicissitudes, cannot help thinking that, compared with the paper franc which since 1914 has lost 99 per cent. of its purchasing power, gold, irrespective of any short-term fluctuations in the price paid for it, is in the long run a trustworthy basis for savings.

It is not possible to estimate exactly the amount of gold held privately within France but a recent calculation * has put the amount of

* The calculation appeared in an article entitled "L'or de la France", in "Perspectives" of 19th February 1949. It was estimated that:

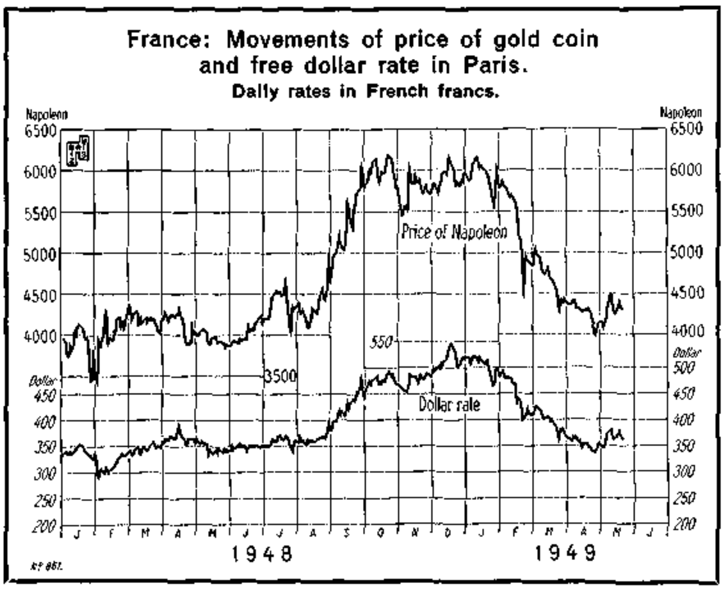
(i) in 1931, when after the prosperous years from 1926 to 1930 hoarding was resumed in France, the amount of gold held by the public was 250 tons, at most;

(ii) at the beginning of 1938 the amount in question had risen to 600 tons, with an addition of perhaps 150 tons in 1938 and probably more in 1939;

such gold held at the beginning of 1949 at approximately 2,000 tons (as compared with 1,750 tons held mainly in the form of gold coins by the French public immediately before the first world war, i.e. at a time when, as a means of payment, gold in the form of coins was as important as notes).

2,000 tons of fine gold has a value of about $2,200 million (at $35 per ounce), to which a certain amount should be added in respect of gold held by Frenchmen in foreign countries. An estimate referring to the time of the Liberation put such gold at a figure of 2 milliard 1914-francs, which would be equal to about 600 tons. It is not easy to tell whether since 1945 the amount of gold thus held has risen substantially or not, since part of it may have been brought home to France. It would seem, however, as if the privately-held gold, all told, would amount to around $2,500–3,000 million.

In France the trade in gold is predominantly in "napoleons", the price of which has regularly been above that paid for other gold coins of the Latin Union and as much as 25 and even 30 per cent. above the price for bullion. Great variations in the quotation have taken place (see the table on page 120). Early in 1946 the "napoleon" sold at more than Fr.fcs 6,000 but by the first half of 1947 the price had declined to Fr.fcs 2,500 (this being at a time when the Swiss authorities sold gold coins on the market of their country). In the course of 1948 the price again went beyond Fr.fcs 6,000, only to fall back to about Fr.fcs 4,300–4,500 in connection with the successful issue of the Reconstruction Loan in February-March 1949 and the manifest improvement in France's economic and financial position, the price dropping even to Fr.fcs 4,000 by the end of April 1949.



France: Movements of price of gold coin and free dollar rate in Paris.
Daily rates in French francs.

In February 1948, a free gold market was opened first in Paris and afterwards in a number of important provincial towns. The transactions partly represent change in ownership of gold already in France and partly the sale of gold

(iii) at the beginning of the second world war, the amount of gold held privately by the French public was thus about 1,000 tons;
(iv) through further influx during the war, the amount was increased to about 1,250 tons at the time of the Liberation; and
(v) through additions in the years 1945–48, the stock was brought up to 2,000 tons at the beginning of 1949.

which has been brought in (through smuggling or otherwise) from foreign countries. Since the beginning of 1949 some gold has also come from the French mines in Africa, the reason being that permission had been given to sell 50 per cent. of the production on the free Paris gold market and the remaining 50 per cent. on foreign markets, with the obligation to repatriate the foreign exchange proceeds resulting from sales abroad; and in April 1949 it was announced that the whole gold output could be sold on the French markets.

In Belgium no free gold market has been established but an authorisation has been given for 40 per cent. of the gold produced in the Belgian Congo to be sold for industrial purposes at prices higher than the official price.

Since for the purposes of the International Monetary Fund the French and Belgian overseas territories form part of their respective mother countries, the sales of colonial gold on the free market or, in the case of Belgium, above parity have been regarded as "internal movements of gold" and thus not contrary to the principle announced by the Fund in its statement of 24th June 1947, in which the Fund made it known that it "strongly deprecates international transactions in gold at premium prices and recommends that all of its members take effective action to prevent such transactions in gold with other countries or with the nationals of other countries".

For the International Monetary Fund a more difficult problem arose when in February 1949 the government of the Union of South Africa, after rejecting devaluation as a way out of the country's financial difficulties, announced that it had contracted to sell gold for non-monetary purposes to a leading firm of London bullion brokers at the rate of 12,500 ounces of gold weekly for eight weeks and at a price of $38.20 per ounce, payment to be made in dollars. After discussions between the South African Government and the International Monetary Fund, an agreement was reached in May 1949 in accordance with which the Union might sell fully fabricated gold as well as semi-fabricated gold at a premium to manufacturers. As long as the Union took care that the gold was fully fabricated before export, the Fund would raise no objection to the Union's participation in this trade. As regards sale of semi-processed gold, the Union would be entitled to export such gold provided that the transaction took place exclusively with the manufacturer and that certain other conditions were fulfilled (presentation of import licences from the manufacturer's country, etc.).

The arrangement between the International Monetary Fund and the South African Government thus admits the applicability of special prices to gold genuinely used for industrial purposes. In the United States, where the authorities have refused to restore a free market for gold, there have been dealings, however, in unrefined gold which was not covered by the regulation that "gold in its natural state (i.e. gold recovered from natural sources which has not been melted, smelted, or refined or otherwise treated by heating or by a chemical or electrical process) may be acquired, transported within the United States, imported, or held in custody for domestic account without the necessity of holding a licence therefor".

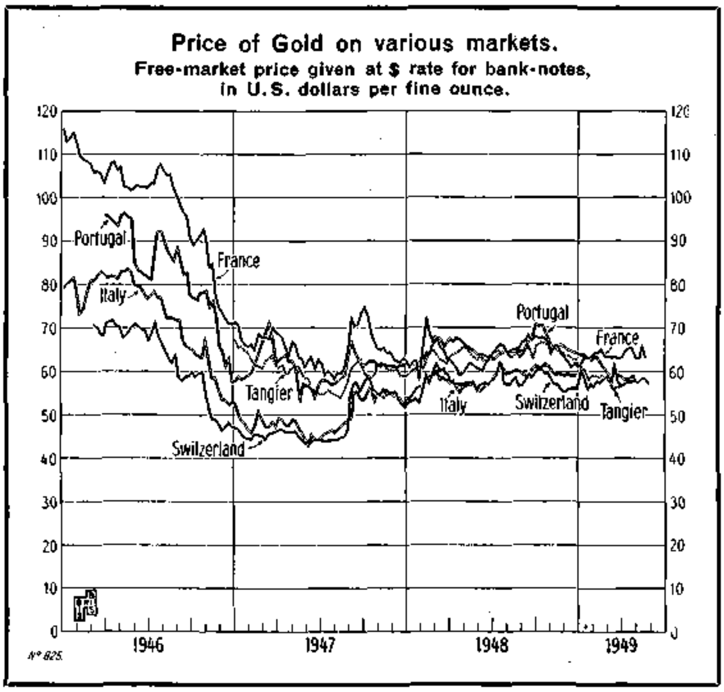
The selling price of such gold in the United States has been reported to be about $39 per ounce of non-refined gold of an assay of 85 per cent., which corresponds to about $46 per fine ounce.

Even higher prices have been quoted in some other parts of the world. A distinction has to be made, however, between sales against actual dollars and sales against various national currencies; in the latter case, conversion at official rates of amounts paid for gold sometimes gives prices of $90 per fine ounce and even more, but then the gold price partly reflects a free (or black) market valuation of the national currency in question.

In the East, where fear of inflation has gone hand in hand with political uncertainty, very high prices have been paid for gold, especially since supplies have been curtailed. In April 1949 the famous free gold market in Hong Kong, which had been one of the most active premium-gold markets in the world, acting as a transhipment point for China, was suppressed by a decision of the colony (it being presumed that the decision was taken after contact with London and in consequence of the principles proclaimed by the International Monetary Fund).

Switzerland, also, has seen fit to take steps to prevent the use of its transport and other facilities for international movements of gold. It had become more and more common for use to be made of free-port depots and transit certificates, a practice which, under the regulations then in force, required no authorisation from the Swiss National Bank. To obtain sufficient control the Swiss Government decided in December 1948 to extend the application of certain earlier regulations (of 7th December 1942) in such a way that not only imports and exports but also gold in transit would be subject to authorisation by the Swiss National Bank.

While in Europe the free transactions in gold are, in principle, being *limited to "internal movements", new transit markets in gold are growing* up elsewhere, e.g. in Beirut and Macao. The governments of Syria and Lebanon decided to authorise the free transport of gold through their territories without imposing any stipulations regarding declaration of destination and the means of transport employed. And Egypt continued to be an important gold market. In the December number of the Economic Bulletin of the National Bank of Egypt it was stated that the supply of sovereigns in Cairo had been ample since the oil companies in Saudi Arabia had begun paying royalties in sovereigns early in 1948, and that considerable quantities were being disposed of in the Egyptian gold market Musky, as the nearest free gold market. The same source added that the main supplier of newly-mined gold to the Musky market had been Ethiopia but that imports from that country had recently ceased.



Other free gold markets are Milan, Tangier, Casablanca, Algiers and Bombay but, owing to the various difficulties of transport and trading, arbitrage does not readily work. From India it was reported that the current gold output on the usual scale was readily absorbed by the market; besides this, gold flowed into the country from abroad through legal and illegal channels. In China another abortive monetary reform in 1948 made people turn increasingly to precious metals; in February 1949 the government announced a series of reforms providing, inter alia, for a free market in silver and gold and the selling of bullion by the central bank whenever necessary to stabilise the market.

* * *

The high prices paid for gold by the public in free and clandestine transactions are influenced predominantly by two factors: on the one hand, the monetary and economic conditions of the country in question, and, on the other hand, the current supply of gold available for sale to the public.

One difficulty in arriving at any firm conclusions as to the importance of these "free" quotations is that the reaction of the public in these matters varies considerably from country to country. In the United States, for instance, there is only a very small section of the population which pays any attention to the higher prices quoted for gold in its natural state and which would even remotely entertain the idea that the real value of the dollar might be affected by such quotations. In fact, the average American seems to be more apprehensive of the possibility of a devastating deflation than of any strong inflation affecting the dollar.

There are also some other countries in which the public is not at all "gold-minded", being completely unmoved by any separate quotations for gold as in any way influencing the value of their national currency. To this group of countries belong, besides the United States, the United Kingdom and, among others, the northern countries, Denmark, Norway and Sweden. In these countries gold is regarded as a valuable asset useful for the settlement of international commitments, and it is the level of prices and the flow of funds, not the quotations for a certain weight of gold, that are regarded as significant for the intrinsic value of the currencies concerned.

There are other countries, however, in which the public has not the same detached attitude. Having had the experience of strong doses of inflation once, twice or, maybe, even more often in the same generation, it looks upon the quotations of very high prices for gold as a sign that the national currency is discredited, and it pays particular attention to "free" quotations existing side by side with the "controlled" exchange rates.

It may be true that the free and clandestine gold markets are often very narrow and, therefore, subject to special influences of supply and demand but the prices quoted in those markets cannot be wholly overlooked — and there is, therefore, a problem of how to treat them correctly.

Clearly one possibility is to arrange for increased supplies of gold in the hope that the price will then fall and people be less keen to buy — as is usually the case in a falling market and as, indeed, happened in France up to the middle of 1947, when gold was to a certain extent being brought in from Switzerland where it had been sold to the public by the Swiss National Bank and by the Finance Department in Berne. But, at the moment, no single principle is universally applied with regard to unofficial trading in gold. On the one hand, there is the prohibition against "international movements" of gold, mentioned on page 147 above. This prohibition was imposed because it was thought that unofficial trading, when permitted on an international scale, would be injurious to the maintenance of exchange stability and lessen the possibilities of strengthening monetary reserves. The suppression of the free market in Hong Kong is a typical instance of this tendency to prevent unofficial movements of gold between different countries and continents.

On the other hand, gold is being made increasingly available for industrial uses by the granting of permission to gold producers to sell at least part of their output at unofficial prices either to manufacturers of articles made from gold or directly on free markets. In that way particular sectors of demand are being supplied and, at the same time, dealings in gold are being allowed more freedom on some domestic markets (involving only "internal movements").

In the spring of 1949 there were some new developments with regard to sales of gold by South Africa and other countries, as mentioned earlier in this chapter, and it is possible that, in the light of the attitude thus adopted, the principles governing unofficial trading in gold will be further clarified.

The present industrial demand for gold, which is more intense than in normal times, reflects in part a lack of monetary confidence in not a few currencies. It is evident that, notwithstanding the progress made in overcoming inflationary tendencies, the demand for gold objects as well as the high unofficial prices quoted for gold are influenced by the monetary uncertainty which still prevails. There can thus be no doubt that the restoration of greater confidence in the various currencies would go a long way towards closing the gap between the official and the free (or clandestine) market quotations for gold.

It is not possible to tell in advance to what extent further progress in restoring monetary confidence will lead to a disappearance of the special gold prices and, therefore, help to solve this whole problem. It is, in particular, difficult to foresee the strength of the Eastern demand for gold and what influence such demand may exert on markets in the Western world. But, since action with a view to the restoration of monetary confidence will continue in any case, a most careful watch must obviously be kept on the effects which progress in this field has upon the quotations on the free and clandestine markets — a case in point being the marked fall in the price of gold on the French market in the early months of 1949.

In addition to the particular problems occasioned by the special prices thus quoted for gold, there is, as often pointed out, a wider question of the possible influence that the price of gold may exert in different respects and especially with regard to the trend of commodity prices — a question on which, it should be added, there is a great difference of opinion. As always in time of war, it was the volume of government expenditure, rather than variations in the supply of gold and the credit policy of the banks, that determined the movement of prices up to 1945; and in a number of countries the price trend is still affected by the aftermath of war financing, with all that this involves with regard to the relative values of currencies and the possibility of attaining a more stable price level all round at a time when government expenditure is still very high and investment needs are great.

These are obviously the problems claiming first attention. It would certainly be a mistake — since it would only involve unnecessary delay — if any solution that should be arrived at in the field of currency values or other similar questions were to be held up in expectation of a general change in the price of gold.

VII. Internal Credit conditions, the trend of Interest Rates and the use of Counterpart Funds.

Great progress towards financial stability was made in 1948 in practically every country and it is likely that 1948 will go down in economic history as the year in which post-war inflation came to an end almost everywhere. Not all countries succeeded in completely closing the gap between their total spending (for consumption and investment) and the total available resources, as derived from current production and financial assistance from abroad. But even those countries which could not wholly close the gap were able to move decidedly nearer to a balanced position, especially towards the end of the year. In the late autumn of 1948 prices began to decline even in a country such as France, where the year as a whole had still been one of rapid inflation; and this may well be taken as a sign of a distinct break with the ways of inflationary financing.

The methods used to achieve financial equilibrium varied according to the institutional framework within which the authorities operated and the financial practices employed in the individual countries. Three main groups are distinguishable:

(i) In countries in eastern Europe, with a fully planned economy based on state ownership, it is, of course, still necessary — if balance is to be maintained — for investments to be covered by genuine savings through a surplus in the budget, surplus gains by nationalised enterprises and such voluntary savings as are forthcoming, eked out by aid from abroad. Since savings involve a reduction of current expenditure, strict "austerity" may have to be imposed to generate the necessary capital-formation, especially in countries with a relatively low average income per head.

(ii) The United Kingdom, the Netherlands, Norway and Sweden form another group, whose policy has been characterised by the application of comprehensive investment controls (together with the maintenance of foreign trade and exchange control) as well as reliance on fiscal policy, which in the United Kingdom and Sweden has procured increased savings through a budget surplus.

(iii) In a third group of countries including Belgium, France, Italy and Germany, investment control is either non-existent or ineffective. Measures had, of course, to be taken to balance the budget but, in addition, reliance was placed mainly on monetary policy in a narrower sense, i.e. an increase in interest rates, together with qualitative and quantitative credit restrictions for the purpose of adapting the monetary purchasing power to the actual level of national production.

It is not possible to bring every country into one of these groups. Switzerland and the United States both had substantial budget surpluses in 1947–48, which were helpful in ensuring financial stability, but in neither country was there any application of investment control.

As regards the movement of interest rates, no general tendency can be found in 1948.

Discount rates of central banks.

Central Bank of	Discount rates at the end of							Change from Dec. 1947 to May 1949
	1929	1938	1945	1946	1947	1948	May 1949 *	
United States (1)	4½	1	½	1	1	1½	1½	+ ½
Canada	.	2½	1½	1½	1½	1½	1½	.
Switzerland	3½	1½	1½	1½	1½	1½	1½	.
England	5	2	2	2	2	2	2	.
Czechoslovakia	5	3	2½	2½	2½	2½	2½	.
Ireland	6	3	2½	2½	2½	2½	2½	.
Netherlands	4½	2	2½	2½	2½	2½	2½	.
Norway	5	3½	3	2½	2½	2½	2½	.
Portugal	8	4½	2½	2½	2½	2½	2½	.
Sweden	5	2½	2½	2½	2½	2½	2½	.
France	3½	2½	1⅝	1⅝	2½	3	3 (2)	+ ½
Yugoslavia	6	5	3	2½–6 (3)	1–4	1–3	1–3	nil to — 1
Austria	7½	4	3½	3½	3½	3½	3½	.
Belgium	4½	2½	1½	3	3½	3½	3½	.
Denmark	5	4	4	3½	3½	3½	3½	.
Bulgaria	10	6	5	4½	4½	3½	3½	— 1
Turkey	.	4	4	4	4	4	4	.
Spain	5½	4	4	4	4½	4½	4 (4)	— ½
Italy	7	4½	4	4	5½	5½	4½ (5)	— 1
Germany	7	4	3½	3½	3½	5 (6)	4½ (7)	+ 1
Hungary	7½	4	3	7	5	5	5	.
Roumania	9	3½	4	4	7	6	5	— 2
Albania	9	6	5½	5½	5½	5½	5½	.
Poland	8½	4½	4½	4½	6	6	6	.
Finland	7	4	4	4	5¼	7¼	6¾ (8)	+ 1½
Greece	9	6	7	10	10	12	12	+ 2

* At the end of March 1949, the following rediscount rates were in force: Danmarks Nationalbank: 3 per cent., National Bank of Poland: 3½ per cent., Bank of Portugal: 2 per cent., Bank of Spain: 3.20 per cent. and Sveriges Riksbank: 2 per cent.

(1) Rates of Federal Reserve Bank of New York for advances secured by government obligations and for discounts of, and advances secured by, eligible paper. For other secured advances: 2 per cent.

(2) During the period between 4th and 29th September 1948 the rate for public securities and bills representing sales was 3½ per cent. and the rate for other commercial bills 4 per cent.

(3) Since the amalgamation of institutions of the public sector with the National Bank, differential rates have been introduced according to the type of debtor.

(4) In effect since 18th March 1949.

(5) In effect since 9th April 1949.

(6) Since 28th June 1948 the discount rate for Länder central banks has been 1 per cent.

(7) In effect since 27th May 1949. The Berliner Zentralbank also lowered its discount rate to 4½ per cent. on 1st June 1949 and the Deutsche Notenbank in the Soviet Zone from 6 to 5 per cent. on the same date.

(8) In effect since February 1949.

Switzerland maintained the official discount rate unchanged at 1½ per cent. but its long-term rates were allowed to fluctuate according to the supply of and demand for funds in the market; from the middle of 1947 to the spring of 1948 long-term rates rose by about ½ per cent., the yield of Federal government bonds attaining a level of about 3½ per cent. But a decline then set in (aided by repatriation of capital, largely from the United States) and by the spring of 1949 the corresponding long-term rates had fallen to about 2¾ per cent.

Such a degree of flexibility (with rates moving freely up and down from one period to another) has, however, been an exception.

In eastern Europe the rate structure varies considerably from country to country. In Czechoslovakia and Yugoslavia the rates charged by banks for advances to enterprises have been related to the official discount rate of 2½ per cent. in Czechoslovakia and to a multiple-rate structure of 1 to 3 per cent. in Yugoslavia.* But in Hungary the discount rate is 5 per cent. and in Poland 6 per cent.

Fairly high interest rates, at 7 and 8 per cent. (or even more), are charged for bank credits in Italy, Germany and Finland — and somewhat lower rates in France. The relatively high level of interest rates has undoubtedly been helpful in checking demand for bank loans — but in each of these countries the interest-rate policy has been reinforced by qualitative and quantitative credit restrictions.

In the countries applying comprehensive investment control — the United Kingdom, the Netherlands, Norway and Sweden — interest rates have been kept low. In Sweden this has been done by support purchases of government bonds by the central bank; in the Netherlands and Norway more by the continuing high liquidity of the whole financial system; and in the United Kingdom (where, however, a rise in long-term rates occurred in 1948) by the weight of money in the market, as fed by a variety of capital transactions on the part of the Treasury.

* * *

The forces which since the end of the war have brought about an expansion of the money supply in the United States, and have thus been largely responsible for the general price rise in that country, were still operative through most of the year 1948. The Federal Reserve System, in co-operation with the Treasury, consequently continued its policy of hardening credit conditions in the money market until a change in the general trend of business led, in the spring of 1949, to a reversal of the credit policy.

Three main factors threatened to sustain the inflationary tendency in 1948:

Firstly, the demand for bank loans on the part of business continued to increase during the greater part of the year.

Secondly, inflow of gold amounting to $1,490 million in 1948 increased deposits and provided the banks with reserves for credit expansion.

Thirdly, non-bank investors, particularly insurance companies and other institutional

United States: All commercial banks.

End of	Loans	Total investments	Cash assets	Total of deposits *
	in millions of U.S. dollars			
1946 December . .	31,122	82,671	34,223	126,377
1947 December . .	38,057	78,226	37,502	131,071
1948 December . .	42,690	71,620	37,480	129,420
1949 March	42,310	70,130	34,100	125,340

* Excluding interbank deposits.

* The rates thus quoted may, however, be partly artificial, since in Yugoslavia, for instance, the rate paid on savings deposits has been as high as 5 per cent. For consumers' short-term credit it varies between 1 and 5 per cent.

investors, shifted from government securities into higher-yield corporate securities and mortgages; and the commercial banks themselves sold government bonds in order to switch over to bank loans and obtain additional reserves. The securities sold by these institutional investors were bought largely by the Federal Reserve System in pursuance of its policy of supporting the prices of medium and long-term government bonds. These purchases, like the gold influx, increased commercial-bank deposits and at the same time improved the reserve position of the commercial banks. The total of bonds bought by the System in 1948 amounted to $8.1 milliard. Purchases, however, practically ceased in November; and from the beginning of December the bond holdings of the System began to decline again.

United States: Reserve Bank credit outstanding.

End of month	Discounts and advances	U.S. government securities			All other items*	Total
		Bonds	Bills, certificates and notes	Total		
	in millions of U.S. dollars					
1947 December	85	2,853	19,706	22,559	536	23,181
1948 December	223	10,977	12,356	23,333	542	24,097
1949 March	299	9,276	12,552	21,828	251	22,378

* Includes industrial loans and acceptances purchased.

Several steps were taken by the Federal Reserve Banks and the Treasury in order to offset the effects of these factors on the supply of money:

(i) The Treasury used its cash surplus of $8 milliard in the calendar year 1948 largely to redeem public debt held by the Federal Reserve System. As can be seen from the above table, the decline in short-term securities held by the System almost completely offset the increase in the bond holdings.

(ii) The Board of Governors raised reserve requirements three times during the year. In February and again in June the reserve requirements in respect of net demand deposits at the two "central reserve cities", New York and Chicago, were raised by two percentage points each time. In August the Board was granted additional power to raise reserve requirements by four percentage points for net demand deposits and 1½ percentage points for time deposits. In September the Board, making use of these new powers, raised the requirements on net demand deposits by two percentage points and on time deposits by 1½ percentage points. These increases required approximately $3 milliard of new reserves.

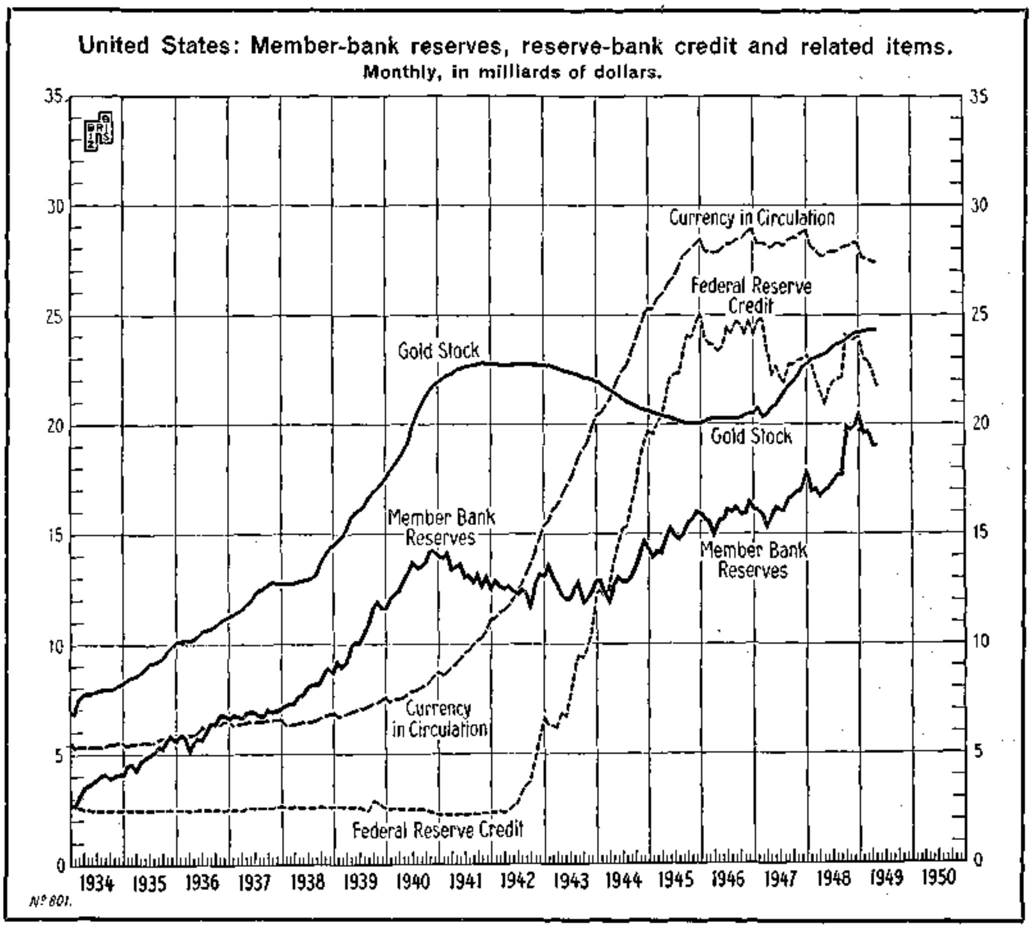
(iii) In order to increase the attractiveness of short-term government securities a further rise in short-term rates was agreed to in 1948. In September the Treasury announced the offering of 1¼ per cent. one-year certificates for the certificates and the notes maturing on 1st October and 1⅜ per cent. 18-month notes in exchange for notes maturing on 15th September. Rates on Treasury bills and other short-term securities fell into line with the higher rates on these two types of securities.

(iv) Finally, the rediscount rate was raised in August 1948 from 1¼ to 1½ per cent.

Yields of U.S. government securities.

Date	3-month bills	9 to 12-month certificates of indebtedness	3 to 5-year taxable issues	15 years and over
	in percentages per annum			
1946 average	0.375	0.82	1.16	2.19
1947 „	0.604	0.88	1.32	2.25
1948 „	1.043	1.14	1.62	2.44
1948 June	0.998	1.09	1.49	2.41
„ September	1.090	1.18	1.69	2.45
„ December	1.154	1.21	1.64	2.44
1949 March	1.162	1.22	1.54	2.38

These policies succeeded in preventing a further expansion of commercial bank deposits; at the end of 1948 they were $2.8 milliard below the level at the end of 1947. And, for the first time since 1937, the total supply of money (as measured by adjusted demand deposits and currency in circulation) ceased to rise and even declined somewhat. The fall continued in the early months of 1949, but this decline reflects, in part, the usual seasonal fluctuation in the supply of money.



United States: Demand deposits and currency in circulation.*

End of	Demand deposits adjusted	Currency in circulation	Total
	in millions of dollars		
1946 December	83,314	26,730	110,044
1947 „	87,123	26,476	113,599
1948 „	85,800	25,700	111,500
1949 March . .	81,000	25,100	106,100

* Total demand deposits adjusted and currency outside banks.

United States: Annual rate of turnover of total deposits (except interbank).

Date	New York City	Other reporting centres
	in percentages	
1946 average .	19.0	10.0
1947 „ .	21.0	12.0
1948 „ .	23.7	12.9
1949 March .	24.1	12.8

To put a stop to further credit expansion seemed all the more necessary as the velocity of circulation of money had shown a rising trend since the end of the war. The annual rate of turnover of deposits in New York had risen from 19.0 in 1946 to 23.7 in 1948 and in other reporting centres from 10.0 to 12.9.

Several indexes seemed to show, towards the end of 1948, that the upward trend of business activity could not be expected to continue in 1949. The wholesale-price index had begun to decline in September 1948; construction contracts showed a falling tendency in the second half of the year; a slackening of demand for the products of several industries was noticeable and sales began to lag, with bank loans declining in the early months of 1949. Such danger signals induced the Board to change its policy in the spring of 1949. Early in March 1949 and again at the end of April the Board decided to relax instalment-credit controls on automobiles, furniture, appliances and related goods by stretching all instalment payments and by reducing the down-payments (except on automobiles). At the end of March, margin requirements for stock purchases were reduced from 75 per cent. to 50 per cent. The Board lowered the reserve requirements, with effect from 5th May, from 26 per cent. to 24 per cent. for demand deposits and from 7½ per cent. to 7 per cent. for time deposits for the central reserve city banks; from 22 to 21 per cent. for demand deposits and from 7½ to 7 per cent. for time deposits for reserve city banks, and (as from 1st May) from 16 to 15 per cent. for demand deposits and from 7½ to 7 per cent. for time deposits for non-reserve city banks — an action which freed $1.2 milliard of reserves.

If comparison is made with earlier periods of decline in business, it must be said that this time the authorities have been quicker than ever before in adopting a policy of easing the conditions of credit.

With a total domestic expenditure (for consumption and investment) which in 1947 exceeded the resources of domestic origin by £630 million (reappearing as a current deficit in the balance of payments where it was met by net loans and gifts from abroad and sales of foreign assets), it was clear that in the United Kingdom steps had to be taken for restoring an overall equilibrium in the economy. The task was taken in hand by budgeting for a substantial surplus in the estimates for 1948–49 and by tightening the direct investment control (carried out through the agency of the Capital Issues Committee and also by means of the allocation of materials required for the construction of capital assets).

Through the various measures taken, the difference between the total expenditure for consumption and investment and the resources of domestic origin was brought down to about £120 million in 1948 — which indicates the rate of progress made. The whole gap was not closed, as shown inter alia by the continued rise in prices and wages and the failure to bring down the demand for non-essential goods (and the consequent failure to make labour shift to any large extent from "non-essential" to "essential" industries, as explained in the Economic Survey for 1949).

There were many who had expected a decline in bank deposits as a result of the budget surplus, but such deposits continued to rise throughout the year 1948.

London clearing banks.

End of	Coin, notes and balances with the Bank of England	Money at call and short notice	Bills discounted	Treasury deposit receipts	Investments	Advances to customers and other accounts	Total net deposits*
	in millions of £ sterling						
1938 . . .	243	159	250	—	635	966	2,188
1946 . . .	499	432	610	1,560	1,427	980	5,439
1947 . . .	502	480	793	1,288	1,483	1,206	5,682
1948 . . .	502	485	741	1,397	1,478	1,378	5,913
1949 April	500	481	799	1,025	1,501	1,435	5,665

* Total deposits minus balances with, and cheques in course of collection, on other banks.

From the end of 1947 to the end of 1948 net deposits rose by £231 million, which was only slightly less than the rise in the previous year. This rise was more than accounted for by an increase of £172 million in bank advances to customers and of £109 million through government borrowing in the form of Treasury deposit receipts.

An important difference between 1947 and 1948 was that in the earlier year the Treasury had much larger sterling receipts from the net sales of foreign currencies (out of reserves, loans and credits obtained, etc.) since in that year the current deficit of £630 million in the balance of payments was £510 million bigger than in 1948. In British statements it has been repeatedly stressed that the budget surplus for 1948–49 was required to offset the decline in receipts due to the reduction in the balance-of-payments deficit.

The considerable extent to which the Treasury borrowed from the banks despite the budget surplus was in part accounted for by special transactions. The Treasury had to borrow for the redemption of the 3 per cent. Conversion Loan 1948–52 and payments in connection with the purchase by the Argentine of the British railways in that country were responsible for the sharp increase in the deposits in March 1948. On the basis of published material, the recourse of the Treasury to the banks in the last nine months of the year cannot be traced in detail to its sources. Tax payments in the first quarter of 1949 had, by March 1949, reduced the volume of deposits to roughly the level of March 1948.

United Kingdom:
Note circulation and deposits.

Period	Notes in circulation, average of Wednesdays	Net deposits of London clearing banks *
	in millions of £ sterling	
1946	1,358	4,932
1947	1,384	5,463
1948	1,254	5,713
1948 March . .	1,239	5,610
June . . .	1,249	5,736
September	1,243	5,771
December	1,275	5,913
1949 March . .	1,242	5,621
April . . .	1,275	5,666

* Averages for the full years 1946–48 but selected dates within each month for the monthly figures March 1948 to April 1949.

United Kingdom:
Yields on government securities.

Period	Short-dated securities	Medium-dated securities	2½ per cent. Consols
	in percentages		
1938 average . . .	2.73	3.27	3.38
1945 „ . . .	2.44	2.99	2.92
1946 „ . . .	2.09	2.55	2.60
1947 „ . . .	2.18	2.67	2.76
1948 „ . . .	2.02	2.79	3.21
1948 January	2.40	2.86	3.08
April	2.17	2.92	3.28
July	1.93	2.82	3.28
October	1.85	2.69	3.18
1949 January	1.68	2.61	3.12
February . . .	1.62	2.60	3.09
March	1.61	2.61	3.11
April	1.82	2.56	3.10

Source: Monthly Digest of Statistics issued by the Central Statistical Office. Representative securities (changed from time to time) are taken; short-dated: 2½% National War Bonds 1952–54 from January 1945; medium-dated: 2½% Savings Bonds 1964–67 from January 1948. The Treasury-bill rate, of primary importance for the money market, has fluctuated very little; the average rate was 0.61 per cent. in 1938 and 0.51 per cent. in 1948.

While deposits have risen, the note circulation has not, present figures being well below those for 1946 and 1947. This has permitted a reduction in the fiduciary issue, which by the end of March 1949 was £150 million below the level at the end of 1947.

The rising trend of interest rates which characterised the year 1947 was reversed in 1948, when the yields on short-dated government securities fell almost uninterruptedly and the yields on medium and long-dated government securities joined in the decline in the latter half of the year. The issues of the 3 per cent. British Transport Stock 1978–88 in January 1948 and of the 3 per cent. British Electricity Stock 1968–73 in the following April were readily absorbed by the market.

Though progress towards financial stability was undoubtedly made in 1948, the pressure of liquid funds and of monetary purchasing power in the hands of the public has not wholly ceased. "In 1949", says the "Economic Survey for 1949", "the nation will face a further stage in the fight against inflation. It is still necessary to restrain home demand in order to maintain the export drive. We expect this year to be able to reduce our dependence on foreign aid and to eliminate the balance of payments deficit of 1948. This change, welcome as it will be, will have inflationary effects which must be offset. In addition, we must try to secure some further easing of the pressure of demand."

In France the supply of money continued to expand throughout the year 1948; notes in circulation however increased at a much slower rate than in the previous two years, whereas deposits grew more rapidly.

France: Notes in circulation and deposits.

End of	Notes	Total deposits of all banks
	in milliards of French francs	
1946	722	625
1947	921	740
1948	933	1,181
1949 January	1,002	.
February	1,025	.
March	1,045	.
April	1,047	.

Bank of France: Balance sheet.

Items	End of 1946	End of 1947	End of 1948
	in milliards of French francs		
Assets:			
Credits to government and other public bodies*	622	824	824
Credits to banks, private business, etc.	58	92	205
Gold	95	55	53
Other assets	18	44	84
Total assets	793	1,015	1,176
Liabilities:			
Notes in circulation	722	921	988
Sight liabilities	64	83	173
Other liabilities	7	11	15
Total liabilities	793	1,015	1,176

* Including over Fr.fcs 400 million in respect of advances which the Bank of France was forced to contract for the payment, during the war, of occupation costs and amounts advanced in the clearing with Germany, etc.

France: Public and private credits by banks.

Items	End of 1946	End of 1947	End of 1948
	in milliards of French francs		
Credits to government and other public bodies	235	179	243
Credits to private business, etc.	250	398	662

Money wages rose at the end of 1947 by 35 per cent. on an average and again by 15 per cent. in September 1948 while wholesale prices rose by about 60 per cent. between the end of 1947 and the end of 1948 and there was also a substantial increase in production. Nevertheless, the note circulation increased by only 8 per cent. — which indicates a considerable rise in the velocity of circulation (see page 63). Such a situation confronts the monetary authorities with some difficult problems but at the same time affords an opportunity for action with good prospects of success.

The Treasury did not increase its borrowing from the Bank of France during 1948 as it had done in the previous year, but instead turned increasingly to the commercial banks. The distribution between credits granted for the government (and other public bodies), on the one hand, and for private business, on the other, is shown in the accompanying table.

In order to limit credit expansion by the banking system, the monetary authorities took measures along the lines of qualitative as well as quantitative credit control. The considerations which directed the credit policy in France in 1948 have been described by the Conseil National du Crédit as follows:

> "The main task of the Conseil National du Crédit has consisted in 1948, as before, ... in making sure that business undertakings do not lack the credit which is required for the expansion of their assets, for production and distribution; but it consisted also in not allowing easy credit conditions to contribute to undesirable price rises or to prevent desirable price reductions. This line of conduct, simple in its motives and its ends, implied however in its application a constant awareness of the double faculty which credit possesses: it helps productive activity but it also feeds inflation."

The banks were directed in January 1947 to grant business credit only for essential purposes and only to firms which could not obtain the funds otherwise. And advances above Fr. fcs 30 million — later Fr. fcs 50 million — had to be approved by the Bank of France. These restrictions did not apply to the discounting of commercial bills, which increased sharply, however, upon the restriction of other forms of credit. As qualitative credit control was difficult to apply, the authorities in September 1948 imposed quantitative restrictions:

(i) The banks have to maintain a special reserve in cash and in short-term securities amounting to 20 per cent. of all new deposits received after 1st October 1948.

(ii) The banks agreed not to reduce the proportion existing on 1st October 1948 between public investments and old deposits.

(iii) Rediscounting with the Bank of France is subject to a "ceiling" fixed for each bank individually, the maximum for all banks together amounting to Fr. fcs 188 milliard.

Finally, the rates charged by the Bank of France were raised.

The rates charged to bank customers are related to the rates of the Bank of France. The banks take a commission of 0.60 per cent. per annum for the discounting of prime commercial paper, so that the rate charged by the banks on this type of paper has amounted to 3.60 per cent. since the end of September 1948. The rates on advances, overdrafts and other paper vary between 5 ½ and 7 per cent. Since the middle of December 1948 a rate of 7.75 per cent. has been charged on mortgage loans by the Crédit Foncier and 7 per cent. by the Crédit National for two to twenty-year advances.

Long-term interest rates in France.

Average rate	3 per cent. perpetual *government* bonds	Government securities *with fixed* interest rates	Corporate bonds
	in percentages		
1946	3.17	4.07	4.36
1947	3.91	5.17	4.98
1948	4.62	6.47	5.86
1949 January	4.01	7.37	6.64
February	3.95	7.39	6.12
March	4.74	7.67	6.64

In January 1949 the government issued a "National Loan for Reconstruction and Equipment" (Reconstruction Loan). It was an irredeemable loan, issued at par and bearing 5 per cent. interest. Some special features characterised the loan, the most important being that: (i) if the government before 1st January 1960 should issue new loans at a rate of 5½ per cent. or more, the interest paid on the Reconstruction Loan will be increased correspondingly; (ii) up to 50 per cent. of the subscription to the Reconstruction Loan could be made by cession of "rentes" at 3 and 3½ per cent. The second feature was largely responsible for the success of the loan, which brought in Fr.fcs 108 milliard in new money. It was also responsible for the rise of the 3 and 3½ per cent. "rentes" in the market in February 1949 (reflected in the fall in the yield in February 1949 — see table page 170).

The policy of maintaining relatively high interest rates and of applying qualitative and quantitative credit restrictions has been increasingly discussed in the spring of 1949 on the ground that it subjects the economy to an undue shortage of credit. While it has been admitted that a decisive downward turn in the business trend might reduce the demand for credit and thus render the restrictions unnecessary, such a stage has by no means yet been reached. It would, however, be preferable if restrictions could be eased thanks to a more ample supply of genuine savings and through the reconstitution of monetary reserves by purchases of foreign currencies, since this would provide the banks with more funds and at the same time strengthen the market for long-term capital issues — which would be another way of reducing the demand on banks for credit accommodation. In any case, the credit policy should be brought into a harmonious relationship with the country's general budget, price and exchange policies.

Great progress was made in Italy in 1948 towards financial stability in spite of the fact that budgetary equilibrium had not yet been attained. Prices had risen sharply until September 1947 but declined in the autumn of that year as a result of severe credit restrictions imposed on the banks; and prices remained approximately stable throughout 1948, as did wages. On the other hand, the volume of currency in circulation continued to rise throughout the year, though at a slower rate than in 1947. In the first three months of 1949, a seasonal reflux of notes to the Bank of Italy reduced the circulation by 70 milliard.

It should be noted that the channels through which the notes came into circulation in 1948 marked a significant difference in the state of affairs as compared with the previous year. Whereas in 1947 the largest single item responsible for the increase in the note circulation was the credit given by the Bank of Italy to the Treasury, it was the accumulation of foreign balances which accounted for the larger part of the increase in the note circulation in 1948 (in that notes were issued against the purchase of foreign currencies). The following table shows the factors making for an increase or decrease in the note circulation in 1947 and 1948.

Italy: Note circulation. Factors making for an increase (+) or a decrease (—).

Items	1947	1948
	in milliards of lire	
Bills discounted [1] in the Italian market	+ 93	— 8
Advances	+ 21	+ 17
Credit to the government	+ 118	+ 98 [2]
Amlire (i.e. notes issued on behalf of the Allied command)	+ 9	0
Foreign exchange accounts [3]	+ 18	+ 169
Deposits at the Bank of Italy [4]	+ 26	— 93
Balance of remaining items	— 2	— 8
Note circulation	+ 283	+ 176

(1) Of the bills discounted, wheat bills accounted in 1947 for an increase of Lit. 67 milliard; in 1948 there was practically no change in the total amount of wheat bills.
(2) The Marshall aid counterpart funds are deducted from the credit to the government.
(3) Foreign exchange held by the Bank of Italy and advances made to the Ufficio Italiano dei Cambi. The amounts shown in the table under the heading "Foreign exchange accounts" correspond to the foreign exchange held by the Bank of Italy and the "Debitori diversi", which, however, include some minor items besides the advances to the Italian Foreign Exchange Control.
(4) An increase in deposits causing a decline in the note circulation is indicated by a minus sign.

The increase of Lit. 98 milliard in the item "Credit to the government and other public bodies" during 1948 did not, in point of fact, exclusively represent credit given by the Bank of Italy to the Treasury, since Lit. 64 milliard of the increase was due to the growth of "Investments in securities on Treasury account", which represented investments of the reserves the commercial banks are required to hold and thus really amounted to credits given to the Treasury by the commercial banks. In the previous year, the amount of such credits had increased by only Lit. 15 milliard. The extent to which in 1948 the Treasury turned from the Bank of Italy to the money market as a source of financing is also reflected in the table below.

Italy: Public and private credits granted by commercial banks.

Items	End of 1946	End of 1947	End of 1948
	in milliards of lire		
Lending to government	370	390	650
Lending to private bank clients	420	710	1,060
Total	790	1,100	1,710

Italy: Currency in circulation, cheque accounts and circular cheques.

Items	End of 1946	End of 1947	End of 1948	Increase in 1947	Increase in 1948
	in milliards of lire			percentages	
Currency in circulation	613	795	971	+ 55	+ 22
Cheque accounts of credit institutions	345	499	737	+ 45	+ 48
Circular cheques of the Bank of Italy and other credit institutions	100	133	152	+ 33	+ 14
Total	958	1,427	1,860	+ 49	+ 30

The credit expansion by commercial banks in 1948 through public and private lending naturally increased the volume of deposits. If the cheque accounts of commercial banks and the "circular cheques" issued by them and by the Bank of Italy are added to the currency in circulation, an approximate measure is obtained of the supply of money in the Italian economy.

The percentage increase in the money supply in 1948 was much lower than in 1947. The wholesale-price index at the end of 1948 was only

3 per cent. higher than a year earlier, whereas at the end of 1947 it had been 50 per cent. above the level at the end of 1946. The relative stability of the price level despite the large increase in the volume of money is not accounted for entirely by the increase in production. Production shows an increase by 7½ per cent. from 1947 to 1948 and it is true that the real increase in the supply of goods was greater since, up to the autumn of 1947, inventories had been accumulated as an inflation hedge and, after the credit restrictions of the autumn of 1947, began to be thrown on the market. But the factor most responsible for the relative stability of price level in 1948, in spite of monetary expansion, would seem to have been the decline in the velocity of circulation. Though little statistical evidence is available to prove that such a decline actually took place, observers agree that the velocity of circulation, which was very high in 1947 as long as prices continued to rise, returned to normal in 1948. If this has really been the case, it cannot be expected that the money supply can be expanded in 1949 on the same scale as in 1948 without bringing about a further rise in the price level.

Italy: Budget deficit. (1)

Year	In milliards of lire
1946–47	— 578
1947–48	— 787
1948–49 (2)	— 410
1949–50 (2)	— 174

(1) Figures given by the Minister of Finance in a speech before the Senate in April 1949.
(2) Estimated.

The budget deficit therefore gives some cause for concern, although it is expected that it will be substantially reduced in the financial years 1948–49 and 1949–50.

Interest rates continued high through 1948, although the yield on government bonds with a maturity of 5–9 years showed a noticeable decline to about 5½ per cent. Bank customers had to pay a rate of 9½ per cent., to which a commission must be added, so that the rate actually amounted to over 10 per cent. * The high interest rates were regarded by many as partly responsible for unemployment in Italy (amounting to between 1.5 and 2 million). In order to relax credit conditions, the Minister of Finance, in his speech before the Senate in April 1949, announced a reduction of the discount rate and the rates on Treasury bills. As a sequel to the reduction of the discount rate by 1 per cent., the rates charged to bank customers by commercial banks were reduced correspondingly. As the supply of savings increases or capital is obtained from abroad for

Italy: Interest rates.

Items	1946	1947	1948	1949
	in percentages			
Perpetual bonds (average)	5.13	5.72	5.43	5.16 (2)
Long-term government securities (average) . . .	4.78	5.59	6.48	6.17 (2)
Government securities with 5–9 years' maturity (average)	5.55	6.88	5.45	5.21 (2)
Discount rate	4.00	5.50 (1)	5.50	4.50 (3)
Rate on Treasury bills (10–12 months)	4.50	5.00 (1)	5.00	4.50 (3)
Rate on Treasury bills (1–2 months)	2.75	3.25 (1)	3.25	2.75 (3)

(1) Changed in September. (2) Average for February 1949. (3) Changed in April.

* See "Interest Rates in Italy", by C. Bresciani-Turroni, "Review of Economic Conditions in Italy". Banco di Roma publication, January 1949, page 12.

investment expenditure, credit conditions will naturally become easier in Italy; but, with monetary demand still as great as it is at present, it is of course an illusion to think that capital resources can be reconstituted by issues of new money.

The event which contributed most to the revival of the economy in the western zones of Germany during 1948 was the currency reform of 20th June of that year, the main features of which are described on page 42.

In connection with the currency reform the balance sheets of banks and other financial institutions were put in order. Before the reform the liabilities of the banks had mostly their counterpart in securities of the old Reich government; in respect of these securities, however, no payments for interest or amortisation had been received since the spring of 1945 and many of these securities had matured but had not been redeemed. Other assets of the banks had also suffered during the war so that even a reduction in their liabilities by 90 per cent. did not suffice to right their position.

Through the currency reform the banks lost practically all their cash and their balances with other banks. On the other hand, they received from the central banks in the individual "Länder" an advance payment in the form of a liquidity allocation corresponding to 1 per cent. of their liabilities in RM. For cover of the liabilities assumed in the new currency period each central bank of an individual "Land" received at the Bank deutscher Länder a book credit corresponding to 30 per cent. of the deposits it owed; each of the other banks received at the central bank of the individual "Land" concerned a book credit corresponding to 15 per cent. of its sight liabilities and 7½ per cent. of its time liabilities and the savings deposits held with it. To the extent that these assets would not suffice, all financial institutions (including the Bank deutscher Länder) were given claims (so-called "Ausgleichsforderungen") against the "Land" in which they were located and in the case of the Bank deutscher Länder against the Bizone and the various "Länder" in the French zone. The claims were made sufficiently large to provide the banks with a capital of their own equal to, as a rule, 5 per cent. of the liabilities arising from the conversion of assets in RM.

The claims thus given to the banks are non-marketable book assets and bear 3 per cent. interest but can be used as security for borrowing from central banks or can be bought by central banks.

A limit of DM 10 milliard, which can only be exceeded through decisions of three-quarters of the members of the Central Bank Board and of six "Länder", was set for the note circulation; and reserve requirements, which had previously never been applied in Germany, were introduced. The Central Bank Board attached to the Bank deutscher Länder has to fix the various minimum requirements: the reserves which each central bank would have to maintain at the Bank deutscher Länder had to be fixed at between 12 and 30 per cent. on demand deposits; and the reserves which other banks would have to maintain at the central bank in the "Land" in which they are located had to be fixed at between 8 and 20 per cent. on demand deposits and at 4 to 10 per cent. on time and savings deposits. In fact, the minimum reserves of the central banks in the individual "Länder" were, for the time being, set at 20 per cent. and for other banks at 10 per cent. on demand deposits and at 5 per cent. on time and savings deposits.

The total amount of DM in notes and deposits (in the form of "free accounts") which emanated from the currency reform was DM 12.6 milliard by April 1949. The free accounts were only gradually released, so that the volume of money originating in the reform increased continuously throughout the second half of 1948; but by February 1949 this process had practically come to an end. In addition, new money was brought into being through the granting of bank credits. Up to 7th August 1948, credits could be granted only on the basis of commercial bills or in favour of public authorities, but later on the granting of credit was on a relatively large scale, the amount of new credits outstanding being DM 6.6 milliard at the end of April 1949.

Germany (western zones): Note circulation and deposits.

End of month	Note circulation	Free deposits
	in millions of DM	
1948 July	3,831	6,131
August . . .	4,178	7,683
September .	5,358	8,696
October . .	5,885	9,396
November .	6,017	10,398
December .	6,319	10,789
1949 January . .	6,167	11,200
February . .	6,216	11,767
March . . .	6,188	12,215
April	6,334	12,827

The fear that budget deficits of the German Länder would contribute to the increase in the money supply turned out to be unfounded. Although all the various budgets showed cash deficits in the first quarter after the reform, some of the Länder were able to accumulate a substantial cash surplus after October 1948.

The increase in the money supply throughout the second half of 1948 led to sharp price rises for industrial products. They were greatly accentuated by the high velocity of circulation of money, which was partly the result of pent-up demand for consumer goods — a demand which, for the first time in several years, could be at least partly satisfied by purchases in shops. No price index exists by which the price increases can be adequately measured, but increases in retail prices by 100 per cent. and more were not uncommon. Agricultural prices were still controlled and in this field the price increase expressed itself in higher black-market prices. Expectations of further price increases led producers and traders to hold back goods from the market, and that contributed to further price rises.

The monetary authorities viewed these developments with concern, but their power to influence the volume of money was limited. They could not stop the gradual expansion of the amount of DM which had come into being through the currency reform, and their power to influence the volume of çredit granted by the commercial banks was still restricted by the fact the the great liquidity of the latter in the first months after the reform made them largely independent of the central banks.* And, although recourse to the central banks increased substantially towards the end of the year, the commercial banks still had considerable excess reserves — an anomaly which can be traced, to a large extent, to the unequal distribution of such reserves, but in some cases also to the "hoarding" of reserves for fear of an increase in the discount rate.

Germany: Central-bank credit and excess reserves.

Month	Bank deutscher Länder and central banks of the Länder: Bills discounted and advances	Reserves of credit institutions (monthly averages)		
	in millions of DM			
		Required	Actual	Excess
1948 September	361	921	1,468	547
October	838	843	1,071	228
November	1,327	847	1,190	343
December	1,628	1,151	1,528	377
1949 January	1,459	1,174	1,582	408
February	1,516	1,179	1,443	264
March	1,561	1,200	1,472	272

In order to put a stop to further price rises the authorities in the fourth quarter of the year took special measures to restrict credit expansion. In November 1948, the Central Bank Board recommended the commercial banks not to increase credits beyond the level reached on 31st October (a recommendation which was not entirely effective) and the Board further restricted the eligibility of bankers' acceptances for rediscounting. Moreover, from 1st December the Board raised the reserve requirements on demand deposits from 10 to 15 per cent. for all banks located in places where a central bank is represented. The rediscount rate was left, however, at 5 per cent. and the lombard rate at 6 per cent., with the commercial banks charging 6½–9 per cent. on their loans to customers.

These measures, together with heavy tax payments at the end of the year, forced firms to sell, and thus brought prices down. In fact, prices had already begun to decline in December and continued to do so in January 1949, and for many products also in February, although some price increases were again reported in the course of that month.

The reaction against the inflationary price rises was not reflected in a fall in the production index but it led to a number of adjustments generally necessary after a long period of redundant money; and with these adjustments came an increase in unemployment; the number of unemployed in the

* The liquidity of the banking system was largely the result of the transfer to certain groups of the commercial banks of the initial allocations made to the German railways, the post office and the public bodies — the amounts in question having been originally credited with the Bank deutscher Länder or with the central bank of the Land concerned. As these deposits were transferred, the reserves of the commercial banks increased.

Trizone, which in the period August–December 1948 had oscillated between 784,000 and 700,000, rose in January 1949 to 962,900 and in April to 1,229,000. In April 1949 the index of production for the Bizone (1936=100) was 86 as compared with 77 in December 1948 and 51 in June 1948 (adjusted for the number of working days).

Inflation being kept in check, the Central Bank Board in March 1949 cancelled the "stop order" issued in November 1948 for the prevention of further credit expansion. Furthermore, in May 1949 there was a relaxation of the principles guiding the purchase of, and granting of credits against, bank acceptances and, at the end of the month, the discount rate of the central banks of the various Länder was reduced from 5 to 4½ per cent. and the lombard rate from 6 to 5½ per cent. The minimum reserve requirements on demand deposits were at the same time reduced from 15 to 10 per cent. for all banks located in places where a central bank is represented and from 10 to 9 per cent. for banks in other places.

The greatest need of the German economy is capital for long-term investment purposes. Although there are signs that private savings are again beginning to come forth (in January 1949 in-payments into savings accounts exceeded out-payments for the first time), the supply of long-term capital from this source cannot be expected to be large in the near future. In April the Anglo-American Control Office began to release part of the "counterpart funds" (which had resulted from imports provided as direct Army relief) for long-term investments in coal mines, electric-power projects, inland water transport and some other industries. E.R.P. counterpart funds may also be released for long-term investment purposes, and in April the American and British Military Governors submitted to governments of other countries a proposal to lift the ban on foreign investments in Germany. The sums so far involved are small in comparison with Germany's need, and lack of capital will presumably continue to characterise the German economy for a long time to come.

France, Italy and Germany all belong to the third group of countries described at the beginning of this chapter (page 161). Another country in this group is Belgium. In July 1948 two laws were passed by the Belgian Parliament which somewhat changed the status and the balance sheet of the National Bank of Belgium; in September an extraordinary meeting of the shareholders of the Bank approved these changes. The structure of the balance sheet was simplified; the various claims of the National Bank of Belgium against the state and against the Brussels Bank of Issue (which had been set up by the Germans during the war) were offset against the state's claims on the National Bank of Belgium. In addition, the Bank surrendered to the state the profits which it had made during the war and the Bank's capital was doubled (from B.fcs 200 to 400 million), the new shares being subscribed by the state. All these changes left the Bank with a credit, vis-à-vis the state, of B.fcs 37.5 milliard, of which B.fcs 35 milliard was consolidated and the remaining B.fcs 2.5 milliard was to be held by the

Belgium: Currency circulation and free accounts.

End of year	Currency in circulation (1)	Cheque accounts (2)
	in milliards of B.fcs	
1946	79.3	72.0
1947	84.6	66.9
1948	89.4	72.6

(1) Bank-notes and Treasury currency.
(2) Current accounts of the National Bank of Belgium, postal-cheque accounts, and demand deposits of private and semi-public banking institutions.

Bank in the form of Treasury certificates. The amount of public credit that can be extended by the National Bank of Belgium (against Treasury certificates, government and government-guaranteed securities) was limited to B.fcs 10 milliard by an agreement between the government and the Bank.

One reason for the continued increase, in Belgium, of notes in circulation and deposits was the freeing of temporarily blocked accounts (having their origin in the currency reform of October 1944) to the extent of B. fcs 4.8 milliard in June 1948; and another reason was the acquisition by the National Bank of (net) B.fcs 2.5 milliard in gold and foreign exchange.

Total deposits of the commercial banks declined from B.fcs 54.5 milliard at the end of 1947 to B.fcs 49.8 milliard at the end of 1948; against this there was a decrease in credit to the government and other public bodies, while the amount of credit granted to business undertakings increased somewhat (as it had been doing since 1945). The withdrawal of deposits was largely responsible for an increase by B.fcs 1.6 milliard in 1948 (as against only B.fcs 663 million in 1947) in bills rediscounted.

Belgium: Commercial-bank credit.

End of year	Private credit			Public credit	Total
	Commercial paper	Advances	Total*		
	in milliards of Belgian francs				
1946	3.7	12.1	15.8	33.5	49.3
1947	5.6	13.0	18.6	32.4	51.0
1948	5.9	13.2	19.1	29.7	48.8

* Not including rediscounts.

The budget deficit in 1948 was halved as compared with 1947 and the budget for 1949 shows a further decline in the deficit. The Treasury raised B.fcs 3.7 milliard by the issue of certificates with a maturity of five to ten years and borrowed $50 million in the United States, obtaining, in addition, roughly B.fcs 1 milliard through the increase in postal-cheque accounts.

Belgium's budget deficit*
(ordinary and extraordinary).

Year	In milliards of Belgian francs
1947	20.9
1948	10.4
1949	4.8

* The figures exclude expenditure for the amortisation of the Currency Reform Loan and the proceeds of the capital levy imposed in connection with the currency reform. They also exclude the subscriptions to the Bretton Woods institutions.

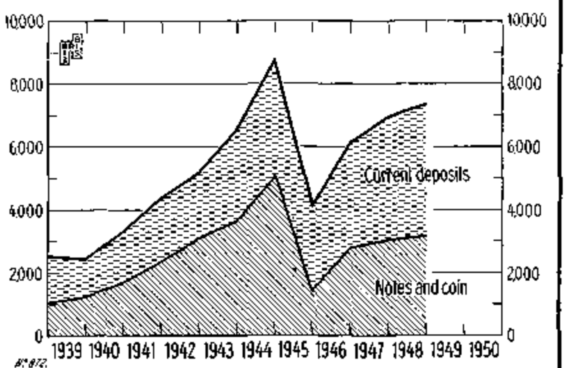
Hardly any change occurred in interest rates — with an official discount rate of 3½ per cent. and a yield of about 4.70 per cent. on the 4 per cent. Unified Rente — while the National Bank continued its selective credit control in 1948 in order to prevent credit from being used for speculative purposes, for consumption and the hoarding of inventories.

Netherlands: Money volume.*

End of year	Currency in circulation	Deposits	Total
	in millions of florins		
1945	1,386	2,714	4,100
1946	2,801	3,392	6,193
1947	3,062	3,892	6,954
1948	3,184	4,148	7,332

* *Calculated in conformity with the recommendations of the International Monetary Fund.*

Nederlandsche Bank:
Notes and coin in circulation and current deposits.
Yearly, in millions of florins.



In the group of countries mentioned on page 161, of which the United Kingdom is the most important member, the Netherlands in the fiscal year 1948–49 received tax amounts which, including the yield of an extraordinary capital levy, corresponded to more than 40 per cent. of the national income. But official financing was also influenced by the fact that some of the receipts were in the form of funds which had been blocked. The total of notes in circulation and deposits continued to increase.

According to an analysis given in the annual report of the Nederlandsche Bank, the increase in 1948 was the net result of the monetary expansion caused by:

	1947	1948
	in millions of florins	
(i) Financing of the Treasury's deficit	+ 525	+ 545 (1)
(ii) Creation of credit by the banks, for private industry	+ 165	+ 180
(iii) Unblocking of balances with credit institutions	+ 165	+ 120

and the monetary contraction caused by:

	1947	1948
(i) Decrease in foreign assets held by the Nederlandsche Bank and the commercial banks	+ 110	— 60
(ii) Increase in deposits on local-currency accounts (2)	—	— 347
(iii) Increase in the banks' own reserves and time deposits	— 204	— 60
	+ 761	+ 378

In 1948, as in 1947, the Treasury's operations were the most important factor in the Dutch money market. But in 1948, in contrast to 1947, the inflationary effects of the Treasury's recourse to the banking system and of its drawing on funds hitherto blocked were largely offset by the

(1) Increase in the Treasury's indebtedness to the Nederlandsche Bank (+ Fl. 500 million), minus decrease in its indebtedness (— Fl. 365 million) to private banks, plus the net amounts paid out by the state in free money although the funds in question had been received in blocked form (+ Fl. 410 millions).

(2) E.R.P. counterpart funds.

Netherlands: 42 commercial banks.

End of year	Public credit	Private credit
	in millions of florins	
1946	3,448	686
1947	3,904	766
1948	3,699	850

sterilisation of money in the local-currency account, i.e. by the counterpart of Marshall aid.

Unlike the Italian and French Treasuries, the Dutch Treasury increased its indebtedness to the central bank while at the same time reducing its indebtedness to the commercial banks; but, even so, the commercial banks' assets in the form of public credit were, at the end of 1948, still 4.4 times as large as their assets in the form of private credit. The slow expansion of bank credit to private business undertakings indicates that firms were largely able to finance themselves out of their own liquid funds.

The liquidity of the market found its expression in the continuance of cheap-money rates. The discount rate of the Nederlandsche Bank remained at 2.5 per cent. — its level since June 1941 — but it is hardly effective, since commercial banks have not much need of central-bank funds. Long-term interest rates varied little, the yield of the irredeemable government loan averaging 3.09 per cent. in 1948 as compared with 3.06 per cent. in 1947. At the beginning of May 1948 the government proceeded to convert the 3–3½ per cent. State Loan of 1938, giving the holders the choice of taking either a 3 per cent. government loan at par, redeemable in 1962–64, or a 3¼ per cent. loan at 100½ per cent., redeemable within fifty years. Both loans together amounted to Fl. 1.5 milliard, a sum greater than the total of the old loan outstanding (Fl. 1.2 milliard). The new loans were fully subscribed. Also in May, 1948, Fl. 152.6 million in 3 per cent. investment certificates and Fl. 27.4 million of 3 per cent. stock were issued and absorbed by blocked funds.

In spite of the steps taken in Norway to cope with the redundancy of money (including the exchange of notes in 1945), excess liquidity continued to be a characteristic of the Norwegian banking system, which in 1948 was able to increase its investments and loans to private clients; but this, combined with a loss of reserves connected with an increase in the note circulation, lowered the ratio of its reserves (i.e. cash on hand plus balances with the Bank of Norway) to deposits from 33 per cent. at the end of 1947 to 21 per cent. at the end of 1948 — this being still a high liquidity ratio, however.

Bank of Norway: Selected items.

End of year	Assets		Liabilities	
	Gold, foreign exchange, foreign bonds	Occupation account (net)	Notes in circulation	Total deposits
	in millions of Norwegian Kroner			
1946	1,157	8,108	1,933	6,217
1947	821	8,094	2,088	5,465
1948	657	7,924	2,159	5,222

Referring to the latent possibilities of credit expansion still remaining, the Governor of the Bank of Norway stated in February 1949:

"Today the Norges Bank is incapable of being an instrument for the community or the government in this (monetary) field, but in a disinflated monetary system, the Bank might become an instrument which — coordinated with the budgetary policy of the government — could restore the balance and contribute to maintaining the policy of stabilisation which has been pursued since the war.

Norway: Joint-stock banks.

End of year	Cash on hand and balances with Bank of Norway	Treasury bills	Bonds and shares	Bills, advances and mortgages	Deposits
	in millions of Norwegian Kroner				
1946	695	1,691	548	1,354	3,185
1947	1,266	952	864	1,852	3,821
1948	814	821	1,013	2,337	3,886

The Governor emphasised that in the existing circumstances in Norway it was the task of the government rather than of the central bank to free the economy of excess purchasing power (mainly by using its capacity to tax). The budget for 1948–49 still reckoned with a deficit of N.Kr. 113 million, but it was later estimated that there would be an approximate balance. The budget for 1949–50 anticipates a small surplus.

Norway: Budget results.

Period	In millions of N.Kr.
1946–47 (actual)	— 664
1947–48 ,,	— 127
1948–49 (budget)	— 113
1949–50 ,,	+ 10

Technically speaking, the problem of disinflating the economy is the problem of reducing and finally eliminating the occupation account, which is by far the biggest asset of the Bank of Norway. Part of the counterpart funds from Marshall aid have been used to this end. As long as excess purchasing power exists in the economic system, interest rates are likely to stay low. The discount rate (which is an ineffective rate in view of the liquidity of the commercial banks) was reduced to 2½ per cent. in January 1946 and has remained at that level ever since. The price of 2½ per cent. government loans averaged 100.58 for 1948 as against 100.14 in 1947.

To restore balance in its economy, Sweden has relied on direct investment controls (through the granting or withholding of building licences, etc.), fiscal policy (through budgeting for a surplus) and income stabilisation (through limitation of wage rises, etc.) rather than on a flexible interest policy. In 1948 the Sveriges Riksbank continued to give support to the 3 per cent. interest rate on government bonds but its bond purchases were on a smaller scale than in the previous year. Helped by the provision of liquid resources from the Riksbank, gross investments in Sweden came to 30 per cent. of the national income in 1947, while gross savings were 24 per cent. of the national income — the difference appearing as a current deficit (of S.Kr. 1,440 million — see page 85) in the balance of payments. While this deficit made an inroad on the monetary reserves, the sale by the Riksbank of foreign exchange absorbed monetary purchasing power and helped to keep down the increase in the note circulation, as shown in the following table.

Sveriges Riksbank: Balance sheet.

End of year or month	Gold and foreign exchange	Bonds and Treasury bills	Domestic bills	Note circulation	Sight deposits		
					State	Commercial banks	Others
	in millions of Swedish Kronor						
1945	2,880	434	7	2,782	831	81	41
1946	2,083	1,544	49	2,877	706	84	85
1947	889	2,747	38	2,895	631	197	72
1948	701	3,317	65	3,113	679	359	102
1949 March	679	2,973	49	2,953	641	93 *	67

* Mostly seasonal decline.

Owing partly to the strict scrutiny to which the banks, on the recommendation of the Sveriges Riksbank, subjected applications for credit, but also to the import cuts and the reduction in the government's investment programme during 1948, bank advances declined slightly in that year. Total deposits of the commercial banks, however, increased, and the banks were able to enter the market as buyers of government securities, whereas in 1947 they had been unloading such securities.

Sweden: Commercial banks.

End of	Cash	Treasury bills and bonds	Advances and commercial paper	Deposits
	in millions of Swedish Kronor			
1945	347	2,152	5,763	6,669
1946	382	991	7,242	6,939
1947	499	533	7,937	7,290
1948	652	717	7,830	7,490
1949 March	328	996	7,837	7,526

Since industrial bonds offered a somewhat better yield than government bonds (3.33 per cent., on an average, as against 3.08 per cent.), there was an inducement for holders of government bonds to shift from these into industrial bonds. The Minister of Finance conferred with savings banks and insurance companies with a view to obtaining an undertaking that they would not reduce their holdings of government bonds and came to an agreement with the latter but not with the former.

During the war and after the Liberation, the monetary authorities of Denmark consistently pursued a policy of mopping up excess purchasing power which had been created as a result of the occupation. The government reduced its debt to the Danish National Bank, the so-called "regulation account" (which had originated in the financing of the occupation), by a further D.Kr. 518 million in 1948 and at the same time increased the credit balance on its account with the National Bank by D.Kr. 116 million. The budget surplus, the proceeds of loans and the counterpart funds from Marshall aid (which are kept in a special account with the central bank) were available to carry out this disinflationary policy.

Danish National Bank: Selected items.

End of year	Assets			Liabilities			
	Gold	Commercial bills and advances	Regulation account	Foreign exchange (net)	Notes in circulation	Government deposits	Sight deposits
	in millions of Danish Kroner						
1946	82,729	3.7	6,626	483	1,633	1,714	2,895
1947	70,568	3.7	5,609	667	1,641	1,742	1,619
1948	70,438	5.9	5,091	553	1,614	1,958	1,063

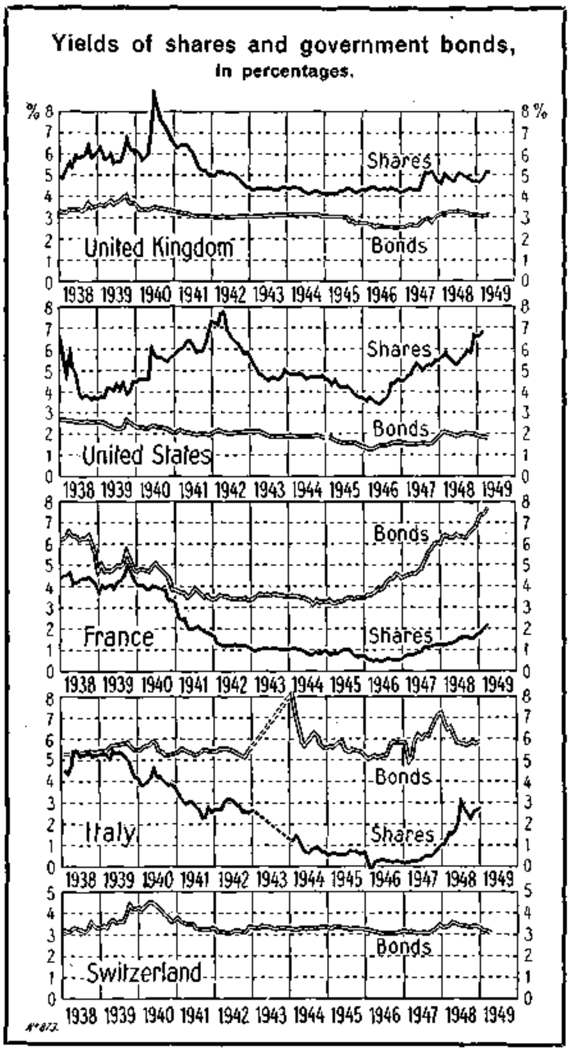
As a result the reserves of the commercial banks declined from D.Kr. 1,987 to D.Kr. 1,252 million. Bank deposits also fell and, in order to finance part of the increasing demand for credits, the commercial banks unloaded government securities. Under these circumstances, it is not surprising that the market tightened in the second half of 1948. The index for bond prices fell from 109 in December 1947 (1938=100) to 100 in December 1948 and long-term interest rates had thus returned to their pre-war level with a yield of about 4 per cent. on government bonds. To ease the position of the banks the reserve requirements of the commercial and savings banks were reduced at the end of 1948 — an action which set free D.Kr. 200 million.

Denmark: Commercial banks.

End of year	Cash plus bank deposits	Investments (bonds and shares)	Loans and discounts	Total deposits
	in millions of Danish Kroner			
1946	3,310	1,282	2,652	5,785
1947	1,987	1,333	3,286	5,436
1948	1,252	1,199	3,916	5,377

The Bank of Finland, in its fight against inflation, resorted in 1947 and 1948 to the classical method of raising its discount rate, until in February 1948 it reached 7¼ per cent. Other interest rates followed suit; in particular, the commercial banks increased their lending rates by 2 to 2½ per cent. and the rates paid for deposits by 2 per cent. This policy is reported to have restricted the demand for credit, increased the flow of funds to the banking institutions and generally contributed to the growing confidence in the Finnish mark; while undoubtedly increasing the flow of genuine savings, the rise in interest rates helped rather than hindered production.

There was, indeed, no increased recourse by the banks and by business undertakings to the Bank of Finland. After having grown by as much as 20 per cent. in 1947, the Bank's total bill holdings (of which only a small part are rediscounted bills), though fluctuating from month to month, finished the year 1948 at the same level as at the end of 1947. The pace at which the note circulation expanded was also much reduced in 1948, the increase by FM 2,207 million during that year being equal to 9 per cent. of the volume outstanding at the end of 1947, whereas in 1947 the note circulation had increased by 38 per cent. On the other hand, total loans of commercial banks continued to expand at approximately the same rate as in 1947.



Nevertheless, as from 1st February 1949, the Bank of Finland lowered its discount rate again by one-half of 1 per cent.

Denmark, to some extent, and Finland, more decidedly, differ from the other northern countries in that they have employed the rate of interest as a primary weapon in their struggle for monetary equilibrium. Switzerland has done so, too, but in that country much narrower movements were sufficient for the purpose. The rates for Swiss Federal bonds reached their highest point with a yield of 3.55 per cent. in March 1948 (after having been below 3 per cent. in the course of the previous year). But in the latter half of 1948 a downward trend set in again on the money and capital markets in Switzerland and this continued in the opening months of 1949, the yield of Federal bonds falling back to 2.87 per cent.

In 1948 not less than Sw.fcs 407 million in fresh funds was made available to the market by the National Bank; of this amount Sw.fcs 320 million was due to the acquisition of gold and foreign exchange by the National Bank and Sw.fcs 187 million to the freeing of formerly blocked proceeds of exports.

Swiss National Bank: Selected items.

End of	Gold and foreign exchange	Bills and advances	Securities and Treasury bills	Notes in circulation	Sight liabilities
	in millions of Swiss francs				
1946	5,108	234	67	4,091	1,164
1947	5,359	395	68	4,383	1,172
1948	6,058*	205	49	4,594	1,243
1949 March . . .	6,228	156	46	4,326	1,666
May	6,402	138	40	4,279	1,811

* Part of the increase in 1948 in the gold and foreign exchange holdings of the National Bank represented amounts taken over directly from the Confederation.

Switzerland: 43 banks.

End of	Cash (1)	Bills	Loans	Mortgages	Securities	Deposits (2)
	in millions of Swiss francs					
1946	540	1,434	3,599	6,653	2,773	14,007
1947	664	1,289	4,299	6,946	2,424	14,706
1948	939	1,736	4,417	7,331	2,162	15,367

(1) Excluding interbank balances.
(2) Including "Kassenscheine", "Obligationenanleihen", and "Pfandbriefdarlehen", but excluding interbank deposits.

The new central-bank funds took the form of notes, the circulation of which rose by Sw.fcs 211 million in 1948. At the same time, the deposits of the Swiss banks with the National Bank increased by Sw.fcs 210 million.

Apart from the injection of new central-bank funds, a reason for the easing of credit conditions was the slackening of the demand for bank accommodation on the part of business undertakings. Bank loans, which had risen sharply in 1947, reached their maximum around the middle of 1948, as did commercial bills held by the banks.

Polish investment programme.

End of year	Planned investments	
	in milliards of zlotys	*as percentage of national income*
1946	40	*21*
1947	85	*21*
1948	190	*19*
1949	310 (1)	*20* (2)

(1) Of this amount, Zl. 290 milliard is intended to be spent under the state investment plan.
(2) In addition to commodity stocks representing 6 per cent. of the national income.

As regards the group of countries with a planned economy based on state ownership (see page 161), comparatively detailed information has been published about the investment programme for Poland and its financing. The Three-Year National Economic Plan envisaged for 1948 total investments of Zl. 190.6 milliard, corresponding to 19 per cent. of the national income. To finance this programme the government relied on funds from various sources:

(i) Out of a budget surplus of about Zl. 45 milliard, Zl. 41.6 milliards would be contributed in 1948.

(ii) Since voluntary savings are small, a law was passed in March 1948 under which persons in receipt of a monthly income above Zl. 20,000 would have to deposit part of their income in blocked accounts. Private enterprise was subjected to a similar kind of forced saving, the rates being, however, considerably higher than those applicable to individuals. This system of saving was expected to produce Zl. 20 milliard.

(iii) The third source was the granting of bank credits. In this the National Bank of Poland participated to a large extent not only directly but indirectly through the extension of credits to the other banks. The rôle played by the National Bank of Poland in financing investments became less important in 1948, however. Two years earlier some 66 per cent. of the total bank credit had been granted directly or indirectly by the National Bank; by the end of 1948 the proportion in question had fallen to 46 per cent. The various credit institutions are all controlled by the Ministry of Finance.

Poland: Credit institutions.

End of year	National Bank of Poland		Other credit institutions			
	Direct credits (1) to industry	Note circulation	Credits	Deposits and current accounts	Investment accounts (2)	Debt to Bank of Poland
	in milliards of zlotys					
1946	17.6	60.1	60.6	25.2	3.6	37.6
1947	59.0	91.5	169.7	57.7	37.0	86.2
1948	78.5	130.7	383.1	112.3	145.0	137.5

(1) Credits by the Bank of Poland to other credit institutions are included in the amounts shown in the last column of the table. (2) *Including funds of government departments for special purposes.*

In October 1948 three decrees were passed for the reorganisation of the Polish banking system. The National Economic Bank describes the purpose of the reform in question as follows:

> "The aim of the banking reform is to subordinate the whole banking system to one central authority in order to realise efficaciously the principles of a planned financial and credit policy, as well as of financial control of the national economy."

Banking activities would henceforth be entrusted to (i) six state banks, (ii) three banks with the status of joint-stock companies and (iii) co-operative credit societies. The range of direct credits by the National Bank of Poland (previously restricted to the three key industries — coal mining, electric power and metallurgy) was to be widened. A new "Investment Bank", which was to replace the National Economic Bank, would be the executor of the entire state investment plan.

In Czechoslovakia, as in Poland, the central bank carries a large part of the burden of financing the government's investment programme, which for 1947 and 1948 was set at Kčs 86 milliard. In Czechoslovakia, however, there was no surplus in the budget but a deficit of Kčs 10 milliard in 1948.

National Bank of Czechoslovakia: Selected items.*

End of	Assets			Liabilities		
	Gold and foreign exchange	Credits	Others	Bank-notes	Bankers' balances and other sight liabilities	Others
	in milliards of Kčs					
1946	5.3	7.9	135.6	43.6	10.1	18.7
1947	4.8	17.4	63.6	58.5	7.3	21.2
1948	4.2	30.2	47.2	72.0	2.0	7.8

* Only accounts in new currency, except for "other" assets in 1946. Assets and liabilities relating to the old circulation were transferred to a "Currency Liquidation Fund" in August 1947.

The recourse had to the National Bank is reflected in the table on page 186. Total credits granted by the Bank increased by Kčs 9.5 milliard in 1947 and by Kčs 12.8 milliard in 1948, while the note circulation rose by Kčs 14.9 milliard and 13.5 milliard respectively.

No figures are available for the credits granted by banking institutions other than the National Bank but certain inferences can be drawn from the movement of their deposits.

**Czechoslovakia:
Deposits with financial institutions.**

End of	"Deposit books"	Deposits in current accounts *	Total
	in milliards of Kčs		
1946	15.2	42.5	57.7
1947	27.5	54.3	81.8
1948	33.6	53.3	86.9
1949 February	35.9	62.9	98.8

* Excluding bankers' balances.

Total credits granted by the banks must have been larger than the increase in deposits, since the banks drew heavily on their own deposits with the central bank.

The structure of the banking system underwent further changes in 1948. In the middle of the year three laws were passed concerning the reorganisation of the banking system. A merger of the nationalised commercial banks reduced their number to two, one for Bohemia and Moravia and one for Slovakia. Henceforth, the banking system will comprise (apart from the National Bank) two commercial banks, an investment bank granting long-term credits for investments under the economic plan, the Post Office Savings Bank and the People's Banking Centre, each with a network of district and local banks, the latter taking the place of the local co-operative loan societies and communal savings banks (which were merged into a unified type of co-operative local bank to be known as a "Savings Bank and Loan Society"). The whole banking system is under the control of the Minister of Finance, who also has authority to fix interest rates. Making use of this power, the Minister in December 1948 announced a complicated schedule of interest rates. The rate on short-term bank loans was fixed at 4 per cent. and that on long-term loans at 3½ per cent., excluding fees, for which very detailed instructions were also given.

* * *

In every country the operations of the Treasury in the handling of government finance have exerted a considerable influence on internal credit conditions, whether a budget deficit had still to be financed, or foreign assistance had to be fitted into the credit situation, or the government had actually a surplus for redemption of national debt.

Towards the end of 1948, the turn in general business conditions from super-boom to a less extreme but still high level of activity began to make itself felt also as regards credit. In the United States and in

Notes in circulation.

Countries	End of June 1939	Dec. 1946	Dec. 1947	Dec. 1948	Dec. 1948
	in millions of national currency units				Index June 1939 = 100
Austria	900 (1)	5,656	4,326 (2)	5,635	626 (3)
Belgium	22,212	73,891	79,761	84,851	382
Czechoslovakia	10,740 (4)	43,589	58,539	71,997	670
Denmark	446	1,633	1,641	1,614	362
Eire	16	45	48	50	307
Finland	2,200	18,233	25,162	27,369	1,244
France	122,611	733,797	920,831	987,621	805
Greece	8,002	537,463	973,609	1,052,000	13,146
Hungary	885 (5)	968 (6)	1,992 (6)	2,817 (6)	318 (6)
Iceland	12	167	107	175	1,410
Italy	21,533 (7)	512,400 (7)	794,988 (7)	970,853 (7)	4,509
Netherlands	1,045	2,744	3,010	3,152	302
Norway	475	1,933	2,088	2,159	455
Poland	1,848	60,066	91,483	130,713	7,074
Portugal	2,096	8,793	8,752	8,696	415
Spain	13,536 (8)	22,777	26,014	26,472	196 (9)
Sweden	1,059	2,877	2,895	3,113	294
Switzerland	1,729	4,091	4,383	4,594	266
United Kingdom	499	1,422	1,350	1,293	259
Canada	213	1,031	1,046	1,115	523
United States	7,047	28,952	28,868	28,224	401
Argentina	1,128	4,065	5,346	7,694	682
Bolivia	301	1,683	1,848	2,169	720
Brazil	4,803	20,494	20,399	21,696	452
Chile	866	3,565	4,067	4,720	545
Colombia	57	260	298	362	631
Costa Rica	28	72	86	112	405
Ecuador	64	362	339	376	584
Guatemala	8	29	30	34	434
Mexico	318	1,804	1,762	2,000	628
Nicaragua	11	44	49	50	468
Paraguay	12 (10)	32	43	65	525 (11)
Peru	113	599	699	761	673
Salvador	15	50	54	57	389
Uruguay	91	214	241	271	298
Venezuela	133 (10)	505	606	769	577 (11)
Turkey	211	937	881	932	443
Egypt	21	137	138	154	743
India	1,846	12,352	12,388	11,882 (12)	644
Iran	893	6,859	6,905	6,631	743
Iraq	4	40	35	35	807
South Africa	19	66	66	68	357
Australia	48	207	205	218	458
New Zealand	16	50	52	53	341
Japan	2,490	93,398	219,142	355,280	12,427

(1) 7th March 1938. (2) 7th December 1947. (3) Compared with 7th March 1938.
(4) Estimate of total circulation in Bohemia, Moravia, Silesia and Slovakia. (5) In Pengő.
(6) In forints, compared with the pengő circulation. (7) Including State and Allied Military currency.
(8) End of December 1941. (9) Compared with end of December 1941. (10) End of December 1939.
(11) Compared with end of December 1939. (12) India notes in circulation in Pakistan are not included.

Switzerland (as the clearest case among the European countries), the demand for fresh bank accommodation showed signs of subsiding. In the Swiss money and capital markets, where flexible conditions had been allowed to prevail all through the post-war period, the slackening of demand, together with an influx of funds from abroad, led almost automatically to a cheapening of credit, including a decided fall in the level of long-term interest rates.

Early in 1949, upon the continuance of the decline in the business turnover, the authorities in the United States, anxious to apply a credit policy designed to lessen the tendencies prevailing in the economy itself (whether towards boom or towards depression) began to ease, in a number of important respects, the prescribed requirements for the extension of credit, etc. (as set out on page 166 above). While it will clearly not be possible to avoid all painful adjustments after so prolonged and intense a boom as the one which, dating from the war, lasted well into 1948, there is no reason why the necessary adjustments should be made more difficult than they perforce must be.

The authorities in the United States are, for various reasons, in a position to adopt an expansionist credit policy without running any great risk of occasioning a new bout of inflation. First of all, recent estimates show a volume of private savings of the American people corresponding to 15 per cent. of the national income, which is as much as or more than the richer European countries ever achieved before the first world war (when taxation was still moderate), while, with few exceptions, these countries now only arrive at a proportion of 5 to 6 per cent. for private savings in relation to the national income. In the United States it may before long be a case of preventing savings from running to waste whereas, with one or perhaps two exceptions, the European countries will still have insufficient domestic savings at their disposal.

Secondly, the United States has its large gold reserves which — even if there were not the export surplus — would make it unnecessary for that country to worry about the emergence of a deficit in the balance of payments. The situation of most European countries is in this respect a very different one, which greatly limits their freedom of action in more than one field.

It is still too early to tell what the business trend will be in the United States under the influence of the anti-depression policy so promptly applied by the authorities. From a general point of view, it is clearly of importance that precisely the country which holds so strategic a position in regard to the world business trend has shown itself prepared to take counteracting measures at an early date. As regards most countries in Europe, it still seems to be incumbent upon them to continue the policy of consolidating their credit position and to rely more on the ease which will result from an improvement in the balance of payments than on relaxation of internal credit conditions. It is of interest in this connection to quote some words from the conclusion of the report for 1948 recently issued by the National Credit Council in France, where the opinion is expressed that "internal credit need not alone be asked to constitute the basis and the counterpart of the necessary increase in the volume of money but it is desirable that circumstances should permit a reinforcement of the gold and foreign-exchange reserves of the Bank of France, which would at the same time help to reconstitute the means available for international settlements and a currency circulation provided with an indisputable backing". This statement may be taken as indicating a growing realisation of the connection between the internal credit policy and the outcome of the balance of payments — a mechanism which works both ways.

Local-Currency Counterpart Funds.*

Deposits made on the special accounts opened in various European countries for "local-currency counterpart funds" exceeded the equivalent of $2,200 million by the end of March 1949; the equivalent of $1,300 million had been withdrawn and spent in certain approved ways, while the equivalent of $900 million remained on the accounts. The size of these figures brings home the great importance of these "counterpart funds" in the European economy during the past year.

"Counterpart funds" in local currencies arise as a direct consequence of United States aid to Europe under the European Recovery Program, as previously under "Interim aid". When commodities are received by European governments in the form of "grants" (or gifts) from the United States, the recipient governments sell the commodities on their internal markets, and the proceeds in the local currencies (at a rate of exchange agreed with E.C.A.) are placed to special accounts known as "counterpart funds". (In practice the local currencies are usually paid into the special accounts of counterpart funds before the sale of commodities takes place in the local markets.)

Interim aid: Local-currency counterpart funds.[1]
Position on 2nd April 1949.

Recipient country	E.C.A. approvals for use				Actual with-drawals
	Debt cancellations	Productive purposes	Other purposes	Total	
	local-currency equivalent in millions of dollars				
Austria	73	29	4	106	106
France	—	308	—	308	308
Italy	—	91	2	92	49
Total . .	73	428	6	506	463

(1) The unencumbered portions of local-currency deposits, for the domestic utilisation of which E.C.A. assumed responsibility of approval under the Foreign Relief Program and Foreign Aid Acts of 1947.

The main lines of the administration of counterpart funds under E.R.P. are laid down in American legislation concerning E.C.A. and are repeated in bilateral agreements made between the United States and the recipient countries. Five per cent. of the local currency thus deposited is allocated to the United States while the remaining ninety-five per cent. may be used by the recipient country, with the approval of E.C.A., for purposes including internal monetary and financial stabilisation, the stimulating of productive activity and the development of new sources of wealth, etc.

Counterpart funds do not arise for those countries which receive E.R.P. aid only in the form of loans, viz. Iceland, Ireland, Sweden and Turkey (nor, of course, for Portugal or Switzerland, which receive no E.R.P. aid at all). The evolution of the counterpart funds on account of E.R.P. aid is shown in the following table.

* The sources of the information contained in the following paragraphs are (a) E.C.A. Report on Recovery Progress and U.S. Aid (dated 14th February 1949) and (b) the monthly reports on local-currency counterpart funds prepared by E.C.A. (Fiscal and Trade Policy Division and Division of Statistics and Reports).

E.R.P. Local-currency counterpart funds.
Position on 2nd April 1949.

Recipient Country	Deposits required (1)	Deposits actually made (2)			E.C.A. approvals for use of 95 per cent. (3)				Actual with-drawals from 95 per cent. deposit (4)
		5 per cent. for U.S.	95 per cent. for domestic uses	Total	Debt cancellations	Productive purposes	Other purposes	Total	
	local-currency equivalent in millions of dollars								
Austria	204	7	137	144	12	—	—	12	12
Belgium	3	0	3	3	—	—	—	—	—
Denmark	43	2	31	33	—	0	—	0	0
France	723	27	514	541	100	189	—	289	289
Germany: Bizone	179	5	98	103	—	—	1	1	1
French Zone	65	1	24	25	—	—	—	—	—
Greece	116	4	84	88	—	23	89	112	64
Italy	227	8	156	164	—	342	93	435	—
Netherlands	160	5	90	95	—	—	—	—	—
Norway	53	2	43	45	22	—	—	22	22
Trieste	8	0	7	8	—	13	—	13	7
United Kingdom	562	24	460	484	433	2	0	433	433
Totals	2,331	87	1,647	1,733	567	569	182	1,318	828

(1) The agreed local-currency values of E.R.P. dollar aid on a grant basis.
(2) Local currency placed by recipient governments to the special accounts at the domestic central bank.
(3) Total amounts approved by E.C.A., including amounts not yet expended.
(4) Actual expenditure of amounts approved by E.C.A. The division of these amounts according to the purpose of utilisation is given in the next table.

The first column, "deposits required", indicates the dollar value of E.R.P. grant aid up to 2nd April 1949, adjusted to take into account the "drawing rights" given or received under the intra-European payments scheme (see chapter VIII). Actual deposits made usually lag behind the U.S. grant expenditure owing to the time necessary for E.C.A. to notify the recipient countries of the detailed items and for the governments to make the required deposits. By 2nd April 1949, $2,331 million had been notified in this way for E.R.P. and the equivalent in local currencies of $1,733 million had been deposited.

As regards the use of counterpart funds, i.e. of the amount actually deposited, the equivalent of $87 million, that is to say five per cent., was for the use of E.C.A. On 2nd April 1949, E.C.A had spent $30 million of this amount, $22 million for the purchase of strategic materials (industrial diamonds, rubber and sisal) in the United Kingdom and the balance almost wholly for the administrative expenditure of the E.C.A. missions in the various countries and by the Office of the Special Representative of E.C.A. in Paris.

But in so far as "aid" is concerned, the real interest attaches to the ninety-five per cent. which may be utilised for approved purposes in the domestic economy. In general, proposals for expenditure of such counterpart funds are first formulated by the recipient government and discussed with the E.C.A. mission in the country concerned. The recommendations of the mission are reviewed by E.C.A., Paris, and E.C.A., Washington; the latter office formulates a final recommendation after discussion with other organs of the U.S. Government (State, Treasury and Commerce Departments and the Federal Reserve Board, all of which are represented on the National Advisory Council, and E.C.A. Public Advisory Board).

The establishment of internal financial stability is a prerequisite to the accomplishment of the aims of E.R.P. Subject to this basic factor, utilisation of local-currency counterpart funds is directed towards the stimulating of productive activity and the exploration for, and development of, new sources of wealth, in order to achieve the maximum recovery in the participating countries.

Under the Economic Co-operation Act of 1948, E.C.A. is responsible not only for the counterpart funds arising under E.R.P. but also for the utilisation of the unencumbered portions of local-currency deposits made in connection with "Interim aid" (under the Foreign Relief Program and Foreign Aid Act, both of 1947).

The broad purposes for which E.C.A. has given approval are classified in the two preceding tables. Approvals total some $1,820 million in all. Generally, approvals are soon followed by utilisation, but it is noteworthy that for Greece, Italy and Trieste approvals have gone ahead of the amount deposited. For Italy it is significant that, compared with $527 million approvals, only $49 million has been actually expended; a programme (including $122 million for agriculture) has been approved but actual releases are made only on the basis of specific projects.

To obtain a clear picture of the amounts actually expended from "Interim aid" and E.R.P. counterpart funds, it is useful to draw up a combined statement.

E. R. P. and Interim aid: Local-currency counterpart funds actually withdrawn for domestic purposes.
Position on 2nd April 1949.

Recipient country	Actually withdrawn				Remaining unused on special accounts	Totals
	Debt cancellations	Productive purposes	Other purposes	Total		
	local-currency equivalents in millions of dollars					
Austria	85	29	4	119	124	243
Belgium	—	—	—	—	3	3
Denmark	—	0	—	0	31	31
France	100	497	—	597	225	822
Germany: Bizone	—	—	1	1	97	98
French Zone	—	—	—	—	24	24
Greece	—	23	40	64 (1)	20	84
Italy	—	49	—	49	199	248
Netherlands	—	—	—	—	90	90
Norway	22	—	—	22	21	43
Trieste	—	7	—	7	1	7
United Kingdom	433	0	0	433	27	460
Totals	640	606	45	1,291 (2)	862 (3)	2,153 (4)

(1) Including $1.8 million of temporary advances.
(2) $463 million on account of "Interim aid" and $828 million for E.R.P. (see previous tables). Small differences arise from adding figures rounded off to the nearest million dollars.
(3) $43 million on account of "Interim aid" and $819 million for E.R.P.
(4) The simple addition of the two previous columns.

Out of $1,291 million actually withdrawn from the special accounts, about one-half has gone for debt cancellation (nearly three-quarters of it in the United Kingdom) and the other half for productive purposes (nearly five-sixths of it in France). Debt cancellation in the United Kingdom and productive purposes in France thus make up three-quarters of all the actual expenditure of counterpart funds for domestic uses up to 2nd April 1949.

The $497 million utilised in France for the promotion of production can be divided into a few broad classes: $226 million has gone to light and power facilities (electricity and gas); $86 million to railways; $85 million to coal mining; $40 million to strategic materials; $23 million to the merchant and fishing fleets; and the remainder to a number of miscellaneous industries (agriculture receiving $8 million).

The $49 million utilised in Italy for productive purposes has been used entirely for the railways.

The only considerable utilisation of counterpart funds for "other purposes" than debt cancellation or production has been the $40 million in Greece; $18 million has gone for the care of refugees and $17 million for housing (and further considerable amounts have been approved for the same purposes).

The table shows that, after withdrawals of $1,290 million, $860 million still stood on the special counterpart accounts on 2nd April 1949; with the $90 million put at the disposal of E.C.A. in local currencies (5 per cent. of the local counterpart of E.R.P. grants), the total amount paid into the local-currency counterpart accounts reaches $2,240 million — a measure of the Interim aid and E.R.P. deliveries in grant form up to 2nd April 1949.

These few paragraphs do not amount to more than a brief description of the counterpart mechanism, with an indication of the amounts involved. As the E.R.P. deliveries grow and reporting time-lags are made up, the volume of local-currency counterpart funds deposited and released for domestic use will run into the equivalent of several milliards of dollars. It is no exaggeration to say that the direct effect of E.R.P. deliveries and the wise use of the resources thus made available will be a decisive factor in the re-establishment of economic and financial order in western Europe.

As regards the release of counterpart funds, it should be pointed out that the Act and the bilateral agreements specify that each participating country shall make appropriate provision for "... taking financial and monetary measures necessary to stabilise its currency, establish or maintain a valid rate of exchange, to balance its governmental budget as soon as practicable, and generally to restore or maintain confidence in its monetary system...". The responsibility of E.C.A., one of whose functions it is to assist the participating countries and, in that connection, to release the counterpart funds for approved purposes, is clearly very great.

Much thought has naturally been given to the principles involved in the release of counterpart funds, and the rule is that, in each country, the release should be based on an assessment of the rôle which counterpart funds can play within the economy considered as a whole. Within the general field of action determined by the need of promoting financial stability (a need which is very much stressed), counterpart funds may be released to finance projects which, after examination of total investment requirements and possible sources of internal financing, are considered to be of first-rate importance for production. But counterpart funds may in no case be expended to postpone essential economic and financial reforms. Indeed, the counterpart funds should be used "... for the purposes of internal monetary and financial stabilisation, for the stimulation of productive activity, and the exploration for and development of new sources of wealth or such other expenditures as may be consistent with the Economic Co-operation Act ...". And this Act may be summarised as having the following main purpose in view: to aid the participating countries to become independent of extraordinary outside economic assistance within the period of operation of the E.C.A.

* * *

There is no doubt that the technique of accumulating counterpart funds and of releasing them for definite purposes constitutes an important part of the administration of Marshall aid, which involves the largest international movement of funds that has ever taken place in time of peace.

For each participating country it is clearly the actual receipt of goods and services from abroad that makes a decisive addition to the total resources and in that way represents the essential element of the aid.

It is also clear that, in order to determine how the aid is really being used, account must be taken of the "entire economic-financial situation in the participating country" — which appears to be one of the points stressed among the guiding principles for the release of counterpart funds. The economic effect of the aid must thus be judged in relation to the general lines of action with regard to the amount of total resources available in each country, its budgets, investments, credits, costs and prices, foreign trade and exchange rates and, more particularly, in relation to the money and credit situation.

In this connection, the accumulation and use of counterpart funds has naturally focussed attention on a phenomenon that existed in many countries long before Marshall aid was given. A similar set of problems arose, in fact, when countries after the war put to use the proceeds of foreign loans and credits (as the British did with regard to the American and Canadian loans and the French with regard to several foreign credits). It is even possible to find a simpler case, viz. when a country uses up its own monetary reserves of gold and foreign exchange; it is, indeed, helpful to make comparisons with what happens in such cases, in order to throw light on the problems involved. But the situation can perhaps best be understood from the examination of a few concrete cases.

1. The Netherlands has received Marshall aid and accumulated counterpart funds but no releases had been made by 2nd April 1949 (the date to which the table on page 192 refers). That does not mean, however, that no use had been made of the material resources which arrived. The very fact that a country has an over-all deficit on the current account of the balance of payments signifies — as is so clearly brought out by the modern methods of national accounting — that the volume of investments in that country exceeds the flow of domestic savings. Had it not been for the receipt of material resources from abroad, the tension between the large volume of investments (if maintained) and the insufficient savings would have given rise to an inflationary creation of credit. Thanks to the arrival of the foreign resources and the accumulation — one might even say the sterilisation — of the counterpart funds at the central bank, the credit system was able to find the funds for the financing of the investment projects without any inflationary tendency.

   It is clear that in the example chosen — which corresponds to what has happened in more than one country — the actual "use" of the resources has been immediate; thus if the amounts accumulated as counterpart funds were to be released and spent at a later date for new investment purposes, there would then be no further provision of corresponding material resources and the result would be an inflationary tendency. The Nederlandsche Bank explains in its report for 1948 that, in so far as the situation which has arisen continues, "maintenance of monetary equilibrium demands that the local-currency counterpart be employed in such a manner that the neutralising effect on the inflationary tendencies still prevalent is maintained. This can be attained by designating the counterpart funds for redemption of government debt to the central bank or for payment into the government's Treasury for financing productive expenditure already provided for in the budget". If the funds went to finance expenditure already provided for in the budget the use thus made of them would clearly not give rise to any fresh expenditure.

2. Another, somewhat simpler, case is that of France, where the equivalent in French francs of some $597 million of E.R.P. and "Interim aid" counterpart funds had, up to 2nd April 1949, been released and actually withdrawn to provide cover for real-investment expenditure in the budget (under the so-called "Monnet Plan"). This case is simple because it corresponds fairly closely to what has happened in the past when a country has

borrowed abroad and used the funds thus received for the financing of domestic investment projects. In such cases the provision of financial means for the projects in question has gone hand in hand with the actual using-up of resources and there has, therefore, been no separation between the methods of internal financing and the provision of foreign exchange to pay for the import surplus which resulted. When that is the case, the receipt and the use of Marshall funds have in themselves neither an inflationary nor a deflationary effect. As far as the receipt of the aid and its application to investment expenditure was concerned, the result was, in fact, the avoidance of inflationary pressure, which would have ensued if the volume of investments on the scale contemplated had continued to be financed by resort to the banking system.

In France, however, the amount released up to 2nd April 1949 included the equivalent of a further \$100 million withdrawn for the purpose of debt cancellation — in effect, for repayment of government debt to the Bank of France.

It is probable that when, in 1948, the aid was actually received there was in France a tension between investments and savings; and it has, therefore, no doubt seemed appropriate that some of the counterpart funds should be definitely removed from the possibility of further spending (a measure which, incidentally, is in conformity with the ideas expressed in the report of the Nederlandsche Bank).

3. As may be seen from the table on page 192, the United Kingdom is the country which has had the largest percentage withdrawals of counterpart funds and practically the whole amount withdrawn has been used for retirement of debt. The effects of the receipt of the aid should be viewed against the progressive improvement in the credit situation and the balance of payments in the course of 1948. In his budget speech on 6th April 1949, the Chancellor of the Exchequer referred to the reduction by £453 million in the total national debt between the end of March 1948 and the end of March 1949. He added that this happy result arose from two causes: "First, the over-all budget surplus which has been realised and, second, the sterling proceeds of the Marshall aid special account, of which £107 million has been applied, with the consent of the U.S. Government, to the redemption of short-term debt." It is of interest to compare this with the main figures for the balance of payments in the second half of 1948.

The reduction in sterling liabilities was achieved by means of the surplus, mainly vis-à-vis the sterling-area countries, in the current account of the balance of payments plus certain direct releases of dollars. As may be seen from the table, it was thanks to the receipt of the aid under E.R.P. that over-all balance could be maintained notwithstanding heavy "unrequited" exports mainly to sterling-area countries. In his budget speech, the Chancellor of the Exchequer specifically mentioned that the debt reduction (resulting from the budget surplus and the use of counterpart funds) has been mostly for the meeting of floating-debt maturities "which arose from the reduction in sterling balances of oversea holders". Thus it is permissible to say that, from an economic point of view, the equivalent of Marshall aid covering the deficit in relation to the dollar area has been one of the factors making possible a net reduction in sterling liabilities.

United Kingdom: Balance of Payments July-December 1948.

Items	July-December 1948 (provisional)
	In millions of £ sterling
Current account:	
Western hemisphere	— 140
Sterling area	+ 160
Other countries	+ 10
Total	+ 30
Capital account:	
Reduction in sterling liabilities	192
Increase in British assets abroad	7
Total	199
Net gold and dollar deficit	169
Difference	+ 30
The net gold and dollar deficit has been covered by:	
Receipts under E.R.P.	147
Use of gold and dollar holdings	22*
Total	169

* Includes £6 million drawn by India from the I. M. F.

4. In Italy releases have been approved but no withdrawals had actually taken place up to 2nd April 1949, so that the amounts accumulated on the E.R.P. special account remained untouched. The whole year 1948 showed deficits on the current accounts of the balance of payments; but towards the end of the year monthly export surpluses had begun to reappear in Italy and it is quite possible that around the turn of the year 1948–49 equilibrium — at least for the time being — had been reached on the current account of the balance of payments. No such result could have been attained without internal investments' being kept down to the volume of domestic savings — and it is well known that in Italy considerable restraint has been observed in appropriating funds for reconstruction of houses and for public works other than the restoration of the railway systems, ports and roads to working order, etc. Since domestic expenditure for consumption and investment could thus be kept in balance with available resources, without counting in full the Marshall aid, it followed that the use of E.R.P. dollars to pay for a greater part of the excess imports from the western hemisphere would set free resources for other visible and invisible exports, some of which might even lead to payments in actual dollars (as might happen to part of the income from tourist traffic). The non-utilisation of the counterpart funds consequently resulted in a strengthening of the gold and dollar reserves. Actually, the chain of events has

been somewhat more complicated, owing to other capital transactions, but the analysis just given brings out some of the most essential factors in the development. It may be added that the Governor of the Bank of Italy, in his report for the year 1948, states that the sale of goods received from abroad as a grant amounted in 1948 to some Lit. 150 milliard — a sum almost equal to that which the Bank of Italy has advanced to the Exchange Control for the financing of the accumulation of foreign exchange.

By starting public works or encouraging other forms of outlay, it would not have been difficult to increase total domestic expenditure in Italy to a point at which a substantial deficit in the balance of payments would have emerged, with no strengthening of the gold and dollar reserves. In that country there are, however, domestic tasks which cry out to be taken in hand and it may squarely be contended that, in so far as the fundamental purpose of the Marshall aid is to "aid the participating countries, through their own individual and concerted efforts, to become independent of extraordinary outside economic assistance within the period of operation of the E.C.A.", the greatest possible encouragement should be given to the replenishment of monetary reserves, *since the absence of such reserves* will always put the countries in question in a vulnerable position.

The effect of accumulation, release and withdrawal — i.e. the technique of handling the counterpart funds — must thus be seen in relation to the total available resources of domestic origin, investment programmes, etc.; but that is not to say that the technique in itself is of no importance. The investment programme of a country may clearly be influenced by the technical decisions taken, i.e. it may, for instance, be cut down if releases should not be made for the purposes contemplated. Conversely, there is perhaps a greater danger that the accumulation and consequent magnitude of the counterpart funds may be a temptation to expenditure, even though the aid through which the counterpart funds came into being had, from an economic point of view, already been fully utilised when the dollar imports arrived, and had at that time specifically helped to keep back inflation. Accumulation as such clearly has its dangers; it may, therefore, be wise to allow releases as a continuous process, whether for productive purposes or for debt cancellation. Since the ultimate effect of any action has to be taken into account, it is obviously most important to ensure that aid already made full use of is not, via the counterpart mechanism, spent twice, so to say; for if that happens an inflationary pressure will be exerted which may upset the stability that was to have been attained and reinforced.

VIII. Intra-European Payments and Compensations.

The Agreement for Intra-European Payments and Compensations, which had been preceded by months of careful examination of the problems involved and by much drafting and redrafting, was signed in Paris on 16th October 1948 by the ministers of sixteen European governments and by representatives of the Military Governors of the Bizone and French Zone of Germany and of the Free Territory of Trieste — in all, the "nineteen" who form the Organisation for European Economic Co-operation (O.E.E.C.). The Organisation itself was set up under a Convention of 16th April 1948 and during the first six months of its existence it was able to make the allocation, among the countries concerned, of the American aid received under the European Recovery Program (E.R.P.) for the year 1948–49 (the scheme of apportionment having been worked out by agreement between the beneficiaries) and also to complete a European agreement which had the effect of redistributing, inside Europe, part of the American aid so allocated.

While the drawing-up of an international treaty between so many participants and the reconciliation of the inevitably conflicting local interests was necessarily a most complicated task, it is noteworthy that the Agreement reposes upon two fairly simple fundamental principles:

(i) "Western-hemisphere" and "overall" payments deficits were dealt with by a combined operation. On the one hand, the E.R.P. dollar allocations were made in proportion to the estimated deficits of the participating countries vis-à-vis the western hemisphere and, on the other hand, a further sub-allocation of aid inside Europe was made under the payments scheme in order to meet the estimated intra-European deficits, as revealed by the movement of the accounts established for the working of the bilateral payments agreements. These accounts — it should be noted — not only relate to European territories but also comprise the extensive monetary areas associated with sterling, the Belgian and French francs and the Dutch florin, and the "intra-European" payments scheme thus extends its influence over a large part of the world.

The combination of the western-hemisphere deficits and the intra-European surpluses and deficits of the participating countries (including their monetary areas) was taken to be a sufficient measure of the "overall" deficits. Certain territories were perforce excluded, the most important being the countries of eastern Europe and the U.S.S.R. The estimates which were finally agreed for the year ending 30th June 1949 are summarised in the following table.

Each of the participating countries received dollar aid in proportion to its estimated deficit with the western hemisphere and it either gave or received "indirect aid", in the form of "drawing rights" inside Europe, according to its European position. In this way, the creditors on current account of intra-European payments pass on to the debtors the equivalent of part of the aid received under E.R.P., the aim being to facilitate the flow of intra-European trade, so essential for the proper working of E.R.P.

(ii) The second general principle observed was that of the automatic "off-setting" of certain debts and credits inside Europe. This operation, taking the form of so-called "first-category compensations", is a further development of the scheme already adopted in the autumn of 1947, under which balances on the payments-agreements accounts were reported by the central banks of the countries concerned to the Bank for International Settlements, acting as their Agent.

E.R.P. dollar aid and intra-European payments scheme: July 1948–June 1949.

Country	Total dollar aid	Basic dollar aid	Intra-European payments scheme: Drawing rights granted	Intra-European payments scheme: Drawing rights received	Intra-European payments scheme: Net receipts (+) under I.E.P.S.	Total dollar and net European aid
	in millions of dollars					
Austria	215	212	3	67	+ 64	279
Belgium-Luxemburg	248	29	219	11	− 208	40
Denmark	109	104	5	12	+ 7	116
France	981	971	10	333	+ 323	1,304
Germany:						
Bizone	411	302	109	99	− 10	401
French Zone	99	84	15	16	+ 1	100
Greece	145	145	—	67	+ 67	212
Iceland	5	5	—	—	—	5
Ireland	78	78	—	—	—	78
Italy	555	508	47	27	− 20	535
Netherlands	470	458	11	83	+ 72	541
Norway	83	67	16	48	+ 32	115
Portugal	—	—	—	—	—	—
Sweden	47	12	35	10	− 25	22
Switzerland	—	—	—	—	—	—
Trieste	18	18	—	—	—	18
Turkey	40	11	29	17	− 12	28
United Kingdom	1,239	919	320	30	− 290	949
Commodity Reserve	13	13	—	—	—	13
Totals	4,756	3,938	818	818	± 565	4,756

The payments plan based on these principles had the active participation of the Economic Co-operation Administration (E.C.A.), the American organisation charged with the application and supervision of E.R.P. When goods supplied under E.R.P. grants (as distinct from the part of the aid furnished in the form of "loans") are available for sale in the recipient countries of Europe, the proceeds in national currency, called "counterpart funds", are placed to a special account in the central bank, where they are earmarked for approved purposes. For the purposes of the payments scheme, it became necessary to establish a new form of E.R.P. aid, neither loan nor grant, called "conditional aid", the condition being that, on receipt of the dollar aid, the countries concerned place an equivalent amount of their national currency at the disposal of their debtors on current account of the balance of payments. In that way, the creditor countries are able to obtain dollars against a surplus of exports to the other participants inside Europe, and with these dollars they are able to pay part of their deficits in relation to the western hemisphere. Thus "conditional aid" was a basic element of the plan and the creditors were not required to make available more of their currency than was covered by E.C.A. "firm allotments of conditional aid". (It may be noted in this connection that it is the country receiving drawing rights which is bound to place an equivalent amount of its national currency to its special account of "counterpart funds".)

In the practical arrangement of the scheme a high degree of co-operation was demanded, especially from the creditors. The "western-hemisphere" deficits and the allocations of dollar aid had been agreed upon before the intra-European payments plan was drawn up. "Conditional" dollars for the creditors were, therefore, not "additional" dollars but part of the original dollar aid they expected to get in any case. How the payments plan affected the various countries will have been gathered from the table.

It is evident that, for the system to work smoothly, the western-hemisphere deficit of any country, which sets the limit of possible "conditional aid" for that country, must be larger than its European surplus, otherwise drawing rights granted would be insufficient. The only country for which this condition was (and still is) of particular importance was Belgium, whose real European surplus was probably greater than its western-hemisphere deficit.

Before proceeding to describe the working of the plan it may be useful to give a summary of the Agreement itself. The Agreement for Intra-European Payments and Compensations is divided into two parts, the first dealing with compensations and the second with drawing rights. In summarising the Agreement it is convenient to maintain this distinction although, in practice, all operations are carried out simultaneously on the same value date each month.

Compensations. The Agreement of 16th October 1948 formally terminated the First Agreement for Multilateral Monetary Compensations of 18th November 1947, for which the Bank for International Settlements, as indicated above, had acted as Agent. The earlier agreement and the mechanism of the "compensations" were fully described in the eighteenth Annual Report, pages 142 to 153, and it is unnecessary to go into greater detail here.

The principles and mechanism of these compensations were taken over in the new scheme with a notable extension of the automaticity of operations. Under the earlier agreements, Belgium (and Luxemburg), France, Italy and the Netherlands (which were the signatory countries), plus the Bizone of Germany, were "permanent" members and only these accepted automatic 'first-category" compensations; all other adherents to the agreement, viz:

Austria, Denmark, Greece, Norway, Portugal, the United Kingdom, Sweden, Switzerland, Turkey and the French Zone of Germany, were "occasional" members, i. e. they retained the right to reject any of the Agent's propositions for compensations. Under the new agreement all countries participating in the scheme (except Portugal and Switzerland, as non-recipients of E.R.P. aid) undertook to accept all "first-category" (or offset) operations prescribed automatically by the Agent; to the extent that these compensations reduce any deficit on the month, they economise the use of drawing rights. "Second-category" operations, which imply a certain transferability of currencies and entail an increase in the amount of currency balances for one of the countries affected, remained optional, as before, and subject to the general transfer policy of the countries concerned.* First-category operations involving Portugal and Switzerland also remained optional for all countries.

Drawing Rights. Each of the signatory countries which was estimated at the beginning of the plan to be in surplus on its current balance of payments with other O.E.E.C. countries established "drawing rights" in

Intra-European payments scheme: Drawing rights established (granted and received).

Amounts established for year 1st July 1948 to 30th June 1949 / Recipient countries	Countries granting drawing rights												
	Austria	Belgium	Denmark	France	Germany: Bizone	Germany: Fr. Zone	Italy	Netherlands	Norway	Sweden	Turkey	United Kingdom	Totals
	in millions of dollars												
Austria	—	4.5	0.1	2.0	32.0	0.5	—	1.0	1.5	—	—	25.0	66.6
Belgium	—	—	—	—	—	—	11.0	—	—	—	—	—	11.0
Denmark	—	6.5	—	2.7	1.0	0.2	—	—	—	—	1.5	—	11.9
France	—	40.0	—	—	63.0	14.0	11.0	—	5.0	—	—	200.0	333.0
Germany:													
Bizone	—	17.0	—	—	—	—	10.1	—	8.0	5.0	12.0	46.5	98.6
French Zone	—	4.0	—	—	—	—	2.6	2.0	—	—	1.5	5.5	15.6
Greece	0.4	13.0	2.0	5.0	4.3	0.1	7.0	5.0	2.0	5.0	13.0	10.0	66.8
Italy	2.0	—	—	—	—	—	—	—	—	—	—	25.0	27.0
Netherlands	—	72.5	—	—	8.5	—	—	—	—	2.0	—	—	83.0
Norway	—	23.0	—	—	—	—	0.5	2.5	—	21.8	0.5	—	48.3
Sweden	0.7	6.0	3.0	—	—	—	0.1	—	—	—	—	—	9.8
Turkey	—	2.0	—	—	—	—	5.0	0.8	—	1.0	—	8.0	16.8
United Kingdom	—	30.0	—	—	—	—	—	—	—	—	—	—	30.0
Totals	3.1	218.5	5.1	9.7	108.8	14.8	47.3	11.3	16.5	34.8	28.5	320.0	818.4

Note: Six of the nineteen signatory countries are missing from the table above. Portugal and Switzerland did not receive E.R.P. aid and did not take part in the European system of drawing rights; Luxemburg is included with Belgium, and Ireland and Iceland, being members of the sterling area, are covered by the figures for the United Kingdom; Trieste did not take part in the European scheme. The figures in the table are taken from Annex C of the Agreement of 16th October 1948 with the addition of $8 million, the drawing right given by the United Kingdom to Turkey according to an agreement made between the two countries on 25th January 1949.

* For a detailed examination of the transferability of sterling as regards European countries and of its relation to second-category compensations, see the eighteenth Annual Report, page 149.

favour of the countries which were expected to have the corresponding payments deficits (requiring to be financed because means of payment in the shape of existing resources or credit margins were not available). The amounts of drawing rights were "established" in dollars, as shown in the preceeding table, and they remained denominated in dollars until they had been "made available" — generally in the currency of the country granting the drawing rights (but occasionally in the currency of the partner or in a third currency).

It should be noted that no "pool" or "fund" has been established, and the Agent is an agent and not a principal. The drawing rights can be "made available", or drawn, only by the Agent and in accordance with the provisions of the Agreement and of the directive to the Agent; the amounts drawn are passed directly from the creditor to the debtor country without any funds' passing even momentarily through the books of the Agent.

Drawing rights as shown in the table apply to the whole year from 1st July 1948 to 30th June 1949. As, at the time when the Agreement was signed, funds had been voted by Congress only up to 31st March 1949, not more than 75 per cent. of the drawing rights could be made available before that date. The remaining 25 per cent. became available in April 1949.

Two changes were made in the table of drawing rights for the year 1948–49 as it had appeared in Annex C of the Agreement of 16th October 1948:

(i) By agreement concluded between the two countries in January 1949, the United Kingdom extended a drawing right of $8 million to Turkey. In February 1949, the Council of O.E.E.C. confirmed the withdrawal of a Turkish reservation on Part II of the Agreement and the establishment of the new drawing right (included in the above table), raising the total from $810.4 million, as in the Agreement, to $818.4 million. Turkey took part in the system of drawing rights from February 1949 onwards.

(ii) Although estimates were established for the whole year from 1st July 1948 to 30th June 1949, the Agreement came into force only from 1st October 1948, so that adjustments had to be made for the quarter July–September 1948, when the plan was not in force. These adjustments were introduced by a second protocol, signed on 31st March 1949. Adjustments were made to take into account the "off-shore purchases" amongst participating countries during the third quarter of 1948. In principle, dollars placed at the disposal of exporting countries as payment for off-shore purchases made by importing countries were deducted from the "basic aid" allocated to the importing countries, and the year's drawing rights were left unchanged. Importing countries, however, retained the right to utilise drawing rights, where they still existed, to repurchase from the exporting countries an amount of dollars equivalent to the off-shore purchases (these dollars being, of course, in excess of the dollar aid which the exporting countries would otherwise have received under E.R.P.). However, in order not to cause embarrassment in those cases where the exporting country had already disposed of the dollars, drawing rights were reduced in three cases, as follows: Bizone in favour of France by $23.3 million, Bizone in favour of Austria by $2.9 million and Turkey in favour of Greece by $0.7 million. In all other cases the importing countries retained, during the last months of the scheme, the right of dollar repurchase by the use of drawing rights. (As the adjustments mentioned in this paragraph apply to the June-September quarter of 1948, no changes on this account have been made in the table of drawing rights for the year 1948–49 given above.)

The Agreement provides that drawing rights are to be made available monthly, normally on the basis of the payments deficit on the month, through the adopted mechanism (as described more fully below). Provision was also made for additional amounts to be drawn in special circumstances, e. g. for the repurchase of gold which had been paid in previous months. Drawing rights as established could be revised only in special circumstances; any drawing rights remaining unutilised at the end of the period were not to be cancelled.

Forming part of the Agreement are three Annexes: Annex A deals with balances which may be excluded from the compensations; Annex B deals with exchange rates; and Annex C contains statistics of the drawing rights established and also of the so-called "agreed existing resources". It had been expressly agreed that certain existing resources should be taken into account before drawing rights were exercised. These were as shown in the table.

Agreed existing resources.

Country possessing resources	Country in whose currency resources were held	Equivalent of the national-currency amount in millions of dollars
Greece	United Kingdom	13.0
Italy	United Kingdom	45.0
Bizone	Sweden	9.8
	Total . . .	67.8

Thus agreed amounts of Greek and Italian sterling holdings were to be utilised before Greece and Italy respectively could avail themselves of their drawing rights in relation to the United Kingdom, and the Bizone had similarly to use up its Swedish crowns before being able to utilise drawing rights in relation to Sweden.

Although this is not mentioned in the Agreement, the United Kingdom, in connection with the arrangements made in Paris, agreed that sterling funds, equivalent to $150 million, held by the Netherlands, Sweden and Turkey could be used to cover deficits which, it was estimated, would arise in the balances of payments of these countries with the United Kingdom during the period of the Agreement. This sum, added to the $58 million shown in the above table and a net amount of $290 million in drawing rights, gives a total of nearly $500 million as having been made available by the United Kingdom to O.E.E.C. countries for payments by them in sterling during the year 1948–49. The surplus exports, visible and invisible, of the United Kingdom alone were estimated at not more than one-fourth of this amount, the remaining three-fourths coming from the rest of the sterling area.

In order that the provisions of the Agreement should come into force from 1st October 1948, i. e. without waiting for its ratification by all the participating countries, a protocol of provisional application was adopted at the same time as the Agreement.

After the signature of the Agreement, on 16th October 1948, a number of technical measures had to be taken with great dispatch to enable the scheme to be put into working order in time for the first compensation to be carried out on the basis of the accounts as at 31st October 1948. These technical measures included authorisations given by each of the central banks to all of its partners: (a) to disclose the state of its accounts at the end of each month to the Bank for International Settlements as Agent of the scheme — this involving to that extent the lifting of banking secrecy — and (b) to give authority for the instructions of the Bank for International Settlements as Agent to be accepted for debiting and crediting the accounts for the purposes of the payments plan.

The Agent circulated an aide-mémoire to the central banks, specifying the forms of telegrams to be used and going into the necessary details with regard to the reporting and related matters. Further, the central banks gave information to the Agent on a number of questions, e. g. the currency in which drawing rights would be made available. On the part of E.C.A., it was necessary to set up a mechanism to provide firm allotments of conditional aid on the successive value dates and to coordinate the Administration's own activity with that of the central banks and the Agent. On the part of the Agent, a series of internal administrative measures had to be taken to cope with the stream of figures coming in at the end of the month, to sift and reconcile the information received, and to handle the resulting data for the purpose of calculating the compensations and drawing rights.

* * *

An essential factor in the operation of the payments scheme is the monthly reporting by European central banks to the Bank for International Settlements, acting in its capacity as Agent.

At the close of business on the last working-day of each month each central bank sends a telegram to the Bank for International Settlements. The telegram, followed by confirmation on a special form, gives the position of the accounts which the central banks of all other participating countries hold at the reporting bank (generally, in the currency of the reporting country). In addition, it contains information regarding exchange rates, credit margins and working balances and also gives details as to payments made in gold and dollars between the participating countries, forward exchange transactions and any other information (such as movements to or from blocked accounts) necessary to maintain the comparability of the figures reported each month.

Utilising this information, the Agent is able to establish (i) the position of each country vis-à-vis its partners at the end of the month and (ii) the net movement from month to month, by means of which the payments deficit or surplus on the month is measured in each bilateral relationship.

On the basis of the position of each country the automatic compensations are calculated, and on the basis of the monthly deficits the amounts of drawing rights to be made available are ascertained. The compensations are thus calculated on the total balances while the drawing rights are made available according to the adjusted movement of the balances.

The Agent has received a directive from O.E.E.C. which lays down the principles to be applied and also sets a strict timetable for the operations each month. By the end of the second working-day the Agent should have received all necessary information from the central banks, a further day being allowed for reconciliation and rectification. From the fourth to the eighth working-day the Agent calculates the compensations and drawing rights. On the ninth working-day the Agent sends instructions to the central banks for all automatic operations, i.e. first-category compensations on total balances and the utilisation of drawing rights calculated on the monthly deficit; at the same time the Agent makes proposals for compensations involving Portugal and Switzerland and also for second-category operations, all of which have to be submitted for the approval of the central banks concerned. By the eleventh working-day replies to these proposals have been received, as well as any requests for additional drawing rights. On the twelfth working-day the Agent sends final instructions to the central banks and requests E.C.A. to make "firm allotments of conditional aid" to the countries granting the drawing rights. The value date for all operations is the fifteenth working-day of the month following that to which the end-of-month statistics refer.

Calculations, for which the Agent has five working-days, thus cover:

(a) the automatic first-category compensations on total balances; and

(b) the drawing rights based on the deficits of the previous month.

The first step for both of these calculations is to establish the end-of-month position of each country vis-à-vis its partners. In cases where there are double accounts in accordance with the payments agreements (such cases forming the majority), it is necessary to take the net position: if, for instance, the Bank of England holds French francs and the Bank of France holds sterling, the difference is taken in order to establish the net position between the two countries. All the net positions are then converted into U. S. dollars, the chosen unit of account, for the sake of comparability and to facilitate the current working of the scheme.

In order to calculate the automatic first-category compensations, the table showing the net positions is adjusted to take into account working balances, which may be excluded from the compensation at the request of a reporting country. The resulting adjusted positions are then subjected to a mathematical process which produces the "optimum circuits" of first-category compensations, i.e. those giving the largest reduction of balances for the group as a whole ("balances" in this sense applying to the net debtor as well as net creditor positions). Each "circuit", to be complete, must comprise at least three countries, the first being creditor of the second, the second creditor of the third and the third creditor of the first. This system of automatic first-category compensation means that a country's assets are automatically offset against its debts, in so far as there is a third country which completes the circuit. Thus countries which are preponderantly debtor or creditor rarely enter the automatic circuits but it may be noted that, during the first six months of the scheme, all the thirteen countries which adhered to the automatic system had entered the circuits at least once. (And, of course, all countries are open to proposals for second-category compensations.)

For the calculation of drawing rights, the net positions at the end of each month are compared with the positions of the previous month, adjusted for the operations, compensations and drawing rights, prescribed by the Agent in the previous month. The movement of the net positions during the month is further adjusted for gold and dollar payments, movements to and from unreported accounts and other items affecting the comparability of the figures, in order to obtain the deficit or surplus of payments on the month for each bilateral relationship. In general these calculations determine the drawing rights to be given or received automatically on the month in those cases where drawing rights have been established, i.e. in 63 out of the 78 bilateral relationships forming the total for the thirteen countries concerned. Further adjustments had, however, to be made: (i) particularly for the effect of the first-category compensation calculated for the current month (where this reduces the deficit on the month and thus the need for drawing rights); (ii) to ensure that no more than 75 per cent. of the drawing rights would be used up before the end of March 1949; and (iii) to comply with a number of provisions which have been laid down as instructions to the Agent.

These instructions may affect particular cases as, for example, when ad-hoc accounts have been opened for the utilisation of drawing rights; or the instructions may be of a more general nature, providing, for instance,

(a) that drawing rights should not be used materially to increase a balance or decrease a debt compared with the position at 30th September 1948; if a country in whose favour drawing rights have been established builds up a balance by having two successive surpluses which in the third month are followed by a smaller deficit, no drawing right is given for the third month nor, indeed, until the balance has been drawn down to about the level at which it stood when the scheme came into effect;

(b) that drawing rights should not be made available by a country which has a debt to the recipient country until that debt has been reduced below the credit margin, etc.

It is also possible for countries to demand "additional" drawing rights for specific purposes such as repurchase of gold paid in a previous month, and such "additional" drawing rights have also to be brought into the operation.

After these calculations, the Agent is in possession of all information necessary for the automatic part of the monthly working and can turn to the non-automatic operations. For that purpose it is necessary to readjust the end-of-month positions for the calculated effect of the automatic compensation and, on that new basis, to calculate further first-category circuits including Portugal and Switzerland. Moreover, with the information at his disposal the Agent has to prepare second-category operations (which may lead to the increase of a balance) with the object of relieving the difficult payments positions and, if possible, preventing gold movements inside Europe.

The Agent then sends out to the fifteen central banks (including Portugal and Switzerland) telegrams in three parts: the first part gives information regarding the calculation of the drawing rights; the second part contains the Agent's instructions for the automatic operations (both first-category compensations and the utilisation of drawing rights); the third part contains propositions for compensations with Portugal and Switzerland and for second-category operations. When the replies have been received to the third part of the telegrams, the resulting operations are prescribed on the same value date as those which are the subject of the second part of the telegrams, i.e. on the fifteenth working-day.

The Agent further telegraphs full information regarding drawing rights to E.C.A., Washington, and requests it to make "firm allotments of conditional aid" (also with the same value date as before) to those countries granting drawing rights.

No information has been published regarding the turnover of the compensations on total balances, but O.E.E.C. in Paris has regularly published each month a summary of the drawing rights exercised, as shown in the tables.

Intra-European payments and compensations: Utilisation of drawing rights.

1. Drawing rights granted.

Country	Totals established for year	Actually utilised						
		1948			1949			Totals utilised in six months
		Oct.	Nov.	Dec.	Jan.	Feb.	March	
	in thousands of dollars							
Granted by:								
Austria	3,100	177	146	—	—	22	17	362
Belgium	219,500	24,865	23,894	16,716	16,225	30,954	34,814	147,468
Denmark . . .	5,100	3	—	79	657	303	153	1,195
France	9,700	45	1,150	1,499	1,708	—	—	4,402
Germany:								
Bizone . . .	108,800	5,875	895	9,912	17,707	7,661	14,821	56,871
French Zone .	14,800	99	—	51	—	55	20	225
Greece	—	—	—	—	—	—	—	—
Italy	47,300	3,284	3,575	7,460	1,658	4,791	4,582	25,350
Netherlands . .	11,300	798	1,363	—	203	756	1,127	4,247
Norway	16,500	—	—	—	531	1,047	79	1,657
Sweden	34,800	3,787	5,857	7,550	2,039	81	692	20,006
Turkey	28,500	—	—	—	—	3,363	3,467	6,830
United Kingdom.	320,000	28,210	19,908	31,188	27,360	32,807	16,385	155,858
Totals . . .	818,400	67,143	56,788	74,455	68,088	81,840	76,157	424,471

2. Drawing rights received.

Country	Totals established for year	Actually utilised						
		1948			1949			Totals utilised in six months
		Oct.	Nov.	Dec.	Jan.	Feb.	March	
	in thousands of dollars							
Received by:								
Austria	66,600	926	154	2,541	15,462	11,049	8,386	38,518
Belgium	11,000	2,762	2,211	1,334	1,658	285	—	8,250
Denmark . . .	11,900	3,569	2,120	51	—	—	637	6,377
France	333,000	32,013	27,314	41,248	25,196	33,498	31,083	190,352
Germany:								
Bizone . . .	98,600	447	1,002	6,126	2,025	5,390	5,665	20,655
French Zone .	15,600	—	360	—	3,032	439	28	3,859
Greece	66,800	590	5,437	6,722	4,138	2,485	4,134	23,506
Italy	27,000	—	—	—	—	—	—	—
Netherlands . .	83,000	6,661	3,154	6,753	9,454	20,315	15,913	62,250
Norway	48,300	6,660	5,663	9,601	6,258	2,360	2,953	33,495
Sweden	9,800	252	146	79	865	4,617	17	5,976
Turkey	16,800	—	—	—	—	1,402	7,341	8,743
United Kingdom.	30,000	13,263	9,237	—	—	—	—	22,500
Totals . . .	818,400	67,143	56,788	74,455	68,088	81,840	76,157	424,471

3. Net drawing rights granted (—) or received (+).

Country	Totals estab-lished for year	Actually utilised (net)						
		1948			1949			Net totals utilised in six months
		Oct.	Nov.	Dec.	Jan.	Feb.	March	
	in thousands of dollars							
Austria	+ 63,500	+ 749	+ 8	+ 2,541	+ 15,462	+ 11,027	+ 8,369	+ 38,156
Belgium	— 207,500	— 22,103	— 21,683	— 15,382	— 14,567	— 30,669	— 34,814	— 139,218
Denmark . . .	+ 6,800	+ 3,566	+ 2,120	— 28	— 657	— 303	+ 484	+ 5,182
France	+ 323,300	+ 31,968	+ 26,164	+ 39,749	+ 23,488	+ 33,498	+ 31,083	+ 185,950
Germany:								
Bizone . . .	— 10,200	— 5,428	+ 107	— 3,786	— 15,682	— 2,271	— 9,156	— 36,216
French Zone .	+ 800	— 99	+ 360	— 51	+ 3,032	+ 384	+ 8	+ 3,634
Greece	+ 66,800	+ 590	+ 5,437	+ 6,722	+ 4,138	+ 2,485	+ 4,134	+ 23,506
Italy	— 20,300	— 3,284	— 3,575	— 7,460	— 1,658	— 4,791	— 4,562	— 25,350
Netherlands . .	+ 71,700	+ 5,863	+ 1,791	+ 6,753	+ 9,251	+ 19,559	+ 14,786	+ 58,003
Norway	+ 31,800	+ 6,660	+ 5,653	+ 9,601	+ 5,727	+ 1,313	+ 2,874	+ 31,828
Sweden	— 25,000	— 3,535	— 5,711	— 7,471	— 1,174	+ 4,536	— 675	— 14,030
Turkey	— 11,700	—	—	—	—	— 1,961	+ 3,874	+ 1,913
United Kingdom.	— 290,000	— 14,947	— 10,671	— 31,188	— 27,360	— 32,807	— 16,385	— 133,358
Totals . . .	± 564,700	± 49,396	± 41,640	± 65,366	± 61,098	± 72,802	± 65,612	± 348,172

Attention has naturally been concentrated on the actual utilisation of drawing rights as compared with the estimates made a year in advance. The tables show how closely the monthly figures have in fact followed the estimates: out of an aggregate of \$818.4 million established for the year 1948–49, \$424.5 million, i. e. 52 per cent., were utilised in the six months ended March 1949; further, drawing rights utilised for each individual month of the half-year were reasonably close to one-twelfth of the total estimate (which would work out at \$68.2 million).

While the over-all figures thus show an even working of the scheme, there has been great diversity in the extent to which individual drawing rights have been used. The United Kingdom's single drawing right (on Belgium) was utilised up to 75 per cent. in the second month of the operation of the scheme while Italy's drawing rights (on Austria and the United Kingdom), totalling \$27 million, had not been utilised at all during the first six months. These are the extreme cases; the larger drawing rights, particularly those in favour of France, have been more regularly utilised.

The procedure described in the preceding paragraphs has, in fact, worked smoothly and without delay or incident. Regularly, on the fifteenth working-day of each month, the drawing rights due have been credited to the current debtors and the current creditors have received their corresponding "firm allotments of conditional aid" from E.C.A. It has invariably been possible, by direct contact, through telephone calls or otherwise, to overcome any minor difficulties which arose. The Agreement signed in Paris (including the instructions to the Agent) may be said to have stood the test of practical application, in that it provided the technical machinery necessary for the distribution of the indirect aid.

The intra-European payments scheme must be judged for what it is and what it has been able to do and not for what it is not and could not possibly do. In particular, it could neither redress a shaken financial position in any country, nor do much to right such fundamental disequilibria as still existed between O.E.E.C. countries, nor yet charm away the practice of bilateral trading in Europe.

The payments scheme is a practical technical mechanism superimposed on existing trade and payments agreements. As such it is open to objections (some of which are mentioned below). But it helped to maintain and develop intra-European trade at a time when a serious breakdown was threatening; it affords an opportunity for curative measures; and in itself it has represented a certain progress towards multilateral settlements; the basic principle of first-category compensation is the automatic repayment by the participating countries of debts, whenever they occur, by the utilisation of credit balances, wherever they may exist (one essential technical requirement being the completion of the circuit within the group).

As regards the maintenance of trade within Europe, the result of the scheme has been that in the first six months of its operation about half of the intra-European deficits were covered by drawing rights which, being an indirect form of grant, leave no problems of indebtedness behind them.

At the same time as the Agreement on the payments scheme was signed, the Council of O.E.E.C. approved certain "trade rules" to be followed by the participating countries (the text is given as an Annex to this Report, page 231). How far these rules have been observed is difficult to tell, it being easier to prescribe than to ensure observance; but the rules can be invoked in case of need. In addition, it may be said that the payments scheme as such has been instrumental in securing some progress in related fields:

(a) a number of accounts were opened with countries (such as Greece and Turkey) where there had previously been no direct financial contact and trade had hitherto been on a barter or "private compensation" basis;

(b) new credit margins were established in some cases where none had previously existed;

(c) a number of consolidations and rearrangements of old indebtedness were undertaken to relieve difficult debtor positions;

(d) gold and dollar payments due at the end of any month as a result of the overstepping of credit margins were postponed until the value date of the next compensation (if, indeed, such payments were not made unnecessary by the operation of the compensation).

This progress in adjacent fields has not been a negligible factor and is likely to become of greater importance as time goes on. In particular, it is not easy to imagine a fully multilateral system of trade and of payments on current account without some degree of freedom for capital movements, at any rate within the group of O.E.E.C. countries.

O.E.E.C. regarded the payments scheme as one of the first fruits of co-operation but it recognised that the scheme as such could be no more than a palliative, providing a breathing-space during which the underlying causes of disequilibrium in Europe should be remedied. The ultimate objective was the release of European trade from hampering restrictions and the restoration of a multilateral payments system; but, as noted above, "the immediate and vital problem was to make European trade possible at all".(1)

Before the war about one-half of the trade of the participating countries was with one another but by 1947 intra-European trade had fallen to less than two-thirds of its pre-war level. Before the war the total imports of the participating countries from one another had been almost four times as great as their purchases from the United States; but by 1947 imports from the United States had grown so much that they were almost equal to the total of imports between the participating countries. In the first half of 1948, however, intra-European trade began to regain importance, imports between the participating countries being already 50 per cent. above imports from the United States. For a time in 1948, E.C.A. financed part of this intra-European trade by allowing countries to purchase supplies from other participants with E.R.P. dollars. These were the well-known "off-shore" purchases, a temporary device to meet a pressing problem; it was this device which was replaced by the intra-European payments scheme, which invested European currencies with a minimum degree of transferability instead of utilising dollars for the trade inside Europe. But at the same time it was recognised that "more complete convertibility of currencies of the participants must await the correction of excessive disequilibria . . .".(2)

It is hoped, before the period of the Marshall aid is over, to restore European trade to at least its pre-war volume, although the pattern of trade is likely to be different owing to major changes in the structure of western Europe. The circumstance that western Germany, with a greatly increased population, is now forced to import foodstuffs, previously obtained within its pre-war frontiers, introduces a new factor for the future. The loss of invisible dollar income by the United Kingdom is another important new factor affecting a number of countries; for before the war European countries relied largely on their export surplus with the United Kingdom to cover their dollar deficit, this being particularly true of Germany and the Benelux countries. On the other hand, trade with the large sterling area forms an economic basis for the use of sterling as an important medium for international settlements.

It will evidently be necessary for western Europe to obtain an over-all balance in its payments, including a balance in relation to the dollar area; but, as O.E.E.C. emphasises, "the need for balance in dollar accounts must not drive western Europe into unnecessary bilateralism".(3) To secure the

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(1) Interim Report on the European Recovery Program, Volume I, dated 30th December 1948, issued by the Organisation for European Economic Co-operation.

(2) A Report on Recovery Progress and United States Aid, dated February 1949, issued by the Economic Co-operation Administration.

(3) Interim Report on the European Recovery Program, Volume I, dated 30th December 1948, issued by the Organisation for European Economic Co-operation.

requisite balance and the expansion of intra-European trade, increased production, not necessarily on traditional lines, is one of the necessary requirements, and relief may further be obtained through the opening-up of new sources of supply as a result of action in the form of technical aid to, and investments in, underdeveloped areas.

There have been a number of criticisms of the payments scheme: e. g. that it is backed exclusively by American aid; that it is too bilateral in character; that it does little to assist in the building-up of central-bank reserves, etc. There is some truth in these strictures but a number of answers suggest themselves. In addition to progress in related fields (mentioned above) it should be remembered that the Agreement was drawn up in two parts, the first dealing with the European mechanism and the second part alone dealing with drawing rights backed by American aid. It may be assumed that, even if the second part lapses, the first part should remain in force so that a permanent nucleus of a regional nature may continue to exist. Moreover, a considerable volume of useful information and statistics, never before available, are being centralised and studied for their bearing on the present and future.

When E.R.P. aid first came into effect there was hardly any other choice than to build on what existed, i. e. the bilateral payments agreements in Europe. On that basis a scheme was prepared which has shown itself capable of practical application and which has helped to sustain the volume of intra-European trade. The detailed description earlier in this chapter may have given the impression that the scheme is extremely complicated. That is not so; in its principles and application the plan is really quite simple. But it can never equal in effectiveness the traditional multilateral settlements which worked so smoothly in the past. Before they can be resumed, however, it is necessary that fundamental equilibrium should be restored within the various economies in a measure not yet attained and that sufficient monetary reserves should be available to cope with normally recurring fluctuations and to strengthen the feeling of confidence. While the restoration of freedom to European payments is thus dependent upon progress towards a solution of the major problem of European equilibrium, there are, of course, technical improvements which can be introduced into the current scheme with a view to rendering payments more flexible and providing more suitable incentives. Thus the payments scheme which has taken its place as part of the present European effort to achieve a greater degree of collaboration and unity may, through the experience gathered and the practical machinery which is being developed, lay the foundation for a more satisfactory monetary order in the future.

The relevant documents, reproduced as annexes to this Report, comprise: the Agreement for Intra-European Payments and Compensations; the (first) Protocol of provisional application; the decision of the Council of O.E.E.C. on the application of certain principles of commercial policy; the Council decision on Turkey; and the (second) Protocol for the revision of Annex C of the Agreement.

IX. Current Activities of the Bank.

1. Operations of the Banking Department.

The balance sheet of the Bank as at 31st March 1949, examined and certified by the auditors, is reproduced in Annex I to the present Report. The form in which it is drawn up shows some slight differences as compared with last year. The assets and liabilities arising from the execution of the Hague Agreements of 1930 appear under a separate heading on each side of the balance sheet, at the foot of the column. Further, the item "Provision for contingencies and miscellaneous items" has been split up so as to show separately the figure for the "Provision for Contingencies".

At the same time, in view of the unblocking of the Bank's assets in the United States and of the fact that since 1947 the assets and liabilities connected with the execution of the Hague Agreements have been segregated under a special heading, it has been possible to simplify the explanatory notes on the balance sheet. In this connection, the paragraph which has appeared for many years stating that "the Bank holds assets in gold at each of the places where gold deposits are repayable and in short-term and sight funds in the same currencies as the corresponding deposits, in all cases substantially greater than the deposits in question" has been deleted as being superfluous. Needless to say, no change in the policy of the Bank is implied by this amendment and, throughout the year and as at the date of the balance sheet, the statement just quoted remained applicable.

* * *

The balance-sheet total at 31st March 1949 amounts to 722.5 million Swiss gold francs (of 0.2903... gramme of fine gold) against 555.8 million on 31st March 1948. This is 43.6 million Swiss gold francs above the immediate pre-war level (as on 31st August 1939) and is the highest figure recorded in a monthly statement of account since 30th April 1933, i. e. just after the devaluation of the dollar.

As in preceding years, the method of conversion of the currencies included in the balance sheet is based on the U. S. Treasury's official selling price for gold and on the exchange rates quoted for the various currencies against dollars on the date of the closing of the Bank's accounts. With two exceptions, which are of minor importance as regards the balance sheet, the rates are the same as last year.

Parallel with the increase in the resources at the Bank's disposal, there has been a considerable expansion in the business handled by the Bank, the turnover being two and a half times as large as in the preceding year.

The progress which the volume of the Bank's activities began to show in 1947 has continued all through the financial year 1948–49. Both as regards credit facilities extended to central banks and gold operations with central banks, it has been possible for the Bank to increase the scope of its action, this being due in part to the increase in deposits; the Bank has also been able to continue the policy of maintaining a large proportion of its assets in actual gold. Certain problems arise for the Bank from the circumstance that its balance sheet is in terms of gold, while of necessity it must hold, in the leading currencies of the world, the amounts required for its transactions in such currencies. Naturally, the Bank's position has been made easier by the fact that it has received larger deposits in the various currencies; the possibility, in some cases, of combining spot and forward transactions has served a similar purpose.

The Bank is, indeed, endeavouring to play its part as an instrument for co-operation between central banks. And, when these banks deposit a part of their gold and foreign-currency reserves with the Bank for International Settlements and thus provide it with increased resources, they at the same time enable the Bank to render greater services whenever required.

* * *

Earmarked gold, not included in the balance sheet, had amounted to 47.3 million Swiss gold francs on 31st March 1948, when it was held on four different markets. By 31st March 1949, the amount of such gold had risen to its maximum for the financial year, namely 169.5 million Swiss gold francs, and it was then distributed among six markets. So high a figure had not been recorded since 31st July 1939, the increase being partly due to fresh deposits in gold and partly to the conversion of currency deposits into gold held under earmark. It is obvious that, the larger the volume of gold deposited with the Bank, the greater the opportunities the various depositors will have of offsetting or exchanging holdings on the various markets through the instrumentality of the Bank, which will in such cases be able to carry out orders with the minimum of expense.

In the past the Bank used to receive relatively larger deposits in earmarked gold; on 31st March 1939, for instance, deposits of this nature amounted to 236.7 million Swiss gold francs compared with a balance-sheet total of 606.5 million, and, on 31st March 1938, 479.1 million compared with a balance-sheet total of 644 million.

* * *

The general development of the Bank's statement of account during the financial year under review can be outlined as follows.

The first appreciable rise brought the total up from 555.8 million Swiss gold francs on 31st March to 579.3 million on 30th June 1948 and to 605.9 million on 31st July. After falling to 579.4 million on 30th September, the total passed the 600 million mark once more in October and reached 642.3 million on 30th November, 663.9 million on 31st January 1949, 683.8 million on 28th February and 722.5 million on 31st March.

The amount of bills rediscounted with the Bank's endorsement and guarantees given, which at the beginning of the financial year stood at about 7 million, or roughly 1.3 per cent. of the balance-sheet total, rose to its peak on 31st August with 9 million (1.5 per cent. of the total). A new low level was reached with 4.1 million at the end of November, and again at the end of December. The closing figure of 4.4 million, on 31st March 1949, represents only 0.6 per cent. of the balance-sheet total.

A. Assets.

The item gold in bars and coins amounted to 122.4 million Swiss gold francs on 31st March 1948. After falling to 92.7 million on 30th June, the figure rose steadily to 134 million on 30th November, went down to 109 million again on 31st January 1949 and finished the financial year at 150.8 million, which is the highest figure recorded since the establishment of the Bank. But, even so, it does not include the amounts of gold involved in current operations when, for instance, spot sales are made in combination with forward repurchases. By the inclusion of such operations and the deduction of gold sold forward and of the weight-of-gold commitments, as they appear among the liabilities under the heading "Short-term and sight deposits (gold)", the figure for the Bank's net stock of gold is obtained: this stock amounted to 83 million Swiss gold francs on 31st March 1947 and 124.9 million on 31st March 1948, while on 31st March 1949 it reached 166.2 million, this being twice the amount held two years earlier.

As mentioned in the Annual Report for the preceding financial year, the amount of 3,740 kilogrammes of fine gold was to be restituted by the Bank, in virtue of the agreement concluded on 13th May 1948 in Washington, as representing monetary gold received from the Reichsbank and subsequently identified as looted.*

The American, British and French Governments having, either directly or through their representatives on the Tripartite Commission for the Restitution of Monetary Gold, requested the Bank to place the gold in question at their disposal at the Bank of England, London, the said gold was so deposited on 24th June 1948. On 28th July the Bank of England confirmed the fact that the transfer of the 3,740 kilogrammes of fine gold

* As explained on pages 11 and 12 of the eighteenth Annual Report, the gold in question, received during the war, represented payments connected with operations carried out by the Bank for International Settlements as far back as 1930–31 in application of the Hague Agreements, the Bank then acting in virtue of the Trust Agreement through which it was associated with the creditor governments recipients of the Annuities under the Young Plan. At the time, these operations gave rise to a series of investments and during the war the Reichsbank continued to effect transfers in the form of remittances of gold or Swiss francs (against Reichsmarks) corresponding to the interest earned on these investments together with a very limited repayment of capital.

in favour of the three governments had duly taken place. Letters subsequently received from each of the three governments constituted an official recognition of the complete and final execution by the Bank of the obligations it had assumed in virtue of the Washington Agreement.

As also mentioned in the Annual Report for the preceding financial year, the amount of gold fixed in the Agreement of 13th May 1948 included about 374 kilogrammes of fine gold received by the Bank for the account of a third party (a central bank). The central bank in question has effected repayment of this amount to the Bank for International Settlements. The net amount of gold restituted by the Bank for its own account thus comes to *3,366 kilogrammes of fine gold.*

Cash on hand and on current account with banks amounted to 42.6 million Swiss gold francs on 31st March 1948. This figure was not exceeded during the financial year, in the course of which the item underwent considerable fluctuations, falling to 10.4 million on 31st August and recovering to 38.7 million on 31st March 1949.

The Annual Report for the preceding financial year mentioned the progressive transfer of the Bank's liquid reserves to the United States — a movement which was continued during the financial year under review. Cash held in Swiss francs had represented about 80 per cent. of total cash holdings on 31st March 1947 and 7 per cent. on 31st March 1948 but it accounted for less than 3 per cent. on 31st March 1949, when practically the whole of the cash on hand was held in dollars. Gold and cash holdings, taken together with sight funds at interest (which have remained, as a rule, below one million Swiss gold francs), amounted to nearly 190 million Swiss gold francs on 31st March 1949, representing more than a quarter of the balance-sheet total.

In this connection it must be remembered that the Bank has received fresh deposits, and that at the present time difficulties are often experienced in obtaining suitable short-term investments; the Bank has, however, not only to keep certain amounts of cash as counterpart for its sight deposits but also to maintain a working-fund, thanks to which it can be ready at any time to respond to requests made by its central-bank correspondents. Experience has shown that swift and not infrequent changes are liable to occur in the position of these correspondents, and this can from time to time occasion demands for amounts which may be fairly considerable, either in gold or in a currency, of which the correspondents in question are, by turns, buyers and sellers.

The rediscountable portfolio, which amounted to 23.8 million Swiss gold francs on 31st March 1948 and rose to 31.3 million on 31st May, fell to 15.1 million on 31st October and finished the financial year at 17.7 million, when the total was divided almost equally between commercial bills and bank acceptances, on the one hand, and Treasury bills, on the other. Most of the bills and acceptances had been purchased on the New York market, which, it may be added, is extremely narrow. To find short-term paper with a yield that is barely satisfactory is becoming more and more difficult.

During the financial year 1947–48 the total of the Bank's liquid resources had shown a larger increase than the balance-sheet total, and the other items had therefore registered a decline. In the financial year 1948–49 the reverse happened: against a rise of only 19 million Swiss gold francs in liquid resources, the increase in "Time funds and advances" and in "Sundry bills and investments" amounted to some 142 million, as may be seen from the following table.

B.I.S.: Time funds and sundry investments.

Items	31st March 1948	31st March 1949	Difference
	in millions of Swiss gold francs		
Time funds and advances			
1. at less than 9 months . . .	15.9	26.3	+ 10.4
2. at more than 9 months . . .	—	0.4	+ 0.4
Sundry bills and investments			
1. at less than 9 months . . .	50.4	175.9*	+ 125.5
2. at more than 9 months . . .	8.0	13.4	+ 5.4

* Including 174.4 million not exceeding three months.

Time funds and advances varied between a minimum figure of 7.7 million Swiss gold francs recorded on 30th April 1948 and a maximum of 33.4 million recorded on 30th June 1948; sundry bills and investments began the financial year at their lowest level (58.4 million) and ended it at their highest (189.4 million).

Funds invested in Germany in execution of the Hague Agreements of 1930 rose from 291.2 million Swiss gold francs on 31st March 1948 to 297.2 million on 31st March 1949. This increase of 6 million, already announced in the preceding Report, reflects the incorporation in the Bank's claim against the Reichsbank of the part of the gold restituted by the Bank for its own account under the Agreement of 13th May 1948 which had not already been included in the balance sheet as at 31st March 1948.

The Annual Report for the financial year 1946–47 set forth the situation of the Bank as regards the funds which it had invested in 1930–1931 in execution of the Hague Agreements.

All the interest payable in the financial year on the Bank's investments other than those in Germany has been duly received.

B. Liabilities.

The Bank's capital and reserves as well as the long-term deposits received in execution of the Hague Agreements of 1930 show the same amounts at the end of the financial year as at the beginning. The item "Miscellaneous" and the "Provision for Contingencies", which together totalled 106.9 million Swiss gold francs on 31st March 1948, work out at almost exactly the same figure for 31st March 1949. The Provision for Contingencies amounts to 101.4 million Swiss gold francs.

Short-term and sight deposits expressed in a weight of gold remained at about the initial figure of 17.7 million Swiss gold francs up to the end of October 1948 and amounted to 22.4 million on 30th November. After falling to their lowest level — 15.1 million — on 31st December, they quickly recovered, reaching 28.2 million on 28th February, when they were higher than at any time since the end of October 1944. The closing figure for the financial year was 21.7 million.

The flexibility which is possible in the handling of these accounts, since any weight of gold, however small, may be debited or credited to them, makes them particularly useful in connection with various gold operations, such as an exchange of gold — more especially since differences, in terms of a weight of fine gold, can be placed to account in this way. Holders of gold deposit accounts with the Bank numbered twenty-one on 31st March 1949, against twenty a year earlier.

The short-term and sight deposits in various currencies at the beginning and at the end of the financial year are shown in the following table, according to the type of depositor and the character of the deposit.

B.I.S.: Short-term and sight deposits in various currencies.

Items	31st March 1947	31st March 1948	31st March 1949
	in millions of Swiss gold francs		
Central banks for their own account	8.1	48.4	218.9
Central banks for account of others	0.9	8.5	0.7
Other depositors	0.6	0.5	0.6
Total	9.6	57.4	220.2
Deposits at:			
3 to 6 months	—	—	6.2
not more than 3 months	3.6	24.4	142.3
sight	6.0	33.0	71.7
Total	9.6	57.4	220.2

There has been a considerable increase in the deposits with the Bank, the amount held at the end of the financial year under review being the highest since 30th September 1937. The revival of the Bank's activity during the past two years is all the more striking if it is recalled that on 31st March 1947 the corresponding deposits were only 9.6 million Swiss gold francs.

After various fluctuations in the period up to the end of September, when the deposits in question amounted to 83.8 million Swiss gold francs, there was a relatively steady increase until the end of December, and a more marked rise during the last three months of the financial year. The following table shows how the deposits in gold and in various currencies have grown during the past three years.

B.I.S.: Deposits in gold and in various currencies.

End of March	Sight deposits	Short-term deposits	Total
	in millions of Swiss gold francs		
1946	21.4	0.3	21.7
1947	23.8	3.9	27.7
1948	50.5	24.6	75.1
1949	93.1	148.7	241.8

It is interesting to note not only the increase in the total but the fact that this increase owes much to the rise in time deposits, which now represent 60 per cent. of the combined figure. The new distribution adds considerably both to the Bank's liquidity and to its means of action. The resources thus obtained from a fairly considerable number of central banks may, as already mentioned, be used for the benefit of other central banks; a number of the credit operations handled by the Bank have, indeed, been triangular in character, since the deposits (or credits) received by the Bank in currencies have been lent almost immediately to other central banks in need of the currencies in question.

As regards gold operations, the Bank has continued to effect the normal transactions — purchases, sales, exchanges and shipments — which its correspondents have asked it to carry out, there having been a larger volume of such operations than in the previous financial year. The various transactions have been arranged on the basis of the official prices fixed by the central banks concerned. The Bank has, moreover, made a point of applying certain self-imposed rules, by limiting its business of this nature not merely to such transactions as are clearly in conformity with the principles adopted but to transactions initiated by central banks themselves.

Among the factors which have tended to restrict the scope of these operations has been the circumstance that requests of the central banks in the field of gold transactions have been reduced in so far as the receipt of E.R.P. aid in various forms has enabled them to avoid making use of their own reserves. It has also happened that movements of gold in which the Bank has been asked to co-operate have been largely in the same direction, which has limited the possibilities of "offsetting": in such cases the Bank has often been able to furnish the counterpart itself for a certain period; thus, in spite of the various limitations, there have been a number of occasions on which it was possible to meet the requirements of the central banks, and the operations then effected were on a comparatively large scale.

During the financial year under review the Bank was asked to lend its assistance to international organisations of a public and charitable character — an activity which falls within the scope of its functions; in every respect possible the Bank has given such organisations the technical help required, as regards the opening of accounts, transfers and extension of cash facilities.

* * *

2. Intra-European Payments Scheme.

The Agreement for Intra-European Payments and Compensations was signed in Paris on 16th October 1948 by representatives of the Governments of Austria, Belgium, Denmark, France, Greece, Iceland, Ireland, Italy, Luxemburg, the Netherlands, Norway, Portugal, Sweden, Switzerland, Turkey and the United Kingdom, the Commanders-in-Chief of the French, United Kingdom and United States Zones of Occupation of Germany and the Commander of the British/United States Zone of the Free Territory of Trieste. (The texts of the Agreement and of other relevant documents are annexed to this Report [page 231. See also page 200].)

The Council of the Organisation for European Economic Co-operation had already requested the Bank for International Settlements to act as the Agent of the Organisation for the purposes of the Agreement. In accepting the invitation to become Agent of the Organisation the Bank made it a condition that its duties under the Agreement should be of a purely technical nature and without political implications of any kind. As a contribution to European co-operation the Bank offered to render its services without any profit or commission on the transactions it carries through; the Bank only has its out-of-pocket expenses reimbursed by the Organisation (these expenses amounting to less than one-tenth of one per mille on the turnover of the operations carried out).

The compensations, including the utilisation of drawing rights, take place on the basis of the statistics furnished by central banks at the end of every month. Each month the Bank as Agent gives instructions for specific amounts of drawing rights to be made available by the crediting of the central-bank accounts of the debtor country and, at the same time, requests the Economic Co-operation Administration to make firm allotments of conditional dollar aid to the countries giving the drawing rights (as explained more fully on pages 203). Full details of all operations undertaken are contained in the monthly report made by the Bank to the Organisation.

The Bank has been authorised by the contracting parties to give instructions for the debiting and crediting of the payments agreements accounts held at the central banks to the extent necessary to carry through the compensations and to make available the drawing rights under the Agreement. The first operations applied to the month of October 1948 and similar operations have taken place regularly each month in accordance with the Agreement. For the six months up to 31st March 1949 the turnover of all operations under the Agreement exceeded $500 million.

3. Trustee and Agency functions of the Bank.

There has been no change or development, during the year under review, in the Trustee and Agency functions of the Bank described in earlier Reports.

4. Financial Results.

The accounts for the nineteenth financial year ended 31st March 1949 show a surplus, including net exchange gains, of 5,101,855.91 Swiss gold francs, the Swiss gold franc being as defined by Article 5 of the Bank's Statutes, i.e. the equivalent of 0.290 322 58... grammes fine gold. This compares with a surplus of 9,541,433.80 Swiss gold francs for the eighteenth financial year. As was mentioned in the previous Annual Report, wider fluctuations are to be expected in the financial results achieved from year to year than was formerly the case, owing to the fact that the income of the Bank is now derived to a much smaller extent from interest on investments and in a much larger measure from receipts arising from various banking operations. It was pointed out that this position is mainly the consequence of the suspension of the interest receipts on the funds invested by the Bank in Germany in 1930–31 in application of the provisions of the Hague Agreements.

For the purpose of the Balance Sheet as at 31st March 1949, the foreign currency amounts of the assets and liabilities have been converted into Swiss gold francs on the basis of the quoted or official rates of exchange or in accordance with special agreements applicable to the respective currencies and all assets have been valued at or below market quotations, if any, or at or below cost.

With regard to the surplus of 5,101,855.91 Swiss gold francs for the financial year ended 31st March 1949, the Board of Directors has decided that it is necessary to transfer 300,000 Swiss gold francs to the account for exceptional costs of administration and 4,801,855.91 Swiss gold francs to the provision for contingencies. The surplus for the previous financial year ended 31st March 1948 was transferred, as to 500,000 Swiss gold francs, to an account for exceptional costs of administration and, as to 9,041,433.80 Swiss gold francs, to the Special Suspense Account 1944–45. This Special Suspense Account, which thereafter had a balance of 13,547,201.77 Swiss gold francs, has now been amalgamated with other amounts which were set aside in earlier years to meet contingencies, as indicated in the Profit and Loss Accounts for those years. In the Balance Sheet as at 31st March 1949, the consolidated account is included in the new item "Provision for Contingencies", which shows a total of 101,448,567.70 Swiss gold francs.

Taking account of the reduced dividends for the financial years 1942–43 and 1943–44 and the absence of dividends for the financial years 1944–45 to 1948–49, the total of the dividends declared is less than the 6 per cent. cumulative dividends laid down by Article 53 (b) of the Statutes by 208 Swiss gold francs per share.

The accounts of the Bank and its nineteenth annual Balance Sheet have been duly audited by Messrs Price Waterhouse & Co., Zurich. The Balance Sheet, together with the certificate of the auditors, will be found in Annex I and the Profit and Loss Account is reproduced in Annex II.

5. Bank building.

During the financial year under review, the Bank was able to purchase on satisfactory terms the whole of the share capital of the company (Grand Hotel and Savoy Hotel Univers Ltd) which is the proprietor of the main building occupied by the Bank since 1930. In the Balance Sheet of the Bank as at 31st March 1949, the shares in question are included amongst the "Miscellaneous Assets".

6. Changes in the Board of Directors and in Executive Officers.

Since the publication of the last Annual Report, the following changes have taken place in the composition of the Board of Directors. Upon his appointment on 7th August 1948 as Governor of the Banca d'Italia, Dr Donato Menichella became an ex-officio Director of the Bank. Dr Menichella appointed Prof. Pietro Stoppani as a Director under Article 28 (2) of the Statutes, and Dr Paride Formentini as his Alternate.

In January 1949, the term of office of Monsieur Emmanuel Monick as an ex-officio Director came to an end upon his retirement as Governor of the Bank of France. Monsieur Monick had served as an ex-officio Director since October 1944 and his cordial interest in the problems and the work of the Bank has been of the greatest value. Monsieur Wilfrid Baumgartner, who succeeded Monsieur Monick as Governor of the Bank of France, and thus became an ex-officio Director, appointed as his Alternate, under Article 28 (1) of the Statutes, Monsieur Jean Bolgert, who had already acted in that capacity for his predecessor on the Board.

Mr Cameron F. Cobbold joined the Board as an ex-officio Director on 1st March 1949, upon his appointment as Governor of the Bank of England in succession to Lord Catto, who had always given his valuable support to our institution. Mr Cobbold has long been associated with the Board and its work; he has appointed Mr G. L. F. Bolton, and, in the latter's absence, Mr J. S. Lithiby, to serve as his Alternate.

The term of office of Mr Ivar Rooth under Article 28 (3) of the statutes expired on 31st March last. Mr Rooth had first served as a Director in the early years of the Bank and had been again elected in 1937, since when his term of office had been regularly renewed. The valuable collaboration of Mr Rooth, both in normal times and during the years of war, has been deeply appreciated. In April 1949, Mr Klas Böök, who had succeeded Mr Rooth as Governor of the Sveriges Riksbank in December 1948, was elected a member of the Board under Article 28 (3) for a period of two years. Dr M. W. Holtrop, President of the Nederlandsche Bank, was re-elected under the same Article to be a Director for a period of three years, ending 31st March 1952.

* * *

In March, the Bank learned with deep regret of the death of Herr Ernst Hülse who, at the time of the foundation of the Bank, had been appointed as the first Assistant General Manager. Herr Hülse had rendered valuable services in that capacity for over five years. Thereafter, he had acted as an Alternate until January 1939.

* * *

At its meeting held on 14th June 1948, the Board decided to elect, under Article 39 of the Statutes, the Chairman of the Board, M. Maurice Frère, to be President of the Bank, the term of office in this latter capacity to coincide with that of Chairman of the Board. At the same time, it was decided to appoint M. Roger Auboin, General Manager of the Bank, to be Alternate of the President, his term of office as Alternate to correspond to that of M. Frère as President.

In June last, M. Marcel van Zeeland, Head of the Banking Department, was nominated as First Manager of the Bank.

Mr Fabian A. Colenutt, previously Head of the Administrative Section, was appointed Deputy Secretary.

Conclusion.

1948 has undoubtedly been a year of general economic and monetary progress, especially in western Europe. The volume of production, both industrial and agricultural, has reached or exceeded pre-war levels and the fight against inflationary tendencies has been successfully waged in almost every country in Europe. Essential as these improvements have been for raising standards of living and laying the foundation for further advances, such is the nature of economic life that the new stage, reached with so much effort, immediately brings forth its own set of problems and preoccupations, and it may seem as if the new difficulties are in many respects even greater than those which have just been overcome. For in the years directly following the war the action which had to be taken comprised a number of obvious steps to arrest the inflationary trend and push on in almost any line of production, while now the task is to adjust an increasing volume of output more exactly to demand under conditions of growing competition and, in general, to establish a balanced position which is at the same time durable and self-sustaining.

The disappearance of the sellers' market has, indeed, given rise to some very real difficulties; since it is no longer possible to find almost everywhere a ready buyer for practically any commodity, much more attention must now be devoted to questions of price and quality. There is hardly a producer or trader who has not begun to be concerned about "markets", in which he must be able to sell at a competitive price. It is still too early to tell whether the change in the complexion of the markets points to a downward turn in the general business trend, since the volume of trade and production has mostly kept up fairly well and there are many sustaining factors operating in the markets. But here again the authorities and the public are concerned about different problems from those which worried them a year ago.

These are clearly fresh developments, but it is not as if there were no experience, derived from somewhat similar situations in the past, to serve as a guide. It is encouraging to observe that in the last few years a much better insight has been gained into one very important relationship: the close connection between the volume and methods of internal financing (of any remaining budget deficit or outlay for investments) and the outcome of the balance of payments, requiring financing from foreign resources. Important questions arise in this connection in regard to the use of the counterpart in national currencies of Marshall aid (questions to which some attention has been given in this Report).

It is also fortunate that, through the progress recently made, the differences found from country to country as regards the balancing of budgets, the arresting of inflation, the available supplies, etc. have been much reduced and the approach to internal balance has clearly brought the countries to a point where the international aspects of the different problems involved can receive more attention and individual measures can be considered more carefully in relation to the requirements for general long-term progress.

Unfailing attention to international conditions is, indeed, indispensable when the countries get to grips with the problem of adjusting their production to the new state of the markets. Throughout the world the key-note today is more production through greater efficiency — and rightly so.

But it is not only a question of volume or even of costs; it is evidently necessary to produce precisely what is in demand. Almost all the manufactured products which Europe itself has for export have to be sold to individual customers all over the world — and there is no doubt that adaptation to a largely new situation of world competition constitutes a very real test for the viability of Europe. If the price system is not allowed to play its part as an indicator of what is in demand and should be produced, how can the variegated economies of the European countries possibly find the right lines of output? There is clearly no other way of knowing to what extent an effective demand exists for Europe's output of largely non-essential goods than to feel the pulse of demand in the markets of the world today; but the indication which those markets supply will not be of real value unless sufficient freedom prevails in them — and, even then, it will be of little avail without sufficient flexibility inside the exporting countries. Moreover, the free movement of goods with the development of multilateral trade, which has been the condition of Europe's prosperity in the past, depends not on European action alone: it requires the adoption of appropriate commercial and monetary policies in countries and areas outside Europe itself.

There must always be a struggle against rigidity — especially in the modern world, where certain technical developments seem to render the economy less flexible; surely, then, it is not too much to ask that the authorities, in framing their policies, should not add unnecessarily to already existing rigidities. An increased volume of production is not automatically followed by larger exports and a better balance on foreign account, since more production gives rise to higher incomes and consequently to increased consumption, including demands for better housing, which is an indirect demand for more investments. A better balance will only be attained if more is saved or more accrues to the state in taxes over and above what is necessary to meet added spending; it is only pro tanto that investment expenditure at home will be more adequately covered by the flow of domestic resources. Production alone, therefore, does not suffice: to be really beneficial, it must be combined with a suitable economic and financial policy. If, then, a country is in disequilibrium because its budget expenditure is too high or its investments are too ample or costs are maintained at an uneconomic level or the exchange rates have got out of line with realities (or there is a combination of two or more of these factors) with the result that an untoward deficit has arisen in the balance of payments:

if, in such a state of affairs, the country concerned obstinately refuses to make any alteration either in its budget or credit policy or in its control of prices or exchanges, there is no reason to assume that the lack of equilibrium will not continue — and this will mean that the monetary reserves of such a country will be eaten into and the proceeds of foreign loans and grants wasted simply to perpetuate the rigidities which were at the bottom of its difficulties. The receipt of foreign resources is of such great value to a country that they should not be wastefully put to uses which will simply postpone necessary adjustments.

The lines of policy adopted in this year 1949 may well prove to be of vital importance. The disappearance of the sellers' market, together with the price reductions that have befallen some producers and traders, has led to almost instant demands for remedial measures of one kind or another — but with little, if any, consideration for the needs of adjustment in the economy as a whole or the urgent need of earning more foreign exchange in order to get rid of balance-of-payments deficits before the internal restrictions are taken off.

It would indeed be a matter for regret if the countries in Europe which have taken steps to balance their budgets and restrict the granting of credits were to abandon this policy of restraint prematurely. Such a policy has, of course, not been imposed for its own sake, but because the arrest of internal inflation is usually the only means of bringing about an expansion on the foreign account, with a reconstitution of monetary reserves and a suppression of arbitrary restrictions with regard to currency payments and the exchange régime generally. An imprudent relaxation of the credit restrictions before decisive results have been obtained in the field of foreign exchanges might jeopardise the achievements so far realised.

The position is in these respects different in the United States. That country, with its high rate of domestic savings and its ample gold reserves, is in a position to adopt immediately, and without incurring any real risk, a liberalising policy designed to lessen the deflationary weight which is beginning to make itself felt in its economy. By doing that the United States may, indeed, contribute to greater steadiness in the trend of business for the whole world. But European countries, with only a weak flow of genuine savings and scanty monetary reserves, are in a different position: only when they can permit ordinary trade and other current operations in their balance of payments to be settled without hampering restrictions will they be able to reap the full rewards of freer commercial intercourse. It is a point to remember that certain measures of direct control (and not least trade and exchange control) tend to intensify the trend towards nationalistic insulation, while the indirect, essentially financial, types of control help to strengthen the ties of free international intercourse. In no case must the co-operation between European countries take the form of a joint imposition of further restrictions, for then the danger of establishing enclosed areas with an autarkic tendency would be a very real one.

It would be a mistake, however, to underrate the difficulties in the way of an advance towards a more normal system of foreign payments, with greater competition from abroad. Control, with its curtailment of imports, seems to many a necessary means of "saving" foreign exchange — but then it is forgotten that expenditure inhibited in one direction mostly leads to increased expenditure in another, to the detriment of exports. Vested interests have also grown up which are in no way anxious to see a dismantling of restrictions. But, despite all obstacles and hesitations, it will be necessary to arrive at a situation in which restrictions are no longer the rule and freedom the exception and one in which ordinary trade in merchandise, the movements of tourists and the regular exchange of services can take their course without interference dictated by monetary considerations. Creditor countries naturally incur little or no risk in admitting imports more freely but debtor countries must also be aware that the practice of keeping out non-essential goods, if applied all round, would soon prevent them, too, from ameliorating their trading position. It is, indeed, becoming increasingly clear which will be the countries with the best chance of standing up to international competition: it will be the first countries to revert to a system of greater freedom by adopting a policy in which each set of measures in the fields of credit, prices, costs and foreign exchanges contributes in a harmonious way to the establishment of a balanced position. When contradictory policies are pursued, as has happened only too often in recent years, it becomes almost impossible to re-establish the credit position without which no genuine contribution from savings will be forthcoming as a durable basis for investments. In these matters, the general public, even though it may be uninformed about many technical details has, after all that has happened, acquired a knack of judging whether the steps taken are likely or not to achieve the desired results.

More is needed of true planning, which consists less in fixing "targets" than in determining precisely what measures should be taken in different fields over (say) the next six or twelve months in order to correct unbalanced positions and achieve further progress. An essential task will be to bring back into operation those parts of the mechanism of adjustment which the modern economy has at its disposal for the purpose of keeping a balance between supply and demand on the markets, between payments and receipts in the balance of payments, etc., and it is then especially necessary to ensure that no artificial creation of monetary purchasing power, beyond what is really earned by contributions to production, upsets the balance at home and in relation to other economies. It is neither more nor less planning that is needed but planning of the proper kind. All too often uncoordinated — and, what is worse, contradictory — measures are adopted by separate branches of the administration having little or no contact with one another. This is then mistakenly given the name of "planning", whereas real planning must, first of all, aim at a proper harmony in the lines of official action and, secondly, relate these measures to the manifold free activities of the people as producers, traders, income-earners and consumers, so that their various efforts are fitted into the general picture under conditions conducive to all-round balance. And this kind of planning must, further, be undertaken with an eye to what is happening in other countries and what opportunities are offered for coordinated action on an international scale. It may well be that no measures would be more likely to combat any deflationary tendencies appearing in the various economies than a speedy abolition of quantitative and other trade restrictions, for that might give just the right expansionist impetus now needed. It is dawning upon the peoples that there is no solution in separation; that those who protect their markets from foreign influences are liable to be less capable of sustaining competition and improving their standards of living, and that, indeed, a truer harmony and added strength are to be found in developing appropriate forms of international co-operation.

Respectfully submitted,

ROGER AUBOIN

General Manager.

AGREEMENT

for INTRA-EUROPEAN PAYMENTS and COMPENSATIONS

AGREEMENT

for INTRA-EUROPEAN PAYMENTS and COMPENSATIONS

Paris, 16th October, 1948.

The Governments of Austria, Belgium, Denmark, France, Greece, Ireland, Iceland, Italy, Luxemburg, Norway, the Netherlands, Portugal, the United Kingdom, Sweden, Switzerland and Turkey, the Commanders-in-Chief of the French, United Kingdom and United States Zones of Occupation of Germany, and the Commander of the British/United States Zone of the Free Territory of Trieste:

DESIRING to move forward towards the liberalisation of Intra-European Payments envisaged in Article 4 of the Convention for European Economic Co-operation signed in Paris on 16th April, 1948;

DESIRING to adopt immediately a plan for limited compensation to be applied until it shall be possible to take further steps towards the establishment of a full multilateral system of payments among themselves;

HAVING REGARD to the adoption on 16th October, 1948, by the Council of the Organisation for European Economic Co-operation (hereinafter referred to as the Council) of a Decision approving the text of the present Agreement; and to the adoption on 16th October, 1948, of a Decision recommending a distribution of American Aid;

CONSIDERING the Decision on commercial policy taken by the Council on 16th October, 1948;

HAVE agreed as follows:

PART I

Article 1 — (a) Subject to the provisions of the present Agreement, the Contracting Parties shall carry out currency compensations. Such compensations shall be first and second-category compensations as defined in Article 18. Compensations shall be used to facilitate all transactions which the Contracting Parties may at any time allow in accordance with their respective transfer policies and with the terms of their payments agreements.

(b) Subject to the provisions of Article 5, the balances available for compensations shall be the balances of accounts kept by one central bank in the name of other central banks. For the purposes of the present Agreement, central banks shall be the central banks or other monetary authorities designated by the Contracting Parties.

Article 2 — The Bank for International Settlements (hereinafter referred to as the Agent), acting in accordance with the agreement between the Bank for International Settlements and the Organisation for European Economic Co-operation (hereinafter referred to as the Organisation) made in pursuance of the Decision of the Council taken on 10th September, 1948, shall be the agent for compensation for the purposes of the present Agreement.

Article 3 — (a) Compensations under the present Agreement shall take place monthly and in accordance with directives given by the Organisation to the Agent.

(b) The Agent shall submit monthly reports to the Organisation on the compensations completed during the month.

Article 4 — (a) First-category compensations shall be applied without the previous consent of the Contracting Parties.

(b) Second-category compensations shall require the previous consent of the Contracting Parties directly concerned in each second-category compensation.

(c) The Contracting Parties, while not binding themselves to accept second-category compensations, intend to co-operate fully in facilitating any reasonable propositions put forward to them by the Agent, having regard to all the circumstances concerning such compensations.

(d) In arranging second-category compensations the Agent shall endeavour to facilitate those compensations which will ease the most difficult debtor/creditor relationships, bearing particularly in mind the desirability of avoiding so far as possible settlements between Contracting Parties in gold or foreign currencies and interruptions in trade or payments.

(e) Nothing in this Article shall prevent any Contracting Party from informing the Agent that it is prepared to accept, without its previous consent, all or any class of second-category compensations which may be arranged by the Agent.

Article 5 — (a) When calculating the balances available for the compensations in respect of any month, the Agent, at the request of a Contracting Party, may exclude certain types of balances owned by that Contracting Party. The types of balances which may be excluded and the procedure for requesting their exclusion are set out in Annex A, which shall form an integral part of the present Agreement.

(b) No balance excluded under paragraph (a) of this Article from the compensations in respect of any month shall be included, by the Contracting Party requesting the exclusion, in the calculation for the purpose of any settlement in gold or foreign currency which would be due to that Contracting Party under a payments agreement made before the signature of the present Agreement and which might follow immediately after the compensations in respect of that month.

Article 6 — Each Contracting Party undertakes not to cause abnormal balances in the currencies of other Contracting Parties to be held by banks other than central banks or otherwise to place such balances so that they will not be available for the purpose of compensations.

Article 7 — (a) Whenever a gold or foreign currency settlement falls due in the course of any month, under a payments agreement between any two Contracting Parties made before the signature of the present Agreement, the settlement shall be postponed until after the compensations in respect of that month.

(b) Any settlement in gold or foreign currency which shall remain due after the compensations in respect of that month shall then be effected immediately. Any such settlement shall be reported by the debtor to the Agent and the Organisation.

(c) Nothing in the provisions of this Article shall preclude a Contracting Party which is a creditor from making different provisions by agreement with another Contracting Party, if, owing to the operation of this Article, a credit margin granted by the former to the latter is being continuously exceeded.

Article 8 — (a) Each Contracting Party shall communicate to the Agent:

(i) All information necessary to enable the Agent to have a clear understanding of the nature and operation of its payments agreements with other Contracting Parties;

(ii) A monthly statement of the balances on the appropriate account or accounts available for compensations, and of the balances which the Contracting Party desires to exclude in accordance with Article 5;

(iii) A monthly report giving a single rate of exchange agreed with each other Contracting Party at which the Contracting Party reporting is prepared for compensations to take place;

(iv) A monthly statement of settlements in gold or foreign currency made by the Contracting Party to other Contracting Parties during the month;

(v) Such information as will enable the Agent to ascertain the amounts of currencies which may be used in accordance with Part II of the present Agreement; and

(vi) Such further information as the Contracting Party considers may assist the Agent in his task.

(b) In the case of Contracting Parties without a unified cross-rate structure, the balances and rates of exchange reported under sub-paragraphs (ii) and (iii) of paragraph (a) of this Article, shall be determined in accordance with the provisions of Annex B, which shall form an integral part of the present Agreement.

PART II

Article 9 — (a) Each Contracting Party which has for the purpose of the present Agreement been estimated to be in credit with any other Contracting Party on current balance of payments for the year ending 30th June, 1949, after taking into account the agreed existing resources of that other Contracting Party, shall establish drawing rights in favour of the latter Contracting Party.

(b) The amounts of drawing rights established by each creditor in favour of each debtor, equivalent to the United States dollar value of goods and services to be provided by the United States Economic Co-operation Administration for the purposes of the present Agreement (hereinafter referred to as conditional aid) to each creditor, are shown in Annex C, which shall form an integral part of the present Agreement.

(c) No debtor shall be obliged to repay to a creditor any amount in respect of drawing rights established by the creditor in its favour, if that creditor has received from the United States Economic Co-operation Administration an equivalent amount of conditional aid to which no obligation to repay is attached.

(d) For the purposes of this Part of the present Agreement "creditor" and "debtor" mean, with respect to any two Contracting Parties, those which are shown as creditor and debtor in relation to one another in Table III of Annex C.

Article 10 — Drawing rights shall be made available and used only in accordance with the provisions of the present Agreement. The amount to be made available and used shall be calculated in accordance with the provisions of Annex B.

Article 11 — (a) Subject to the provisions of paragraph (b) of this Article, drawing rights shall be made available in the currency of the Contracting Party making them available, or, if another currency is normally used for payments between that Contracting Party and another Contracting Party, in that other currency. Each Contracting Party shall, not later than 31st October, 1948, report to the Agent the currencies in which it will make drawing rights available in accordance with this paragraph.

(b) Any two Contracting Parties may agree, not later than 31st October, 1948, that the drawing rights established by one in favour of the other shall be made available in a currency different from the currency in which they would otherwise be made available under paragraph (a) of this Article. A report on any such agreement shall be given by the two Contracting Parties to the Agent not later than 31st October, 1948.

(c) An agreement between two Contracting Parties under paragraph (b) of this Article shall not prevent them from subsequently making an agreement that the drawing rights established by one in favour of the other shall be made available either in the currency of one of them or in a currency which, at the time of the subsequent agreement, is normally used for payments between them. Immediately after any such subsequent agreement, the two Contracting Parties shall make a report thereon to the Agent.

Article 12 — Amounts of currency in respect of drawing rights shall be made available to the Agent immediately upon request by him, provided that a Contracting Party shall not be required to make amounts of currency available to the Agent earlier than the time at which equivalent amounts of conditional aid are firmly allotted to it.

Article 13 — Requests under Article 12 in respect of the drawing rights established in favour of any Contracting Party in any currency shall not be made before the agreed existing resources of that Contracting Party in that currency, as set out in Annex C, have been exhausted.

Article 14 — The Agent shall use amounts of currencies made available under this Part of the present Agreement in compensations under the present Agreement in accordance with the following provisions:

(a) (i) The Agent shall be entitled to use in any month an amount of any one currency up to the total of each deficit on the month between each debtor and each creditor to the extent to which the remaining amount of agreed existing resources of that debtor in that currency is not sufficient to cover that deficit.

(ii) If in any month an amount of such currency is not made available as a result of the operation of Article 12, the whole or part of that amount, when it becomes available, may be used by the Agent in any succeeding month in addition to the amount which he may use under sub-paragraph (i) of this paragraph.

(b) The Agent may, at the request of a debtor, use all or any part of amounts of a particular currency, additional to those which might be used under paragraph (a) of this Article, as the debtor may intimate to him, provided that:

(i) any Contracting Party, whose monthly deficit against the Contracting Party by which the drawing right has been established in favour of the debtor is to be reduced by the use of the amount, has no balance standing to his credit with the Contracting Party which has established the drawing right, or

(ii) the consent of the Contracting Party by which the drawing right has been established has first been obtained.

(c) If in any month the aggregate amount of any one currency which the Agent is entitled to use under sub-paragraph (a) of this Article exceeds the amount of such currency available under this Part of the present Agreement, the Agent shall, in principle, use such currency as between the Contracting Parties in deficit on the month in that currency in proportion to such deficits, but may make moderate adjustments in this proportionate distribution having regard to the desirability of creating a minimum of interruption in trade and payments and of assisting in the avoidance of gold and foreign currency settlements.

Article 15 — Not more than 75% of the amount of drawing rights established by a Contracting Party in favour of another Contracting Party as shown in Annex C shall be made available and used in compensations in respect of the nine months ending 31st March, 1949. In particular cases this percentage may be increased by decision of the Organisation.

Article 16 — (a) If a Contracting Party, either under a payments agreement or because it has no available credit balance in the currency of another Contracting Party, has made a payment in gold or foreign currency falling due on or after 1st October, 1948, to that other Contracting Party because at the time of payment drawing rights established in its favour by that other Contracting Party could not be used by the Agent as a result of the operation of the provisions of Articles 12 and 15, the Agent, at the request of the Contracting Party which has made the payment, shall take the necessary steps to enable such drawing rights to be used to repurchase the whole or part of any amounts of gold or foreign currency so paid provided that the use of the drawing rights is no longer prevented as a result of the operation of the provisions of Articles 12 and 15.

(b) The request and arrangements under paragraph (a) of this Article shall be made and put into effect during the course of the compensations in respect of the month when the provisions of Articles 12 and 15, as the case may be, cease to prevent the use of the drawing rights.

(c) The amount which the Agent may use under this Article in respect of any month shall be in addition to the amounts which the Agent may use in respect of that month under Article 14.

Article 17 — (a) It is contemplated that drawing rights will normally be used as established under Article 9 of the present Agreement. The procedure for revisions provided for in paragraphs (b), (c) and (d) of this Article shall be administered with this in mind.

(b) Revision of the amounts and distribution of drawing rights shall take place, at the request of a Contracting Party, only in circumstances resulting from:

(i) force majeure or catastrophe;

(ii) a situation in which a debtor maintains and satisfies the Council that it has been unable to use the whole or any part of its drawing rights although it has made all reasonable efforts to do so; or

(iii) a situation in which a creditor maintains and satisfies the Council that the whole or any part of drawing rights established by it are no longer required by a debtor for the purposes for which they were established.

(c) The Council shall establish appropriate bodies to deal with cases arising under this Article.

(d) The Council shall decide what recommendations for revision of the amounts of and for the redistribution of drawing rights should be made to the United States Economic Co-operation Administration.

PART III

Article 18 — (a) "First-category compensation" means an operation which produces for any Contracting Party all or any of the following results:

(i) a decrease in one or more debit balances against an equivalent decrease in one or more credit balances, or

(ii) the offsetting, by the use of amounts in respect of drawing rights established in its favour, of the whole or part of its deficit for the month with the Contracting Party by which the drawing rights have been established, or, in the case of amounts which may be used under Article 14 (a) (ii), the offsetting of the whole or part of a deficit with that Contracting Party remaining uncovered from a previous month or months,

provided that amounts in respect of drawing rights shall, to the extent to which they are not used to offset deficits under sub-paragraph (ii) of this paragraph, be treated for the purposes of sub-paragraph (i) as if they were credit balances.

(b) "Second-category compensation" means any operation, other than one included under paragraph (a) of this Article, which results in the increase of a balance or the formation of a new balance in comparison with the position before the operation.

Article 19 — If a Contracting Party in placing information at the disposal of the Agent for the purposes of the present Agreement intimates that it desires the information to be treated as confidential, because the information has not been published by it, the Agent shall have due regard to the intimation in making use of the information.

Article 20 — (a) Any compensation which requires the use of the balance of any account kept by or in the name of the central bank of Portugal or Switzerland shall be subject to the previous consent of Portugal or Switzerland and the respective creditor or debtor.

(b) Subject to approval by the Council, the Government of Portugal or the Government of Switzerland may, at any time, decide to accept without their previous consent all first-category compensations. Upon such approval, the provisions of paragraph (a) of this Article shall cease to apply to Portugal or to Switzerland, as the case may be, and to their respective creditors and debtors.

(c) Part II of the present Agreement shall not apply to Portugal or to Switzerland.

Article 21 — If a special Agreement is made between any Contracting Party and the United States Economic Co-operation Administration with respect to the loan of United States dollars to any such Contracting Party for the purposes of the present Agreement, Part II of the present Agreement shall operate in relation to that Contracting Party upon such conditions regarding its application for the purposes of the present Agreement as may be proposed by that Contracting Party in agreement with the United States Economic Co-operation Administration and approved by the Council. The conditions will, upon approval by the Council, be communicated by the Secretary-General to the Agent.

Article 22 — (a) The supervision of the operation of the present Agreement shall be undertaken by the Organisation.

(b) Should any question arise concerning the interpretation or the application of the present Agreement, it may be referred by any Contracting Party to the Council, which may take decisions on the question.

Article 23 — (a) The present Agreement shall be ratified.

(b) The instruments of ratification shall be deposited with the Secretary-General of the Organisation, who will notify each deposit to all the signatories.

(c) The present Agreement shall come into force upon the deposit of instruments of ratification by all the signatories.

Article 24 — (a) Drawing rights not used before the termination of the present Agreement shall not be cancelled. They will remain at the disposal of the Contracting Parties in whose favour they have been established under no less favourable terms than those originally enjoyed.

(b) The precise method by which such unused drawing rights shall be disposed of in the period subsequent to the termination of the Agreement shall be the subject of discussion by the Organisation at the appropriate time.

Article 25 — (a) With the exception of Article 24, the present Agreement shall remain in force until the completion of the compensations in respect of the month of June, 1949, and the present Agreement may be continued in force thereafter on such terms as the Contracting Parties may agree. Article 24 shall remain in force until the unused drawing rights have been finally disposed of.

(b) Not later than 1st May, 1949, the Contracting Parties, acting through the Organisation, shall consider how the present Agreement has worked and whether it shall be continued.

(c) If it becomes apparent that the present Agreement is not likely to be continued in force, the Contracting Parties shall, at the request of any Contracting Party, entrust a Committee or Committees with the preparation of recommendations as to the provisions which may be required to avoid

(i) interruptions in trade or payments,

(ii) payments of gold or foreign currency,

(iii) the prevention of repurchase of gold or foreign currency which would otherwise have been possible under the provisions of the present Agreement, or

(iv) other similar possible consequences,

which may arise, within a reasonable time from the termination of the present Agreement, as a result of changes in balances caused by compensations made under the present Agreement.

Article 26 — The present Agreement terminates the First Agreement for Multilateral Monetary Compensation signed in Paris on 18th November, 1947, as from the completion of the compensations in respect of the month of September, 1948.

Paris, 16th October, 1948.

ANNEX A

Excluded Balances

I. The following balances may be excluded from compensations under Article 5 of the present Agreement:

(a) Working balances, which will normally fall under one or more of the following heads:

(i) normal central banking balances (fonds de roulement), that is to say, sufficient funds to cover outstanding payment orders and to maintain normal banking relationships,

(ii) balances held as cover for oversold forward exchange positions, or

(iii) balances held as cover for banking credits due to mature within a short period.

(b) Balances representing the proceeds of capital transactions expressly undertaken for the financing of specific capital expenditure.

(c) Balances not arising under a payments agreement or from current trade transactions and which are freely convertible into gold or United States dollars.

(d) Other balances which, owing to special provisions in payments agreements in force at the date of signature of the present Agreement, represent the proceeds of certain exports earmarked for debt services or other contractual obligations.

(e) In the case of Greece and Turkey, in view of the essentially agricultural structure of their economies, a reasonable proportion of their balances in the currencies of other Contracting Parties with which they have no payments agreements providing for credit margins in their favour, it being understood that these balances would be used, during the year following the date of their first exclusion, to pay for imports from the countries in which the balances are held.

II. (a) Each Contracting Party requesting the exclusion, under any of the foregoing provisions of this Annex, of a balance owned by it shall state to the Agent the provisions of this Annex under which each reservation is requested and give information as to the facts in reasonable detail.

(b) If the Agent is unable to satisfy himself with regard to the requested exclusion from the information given him, he may seek further information.

(c) If he remains unsatisfied, he shall make a report on the matter to the Organisation and shall furnish a copy of such report to the Contracting Party making the request.

ANNEX B

I. The following procedure shall be used in determining the balances and rates of exchange for the purpose of reports under Article 8 by Contracting Parties without a unified cross-rate structure:

(a) Debit and credit balances in the currency of any Contracting Party without a unified cross-rate structure in relation to Contracting Parties having a unified cross-rate structure shall be reported to the Agent in the currency of the latter Contracting Parties, after having been calculated at a rate of exchange to be fixed by agreement between the two Contracting Parties concerned. The rate of exchange so agreed should be that effectively in use for current operations between them. If there are variable rates, or more than one rate, the rate agreed should be based on the weighted average of those rates.

(b) The debit and credit balances between each pair of Contracting Parties not having a unified cross-rate structure, unless expressed in the currency of a Contracting Party having a unified cross-rate structure, shall be reported to the Agent in the money of account used for compensations by him, after having been calculated at a rate of exchange agreed between the two Contracting Parties.

(c) The Contracting Party shall also report to the Agent the method of calculation of the reported balances including the data necessary to show how the rates of exchange have been determined for the purpose of their calculation.

II. The following procedure shall be used for the purpose of calculating monthly deficits and of determining the amounts in respect of drawing rights to be made available and used in each month:

(a) The Agent shall establish the net balances existing between Contracting Parties and shall convert such net balances into the money of account on the basis of the rates already reported to him. The Agent will then be able to ascertain, in the money of account, the monthly deficits and surpluses and the amounts of drawing rights to be made available and used in each month.

(b) In the event of the rate of exchange of the currency of any Contracting Party changing, the Contracting Parties concerned shall advise the Agent of the balances held between them as at the close of business on the day preceding the change and give details of any adjusting payments which may have been made in accordance with the terms of exchange guarantees. The Contracting Parties concerned shall also forward to the Agent a report in accordance with the terms of Article 8 (a) (iii) of the Agreement giving the new agreed rate of exchange.

This information will enable the Agent to make allowance for the change in the rate of exchange when calculating the monthly deficits and surpluses and also the amount of drawing rights to be made available.

III. In order to give effect to the compensations in respect of any month, including the use of amounts in respect of drawing rights, the figures notified by the Agent to the Contracting Parties in the currency of Contracting Parties having a unified cross-rate structure or in the money of account shall be converted by the Contracting Parties, if necessary, in the currencies of Contracting Parties without a unified cross-rate structure on the basis of the rates agreed in accordance with paragraph I of this Annex.

ANNEX C

TABLE I

Agreed Existing Resources

The following table sets out the amounts of the agreed existing resources referred to in Article 13 of the present Agreement.

Contracting Parties	Amount of the agreed existing resources	Contracting Parties in whose currency the agreed existing resources are held	Dollar equivalent of the amounts of agreed existing resources, calculated prior to the signature of the present Agreement
	(Figures in millions)		(Figures in millions)
Greece	3.23 £ sterling	United Kingdom	13
Italy	11.16 £ sterling	United Kingdom	45
Bizone	35.22 Swedish crowns	Sweden	9.8
Total	14.39 £ sterling 35.22 Swedish crowns	Total	67.8

TABLE II

Drawing Rights

(a) Column 2 of the table sets out the total amount of drawing rights established under Article 9 of the present Agreement by each Contracting Party which has been estimated to be in credit with any other Contracting Party on current balance of payments for the year ending 30th June, 1949, after taking into account the agreed existing resources of that other Contracting Party.

(b) Column 3 sets out the corresponding total amount of drawing rights established in favour of each Contracting Party.

(c) The amounts specified in this table and in table III are subject to adjustment as follows:

(i) From the amount of the respective drawing rights established by any Contracting Party there shall be deducted the amount of the advance allotments authorised in respect of the third quarter of 1948 by the United States Economic Co-operation Administration under the Economic Co-operation Act of 1948 for the payment for commodities sold by that Contracting Party to any other Contracting Party;

(ii) From the amount of the respective drawing rights established in favour of any Contracting Party there shall be deducted the amount of such advance allotments authorised in respect of the third quarter of 1948 for the payment for commodities purchased by that Contracting Party from any other Contracting Party.

The Secretary-General of the Organisation will ask the United States Economic Co-operation Administration to inform him of the amounts of the advance allotments mentioned in sub-paragraphs (i) and (ii) of this paragraph. The Secretary-General will submit to the Council for approval the amounts adjusted in accordance with sub-paragraphs (i) and (ii) of this paragraph. Upon approval by the Council, these amounts shall be substituted for the corresponding amounts shown in this table and in table III and shall be forwarded by the Secretary-General to the Agent not later than 31st October, 1948.

(d) Subject to approval by the United States Economic Co-operation Administration and by the Council, the respective amounts of drawing rights may be further adjusted to the extent to which a Contracting Party has been unable to use any advance allotment.

The Government of Turkey, while approving the terms of the present Agreement, reserves its position as to the accuracy of the figures shown in the Annex C relating to Turkey and will, as soon as possible, make every effort, under the aegis of the Organisation, to reach agreement with the countries concerned on the adjustment of these figures.

Column 1 Contracting Parties	Column 2 Total amounts of drawing rights established by the Contracting Parties named in column 1 in favour of other Contracting Parties	Column 3 Total amounts of drawing rights established in favour of the Contracting Parties named in column 1 by the other Contracting Parties
	Equivalent in United States Dollars (figures in millions)	Equivalent in United States Dollars (figures in millions)
Austria	3.1	66.6
Belgium-Luxemburg	218.5	11.0
Denmark	5.1	11.9
France	9.7	333
Greece	.	66.8
Italy	47.3	27
Netherlands	11.3	83
Norway	16.5	48.3
Sweden	34.8	9.8
Turkey	28.5	8.8
United Kingdom	312	30
Bizone	108.8	98.6
French Zone	14.8	15.6
	810.4	810.4

NOTE: The figures inserted for the United Kingdom cover also the countries (including Iceland and Ireland) which comprise the sterling area, that is to say the "Scheduled Territories" as defined for exchange control purposes in United Kingdom legislation.

TABLE III

Details of drawing rights

(a) The following table sets out in detail the distribution as between each pair of Contracting Parties of the amounts of drawing rights set out in Table II.

(b) It also shows the pairs of Contracting Parties which are, for the purpose of Part II of the present Agreement, creditors and debtors in relation to one another, as indicated by the figures in the lines opposite and columns under their names.

All figures in millions of dollars.

Contracting Parties by which amounts of drawing rights shown are established (creditors)	Contracting Parties in favour of which amounts of drawing rights shown are established (Debtors)													Total amount of drawing rights established by Contracting Parties
	Austria	Belgium Luxemburg	Denmark	France	Greece	Italy	Netherlands	Norway	Sweden	Turkey	United Kingdom	Bizone	French Zone	
Austria	—	—	—	—	0.4	2.0	—	—	0.7	—	—	—	—	3.1
Belgium-Luxemburg .	4.5	—	6.5	40.0	13.0	—	72.5	23.0	6.0	2.0	30.0	17.0	4.0	218.5
Denmark	0.1	—	—	—	2.0	—	—	—	3.0	—	—	—	—	5.1
France	2.0	—	2.7	—	5.0	—	—	—	—	—	—	—	—	9.7
Greece	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Italy	—	11.0	—	11.0	7.0	—	—	0.5	0.1	5.0	—	10.1	2.6	47.3
Netherlands	1.0	—	—	—	5.0	—	—	2.5	—	0.8	—	—	2.0	11.3
Norway	1.5	—	—	5.0	2.0	—	—	—	—	—	—	8.0	—	16.5
Sweden	—	—	—	—	5.0	—	2.0	21.8	—	1.0	—	5.0	—	34.8
Turkey	—	—	1.5	—	13.0	—	—	0.5	—	—	—	12.0	1.5	28.5
Unided Kingdom . .	25.0	—	—	200.0	10.0	25.0	—	—	—	—	—	46.5	5.5	312.0
Bizone	32.0	—	1.0	63.0	4.3	—	8.5	—	—	—	—	—	—	108.8
French Zone	0.5	—	0.2	14.0	0.1	—	—	—	—	—	—	—	—	14.8
Total amounts of drawing rights established in favour of Contracting Parties.	66.6	11.0	11.9	333.0	66.8	27.0	83.0	48.3	9.8	8.8	30.0	98.6	15.6	810.4

NOTE: (1) The above amounts of drawing rights are based in part on estimates by the Bizone of coal exports. If these figures are altered during the year ending 30th October, 1948, adjustments may be necessary as outlined in paragraph 7 of the Council Decision on 11th September, 1948, on the division of direct aid and redistribution of contributions and drawing rights (Doc. No. C [48] 158).

(2) The figures inserted for the United Kingdom cover also the countries (including Iceland and Ireland) which comprise the sterling area, that is to say the "Scheduled Territories" as defined for exchange-control purposes in United Kingdom legislation.

IN WITNESS WHEREOF, the undersigned Plenipotentiaries, duly empowered, have appended their signatures to the present Agreement.

Done in Paris this sixteenth day of October, Nineteen Hundred and Forty Eight, in the English and French languages, both texts being equally authentic, in a single copy, which shall remain deposited with the Secretary-General of the Organisation for European Economic Co-operation by which certified copies shall be communicated to all the signatories.

For Austria:	Karl Gruber
For Belgium:	Paul-Henry Spaak
For Denmark:	Gustav Rasmussen
For France:	Robert Schuman
For Greece:	Constantin Tsaldaris
For Iceland:	Petur Benediktsson
For Ireland:	Sean McBride

As Ireland has no payments agreements with other countries and is a member of the sterling area, the provisions of the present Agreement require no specific action by her and signature of the present Agreement on her behalf is subject to the understanding that its operation will not modify the existing arrangements governing payments between her and the other Contracting Parties.

For Italy:	Pietro Campilli
For Luxemburg:	Josef Bech
For the Netherlands:	D. U. Stikker
For Norway:	Brofoss
For Portugal:	Marcello Mathias
For Sweden:	Osten Unden
For Switzerland:	Carl J. Burckhardt
For Turkey:	Menemencioglu
For the United Kingdom:	Stafford Cripps
For the French Zone of Occupation of Germany:	Tarre
For the United Kingdom and United States Zones of Occupation of Germany:	Cecil Weir Wilkinson
For the British/United States Zone of the Free Territory of Trieste:	Ivan White

PROTOCOL OF PROVISIONAL APPLICATION

of the Agreement for Intra-European Payments and Compensations

16th October 1948.

The Signatories to the Agreement for Intra-European Payments and Compensations (hereinafter referred to as the Agreement) signed this day;

DESIRING to give immediate and provisional effect to the Agreement;

HAVE AGREED as follows:

1. The Parties to the present Protocol shall apply the provisions of the Agreement provisionally as if the Agreement had been effective on and after 1st October, 1948.

2. The present Protocol shall come into force on this day's date and shall continue in force until the Agreement comes into force.

3. (a) Any Party to the present Protocol may withdraw from the Protocol by giving not less than three months' notice of withdrawal in writing to the Secretary-General of the Organisation for European Economic Co-operation (hereinafter referred to as the Secretary-General).

(b) Three months after the date on which such notice is given, or at such later time as may be specified in the notice, the Party giving it shall cease to be a Party to the present Protocol.

(c) The Secretary-General will immediately inform all Parties to the present Protocol and the Agent of any notice given under this paragraph.

4. If notice of withdrawal is given under paragraph 3, the Parties to the present Protocol, acting through the Organisation, shall, at the request of any Party, entrust a Committee or Committees with the preparation of recommendations as to the provisions which may be required to avoid

(i) interruptions in trade or payments,

(ii) payments of gold or foreign currency,

(iii) the prevention of repurchase of gold or foreign currency which would otherwise have been possible under the provisions of the Agreement, or

(iv) other similar possible consequences,

which may arise, within a reasonable time from the date when the notice of withdrawal takes effect, as a result of changes in balances caused by compensations made under the Agreement. The Committee or Committees shall also consider the position of drawing rights which may remain unused at the date on which the notice of withdrawal takes effect.

IN WITNESS WHEREOF, the undersigned Plenipotentiaries, duly empowered, have appended their signatures to the present Protocol.

Done in Paris this sixteenth day of October, Nineteen Hundred and Forty Eight, in the English and French languages, both texts being equally authentic, in a single copy which shall remain deposited with the Secretary-General of the Organisation for European Economic Co-operation, by which certified copies shall be communicated to all the signatories to the present Protocol.

For Austria:	Karl Gruber
For Belgium:	Paul-Henry Spaak
For Denmark:	Gustav Rasmussen
For France:	Robert Schuman
For Greece:	Constantin Tsaldaris
For Iceland:	Petur Benediktsson
For Ireland:	Sean McBride
For Italy:	Pietro Campilli
For Luxemburg:	Josef Bech
For the Netherlands:	D. U. Stikker
For Norway:	Brofoss
For Portugal:	Marcello Mathias
For Sweden:	Osten Unden
For Switzerland:	Carl J. Burckhardt
For Turkey:	Menemencioglu
For the United Kingdom:	Stafford Cripps
For the French Zone of Occupation of Germany:	Tarre
For the United Kingdom and United States Zones of Occupation of Germany:	Cecil Weir Wilkinson
For the British/United States Zone of the Free Territory of Trieste:	Ivan White

DECISION of the COUNCIL of O.E.E.C.

on the Application of Certain Principles of Commercial Policy.

16th October 1948.

The Council:

Taking into consideration Article 11 of the Convention for European Economic Co-operation dated on 16th April, 1948, which lays down that: "The aim of the Organisation shall be the achievement of a sound European economy through the economic co-operation of its members. An immediate task of the Organisation will be to ensure the success of the European recovery programme, in accordance with the undertakings contained in Part I of the present Convention", and

Taking into consideration Article 13 of the said Convention which lays down that: "In order to achieve its aim as set out in Article 11 the Organisation may: (a) take decisions for implementation by members", and

Having regard to the introduction of the plan for intra-European payments and compensations and the circumstances in which it is being introduced;

Hereby decides:—

(i) To call upon members to implement the recommendations in respect of certain principles of commercial policy annexed hereto.

(ii) This decision shall have effect as from the date of signature of the Agreement for Intra-European Payments and Compensations recommended this day by the Council for signature and shall be binding only as between the members which are bound to apply the provisions of the said Agreement for as long as they are so bound.

ANNEX

General Recommendations

for certain Principles of Commercial Policy during the Currency of the Intra-European Payments Scheme.

1. In general, it is important that the new resources to be made available to participating countries under the intra-European payments scheme should be used wisely and to the maximum advantage of the participating countries taken as a whole. Further, it is desirable that the development of trade should be along lines which will facilitate orderly progress towards multilateral trading. It is there-

fore necessary that the commercial policies followed by the participating countries should aim both at a restoration of their external equilibrium and at a rationalisation as well as an increase in the flow of intra-European trade, within the framework of the long-term objectives of the Organisation.

2. In particular, the use of the new resources to be made available to participating countries under the intra-European payments scheme is intended to enable debtor countries, to the full extent practicable, to buy under reasonable commercial conditions goods necessary for their recovery.

3. The Council agrees that, at this stage, it would not be advisable to go beyond the formulation of certain principles for the guidance of participating countries in their commercial relations with other participating countries.

4. The participating countries fall into three groups:

(a) Countries which are in substantial surplus (on their balance of payments on current account) with the other participating countries taken as a whole. For convenience, these countries will be referred to in this paper as "net creditor countries".

(b) Countries which are in substantial deficit (on their balance of payments on current account) with other participating countries taken as a whole. For convenience these will be referred to in this paper as "net debtor countries".

(c) Countries which are more or less in balance. For convenience, these will be referred to in this paper as "intermediate countries".

5. The fundamental task of participating countries, as stated in Article IV of the Convention for European Economic Co-operation, is that they should, collectively and individually, correct or avoid excessive disequilibrium in their financial and economic relations, both among themselves and with non-participating countries. The Council wish to make it clear that the recommendations made in paragraph 6 below have been formulated, and must be applied, with due regard to these objectives.

6. In order to attain conditions favourable for the achievement of the objectives set out in paragraphs 1 and 5, the Council recommends that, subject to any modifications necessary to conform to any particular policies recommended by O.E.E.C., the following policies should be pursued during the currency of the intra-European payments scheme.

(i) All countries should seek to increase their trade in order to reach a satisfactory level of economic activity with a view to facilitating their recovery.

(ii) All countries should maintain normal exports necessary to the recovery of other participating countries and each should do its best to increase such exports, if this would enable other participating countries to obtain in Europe goods which are otherwise obtainable only for dollars, provided that such an increase would not prejudice the exporting country's recovery programme.

(iii) Net debtor countries and intermediate countries should do their best to increase their current exports to net creditor countries in order to reduce the disequilibrium as much and as quickly as possible. To this end, net debtor countries and intermediate countries should in respect of exports to net creditor countries take similar steps to those they are taking in respect of current exports to any other country, although they should not be expected to have to accord to the net creditor countries such priorities as may be accorded to exports to countries with whom they have special relations, including those between a metropolitan country and its associated territories.

(iv) Net creditor countries and intermediate countries should buy from net debtor countries additional goods and services as freely as is reasonably practicable in order to reduce the disequilibrium. So far as the export of goods not necessary for the recovery of net debtor countries is concerned, net creditor and intermediate countries should follow a policy which would help the net debtor countries in their efforts to reduce the disequilibrium.

(v) Net creditor countries should buy from intermediate countries, for the purpose of safeguarding the latters' equilibrium, additional goods and services as freely as is reasonably practicable. So far as the export of goods not necessary for the recovery of intermediate countries is concerned, net creditor countries should follow a policy which would help the intermediate countries in their efforts to safeguard their equilibrium.

(vi) Net creditor countries will facilitate the use of the new resources to be made available under the intra-European payments scheme for the purchase of goods necessary for recovery. More particularly, net creditor and other participating countries should do their best to increase their exports to other participating countries of products whose procurement within the group of participating countries may be understood between the countries concerned, or may be considered by the Organisation, to be necessary as a result of decisions taken by the Organisation with respect to the distribution of aid.

It is not intended that the application of these principles should jeopardise a vital economic interest in any participating country.

(vii) Net debtor countries should exercise, in their external expenditure, the maximum of economy compatible with their economic recovery.

7. No attempt has been made at this stage, apart from paragraph 6 (i) and (ii), to formulate general principles for the commercial relations of net creditor countries with each other, or of net debtor countries with each other, or of intermediate countries with each other. It is hoped that the appropriate pattern of trade may be expected to emerge in these cases, if the recommendations in paragraph 6 are followed in respect of the cases in that paragraph.

8. The Council therefore invites the participating countries to examine whether the commercial policies pursued by them during the currency of the intra-European payments scheme are in accordance with the recommendations in paragraph 6; and to inform the Organisation, in time for a further report to the Council by a date to be fixed by the latter, of the result of this examination and of such modifications as they may have made, or may propose to make, in respect of their import and export policy in conformity with these recommendations.

9. The Council recommends also that O.E.E.C. should keep under general review the implementation of the recommendations in paragraph 6, and that it should be open to any participating country to call the attention of O.E.E.C. to instances in which, in its opinion, the recommendations are not being followed.

10. The foregoing provisions are not intended to modify the application of the existing trade agreements between the participating countries, save for possibilities for adjustment by mutual agreement.

Paris, 16th October 1948.

DECISION of the COUNCIL

on the Drawing Rights extended by, or granted to, TURKEY

under the Payments and Compensation Agreement.

16th February 1949.

The Council:

CONSIDERING Annex C of the Intra-European Payments and Compensation Agreement of the 16th October 1948:

HEREBY TAKES NOTE of the Turkish Government's announcement to the effect that an agreement has been reached with the countries concerned enabling Turkey to withdraw the reservation made at the signature of the Payments and Compensation Agreement of the 16th October 1948, regarding the tables in Annex C of the said Agreement;

APPROVES the agreement reached on the 25th January 1949 between the Government of the United Kingdom and the Government of Turkey which provides that the United Kingdom shall grant Turkey a drawing right equivalent to $8 million U. S. under the Intra-European Payments and Compensation Agreement of the 16th October 1948;

DECIDES that this drawing right shall be made available and used in accordance with the provisions of the Payments Agreement on the same terms as if it figured as a drawing right granted by the United Kingdom to Turkey in Annex C, Table III of the above-mentioned Agreement.

RECOMMENDS that the United States Economic Co-operation Administration make such arrangements as may be necessary for the allocation of the conditional aid entailed by the utilisation of this drawing right.

Paris, 16th February 1949.

SUPPLEMENTARY PROTOCOL No. 2

amending the Agreement for International Payments and Compensations.

31st March 1949.

THE GOVERNMENTS of Austria, Belgium, Denmark, France, Greece, Ireland, Iceland, Italy, Luxemburg, Norway, the Netherlands, Portugal, the United Kingdom, Sweden, Switzerland and Turkey; the Commanders-in-Chief of the French, United Kingdom and United States Zones of Occupation of Germany; and the Commander of the British/United States Zone of the Free Territory of Trieste;

BEING THE SIGNATORIES of the Agreement for Intra-European Payments and Compensations (hereinafter referred to as "the Agreement"), signed on 16th October 1948, and of the Protocol of Provisional Application of the Agreement, signed on the same date, in accordance with paragraph 1 of which Protocol the Agreement is being provisionally applied as if it had been effective on and after 1st October, 1948;

HAVING AGREED to sign a Supplementary Protocol providing for certain amendments to Annex C of the Agreement which Annex forms an integral part of the Agreement;

BEING DESIROUS of giving immediate effect to certain provisions of the said Supplementary Protocol; and

HAVING REGARD to the adoption on 28th March, 1949, by the Council of the Organisation for European Economic Co-operation, of a Decision approving the text of the said Supplementary Protocol;

HAVE AGREED AS FOLLOWS:

Article 1 — Paragraphs (c) and (d) of Annex C to the Agreement shall be abrogated.

Article 2 — The following paragraphs (e) and (f) shall be added to Annex C to the Agreement:

"(e) (1) Except as provided for in this paragraph, the amounts specified in Tables II and III shall not be subject to any adjustment in respect of advance allotments.

(2) The following adjustments shall be made: From the amounts of the respective drawing rights established by the United Kingdom and United States Zones of Occupation of Germany, and Turkey in favour of Austria, France and Greece there shall be deducted the following amounts:

TABLE IV

Adjustment of Drawing Rights.

Creditors	Debtors	Amount of adjustment of drawing rights (Equivalent in millions of United States Dollars)
Bizone	Austria	2.9
Bizone	France	23.3
Turkey	Greece	0.7

(3) The amounts adjusted in accordance with this paragraph shall be substituted for the corresponding amounts shown in Tables II and III and shall be communicated by the Secretary-General to the Agent forthwith."

"(f) (1) In cases not provided for by paragraph (e), any Contracting Party which has purchased commodities in respect of advance allotments (hereinafter referred to in this paragraph as the 'importing country') from any other Contracting Party which has established drawing rights in its favour (hereinafter referred to in this paragraph as the 'exporting country') shall have the right to recover against an equivalent amount of its drawing rights any amount of United States dollars which the exporting country has received in payment for the commodities in question provided that:

(i) The importing country makes an application with the exporting country for such payment and notifies the Organisation and the Agent of its application on or before 30th June, 1949;

(ii) After the presentation of all necessary documents in support of its application by the importing country to the exporting country and subject to sub-paragraph (4) of this paragraph, an amount is determined between them as the net amount of United States dollars received by the exporting country in respect of advance allotments referred to hereinbefore;

(iii) The said net amount shall be determined after deduction of payments in United States dollars, if any, received or to be received on or before 31st May, 1949, by the importing country in respect of advance allotments for commodities sold by the importing country to the exporting country;

(iv) The United States dollars in respect of which the application is made by the importing country have in fact been received by the exporting country on or before 31st May, 1949.

(2) Upon notification by the importing country in accordance with sub-paragraph (1) (i) of this paragraph that it has made an application to an exporting country under that sub-paragraph, the Agent shall earmark the drawing rights in respect of the amount applied for.

(3) The maximum sum which the importing country making an application under this paragraph can recover shall not exceed the equivalent in United States dollars of the amount of its remaining drawing rights.

(4) The maximum sum of United States dollars which the exporting country can withhold under sub-paragraph (1) (iii) of this paragraph shall not exceed such amount of United States dollars as the importing country has received or may receive on or before 31st May, 1949, in respect of the advance allotments referred to therein and which is still subject to determination as between the exporting and importing countries. The exporting country can withhold such amount up to but not after 30th June, 1949.

(5) The importing and the exporting countries shall notify the Organisation and the Agent of the outcome of their negotiations with regard to any application made under this paragraph.

(6) For the purposes of paragraphs (e) and (f) the term 'advance allotment' shall mean any advance allotment or supplementary allotment authorised for the third quarter of 1948 by the United States

Economic Co-operation Administration under the Economic Co-operation Act of 1948 in pursuance of which a procurement authorisation was issued which is listed in the Memorandum from the United States Economic Co-operation Administration dated 21st March, 1949, addressed to the Secretary-General of the Organisation, which is appended to the Council Decision of 28th March, 1949, concerning the present Supplementary Protocol."

Article 3 — (1) Articles 1 and 2 of the present Supplementary Protocol shall form an integral part of the Agreement.

(2) Subject to the provisions of Article 5 below, the present Supplementary Protocol shall come into force as soon as the Agreement comes into force.

(3) The present Supplementary Protocol shall remain in force until the operations for which it provides are completed.

Article 4 — Upon the termination of the Agreement any transfers of United States dollars due under Article 2 of this Supplementary Protocol shall take place as against drawing rights remaining at the disposal of the Contracting Parties concerned.

Article 5 — Notwithstanding the provisions of Article 3, the Parties to the present Supplementary Protocol shall apply the provisions of its Articles 1 and 2 with immediate effect.

IN WITNESS WHEREOF the undersigned Plenipotentiaries, duly empowered, have signed this Supplementary Protocol.

DONE in Paris this 31st day of March, 1949, in the English and French languages, both texts being equally authentic, in a single copy which shall remain deposited with the Secretary-General of the Organisation for European Economic Co-operation, by which certified copies will be communicated to all the Signatories of this Supplementary Protocol.

For Austria:	Meinrad Falser
For Belgium:	Hadelin de Meeus d'Argenteuil
For Denmark:	Ejnar Waerum
For France:	Hervé Alphand
For Greece:	Alexandre Verdelis
For Iceland:	Petur Benediktsson
For Ireland:	T. J. O'Driscoll
For Italy:	Attilio Cattani
For Luxemburg:	Nicolas Hommel
For the Netherlands:	D. P. Spierenburg
For Norway:	Otto Chr. Malterud
For Portugal:	Ruy T. Guerra
For Sweden:	Dag Hammarsjköld
For Switzerland:	Gérard Bauer
For Turkey:	Burhan Zihni Sanus
For the United Kingdom:	Edmund Hall-Patch
For the French Zone of Occupation of Germany:	Colonel Paquette
For the United Kingdom and United States Zones of Occupation of Germany:	Malcolm R. White
For the British/United States Zone of the Free Territory of Trieste:	Lt. Colonel W. J. Fleming

SCHEDULE of PAR VALUES

as announced by the International Monetary Fund

and completed up to end of May 1949.

Foreword.

The following is a schedule of the par values which have been established under the Articles of Agreement of the International Monetary Fund.

The Fund Agreement requires that "the par value of the currency of each member shall be expressed in terms of gold as a common denominator or in terms of the United States dollar of the weight and fineness in effect on July 1, 1944". For convenience, all par values in the following schedule have been expressed both in terms of gold and of United States dollars in a uniform manner and with six significant figures, i.e., six figures other than initial zeros. For these reasons, there may arise in a few cases discrepancies in the last rounded decimal figures.

Par values for the following 32 members were established on December 18, 1946:

Belgium	El Salvador	Netherlands (3)
Bolivia	Ethiopia	Nicaragua
Canada	France (2)	Norway
Chile	Guatemala	Panama
Colombia (1)	Honduras	Paraguay
Costa Rica	Iceland	Peru
Cuba	India	Philippine Republic
Czechoslovakia	Iran	Union of South Africa
Denmark	Iraq	United Kingdom
Ecuador	Luxemburg	United States
Egypt	Mexico	

Par values for the countries listed below have been established subsequently:

Venezuela on April 18, 1947
Turkey on June 19, 1947
Lebanon on July 29, 1947
Syria on July 29, 1947
Australia on November 17, 1947
Dominican Republic on April 23, 1948
Brazil on July 14, 1948
French Somaliland on March 22, 1949
Yugoslavia on May 24, 1949.

Par values have not yet been established for the currencies of Austria, China, Finland, Greece, Italy, Poland and Uruguay.

(1) On the proposal of the Government of Colombia in which the Fund concurred on December 17, 1948, the par value of the Colombian peso was changed to the parities appearing in this issue of the Schedule.

(2) In January 1948, the French Government made a proposal to the Fund which included a change in the par value of the franc. On January 26, 1948, the proposal of the French Government was put into effect without the approval of the Fund, and at the present time there is no par value for the French franc agreed with the Fund. The proposal of the French Government related to some but not all of the separate currencies in French non-metropolitan areas, but all of these separate currencies have been omitted from the Schedule at the request of the French Government. A par value for French Indo-China has never been established.

(3) A par value for Indonesia has never been established.

I. Currencies of Metropolitan Areas.

Member	Currency	Par Values in Terms of Gold		Par Values in Terms of U. S. Dollars	
		Grams of fine gold per currency unit	Currency units per troy ounce of fine gold	Currency units per U. S. dollar	U. S. cents per currency unit
Australia	Pound	2.865 07	10.856 1	0.310 174	322.400
Austria	Schilling	Par Value not yet established			
Belgium	Franc	0.020 276 5	1,533.96	43.827 5	2.281 67
Bolivia	Boliviano	0.021 158 8	1,470.00	42.000 0	2.380 95
Brazil	Cruzeiro	0.048 036 3	647.500	18.500 0	5.405 41
Canada	Dollar	0.888 671	35.000 0	1.000 00	100.000
Chile	Peso	0.028 666 8	1,085.00	31.000 0	3.225 81
China	Yuan	Par Value not yet established			
Colombia	Peso	0.455 733	68.249 3	1.949 98	51.282 5
Costa Rica	Colón	0.158 267	196.525	5.615 00	17.809 4
Cuba	Peso	0.888 671	35.000 0	1.000 00	100.000
Czechoslovakia	Koruna	0.017 773 4	1,750.00	50.000 0	2.000 00
Denmark	Krone	0.185 178	167.965	4.799 01	20.837 6
Dominican Republic	Peso	0.888 671	35.000 0	1.000 00	100.000
Ecuador	Sucre	0.065 827 5	472.500	13.500 0	7.407 41
Egypt	Pound	3.672 88	8.468 42	0.241 955	413.300
El Salvador	Colón	0.355 468	87.500 0	2.500 00	40.000 0
Ethiopia	Dollar	0.357 690	86.956 5	2.484 47	40.250 0
Finland	Markka	Par Value not yet established			
France	Franc	No Par Value agreed with the Fund			
Greece	Drachma	Par Value not yet established			
Guatemala	Quetzal	0.888 671	35.000 0	1.000 00	100.000
Honduras	Lempira	0.444 335	70.000 0	2.000 00	50.000 0
Iceland	Krona	0.136 954	227.110	6.488 85	15.411 1
India	Rupee	0.268 601	115.798	3.308 52	30.225 0
Iran	Rial	0.027 555 7	1,128.75	32.250 0	3.100 78
Iraq	Dinar	3.581 34	8.684 86	0.248 139	403.000
Italy	Lira	Par Value not yet established			
Lebanon	Pound	0.405 512	76.701 8	2.191 48	45.631 3
Luxemburg	Franc	0.020 276 5	1,533.96	43.827 5	2.281 67
Mexico	Peso	0.183 042	169.925	4.855 00	20.597 3
Netherlands	Guilder	0.334 987	92.849 8	2.652 85	37.695 3
Nicaragua	Córdoba	0.177 734	175.000	5.000 00	20.000 0
Norway	Krone	0.179 067	173.697	4.962 78	20.150 0
Panama	Balboa	0.888 671	35.000 0	1.000 00	100.000
Paraguay	Guaraní	0.287 595	108.150	3.090 00	32.362 5
Peru	Sol	0.136 719	227.500	6.500 00	15.384 6
Philippine Republic	Peso	0.444 335	70.000 0	2.000 00	50.000 0
Poland	Zloty	Par Value not yet established			
Syria	Pound	0.405 512	76.701 8	2.191 48	45.631 3
Turkey	Lira	0.317 382	98.000 0	2.800 00	35.714 3
Union of South Africa	Pound	3.581 34	8.684 86 (or 173 shillings 8.367 pence)	0.248 139 (or 4 shillings 11.553 pence)	403.000
United Kingdom	Pound	3.581 34	8.684 86 (or 173 shillings 8.367 pence)	0.248 139 (or 4 shillings 11.553 pence)	403.000
United States	Dollar	0.888 671	35.000 0	1.000 00	100.000
Uruguay	Peso	Par Value not yet established			
Venezuela	Bolivar	0.265 275	117.250	3.350 00	29.850 7
Yugoslavia	Dinar	0.017 7734	1,750.00	50.00	2.000

II. Currencies of Non-Metropolitan Areas.

Member and Non-Metropolitan Areas	Currency and relation to Metropolitan Unit	Par Values In Terms of Gold		Par Values In Terms of U.S. Dollars	
		Grams of fine gold per currency unit	Currency units per troy ounce of fine gold	Currency units per U.S. dollar	U.S. cents per currency unit
Belgium.					
Belgian Congo	Franc (Parity with Belgian franc)	0.020 276 5	1,533.96	43.827 5	2.281 67
France.					
French Somaliland	Djibouti Franc	0.004 145 07	7,503.73	214.392	0.466 435
Netherlands.					
Surinam & Netherlands Antilles	Guilder (= 1.406 71 Netherlands guilders)	0.471 230	66.004 9	1.885 85	53.026 4
Indonesia	Guilder	Par Value not yet established			
United Kingdom.					
Gambia	West African Pound (Parity with sterling)				
Gold Coast					
Nigeria					
Sierra Leone					
Southern Rhodesia	Southern Rhodesian Pound (Parity)				
Northern Rhodesia					
Nyasaland					
Cyprus	Cyprus Pound (Parity)	3.581 34	8.684 86	0.248 139	403.000
Gibraltar	Gibraltar Pound (Parity)				
Malta	Maltese Pound (Parity)				
Bahamas	Bahamas Pound (Parity)				
Bermuda	Bermuda Pound (Parity)				
Jamaica	Jamaican Pound (Parity)				
Falkland Islands	Falkland Islands Pound (Parity)				
Kenya	East African Shilling (20 per pound sterling)	0.179 067	173.697	4.962 78	20.150 0
Uganda					
Tanganyika					
Zanzibar					
Barbados	British West Indian Dollar (4.80 per pound sterling)	0.746 113	41.687 3	1.191 07	83.958 3
Trinidad					
British Guiana					
British Honduras	British Honduras Dollar (4.03 per pound sterling)	0.888 671	35.000 0	1.000 00	100.000

II. Currencies of Non-Metropolitan Aeras (continued).

Member and Non-Metropolitan Areas	Currency and relation to Metropolitan Unit	Par Values In Terms of Gold		Par Values In Terms of U.S. Dollars	
		Grams of fine gold per currency unit	Currency units per troy ounce of fine gold	Currency units per U.S. dollar	U.S. cents per currency unit
United Kingdom (continued).					
Mauritius	Mauritius Rupee . . (13⅓ per pound sterling)	0.268 601	115.798	3.308 52	30.225 0
Seychelles	Seychelles Rupee . . (13⅓ per pound sterling)				
Fiji	Fijian Pound . . . . (1.11 per pound sterling)	3.226 44	9.640 20	0.275 434	363.063
Tonga	Tongan Pound . . . (1.2525 per pound sterling)	2.859 36	10.877 8	0.310 794	321.756
Hong Kong	Hong Kong Dollar . (16 per pound sterling)	0.223 834	138.958	3.970 22	25.187 5
Malaya (Singapore and Federation of Malaya)	Malayan Dollar . . . (8.571 428 57 per pound sterling, or 2 shillings 4 pence per Malayan Dollar)				
Sarawak British North Borneo	The Sarawak and British NorthBorneo Dollars which circulate alongside the Malayan Dollar (which is legal tender) have the same value.	0.417 823	74.441 7	2.126 91	47.016 7

ANNEXES

BALANCE SHEET

IN SWISS GOLD FRANCS (UNITS OF 0.29032258...

ASSETS			
			%
I—GOLD IN BARS AND COINS		150,768,767.94	20.9
II—CASH			
On hand and on current account with Banks		38,709,121.76	5.4
III—SIGHT FUNDS at interest		494,049.66	0.1
IV—REDISCOUNTABLE BILLS AND ACCEPTANCES			
1. Commercial Bills and Bankers' Acceptances	8,924,046.38		1.2
2. Treasury Bills	8,756,667.68		1.2
		17,680,714.06	
V—TIME FUNDS AND ADVANCES			
1. Not exceeding 3 months	18,733,547.55		2.6
2. Between 3 and 6 months	7,551,163.64		1.0
3. Over 1 year.	354,364.01		0.0
		26,639,075.20	
VI—SUNDRY BILLS AND INVESTMENTS			
1. Treasury Bills			
(a) Not exceeding 3 months	43,036,310.41		6.0
(b) Between 9 and 12 months	1,119,735.89		0.2
2. Other Bills and Sundry Investments			
(a) Not exceeding 3 months	131,339,214.97		18.2
(b) Between 3 and 6 months	1,526,373.14		0.2
(c) Over 1 year.	12,329,598.51		1.7
		189,351,232.92	
VII—MISCELLANEOUS ASSETS		1,643,015.36	0.2
EXECUTION OF HAGUE AGREEMENTS OF 1930			
Funds invested in Germany:			
1. Claims on Reichsbank and Golddiskontbank; Bills of Golddiskontbank and Railway Administration and Bonds of Postal Administration (matured)	221,019,557.72		
2. German Treasury Bills and Bonds (matured)	76,181,040.—	297,200,597.72	41.1
		722,486,574.62	100.0

NOTE I — For Balance Sheet purposes, the currency amounts of the assets and liabilities have been converted into Swiss gold francs on the basis of quoted or official rates of exchange or in accordance with special agreements applicable to the respective currencies.

The Bank's commitment in respect of the Annuity Trust Account Deposits of the Creditor Governments is not clearly established, but it is stated at its maximum amount in Swiss gold francs.

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS
OF THE BANK FOR INTERNATIONAL SETTLEMENTS, BASLE.

In conformity with Article 52 of the Bank's Statutes, we have examined the books and accounts the information and explanations we have required. Subject to the value of the funds invested in is properly drawn up so as to exhibit a true and correct view of the state of the Bank's affairs books of the Bank, as expressed in the above-described Swiss gold franc equivalents of the currencies

ZURICH, May 4, 1949.

AS AT MARCH 31, 1949

GRAMMES FINE GOLD — ART. 5 OF THE STATUTES)

LIABILITIES			%
I—CAPITAL			
Authorised and issued 200,000 shares, each of 2,500 Swiss gold francs.	500,000,000.—		
of which 25 % paid up		125,000,000.—	17.3
II—RESERVES			
1. Legal Reserve Fund	6,527,630.30		
2. General Reserve Fund	13,342,650.13		
		19,870,280.43	2.7
III—SHORT TERM AND SIGHT DEPOSITS (Gold)			
1. Not exceeding 3 months	244,319.37		0.0
2. Sight	21,409,447.49		3.0
		21,653,766.86	
IV—SHORT TERM AND SIGHT DEPOSITS (various currencies)			
1. Central Banks for their own account:			
(a) Between 3 and 6 months	6,166,076.80		0.9
(b) Not exceeding 3 months	142,213,562.55		19.7
(c) Sight	70,496,736.82		9.8
2. Central Banks for the account of others: Sight	688,741.71		0.1
3. Other depositors:			
(a) Not exceeding 3 months	88,409.91		0.0
(b) Sight	540,003.—		0.1
		220,193,530.79	
V—MISCELLANEOUS		5,411,053.84	0.7
VI—PROVISION FOR CONTINGENCIES		101,448,567.70	14.0
EXECUTION OF HAGUE AGREEMENTS OF 1930			
Long term deposits:			
1. Annuity Trust Account Deposits of Creditor Governments	152,606,250.—		
2. German Government Deposit	76,303,125.—	228,909,375.—	31.7
		722,486,574.62	100.0

NOTE II — Bills rediscounted with the Bank's endorsement and guarantees given amount to Swiss gold francs 4,379,979.70.

NOTE III — Dividends declared prior to the date of the Balance Sheet are less than the 6 % cumulative dividends laid down by Article 53 (b) of the Statutes by Swiss gold francs 170.50 per share or in total Swiss gold francs 34,100,000.

of the Bank for the financial year ending March 31, 1949, and we report that we have obtained all
Germany, we report that in our opinion the above Balance Sheet, together with the Notes thereon,
according to the best of our information and the explanations given to us and as shown by the
concerned.

PRICE WATERHOUSE & Co.

PROFIT AND LOSS ACCOUNT

for the financial year ended March 31, 1949

		Swiss gold francs
Net Income from the use of the Bank's capital and the deposits entrusted to it (including net exchange gains)		7,614,851.44
Transfer fees		883.75
		7,615,735.19
Costs of Administration:—		
Board of Directors — fees and travelling expenses	142,678.21	
Executives and staff — salaries, pension contributions and travelling expenses	1,913,189.86	
Rent, insurance, heating, light and water	96,913.20	
Consumable office supplies, books, publications	187,418.73	
Telephone, telegraph and postage	69,701.71	
Experts' fees (auditors, interpreters, etc.)	29,326.88	
Cantonal taxation	35,483.50	
Tax on French issue of Bank's shares	27,695.40	
Miscellaneous	123,101.02	
	2,625,508.51	
Less: Expenses incurred as Agent under the Agreement for Intra-European Payments and Compensations dated October 16, 1948	111,629.23	2,513,879.28
		5,101,855.91
The Board of Directors has decided that it is necessary to transfer		
to the account for exceptional costs of administration	300,000.—	
to the provision for contingencies	4,801,855.91	5,101,855.91

BOARD OF DIRECTORS*

Maurice Frère, Brussels	Chairman of the Board of Directors President of the Bank
Sir Otto Niemeyer, London	Vice-Chairman

Wilfrid Baumgartner, Paris
Klas Böök, Stockholm
Baron Brincard, Paris
Cameron F. Cobbold, London
Henri Deroy, Paris
Dr M. W. Holtrop, Amsterdam
Albert E. Janssen, Brussels
Prof. Dr. Paul Keller, Zurich
Dr Donato Menichella, Rome
Prof. P. Stoppani, Rome

Alternates

Hubert Ansiaux, Brussels
Jean Bolgert, Paris
George L. F. Bolton, London, or
John S. Lithiby, London
Dr Paride Formentini, Rome

EXECUTIVE OFFICERS

Roger Auboin	General Manager, Alternate of the President
Dr Raffaele Pilotti	Secretary General
Marcel van Zeeland	First Manager, Head of Banking Department
Per Jacobsson	Economic Adviser, Head of Monetary and Economic Department
Oluf Berntsen	Manager
Frederick G. Conolly	Manager

Fabian A. Colenutt	Deputy Secretary

* With regard to the German and Japanese membership of the Board, the legal consequences arising from the situation at the date of this Report remain to be determined.

13th June 1949.