Should Sterling be devalued?

by

THOMAS BALOGH

The Marshall-Plan and Western European reconstruction have plainly arrived at a most critical point. The next six months must give an answer to the question whether the steady improvement which we witnessed in 1948 will continue. The progress towards re-establishing the disturbed equilibrium between Europe and the Western Hemisphere was admittedly slower than the internal recovery in the former. But one could hope that the practical demonstration of the success of the conception underlying the Marshall Plan would lead to its broadening and intensification in order to reduce the grave discrepancy in the international distribution of wealth and income.

The U.S. slump inevitably complicates and aggravates the long-term problem of the dollar shortage from which, however, it should be severely distinguished. It will inevitably depress U.S. demand and increase the pressure of U.S. exports. It will therefore worsen the dollar shortage. This still underlines the importance of reinforcing the policy of Marshall Aid and Mr. Truman's Fourth Point as the only hopeful way of escaping from a competitive vicious circle of deflation and deflation. It would be a mistake to suppose that a premature abandonment of the discriminatory unification of Western Europe as an economic unit and planned expansion of its trade with other countries would lead to anything but a catastrophic drop in international trade and income.

Unfortunately the short-sighted pressure of American business to secure foreign markets has led to a recrudescence of the earlier Free market dogmas associated with the names of Mr. Cordell Hull and Mr. Clayton. Ignoring the fact that dollar purchases are limited by the supply of dollars only they demand a devaluation of European currencies and a restoration of convertibility at least within Western Europe. Especially the need and probability of the devaluation of sterling is being canvassed with unfavourable consequences on British exports.

None would deny that there is always a degree of deflation and unemployment which will balance the current account of any country at any rate of exchange without restrictions. But the question is whether the position the countries reach will represent the highest standard of life in the poorer countries. In the press the paper will be put forward that it is likely to endanger the recovery in Europe and lead to unnecessary hardship. In particular it will be contended that:

(a) devaluation at present would do little to improve our dollar unbalance and might worsen it;

(b) apart from the grievous consequences of the decrease of U.S. imports there is little reason to fear increased competition of the U.S. in third markets so long as pressure is favourable of (even partial) convertibility of European currencies into gold or dollars is resisted;

(c) on the other hand a devaluation might lead to a breakdown in the policy of price stabilisation and thus of the policy of planned full employment;

(d) in the meantime the Export Credit Guarantee Department should be enabled to grant insurance policies against devaluation as to remove the unfavourable effects of the irresponsible talk about an impending devaluation on current exports;

(e) eventually, when the extent of the U.S. slump and the nature of the measures contemplated in that country are better known, a readjustment of all currencies might be contemplated, combined possibly with a revaluation of gold;

(c) immediate steps should be taken to call a Western economic conference to take steps to arrest the threatening slump emanating from the U.S.

It is suggested that the U.S. slump would aggravate the direct dollar gap: the U.S. will undoubtedly buy less in Great Britain and the sterling area. Devaluation is, therefore, advocated to counteract the effects of the slump, by cheapening British exports.

It is argued that there is growing discrepancy between British (European) and American export prices. Hence British (European) manufactures will be displaced by American exports thus impeaching the restoration of economic viability to which we are pledged by the Marshall Plan.

2. The first line argument implicitly applies to the present highly peculiar position: considerations which are based on assumptions which do not hold. In particular it is assumed that world demand is given and will not be affected by devaluation, and that free competition obtains (that is, that international markets are perfect). This is patently untrue.

It is not specified whether an isolated move by Britain is to be contemplated or a general revaluation of currencies in terms of the dollar. Nor are there any indications given as to the quantitative aspect of the measure. It is not even specified that it should be remembered, however, that the Bretton Woods agreement precludes a unilateral devaluation of a currency (i.e. a devaluation without the consent of the Fund) by more than 10 per cent and that in principle only countries which suffer from a fundamental disequilibrium can ask for permission to change the value of their monetary unit. Most countries, one presumes, would qualify on the latter ground for permission to devalue their currency. They all suffer from a dollar shortage. Most of them also suffered from a sterling shortage and only the more liberal attitude on non-essential imports and the release of blocked balances has ameliorated their position.

The question is therefore resolved into what degree of devaluation is to be contemplated by most countries (1). A unilateral devaluation of the £ not followed by other currencies can be ruled out as extremely improbable (2). On the contrary it is probable that in a race of competitive devaluation, sterling will not on the whole (as happened in the 1930s) be left behind, having eventually a greater rather than a smaller problem to face in its relation to the non-dollar area. The relation of the smaller countries to Britain and the sterling area is more vulnerable than the position of the non-dollar countries as a whole to the United States. As the following table shows, their trade with each other has been much more heavily and intensively at great cost and effort, coming on to the dollar shortage would hardly be bearable.

THE TRADE OF O.E.E.C. COUNTRIES WITH NON-PARTICIPANTS (1)

<table>
<thead>
<tr>
<th>Period</th>
<th>Dollar trade</th>
<th>Non-dollar trade</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Exports</td>
<td>Imports</td>
<td>Exports</td>
</tr>
<tr>
<td>1948-49</td>
<td>3,593,540</td>
<td>6,153,183</td>
<td>3,593,540</td>
</tr>
<tr>
<td>1949-50</td>
<td>2,125,625</td>
<td>6,153,183</td>
<td>2,125,625</td>
</tr>
</tbody>
</table>

(1) It is difficult to see that in a country like Belgium could be kept at the present parity with the U.S. if most other currencies were devalued. Their severe unemployment would be further accentuated. Even in cases such as Australia whose most important export prices are determined by the dollar market would hardly be able to maintain the parity on account of the pressure of imports on their volume production. The German and Japanese parties are determined by the Allied (U.S.) Occupation Authorities. But it is difficult to believe that in the case of either one of these countries would be willing to face the worsening of the balance of trade and in the inevitable if they did not follow their non-dollar currencies.

(2) Indeed it is more probable that the problem of sterling will arise as a result of the devaluation of the currency of the European countries which have adopted a more or less laissez-faire policy. From the point of view of effective planning of their recovery of social and democratic progress was obviously premature. And a devaluation will further worsen internal social conditions because of the fall in real wages, which is its first impact effect. Nevertheless it will as difficult to isolate Britain from the effects of a devaluation in Europe (as the growing unemployment will lengthen the period of wage adjustments) as it would be for the Continental countries to ward off the consequences of an isolated British devaluation. It is this point at which the fate of an ordered European reconstruction will in effect be decided.

The problem of the degree of devaluation necessary will be determined mainly by the flexibility of European demand for dollar imports and the changes in U.S. demand for European exports. We must bear in mind, however, that these relations are exceedingly complex: they are by no means determined by the reactions of buyers to price changes alone (4).

(a) On the European side imports from the U.S. are not in most countries, and certainly not in Britain, limited by an interaction of domestic price and income but are directly determined by direct regulation (5). Devaluation and a rise in prices as such would, therefore, not necessarily affect them. A cut in imports from the U.S. as they represent necessities, would have to be enforced by rigorous measures directly cutting demand or, alternatively, by a general and severe deflation. In the case of Britain the visible import surplus from the United States which in 1946 had been reduced to below £ 10 million per month (£ 113.6 million) has in the first two months of this year again risen to £ 11.5 and £ 12.8 million respectively. The Canadian trade showed a deficit of £ 12.3 (C$ 194.9 million) for the year and £ 1.1 and £ 1.7 million respectively. Imports from these countries were running last year at an average monthly level of £ 16.4 and £ 18.1 million respectively.

The share of imports from the Western Hemisphere was to have decreased from 46 per cent in 1947 (or £ 677.4 million of which £ 128.1 million Argentina and £ 168.2 the rest of the hemisphere) to 28 per cent in the first half of 1949 (6). Moreover part of the Western Hemisphere imports (e.g. Argentina) need no longer be reckoned as dollar imports as they are not burdened with a convertibility clause and British export capacity is being restored. Nevertheless the residue, especially Canadian wheat and U.S. tobacco, consists of items difficult to compress. Nevertheless cut will have to be undertaken, especially with respect to petroleum, paper-pulp, etc., imports if only to strengthen our bargaining power (by showing the disastrous consequences of the present trend to the U.S. herself). It should be noted, however, that such measures would in part aggravate the problem of Western Europe as Britain would in turn have to switch from sterling to dollar purchase. But this power of curtailing European sterling supplies may be valuable when it comes to working out a common policy for Western Europe. Should the volume of dollars available for imports from U.S. be severely cut the reduction of cuttings and cuttings will have to be considered in order to equalise the sacrifice enforced. In any case no further relaxation of control at any stage of the production process involving dollar supplies must be contemplated.

So long as the U.S. devaluation continues unabated, the argument for devaluation as a means of cutting imports would favour not a devaluation of a fixed percentage but a lowering of the pound (and other European currencies) find its own level, i.e., the abandonment of a fixed parity with the dollar, as U.S. prices will fall, further, necessarily a repetition of the experiment. The effect of this policy on confidence and thus on the capacity of the Authorities to enforce exchange controls, however, would be devastating. The advocates of devaluation therefore must be in favour not merely of devaluation but also of the simultaneous adoption of deflation and decontrol. The do not hope for an equilibrium from a cut in prices but really from unemployment and a fall in demand. No doubt almost any rate of exchange is compatible with an equilibrium in this sense. But it cannot be held to maximise welfare in any sense of the word.

(b) The case is equally weak so far as exports are concerned. The most massive of sterling exports to America consist of raw materials and foodstuffs from the sterling area and their dollar price is fixed by American demand (7). Indeed an increase in supply consequent to an increase in sterling prices due to devaluation might even result in a fall in total proceeds, as demand is not likely to increase with declining dollar prices. There is no appreciable competitive supply available in the Western Hemisphere which could be displaced by sterling exports. The most important are as follows:

<table>
<thead>
<tr>
<th>Merchandise</th>
<th>£ m.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cents</td>
<td>159</td>
</tr>
<tr>
<td>Tea</td>
<td>13</td>
</tr>
<tr>
<td>Sugar</td>
<td>13</td>
</tr>
<tr>
<td>Silk</td>
<td>24</td>
</tr>
<tr>
<td>Wool</td>
<td>677</td>
</tr>
<tr>
<td>Gold U.K.</td>
<td>1,196</td>
</tr>
<tr>
<td>S.A.</td>
<td>1,954</td>
</tr>
<tr>
<td>Br. Pac. Islands</td>
<td>26</td>
</tr>
<tr>
<td>Total Sterling. £</td>
<td>2,022</td>
</tr>
</tbody>
</table>

It is much to be hoped that the U.S. Government will accelerate the stockpiling programme and similar measures to stabilise the increase of primary producers hitherto postponed for fear of creating inflation. It would be folly to permit the foundering of non-Soviet recovery at this stage. This would be the most important step in stabilising the supply of dollars to Europe.

As far as direct British exports to America are concerned, it is not probable that American demand would expand sufficiently if British exports are made generally (in contrast to selective) cheaper as to more than offset the fall in dollar prices, especially if Britain tried to force the pace during a depression. The American markets for British products are mostly limited because of output, and knowledge on the part of the final consumer in the Middle and Far West of America are lacking. Even in the Eastern Seaboard they are little known.

The importance of customs procedure is shown by the fact that while average duty collected on dutiable commodities has increased from 36 per cent in 1933 to 55 per cent in 1946, 1947, 1948, and 1949, the volume of dutiable imports did not increase more than could be expected from the increase in non-sterling production in the U.S. national income.

Shally does not increase at a rate faster than U.S. productive capacity.

It would be possible to stimulate American demand for foreign imports by a simplification of customs procedure.

The extreme repressibility of the new U.K. Export Credit Guarantee Department may be instructed to issue 6 months insurance policies against devaluation, or the Bank of England should sell 6 months forward dollars against sterling, against legitimate exports to hard currencies.

These observations would seem to hold good for any situation in which there is no over-employment, in which, that is, U.S. demand need not increase at a rate faster than U.S. productive capacity.
of customs regulations and practices or by a unilateral abolition or lowering of the U.S. tariffs. Certain provisions have been made with regard to the former at the time of the conclusion of the General Agreement on Tariffs. Their implementation is as yet uncertain because of the unlikelihood of any early consent of Congress. The general reduction of U.S. tariffs has had disappointing results. While the maintenance of quantitative regulations by most countries outside the U.S. has had the effect of bringing about a de facto unilateral decrease of American protection, de jure the concessions were multilateral and balancing. The U.S. however retained the right of revoking concessions should they prove detrimental to domestic producers. This uncertainty must have had (even apart from the stringent customs procedure) a discouraging effect on would-be foreign exporters to the U.S.

Uncertainty has been further increased by the recent slump in the U.S. While national income has only fallen from 213 billion to 220 billion, or per cent, imports in May show a decline of less than 14 per cent. In other countries the decline in the volume of U.S. marginal propensity to import was relatively higher than the average (though absolutely still very low at even the 1938 demand levels) seems to be borne out (10). A total decline of U.S. imports from 7.1 billion in 1938 to the level of 1937 (5.7 billion) is a distinct possibility and a considerable part of the loss might well fall on the sterling area. The fall in the supply of dollars might represent a large portion of U.S. exports to this area which they now contribute to finance.

We must conclude that the argument for devaluing sterling (and other non-dollar currencies) has little to commend itself at the moment. It is unlikely to improve the dollar balance and might worsen it. In any case it is bound to depress the standard of living unnecessarily and might retard an inflationary spiral.

3. Another train of thought represented by the more sophisticated critics (e.g., the Econ. Inst.) argues that devaluation has become necessary, not so much because of the desire to gain American markets but because of the need to retain third markets against American competition. This is a more plausible argument but one which is still not sufficiently discriminarting.

We must, first of all, differentiate between a disparity of prices due to a proportionately large increase in British wages, a disparity due to discriminating high prices being charged for exports, and, last but not least, the consequences of a readjustment of imports from the dollar towards the sterling and other soft currency areas.

(a) Calculations made by the Economic Commission for Europe (11) show that British wages per hour increased 14 per cent less than those in the United States, if account is taken of the depreciation of the pound in 1939 (12). Productivity in the latter, however, increased more than in the U.K. Relative efficiency wages, therefore, are practically unchanged.

Such calculations are subject to a large margin of error; they leave out account the need for increased European exports. They tend to show that the pressure on Europe originates in the much higher rate of technical progress in the U.S. and her more aggressive selling policies which secure important monopolistic advantages for her products (e.g., tied loans). It is probable that the depression will very much increase this pressure, to which all other European countries are also exposed. The explanation is provided by the colonial expansion in the U.S. during and immediately after the war, when Europe and other countries were in the doldrums. It would be contrary to the spirit of the Marshall Plan if readjustments were to be enforced by a sudden sharp cut imposed on the European standard of life.

Unilateral U.S. help, e.g., by onceded tariff reductions or by Marshall Aid, might in due course diminish this particular cause of disequilibrium.

Thus the discrepancy between the price of British (European) and American supplies due to the higher rate of technical progress in the U.S. would make it desirable to discriminate multilaterally against American exports and thus deliberately to worsen U.S. terms of trade, if the British and European standard of life and employment are to be maintained without continued and increased direct aid. In other words, the extended need better treatment in the U.S. and preferential treatment in other markets if the dollar shortage is to be eliminated and it is to be made to a «market economics» in international trade in the teeth of America's disproportionately growing competitive power, without a sharp rise in the international inequality of incomes.

(b) Secondly, attempts have been made by countries, including Britain and the soft currency area, to charge discriminatingly high prices for the import of essential products to other soft currency areas. This is «discriminatory» being in proportion to the softness of the currency. Thus it is far from the majority of these deals are concerned a system equivalent to a hidden devaluation of the soft currencies in varying proportions has been practised. The new report of the European Economic Commission (especially Chapter 5, sub-section 3) gives an excellent account, and tries to estimate the extent, of some of these discriminatory practices. In the case of steel, 60 per cent, in the case of coal up to 100 per cent, discrimination was found. The discrimination between the home and export price index [February 1949 29.6 (1938 = 100) as against 19.2 for manufactures on the home market] shows that these practices are not restricted to a few instances. In so far as home market prices cannot be said to be below costs (and there is a very substantial margin in at least a considerable number of export prices for a readjustment without undue hardship and without devaluation), a roughly ten per cent cut in export prices should be manageable in the less competitive trades. But it is more favourable to Europe to cut export prices only where necessary and where some favourable result is likely instead of cutting it by a given proportion through devaluation.

Decontrol over a large field of home consumption in Britain (not to talk of the Continent) has much weakened the power of the authorities to force exports despite the possible fall of profit margins below those still obtainable in the home trade and tends to favour the adoption of a general deflationary policy in order to discourage home sales. In view of the unfavourable developments, European governments should take steps to reduce these controls on home consumption (taxation and other discrimination of supplies), which would enable it to import some goods instead of having to enforce a general cut in incomes, consumption and consequently mass unemployment (13).

(c) The last problem involved in this growing price discrepancy is the problem of the redistribution of trade due to the dollar shortage. Certain supplies which could hitherto be acquired in America must increasingly be purchased in the soft currency area. Accordingly, demand for sterling or other soft currency supplies has increased. This would inevitably have brought some disorder into price relations, tending to raise soft currency prices above dollar prices at official rates of exchange. The difficulties have, however, been increased by the almost simultaneous fall of demand and employment in the dollar area. This decline in the U.S. was not entirely due to the shift of European demand away from American markets through the latter must undoubtedly have intensified the trend. There is little that can be done by Europe to remedy this particular problem, due to the exceptional position of the U.S. in the world economy. If as we have argued it is probable that Europe's dollar receipts for exports in the short run would decline as a result of devaluation.

Direct subsidies can hardly be employed in our effort to capture the U.S. market, it would invite immediate retaliation. It might be worth investigating whether a mild increase in taxation especially whether increases in depreciable allowances could be granted in respect to exports to hard currencies areas, the unexpected lag in establishing Development Councils which would have cooperated with Government agencies in overcoming such resistance must be deployed. The finance of these expenditures by a general (and possibly an excess) levy on the whole output of the industries concerned could, moreover, have contributed to equalizing the burden of selling in the U.S.
lation, then we should have to curtail further purchases from the dollar area. Thus unless we are content to cut income and employment, we should have to increase purchases elsewhere and to enforce the cost of the discrepancy between dollar and sterling prices as stable prices will rise further. A vicious circle would be created which would decrease the national income of England and other European countries unless at the same time creating the very same anomalies which we tried to overcome, until, if the orthodox solution were pursued far enough, equilibrium would be secured by unemployment and the decline in the standard of life.

(ii) We must now consider the consequences of these price discrepancies on third markets. These markets can be divided into two categories. There are, first of all, those which have at present dollar surpluses and, secondly, those which have no dollars or use dollars they can export. The latter group includes especially few countries which are in the first favourable position, because they have rubber and tin, and their exports are decreasing indirect taxation falling on the poorer classes. There are, of course, a few other countries in the same position, in the case of which complicated administrative arrangements are not possible. Only a few, like Israel, could be an important source of dollars. In these cases indirect measures might be employed in order to overcome the price difference. It was rumoured, for example, that Israel would be prepared to give Britain free cash for every £ 100 of capital investment. Such schemes should be very carefully investigated. It is probable that there will be some falling off of exports and of employment. Unremunerated exports which are combined with current transactions which bring in dollars and subsequently increase our invisible exports would represent an exceedingly profitable Public Works Programme.

In other cases outright subsidies will have to be considered in bringing down the price of our exports (40), without worsening our terms of trade with the U.S. It is sometimes argued that no further subsidies exist for such vital purposes but because taxation has reached its limits. This argument cannot be advanced by those who advocate devaluation. A devaluation means nothing more than a flat indirect tax on all imports and a flat duty on all exports. But, as we argued, it would be wise to increase indirect taxation indiscriminately and equally on all imports, in the case of many exports, moreover, there is no need to grant an export subsidy which is automatically given by devaluation. A selective system of indirect taxation, plus subsidies, would therefore be less dangerous to the stability of the nation's policies than devaluation and its influence can be more accurately controlled. The only telling argument against this method is that it might be too difficult to administer. This argument has been used often before. In the majority of cases, after some time had been lost, events forced the adoption of the policy considered impossible. In view of the fact that only a small number of countries and a narrow range of commodities would fall into this category it would seem advisable to work out detailed programmes immediately.

It is unfortunate that it is not likely that our exports to the sterling area countries will suffer as a result of the decline in the American market and the consequent decline in dollar prices and in the volume of U.S. purchases. Unless alternative (sterling) markets can be found in areas not affected by the U.S. slump, incomes and demand in these areas will decline. Thus both dollar earnings and British exports are likely to be affected. Far too little attention has as yet been paid to the problems of intra-sterling area stabilisation (45).

Secondly, there are countries which at the moment have no dollar surplus. These can be divided into two categories: those who have no (considerable) dollar earnings at all and those who at present have such dollars they can obtain for purchases in the United States. Most of these countries would like to increase their purchases in the U.S. still further. They are prevented from doing so by their inability to obtain more dollars. Theoretically Britain (and Europe) could transform these countries into net dollar surplus countries by displacing U.S. exports. And we might assume that those who wish this and other countries to devalue, hope that such displacement could be effected.

The answer to this argument is that while it might theoretically be possible to displace American goods sufficiently to obtain dollars in this triangular fashion in practice it is not possible to do so in the short run as supplies now obtained in the United States are either not available elsewhere or if available are severely hampered by market imperfections (taste etc.) in favour of the U.S. products. Nor is it evident that a competitive devaluation and deflation necessary to displace the U.S. by straight price competition will result in optimum real income in Europe.

It is a mistake to suppose that the U.S. depression will necessarily affect the volume of British (and European) exports to the non-dollar areas. There is no manifest destiny in the course of our trade. Provided we refuse to compete with American depression dumping and isolate ourselves, Europe might restrict the U.S. slump to the consequences of the decline of the American imports. These will in all probability be serious (46). The overwhelming majority of the non-Communist world consists of countries which have no saleable dollar earnings or which spend such dollars they have on U.S. supplies. How much they buy in the U.S. is therefore determined by their dollar earnings. They cannot increase their purchases in the U.S. beyond that level however cheaper American supplies may be. If they want to buy foreign goods (mainly manufactured beyond the level permitted by their dollar earnings (even of the same general type as those which they buy from the U.S.) they can only buy these from countries to which they can sell and earn foreign exchange, i.e., Britain and Europe. Moreover it is more important for them to sell at relatively attractive prices than to match transitory profits by buying cheaply because they must be well aware of the fact that the inevitable and ultimate consequence of the transitory gain by buying cheap will be that their export prices will also be cut. That this is being realized is
shown by the successful conclusion of a 5-year agreement with Argentina which circumvents the dollar shortage (17).

It might be objected that they will refuse to buy the same goods «dearer» elsewhere than they can obtain them in the U.S. This objection is founded on a double fallacy. These countries cannot obtain all the goods they desire from the U.S. (over and above their dollar earnings) for they have no dollars. An attempt to extract dollars from their trading partners — as, for example, Belgium has attempted — would merely result in retaliatory decrease of their exports, for no country has «plus» dollars. It is the dollar shortage which forces a decrease of U.S. exports and not the «wickedness» of «planners». The only question which is open is whose purchases from the U.S. will be reduced. This question can be answered by planned distribution of available dollars (to those countries having relatively greater supply paying for some of their imports from their less favoured partners in dollars) or by an interstate struggle for dollars through competitive devaluation and devaluation hoping to achieve extra-U.S. surpluses convertible into dollars (18). In the latter case they might try to snatch transitory gains by insisting on being paid in dollars in order to buy in the U.S. The consequence inevitably will be a further narrowing of trade. These gains obtained by buying «cheap» will fade as every country will find itself unable to export. Their own prices will begin to drop either because of an enforced deflation in Britain (and Europe) or because of the value of their currency in terms of sterling for other European currencies is still appreciated. The U.S. markets will be narrower.

On the other hand, by concluding reciprocal agreements and maintaining a tolerably stable price level, the consequences of the U.S. slump can be restricted to the losses suffered by not being able to sell to U.S. at better prices and in larger quantity. Even this will be inconvenient and might be extremely damaging; but the real catastrophe of a multiple shrinking of foreign trade could be avoided.

If we bear this in mind the clamour about «defending» «third» markets is difficult to understand (with the exception of those few in the first category which still have dollar surpluses).

The problem of the third countries is exactly analogous to our own. The import requirements from the U.S. at a tolerable standard of life are far higher than dollar earnings. In the short run the «free» play of price mechanism will not make available non-dollar supplies in sufficient quantity to take the place of goods now supplied by America. This is as much true of machinery and manufactures which South America needs, as it is of food and raw materials we need. If dollars were available, the change in taste towards American products, the superior capital resources enabling aggressive sales and the grant of credits will mean another war in the dollar market. The drastic decrease in the standard of life needed to match U.S. competition without discrimination is politically so dangerous as to be ruled out. Nor could the non-dollar world escape this dilemma by a general devaluation — because of the probable fall in dollar earnings and because of the consequent inevitable further aggravation of the U.S. slump.

There is not the slightest reason to doubt that even a partial convertibility of European currencies into dollars would now cause a wholesale restriction on European trade, especially if, as is unhappily probable, the American deflation continues, and an interstate struggle for dollars would be started. The interconvertibility of currencies in Europe will follow as soon as a greater monetary unification has taken place in Europe. It is not possible so long as only Britain is engaged in keeping on an even keel, neither inflating nor deflating. Intra-European payments and trade should be encouraged. But this can be done most effectively by a tentative relaxation of quantitative restrictions. Even that would have to be accompanied by a much closer co-ordination of investment and general economic policies than has hitherto been the case. Dollar convertibility can be restored even partially after European reconstruction has been achieved in diminishing the inequality of opportunity between the two Continents, and the U.S. regained her equilibrium.

It is from this point of view that recent proposals in favour of «liberalising» intra-European trade must be judged (20). To these we now turn.

(19) The loss of gold by Britain of 4.1 million dollars is Britain, £5 million to Switzerland, and £4.5 million to Germany. A total of 4.1 million dollars is Britain, £5 million to Switzerland, and £4.5 million to Germany. Germany suggests that too little attention has been paid in the flush of recovery of 1949 to these questions.

(20) The unbroken increase of British imports indicates, however, that, as in 1946, the Government has raised control too much. A repetition of the 1947 exchange crisis is a distinct possibility.

4. These considerations suggest that a devaluation of sterling and of other non-dollar currencies should not be contemplated as long as the extent of the U.S. slump is not calculable. A devaluation would aggravate the dollar shortage and might aggravate the slump and thus intensify the original problem. In the meantime the policy hitherto pursued by O.E.C.D. to strengthen the productive capacity of the non-dollars would need to be intensified and steps taken to reinforce controls needed to isolate Europe from the consequences of the U.S. slump which would otherwise retard capital investment and thus slow down the increase in European productivity.

The essential task, as we have seen, is the prevention of a competitive struggle for dollars. In relation to non-American territories this could be achieved by reciprocal bulk purchase agreements. As most European (and British) imports are standardised this should prevent little difficulties. European (and British) exports are more difficult to deal with as they mainly consist of an infinite variety of manufactured products. This difficulty can most easily be overcome by securing agreements which will release the money from bulk purchase goods free to choose between the goods forming the exportable surplus of the bulk purchasing country. The vendor would, however, not be free to spend the money caused by the bulk purchase contracts anywhere else except with the permission of the purchaser.

The liberalisation of trade promised to the Americans should be undertaken by relaxing quantitative controls rather than by automatic transferability and steps should be taken to review the rights and duties of the vessels and administrative transferability. Thus competition for dollars might be avoided and a shrinkage in trade prevented; final judgment must wait for the exact wording of the agreement to be published.

It is in our relations with the non-dollar
area, however, that British economic statesmanship will be tested. A split in the policy of these countries, the spread of the deflation among them, would narrow the area in which a satisfactory level of foreign trade can be maintained. Already Belgium and Germany suffer from unemployment of a severity not much better than 1929/32 and show an export surplus with all other areas of Europe and the sterling area. The wider the spread of the degree of enforced self-sufficiency, the greater the shrinkage of imports will have to be curtailed.

Britain will have to make active contributions from her own export surplus in a group of countries dedicated to full employment policy. Her standard of life is greater than that of any of the other countries. Thus any policy to counter the inevitable losses in dollar-markets (21) will have to give priority to a scheme of foreign investments (unrequited exports). This is the more desirable as it would to a considerable extent avoid the large-scale shifting of labour inevitable if the usual 'public works' programmes were undertaken and which seem politically unmanageable. The effects of unrequited exports by the grant of Loans or permission to draw on blocked sterling balances could be combined with agreements which either promptly or eventually bring in foreign income or improve our supplies, i.e. our terms of trade. With the increase in steel production we should be able to do this without undue strain as most overseas would wish to increase the imports of capital goods. The investment programme in the Colonial Empire could be speeded up. Britain could also participate in the investment programme of Israel which, as mentioned above, would bring in some important elements. We might come to some combined trade and payments agreement with India by which our self-balancing trade with India would increase, provided we permitted them to draw... (21) On the negative side, the sacrifice due to the fall in U.S. supplies should be equitably distributed. It will be necessary to re-introduce clothing rationing and a rationing of tobacco and spirits. The size of newspapers will have to be curtailed, and less likely to be reduced in the near future. It would be desirable to explain to the potential user that the measure of the sacrifice exacted should not lead to astonishment.
The Dilemma of the O.E.E.C.

by

GIUSEPPE UGO PAPI

I - The dilemma of the post-war period.

In this post-war period all countries, and above all those of Europe, find themselves faced by the following dilemma: they must either return to a policy of economic self-sufficiency, reducing their imports from the dollar area and producing for themselves such staples as cereals, meat, and fats, or they must continue importing on a large scale from the dollar area and intensify their trade with other countries. This is not — as some may be inclined to think — a theoretical debate. The problem involved will come up for discussion during the new stage of the work of the O.E.E.C.

A study of the plan for 1949-50 and of the long-term plan extending to 1952-53 presented by the 19 participating countries to the Paris meeting of the O.E.E.C. confirms the presence of this alternative, for it leads us to note the following fundamental facts: (1) that in 1952 the whole productive effort of the participating countries will not suffice to raise the food level of the European countries represented above that of the pre-war period; (2) that neither will the expected growth of trade between the participating countries suffice to rebalance their several economies. What then is the path each country should follow to secure once more a lasting economic balance?

II - The self-sufficiency hypothesis.

Should a self-sufficiency policy be adopted, it might perhaps be possible to economise some hundreds of millions of dollars on imports from the dollar area during the E.R.P. period; but then countries like Italy would have to meet the situation arising from the production of larger quantities of certain staples at ever growing costs; to introduce high protective duties or other forms of protection against the competition of the low cost countries; to shift the balance now attained in plans for public works — as for instance in agriculture — and to favor land-reclamation rather than well-considered irrigation works. Such countries would also be forced to follow a more active policy for assuring growers of the leading staples remunerative prices on the home market; in some case, more especially for wheat and sugar; these prices would have to be considerably above those ruling in transoceanic countries. But this — experience acquired in the period between the two wars shows it — would not bring about the rebalancing of the economics of the several countries. The recovery of that balance can only be secured — need we repeat it? — by the active operations of the mechanism of imports and exports. Should that mechanism fail to operate, should it not operate from now till 1952, the economic structure of each country, whether participating or not in the benefits conferred by the E.R.P., instead of remaining at the level attained will suffer an inversion.

III - The larger trade hypothesis.

Under the second hypothesis which foresees a steady growth of the trade of each country with all the others, both European and non-European, the prospective situation would be different.

Italy would still need remunerative prices and moderate protection for some agricultural staples, on lines in keeping with those of a