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CONSUMPTION PATTERNS IN THE UNITED KINGDOM AND THE UNITED STATES

Robert A. Rennie

The theoretically unique relationship between consumption and income--the Consumption Function--has been one of the foremost tools of economic analysis during the past decade. This function is an abstraction, representing the changes in consumption accompanying changes in income when the impact of all other variables is assumed to be removed. As a generalization from economic data, it has been utilized with varying success to forecast consumer expenditures in the postwar period. If past inadequacies are to be avoided, it will be necessary in the future to proceed with considerably more intensive analysis of other factors independently influencing consumption.

Two of these factors are particularly applicable at the present time in both the United Kingdom and the United States, (a) the satisfaction of consumer demands which could not be met during the war, and (b) the current spending by certain income groups of liquid assets which were accumulated more or less involuntarily. The backlog of demand and the "surplus" of liquid assets are closely interrelated in origin for the inability to satisfy normal demands produced an accumulation of savings which would not otherwise have appeared. But presumably there was a partial shifting of expenditures to commodities and services which were more readily available during the war.

As a result, current involuntary savings might have been initially less than the unfulfilled demand for specific types of commodities which the public normally would have wished to buy. On the other hand, with the passage of time, certain deferred demands expired or did not accumulate in regular progression. For instance, a person who customarily renewed his automobile every two years did not desire two vehicles at the end of hostilities. Thus, the accumulation of liquid assets was probably larger than the backlog of demand. Except for certain types of commodities, however, it would be difficult to express in quantitative terms the extent of such suppressed demand.

A further consideration would arise if there were any significant upward price movements. The cost of replenishing the depleted stocks of consumers' goods would have been considerably affected. It is reasonable to assume that the price elasticity of such deferred demand is less than unity, and that, if income remained constant, total demand would be increased. It is unlikely, however, that there would have been significant changes in the money value of the liquid assets. It was government policy both in the United States and in the United Kingdom to maintain public securities above par. Thus, their purchasing power would decrease, and effective demand might decline on balance.

Moreover, with rising prices, the public would feel the need to hold larger reserves of liquid assets for precautionary purposes. It is possible that prices might rise to such an extent that the willingness of individuals in the aggregate to decrease their holdings of claims and assets would be zero. This point is reinforced by the findings of the Survey of Consumer Finances conducted for the Board of Governors of the Federal Reserve System: "Only a relatively few people consider their government bonds and bank deposits as liquid funds, that is, as funds temporarily held in these forms pending opportunities for spending or investment."1/ Under these circumstances, current disposable income would be divided between deferred, present, and future demands in such a manner that the most urgent requirements would be satisfied. Although there might be some element of substitution between present and future commodities (i.e. savings) because prices are expected to decline in the future or because certain classes of goods are relatively scarce, in general, deferred requirements would be met partly by sacrificing current marginal demand but primarily by reducing the present volume of personal savings.

To give the foregoing analysis a concrete setting, the relation between disposable income2/ and consumption has been calculated for the United Kingdom and the United States during a period encompassing widely varying economic conditions. The series in Table I have been expressed in terms of dollars and pounds of uniform purchasing power. It is necessary to make such an adjustment, since a regression formula derived from series in current values would have little meaning. In such a case, it would be possible to

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1/ George Katona and Rensis Likert, "Relationship between Consumer Expenditures and Savings: The Contribution of Survey Research", The Review of Economic Statistics, November 1946, p. 198.

2/ Disposable income equals national income less corporate savings less personal taxes less contributions to social security funds plus transfer payments.

derive a wholly fictitious regression line from observations which reflected nothing more than changes in the price level.[1] The series have also been adjusted to eliminate the influence of population changes upon the basic data.

Table I
Disposable Personal Income and Consumption[a]

Year	United Kingdom: Disposable income (In billions of pounds sterling)	United Kingdom: Consumption (In billions of pounds sterling)	United Kingdom: Consumption as percentage of disposable income	United States: Disposable income (In billions of dollars)	United States: Consumption (In billions of dollars)	United States: Consumption as percentage of disposable income
1924	3.2	3.1	96.9	66.9	59.4	88.8
1925	3.3	3.2	97.0	67.9	61.0	89.8
1926	3.4	3.3	97.1	69.6	62.8	90.2
1927	3.5	3.4	97.1	70.2	63.0	89.7
1928	3.6	3.5	97.2	71.3	64.3	90 2
1929	3.6	3.7	102.8	74.6	66.3	88.9
1930	3.4	3.6	105.9	67.1	61.7	92.0
1931	3.4	3.6	105.9	61.7	56.2	91.1
1932	3.4	3.8	111.8	52.1	49.3	94.6
1933	3.7	4.0	108.1	53.6	51.5	96.1
1934	3.9	4.1	105.1	58.9	55.1	93.5
1935	4.2	4.2	100.0	63.1	58.5	92.7
1936	b/	b/	-	71.8	65.2	90.8
1937	b/	b/	-	73.1	66.0	90.3
1938	4.4	4.3	97.7	67.1	62.4	93.0
1939	4.5	4.3	95.6	72.8	66.3	91.1
1940	4.3	3.8	88.4	77.1	69.6	90.3
1941	4.4	3.7	84.1	92.0	82.3	89.5
1942	4.6	3.6	78.3	103.8	81.1	78.1
1943	4.6	3.6	78.3	109.3	84.4	77.2
1944	4.7	3.6	76.6	118.0	89.2	75.6
1945	4.7	3.8	80.9	117.8	95.1	80.7
1946	4.5	4.1	91.1	112.9	102.4	90.7
1947[c]	4.6	4.4	95.7	113.2	105.9	93.6

a/ Adjusted for cost-of-living and population changes.
b/ Not available.
c/ See footnotes (b) and (c) to Table II.

Several significant facts emerge from the data, especially in the case of the United Kingdom. Beginning in 1929 and continuing throughout the early 'thirties, consumption exceeded disposable income in that country. This situation did not occur at any time in the United States although there was a substantial increase in the ratio of consumption to income in this country as well. Analyzing the underlying series for the United Kingdom, Colin Clark ascribes this dissaving to the desire of upper income groups to

1/ Paul A. Samuelson in Alvin H. Hansen, Fiscal Policy and Business Cycles, (New York, 1941), p. 252.

maintain their standards of living.1/ At no time during the depression did the consumption of this group, measured in real terms, fall below the average of the period 1924-28. Consumption was maintained at the expense of a decline in overseas assets; a large segment of the undistributed savings of corporations during this period thus was offset.

Of more immediate relevance to current analysis is a comparison of consumption trends in the two countries during the war and postwar period. First, a measure of suppressed consumption was obtained in order to reveal the relative sacrifice of consumption. It also serves to indicate in approximate terms the general magnitude of the liquid assets accumulated by the public over and above what would have been saved in a normal period. To derive such a measure, a comparison was made between potential consumption as indicated by the normal relation between disposable income and consumption in the period preceding the war, and actual consumption as revealed in the national income series.

The consumption functions for two different periods were derived, one for all the prewar years subsequent to 1923, and another omitting all the years of depression. As Woytinsky has indicated,2/ there may be logical reasons for separating the years of prosperity from those of depression in deriving consumption functions, but in this case a comparison of the relation revealed that there was merely a shifting in the level of consumption between the two periods. Since we are not specifically concerned with the absolute values of consumption, but primarily with the comparison of consumption trends between the United States and the United Kingdom during this period, the choice of a base period makes no particular difference in our analysis.3/ The data for all the years supply a greater range of observations and give a much better fit to the regression line; this period has been selected therefore as the basis for deriving the quantity which, with the given volume of disposable income, the public would have wished to consume during the war and postwar period. However, to illustrate how slightly the results would have been affected by the selection of a different base, the index of suppressed consumption computed from a regression formula for the prosperous years only is appended to Table II.

A study of Table II reveals that suppressed consumption as a percentage of disposable income was much higher in the United Kingdom than in the United States during the war. Whereas suppressed consumption rose to 21.7 per cent of such income in 1943 in the United Kingdom, it never exceeded 10 per cent of disposable income in the United States. The postwar experience

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1/ Colin Clark, National Income and Outlay, (London, 1937), pp. 250-254. The aggregate statistics in Table I do not reveal the consumption-income ratio for the upper income groups. For persons with incomes above £250 annually, the relationship was 91.7 per cent during the period 1924-28, 116.6 per cent in 1930, 125.9 per cent in 1931, 136.0 per cent in 1932, 115.9 per cent in 1933, 109.8 per cent in 1934, and 110.7 per cent in 1935.

2/ W. S. Woytinsky, "Relationship between Consumers' Expenditures, Savings, and Disposable Income", The Review of Economic Statistics, February 1946, pp. 2-3.

3/ When absolute levels in a particular country are under consideration, the choice of a base period for the computation of the consumption function is of significance. But since there is such a small change in the level of consumption when the alternative base period is chosen, our conclusions are not materially affected.

is markedly different. While the United Kingdom has had to divert an increasing proportion of its production to exports and to the replacement of capital, the United States has consumed a larger proportion of its income than would have been anticipated from the normal prewar relation between consumption and income. We would have expected this result in a country where most wartime controls have been lifted and where the backlog of consumer purchasing power serves to make the production of consumer goods relatively more profitable.

Table II
Index of Suppressed Consumption

Year	Disposable personal income	Potential consumption	Actual consumption	Suppressed (+) or overconsumption (-)	Suppressed (+) or overconsumption(-) as percentage of disposable income a/	
	United States (In billions of dollars)					
1941	92.0	80.4	82.3	-1.9	-2.1	(1.1)
1942	103.8	89.5	81.1	8.4	8.1	(9.4)
1943	109.3	93.7	84.4	9.3	8.5	(10.1)
1944	118.0	100.5	89.2	11.3	9.6	(11.3)
1945	117.8	100.3	95.1	5.2	4.4	(6.2)
1946	112.9	96.5	102.4	-5.9	-5.2	(-3.6)
1947 b/	113.2	96.8	105.9	-9.1	-8.1	(-6.5)
	United Kingdom (In billions of pounds sterling)					
1939	4.5	4.5	4.3	0.2	4.4	(2.0)
1940	4.3	4.3	3.8	0.5	11.6	(7.8)
1941	4.4	4.4	3.7	0.7	15.9	(12.3)
1942	4.6	4.5	3.6	0.9	19.6	(16.9)
1943	4.6	4.6	3.6	1.0	21.7	(19.6)
1944	4.7	4.6	3.6	1.0	21.3	(18.4)
1945	4.7	4.7	3.8	0.9	19.1	(13.4)
1946	4.5	4.5	4.1	0.4	8.9	(5.4)
1947 c/	4.6	4.6	4.4	0.2	4.3	(0.8)

a/ The first column presents the percentage derived from the consumption function for all prewar years subsequent to 1923. The column in parentheses is the percentage as derived from the consumption function for the base period with the years of depression omitted.
b/ On the basis of data for the first three quarters.
c/ An estimate for the year based on official data.

With regard to the United States, the next question is whether any projection of the present trend in "overconsumption" can be made, and what significance it would have for the level of economic activity in this country. If there should be a return to the prewar relation of consumption to income, it is likely that there would be at most only one more year of "overconsumption" of the present type.[1] Certainly most of the backlog of consumer demand will have been met by that time, and the continuing advance in prices will curtail most of the voluntary spending of liquid assets. Such a return to the prewar relation between consumption and income would pose several serious problems for the future maintenance of a high level of business activity in this country. Not only would a decline in the ratio of consumption to income increase personal savings but it would also reduce the amount of induced investment. Furthermore, the psychological shock to business expectations of such a relative decline in consumption at this juncture might well be serious.

The situation is very different in the United Kingdom. Although scheduled capital expenditures have recently been reduced by government action, there is little likelihood in 1948 that the public will be able to increase consumption to the level indicated by the prewar consumption function. The allocation of manpower and resources to the export industries will continue to be necessary in order to reduce the gap in overseas payments. It would appear, therefore, that the present excess volume of liquid assets accumulated during the war must be held indefinitely, even though unwillingly, by the public unless the Government introduces measures which would either withdraw them from the economy or neutralize their effects upon incentives. Such government policies would indeed seem imperative, because these liquid assets are a deterrent to the achievement of production and export goals. A change in monetary and credit policy is required which would restore equilibrium between purchasing power in the hands of the public and the current volume of consumers' goods.

1/ The assumption of a return to the prewar consumption function is basic to this type of analysis. It is possible that the increase in consumers' expenditures results from a fundamental redistribution in income during the war. Although the present statistics are inadequate to form a definite conclusion, a preliminary study indicates that changes in the consumption function for this reason are relatively small. Cf. Harold Lubell, "Effects of Income Redistribution on Consumer's Expenditures", The American Economic Review, March 1947, pp. 157-170.

ARGENTINE TRADE AND FINANCIAL AGREEMENTS

Ernest C. Olson and Harry Gillis

In recent months a number of trade and financial agreements have been negotiated by Argentina with various other countries. Although these agreements necessarily differ markedly with respect to trade provisions pertaining to specific commodities, and with respect to the amount of credit extended where financial provisions are included, a pattern is discernible for types of agreement and for certain geographic areas. An examination of the differences and similarities serves to illuminate Argentine economic policy during a period of slightly more than a year--from June 1946 to July 1947. No attempt is made to present a detailed analysis of each agreement nor to report an exhaustive list of treaties to which Argentina is a party. The discussion is confined to the more important provisions of the agreements negotiated during the interval cited.

Mid-year of 1946 found Argentina producing and exporting large quantities of agricultural commodities which were desperately needed by war-devastated areas and in considerable demand elsewhere. The present Government, which assumed office on June 6, 1946, appears to have taken early advantage of this fortunate circumstance in bartering to obtain favorable treatment with regard to its imports, notably to assure delivery of specified amounts of certain scarce commodities. Although during the previous two and one-half years Argentina had signed only three agreements of the type discussed below, one with Spain in 1944, one with Sweden, and one with the United States in the following year, eleven agreements were signed between June 6, 1946, and the end of July 1947. The following table summarizes these agreements but does not include others which were still under negotiation at the end of this period. Arrangements of a special contractual nature, such as the meat contract with the United Kingdom, the purchase of the French and British Railways, and the linseed oil contract with the I.E.F.C., do not appear in the table.

Country	Date of Signature	Type of Agreement a/
Peru	June 14, 1946	Supply: Minerals for Wheat
Ecuador	August 5, 1946	Supply: Rubber and Petroleum for Wheat
South Africa	August 9, 1946	Supply: Coal for Corn
India	September 27, 1946	Supply: Jute for Grain
Spain	October 30, 1946	Commercial and Financial
Brazil	November 29, 1946	Supply: Rubber and Textiles for Wheat b/
Chile	December 13, 1946	Commercial and Financial
Switzerland	January 20, 1947	Commercial
Bolivia	March 26, 1947	Commercial and Financial
Czechoslovakia	July 2, 1947	Commercial and Financial
France	July 23, 1947	Commercial and Financial

a/ "Supply" agreements are those concerned only with the delivery of specific commodities. The designation "Commercial" refers to a broader type of agreement which includes, in addition to supply provisions, various clauses pertaining to commercial aviation, insurance, shipping, and the exchange of motion picture films, books and periodicals, students, skilled workers, and persons engaged in various professions. Commercial agreements which involve an extension of credit by Argentina are designated "Commercial and Financial" agreements.

b/ The Brazilian agreement although classified as a "supply agreement", also contains a navigation clause which provides that commodities covered by the agreement shall be transported preferably in Argentine and Brazilian vessels, in equal proportion.

Supply Agreements

Under this type of agreement Argentina is committed to guarantee or facilitate the export of certain Argentine products (chiefly grains) to the other signatory country in exchange for similar concessions with respect to specified products which Argentina desires to import, in most instances coal, petroleum, rubber (including tires), and jute. The supply agreements, characteristic of the early months of this period, appear to be interim arrangements entered into through a simple exchange of notes pending the negotiation of more comprehensive agreements at a later date. Evidence to support this view may be found in the supply agreement between Argentina and Ecuador which specifically provided that steps would be taken to negotiate a commercial agreement.

The first agreement, that with Peru, provided that Argentina would make available to Peru a specified quantity of wheat at a stated price for a period of one year, while Peru would undertake a similar obligation with regard to Peruvian products desired by Argentina. The Ecuadorian agreement provided not only that certain products would be traded but also that each party would request legislative approval of certain tariff reductions. The parties further agreed to enter into the negotiation of a commercial treaty. The terms of the agreement with South Africa provided for the exchange of only two commodities, coal and corn, and for the preferential use of Argentine vessels in this trade. Although the details are not available, it is understood that the agreement with India was to remain in effect for one year and that the terms were similar to those of the other supply agreements. The supply agreement with Brazil, although established by an exchange of notes, became effective only after the formal signing of the treaty. Certain elements characteristic of the later commercial agreements are discernible in this treaty: (1) the terms require the parties to buy or sell specified amounts of selected commodities instead of stipulating that the parties promise merely to make available such shipments; (2) the parties agree that shipments made under the terms of the agreement shall be carried preferably by vessels of the signatories and in equal proportion; and (3) the agreement is to remain in effect for five years.

Commercial Agreements

The first commercial agreement of this series was reached with Spain on October 30, 1946, establishing a pattern for subsequent agreements with Chile,1/ Switzerland, Bolivia,2/ Czechoslovakia, and France. Although all of these agreements have a number of points in common, they may be divided geographically into two groups, those with Latin American countries and those with others. The agreements with the former (Chile and Bolivia) provide for a limited customs union and for investment of Argentine funds in those countries, but such provisions do not appear in the agreements with the European countries. It is not improbable that Argentina entertains the desire to negotiate commercial treaties with other Latin American countries; indeed, the Foreign Minister of Ecuador has already indicated that such an agreement is contemplated. It also may be presumed that Argentina will try to conclude further agreements with other European countries.

The principal points which are common to all six of the commercial agreements are: (1) a duration of five years (with the exception of certain development provisions of the Chilean and Bolivian agreements which are to run longer); (2) trade provisions are to be carried out by the Argentine Institute for the Promotion of Trade; (3) with the exception of

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1/ See this Review, January 14, 1947.
2/ See this Review, April 22, 1947.

the Swiss agreement, all involve an Argentine loan or credit; (4) means of transport are to be given the most favorable treatment compatible with the laws of signatory countries. Since Switzerland and Czechoslovakia have no direct communication with Argentina, this provision does not appear in their agreements; (5) goods covered by the agreements are to be carried preferably in ships of the respective parties on an equal basis. This does not appear in the Bolivian agreement since communication presumably would be by land, while the agreement with Czechoslovakia provides that shipment shall be made preferably in Argentine vessels; (6) commercial aviation will be encouraged and necessary facilities will be provided on a reciprocal basis; (7) studies are to be made for the purpose of concluding special aviation agreements; (8) each country may require that shipments under the agreement be insured with companies of its nationality when the risk of transport is for the account of that Government or its nationals; (9) the parties agree that measures will be taken to encourage the exchange of motion picture films. This provision does not appear in the agreement with Czechoslovakia; (10) the establishment of branches or agencies of banks or other organizations by one of the parties in the territory of the other will be facilitated by the latter.

The commercial agreements with countries outside Latin America are those with Spain, Switzerland, Czechoslovakia, and France; the provisions of all four agreements are in general quite similar. The French agreement, for example, is divided into eight chapters headed as follows:

1. General Provisions
2. Exportation of Argentine Products to France
3. Exportation of French products to Argentina
4. Financial Provisions and System of Payment
5. Marine and Air Communications
6. Insurance
7. Books, Publications, and Motion Picture Films
8. Final Provisions

The agreements with Czechoslovakia and Switzerland omit chapters seven and four, respectively. The agreement with Spain omits the chapter on insurance but includes a chapter on emigration. Chapter 1 sets forth the purpose of each agreement which is declared to be the strengthening of economic ties and the encouragement of trade on a basis of strict reciprocity, especially with regard to taxes, duties, administrative regulations, etc., and the labeling of goods for origin and quality. The chapter headed Final Provisions provides for facilitating access by Argentina to technical processes and the services of technicians. In the Swiss and Czechoslovakian agreements this provision applies only to processes and the services of technicians related to machinery purchased under the agreement. This chapter also contains the provision for facilitating the establishment of branches or agencies of banks or other official organizations, previously noted as being common to all six agreements.

The remaining agreements of the series are those with the neighboring countries of Chile and Bolivia, although these agreements have not yet been ratified by either of the above countries, and are consequently subject to change. The first four chapters are concerned with the following subjects:

1. Customs Union
2. Financial Provisions
3. Argentine Investments in Chile or Bolivia
4. Loans for Development and Public Works in Chile or Bolivia

The remaining chapters are concerned with provisions which are quite similar to those listed as (5) through (8) above.

The striking similarities, to the point of identity, among the commercial agreements would seem to indicate that the agreements were drafted by Argentina and are presumably expressions of Argentine economic policy. Differences, especially of principle, may be due to the other contracting countries' insistence upon changes of Argentine terms and to Argentina's willingness to compromise in order to assure negotiation of the agreement.

One of the fundamentals of present Argentine trade policy, to be found in numerous public statements by representatives of the Argentine Government and embodied in all of the agreements, is the strong advocacy of bilateralism and strict reciprocity. This, of course, clearly negates the most-favored-nation principle. Even in the "commercial" agreements, trade is based on a list of specified commodities in a specified quantity, and in general it is provided that the Argentine goods purchased are for the internal consumption of the buying country. Importing countries, however, are allowed to purchase elsewhere if prices are lower than those of the Argentine. Such opportunities would be limited in view of Argentina's favorable supply position in many of the desired commodities.

All of these agreements, except that with Switzerland, involve the extension of a rotating credit by Argentina, thus indicating that expansion of Argentine trade with these countries can occur only on the basis of credits. The ability of Argentina to continue to make this type of agreement depends upon a satisfactory solution of the sterling convertibility problem. If a settlement can be reached with the United Kingdom which will permit Argentina to acquire dollars with its sterling holdings, it will be able to extend credit to its trade partners. At present the ability to lend is a limiting factor. It seems likely that, if all the credits at present in force were drawn upon simultaneously to their full extent, Argentina would not be able to meet its commitments.

The table below may give some idea of the importance of the 1,520 million pesos (US$380 million) extended in rotating credits, both for the total export trade of Argentina and for the total import trade of the other contracting countries. The fact that in every case the extended rotating credit was larger than the Argentine exports in 1946 to the respective countries would seem to indicate that Argentina was attempting to assure an increase of trade and not merely the maintenance of the given base level.

While these rotating credits are for the purpose of facilitating the purchase of Argentine products, the long-term loans to be extended to neighboring countries may be viewed as aids to the Argentine economy through the development of a more integrated economic system in that part of the world. As noted above, there is some indication that this policy may be extended to Ecuador, and presumably to other neighboring countries as well.

Relation of Rotating Credit to Trade of Commercial and Financial Agreement Countries
(Absolute figures in millions of U.S. dollars)

	Bolivia	Chile	Czecho-slovakia	France	Spain
1) Argentine rotating credit	12.5	25.0	5.0	150.0	187.5
2) Argentine exports in 1946	9.4	22.6	2.8	105.0	34.3
3) Relation of this trade (Item (2) to total Argentine exports: $1,183.1 million. (In per cent)	0.8	1.9	0.2	8.9	2.9
4) Total imports in 1946	52.2	196.5	204.7	1,965.9	252.5
5) Relation of credit to total imports of respective country. (In per cent)	23.9	12.7	2.4	7.6	74.3

Argentina appears prepared to insist absolutely on the insurance and navigation provisions. The fact, however, that the navigation clause is not mandatory, being qualified by the word "preferably", and that it is usually followed by a provision recognizing that goods need not be delayed nor prices raised due to the implementation of the navigation clause probably indicates a realization that there will be occasions when ships of neither party will be available to transport goods.

One of the important features of the commercial agreements is the provision that all purchases under the terms of these agreements be made through the Argentine Institute for the Promotion of Trade (IAPI), the organization through which Argentina conducts its international commerce. The existence of such a state-trading agency facilitates the negotiation of bilateral contracts through the ability to make specific quantitative commitments, an ability which tends to place private enterprise trading countries at a disadvantage. The Argentine Government has used the Institute largely for two purposes, (1) to handle the export of Argentine products, an arrangement which yields the Government substantial profits, and (2) to control imports. These functions are essential to the fulfillment of the present economic policy; thus, for reasons of both external and internal policy it seems unlikely that any international agreement will be entered into which would jeopardize the effectiveness of this agency.

THE U.K.-SOUTH AFRICA FINANCIAL AGREEMENT

Florence Jaffy

An agreement negotiated October 9, 1947, between the United Kingdom and the Union of South Africa, and dealing with several aspects of financial relations between the two countries, is now awaiting action by the January session of the South African legislature.

The chief provisions of the agreement may be summarized as follows:

1. South Africa is to make a gold loan to the United Kingdom in an amount equivalent to £80 million ($324 million) carrying interest at 1-1/2 per cent, and repayable at the end of three years;

2. South Africa may at any time require repayment of part of the loan in sterling (which it can use to meet trade deficits) if its gold reserves fall below £100 million;

3. South Africa is to sell gold to the Bank of England in an amount equivalent to net payments which South African residents make through the United Kingdom, to countries outside the sterling area;

4. The two governments agree to maintain existing arrangements under which U.K. residents are permitted to make investments in South Africa, but will consult in regard to measures which may be necessary to control capital movements from the United Kingdom that would not serve any useful purpose in South Africa.

5. The United Kingdom undertakes to import from South Africa over the next three years specified commodities of a semi-luxury nature, to a total value of £12 million each year.

This new agreement supersedes a two-year agreement made in 1946. By the earlier arrangements, South Africa undertook to sell not less than £80 million of gold per year during 1946 and 1947 to the United Kingdom, except that South Africa could deduct from this sum gold sold directly to the United States, up to a maximum of £10 million in each year. The United Kingdom, in turn, undertook to cover, against sterling, all South African requirements of foreign currencies, except such dollars as South Africa obtained by direct sales of gold to the United States.

Under the 1946 agreement, the net hard currency receipts of the United Kingdom depended on the relation between the amount of gold sold to it by South Africa and the extent to which it supplied South Africa with foreign currencies--i.e., the extent to which South Africa drew on the British dollar pool.1/ Since the agreement placed only a lower limit on South African gold sales to the United Kingdom, actual gold sales could

1/ That is, it is assumed that the great bulk of South African non-sterling payments are in hard currencies.

be higher than £70 million if the South African overall balance of payments deficit with the sterling area, on current and capital account, exceeded this figure. (South Africa has very little accumulated sterling.) While official figures are not available, the London press stated in October that South Africa had contributed more gold to the United Kingdom than it had drawn out in the form of dollars, and that in fact the net gain by the United Kingdom under the agreement, in 1946 and 1947, will probably amount to between £50 million and £60 million. An examination of the figures for dollar sales of the South African Reserve Bank, gold sales by South Africa in New York and in London, and changes in South African dollar balances, leads to the conclusion that Britain may have gained in reserves a net amount of about £36 million from its transactions with South Africa during the year ending March 31, 1947 alone.

Since South Africa's deficit with the sterling area is a current account deficit, offset in part by a surplus on capital account, it is clear that British net acquisitions of hard currency would have been greater if the movement of capital from the United Kingdom to South Africa had been less. The trade deficit of South Africa with the United Kingdom alone in the year ending March 31, 1947, amounted to £61 million. In view of the fact that trade with the remainder of the sterling area and the inclusion of invisible items would probably increase and not decrease this figure, it may be estimated that the United Kingdom acquired gold in this period for only a little over half of its export surplus to South Africa. The remainder of the surplus, therefore, must have been financed by capital movements from the United Kingdom.

Although the existence of this capital flow, and the fact that it has been especially heavy over the past year is clear, there is uncertainty as to its amount and the extent to which the capital movement is for productive investment. New investment, whether British or local, is undoubtedly necessary to South Africa, for purposes of equipping and maintaining its industry (notably gold mining); and while the necessary purchases would probably be made in the United Kingdom regardless of the source of the financing, the British naturally wish to maintain their investment position in South Africa. On the other hand, capital flows which are not of this useful type serve merely to enable more British exports to South Africa to be paid for in sterling instead of gold, or enable South Africa to obtain more hard currencies from the United Kingdom. The total amount of capital movement has been given by the Chancellor of the Exchequer for the year ending June 30, 1947, as £35 million. It is understood that the British consider most of this to represent productive investment. However, the London Economist put the amount at close to £100 million for the 12 months ending September 1947, calling the bulk of it "refugee capital." The South African Reserve Bank estimated the net inflow over the year ending March 31, 1947, to be "not much more than £20 million" (although pointing out that the bulk of this occurred in the first quarter of 1947) and stated, in a commentary on the new financial agreement that "a considerable influx of 'hot money' from the United Kingdom" had taken place, particularly since the middle of 1947 and that "the bulk of it lies on deposit with the banks."

In the light of these facts, the changed provisions of the new financial agreement are significant. The 1946 agreement placed no limitation on South Africa's right to acquire dollars from the United Kingdom against sterling, irrespective of the origin or the character of the sterling balances. Under the new plan, the Union must sell at least enough gold to the United Kingdom to cover its net payments through London to non-sterling countries, regardless of the increase in South African sterling balances caused by capital inflow. However, the new agreement continues to permit the use of sterling balances (irrespective of their source) by South Africa to meet its deficit with other sterling area countries.

The agreement does, however, make provision for the possible introduction of control over undesirable capital movements, i.e., those which do not serve any useful economic purpose in the Union. It has been suggested that such measures might include blocking of idle non-resident deposits in South Africa or repatriation of such deposits as the British or South African authorities may order to be repatriated. However, the South African Reserve Bank calls these "drastic measures which the Union authorities will be reluctant to enforce unless the situation reaches unmanageable proportions."

The remaining provisions of the agreement are the loan itself, and the import commitment. The gold loan itself will come out of South African gold reserves, which were £197.6 million ($804.4 million) at the end of October. Since South Africa's current deficit with the sterling area will continue to be financed through sales of gold from new production, the loan will constitute a temporary addition to British gold reserves which will offset in large part U.K. gold sales to the United States in the latter part of 1947.

The provision regarding imports of certain non-essential goods represents an increase of 20-25 per cent over import of the same items during 1946. Since the United Kingdom has been restricting luxury imports from hard currency countries, it might consider their purchase from South Africa unjustifiable in the absence of a consideration such as this loan provides.

U.S. FOREIGN TRADE, FIRST NINE MONTHS OF 1947

Gretchen Fowler

U.S. exports for the third quarter of 1947 were below the level of the two previous quarters, although at a value of $3,393 million they were nearly 30 per cent above the third quarter of 1946. The monthly value of exports reached a postwar high of $1,421 million in May 1947, declining almost every month thereafter to $1,101 million in September. For the first nine months of the year, however, exports rose 54 per cent in value over the same period of 1946, totaling $10,948 million as compared with $7,121 million. Price movements accounted for a substantial share of the gain. According to the Department of Commerce index of unit values, export prices in September 1947 were about 25 per cent higher than in September 1946. The increase in the volume of exports during the nine-month period appears to have been around one-third.

The value of imports also declined during the summer months, but rose again in September. Normal seasonal influences may be expected to hold imports at least at the September level ($481 million) for the remainder of the year. Although the value of imports into the United States rose 19 per cent during the first nine months of 1947 as compared with the same period of 1946, the price index rose about 28 per cent; the volume of imports actually declined. Imports during the third quarter of 1947 were the lowest for any quarter since the same period of 1946. Data on imports and exports by quarters are given in the attached Table IV.

The export balance on merchandise account during the first nine months of 1947 totaled $6,754 million, as compared with $3,604 million for the same period in 1946. As shown in the following table, 48 per cent of this surplus resulted from trade with the European Recovery Plan nations.

Table I
U.S. Trade - January through September

	Total U.S. trade	Trade with Europe	Trade with ERP nations[a/]	Trade with ERP nations as per cent of: Total U.S. trade	Trade with Europe
	(In millions of dollars)				
1946:					
Exports	7,120.6	3,178.2	2,448.5	34.4	77.0
Imports	3,516.3	566.8	481.6	13.7	85.0
Excess of exports	3,604.3	2,611.4	1,966.9	54.6	75.3
1947:					
Exports	10,948.4	4,029.3	3,276.0	34.0	92.5
Imports	4,194.3	595.3	498.7	11.9	83.8
Excess of exports	6,754.1	3,434.0	3,227.3	47.8	94.0

a/ Includes U.S. trade with Germany.

Shifts in the geographic distribution of U.S. trade in the January-September period of 1947, compared with the same months of 1946, can be seen in the table below.

Table II
Geographic Distribution of U.S. Trade - Jan.-Sept. 1947

	Value Indexes (Jan.-Sept. 1946 = 100) Exports	Imports	Increase (+) or decrease (-) from Jan.-Sept. 1946 (Millions of dollars) Exports	Imports
North America	163	134	+ 1,096	+ 407
South America	230	111	+ 1,008	+ 86
Europe	127	105	+ 851	+ 29
Asia	150	129	+ 483	+ 175
Australia	270	90	+ 147	- 14
Africa	165	99	+ 243	- 3
Total	154	119	+ 3,828	+ 678

U. S. exports to all areas showed substantial gains. In South America, the principal increases were to Argentina ($393 million), Brazil ($253 million), and Venezuela ($170 million). These three countries at the end of the war held large dollar balances, and all three are seeking to industrialize their economies. In North America, Canada received an increase of $570 million of U.S. exports for the period, Cuba $162 million, and Mexico $118 million. Cuba, nevertheless, enjoyed a favorable trade position vis-a-vis the United States for the first nine months of 1947.

The nations of Western Europe received greatly increased imports from the United States, but these gains were partially offset by decreases for the U.S.S.R. ($203 million), and most of the other eastern European nations. These lower exports were caused by the virtual cessation of UNRRA and lend-lease aid. Russia, in the third quarter of 1947, had a favorable trade balance with the United States. In Asia, increased exports to India and the Republic of the Philippines were partially offset by decreased shipments to Japan and China. Here again, the cessation of UNRRA and other relief activities has probably caused the decline in exports. Australia took $112 million more in exports from the United States and the Union of South Africa $149 million more in the first nine months of 1947 than during the first three quarters of 1946.

U. S. imports increased from Canada ($159 million), Cuba ($159 million), British Malaya ($234 million), and the Philippines ($94 million). Heavy imports of newsprint, sugar, rubber, and copra from the respective countries accounted for the bulk of the expansion. Notable decreases were registered for imports from Japan ($36 million), French Indo-China ($28 million), Afghanistan ($27 million), and the Union of South Africa ($51 million). Factors partly responsible for this development were the fall in raw silk imports, political disturbances, and the lower shipments of diamonds.

Trade by commodity classes during the first nine months of 1947 departed somewhat from the pattern for 1946. Greatly increased exports of semi-finished and finished manufactures accounted for most of the gain in total exports.

Table III
Commodity Composition of U.S. Trade
January through September 1947

	Value Indexes (Jan.-Sept. 1946 = 100)		Increase (+) or decrease (-) from Jan.-Sept. 1946 (Millions of dollars)	
	Exports	Imports	Exports	Imports
Crude Materials	117	105	+ 175	+ 65
Crude Foodstuffs	125	122	+ 125	+ 130
Manufactured Foodstuffs	94	131	- 70	+ 116
Semimanufactures	200	138	+ 656	+ 248
Finished Manufactures	185	123	+ 3,001	+ 132
Total	156	120	+ 3,886	+ 690

A sharp decline in the value of many individual components of the manufactured food exports category is partially concealed by the classification used in the preceding table; large decreases in exports of meat products, dairy products, canned vegetables, and dried eggs were almost entirely compensated for by a rise of $229 million in exports of wheat flour. Moreover, according to the Department of Commerce cumulative index of unit values for the first nine months of 1947, prices in this category rose 27 per cent over the same period of 1946. On the basis of these price changes, the volume of manufactured food exports declined 25 per cent during the first nine months of 1947 from the similar period of 1946.

Price and volume changes as indicated by the Department of Commerce indexes for January-September 1947 from the same period in 1946 for the other economic classes of exports were as follows:

	Unit values	Volume
	(Per cent)	
Crude materials	+ 25	- 6
Crude foodstuffs	+ 10	+ 13
Semimanufactures	+ 29	+ 55
Finished manufactures	+ 19	+ 56

Changes in exports of individual commodities were sharp compared with 1946 levels. The great increase in coal kept values high in the crude materials category even though there was a tremendous third-quarter decline in exports of unmanufactured cotton. Greatly increased shipments of corn more than compensated in the crude foodstuffs category for the drop in wheat exports. Semimanufactures showed gains in all commodities, and finished manufactures, with the exception of those of wool and synthetic rubber, were exported at a high rate.

On the basis of price changes in economic classes of imports, volumes during the first nine months of 1947 were generally below the levels of the same period of 1946:

	Unit values	Volume
	(Per cent)	
Crude materials	+ 10	- 5
Crude foodstuffs	+ 42	- 14
Manufactured foodstuffs	+ 24	+ 6
Semimanufactures	+ 30	+ 6
Finished manufactures	+ 28	- 5

Decreases during the third quarter of 1947 from that period of 1946 in the values of individual commodities in the crude materials category have emphasized the shifts that first become evident earlier in the year. Imports of furs, raw silk, unmanufactured wool, and diamonds were still declining, and shipments of crude rubber and oilseeds during the third quarter were well below levels established during the first two quarters of 1947. In the crude foodstuffs class, imports of cocoa and coffee continued to show value increases during the third quarter of 1947, but prices during the first nine months of this year had increased markedly from the level during the first nine months of 1946 (47 per cent for coffee and 163 per cent for cocoa) and masked the volume decreases of 17 per cent and 2 per cent respectively for the nine-month periods. Cane sugar shipments kept value and volume in the manufactured foods class at a high level. In semimanufactures the increased imports of wood pulp, expressed oils, and copper more than offset the drop in shipments of diamonds, cut but not set. During the third quarter of 1947, imports of tin, copper, and wood pulp were accelerated. Value increases of burlap and newsprint imports during the third quarter of 1947 and for the nine months of 1947 made these commodities the key items in the finished manufactures category.

Table IV
U. S. Foreign Trade - Selected Countries 1/
(Millions of dollars)

Continent and Country	4th quarter 1946	1st quarter 1947	2nd quarter 1947	3rd quarter 1947	Jan.-Sept. 1947
Total Exports	2,621.1	3,593.4	3,962.0	3,393.0	10,948.4
North America	809.6	912.2	1,018.1	899.5	2,829.8
Canada	462.6	473.3	572.1	503.6	1,549.0
Mexico	159.5	163.9	160.8	138.8	463.5
Cuba	87.6	113.1	131.9	101.0	346.0
South America	378.7	571.4	648.3	561.4	1,781.1
Venezuela	66.6	94.2	120.6	100.2	315.0
Brazil	119.0	174.5	179.7	135.7	489.9
Argentina	79.2	134.6	178.9	193.1	506.6
Europe	919.9	1,375.7	1,444.1	1,209.5	4,029.3
ERP countries 2/	829.9	1,263.8	1,317.4	1,144.8	3,726.0
Other Europe	104.3	132.9	161.9	85.7	380.5
Asia	367.5	487.8	547.3	424.0	1,459.1
India and dependencies	57.9	96.0	136.1	81.8	313.9
Republic of the Philippines	92.4	126.0	94.4	98.7	319.1
China	109.5	113.0	123.1	71.1	307.2
Australia and Oceania	30.1	63.7	73.9	96.5	234.1
Africa	115.7	182.7	230.3	201.9	614.9
Union of South Africa	64.8	97.0	112.9	101.4	311.3
Total Imports	1,411.3	1,411.8	1,451.5	1,331.0	4,194.3
North America	462.0	495.7	567.7	528.4	1,591.8
Canada	261.9	243.4	266.9	269.0	779.3
Cuba	89.4	104.5	156.6	131.1	392.2
South America	303.5	309.2	290.7	276.5	876.4
Brazil	105.1	118.4	86.3	106.1	310.8
Europe	229.2	186.0	196.7	212.6	595.3
ERP countries 2/	197.3	173.1	165.5	160.1	498.7
Other Europe	50.3	36.4	45.4	56.0	137.8
Asia	296.0	305.9	268.8	205.2	779.9
India and dependencies	61.8	69.5	55.4	67.8	192.7
British Malaya	54.3	94.5	85.1	54.6	234.2
Republic of the Philippines	20.7	37.7	48.0	27.6	113.3
Australia and Oceania	44.7	45.7	53.5	25.2	124.4
Africa	75.7	69.4	74.1	83.0	226.5

1/ Selected on the basis of $300 million for 9 months' trade in Exports, $200 million for 9 months' trade in Imports, except for Europe, where subtotals were calculated for the 16 ERP nations, including Germany.

2/ Includes trade with Germany; also includes non-European Iceland and Turkey.