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RECENT MONETARY DEVELOPMENTS IN SWEDEN

Paul Gekker

Recent monetary developments in Sweden are interesting for two reasons. First, the revived active use of central banking credit control instruments - the discount rate, open market operations and commercial bank reserve requirements - has been characterized as a "return to monetary policy." 1/ Secondly, a number of supplementary measures which have recently been considered or adopted in the anti-inflationary program reflect the traditional Swedish preoccupation with counter-cyclical techniques.

The transition from a condition of relative monetary stability in mid-1949 to the re-emergence during 1950 of predominantly inflationary tendencies - initially a post-devaluation boom aggravated by the repercussions of Korea - has brought with it a definite change in the direction of Swedish economic policy. Since the end of 1949, and particularly from March 1950 on, economic developments have been characteristic of a typical peacetime boom. The level of industrial production in 1950 stood at 55 per cent above 1938 and rose by approximately 4 per cent over 1949. In contrast to other European countries, export prices rose more than import prices. The resulting expansion of export earnings in turn made possible a considerable increase in the volume of imports, especially of consumers' goods, which brought about a temporary saturation of demand in many lines. The accompanying decline in the domestic consumer goods industry, however, was more than offset by increased production of capital goods. Finally, stock market activity has been extremely lively, with share quotations exhibiting an almost uninterrupted rise.

On the other hand, until recently the internal price repercussions of devaluation were cushioned by fresh budget subsidies. At the same time a certain stabilization of incomes was assured by the agreement maintaining wage ceilings, although some "unofficial" upward movement of wages had continued. By the end of 1950, however, most price subsidies were abandoned, and the wage agreement has expired and is being replaced by free contracts. Added to these potential inflationary pressures are those arising from increased defense expenditures in the coming year.

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1/ Lars-Erik Thunholm, "Sweden's Steps to Check Inflation," in The Banker, September 1950, pp. 163-168; and "Interest Rates in Europe," in The Economist, December 9, 1950, p. 1041.

## Monetary developments

Prices and wages - Changes in the principal price indices in the year since the devaluation of September 1949 are given in Table 1.

Table 1

Sweden - Price Movements, 1949-50

| Index 1/ | Percentage change in index in period: | | | | |
|---|---|---|---|---|---|
| | Aug. 1949 Dec. 1949 | Dec. 1949 June 1950 | June 1950 Sept. 1950 | Sept. 1950 Nov. 1950 | Aug. 1949 Nov. 1950 |
| Wholesale prices | +2.3 | +1.8 | +2.2 | +6.6 | +13.6 |
| Cost-of-living | 2/ | +0.6 | +0.6 | +1.8 3/ | +3.0 4/ |
| Import prices | +21.3 | +0.3 | +10.5 | +5.2 | +41.5 |
| Export prices | +10.2 | +13.1 | +14.6 | +3.9 | +48.3 |

1/ 1935=100 for all series.
2/ Unchanged for period June-December 1949; index computed quarterly.
3/ September to December 1950.
4/ June 1949 to December 1950.

Source: Kommersiella Meddelanden, November 1950, and unpublished reports.

For the entire period, stability of the cost-of-living index, as well as the moderate degree of the rise in wholesale prices from August 1949 to September 1950, are due to subsidies imposed at the time of devaluation. Following the initial increase in import prices in the quarter following devaluation, the index was virtually stable during the first half of 1950. The uninterrupted rise in export prices from devaluation to June 1950 was due largely to price increases on products of the forestry and engineering industries. In the third quarter of 1950, the renewed increase in import prices mirrors the rise in raw material markets following the outbreak in Korea. The continued rise in export prices during this period is the result almost exclusively of price increases for pulp in response to the continued high level of demand in the United States and other markets.

Recent reports indicate that the inflationary development received a marked impetus during October and November 1950, when a growing awareness of the trend toward higher prices was reflected in some hoarding activity. The volume of retail sales in October and November was considerably above corresponding months in 1949, with buying for the Christmas season at record levels. The strength of consumer buying after Christmas, moreover, indicated the persistence of hoarding.

In October and November wholesale prices increased by 6.6 per cent, matching the rise in the year after devaluation. The increase in wholesale prices during 1950 is the largest for any postwar year. In the same two months import and export prices continued upward, rising by 5.2 and 3.9 per cent, respectively. From devaluation to November 1950, therefore, wholesale prices have risen by 13.6 per cent, import prices by 41.5 per cent and export prices by 48.3 per cent. In December 1950, the cost-of-living index rose by 1.8 per cent over the previous quarter, but the index does not yet reflect numerous recent price increases.

Termination of the "wage-freeze", which has been in effect for three years, is being followed by negotiations for new agreements. In all, agreements affecting about 300,000 workers have already been signed, raising wages in the range of 8 to 15 per cent. In addition, 250,000 Government and municipal employees have received "stopgap" increases of 8 per cent in the cost-of-living supplement to basic salaries pending conclusion of a new salary agreement. It is generally expected that these new contracts, and others likely to come, will raise the 1951 wage level about 10-15 per cent above 1950.

<u>Credit expansion</u> - The principal feature of monetary developments in 1950 was the increase in lending activities of the commercial banks, reflecting the combination of a higher level of production and building activity, and record values in foreign trade.

The rise in bank credits shown in Table 2, amounting to 945 million kronor in the first ten months of 1950, is the largest increase for the same period since 1947, when the peak of post-war investment and credit expansion was reached.

Table 2

Sweden - Increase in Commercial Bank Loans and Advances 1/
(In millions of kronor)

| Year | 1st Quarter | 2nd Quarter | 3rd Quarter | October | Total January-October |
|---|---|---|---|---|---|
| 1949 | +3 | -30 | +207 | -13 | +167 |
| 1950 | +255 | +208 | +478 | +4 | +945 |

1/ Exclusive of unutilized credits.

Source: Uppgifter om Bankerna.

In the first half of 1950 the increase in loans and advances amounted to 463 million kronor whereas a slight decline occurred during the same period in 1949. For the third quarter of 1950 the increase in loans more than doubled the rise in credits for the corresponding months in 1949, and also exceeded the combined increase from January to June 1950.

Table 3 indicates that the expansion in lending is concentrated in four categories of loans. The increase in real estate credit is due partly to a less restrictive policy in granting building licenses. In part it also reflects a shift in this lending activity from savings to commercial banks, a development associated with a tighter liquidity situation in the savings banks where a declining trend in deposit growth has recently been evident. There has also been some delay in the release of funds by the Royal Housing Board, retarding the replacement of commercial bank short-term loans by long-term loans from other lending institutions which normally follows the completion of building ventures. The rise in advances against shipping documents is attributable to the very favorable foreign trade development, while increased lending against bills of exchange is the counterpart of a higher level of production and trade. Finally, the extension of credit against promissory notes represents chiefly increased borrowing by municipalities against notes which are repayed upon later receipt of income tax collections transferred to them by the central Government.

Table 3

Sweden - Increase in Commercial Bank Loans, by Category of Loan
(In millions of kroner, (-) signifies decrease)

| Type of Loan | January-October 1949 | January-October 1950 |
| --- | --- | --- |
| Real Estate Mortgages | -8 | +322 |
| Stocks | -36 | -3 |
| Bonds | +13 | +28 |
| Merchandise | +22 | +20 |
| Promissory notes | +120 | +226 |
| Documentary credits | -65 | +105 |
| Discounted bills 1/ | +119 | +211 |
| Total credits 2/ | +166 | +909 |

1/ Domestic bills only.
2/ Includes unutilized credits; breakdown of unutilized credits by type of loan not available.

Source: Uppgifter om Bankerna.

As in an earlier period (1946-48), the banks sold Treasury bills and Government bonds to finance the recent expansion of credit. During the first half of 1950, however, the made possible on the basis of the influx of foreign exchange receipts in the previous half year still permitted some net increase in holdings of Treasury bills and bonds, amounting to 169 million kronor. During the third quarter of 1950, on the other hand, the reduction of bank holdings of both bills and bonds totalled 291 million kronor.

Reserve requirements - Increasing concern over the inflationary implications of the credit expansion during the first half of 1950 led the Riksbank on July 22nd to petition for authority to impose higher reserve requirements. Under the basic commercial bank legislation of 1911, reserve requirements were set at 25 per cent of demand liabilities, to consist of readily realisable assets which in practice have come to comprise cash, cash collection items, central bank deposits, demand deposits in Swedish and foreign banks, foreign currency and Treasury bills and Swedish Government bonds. In 1937 the Swedish Parliament passed enabling legislation - which with some amendments has been continued - permitting the Riksbank to request authority to impose reserve requirements to a maximum of 25 per cent of a wider grouping of liabilities than under the older law.

The decree which followed the Riksbank's proposals classed the commercial banks into three groups according to the size of their capital funds for the determination of reserve requirements. Banks with funds over 50 million kronor, those with funds between 10 and 50 million kronor, and banks with less than 10 million kronor in capital funds were required to hold a reserve amounting to 10, 8 and 6 per cent, respectively, of total liabilities with the sole exception of savings deposits and the banks' liabilities on their own secured endorsements. 1/ Of the total reserve, 40 per cent was to consist of cash and sight deposits in the Riksbank, and of the 40 per cent portion 25 per cent had to be kept on deposit in the Riksbank.

The new reserve requirements became effective on October 1st. At the time they were proposed the condition of most banks would have permitted relatively easy compliance with the requirements, although a few of the smaller banks were

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1/ The new, smaller reserve percentages exceed the older provision for a 25 per cent reserve because of the more comprehensive grouping of liabilities against which reserves must now be held. The older reserve stipulation was applied against sight deposits (and granted but unutilized credits) only, whereas the new reserve must be held against total liabilities with the sole exception of savings deposits and guarantees. Reserves are now applied against both sight and term deposits, and the latter comprise over 60 per cent of total deposits in Swedish commercial banks. As a result, the banks can less easily evade the reserve requirements than under the older law, e.g. when the reserve applied to sight deposits only, it was possible to avoid the reserve adjustment required for additional deposits resulting from an expansion of credit by encouraging a shift to some extent to term deposit accounts.

than in a condition of reserve deficiency. The effective date, however, permitted the banks some leeway in adjusting their reserve positions. In addition, their entrance into effect coincided with the normally liquid condition of the banks because of heavy seasonal foreign exchange receipts. The requirements were no doubt timed with the object of making the transition easier, thereby avoiding pressure on the level of Government bond prices should the banks be obliged to sell securities to adjust to the new requirements.

Open market operations - Two days after submitting its proposals for higher reserve requirements, the Riksbank took the related and more significant step of withdrawing from the Government bond market. This move was widely interpreted as signifying abandonment of the postwar policy of supporting the 3 per cent interest level on Government bonds, disagreement over which had led, in December 1948, to resignation from office of Mr. Ivar Rooth, then Governor of the Riksbank.1/ Throughout 1946-48 the Bank had made large purchases of bonds at a time when the commercial banks were replacing these earning assets by more profitable investments in loans. Mr. Rooth's resignation at the end of 1948, however, coincided with the tapering off of the postwar boom, so that the tendency for banks to shift from securities into loans was arrested. With the passing of the peak in credit expansion, commercial banks again placed their available funds in Government securities, so that pressure on the bond price eased and intervention by the central bank took the opposite course in 1949. The resurgence of an active demand for credit in 1950, especially in the post-Korean period, led the banks to liquidate a considerable portion of their security holdings.

The Riksbank was evidently permitted to allow these bank offerings to exert a downward influence on the price, thus providing for an increase in yield from an average of 3.03 per cent in January-June 1950 to 3.32 per cent in December.

1/ The controversy over interest rate policy has been reviewed by Caroline Lichtenberg in this Review, April 26, 1949.

In conjunction with the desire to permit some upward adjustment in the interest rate structure, it is likely that the action was also taken with a view to reinforcing the higher cash reserve requirements, whose restrictive effect could easily have been nullified if the commercial banks had been permitted to sell large amounts of their holdings of Government bonds in an assured market.

Voluntary agreement to restrict credit - On August 28th, following discussions initiated by the Riksbank, the private lending institutions accepted an agreement for the voluntary restriction of credit. The Riksbank announced that agreement had been reached with regard both to the necessity of preventing the further expansion of credit, and to the necessity of supplementing the admittedly insufficient higher reserve requirements by other measures, notably the cooperation of lending institutions. In implementation of these objectives the agreement specified five general rules intended as guides to lending policy:

(1) In the granting of loans, preference was to be given to activities which contributed either to the maintenance of exports or to the reduction in import requirements of goods considered essential to the economy. The greatest possible restriction was to be observed in granting credits for the financing of new or expanded production of relatively unessential commodities.

(2) The financing of direct or indirect consumer credit was to be restricted, these credits being considered as contributing to the mobilization of purchasing power for other than productive purposes. During 1950, a considerable portion of consumer credits represented financing of a spectacular volume of automobile imports.

(3) Credits for speculative uses were not to be granted; specifically mentioned were credits which might make possible a postponement of collections from abroad, and credits in an amount or number beyond the borrower's customary scope of activity or normal volume of operations.

(4) Stricter rules with regard to collateral and amortization should be applied; in particular, inflated property values in the current favorable real estate market were not to be used as a basis for the extension of loans.

(5) All prospective flotations of new security issues were to be reviewed in advance by the Riksbank, with a view to agreement regarding the urgency, timing and terms of the issue.

The new rules were essentially similar to those adopted in the fall of 1947, except that they had then constituted an isolated measure, whereas the 1950 agreement supplemented the other anti-inflationary measures already in effect.

Interest rate policy

Following the Riksbank's withdrawal from the bond market late in July, the prices of long-term bonds underwent a slight decline, resulting in a rise in the effective rate of interest to approximately 3 1/3 per cent. Initially there was no increase in selling transactions due to a measure of self-restraint reportedly organized by one of the larger Swedish banks.1/ In addition, the moderate market response indicated caution pending more definite knowledge of the Government's long-term borrowing plans. On October 5th the Riksbank adjusted certain of its interest rates, raising the rate on advances against gilt-edged bonds from $2\frac{1}{2}$ to 3 per cent, and abolishing the $\frac{1}{2}$ per cent rebate accorded commercial banks and certain agricultural institutions on rediscounted bills.

The rise in yields, which followed the abandonment of open market purchases, was actually rather small in view of the noticeable shortage of investment capital. The

1/ It is interesting to recall a technique used in Sweden on a previous occasion. In May 1948, a mild selling panic induced by apprehension of a rise in interest rates following a Riksbank memorandum calling attention to inflationary trends was met by large-scale purchases by the central bank. Subsequently, however, the Government secured agreement by the Swedish life insurance companies to maintain their bond holdings without reduction during a period of six months. Although two companies made certain reservations in principle, and cooperation of the savings banks could not be obtained, the agreement worked satisfactorily. It is a good example of what can be accomplished by voluntary agreement in small countries with a closely-knit financial structure.

current dearth of long-term investment funds is attributable to a decline in personal savings, resulting in a tightened liquidity situation in the savings banks and insurance companies, which constitute virtually the entire market for long-term securities in Sweden.

On November 15th the Government opened subscription for a $3\frac{1}{2}$ per cent, 15-year loan at par, the first long-term financing venture since the end of 1946. No limit was set on the amount, but in the ten days during which subscription was open, 203 million kronor was taken up. Most of the loan, which followed a smaller long-term issue floated by the city of Stockholm, was taken by insurance companies, which apparently pledged their entire expected income for the first quarter of 1951.

Effective December 1, the Riksbank announced an increase of from $2\frac{1}{2}$ to 3 per cent in the official discount rate, the first such change since February 1945, and adjusted most of its loan rates upward by one-half per cent, and the loan rate against Government bonds by $\frac{1}{2}$ per cent. These increases were matched by upward adjustments of deposit and loan rates by the commercial banks and some savings institutions.

In mid-December the Swedish Riksbank reportedly resumed open market purchases, apparently at the insistence of the Government. The action is said to be related to the prospective borrowing needs of the Government, estimated at 700-800 million kronor for the first half of 1951.

Fiscal measures to counteract inflation

In addition to the renewed use of monetary policy in the traditional sense, the authorities have considered two measures which recall the familiar Swedish preoccupation with counter-cyclical techniques.

Export duties - The Swedish Government became concerned at the inflationary implications of marked increases in pulp and paper export prices in September 1950. Following negotiations with the industry, agreement on the imposition of price-equalization fees on exports of timber products was announed on November 5th. These duties can be considered a limited alternative to an appreciation of the krona, which has been rumored in recent months. The proceeds will be sterilized and repayment effected over a five-year period beginning in 1958, at the rate of 20 per cent annually. Of the **total** proceeds, 70 per cent will be repaid to the industry; of the remainder, one-third will be made available for private forestry undertakings and two-thirds to social funds for employees of the timber industry. 1/

The taxes are based on prices for delivery to the United Kingdom, and vary with different grades of pulp and paper, the prices of which were advanced on the average by 25 per cent for the fourth quarter of 1950. It is estimated that the tax absorbs two-thirds of the increase in price.

Investment tax - In 1938 the Swedish Government reformed the regulations governing tax deductions permitted for depreciation and obsolescence. The change introduced a system of "free depreciation" whereby corporations could claim tax exemptions for the portion of gross income devoted to the expansion and modernization of capital equipment on a more liberal basis than had previously been the case. In accordance with the provisions for accelerated depreciation, most industries were encouraged to devote larger than normal proportions of their profits toward expansion and rationalization. While the original intention had been to discourage a reduction of investment, however, the effect in the postwar period has undoubtedly been to accentuate inflationary pressures.

The Swedish Government has proposed a tax on investments financed under the privileges of the free-depreciation provisions. Alternatively, temporary sterilization of some portion of business earnings has been suggested. Although

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1/ These export duties revive the system which was in effect earlier in the postwar period. Similar price-equalization fees were imposed in April 1947, concurrently with the removal of price control in Sweden. They were introduced with the aim of counteracting the direct inflationary impact of rising world market prices on the domestic market. The system was discontinued in September 1948 when resistance to high prices for Swedish pulp led to a considerable decline in sales, especially in the United States market. Provisions for sterilization of the proceeds of these duties as well as the terms of repayment, varied somewhat from the ones now in effect.

the investment tax has been widely criticized, largely on the grounds of its contradiction with the objectives of the earlier legislation, the most recent proposal is still a tax of 10 per cent of the value of increases in inventories and investments in new machinery.

## Summary

In 1950 considerable inflationary pressure was generated by the business boom, the favorable development of export incomes, and other reactions to the Korean war. To meet this situation the Swedish Government early adopted an interesting counter-inflationary program which in a number of particulars involved a break with previous postwar economic policy. The preoccupation of the monetary authorities was to prevent any addition to inflationary pressures which would follow from an expansion of bank credit.

This policy could not be expected to stop entirely the expansionary development. In October and November there was some slowing down of the rate of increase in loans, which could be regarded as the initial effect of the measures adopted. At the present time there appears to be some uncertaintly regarding future economic and monetary policy. The prospect that inflationary tendencies will be intensified, especially as a result of additional defense expenditures, suggests that there is room for a strengthening of the type of program thus far adopted.

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PRICE DEVELOPMENTS IN INDONESIA

A. B. Hersey and
Harrison Parker

The Republic of Indonesia became an independent nation at the end of 1949 after four years of intermittent hostilities between its own forces and those of the Netherlands. This unrest had hampered reconstruction and trade. The already inflationary situation inherited from the Japanese occupation was aggravated by further currency expansion to finance military operations.1/ The stabilization of the administration in 1950 permitted the reconstruction of communications and trade in many areas previously cut off from each other, and enabled the government at last to carry out the greatly needed monetary and exchange reforms of March 1950. These actions, together with the strong external demand for Indonesia's exports, have resulted in a better structure of prices within Indonesia, which for the first time in the postwar period encourages exports and enables the maintenance of equilibrium or a surplus in the balance of payments without severe direct restrictions on imports.

The available indexes of both wholesale and retail prices in Indonesia seem to show that no general price inflation occurred in Indonesia in 1948 and the first half of 1949, although the price level differed markedly in various localities and showed some seasonal variations. Retail prices of domestic foodstuffs varied from nine to fifteen times prewar (1938), depending on the locality.

As a result of the devaluation of the Indonesian guilder (now the rupiah) from 37.7 U. S. cents to 26.3 U. S. cents in September 1949, the monetary reform and introduction of the certificate rate exchange system in March 1950, and the subsequent rise in world market prices of Indonesia's chief exports, there were sharp changes in prices in the latter part of 1949 and 1950.

From mid-1949 into the second quarter of 1950 prices of domestically consumed products rose substantially, particularly prices of imported goods, of other products more or less competitive with imports, and of those domestic consumption articles that are potentially exportable. This rise was related, of course, not only to the monetary inflation associated with the government's fiscal deficit, but also to the devaluation in September 1949 and the introduction in March 1950 of the multiple rate system, which taken together made import costs (at official rates) 4.3 times as expensive as before devaluation. In the third quarter of 1950, however, prices dropped sharply because of the relaxation of import restrictions, the accumulation of inventories and the reduction of profit margins on imported goods. Retail prices of food in major cities in Java remained about 15 per cent higher than a year before. At these levels, food prices in various localities in Java were thirteen to fourteen times the 1938 levels.

1/ See this Review, January 25, 1949, Postwar Internal Financial Situation in Indonesia.

Rupiah prices of export commodities other than rubber in June 1949 were only 3-1/2 to 5-1/2 times prewar (1938). Rubber was only double its prewar local price at that time in the legal market, but black market prices for rubber smuggled out of the country were considerably higher. From June 1949 to March 1950 the increases of export prices ranged from 5 per cent for tin to 85 per cent for copra, with rubber showing a rise of about 50 per cent. From March to September, rupiah export prices of tin, tea and kapok doubled, largely as the result of the new exchange rate system; the price of copra nearly tripled in this period, while the rubber price rose nearly five-fold despite an increase in the export duty. After this rise the relationship to prewar levels of rubber and kapok prices (up 14 to 15-fold) was comparable to the relationship for domestic retail food prices. Tin was up only 7 times from prewar, but copra was at 29 times its 1938 price.

To summarize, in 1950 the terms of trade for Indonesian export producers (internal prices of export goods versus those of imported goods) moved sharply in a direction to restore prewar relationships, but the general price level at the same time showed a definite increase over 1948 and 1949 levels even though the increase in the supply of imported necessities did result in declining prices of imports and domestic products in the third quarter. There still remained a clear danger that all prices might move upward again as a result of inflationary financing of the government's continuing fiscal deficits.

Weighted Index Numbers of Retail Prices of 19 Foodstuffs
on the Free Market
(July 1938 = 100)

| | | Djakarta (Java) | Surabaya (Java) | Medan (Sumatra) | Mocassar (Celebes) |
|---|---|---|---|---|---|
| 1948 | March | 1391 | 1166 | 1616 | 1308 |
| | June | 1115 | 906 | 1304 | 1129 |
| | September | 1032 | 981 | 1376 | 1061 |
| | December | 1531 | 1498 | 1448 | 1175 |
| 1949 | March | 1318 | 1014 | 1342 | 1150 |
| | June | 1142 | 877 | 1420 | 1007 |
| | September | 1210 | 1150 | 1377 | 1083 |
| | December | 1313 | 1316 | 1391 | 992 |
| 1950 | March | 1410 | 1222 | 1563 | 1236 |
| | June | 1542 | 1379 | 2214 | 1685 |
| | September | 1414 | 1284 | 1865 | 1537 |

Index Numbers of Retail Prices in Free Market, Djakarta
(July 1938 = 100)

| | Domestic Goods | | | | Imported Goods | | | |
|---|---|---|---|---|---|---|---|---|
| | Rice | Coconut oil | White sugar | Cigarettes | Textiles 1/ | Wheat flour | Condensed milk | Razor blades |
| 1948 March | 1142 | 1389 | 2550 | 970 | 4566 | 1913 | 879 | 1065 |
| June | 663 | 1367 | 1450 | 1130 | 2354 | 1653 | 758 | 1002 |
| September | 742 | 1406 | 1767 | 1000 | 2490 | 1740 | 694 | 1024 |
| December | 1959 | 1311 | 1825 | 1000 | 2325 | 1827 | 705 | 1011 |
| 1949 March | 1593 | 1111 | 1508 | 1120 | 2562 | 1740 | 691 | 998 |
| June | 1085 | 1006 | 1175 | 1240 | 3240 | 1847 | 584 | 957 |
| September | 1075 | 1089 | 1933 | 1730 | 4970 | 2120 | 673 | 998 |
| December | 1317 | 1111 | 2825 | 1490 | 4701 | 2213 | 803 | 994 |
| 1950 March | 1402 | 1667 | 2850 | 2210 | 4769 | 2277 | 989 | 974 |
| June | 1073 | 2222 | 3275 | 3190 | 5811 | 2833 | 1702 | 1127 |
| September | 1073 | 2183 | 2433 | 2285 | 3651 | 1433 | 947 | 865 |

1/ Printed shirtings, white jeans, white shirtings.

Index Numbers of F.O.B. Prices of Export Products
(1938 = 100)

| | Copra | Kapok | Rubber | Tea | Tin |
|---|---|---|---|---|---|
| 1948 March | 1163 | 469 | 205 | 395 | 241 |
| June | 1092 | 450 | 224 | 390 | 253 |
| September | 819 | 501 | 224 | 359 | 265 |
| December | 961 | 512 | 187 | 415 | 301 |
| 1949 March | 697 | 516 | 213 | 381 | 313 |
| June | 552 | 499 | 193 | 406 | 341 |
| September | 575 | 496 | 222 | 451 | 337 |
| December | 955 | 616 | 295 | 570 | 326 |
| 1950 March | 1020 | 732 | 291 | 543 | 347 |
| June | 2273 | 1500 | 760 | 794 | 734 |
| September | 2908 | 1464 | 1393 | 1024 | 684 |

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## A PROPOSAL FOR INTERNATIONAL CONTROL OF CARTELS IN EUROPE

Edward Marcus

The Secretariat-General of the Council of Europe, after discussions with the Secretariat of the Interim Commission of the International Trade Organization, has drawn up a "Draft European Convention for the Control of International Cartels" as a basis for further discussions. This proposal marks another milestone in the post-World War II efforts to erect an international economic framework within which trade could flow along relatively unobstructed channels.

Historically, the domestic policy of the United States has been one of hostility to combinations in restraint of trade -- loosely, those designated as trusts or monopolistic combinations, or, in European terminology, cartels. The long period of agitation leading to the enactment of the Sherman Anti-Trust Act in 1890, and the repeated demands by the leading political parties that the anti-trust laws be enforced strictly are sufficient evidence of the public antagonism to "private restrictionism". Hence, with the emergence of a positive international policy on the part of the United States as an outgrowth of the Second World War, it was natural for those framing our international economic principles to include opposition to private combinations as a cardinal point in our doctrine.

In the November 1945 "Proposals for Expansion of World Trade and Employment", the United States Government, through the Department of State, "suggested that a special agency be established within the /proposed/ International Trade Organization to receive complaints concerning restrictive practices of international combines and cartels, to obtain and examine the facts which are relevant to such cases, and to advise the Organization as to the remedies that may be required." (p. 5) 1/ It might be noted, however, that the Webb Export Combination Act (1918), permits U. S. firms to form combinations to engage in the export trade. This Act might have to be modified or repealed were the United States to ratify the Havana Draft of the International Trade Organization Charter. 2/

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1/ Cf. also p. 19.

2/ Cf. "the International Trade Organization", Report of the Committee on Foreign Affairs, 80th Congress, 2nd Session, page 19.

This suggestion was elaborated more specifically in Chapter V of the "Suggested Charter for an International Trade Organization of the United Nations".1/ Not only were Members to agree to take appropriate individual and collective measures to prevent practices that restrain competition (Art, 34, Sec. 1), but the International Trade Organization was to have power to investigate complaints and make recommendations for appropriate remedial action (Art. 35). Following such recommendations, members were to take actions terminating and preventing the recurrence of the practice condemned (Art. 37, Sec. 5).

The essence of these proposals was embodied in Chapter V of the (final) Havana Charter for an International Trade Organization,2/ which has not yet been ratified. However, the enforcement provision in the Havana Charter is somewhat weaker than the United States had proposed. Article 50 Section 1, requires that "each Member shall take all possible measures by legislation or otherwise, in accordance with its constitution or system of law and economic organization, to ensure, within its jurisdiction, that private and public commercial enterprises do not engage in [restrictive business] practices . . .". Section 4 requires that "each Member shall take full account of each request, decision and recommendation of the organization . . . and . . . take in the particular case the action it considers appropriate having regard to its obligations under this Chapter."

At this stage, doubts were expressed whether the other nations were willing to pursue a genuinely anti-monopoly program. Thus, the Committee for Economic Development noted that "many of the countries which finally accepted these provisions have no traditional allegiance to the principle of competition," and it regarded Chapter V as "an important concession to the American point of view."3/ The National Association of Manufacturers, on the other hand, urged the rejection of the Havana Charter,

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1/ Department of State, September 1946, Publication 2598, Commercial Policy Series 93.

2/ March 24, 1948. The text is contained in the Department of State Publication 3206, Commercial Policy Series 114 (September 1948).

3/ "The International Trade Organization and the Reconstruction of World Trade" (June 1949), page 23.

accusing it of leaving "the doors wide open" to cartels and monopolies. 1/

However, the fears expressed by the more hostile critics may have been too extreme. In the late summer of 1949, at the First Session of the Council of Europe, 2/ a Report was adopted by the Consultative Assembly requesting the Committee of Ministers "to draw up a draft European convention for the control of international cartels, which it will present to the Assembly". 3/ Subsequently, at the Third Session (March 30-April 1, 1950) the Committee of Ministers requested a study of the issue in collaboration with the preparatory commission of the International Trade Organization, 4/ and, on January 24, 1951 the Draft European Convention for the Control of International Cartels was completed for transmission to Member countries. 5/

The most significant provisions, naturally, are those describing the enforcement of the Draft aims. The Convention provides for the establishment of a Board with which restrictive agreements would be registered, and which would investigate, and, if possible, settle complaints regarding restrictive practices. If no settlement were reached, the complaint could be carried to the European Court established in the Convention for Protection of Human Rights and Fundamental Freedoms. 6/ Two alternative paragraphs are then put forth (Art. 34, pars. 2a and 2b) should the Court decide that a practice is harmful. One proposal is to award damages to the complainant and impose fines up to three times the estimated profit the respondent derived from the harmful practice. The other proposal would limit the Court to recommending further action (including penalties), and would leave it to the High Contracting Parties to give effect to the judgement, with the Committee of Ministers supervising its execution.

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1/ "The Havana Charter for an International Trade Organization", Economic Policy Division Series, No. 9 (April 1949), page 3. For a more balanced view, cf. "The International Trade Organization", Report of the Committee on Foreign Affairs, 80th Congress, 2nd Session, pp. 35-36, where it is remarked that the original United States proposal was "too strong" for some of the other delegations.

2/ Held at Strasbourg, August 18-September 8, 1949.

3/ Document 30, September 2, 1949, Sec. I, par. 6.

4/ International Organization, August 1950, p. 513.

5/ Cf. the Appendix for a summary of the more important articles of the Convention.

6/ Signed at Rome, November 4, 1950.

In addition, under Article 36, the High Contracting Parties would take the necessary measures to ensure that, within their jurisdictions, private and public commercial enterprises do not engage in harmful restrictive practices.

Were the Draft to be ratified, the necessary legal sanctions are provided to reduce greatly the influence of restrictive business practices. Price fixing, territorial allocation, production limitations, and the prevention of the development of new inventions are all proscribed, whenever engaged in by monopolies or monopolistic groups in intra-European trade in such a way as to "have harmful effects on the expansion of production or trade necessary to maintain a high standard of living or of employment". (Articles 1 and 2). These provisions are sufficiently specific to outlaw the more common and obvious abuses associated with cartels. Hence, mitigation of such restrictionism would depend on the vigor of the enforcing body, and on the interpretation given to the concept of "harmfulness"; many restrictive practices might escape condemnation if this concept were interpreted too strictly.

Special attention will have to be given to the attitude of the West German Government towards cartels. Many of the European cartels include German units. That Germany's preference for cartels is not a dead issue may be inferred from the current negotiations on the Schuman Plan for merging the coal and steel production of Western Europe. Thus, "the Western German regime . . . so far has refused to accept a provision barring cartels in the two industries",1/ a stand which may well determine the fate of the Schuman Plan.2/

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1/ The New York Times, January 19, 1951, page 11.

2/ Cf. Harold Callender in The New York Times, February 5, 1951, page 4.

## Appendix

## Summary of Draft European Convention for the Control of International Cartels 1/

Art. 1 - Restrictive practices are defined as those (affecting trade between the signatories) which restrain competition, limit access to markets, or foster monopolistic control. These include fixing prices or other terms or conditions of sale; territorial allocations; discrimination against particular enterprises; production quotas and limitations; preventing the development or application of new technological advances; or abuse of patent rights.

Art. 2 - Such practices are defined as being "harmful" when the offenders (one or more private or public enterprises) "possess effective control of trade among a number of countries in one or more products" and their practices have or will have harmful effects "on the expansion of production or trade necessary to maintain a high standard of living or of employment".

Art. 5 - A European Cartel Board shall be established.

Art. 6 - The Board (cf. Art. 5) shall (a) register all restrictive agreements concluded between commercial enterprises within the jurisdiction of two or more of the High Contracting Parties; (b) notify the High Contracting Parties of prima facie cases of harmful practices; (c) investigate such restrictive practices; and (d) consider complaints, and, if possible, settle them.

1/ This is the writer's summary of the main provisions of the Draft, dated 24 January, 1951, at Strasbourg (SG/R(51)5. RESTRICTED).

Art. 15 - "Failure to register an agreement in accordance with Article 6 or refusal to furnish information requested by the Registrar will raise a presumption that the agreement is harmful, though the parties thereto will be free to prove the contrary."

Art. 21 - Any High Contracting Party may lodge a complaint that any private or public commercial enterprise in the jurisdiction of any High Contracting Party is engaged in harmful practices.

Art. 22 - Provided it is not anonymous, any affected person, enterprise, or organization within the jurisdiction of a High Contracting Party may lodge a complaint that any private1/ commercial enterprise within the jurisdiction of any High Contracting Party is engaged in harmful practices.

Arts. 27 and 28 - A Commission of the Board is to prepare a report on each case, either summarizing the facts and stating the settlement reached, or reporting on the facts and giving its opinion as to the correctness of the allegation.

Arts. 29 and 30 - The European Court provided for in the Convention for the Protection of Human Rights and Fundamental Freedoms shall have jurisdiction over complaints which the Board Commission does not settle or the settlement of which is not implemented.

Art. 34 - Alternative proposals regarding the effect of judgements of the Court. Cf. the text, page 3.

Art. 36 - "The High Contracting Parties shall take all possible measures. . . to ensure, within their respective jurisdictions, that private and public commercial enterprises do not engage in harmful practices as defined in this Convention, and shall assist the Board in preventing these practices."

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1/ Note that only a Government can enter a complaint against a public commercial enterprise (Art. 21).

Art. 40 - "Execution [of European Court decisions] in the territory of the High Contracting Parties shall be effected in accordance with the legal procedure in force in each of them and after a writ of execution has been issued, *without any review of the decision itself*,1/ in the State on whose territory the decision is to be executed."

Art. 41 - Complaints by High Contracting Parties regarding operations of such services as transportation, telecommunications, insurance and the commercial services of banks shall be negotiated with the other Party or Parties concerned before the matter is referred to the Board.

Art. 42 - Operations in conformity with Inter-governmental Commodity Agreements under Chapter VI of the Havana Charter and operations of public commercial enterprises in accordance with other agreements among at least two-thirds of the High Contracting Parties are exempt from the provisions of the Convention.

Art. 46 - The Convention may be extended by a High Contracting Party to its territories.

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1/ Italics not in original.