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Nationalization of the Bank of England

Beatrice Bulla

Facts in regard to the pending nationalization of the Bank of England are so few at the present time that speculation has a very wide field. Since the announcement late in July of the Labor victory in the election of July 5, there has been a swelling tide of conjecture as to the method of nationalizing the Bank, the changes to be introduced in its structure and operations, and the consequences of these changes. The Labor Party's platform for the election included nationalizing the Bank, establishment of a peace-time policy of direction of investments to support industrial reconstruction, and nationalization of certain heavy industries.

The following official statement of the plans of the new Government for the Bank was included in the King's Speech at the opening of Parliament on August 15:

"In order to promote employment and national development, machinery will be set up to provide for the effective planning of investment and a measure will be laid before you to bring the Bank of England under public ownership."

Two semi-official statements in radio broadcasts to the United States had preceded this pronouncement. Sir Stafford Cripps, President of the Board of Trade, had affirmed the Party's policy of granting fair compensation for any interests taken over by the State, and Professor Laski had given notice that nationalization of the Bank and investment control would have first priority. In Parliamentary debate on the King's Speech, the Chancellor of the Exchequer, Dr. Dalton, made

a number of official disclosures regarding forthcoming action. First, there will be "fair compensation" to private stockholders; second, Lord Catto, the Governor of the Bank, will remain at his post for a time to inaugurate the new regime; and third, the Government does not contemplate constant interference with the day-to-day work of the Bank. He stated that when the House met again in the autumn the Government would introduce a bill to carry out the undertakings in the King's Speech. The session which began August 15 rose for recess on August 24 and will reassemble October 9. Until the introduction of the promised bill, there will probably be no more definite information on the procedure of nationalization.

Opinion in the British press largely bears out the Chancellor's view that "to a large extent the change proposed would have the effect of bringing the law into accord with the facts of the situation as they had developed." Discussion in the press has centered on the Bank rather than on the "effective planning of investment," which seems to be taken for granted. The Economist points out that this formula may mean much or little and that judgment will have to await publication of the bill.

One immediate effect of the election and the impending nationalization program was a sharp break in the price of Bank of England shares, followed shortly by a rally. The Stock Exchange Gazette expressed the opinion that the threat of nationalization should support the quotation of Bank of England stock, in view of possible compensation in Government stock with an equivalent return. A financial commentator suggested that the Bank might have greater influence as an adviser to the Government after it came under public control than when privately owned. A few warnings have been given, such as the Statist's reminder that the danger of finance being made the instrument of party politics must increase, and that there may prove to be incompatibility between a nationalized Bank and an independent commercial banking system, unless the Government relies exclusively for its inflationary extra-budgetary finance on the central institution.

Although practically every recent discussion admits that the ascendancy of Treasury policy over Bank policy is of long standing and that the Bank has been "as good as nationalized for many years," the change that has occurred in the inter-war period can be illustrated by a few citations. In 1926, Walter Leaf described the Bank's relation to the Government as follows:

"The Governor is in constant touch with the Chancellor of the Exchequer and is the medium by which the financial policy of the Government is conveyed to the City for execution."

The last independent move of the Bank, Dr. Einzig remarks, was to increase the Bank rate in February 1929 without consulting the Treasury. But in 1931 Sir Ernest Harvey, Deputy Governor of the Bank, in his testimony before the Macmillan Committee, still claimed that a central bank

"should be free from being required to submit to political pressure and to subordinate sound finance to the dictates of political expediency. For that reason .... we feel that it should be free from political control."

A speech made by Mr. Montagu Norman, Governor of the Bank, at the Mansion House in 1936 is frequently cited to mark the formal surrender of the independence of the Bank after the adoption of new financial machinery following the departure from the gold standard in 1931. The speech contained the assurance that the Ministers "will at all times find us willing with good will and loyalty to do what they direct us as though we were under legal compulsion."

After the outburst of debate and discussion following announcement of the pending nationalization, it seems likely that the bill, when it appears, will prove to be an anti-climax.

#### The Swiss Banking Crisis

Rosa Ernst

It was to be expected that the end of the war in Europe would create difficult economic problems for neutral countries attempting to readjust their economies to a normal peace-time basis. Difficulties recently experienced by several of the Swiss commercial banks reflect one aspect of the adjustment process. Articles in the American press in the early part of August referred (with some exaggeration) to two banks as having already "gone under" and to a third as being on the verge of bankruptcy.

The banks mentioned in the first category are the Basler Handelsbank (Banque Commerciale de Bâle) in Basel, and the Eidgenössische Bank A.-G. (Banque Fédérale S.-A.) in Zürich--erroneously mentioned by the press as being located in Chur. The third bank, Aktiengesellschaft Lou and Co., Zürich, issued a statement on August 3 to the effect that the institution was in a liquid position and able to take care of all its commitments. Public confidence was steadied by this announcement and quotations on the bank's shares rose from 290 on June 30 to 296 on August 7. All three banks are among the leading financial institutions of the country and belong to the group of the so-called seven large commercial banks. The Basler Handelsbank was established in 1862 and the Eidgenössische Bank in 1864, while the foundation of the Aktiengesellschaft Lou and Co. dates back to 1755.

Basler Handelsbank

On August 1 the Swiss Banking Commission (set up in 1942 by the Federal Government and charged with the granting and supervision of moratoria for commercial and savings banks) announced that the Basler Handelsbank had been granted a moratorium. The bank justified its request for such action by disclosing that during the last days of July runs on the bank had developed with a resulting precipitous decrease in sight deposits and that quotations on the bank's shares had experienced an unprecedented drop on the market. A moratorium granted to any bank by the Federal Banking Commission implies that the institution is illiquid, but not necessarily bankrupt. Under the terms of the moratorium the Handelsbank will be enabled to put its finances on as sound a basis as possible without being under constant pressure of withdrawals, and will gain time to make the necessary decisions and take the necessary steps with regard to a possible out-of-court settlement of its affairs which under certain conditions might include a merger with another institution. The bank will be put under the supervision and control of a commissioner appointed by the Federal Banking Commission. He will ascertain the position of the bank, submit his report to the Commission and to the bank and take measures to keep the institution running. The authority of the bank to administer its affairs is not jeopardized under the moratorium, which is originally granted for one year but which may be renewed for another year and again for six months if conditions should warrant such action.

To anyone following the quotations of the bank's shares on the stock exchange the bank's request for a moratorium caused no surprise. During the first half of 1945 the quotations remained at about the lowest levels quoted in 1943 (265) and 1944 (263), but between July 2 and July 25 they dropped rapidly from 275 to 200 francs per share. Between July 26 and 30 they fell to 59, the lowest level reached, and rose again to 68 by July 31. Even without this catastrophic decline in share quotations it was evident that the complete collapse of Swiss-German merchandise and financial transactions could not be without influence on an institution holding considerable foreign assets, the greatest part of which were German credits subject to limited transfer. The present difficulties of the bank are perhaps not alone the outcome of the war just ended, but are also the result of long-term investments made in Germany at the time of the Dawes and Young loans, service on which was subsequently blocked by the German authorities. The bank in 1935 had been granted a two-year moratorium made necessary because it held 65 million Swiss francs of illiquid assets, of which 62 million alone were German credits. When the bank was reorganized in 1937 a sum of 34 million francs was set aside to take care of future risks of various kinds, particularly of transfer risks. This reserve has now proved inadequate. During the late 'thirties and especially after the outbreak of hostilities the bank had no opportunity to reduce its foreign holdings. At the same time normal domestic business expansion was hampered because of war conditions. All through the war years, interest from German credits and clearing claims was received by the bank, thus affording it at least a certain income, but the defeat of the Axis put a sudden stop to the servicing of these commitments. Ever since the reorganization the

balance sheet totals have followed a declining trend from a total of 206.6 million in September 1937 to 153.5 million at the end of June 1945, the bank thus showing the smallest balance sheet total of any of the seven large banks. One reason for this retrogression may be that the bank during recent years has followed a determined policy of redeeming its bond issues which in 1937 amounted to 58 million francs, but which were completely amortized by the end of 1944.

The last annual report of the bank (February 1945) stated that it was not possible to give an accurate evaluation of the institution's foreign holdings. This may be because legal questions regarding interpretations of the term "domicile" are involved. It is expected that the bank will be able to pay its depositors in full, though the stockholders may lose their investment. Among its realizable assets the bank is reported to hold 20 million francs of good Swiss debts, a 51 per cent control of a widely-known pharmaceutical company (F. Hoffmann-La Roche and Co.), a 95 per cent interest in a leading utility company (Société Suisse d'Industrie Electrique Bâle), and bank buildings valued at 10 million francs. The balance sheet for June 30 is given below.

Eidgenössische Bank A.-G.

As early as March of this year the Board of Directors of the Eidgenössische Bank called the attention of the General Meeting of Stockholders to the fact that the bank's reserves alone were not sufficient to cover its holding of blocked foreign assets (chiefly German and Italian). Subsequent developments forced the bank to appeal for outside help in an effort to put its finances in order. On July 26 it was announced that the Schwoizerische Bankgesellschaft (Union Bank of Switzerland) had agreed to take over the business of the Eidgenössische and to effect a merger between the two institutions. The stockholders of the Eidgenössische Bank are to receive three shares of Union Bank stock for ten shares of the old Eidgenössische Bank stock. The share quotations of the latter during the period from May 30 to July 30 had fallen from 360 francs to 226 francs per share. Shares of the Union Bank were quoted at 685 on May 30, at 690 on June 30, and at 705 on July 30.

German assets held by the Eidgenössische Bank, estimated at 21 million Swiss francs, are to remain the exclusive property of the shareholders of the Eidgenössische Bank. They have long been held on deposit with the Gesellschaft für Hypotheken und Immobilienwerte, Chur (Society for Mortgages and Real Estate, Chur), a company founded for this specific purpose. The balance sheet of the merged institutions will show no blocked German assets whatever, the Union Bank having been able in the past to write off or amortize its own blocked foreign commitments. Through the merger the capital of the Union Bank will be increased from 40 to 50 million Swiss francs and the reserves from 32 to 40 million francs. The Union Bank will no doubt experience a considerable business expansion; it is expected that its balance sheet total from now on will exceed one billion francs, thus strengthening its position as the third largest of the six remaining commercial banks, surpassed only by the Société de Banque Suisse and the Crédit Suisse. A balance sheet for the Eidgenössische Bank for June 30, 1945, is given below. Its total amount



Netherlands Gold

J.H.F.

The Netherlands Bank disclosed at the beginning of July 1945 that it had revalued its gold holdings in conformity with the devaluation of the Netherlands guilder which occurred at the beginning of the campaign of liberation in the fall of 1944. Before the German invasion, the Bank valued its gold holdings at the rate of 2,009 guilders per fine kilogram, or about 4 per cent below the actual market rate. The German-dominated administration increased the valuation in July 1943 to 2,097 guilders, a price conforming to the official rate of the guilder in relation to the reichsmark and the dollar. Now the price of gold has been raised to 2,970 guilders. On the basis of this price, the gold parity of the guilder in relation to the dollar is 37.9 cents per guilder. This rate is practically identical with the rate of 37.7 cents which may be derived from the official guilder-sterling relationship of 10.691 guilders per pound sterling, and is close to the authorized redemption price for guilder notes presented in New York (37.38 cents).

At the time of the German invasion (May 1940), the gold holdings of the Bank were 625 million dollars. Since the Germans took over all of the gold reserves that had not been removed from the country, the official holdings decreased to 500 million dollars at the beginning of 1943. Most of these were held under earmark with the Federal Reserve Bank of New York. In the winter of 1944-45, about 102 million dollars of these reserves were pledged to a group of New York banks as collateral for a loan negotiated by the Netherlands Government. It is also known that about 65 million dollars' worth of gold was spent by the Government-in-Exile for war purposes in the United States. Now it has been disclosed that an additional 63 million dollars was used for such purposes in other countries so that the amount of free gold in the possession of the Bank has been reduced to 270 million dollars. At the previous valuation, this amount would have been shown as 504 million guilders. As the result of the revaluation, the figure is now 713 million guilders, leaving a revaluation "profit" of 209 million guilders. This profit no doubt has been used to reduce the Government debt resulting from the use of the Bank's gold.

The Bank's gold holdings represented coverage of 20 per cent for bank notes circulating at the end of July 1945. There can be little doubt that the Bank's reserves will be increased in the near future by conversion of the New York loan and release of the gold pledged as collateral therefor. Moreover, the Government expects that the currency exchange started in June 1945, together with a loan drive and tax program yet to be implemented, will continue to reduce the amount of currency in circulation. Thus it seems likely that the final coverage figure will be well in excess of the present one although it certainly will not reach the pre-war proportion of more than 100 per cent.

National Income and Private Consumption in Germany  
and in the United States

Paul Hermsberg

During the last decade before the war, changes in national income in the United States and Germany showed remarkable similarity. Only in the first and last years of this period did a sizeable difference appear between the dollar amount of United States national income and the reichsmark amount of German national income. Adjustment of the income data for price changes has a very small effect on the picture; in spite of the devaluation of the dollar in 1933, the cost of living in both countries followed parallel lines. German national income reacted somewhat more slowly in the business cycle than that of the United States, but only during the crisis of 1933 (which failed to affect the German economy, supported as it was by large expenditures for rearmament) did income developments in the United States and Germany move in opposite directions. Table I indicates that the German national income was about one-fourth of the American in 1929, increased to about 28 per cent during the following period, and jumped to 34 per cent in 1938. This comparison, however, requires a conversion of the reichsmark value of German national income into a dollar amount, a conversion which can only be calculated in an arbitrary manner on the basis of the relative purchasing powers of the two currencies.<sup>1/</sup>

Table I. National Income in Germany and in the United States<sup>1/</sup>

Year	Germany				United States		German income as per cent of U.S. income
	National income (In billions of RM)	Index of cost of living	Purchasing power of RM (In U.S. cents) <sup>2/</sup>	Purchasing power of national income (In billions of dollars)	National income (In billions of dollars)	Index of cost of living	
1929	72.3	100.0	28.1	20.3	83.3	100.0	24
1930	66.2	96.2	28.5	18.9	68.9	97.5	27
1931	53.8	88.4	28.2	15.2	54.5	88.7	28
1932	42.6	78.3	28.6	12.2	40.0	79.7	31
1933	44.1	76.6	27.8	12.3	43.3	75.4	28
1934	50.4	78.6	27.9	14.1	49.5	78.1	28
1935	56.3	80.0	28.1	15.8	55.7	80.1	28
1936	62.6	80.8	28.1	17.6	64.9	80.9	27
1937	70.3	81.2	29.0	20.3	71.5	83.8	28
1938	77.4	81.6	28.4	22.0	64.2	82.3	34

<sup>1/</sup> The tables in this article are based on calculations by the author for a special report, "German National Income and National Product Between the Two World Wars."

<sup>2/</sup> The purchasing power of RM in cents has been calculated for each year according to the following formula: purchasing power rate for 1929 x  $\frac{\text{U.S. index of cost of living}}{\text{German index of cost of living}}$ . See appended note for further explanation.

<sup>1/</sup> See appended note.

Although at first glance the economic development of the two countries, despite widely divergent economic policies, appears surprisingly similar, each advance into more detailed investigation shows clearly the particular effect of national-socialist economic policy and of rearmament on German national income. In both countries, the derivation of national income by industries was strongly influenced by the business cycle. As usual, the economic breakdown affected manufacturing industries with particular force; in both countries, these industries contributed their lowest absolute amounts and smallest percentage shares of the national income in 1932 and regained their 1929 positions in 1937. One typical difference between the two economies is shown in the development of agricultural income. While in the United States agriculture followed the general trend of business, German agriculture--in consequence of governmental aid--showed stronger resistance to the depression than other industries. During the rearmament period, however, German governmental interest centered in the manufacturing industries and agriculture slipped back to the relative position of 1929. Both in the United States and in Germany the various industrial divisions participated in the national income in 1937 in approximately the same proportions as in 1929. Consequently, the percentage derivation of the national income as shown in these years may be taken as typical for each country.

Table II. National Income by Industrial Divisions  
(Per cent of total)

Year	Germany				United States			
	Agriculture	Mining and manufacturing <sup>1/</sup>	Other industry	Total	Agriculture	Mining and manufacturing <sup>1/</sup>	Other industry	Total
1929	13	50	37	100	8	33	59	100
1930	13	46	41	100	8	30	62	100
1931	15	42	43	100	7	26	67	100
1932	16	37	47	100	6	22	72	100
1933	16	38	46	100	7	25	69	100
1934	16	45	39	100	7	27	66	100
1935	15	48	37	100	9	29	62	100
1936	14	50	36	100	8	30	62	100
1937	13	51	36	100	9	32	59	100
1938	13	51	36	100	8	28	64	100

<sup>1/</sup> Includes "contract construction" and "power and gas."

In neither case does this derivation of national income correspond to the division of the labor force by industry. Agriculture, in particular, used a much larger share of the national labor force than is indicated by its participation in the national income. This discrepancy would remain even if the underestimation of agricultural income, which is notorious for all national income estimates, were corrected. It may be pointed out that the contrast was much greater in the United States than in Germany, in spite of the fact that in Germany 4.6 million of unpaid female family workers were included in the agricultural labor force against only 226,000 in the United States.

Table III. Experienced Labor Force and National Income  
by Industrial Divisions  
(Per cent of total)

Industrial group	Germany <sup>1/</sup>			United States <sup>2/</sup>	
	1925	1933	1938	1930	1938
Experienced labor force					
Agriculture	31	34	26	22	18
Mining and manufacturing <sup>3/</sup>	42	34	42	33	34
Other industrial groups	27	32	42	45	48
Total	100	100	100	100	100
National income					
Agriculture	15	16	13	8	8
Mining and manufacturing <sup>4/</sup>	53	38	51	30	28
Other industrial groups	32	46	36	62	64
Total	100	100	100	100	100

- <sup>1/</sup> The figures for the German experienced labor force (Erwerbsspersonen) refer to the old Reich--excluding Saarland. For 1938, figures of the census of May 17, 1939, are used.
- <sup>2/</sup> United States figures for 1930 refer to "gainful workers in the main industry groups;" figures for 1938 to "experienced labor force by industry" in 1940. The figures are not closely comparable.
- <sup>3/</sup> Mining and manufacturing include construction, business and repair services, and utilities.
- <sup>4/</sup> Mining and manufacturing include construction and power and gas.

A further distinction may be seen in the fact that in Germany the share of mining and manufacturing industry in the national income was relatively higher than its use of labor, while in the United States "other industrial divisions"--especially transportation and finance--were responsible for a much greater proportion of national income than of employment.

In Germany, as in the United States, the distribution of the national income between salaries and wages on the one hand and income of proprietors and capital on the other showed the usual development in the business cycle. The participation of capital decreased during the depression and increased during the recovery. In the United States, the reaction was sharper but the subsequent increase in the share of capital stopped in 1936, while in the Third Reich, in spite of the professed aim of "smashing interest slavery," the share of capital rose constantly after the Nazi seizure of power.

Table IV. National Income by Distributive Shares  
(Per cent of total)

Year	Germany				United States		
	Employees	Proprietors and capital	Public enterprises	Total	Employees	Proprietors and capital	Total
1929	66	31	3	100	64	36	100
1930	67	30	3	100	70	30	100
1931	70	28	2	100	74	26	100
1932	69	29	2	100	79	21	100
1933	67	31	2	100	70	30	100
1934	66	32	2	100	70	30	100
1935	65	33	2	100	67	33	100
1936	64	34	2	100	66	34	100
1937	62	36	2	100	68	32	100
1938	62	36	2	100	70	30	100

Comparison of the share of private consumption in the gross national product in Germany and in the United States gives evidence of the violent modification affected by national-socialist policy in the composition of the national income. Until 1933, the share of private consumption in all goods and services available for domestic use was very similar in both countries. It amounted to 72-73 per cent in 1929 and increased during the depression to 78-79 per cent in 1932; during the recovery, private consumption again decreased relatively in both countries. In the United States, however, private consumption never fell below the share of 1929, while in Germany rearmament claimed an increasing part of the national product and finally limited private consumption to little more than one-half of all goods and services available for domestic use. It has been suggested that German national income probably reached one-third of the United States national income in 1938. Nevertheless, between 1929 and 1938, the consumption of the German people probably remained relatively unchanged at about one-fourth of American consumption. The entire additional production of goods and services was devoted to rearmament and other special projects of the National-Socialist Government.

Table V. Goods and Services Available for Domestic Use

Year	In Germany			In the United States			German consumption as % of U.S. consumption
	Total	Private consumption		Total	Private consumption		
	(In billions of dollars) <sup>1/2/</sup>	(Per cent of total)		(In billions of dollars)	(Per cent of total)		
1929	25.3	18.5	73	99.0	70.8	72	26
1930	24.2	18.1	75	87.4	64.9	74	28
1931	19.7	15.7	79	71.7	54.2	76	29
1932	16.9	13.2	79	55.1	43.0	78	30
1933	16.0	12.2	76	54.2	42.4	78	29
1934	18.1	12.9	71	63.1	47.7	76	27
1935	20.3	13.0	64	70.4	52.2	74	25
1936	22.1	13.4	60	82.0	59.1	72	23
1937	25.6	14.7	58	87.2	62.5	72	24
1938	27.8	14.4	52	79.4	58.5	74	25

<sup>1/</sup> Gross national product less export surplus of goods and services (including gold and silver for private use).

(Footnote 2 at bottom of following page.)

Note on the calculation of German-United States rates on a purchasing-power basis.

Any conversion of the reichsmark value of the German national income into a dollar amount will be arbitrary. The official exchange rate would indicate that one reichsmark was equal to 23.8 United States cents in 1929 and to 40.2 cents in 1938. The parallel development of the cost of living in the two countries, however, indicates that the latter rate was wholly artificial and that the devaluation of the dollar in 1933 was neutralized by subsequent exchange control and governmental exchange manipulation on the part of Germany. In fact the relation between the purchasing power of the dollar and of the reichsmark remained nearly unchanged during the entire period from 1929 to 1938. But this does not mean that the official exchange rate of 1929 offers an exact measure for converting German national income figures into dollars. The question of how much purchasing power is represented by one reichsmark inside Germany in relation to the purchasing power represented by one dollar inside the United States can only be answered approximately. The answer depends on the kinds of goods for which the money was spent. In a detailed statistical study of the problem of purchasing-power parities, Colin Clark<sup>1/</sup> calculated that on the basis of the official exchange rate of 1 RM = 23.8 cents in 1929, a basket of goods representing the commodity and service composition of German national income would have sold on American markets at a price 17.9 per cent higher than in Germany. The corresponding purchasing-power rate, according to this calculation, would have been 1 RM = 28.1 cents. A basket of goods representing the composition of American national income and sold on German markets would have sold for 5.7 per cent less than in the United States. The corresponding purchasing-power rate would have been 1 RM = 25.2 cents. Assuming the difference between the two purchasing-power rates to be real and not to have originated from gaps and errors in the material used by Clark, the logical method of utilizing his findings would appear to be as follows: to compare the United States national income of 1929 with the German national income of the same year from an American point of view, one should convert the reichsmark amount of the German national income into dollars at the purchasing-power rate of 1 RM = 28.1 cents; to make a similar comparison from a German point of view, one should convert the dollar amount of the American national income into reichsmark at the purchasing-power rate 1 RM = 25.2 cents. There is no logical reason to make the comparison (as Colin Clark does) from some middle point of view using a purchasing-power rate equal to the geometrical mean between 28.1 cents and 25.2 cents.

It is pertinent to note that the official pre-war exchange rate of 1 RM = 40.2 cents was generally replaced in German foreign trade transactions by manipulated special rates about 30 per cent lower. Consequently, the effective exchange rate of approximately 28.1 cents in 1938 was pretty close to the purchasing-power rate as calculated above for that year of 28.4 cents.

1/ "Internationaler Vergleich der Volkseinkommen," Weltwirtschaftliches Archiv, Volume 47, 1938, p. 51, and repeated in other publications.

Footnote to table on preceding page:

2/ Dollars of purchasing power equal to that of a dollar in the United States: see appended note and Table I.