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New Currency in Hungary.....	1
Further Depreciation of the Chinese National Dollar.....	4
Coordination of Economic Research Activity of Internal Agencies.....	5
On the Elasticity of Import Demand Schedules.....	8

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New Currency in Hungary

J. Herbert Furth

The first phase of the Hungarian hyper-inflation was concluded on July 31 with the demonetization of the pengő. The increase in the circulation of pengő banknotes between the end of 1939 and June 22, 1946 (latest date available) is shown in Table 1 on the following page. Hungarian currency circulation increased approximately 10 times during the war, and increased almost eight billion times in the period from the beginning of the Russian occupation to the third week of June, 1946. As usual under such circumstances, the acceleration became faster and faster, the circulation increasing 1200 times in the last three-week period alone. The June figure, therefore, does not give any indication as to the magnitude of the currency circulation at the end of July.

The foreign exchange value of the pengő decreased even more rapidly than the circulation increased. The changes in the dollar quotation between the end of 1939 and July 11, 1946 (latest date available) are shown in Table 2. The value of the dollar in terms of pengő increased 15 times during the war but almost two trillion times under the Russian occupation up to June 22, 1946, and another two million times in the period from June 22 to July 11. In consequence, the dollar value of the total domestic currency in circulation shrunk to approximately two per cent of the prewar level.

The domestic purchasing power of the pengő declined almost as rapidly as its foreign exchange value. This decline is evidenced by the official quotation of the "tax pengő" ^{1/} which was introduced as of

1/ see Review of Foreign Developments, February 11, 1946, p. 1

Table I

Currency Circulation in Hungary
(Billions of Pengö)

1939	Dec. 31	1
1941	Dec. 31	2
1944	Nov. 30	11
1945	Sep. 30	42
	Dec. 31	765
1946	Jan. 31	1,646
	Feb. 28	5,238
	Mar. 31	34,002
	Apr. 30	434,304
	May 31	65,588,000
	June 22	78,424,250,000

Table II

Dollar Rates in Hungary
(Pengö per Dollar)

	<u>Official</u>	<u>Black Market</u>
1939 (Dec.)	5.70	
1941		9.00 - 14.40
1944 (Dec.)		92
1945 Apr. 30		250 ^{1/}
June 30		635 ^{1/}
Sep. 30		5,500 ^{1/}
Dec. 31	141,550	275,000
1946 Jan. 31	382,000	777,500
Feb. 28	2,535,000	2,700,000
Mar. 31	10,900,000	16,500,000
Apr. 30	153,700,000	220,000,000
May 31	26,352,000,000	54,000,000,000
June 22	22,008,000,000,000	165,000,000,000,000
June 30	1,835,000,000,000,000	30,000,000,000,000,000
July 11		350,000,000,000,000,000

^{1/} Tolerated "free market."

January 1, 1946, as an accounting unit of supposedly stable purchasing power. At the time of its introduction, the tax pengő was equal to the ordinary pengő. By April 30, 1946, it had reached the value of 570 pengő, and by June 28 (latest date available) that of three billion pengő. On July 11, when the dollar was quoted at 350 quintillion pengő, a dollar rate of 6.5 million tax pengő was reported. On this basis, the tax pengő was worth approximately 54 trillion pengő.

On July 11, 1946, the issue of ordinary pengő notes was discontinued and "tax pengő" certificates declared legal tender. This measure did not prevent a further depreciation of the currency. On July 31, the tax pengő finally was replaced by the forint, the name of which was taken from the silver florin, the currency of the Austro-Hungarian monarchy before the introduction of the gold standard at the end of the 19th century. The new unit was declared equal to 8.51839 United States cents (\$1 = 11,7393 forints) and to 200 million tax pengő. This relation corresponds to a dollar rate of approximately 2,348 million tax pengő, or on the basis of the July 11th ratio between tax pengő and ordinary pengő, to a dollar rate of about 126.8 sextillion pengő (126,800,000,000,000,000,000,000). This figure is probably the highest exchange ratio ever quoted in the history of money.

The new currency is "backed" by approximately 32 million dollars in gold, returned to the Hungarian Government by the United States armed forces in Germany. The Government plans to restrict for the time being the issue of banknotes to 240 million forints. If this program is executed, the new banknotes would have a gold cover of more than 100 per cent. Actually, however, the newly acquired gold cover can give the new currency only psychological support. The Hungarian inflation was mainly the result of two factors: an inadequate fiscal system forced the Government to finance its expenditures by means of credits from the central bank, and Russian exactions prevented a reduction in those expenditures and an increase in the supply of goods for domestic consumption which alone could have provided a base for additional government revenue. The Soviet authorities have now granted the Hungarian Government a limited moratorium on reparation payments. Reparations, however, were a very minor burden as compared to the goods and services requisitioned by the Soviet authorities as occupation costs or as confiscation of "German" assets. The country's economic system, as well as its new currency, has a chance of stabilization only if these burdens are substantially eased.

The Hungarian Government has used the introduction of the forint and the establishment of new exchange rates as an occasion for creating a substantial disparity between the domestic purchasing power and the foreign exchange value of the new currency. While the dollar value of the forint is about half the prewar dollar value of the pengő, retail prices of industrial products are five to nine times as high as before the war. Retail food prices are about three times, and average wages about twice the prewar figure.

There is a strong suspicion that this disparity was introduced under communist pressure in order to make trade between Hungary and the Western democracies more difficult. ^{1/} It is questionable, however, whether such a strategem can be successful unless it is continuously implemented by further actions aimed at preventing the reestablishment of a price level corresponding to world market prices at the current exchange rate. Moreover, the discrepancy exists only in the case of industrial products which Hungary exported before the war to the East rather than to the West, and it encourages rather than hampers imports, which in the immediate future may be more important to the Hungarian economy than exports.

Further Depreciation of the Chinese National Dollar

J.E.

On August 19, the Central Bank of China announced a new selling rate of 3,350 Chinese national dollars (CN\$) to one United States dollar, as compared with the rate of CN\$2,020 to U.S.\$1 which had prevailed since March 4 of this year when the present system of exchange control was introduced.

Although the 2020 to 1 rate, when it was established, showed promise of stimulating both Chinese exports and remittances from overseas Chinese, the two principal sources of receipts in China's balance of payments on current account, the stimulation proved temporary. The rise in internal prices has been so rapid over the past few months that the domestic purchasing power of the Chinese national dollar has fallen more and more behind its power to purchase imports. It was reported, for instance, that American goods, priced at as much as 40 per cent above prewar levels, paying three times the prewar freight rates, subjected to pilferage and extortionate landing and handling charges at Shanghai, and paying double the ordinary import duties (since valuations are based on Chinese inflated market prices rather than on direct invoice values), could still be sold at a profit in competition with locally manufactured goods. As a result imports have run at approximately ten times the level of exports and the drain on China's foreign exchange reserves has become prohibitive. Unfortunately, available statistics on Chinese prices give no assurance that the present depreciation of the exchange will do much to effect a balance in China's trade. An equilibrium rate, if such a term is applicable to so chaotic a situation, would probably lie within the range of 6,000 to 8,000 to 1. It is extremely doubtful that any reasonable balance in the current items of China's balance of payments can be achieved by depreciations of the exchange as long as the civil war with the Communists continues. The Nationalist Government is committed to a program of heavy military expenditures which can only be paid for by recourse to the printing press. It is estimated that the current budget deficit is at the rate of CN\$15 billion per day. Unless this gap between Government receipts and expenditures can be narrowed, other measures designed to stabilize the Chinese internal economy, no matter how drastic they may be, are sure to be ineffective.

^{1/} see Review of Foreign Developments, August 12, 1946, p. 8

Coordination of Economic Research of International Agencies

C. R. Harley

A report^{1/} prepared by Mr. Winant for the Secretary of State indicates that certain statistical and economic research activities to be undertaken by the Economic and Social Council of the United Nations or its sub-commissions may tend to overlap or duplicate similar research activities to be carried out by the International Monetary Fund or the International Bank for Reconstruction and Development. A brief outline of the organization and functions of ECOSOC will be presented in the following paragraphs, followed by comments on the specific functions of various organs of the Council, in so far as these have been determined, which may be similar to those of the Bank or Fund.

The Economic and Social Council is authorized by Article 60 of the United Nations Charter and is charged with responsibility, under the authority of the General Assembly, for carrying out those functions of the United Nations designed to create higher standard of living throughout the world, to solve economic, social, and health problems, to further educational and cultural cooperation, and to widen the area in which "human rights and fundamental freedoms" are enjoyed without distinction as to race, sex, language or religion. The Council consists of representatives of 18 members of the United Nations elected by the General Assembly.

At its first session in London (beginning January 23, 1946) the Council established one permanent commission and five temporary or "nuclear" commissions as follows:

1. Commission on Narcotic Drugs (Permanent)
2. Commission on Human Rights
3. Economic and Employment Commission
4. Statistical Commission
5. Temporary Social Commission
6. Temporary Transport and Communications Commission

The nuclear commissions prepared recommendations for their permanent composition and functions and these were presented to the second session of the Council (May 25-June 21 in New York); the Council approved permanent status for all of the Commissions listed above and approved as well full commission status for what had originally been a Subcommittee on the Status of Women, under the Commission on Human Rights. Definitive organization of these commissions will be a part of the order of business of the third session of the Economic and Social Council scheduled for September 11, 1946. A Fiscal Commission has also been proposed, but the proposal has not yet been approved by the Council.

The Council also established a Committee on Negotiations with Specialized Agencies whose function is to arrange for cooperation of such

^{1/} The Economic and Social Council of the United Nations. Report to the Secretary of State by the Honorable John G. Winant, United States Representative on the Council. July 15, 1946.

agencies with the United Nations.^{1/} This Committee has negotiated agreements with the Food and Agriculture Organization of the United Nations, the International Labor Office and the United Nations Educational, Scientific and Cultural Organization. The International Bank and the International Monetary Fund are the principal specialized agencies with which negotiations are yet to be successfully concluded. Mr. Winant in his draft report mentions "the extension of the area of relationships" with these agencies as an important matter for consideration by the third session of the Council.

The major provisions common to the agreements reached with the three organizations mentioned in the previous paragraph may be briefly summarized:

1. The United Nations recognizes the competence of each agency in its field.
2. Attendance of representatives of the specialized agencies shall be invited at meetings of ECOSOC, and its subsidiary commissions, of the General Assembly and its main committees, and of the Trusteeship Council when items in which the particular specialized agency has an interest are under discussion. Such representatives may participate in discussions but will have no voting privileges. Reciprocally, representatives of the United Nations may attend and participate, without vote, in meetings of the specialized agencies.
3. Written statements and recommendations may be submitted by the specialized agencies to the United Nations and its subdivisions as well as to the individual Member States,
4. Provision is made for the exchange of agenda items between the signatory bodies.
5. The specialized agencies agree to consider recommendations of the General Assembly and ECOSOC.
6. The specialized agencies agree to furnish information to and assist in carrying out programs of the Security Council upon request.
7. The specialized agencies may seek advisory opinions on certain legal problems from the International Court.
8. The specialized agencies will consult with the United Nations in the preparation of their annual budgets. The General Assembly may make recommendations to the agencies on budgetary matters.

^{1/} Article 57 of the United Nations Charter states that "the various specialized agencies, established by intergovernmental agreement and having wide international responsibilities, as defined in their basic instruments, in economic, social, cultural, educational, health and related fields, shall be brought into relationship with the United Nations in accordance with the provisions of Article 63." and Article 63 provides that the Economic and Social Council may enter into agreements with such agencies defining mutual relationships and "may coordinate the activities of the specialized agencies through consultation with and recommendations to such agencies and through recommendations to the General Assembly and to the Members of the United Nations."

9. Coordination shall be sought in the collection, analysis and publication of statistical data.

The organs of the Economic and Social Council whose research work will be in the same general fields as that of the Fund and Bank are the Economic and Employment Commission and the Statistical Commission; if a Fiscal Commission is established, it will also deal with closely related matters. The terms of reference of the Economic and Employment Commission (as revised on recommendation of the nuclear commission) authorize that body to report to and advise ECOSOC on general economic questions and more particularly on the following problems: prevention of wide fluctuations in business activity; international action to coordinate national full employment policies; problems of reconstruction of devastated areas; and promotion of economic development in less developed areas.

The following item in the terms of reference of the Economic and Employment Commission deals particularly with the relationship of that Commission to the specialized agencies:

"The Commission shall make recommendations to the Council with reference to economic questions involving concerted study and/or action by more than one specialized agency or commission of the Council and in particular shall draw the attention of the Council to the probable influence of the policies and activities of other commissions of the Council, the specialized agencies or other international organizations on the issues mentioned in the preceding paragraph."

The Economic and Employment Commission will have subcommissions on Employment, Balance of Payments, and Economic Development; a temporary subcommission on Economic Reconstruction of Devastated Areas was authorized by the Council at its second session. The following brief description of the functions of the Balance of Payments subcommission contained in the Council resolution authorizing that group is of interest in view of the existence of a similar research section in the Fund:

"to study and advise the Commission on balance of payments problems, especially in so far as they require for their solution concerted action by governments or by more than one specialized agency."

The Statistical Commission will presumably be an advisory and research body rather than an operating group. Collection, analysis and publication of statistical data will be carried out by the Secretariat Statistical Division. Among the problems listed as unfinished business for the Commission in Mr. Winant's report is that of "working out in further detail with the Secretariat the substantive problems of coordinating statistical activities of the United Nations and the specialized agencies."

Although organization of a Fiscal Commission under the Economic and Social Council has been proposed, no such body has as yet been established. Tentative terms of reference for this commission indicate that it would be expected not only to continue the type of work carried on by the Fiscal

Committee of the League of Nations (e.g., general studies of taxation systems and techniques with a view to advising less developed areas on fiscal problems; study of the effects of double taxation on international financial relationships and development of draft agreements to ease the burden of corporations subject to tax in more than one country), but also to investigate the efficacy of fiscal techniques in the prevention of inflationary developments and to seek exchange of information among members of the United Nations as to the social and economic effects of their fiscal systems.

On the Elasticity of Import Demand Schedules

Randall Hinshaw

In the classical theory of international trade, it was assumed that the average price elasticity of a country's demand for foreign goods is greater than unity. This assumption is essential to the classical explanation of how international equilibrium is achieved. Thus the classical remedy for an adverse balance of payments was a policy of price deflation in the affected country, since it was assumed that a fall in (export) prices would lead to an increase in the value of the country's exports. But an increase in value of exports in this situation could occur only if the foreign demand for the country's products were greater than unity. For if the foreign demand were of unit elasticity, a fall in export prices would leave the value of exports unaffected, while if the foreign demand were of less than unit elasticity, a fall in export prices would result in a fall, rather than a rise, in the value of exports.

However, it was generally believed by the classical writers that their assumptions concerning price elasticity were abundantly justified. Indeed, according to Alfred Marshall, the chances are exceedingly small that a country's demand for imports might be substantially inelastic with respect to price. "Nothing approaching to this," he wrote, "has ever occurred in the real world: it is not inconceivable, but it is absolutely impossible."^{1/} Language could hardly be more emphatic. It seems possible, however, that the foregoing dictum may have been as unfortunately phrased as Mill's famous remark concerning the finality of classical value theory. Recent statistical analysis, for what it is worth, simply does not bear out Marshall's statement; import price elasticities of less than unity, far from being impossible or even exceptional, appear to be fairly common.^{2/} Unfortunately, the relevant figures are available for only a few countries; the following discussion includes but three: the United States, the United Kingdom, and Sweden.

^{1/} Alfred Marshall, Money, Credit, and Commerce, Appendix J, p. 354.

^{2/} The reader is referred to J. H. Adler, "United States Import Demand during the Interwar Period," American Economic Review, June, 1945; J. Tinbergen, "Calcul du montant maximum transferable d'un pays," Société Belge d'Etudes et d'Expansion, Bimonthly Bulletin, May-June, 1946; and Randall Hinshaw, "American Prosperity and the British Balance-of-Payments Problem," Review of Economic Statistics, February, 1945.

It should be emphasized that the ensuing statistical findings are of a preliminary character. Except for a few remarks concerning the method employed, only the results are here presented.

In the classical adjustment mechanism, price is the dominant variable. The modern explanation of the adjustment process recognizes the importance of price changes, but also places emphasis on what the classical writers tended to ignore--namely, changes in income. The assumption underlying the statistical investigation here summarized is that variations in the volume of a country's imports can be adequately explained only in terms of both these variables. This assumption was tested by the method of multiple correlation, from which the estimates of import price elasticity were derived as by-products. For each of the three countries, quantum of imports, the dependent variable, was related to two independent variables, (1) the country's level of import prices, and (2) the country's national income. In the case of two of the countries, it was possible to cover the bulk of the interwar period; for the United States, the period covered is 1922-37 and for Sweden the period is 1923-37. In the case of the United Kingdom, only the years 1924 through 1929 were included because of the abrupt change in British commercial policy during the depression.^{1/}

From certain constants obtained in multiple correlation, it is possible to derive estimates of the average price elasticity of a country's demand for imports. For the three countries here studied, the computed elasticities, over the periods covered, are uniformly low. In fact, in each case, the estimated average price elasticity is below unity. For the United States, the figure is .48; for the United Kingdom, it is .67; and for Sweden, it is .61.

In each case, a high coefficient of multiple correlation was obtained for the periods covered; for the United States, the coefficient is .97; for the United Kingdom, it is .94; and for Sweden, it is .93. Also high in each case is the partial-correlation coefficient showing the degree of correlation between quantum of imports and the import price level after allowing for changes in the level of national income. As would be expected, this correlation in each case is negative, indicating that, at a given national income, the quantum of imports varies inversely with the import price level. For the United States, this coefficient is -.92; for the United Kingdom, it is -.94; and for Sweden, it is -.88. The fact that these multiple and partial correlation coefficients are high constitutes strong evidence that a country's volume of imports is primarily a function of its level of income and its level of import prices.

^{1/} The British indexes of import prices and import volume do not begin until 1924.