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THE BALANCE OF PAYMENTS OF BIZONAL GERMANY, 1947 AND 1948

J. Herbert Furth

The reports of Military Government and the Joint Export-Import Agency for 1947, and revised estimates of bizonal import requirements and export potentialities for 1948, make possible the presentation of balance of payments data for 1947 and 1948 on a basis more reliable than that of previous attempts. Interzonal trade is excluded from the discussion.

Development in 1947

In 1947, exports from the bizonal area totaled $225 million, and imports $674 million. Exports included the shipment of cotton goods under processing arrangements with the U.S. Commercial Company (USCC) and commercial transactions under the supervision of the Joint Export-Import Agency (JEIA). Imports consisted of noncommercial shipments of food, seeds, fertilizer, and petroleum products financed by U.S.-U.K. appropriations; shipments of raw cotton under the USCC arrangements; and commercial transactions under the supervision of JEIA. If noncommercial and commercial shipments are combined, the bizonal area had an import surplus of $449 million, but if only commercial exports and imports are considered, it had an export surplus of $185 million.

The transactions, together with the methods of financing them, are shown in the following table:

Balance of Payments, U.S.-U.K. Zones, 1947
(In millions of dollars)

Receipts

A. Current Account		
Exports of cotton goods		3 a/
Exports of coal	122	
" " timber	39	
" " other goods	36	
" " services	25	222
B. Capital Account		
Advances (U.S.-U.K. appropriations)		624
Advances (USCC agreement)		10
		859

Payments

A. Current Account		
Imports of food	525	
" " seeds	34	
" " fertilizer	41 b/	
" " petroleum products	24	624 c/
Imports of cotton		13 a/
Imports of other goods and services		37
B. Capital Account		
Increase in foreign exchange holdings		185
		859

a/ Under agreement with the U.S. Commercial Company.
b/ Figures for November and December estimated.
c/ Financed by U.S.-U.K. appropriations.

Although foreign trade in 1947 was substantially larger than in 1946,[1] its level has remained disappointingly low. Moreover, its composition was as far from normal as in the earlier year. Exports still consisted overwhelmingly of coal and timber rather than of industrial products. Imports still were confined almost exclusively to necessities of life, mainly foodstuffs. The importation of industrial raw materials remained at a mere trickle, and that of capital equipment at zero.

Of the noncommercial imports financed by U.S.-U.K. appropriations, shipments of $534 million took place in the first ten months of the year. Under the bizonal agreement of 1946, this sum was to be financed in equal parts by the two occupying powers. Noncommercial imports in November-December amounted to $90 million; the United Kingdom, under the amended bizonal agreement of 1947, was responsible for financing the equivalent of $34 million, while the United States assumed responsibility for the rest. Altogether, therefore, the noncommercial imports totaling $624 million were to be financed to the extent of $323 million by the United States and of $301 million by the United Kingdom.

The cotton-processing agreement with the U.S. Commercial Company proved unsatisfactory. Despite the world scarcity of cotton goods, sales lagged, and the indebtedness to USCC increased by $10 million during the year.

1/ See this Review, July 1, 1947, p. 4.

Various explanations for the low level of these exports have been given: reluctance of German processors to make products available for exportation rather than for more profitable domestic black market transactions; difficulties inherent in government management of foreign trade; and the necessity of asking for payment in U.S. currency.

Commercial exports (in addition to coal, timber, and services) consisted mainly of machinery, other metal goods, optical instruments, chemicals, ceramics, textile products, salt, and hops. Commercial imports included miners' clothing and other consumers' goods used as incentives for increased labor efficiency, lignite, pulp, textile fibers, rubber, and smaller amounts of various other industrial materials.

A breakdown of commercial exports and imports by countries is shown in the following table:

Commercial Exports and Imports, U.S.-U.K. Zones, by Countries, 1947
(In millions of dollars)

	Exports	Imports	Export Surplus
United Kingdom	55.4	16.3	39.1
Belgian-Luxembourg	34.8	0.9	33.9
Netherlands	23.7	2.4	21.3
France	22.8	0.6	22.2
Austria	21.4	0.5	20.9
Denmark	14.5	0.2	14.3
Italy	10.1	1.6	8.5
Norway	8.3	0.4	7.9
Sweden	6.9	3.9	3.0
Switzerland	6.7	0.3	6.4
United States	6.2	2.7	3.5
Other countries	11.2	6.9	4.3
Total	222.0	36.7	185.3

Commercial exports went primarily to continental Western Europe (68 per cent) and the United Kingdom (25 per cent), while the United States received only 3 per cent and Eastern Europe and the rest of the world about 2 per cent each. Commercial imports were supplied mainly by the United Kingdom (44 per cent), continental Western Europe (32 per cent), and Eastern Europe (13 per cent), with the United States furnishing 7 per cent and the rest of the world 4 per cent of the total.

The import pattern is quite different, however, if both noncommercial and commercial imports are considered. The great bulk of the imports financed by U.S.-U.K. appropriations (around $535 million) as well as all of the cotton imported under USCC arrangements was shipped from the United States; the United States therefore supplied almost 82 per cent of all goods actually imported by the combined zones.

The difference between the methods of financing noncommercial and commercial imports leads to interesting results in the relation between the bizonal area and the occupying powers. On the basis of commercial transactions, the combined zones had a small export surplus in relation to the United States, and a considerable one in relation to the United Kingdom. If noncommercial transactions are taken into consideration, however, the bizonal area had a moderate deficit in relation to the United Kingdom, and a formidable one (about $545 million) in relation to the United States. Since noncommercial imports from other areas were of minor importance, they did not greatly influence the bizonal balance of trade in relation to the rest of the world: the bizonal area had a large export surplus in relation to continental Western Europe, and moderate deficits in relation to Eastern Europe and to the rest of the world.

Purchasers of German goods are required to pay for their trade balance in U.S. currency. The excess of commercial exports from the bizonal area therefore means a substantial dollar drain for Western Europe. Under the bizonal agreement of 1947, even the United Kingdom will have to make such payments in U.S. currency, despite the fact that its noncommercial shipments to the combined zones, to be financed by appropriated funds, will continue to exceed its deficit in regard to commercial transactions. In 1947, the hard currency drain was greatest for the Benelux countries ($55 million), and considerable in the cases of France, Austria, and Denmark. In the future, it may be possible for these dollar payments to be met from funds allocated to Western European countries under the European Recovery Program. Moreover, the export surplus to France will be reduced by the recent tripartite decision to grant France priority for coal exports from the Saar, and to curtail accordingly coal exports from the combined zones (Ruhr). In the case of Austria, expanded sales of electric power and fertilizer to the combined zones may bring trade somewhat more into balance.

Estimates for 1948

The outlook for 1948 is more promising for Western Germany than the figures for 1947 would indicate. Noncommercial imports of necessities, financed by U.S.-U.K. appropriations, will continue at a somewhat higher rate than in 1947. The European Recovery Program tentatively provides for the importation of foodstuffs, seeds, fertilizer, and petroleum products of about $750 million annually (including freight charges). Under the new bizonal agreement, the United Kingdom will contribute $88 million, and the United States will assume responsibility for the remainder.

In addition, the Joint Export-Import Agency finally has decided to put into use its accumulated funds, including the $121 million original contribution of the United States and the United Kingdom[1] and the $185 million surplus arising from commercial trade in 1947. Net of liabilities for current payments of about $60 million, these funds reached on January 1, 1948, the equivalent of $240 million, of which $50 million and £25 million were in cash, and the remainder (mainly U.S. dollars) in claims for unpaid exports.

The Agency has announced that it would finance imports of raw materials and consumer goods of $100 million in each of the first two quarters, and even larger amounts in the third and fourth quarters of 1948.

1/ See this Review, January 28, 1947, Supplement, p. 11.

It should not experience any difficulty in financing annual imports of \$500 million out of its liquid funds and current earnings, and by the end of the year actually should hold somewhat larger funds than at the beginning. Such imports, although still far below normal, would be ten times as large as commercial imports in 1947.

Finally, the European Recovery Program tentatively provides for the importation of steel and machinery, mainly transportation and mining equipment, which will enable the bizonal area to reemploy its productive facilities for the benefit of the entire European economy. If shipments in 1948 approximate three-fifths of the quantities proposed for the first fifteen months of the Program, their value may be estimated at \$150 million. It is assumed that credit arrangements, including allocations of ERP funds, will be made in order to finance these imports.

Under these assumptions, all imports, including those to be financed by U.S.-U.K. appropriations, the use of JEIA funds, and other credit arrangements, would reach an estimated total of \$1,400 million, or more than twice the amount of total imports in 1947.

As a result of the importation of raw materials and equipment, exports may be expected to increase at least as rapidly as imports. By the last quarter of 1947, exports of coal, timber, and services had reached an annual rate of \$270 million, and export <u>contracts</u> for goods other than those just mentioned an annual rate of \$330 million. In January 1948, further advances were made. Experience shows that only about 10 per cent of the contracts is canceled, and that the remainder is executed within less than a year. If performance in 1948 corresponds to that pattern, total exports (including services) can be expected to rise from \$30 million per month at the beginning of the year to more than \$60 million at the end, making a total of about \$550 million. This sum would be lower than the estimates contained in the ERP country report, but 145 per cent above 1947.

On the basis of these assumptions, the balance of payments of the bizonal area for 1948 might be estimated as follows:

Estimated Balance of Payments, U.S.-U.K. Zones, 1948
(In millions of dollars)

Receipts

A. Current Account		
Exports of coal	225 a/	
" " timber	45	
" " other goods	250	
" " services	30	550
B. Capital Account		
Advances (U.S.-U.K. appropriations)		750
Other advances		150
		1,450

Payments

A. Current Account		
Imports of food	640	
" " seeds	35	
" " fertilizer	45	
" " petroleum products	30	750
Imports of raw materials and consumer goods		500
Imports of equipment		150
B. Capital Account		
Increase in foreign exchange balances		50
		1,450

a/ The increase over 1947 will be due primarily to a rise in coal prices decreed in September 1947.

The trade pattern of the combined zones is likely to undergo considerable change in 1948. Exports will include, in terms of value, about as large an amount of manufactured products as of raw materials. Although most of the exports are expected to go to Western Europe, as they did in 1947, the geographical distribution will be less markedly dominated by the need of the purchasing countries for Ruhr coal. Imports will include about as large an amount of raw materials and capital goods as of foodstuffs, and the predominance of the United States as a source of supply is likely to diminish. As a result, both the bizonal import deficit with the United States and the export surplus in relation to Western Europe are likely to be slightly reduced. In view of the expected doubling of the total volume of foreign trade, however, the aggregate import deficit also will be about twice as great as in 1947.

The tentative nature of these estimates is obvious: the bizonal area easily could import and utilize far greater amounts of foodstuffs, raw materials, and capital equipment, if larger sums were available, either under appropriations or other advances (including ERP allocations) or because of more liberal spending of JEIA funds. Moreover, the total volume of trade might be expanded without an increase in the deficit on current account, if the allocation of ERP funds to other European countries induced these countries to step up their purchases from the bizonal area at a more rapid pace. On the other hand, the lack of free trade between the combined zones and the Soviet zone, as well as delays in carrying out the currency reform and an adjustment of the German price system to the world market level, probably will continue for some time to retard the expansion of economic activity.

"FRANCO VALUTA" IMPORTS IN FRANCE

Albert O. Hirschman

On February 13, the French Exchange Control Office issued a decree (Avis No. 299) introducing in France a special form of private barter or compensation system similar to that which had been developed since the end of the war in Italy under the name of "franco valuta" imports.1/ According to the decree, importation of a wide range of goods is permitted without licensing, provided that such imports "do not give rise to any financial settlement between France and abroad." In other words, imports of certain commodities are authorized provided that they do not result in a foreign exchange outlay on the part of the Exchange Control Office, but can be financed independently from such sources as imports of foreign capital, repatriation of French capital held abroad, foreign tourists' expenditures, etc.

Only two categories of commodities are excluded from the benefits of such arrangements; these are commodities subject to international allocation and certain goods included in a special list B annexed to the decree. The goods on this list are in the main luxury goods, such as furs, passenger automobiles and all articles subject to luxury taxes.

The admitted commodities also fall into two categories: those specified in list A which can be imported without import license, and all other commodities (except those in list B) for the importation of which licenses are still required. Licenses for these commodities will be forthcoming generously, according to official assurances. List A contains a wide range of food products (including such non-essentials as fruits, coffee, tea, pepper), practically all types of industrial raw materials, semi-finished products, and agricultural and industrial machinery. The goods for which licenses are required are therefore mainly finished consumers' goods other than foodstuffs.

By relaxing previous restrictive regulations the Italian Government, in the fall of 1947, caused a large inflow of franco valuta imports of fats, meat, and sugar which was one of the principal factors in the fall of Italian prices after October 1947. The French move certainly was largely inspired by that successful experience, but from the outset the French system has been placed on a scale broader than even the most liberal form of the oft-revised franco valuta system in Italy.

After the establishment of the controversial dual rate system for the dollar (one of whose principal objectives was to attract capital—foreign and French—from abroad2/), the introduction of the franco valuta system by the French has been widely interpreted as an admission of failure of the "free" dollar market to result in any appreciable repatriation of capital. This theory, however, seems suspect if only on the grounds that bureaucracies do not, as a rule, recognize their mistakes so quickly. It seems more likely that the new French move was motivated less by the desire to add a set of franco valuta rates to the existing dual franc-dollar rate than by the determination to create dual rate systems for the currencies

1/ See this Review, May 6, 1947.
2/ See this Review, February 10, 1948.

of those countries with which it has proved difficult or impossible to agree on "free" market arrangements--mainly Belgium and Switzerland. Since the currencies of both countries commanded substantial premiums in the French black market, substantial exchange receipts from Belgian and Swiss tourists and other invisible transactions failed to accrue to the Exchange Control authorities; there has also been capital flight to both countries[1] and payments difficulties have led to interruptions in the flow of imports. The new measure, unlike the "free" market system, applies equally to all currencies; it will, therefore, facilitate the conversion of flight capital, tourist receipts, etc., from Belgium and Switzerland into imports useful for the French economy. As a matter of fact, there is little the free market for Belgian notes as originally proposed by the French Government[2] would have done that will not be accomplished by the new system.

Furthermore, the franco valuta system is likely to be more successful than the open market in encouraging repatriation of capital. Because of the more liberal import regulations under the franco valuta system, the rates offered to holders of foreign exchange by franco valuta importers presumably will be more favorable than those offered by bidders in the open market. Still another advantage of the new system, from the point of view of the holder of flight capital, is the absence of any provision concerning the 25 per cent tax on repatriated capital which is imposed if repatriation proceeds via the "free" market.

What the franco valuta system does not accomplish is to provide an additional devaluation for purposes of promoting French commodity exports. Such a devaluation was desired with respect to the Swiss franc and agreement has now been announced on the establishment of an open market for the Swiss franc in Paris where 50 per cent of the proceeds from exports to Switzerland can be sold.

Insofar as the dollar is concerned, it is likely that henceforth any capital repatriation will take place through the franco valuta system rather than via the open market and that a new franco valuta rate--higher (in terms of francs per dollar) than the open market rate--will emerge. The exchange rate is of course implicit in, and may be different for, each compensated transaction, but commodity arbitrage is likely to operate toward a nearly uniform rate for franco valuta transactions; the black market rate for bank notes may serve as an approximate indicator of this rate. In this connection, it is of interest to note that in the week following the introduction of the franco valuta system the black market rate for one dollar rose from 317 to 335 as against a rate of 305 in the "free" market.

No consideration seems so far to have been given to the question whether the establishment of the franco valuta system which definitely affects the French exchange rate structure called for consultation with the International Monetary Fund.

1/ See this Review, December 2, 1947, p. 7.

2/ The proposal differed from the open market arrangement in effect for the dollar and escudo in that it did not provide for the sale of half of the export proceeds in the open market.

PROPOSED INTERNATIONAL WHEAT AGREEMENT

Wilellyn Morelle

Representatives of 36 nations became signatories to an international wheat agreement at an open session of the International Wheat Conference on March 5, 1948. If the agreement is approved by Congress and by the appropriate legislative bodies in the other countries, it will prove a milestone in a series of negotiations which have been carried on for two decades. On only two other occasions have negotiations resulted in an agreement: (1) the agreement of 1933 among 21 countries which operated for one year, and (2) the memorandum of agreement signed by five countries in 1942 which has operated on an advisory basis up to the present time. Argentina, the Danubian countries, and the U.S.S.R.--all members of the 1933 agreement--do not participate in the present agreement. Of these exporting countries Argentina is probably the only one with potential exports large enough to threaten the success of the agreement, although offers of wheat from Eastern Europe could contribute to pressures for breaking the agreement or revising its terms. Since all of the important importing countries are members of the agreement, Argentina may find herself with a reduced market for wheat and consequently may ask to become a member.

The present agreement provides more flexibility than the 1933 agreement and the Draft Agreement which failed of ratification at the London Conferences in the spring of 1947. For this reason and also because it can be coordinated with the Marshall Plan, it should have a good chance to operate successfully, although it is necessarily based in part on expectations of crops and of general economic and political conditions which may or may not prove realistic.

Provisions of the 1948 agreement

The agreement provides for guaranteed purchases on the part of the 33 importing countries of 500 million bushels of wheat per year for the next five years from the three exporting member countries. Imports of these 33 importing countries in the 1945-46 season exceeded 600 million bushels. The exporting countries are to make the 500 million bushels available at a price which shall not exceed $2.00 per bushel during the life of the agreement. On the other hand, the "agreement price" shall not be less than $1.50 for the first crop year 1948-49; the minimum price shall decrease thereafter by 10 cents each year. Thus in the last year of the agreement--1952-53--there is provided a range of 90 cents within which free-market prices may fluctuate.1/ Annual quotas or "guaranteed sales" of the exporting countries are divided as follows: Canada, 230 million bushels; United States, 185 million bushels; and Australia, 85 million bushels. The quota of 185 million bushels for the United States contrasts sharply with her quota of 47 million bushels under the 1933 agreement. Argentina, which had a quota of 110 million bushels in the 1933 agreement, and the Danubian countries, with quotas amounting to 50 million bushels, are not participating in this agreement. The sales figure guaranteed for the United States excludes requirements for occupied areas, which in the current season are

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1/ Prices quoted are in Canadian currency at the par value for the Canadian dollar on February 1, 1948. They refer to No. 1 Manitoba northern wheat in store Fort William-Port Arthur.

estimated at 115 million bushels and which in later years will probably be less. Total exports from this country during the present season (ending June 30) will probably amount to 450-500 million bushels; exports before the war averaged around 50 million bushels. Larger exports in recent years have been made possible by exceptionally high yields per acre, and to some extent by expansion of acreage beyond what may prove desirable in terms of soil conservation. A high volume of exports has been required in considerable part because production in importing countries has been low. It now seems likely that in the first season to which the proposed agreement would apply, the United States will have a crop fully large enough to meet the commitment of 185 million bushels and to provide wheat required for occupied areas without drawing down the carryover.

Annual quotas or "guaranteed purchases" of the principal importing countries are as follows: United Kingdom, 180 million bushels; Italy, 37; France, 36; Netherlands, 31; India, 28; Belgium, 26; Brazil, Greece, and Austria, 19 each; the 24 other countries, 109 million bushels.

During the first year of the agreement, the U.S. support price may be as much as 30 cents a bushel higher than the maximum price provided in the agreement. Any difference between the domestic price and the export price under the agreement will presumably be absorbed by the Government; at the same time, however, grants for wheat exports under the Marshall Plan will be lower than would have been the case in the absence of the agreement.

The agreement provides for the establishment of a new International Wheat Council. In addition to one delegate from each member country, the Council will have one non-voting representative each from the FAO and the ITO and, temporarily, a non-voting representative from the Interim Coordinating Committee for International Commodity Arrangements, established by the Economic and Social Council of the United Nations. The delegates of the importing countries will have 1,000 votes distributed according to the size of their annual guaranteed purchases. The delegates of the exporting countries will also have 1,000 votes pro-rated according to the size of their guaranteed sales. The Council is to meet at least twice a year and will be organized at a meeting of the representatives of the member nations which is scheduled to be held in July 1948. An Executive Committee, in which both importing and exporting countries will have equal voting power, will perform those functions delegated to it by the Council.

Any member country may apply to the Council for adjustment of its obligations. If an exporting country, for instance, is embarrassed by a short crop, the Council may ask the other exporting countries to assume part of its quota. If this is not possible, the Council may reduce the total quotas of the importing countries for the year by the amount of the deficiency expected in the guaranteed sales of the exporting countries. In case of an emergency need for a greater amount of wheat on the part of any country than that stipulated in the agreement, the Council may, by two-thirds vote of the importing countries <u>and</u> by two-thirds vote of the exporting countries, reduce the guaranteed purchase of the other importing countries on a pro-rata basis and channel this wheat to the emergency area.

The Council may assist exporting or importing member countries in making additional sales or purchases as the case may be but neither the circumstances nor the terms of such transactions are specified in the agreement. Exporting countries may export wheat at special prices for use in nutritional programs approved by the FAO as long as the full guaranteed demand of the importing countries is met at the minimum price specified for the period under the terms of the agreement.

The exporting countries are required to have on hand at the end of their respective crop years, stocks of old wheat amounting to 170 million bushels (including farm stocks) for the United States and 70 million bushels and 25 million bushels respectively for Canada and Australia (excluding farm stocks). These stocks may be drawn below the minimum specified if the Council decides that the wheat is needed to meet domestic requirements of the exporting countries or the guaranteed imports of the importing countries. In addition, all member countries, except those who are predominantly importers of flour, may be required, under appropriate conditions, to accumulate price stabilization reserves up to 10 per cent of their guaranteed annual purchases or sales. Member governments are to accumulate reserves at the world price when the free-market price is below the minimum "agreement price" prescribed for the year and are to sell or use their reserves when the price is above the basic price range.

The agreement may be amended by a simple majority vote of the importing nations (subject to a favorable vote by the United Kingdom) together with unanimous accord of the exporting countries--United States, Canada, and Australia. Any importing country that does not accept an amendment may withdraw after giving due notice, but it must fulfill all commitments for that crop year. At the first meeting of the Council established under the 1948 agreement, any member will be given an opportunity to withdraw if it feels that not enough countries have ratified the agreement to assure its successful operation. In the event that a country considers that its national security is threatened by the outbreak of hostilities it may withdraw from the agreement. Admission of new members to the agreement is subject to unanimous vote of the Council and to such conditions as the Council may require.

Background of the wheat agreement

Experiments with international commodity agreements began as early as 1902 with an inter-governmental sugar agreement. Since that time approximately 16 commodities have been subject at one time or another to inter-governmental agreements. Only six of these have operated for as long as five years continuously. The high tide of commodity agreements from the standpoint of range of commodities and volume in world trade was the period 1937-39. Among the agreements, only those relating to sugar and wheat have included large representation of consuming countries in their membership.

Efforts to promote international measures to obtain the orderly production and distribution of wheat began in 1927 with the convening of a world conference in Rome. No agreement was reached at this meeting. Government intervention to protect domestic growers became more widespread in the late 'twenties and the early 'thirties as world wheat surpluses multiplied, and the need for a multilateral inter-governmental agreement became increasingly urgent. In the period from January 1930 to September 1932, there were 21 international meetings and conferences in Europe concerned with the problem of wheat surpluses. The tangible results of these conferences were negligible. Yet they contributed to a common understanding of the wheat situation and gave rise to numerous suggestions for international measures which later crystallized into certain lines of action.

In August 1933 an agreement was reached in London among 21 exporting and importing countries. All the exporting countries agreed to accept quotas which were to be reduced in the second year of the agreement (1934-35) and the four overseas exporting countries agreed to reduce acreage or production--a point not clearly defined--in the 1934 crop year. The importing countries agreed to discourage domestic production, to encourage increased consumption of wheat, to reduce tariffs under certain conditions relating to price and to accept in principle the desirability of relaxing certain trade restrictions. Finally, the signatory countries agreed to set up a wheat advisory committee in London with power to convene a general meeting when it saw fit.

Experience with this agreement was disappointing in almost every respect. The loose wording of the commitment to reduce acreage or production inevitably led to misunderstandings among the four overseas exporting countries. Argentina, faced with an unexpectedly high yield of wheat and little popular support for the agreement, exported more than her quota. Both the United States and Australia failed to meet their quotas. largely because of crop failures. Efforts to revise and strengthen the arrangement for the second year won the support of nearly all the member countries. As a result of Argentine rejection of all compromise proposals offered, however, the agreement was permitted to lapse. The Wheat Advisory Committee continued to meet in London from time to time.

Although weather and crop conditions thus contributed to the breakdown of the scheme, the 1933 agreement may well have been too ambitious. Member nations signed an agreement which committed them to lines of action within their domestic economies which their people were not prepared to support. Neither the importing nor the exporting nations had administrative machinery ready to carry out those provisions of the agreement designed to remedy long-run maladjustments in production. In addition, the farmers of the member nations were not inclined to give up the protection afforded by trade barriers, some of which had been set up only a short time before.

A succession of bad crop years in the United States and Canada from 1933 through 1936 brought about a readjustment in world wheat stocks and prices such as the agreement had been designed to achieve. A recurrence of a world wheat surplus in 1938 gave impetus to efforts to draw up another agreement. Negotiations directed to that end were interrupted by the outbreak of the war in 1939.

Two years later at the invitation of the U.S., representatives from Australia, Argentina, Canada, and the United Kingdom resumed discussions in Washington and entered into an interim agreement to be effective throughout the war and not more than two years thereafter. An International Wheat Council was set up in Washington as part of this agreement and has met twice a year since that time. As events have turned out, most of the problems concerning the distribution of wheat and flour in recent years have been handled by the Combined Food Board, which was established in 1942 to coordinate food supply programs, and by its successor, The International Emergency Food Council. A pool of wheat set up for relief feeding by the 1942 agreement was turned over to UNRRA and the Wheat Council devoted itself to policy planning for the future.

An International Wheat Conference was convened in London in early 1947 to prepare a draft agreement, but broke down on the question of maximum prices. The United Kingdom refused to sign because the prices specified were believed excessive. Argentina also had indicated that it would not become a party to the agreement.

If the 1948 wheat agreement is approved, it will provide a test, but because of the unusual conditions prevailing only a very partial test, of the extent to which nations have learned to cooperate in this field.

Conclusion

Historically, international commodity agreements have for the most part represented producer combines interested in stabilizing prices at the highest possible levels with little concern for consumer interests. In the 1948 wheat agreement, with 33 importing countries out of the 36 member countries, and with substantial voting power for the importing countries, the consumers' point of view is well represented. Such representation should assure a more equitable price range than has obtained for most commodity arrangements of the past and also more reasonable adjustments to unforeseen changes in conditions. Since the Council has considerable discretionary powers and provision is made for amendment, the agreement may prove adaptable to periods of easy supply.

In achieving flexibility the 1948 agreement has lost many of the characteristics of international commodity agreements as set forth in the proposals of the FAO and the ITO. Also, this agreement--more in the nature of a commercial contract with a price stabilization feature--has a considerably narrower scope than previous proposals. This limitation may actually enhance its chances of survival.

Because a price range has been agreed upon and quotas have been accepted by the importing countries which in many cases are less than their total import requirements, the door has been left open for considerable trade in the free market. The unpleasant remedies which are necessary to cure chronic over-production no longer appear in the agreement although they are implicit in its terms. Among the measures dropped are clauses providing for reduction of acreage and production, limitations on the accumulation of stocks, abolition of protective devices which foster uneconomic production, and the encouragement of increased consumption. The sacrifice of long-run adjustment commitments which was necessary to achieve an agreement at all will have no immediate consequences. Yet after production returns to normal in the war-stricken areas the problem of over-production may recur. If the 1948 agreement is adopted and if the member countries are satisfied with its performance, they may subscribe to a more ambitious pact in the future.

NOTES ON INFLATION IN CHINA AND JAPAN

Arthur B. Hersey

Acceleration of the Chinese inflation became an accepted fact in 1947. The Shanghai wholesale price index, for example, which had doubled in six months from the spring of 1946 to the autumn of that year and had increased 2½-fold in the next six months, quadrupled between April and October 1947.1/

This acceleration is continuing. In the five months since last October the Shanghai wholesale price index has increased 5½-fold already. An extraordinarily sharp rise set in after the Chinese New Year holidays in the second week of February. On March 11, when the black market rate for the U.S. dollar first touched half a million yuan, which is nearly 150,000 times the prewar exchange rate, the Shanghai wholesale price index reached 333,000 times prewar.

Chinese Price and Exchange Rate Indexes

	Shanghai wholesale price index a/ (1)	Black market rate for U.S. dollar		Ratio of indexes (1) ÷ (3)
		CN dollars (2)	Index on prewar exchange rate b/ (3)	
May 31, 1946	4,160	2,330	690	6.0
June 29, 1946	3,700	2,650	790	4.7
October 30, 1947	61,600	83,000	24,600	2.5
November 27, 1947	73,400	148,000	43,900	1.7
March 11, 1948	333,000	490,000	145,000	2.3

a/ January-June 1937 = 1.
b/ January-June 1937 (CN$3.37 per US$1) = 1.

Food prices, and commodity prices generally, increased much faster beginning in December than black market dollar rates and the price of gold. In the earlier years of the Chinese inflation there had been a general tendency for the commodity price inflation to run ahead of the external depreciation of the currency. This tendency was reversed from the summer of 1946 through November 1947, primarily because of a substantial flow of imports paid for at relatively favorable official exchange rates or obtained free by the Chinese Government through UNRRA. On the other hand, traders attempting to convert their earnings into assets abroad were putting heavy pressure on the black exchange market during that period and are continuing to do so. The recent stepping up of the rate of commodity price inflation probably reflects a real accentuation of the flight from the currency. A significant increase in the velocity of circulation of money seems to have taken place, indirect confirmation of which is given by press reports to

1/ See this Review, December 2, 1947.

the effect that high officials are thinking of publishing the figures of note circulation. The amount of money in circulation is said to be lower than has been generally rumored.

Some shutdowns and layoffs in Shanghai industry have been reported. While the monthly adjustment of wages to the steeply rising cost-of-living index creates a special problem for employers, shortages and hoarding of materials appear to be the main cause of this industrial contraction. Underlying this development are (1) increased disruption of internal trade by the civil war, (2) a tightening of import licensing policy forced by the decline in official foreign exchange assets, and (3) expectations of continuing inflation.

The Japanese price level has been rising steadily, at a rate of two-and-a-half to three times in the course of a year. Efforts to balance budgetary receipts and expenditures have not succeeded and the Bank of Japan note issue reached 219 billion yen at the end of 1947, 135 per cent above the figure for December 31, 1946.

Indexes of Money and Prices in Japan
(December 1946 = 100)

	1945	1946			1947		
	Dec.	Mar.	Sept.	Dec.	Mar.	Sept.	Dec.
Money indexes							
Bank of Japan note issue	59	25 e/	69	100	124	168	235
Note issue and ordinary banks' "new account" deposits	n.a.	n.a.	70	100	115	152	n.a.
Price indexes							
Bank of Japan retail a/	n.a.	43	79	100	107	199	334
Consumers (SCAP) b/	n.a.	n.a.	88	100	141	232	f/
"Free and black market" c/	64	92	84	100	175	260	294
Bank of Japan wholesale a/	n.a.	51	87	100	113	286	381
"Actual capital goods" d/	n.a.	n.a.	97	100	152	279	317

n.a. = not available.

a/ Indexes recently revised by the Bank of Japan.

b/ Based on sample survey ratios of total cost to quantity purchased whether in official or free market.

c/ Tokyo Chamber of Commerce and Industry.

d/ Bank of Japan.

e/ Just after currency exchange.

f/ November index was 256.

In the table various available indexes have been placed on a uniform base of 100 for the end of 1946. Very little is known about the composition of some of these indexes, but the Bank of Japan wholesale and retail indexes are derived from official rather than black market prices, and they may overstate the rate of price inflation during 1947 because of changes in official prices which brought them more nearly in line with the black market than at the end of 1946. Very substantial revisions were made in wholesale textile prices in September and the price of rationed rice to the consumer was raised by 50 per cent on November 1, 1947.

Various indexes which give comparisons with prewar dates indicate that the Japanese price level in December 1947 was 85-95 times the level of 1930 or 1933-36, without allowance for still higher black market prices. In 1930 the yen was valued in the foreign exchange market at 49+ cents and in 1933-36 at about 29 cents. Purchasing power parity calculations using the increase in U.S. average wholesale prices (90 per cent from 1930 and 116 per cent from 1933-36), would place the nominal value of the yen at the end of 1947 in the range of one-hundredth to one-hundred-and-fiftieth of a U.S. dollar. A commercial exchange rate has not been fixed. No alteration of the military rate has been made since March 1947, when this rate was changed from 15 yen to 50 yen per dollar.