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INVESTMENT AND BUDGETARY POLICY IN WESTERN EUROPE

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Investment has a particularly crucial role in the European Recovery Program. In fact, the success of the Program will ultimately be determined by the investment efforts of the European countries. Achievement of viability rests upon the investment programs. But investment generates income, and the additional income could generate inflation during the life of the Program and maintain consumption at "excessive" levels. Further, OEEC countries estimate levels of investment in 1952-53 substantially in excess of private savings. A budget surplus--the so-called policy of "disinflation"--is often recommended as a means of ensuring stability under those conditions. After considering the limitations of this policy, the present note suggests that the policy of a budget surplus is at least a necessary step in the direction of monetary stability.

One model of the Recovery Program which highlights the significance of investment can be constructed on the assumption that European consumption cannot be reduced sufficiently to secure immediate external equilibrium. Only if there is a lower limit to consumption can balance-of-payments disequilibrium appear as a general problem, since equilibrium could theoretically always be effected through reduced consumption. With consumption a variable with a fixed

lower limit, it follows that the principal objective of the Program is so to rehabilitate and expand European capacity that these countries will be able to maintain consumption without external strain. Only by an adequate increase in capacity growing out of investment can this goal be achieved.

The current excess of investment over internal savings is consistent with the model. No peculiar danger of inflation arises where foreign aid provides external resources to accommodate the excess investment. Balance-of-payments equilibrium is attained by dollar aid and resource equilibrium is provided internally by foreign aid goods. But American aid is to decline progressively to final elimination in 1952-53. At the same time, the expanded capacity growing out of investment will lead to a steady rise in national real income up to 1952. ^{1/} Thus, real income will increase over the life of the Program, to be offset by the elimination of the excess of imports over exports. A necessary, though not sufficient, minimum condition for achieving viability is that the increment in real income by 1952 be equivalent to the eliminated external deficit. ^{2/} More precisely, the increment in real income must offset the current foreign deficit plus any rise in real consumption by 1952. The greater consumption increases above current levels, the greater the increment in real income should become.

Consumption is now at levels inconsistent with external balance. More important, however, the investment process as it continues over the life of the Program will bolster money income and, hence, tend to maintain or expand consumption. Is there not danger, then, that investment will maintain consumption at "excessive" levels throughout the Program and that European countries will find viability in 1952 impossible without adjustments not now contemplated? In other words, may not the rise in real income be insufficient to offset both the eliminated foreign aid and the additional consumption resulting from higher incomes?

Differentiating between the income-effect and the productivity-effect of investment helps to make clear the process by which investment generates inflationary pressures and tends to support consumption. The income-effect points to the added money income paid out of investment expenditures: the income distribution begins as soon as the project gets under way. The productivity-effect, by contrast, points to the added capacity and--with a time-lag--the added final products accruing from the project: the additional products do not appear until the project is completed or for some time afterwards. The time-lag between the instantaneous increment to money income and the eventual addition to finished goods supply underlies the expansionary pressure associated with investment.

^{1/} Individual country programs estimate increases in national income of about 35 per cent above the 1947 level and 20 per cent over the 1938 figure. However, the OEEC Interim Report believes that these estimates are overoptimistic.

^{2/} This reasoning is based upon the assumed model. Clearly, alternatives are available. Even within this model, viability could still be achieved in 1952 by a reduction in consumption, and resource equilibrium by elimination of a sufficient portion of investment in excess of internal savings.

The inflationary pressures associated with the investment process are aggravated by conditions found in Western Europe. The inflationary pressure is at a minimum where supplies of consumer goods can expand at a pace to absorb the money income generated by investment. The parallel expansion of consumer goods output and investment activity is facilitated where idle resources are available in sufficient volume. The mere existence of idle resources is insufficient to minimize inflation, as several continental countries discovered in programming high levels of investment without providing enlarged supplies of consumer goods. Where resources are fully employed, however, investment activity and consumer income compete for available resources and price tension results. Further, the productivity-effect of investment can create additional real income more easily where idle resources are available than under full employment conditions. With full employment, increases in real income occur only to the extent that more efficient resource utilization takes place. In Europe, despite full employment, productivity-growth has been facilitated by transfer of labor from employment with limited productivity; but frictions restraining the continuous rise in productivity may become more powerful as investment proceeds. The danger of a "production plateau"--with total production and productivity increases expanding at a diminishing rate--has already begun to emerge in many countries. Here again, pressure on prices grows as income continues to expand and the rate of productivity increases begin to decline. These inflationary pressures are intensified in that these countries continue to wage more or less successful battles to contain a large volume of wartime and post-war purchasing power which continues to exert pressure on prices and wages.

The Problem of "Excess" Investment

The additional income generated out of high levels of investment helps to explain why the European countries have thus far been more successful in expanding output than they have been in approaching monetary stability. But an investment program, however large, ought to create monetary difficulties only when investment is not offset by private savings. Consumption, already "excessive", appears to have risen substantially in 1948, in part as a consequence of unusually favorable domestic harvests last fall. Accompanying this rapid rise in current consumption is the general shortfall in internal savings. These two related phenomena are aggravating monetary instability and begin to emerge as grave dangers to the viability goal.

Specific evidence that current consumption is rising rapidly is difficult to accumulate, especially with the wide disparities in consumption patterns and levels found in the seventeen ECA countries. The OEEC Report suggests that average consumption in 1948 was perhaps around 20 per cent below that of 1938. This is an average of many countries; consumption in some is near the pre-war level and in others well below the average. If the national programs were successful, average consumption per head in 1952-53 might be very little below the 1938 level and very appreciably above those in 1948. The Report concludes that the objectives cannot all be achieved within the life of the Recovery Program and that a level of consumption some 5 to 10 per cent above that of 1948

might be consistent with external aid. ^{1/} Estimates of consumption in 1952-53 are highly preliminary and calculations of the increase in 1948 levels which would be consistent with viability in 1952 are most uncertain. The more successful the investment programs prove to be in expanding capacity and output, the less the need to restrain consumption is likely to be. With money incomes to continue at high levels, however, excessive absorption of real income into consumption is a continuing threat and a major preoccupation of policy.

Even if the rise in consumption is limited to the reduced calculations of the OEEC, pressure on internal resources in 1952 will be significant. Indicative of the problem is the considerable shortfall in savings expected in 1952 by the ERP countries as shown in the table. Investment is estimated by most countries at about 20 per cent of gross national product or more; however, for the few countries for which data are available, savings estimates appear to be clustered mainly in the 11.5 to 13 per cent range. These savings estimates appear to include total expected private savings, including corporate. The percentage excess of investment over savings of from 7 to 9.5 per cent of gross national product is substantial.

TABLE I

OEEC Countries: Estimates of Savings and Investment
as Per Cent of Gross National Product, 1952-53

	1952-53	
	Investment Per cent	Savings Per cent
Austria	14	-
Benelux	19	-
Denmark	20	-
France	20	12
Greece	-	8
Ireland	19	11.5
Italy	12	-
Norway	26	12
Sweden	24	-
U. K.	20	13
Bizone	23	-
French Zone	^{a/} 9	5

^{a/} To be revised

^{1/} Op. cit. pp. 103-105.

The need to maintain stability in the face of the gap between investment and expected private savings, both prospective and current, has stimulated interest in the possibility of using a government budget surplus--the policy of "disinflation", after the British model--for this purpose. Disinflation has the attraction of arithmetic simplicity, and several countries have already embarked upon this line of action. Thus far, the United Kingdom, Denmark and Norway among the ex-belligerent countries have been conspicuously successful in beginning such a program. Among the neutrals, Sweden, Switzerland and Portugal report budget surpluses, although the present program is hardly adequate in Sweden.

In the remaining European countries, however, the governments have not yet achieved, nor in 1949 plan to achieve, budget surpluses, although a surplus is the eventual aim of fiscal policy in several of them. ^{1/} At present, government deficits are continuing along with shortages of private savings. As a result, progress toward financial stability continues at a slow pace. In reviewing wholesale price trends in 1948, as reflected in official indexes, prices have been rising rapidly in France and Greece, moderately in Bizone and to a lesser extent in Belgium. Despite controls, prices have risen somewhat in the Netherlands. Following persistent rises in the preceding 21 months, prices appear to have been leveling off in Ireland since the end of 1947. Italy is the only country where a large budget deficit has been associated with a remarkable degree of stability in the course of 1948.

It is undeniable, however, that progress toward monetary stability was made during 1948; moreover, the new budgets provide, without exception, for reduced deficits, and a balance or surplus is being approached, however long this difficult road may prove to be.

The Attractiveness of Disinflation

Faced with a shortfall of private savings and with a desire to maintain investment at projected high levels, many consider that the policy of surplus-budgeting or disinflation provides a convenient means of coping with excess investment. Such a policy of course requires a profound change in official Treasury thinking on budget planning. For the budget is normally designed to finance government operations and, perhaps, reconstruction and particular public projects. Thus, a compensatory fiscal policy, geared to conditions of inflation rather than deflation, marks a long step away from traditional Treasury thinking. However, the easy arithmetic by which stability is effected with a budget surplus plus private savings combined to equal projected

^{1/} The deficit in many of these countries is due to heavy government investment expenditures, for the current "ordinary" budgets of most countries in this group are already in balance. Excess government investment expenditures, accompanied by shortages in private savings, result in serious inflationary pressures.

investment makes the emphasis currently placed upon the disinflation policy explicable.

In a situation where intended consumption plus intended investment is greater than current production at existing prices, savings would normally be equated with investment through "forced" savings brought about by rising prices. Prices rise as resources are diverted to producer goods industries and consumer goods supply is insufficient at prevailing prices to satisfy disposable income. With incomes trailing prices, consumption would be effectively curbed by the price rises. To forestall the cumulative generation of inflation, the weapons of monetary policy--including general credit restriction or selective credit controls and perhaps higher interest rates--would normally be brought into play. Yet it is widely thought difficult to utilize instruments of credit control without the risk of reversing the direction of the economy. To be effective, the credit policy would have to restrain investment, and the restraint on investment could easily end in unemployment and a substantially reduced volume of investment: the emergence of sharply curtailed investment as a result of the credit restrictions in Italy in mid-1947 points to the possible dangers of this development.

It is precisely this chain of events which disinflation seeks to prevent. If continued inflation is undesirable, the alternative of deflation is even less attractive. That both these effects are to be avoided is the principal attraction of a policy of disinflation. For the budget surplus is designed to sop up excess purchasing power and, hence, to relieve income pressure on available resources. As a result, demand for less essential consumer goods declines and resources are freed for diversion to investment or export activity. Here the initial brunt of the adjustment from the "absorbed" demand falls on consumer industries and not, as in deflation, on investment.

Thus, disinflation would appear to offer a solution to the difficulty of excess investment at full employment and has advantages in theory over either continued inflation or the process of deflation.

The Difficulties in Achieving a Budget Surplus

Yet, realization of the objective of a sufficient budget surplus to supplement internal savings has proven to be difficult. Experience has shown that a budget surplus is not easily achieved, and the importance of the factors creating difficulties should be recognized.

The OEEC Report points to two sources of difficulty in achieving a balanced budget. First, the greatly increased levels of taxation resulting from the war and from post-war needs have imposed a far heavier burden on fiscal systems than these have been able to sustain. Second, an inflation, once underway, creates special problems for the tax authorities. ^{1/}

^{1/} Op. cit. p. 101. See also pp. 99 and 100.

For the coming years, the weakness of the fiscal system is likely to be more important in fact than the special difficulties associated with inflation. Certainly the former is a more general problem than the latter. Surplus budgeting requires an efficient fiscal machinery if budget objectives are to be realized without injustice or actually defeated through widespread evasion. The fiscal system in many European countries cannot perform this task. That the fiscal machinery is inadequate in countries like France, Italy, Greece and Germany is notorious, and these are the countries where difficulties are greatest.^{1/} Evasion leads to loss of tax revenue and to unequal distribution of the tax burden upon the population since indirect taxes and wage and income taxes withheld at the source are likely to become the most important sources of revenue.

Efforts are being made to reform and modernize the domestic fiscal systems in Europe, and emphasis is being placed rightly upon reducing tax evasion and simplifying the tax structure. This is a slow process and is made much more difficult by the fact that the reforms are being carried out under inflationary pressures. Even in the Scandinavian and the Low Countries, tax evasion is enough of a problem to require remedial action. Consequently, the limitation of the mere mechanics of the tax collection machinery is a general difficulty in realizing a budget surplus.

Further, the difficulties in obtaining additional revenue through fiscal reform are matched by rigidity in the scale of public expenditures. It is well to recognize that non-investment government expenditures seem to behave rather like money-wages in that increases are easier to bring about than declines. This rigidity is enhanced where fixed charges and welfare, reconstruction and defense items of vital political significance make up a large portion of the budget.

Nor is there great flexibility in reducing investment spending. All the European countries plan that government finances some portion of the investment projected to achieve viability. Among those countries where large deficits are found are countries, such as Italy and France, where the portion of essential investment financed by government is substantial. A large reduction of the investment would be self-defeating.

Finally, even when achieved, a government surplus often proves ephemeral, being too convenient a target for fiscal necessity and political pressure. Utilization of surpluses to reduce taxation, extend welfare measures

^{1/} An excellent discussion of the French fiscal weaknesses is found in France in 1948, a report of the ECA Mission to France, pp. 116 ff. The two major failings of the French system are: (1) Total tax yield has been far too low in relation to governmental expenditure; and (2) the fiscal burden is not borne equally by the different segments of the population. For example, the progressive income tax provided only 23 per cent of tax receipts in 1946 and 32 per cent in 1947, compared with 72 per cent in the U. K. and 78 per cent in the U. S. in 1946.

and finance rearmament happens so often as to limit the prospects of actually realizing a surplus.

Limited Effectiveness of Disinflation

That it is difficult for disinflation to achieve a budget surplus sufficient to provide a balance between savings and investment is perhaps its most questionable aspect. Most of the British critics of the Crippsian fiscal policy point to evidence that disinflation is not fully operative, not that the disinflationary process is being carried too far. The specific factors already considered which make it difficult to achieve a sufficient surplus explain only part of the limited effectiveness of the policy, and there appear to be other reasons contributing to this result.

In the first place, a budget surplus (even when realized) may be at the expense of reduced savings in the private sector. Current high taxation is clearly reducing individual and corporate savings. Where the additional tax revenue would be drawn from funds which would otherwise be saved, the basic problem in terms of aggregates is unaltered. Savings are merely shifted from the individual to the government. By reducing savings, consumers have a direct means of frustrating the consumption objectives of fiscal policy.

It is of course possible to devise special consumption-reducing taxes but, in reality, there are political limits to such a program. Considerable resistance and evasion should be expected where consumption would be reduced below customary or expected standards of living, even though investment may require lower consumption. Where the gap between investment and private savings is in the range of 7 to 9.5 per cent of gross national product, it is unlikely that a special tax program along these lines could make a significant contribution to stability.

Secondly, high taxation is already limiting private investment and draining into the budget funds which could be used for financing corporate investment. A cut in private investment, following higher tax payments, frustrates the investment objectives of fiscal policy just as reduced savings of individuals can frustrate the consumption objectives. This limitation has important implications. To prevent adverse effects on investment, tax measures in the wide area directly affecting incentives and private savings would have to be used with care. Yet several important taxes, including individual and corporate income taxes and corporate distributed and undistributed profit taxes, which are convenient from an administrative point of view, are found in this area.

More general considerations also point to the limited effectiveness of the budget surplus. Clearly, the income-effect of a continuing high-level investment program generates income pressures which threaten price stability unless enough surplus income is continuously syphoned off by the budget. Any relaxation of the policy would be fatal. At the same time, a slowing down of the rate of

increase in productivity and production does not reduce inflationary forces. Similarly, full resource utilization tends to enhance labor immobility and to maintain wages. In short, disinflation is confronted with a series of stubborn economic difficulties. At the root is consumer preference expressed in the form of private savings inadequate to support projected investment.

Can fiscal policy, through income absorption, alter consumer preference sufficiently without creating new difficulties? In short, does not the willingness of the population to save impose a limit to the scale of investment which can be undertaken? The very real difficulties resulting from this problem are familiar to the Western European governments today. As the OEEC Report points out, "it is necessary to work out a very fine balance between failure to make the fullest possible use of resources on the one hand, and the perils of inflation on the other". ^{1/}

To point out that disinflation alone has limited effectiveness, therefore, is not to deny that there is much to recommend such a program. In working out the delicate balance, a policy of disinflation can make a significant contribution. A balanced budget, and a budget surplus, is essential if progress toward financial stability is to be achieved in Western Europe. Even the old-type credit deflation involved, as the Economist recently pointed out, a balanced budget. ^{2/} The results of disinflation may prove in fact to be less than had been hoped, and budgetary policy alone may not be able to stabilize the excess-investment economies of Western Europe; but the step of actually achieving a budget surplus is clearly in the right direction.

^{1/} Op. cit. p. 99.

^{2/} See January 22, 1949, p. 150.

CURRENCY CONVERSION AND FOREIGN TRADE OF WESTERN GERMANY ^{1/} J. Herbert Furth

The international economic relations of Western Germany were influenced in 1948 not only by the currency conversion and its effect upon production and prices, but also by the following events: (a) the progressive relaxation of foreign trade controls; (b) the introduction of a uniform conversion factor for all commercial transactions; (c) a limited fusion between the bizonal area and the French zone of occupation; and (d) the start of the ECA program.

(a) The license requirements for imports were simplified and relaxed; a bonus plan for encouraging exports, originally adopted in 1947, ^{2/} was improved; and export procedures were liberalized. In February 1949 new foreign trade regulations were enacted, abolishing the bonus scheme but making it possible for Western German merchants to enter into contracts with foreign exporters within the limits of foreign exchange quotas established for various categories of imports, virtually without further interference by the Joint Export-Import Agency or the German authorities.

(b) From May 1948 on, the ratios determining the mark value of internationally traded goods, which previously had varied widely for different commodities, were replaced by a uniform conversion factor of 30 cents per mark, which also superseded the previous military exchange rate of 10 cents per mark. ^{3/} For all practical purposes, this conversion factor fulfilled all functions of an exchange rate, except that relief imports of staple foodstuffs continued to be priced in marks at the existing levels without regard to the world market price. This last exception will be eliminated in the spring of 1949. In order to facilitate the transition from the system of varying ratios to that of a uniform conversion factor, all exports approved before July 25, 1948 were permitted to be executed at the legal German price that prevailed on July 6, 1948. Since the execution of these contracts extended over a considerable period, the practical effect of the introduction of the new conversion factor made itself felt very slowly. As late as in October 1948, only 18 per cent of all exports was shipped under a conversion factor of exactly 30 cents per mark, and as much as 36 per cent was shipped under conversion ratios of less than 25 cents per mark.

(c) The fusion of the bizonal area with the French zone had been under consideration ever since the establishment of the bizonal organization in December 1946. The Joint Export-Import Agency finally was merged with the corresponding French zone office in October 1948. Since the French authorities, however, did not feel themselves bound to apply JEIA decisions in their zone,

^{1/} For a discussion of the domestic effects of the German currency reform see this Review, March 8, 1949, p. 1.

^{2/} See this Review, August 26, 1947, p. 11.

^{3/} See this Review, April 20, 1948, p. 12.

the fusion had only limited effects. However, JETIA took over the handling of receipts from, and payments for, foreign trade transactions of the French zone, and US-UK financed relief imports also became available to the population of the French zone.

(d) ECA started to operate in April 1948, and by the end of the year had authorized contracts totalling \$337 million for the bizonal area and \$63 million for the French zone. Actual shipments in 1948 reached only \$99 million for the bizonal area and about \$30 million for the French zone. The bulk of these shipments consisted of subsistence rather than rehabilitation goods, similar to those financed by US-UK army relief appropriations. The importance of ECA for Western Germany's foreign trade, however, was enhanced by the institution of the intra-European payments scheme designed to stimulate trade among the nations participating in the Organization for European Economic Co-operation. While the actual settlements carried out in 1948 were not large, the principle involved was significant because normally at least half of Western Germany's foreign trade would be conducted with other OEEC nations.

Development of Foreign Trade

Western Germany's imports and exports increased substantially during the year and their composition became more normal. The development of bizonal trade in 1947 and 1948 and the ERP estimates for 1948-49 are shown in the following table.

Bizonal Foreign Trade, 1947 and 1948

(millions of dollars)

	<u>1947</u>	<u>1948</u> <u>Jan.-June</u> ^{1/}	<u>1948</u> <u>Jul.-Dec.</u> ^{1/}	<u>1948-49</u> <u>(ERP Est.)</u>
Imports:				
Food	559.4	872.2	929.0	932.0 ^{2/}
Fertilizer and oil products	64.7	72.6	78.0	93.0 ^{2/}
Other commodities	99.8	315.4	541.4	779.0 ^{2/}
"Invisibles"	<u>2.6</u>	<u>10.8</u>	<u>10.8</u>	<u>47.0</u>
<u>Total</u>	<u>726.5</u>	<u>1,271.0</u>	<u>1,559.2</u>	<u>1,851.0</u>
Exports:				
Coal and timber	160.8	267.0	351.0	275.0
Other commodities	36.3	143.4	317.4	391.0
"Invisibles"	<u>24.9</u>	<u>48.4</u>	<u>71.2</u>	<u>77.0</u>
<u>Total</u>	<u>222.0</u>	<u>458.8</u>	<u>739.6</u>	<u>743.0</u>

^{1/} Annual rate.

^{2/} Including freight.

Bizonal imports were still dominated by so-called Category A Commodities (food, fertilizer, and petroleum products) ^{1/} the importation of which was financed overwhelmingly by US-UK army appropriations. The so-called Category B imports, however, which include all other goods (and so-called "invisibles", i.e., service transactions), rose from 14 per cent of all commodity imports in 1947 to 35 per cent in the second half of 1948.

In the field of exports, shipments of goods other than coal and timber increased from 18 per cent of all exports in 1947 to 46 per cent in the second half of 1948. In November and December, exports of coal and timber actually were lower than those of other goods.

Imports in the second half of 1948 were somewhat lower than the target set by ERP estimates for 1948-49 while exports were almost exactly equal to it.^{2/} The importation of foodstuffs was about as high as planned, but the importation of industrial materials and capital equipment was smaller by one-fourth. The expected increase in ECA shipments and the liberalization of import procedures will, however, change the situation in the first half of 1949. Exports of coal and timber were larger than scheduled and exports of manufactured products correspondingly lower; the trend, however, was clearly toward a closer correspondence with the program, and December exports actually exceeded the program average considerably also in the field of industrial goods — largely as a result of scrap shipments. Provisional figures for January and February 1949 confirm the rising trend in exports, and there can be little doubt that the ERP export estimates for 1948-49 will prove too modest.

Foreign trade figures for the French zone are available only for part of the year and are of doubtful accuracy. On the basis of preliminary data imports may be estimated at \$180 million and exports at \$110 million. Foodstuffs accounted for 60 per cent of imports; agricultural products (wine) and lumber for 45 per cent of exports. The proportion of exported industrial goods was higher than in the bizonal area because of the absence of coal exports and large shipments of chemicals. In comparison with 1947, imports increased by one-third, largely because of shipments financed by ECA, while exports dropped by one-sixth. However, since the Saar area was included in the 1947, but excluded from the 1948 figures, the data for the two years are not comparable. Even without that factor a drop in exports would be explicable because before 1948 exports had been forced at the expense of the maintenance of an adequate minimum level of subsistence in the zone. Both import and export figures were about one-fifth lower than the ERP estimates for 1948-49.

In comparison with prewar, Western German trade still was very small. In 1937 total German imports amounted to about \$2.2 billion and total German exports to \$2.4 billion. It may be estimated that approximately 65 per cent of that trade concerned the area of the present Western zones of occupation, and that the dollar had a purchasing power about twice as high as in 1948. On the basis of these assumptions, the 1937 level of the foreign trade of the

^{1/} See this Review, January 28, 1947, supplement, p. 11.

^{2/} Total figures for 1948 conform even more closely to the estimates given in this Review, March 23, 1948, p. 6.

present Western German area represented, in terms of 1948 dollars, imports of about \$2.8 billion and exports of about \$3.1 billion. In contrast, 1948 imports reached \$1.6 billion and exports \$0.7 billion. Imports were thus about 57 per cent and exports about 23 per cent of the 1937 level. The total external trade volume of the area has contracted even more seriously because the figures exclude trade with Eastern Germany, which in 1948 was only an insignificant fraction of prewar. The lag in the importation of industrial raw materials and equipment and in the exportation of industrial products -- normally the backbone of Western Germany's foreign trade -- was even greater than in total trade. Moreover, the relatively better showing of imports was made possible only by the fact that almost 65 per cent of all imports was financed either by US-UK army relief appropriations or by ECA assistance. Commercial imports alone were only 20 per cent of the prewar volume.

Influence of the Currency Conversion

The creation of a working currency system, together with the establishment of a uniform conversion factor, made it possible for Western German traders, for the first time since 1933, to compare rationally domestic and international prices and thus to base the relation between domestic and foreign sales and purchases of commodities to which that factor applied on the principle of comparative advantage. The question arose, however, whether the particular factor chosen by the occupation authorities would correspond roughly to the relation between the German and the world market price level, and would be consistent with the development of Western German trade as planned under ERP.

Actually, even a complete correspondence between general German and world market price indices would not have meant much since price developments in Germany had been divorced completely from those in the world market, and wide price disparities in the case of individual commodities were inevitable. ^{1/} With any reasonable conversion factor, many exporters would have complained about the factor being too high to permit resumption of prewar exports, and many importers about the same factor being too low to permit resumption of prewar imports.

Moreover, the importation of Category A goods (relief) was not affected by the currency reform. The exports of coal and timber also had little connection with currency problems since they were determined by orders of the occupation authorities rather than by price considerations. The main impact of the monetary development was therefore to be expected upon commercial imports and upon exports of manufactured products.

On the average, the conversion factor of 30 cents per mark (as against a prewar rate of 40 cents) almost certainly undervalued the German currency at the moment of the currency reform as far as legal prices were concerned. Average legal prices were hardly 60 per cent about 1938 as compared

^{1/} See this Review, January 14, 1947, p. 14.

with a rise in the world market level (in terms of dollars) of about 100 per cent. Taking into account the probable overvaluation of the mark in 1938, the new rate had the result that, in terms of dollars, the average of Western German legal prices was about 20 per cent below the world market level. This undervaluation did not produce the usual results of reduction in imports and excessive rise of exports, mainly because of the pent-up demand for imported raw materials and equipment on the part of producers, and for domestically produced goods on the part of domestic consumers. Before these transitional obstacles were removed, the price level in Western Germany began to rise, and whatever undervaluation of the mark there was in June 1948 probably had disappeared by the end of the year. Moreover, the influence of price discrepancies was overshadowed on the export side by the rise in production, and on the import side by the limitation of foreign exchange supplies. The increase in imports was limited not only by the size of foreign exchange reserves, but also by the policy of the Allied authority (JEIA) which used its power of allocating these resources for increasing the Western German holdings of foreign exchange rather than for financing a maximum of imports (see below, p.17.). It is possible to justify this policy by the assumptions that a more rapid rise in imports might have exceeded the capacity of the Western German industry, and that Western Germany's "terms of trade" were rather unfavorable in the second half of 1948, with import prices at their postwar peak.

The percentage increase in exports of industrial products matched approximately the rise in industrial production. The initial export figure was so small, however, that percentage comparisons have little economic meaning.

A German study under the direction of Mr. Harmssen has suggested that a conversion factor of 27 cents per mark would better correspond to the "purchasing power parity". Such a change, however, would not affect the basic problem of individual price disparities. Furthermore, as long as a substantial part of all exports was transacted at rates different from the conversion factor, and as long as the volume of imports was determined more by the policy of JEIA than by the decision of German importers, the actual development of foreign trade did not provide a reliable basis for definite conclusions. Trade conditions in the first half of 1949, however, may be more revealing and it may become possible to decide whether or not the present or a different "conversion factor" should be transformed into a permanent and internationally recognized exchange rate.

Illicit Transactions

A paradoxical consequence of the currency reform was the apparent rise in smuggling and international black market transactions. Before the reform, Western German production was so low that virtually no exportable surplus was available, and illicit transactions had been mainly confined to petty deals involving the exchange of canned food, cigarettes, coffee, and other necessities or semi-luxuries (mainly of U. S. origin) for antiques, china, and similar household goods. Some of these deals involved "terms of trade" very favorable to the foreign "traders" (mainly members of the occupation forces), but the ignorance of many of these "traders" of the value of alleged antiques,

etc., probably turned the terms of trade quite often in favor of their German partners. On the whole therefore the damage done by these transactions to the Western German economy probably was negligible.

The currency reform made the mark again interesting to foreign speculators. Moreover, the Western German industries started again to produce goods that were in great demand abroad. The temptation to evade the strict foreign trade and exchange regulations increased, therefore, and the situation became even more serious when export controls prevented some commodities most eagerly sought by nations in the Soviet orbit (machinery increasing the war potential) from being shipped to these nations. The volume of total illicit exports has been estimated by occupation officials at an amount as high as \$200 million annually, which would be almost as large as all 1948 exports from the bizonal area other than coal and timber. It is impossible to judge the merits of that estimate on the basis of the information available at present.

The countervalue of these illicit exports consisted partly of luxury goods (largely liquor) smuggled into Western Germany, and partly of foreign exchange made available to German exporters in some "neutral" country, mainly in Switzerland. Available data again do not permit reliable estimates of the magnitudes involved.

In addition to these illicit foreign trade transactions, probably a considerable flow of goods crosses the border between the Western and Eastern zones of Germany in defiance of the Soviet blockade and the Allied counter-blockade. Since interzonal trade was extremely small even before the imposition of the blockade -- exports from Western Germany to the Soviet zone and Berlin were valued at about \$100 million during the first half of 1948 and fell to less than \$30 million in the second half --, the economic effect of that illicit trade probably is insignificant.

Apart from these completely illicit trade transactions many legal shipments are accompanied by illegal exchange deals. In all countries subject to strict foreign trade and exchange controls, traders find ways to evade the regulations; by under-invoicing exports and over-invoicing imports, for instance, both exporters and importers can build up clandestine foreign balances. Occupation officials have estimated the amount of such balances at 10 per cent of commercial transactions; if this estimate were correct, Western German merchants would have accumulated about \$140 million in foreign exchange during 1948.

Illicit foreign exchange transactions also take place without any connection with foreign trade. Both members of the occupation forces and Germans are known to buy and sell marks for foreign exchange, mainly through Swiss middlemen. The "free market" rate of the mark in Zurich is published regularly, and its fluctuations have an important effect upon the confidence of the Western German population in the future of the mark.

Foreign Exchange

The free market rate of the mark in Zurich seemed for a long time to develop in a manner contrary to economic reason. In view of the political uncertainties in Western Germany, it was to be expected that holders of German marks would welcome opportunities to acquire hard currencies at rates which were not only substantially lower than the official conversion factor, but also far lower than any conceivable purchasing power parity. It could therefore cause neither astonishment nor worry that the new currency, at the time of its introduction, was quoted in Zurich at a rate of approximately 60 francs per 100 marks, or about 5% per cent of the official parity. It was astounding, however, that in the following months the rate dropped persistently until by the end of November it stood at less than one-third of the initial rate, or 19.50 francs. Although the turnover was rather small and the rate could not be taken too seriously as an expression of general public opinion, such a drop could not help but shake the confidence of the German population and encourage overspending and capital flight. It thus added to the inflationary pressure to which the Western German economy was subjected at that time.

In January 1949 the situation changed suddenly and the quotation of the mark rose in a spectacular fashion, reattaining, at the end of February, approximately the initial level (60 francs per 100 marks); at the beginning of March, the rate weakened, but remained far above the level of the previous months. It is not quite clear whether the rise was due to an improvement in the enforcement of Western German currency controls (diminishing the supply of marks in Switzerland) or to the same change in the psychological climate (diminishing the demand for dollars and raising the demand for marks), which brought the rise in prices and the expansion in the supply of money within Western Germany to a stop at about the same time. However, since the rise in the mark quotation coincided with the general rise in the Swiss rates for Continental European currencies, the main factor probably was a more optimistic political and economic outlook. If this is true, the changes in the domestic monetary situation of Western Germany and in the external value of its currency had the same psychological basis.

The psychological factor may have been supported by the increase in the foreign exchange holdings of the central bank of Western Germany, the Bank of the German States. This bank acts as trustee for the Joint Export-Import Agency, which controls all of Western Germany's official foreign exchange resources. JEIA started its operations on January 1, 1947 with an initial capital supplied in equal parts by the United States and the United Kingdom out of the proceeds of exports from the US-UK zones in 1945-46 and out of "safe-haven" funds (German flight capital in neutral countries) put at the disposition of the US and UK governments through an agreement with Sweden; this capital amounted to \$115 million. In 1947, JEIA had a surplus of exports

over commercial imports (including goods contracted under processing agreements and stocks taken over from the occupation authorities) of \$95 million, and a deficit on service account of \$0.5 million. In 1948, JEIA had a similar export surplus of \$125.5 million and a surplus on service account of \$46.5 million. In the two years of 1947 and 1948, JEIA thus increased its original foreign exchange holdings of \$115 million out of bizonal transactions by a total of \$266.5 million. It should therefore have held at the end of the year foreign exchange to the amount of \$381.5 million. Actually the Bank of the German States showed in its year-end statement net foreign exchange holdings of only 980 million marks equal to \$294 million. The difference may be explained by two factors: Firstly, foreign importers may be slower in paying for export deliveries than German importers so that pending claims in foreign exchange might be larger than unpaid liabilities. Secondly, under the agreement of October 18, 1948 providing for the fusion of the foreign trade of the French zone and the combined US-UK zones, JEIA took over the assets and liabilities derived from import-export operations of the French zone. This provision seems to imply that JEIA had to cover the import deficit of the French zone, which (excluding the shipments financed by ECA) may be estimated at \$40 million as of the end of 1948.

In January 1949, the net foreign exchange holdings of the Bank of the German States rose by another \$29 million reaching the equivalent of \$323 million at the end of the month. If the rise in foreign exchange holdings continues under the recently liberalized import procedures, it may indicate that the Western German economy is able to finance out of its own resources a higher proportion of its import requirements than had been anticipated. Western Germany needs an adequate working balance in foreign exchange, and should not be penalized for exceeding the recovery target set under ERP. However, if a sizeable portion of U. S. assistance, which still finances the greater part of Western German imports, were steadily used for accumulating foreign exchange reserves, it might become possible to consider a reduction in future aid for the benefit of either the U. S. Treasury or the other OEEC nations.

U. S. EXPORT SURPLUS DROPS 43 PER CENT IN 1948 ^{1/}

Gretchen Fowler and
Samuel I. Katz

Recorded exports of merchandise in 1948 amounted to \$12.6 billion compared with \$15.3 billion in 1947. Since 1948 exports decreased despite a 6 per cent rise in unit value, the drop in export volume was sharper than the reduction in export value. Preliminary data for eleven months indicate that export volume was about 24 per cent below the 1947 index.

On the import side, 1948 imports reached an all-time high of \$7.1 billion, an increase of \$1.3 billion from the 1947 level. The heavier imports were the result of an 11 per cent rise in unit value and about an 11 per cent increase in physical volume.

The record imports and reduced exports resulted in an export surplus of \$5.5 billion or 43 per cent below the \$9.6 billion in 1947. There was a particularly sharp reduction in the last two quarters of 1948 when the surplus ran at a quarterly rate of only \$1.2 billion or about the same as the rate which actually prevailed in 1946. About two-thirds of the reduction in export surplus was due to lower exports and the remaining one-third to the higher levels of imports.

A number of factors contributed to the sharp reduction in the trade surplus. On the export side, greater availabilities of goods from non-dollar sources in 1948 and the general dollar stringency resulting from the depletion of war-accumulated and other dollar resources in 1947 were the principal contributing factors. Both these factors underlay the foreign exchange and trade restrictions designed deliberately to curtail dollar imports which resulted in increased difficulties for American exports in 1948 in many markets. At the same time, expanded local production and greater supplies from important exporting countries, especially in Europe, contributed to a general reduction in the urgency for goods which had led to the record United States export surplus in 1947.

The increased goods imports into the United States also contributed to the reduced export surplus. These imports, which reached record levels, were the result of both higher prices and heavier volume. Greater availability of world supplies, accelerated by rehabilitation of facilities in several important war-disrupted sources of imports, and the high level of production in the U. S. in 1948 led to the sharp rise in imports. Since United States imports in 1946 and 1947 were substantially below the level to be expected on the basis of the pre-war relation between U. S. imports and gross national product, the growth in imports was not surprising. In fact, imports in 1948, despite expansion, were well below the pre-war relation. In addition, concerted efforts to expand dollar

^{1/} For reviews of U. S. trade for earlier periods of 1948, see this Review for October 19, 1948, pp. 11-19, and December 28, 1948, pp. 8-15.

earnings by encouraging exports to the U. S. had an important bearing on the heavier U. S. imports from several countries.

Important changes occurred in the regional distribution of the export surplus in 1948. The decline in surplus compared with 1947 was general for all areas, as shown in Table I. More important, the surplus in the last half of the year was nearly 20 per cent below the average for the first six months and even further below the 1947 quarterly average. The surplus with ECA-Europe, although reduced, became an increasingly larger proportion of the global surplus since the surplus for other areas was more greatly reduced than for the European countries. The rise in the U. S. export surplus for the four countries receiving special types of aid in addition to ECA funds more than offset the sharp decline in the export surplus of the thirteen other ECA countries. These thirteen countries reduced their U. S. export surplus in 1948 not only in value but also in proportion to the global surplus as compared with 1947.

TABLE I

U. S.: Export Surplus by Major Areas
(in millions of dollars)

Area	Quarterly Averages				1948 by Quarter			
	1938	1946	1947	1948	I	II	III	IV
17 ECA Countries:	174	650	1,150	809	913	840	740	742
4 special aid countries	8	53	213	311	295	342	329	280
13 other ECA countries	167	597	936	497	618	497	412	463
Other Europe	14	168	74	3	39	-15	-11	-3
North America	63	224	420	214	184	284	170	217
South America	9	14	279	93	126	133	64	48
Asia	-13	113	324	190	195	213	214	140
Australasia	19	-17	41	-3	-6	-	-18	13
Africa	16	46	124	95	81	113	87	97
TOTAL	284	1,205	2,405	1,387	1,524	1,547	1,222	1,255

Noteworthy progress in balancing their trade was made in 1948 by South America, Australia, and, to a lesser extent, North America and Asia. In large measure this progress was due to increased import restrictions. The import restrictions adopted unevenly affected American trade. U. S. exports of manufactured food products and textiles, for example, were particularly affected.

The effect of import policies on our export trade is brought out by the statistics in Table II below. It will be seen that reduced exports accounted for 67 per cent of the \$4.1 billion reduction in the 1948 export surplus and increased U. S. imports for only 33 per cent. More important perhaps is the comparison in columns (4) and (6) which show the distribution of the reduction in surplus by area between decreased exports and increased imports. Only in the cases of Africa and Asia were higher shipments to the U. S. more important than reduced purchases of American goods. Australasia is an example of an area which depended almost entirely on a severe reduction in dollar imports to bring about a balance in 1948. The reduced export surplus for non-ECA-Europe was due almost entirely to U. S. export controls. In the case of ECA countries as a whole, the reduced export surplus was due mainly to reduced purchases from the United States rather than heavier sales to this country. But the very sharp cut in U. S. exports to, and the reduced export surplus with, the thirteen ECA countries in Western Europe should be contrasted with the four special-aid countries where a substantial rise occurred in both exports and the 1948 export surplus. The improvement in the position of North and South American countries as a whole was more balanced. Although reduced purchases accounted for the larger portion of the reduced U. S. surplus, higher sales to the U. S. made a very substantial contribution to their improved position, the increase in U. S. imports from Canada being particularly noteworthy.

TABLE II

U. S.: Reduction in Export Surplus Between
1947 and 1948 by Major Areas

(Amounts in millions of dollars)

	<u>Total reduction in export surplus</u>		<u>Distribution of reduction between exports and imports:</u>			
			<u>Reduction in U.S. exports</u>		<u>Increase in U. S. imports</u>	
	<u>Amount</u>	<u>Per cent of total</u>	<u>Amount</u>	<u>Per cent</u>	<u>Amount</u>	<u>Per cent</u>
17 ECA Countries (including Turkey):	-1,361	33	-1,101	81	260	19
4 Special Aid countries a/	+ 392	-10	+417	b/	25	b/
13 Other ECA countries	-1,753	43	-1,518	87	235	13
Other Europe	- 283	7	- 277	98	6	2
North America	- 829	20	- 435	52	394	48
South America	- 747	18	- 446	60	301	40
Asia	- 528	13	- 244	46	284	54
Australasia	- 175	4	- 167	95	8	5
Africa	- 116	3	- 36	31	80	69
Total	-4,066	100	-2,727	67	1,339	33

a/ Includes Germany, Austria, Greece and Turkey.

b/ Not applicable.

Trade by Commodities

The 1948 decline in exports was shared by all major commodity categories. Although the largest absolute drop is found in the finished manufacture group, the percentage declines compared with 1947 were greater in the manufactured food and semimanufacture categories. Shipments of crude materials and crude foodstuffs were relatively well maintained, reporting declines less than 7 per cent.

Since 1947 exports were abnormally high, comparison of the distribution of 1948 exports by commodity group with 1946 may be instructive, although the special post-war conditions prevailing in 1946 should be borne in mind. Most impressive is the fact that crude foodstuff shipments have been increasingly important in 1947 and 1948, despite the heavy UNNRA movement in 1946. On the other hand, the importance of manufactured foodstuffs has steadily declined. In fact, it is only in this category that the absolute value of 1948 shipments is below the 1946 figure, with reductions in meat products, dried eggs, and dairy products especially marked. Despite the sharp declines over 1947, the 1948 exports of semimanufactures and finished manufactures were substantially above the 1946 value.

TABLE III

Distribution of U. S. Merchandise Trade
(In millions of dollars)

	<u>Exports</u>					
	<u>1946</u>	<u>Per cent of total</u>	<u>1947</u>	<u>Per cent of total</u>	<u>1948</u>	<u>Per cent of total</u>
Crude Materials	1,416	14.9	1,602	10.5	1,490	11.9
Crude Foodstuffs	648	6.8	1,350	8.9	1,268	10.2
Manufactured Foodstuffs	1,524	16.1	1,756	11.6	1,319	10.6
Semimanufactures	896	9.4	1,785	11.8	1,368	10.9
Finished Manufactures	5,019	52.8	8,672	57.2	7,054	56.4
Total	9,503	100.0	15,163	100.0	12,498	100.0

	<u>Imports</u>					
	<u>1946</u>	<u>Per cent of total</u>	<u>1947</u>	<u>Per cent of total</u>	<u>1948</u>	<u>Per cent of total</u>
Crude Materials	1,709	35.6	1,743	30.9	2,109	30.0
Crude Foodstuffs	814	16.9	1,017	18.0	1,271	18.0
Manufactured Foodstuffs	503	10.5	656	11.6	731	10.4
Semimanufactures	930	19.4	1,245	22.1	1,632	23.2
Finished Manufactures	845	17.6	983	17.4	1,296	18.4
Total	4,801	100.0	5,643	100.0	7,038	100.0

In 1948, finished manufactures continued to predominate, accounting for 56 per cent of shipments. The \$1.6 billion drop in this category between 1947 and 1948 was mainly accounted for by merchant vessels and cotton manufactures. The sharp reduction in merchant vessels is not surprising since the ship-sales program, a non-recurring portion of our export trade, was most active in 1947. The important cut in cotton manufactures, however, is of a different order. Greater availabilities from local production and accelerated export drives by non-dollar sources, which facilitated dollar savings on textile imports, are partly responsible for the substantial cut in the value of shipments. These two commodities account for 42 per cent of the reduction in this group and in the case of no other commodity in this category did the 1948 reduction exceed \$100 million. Detailed statistics will be found in Table VI.

The four remaining commodity groups shared the remaining export trade in about equal proportions. Crude foodstuffs, which were exceptionally well maintained, were sustained by the heavy increase in wheat shipments which was sufficient to offset the sharp drop in the movement of corn. The substantial decline in manufactured foodstuffs was a continuation of a trend begun in 1947. The 1948 data are marked, however, by a substantial reduction in wheat flour from 1947 levels as well as a continued drop in other major manufactured foodstuffs.

Important changes occurred within the crude materials group. A very large reduction took place in the movement of coal to Europe, reflecting improved supply conditions there. Raw cotton, the largest item in this group, expanded considerably during 1948 but a 20 per cent decline occurred in tobacco shipments.

Changes in the semimanufactures group were distributed over a wide range of products. About 25 per cent of the 1948 reduction was in the iron and steel semimanufactures groups. A lesser reduction occurred in industrial chemicals.

Contrasted with the 18 per cent reduction in exports, U. S. imports of merchandise increased by 23 per cent over the 1947 level. The substantial expansion was shared generally among the major commodity categories. Crude materials, which accounted for almost 30 per cent of total imports, and semimanufactures, second in importance, showed substantial increases in value. Only in the category of manufactured foodstuffs, the smallest commodity group, was the increase in 1948 value limited to a mere 10 per cent.

Among semimanufactured products, increases were reported for tin, petroleum products, copper, and wood products, especially sawed boards and wood pulp.

The substantial increases in crude petroleum and raw wool imports accounted for nearly two-thirds of the increase in the important crude materials group. Undressed furs, hides and skins, and non-ferrous ores also participated in the rise.

Heavier coffee shipments accounted for about 20 per cent of the increase in crude foodstuffs, but noteworthy increases also took place in cattle and cocoa. Both the unit price and quantity of coffee imports were higher in 1948. The substantial increase in cattle imports followed the removal of restrictions on the export of cattle in Canada.

A 50 per cent increase in imports of machinery and vehicles and a considerable increase in newsprint shipments accounted for about half the expansion in finished manufactured products. An important part of the increase in machinery and vehicles resulted from continued rise in U. S. imports of vehicles and farm machinery from the United Kingdom. The substantial increase in newsprint imports was part of Canada's dollar export drive, and the 1948 value total reflects a significant expansion in the quantity.

The most noteworthy changes in the manufactured foodstuffs category were the large meat product increase and the substantial reduction in cane sugar imports, following the reduction in quotas through the operation of the new sugar act. Detailed changes in imports by commodities are shown in Table VII.

Trade by Area

The export decline in 1948 was general for all areas, except the area containing four ECA countries to which the U. S. is sending military aid or civilian supplies, and for practically all countries, as shown in Tables IV and VIII below. ^{1/} Particularly marked was the decline in shipments to Europe. Europe received 34 per cent of U. S. exports in 1948 compared with 37 per cent in 1947 and 42 per cent in 1946. This decrease is attributable to the declining shares of Eastern Europe and the thirteen Western European countries. Eastern Europe dropped from 9 per cent in 1946 to 3 per cent in 1947 and 2 per cent in 1948, while Western Europe dropped from 31 per cent in 1946 to 28 per cent in 1947 and 22 per cent in 1948. The share of the four ECA countries to which special aid is being given rose from 3 per cent in 1946 to 11 per cent in 1948. South America held its relative position as a U. S. market, receiving 15 per cent of U. S. exports in both 1948 and 1947, compared with 12 per cent of the smaller total in 1946. Asia increased in importance, accounting for 17 per cent of 1948 exports compared with about 15 per cent in the two previous years. Changes in the positions of other areas were relatively unimportant. All areas except for Western Europe and "Other Europe" showed dollar increases in exports from the U. S. in 1948 over 1946.

^{1/} Important exceptions were Germany, where exports increased by \$286 million; Venezuela, with a rise of \$90 million; and the Union of South Africa, with exports \$78 million higher.

TABLE IV

Distribution of U. S. Merchandise Trade by Areas
(Amounts in millions of dollars)

	<u>Exports</u>					
	<u>1946</u>		<u>1947</u>		<u>1948</u>	
North America	2,532	26.0	3,828	25.0	3,393	26.9
South America	1,152	11.8	2,354	15.3	1,908	15.1
Europe:	4,109	42.2	5,683	37.0	4,285	34.0
17 ECA Countries (including Turkey):	3,278	33.7	5,292	34.5	4,191	33.2
4 special-aid countries	307	3.2	938	6.1	1,355	10.7
13 other ECA countries	2,971	30.5	4,354	28.4	2,836	22.5
Other Europe	867	8.9	473	3.1	196	1.6
Asia	1,343	13.8	2,338	15.2	2,094	16.6
Australasia	117	1.2	320	2.1	153	1.2
Africa	488	5.0	822	5.4	785	6.2
Total	9,740	100.0	15,345	100.0	12,618	100.0
	<u>Imports</u>					
	<u>1946</u>		<u>1947</u>		<u>1948</u>	
North America	1,642	33.4	2,144	37.4	2,538	35.9
South America	1,095	22.3	1,237	21.6	1,538	21.8
Europe:	802	16.3	819	14.3	1,091	15.4
17 ECA Countries (including Turkey):	679	13.8	697	12.2	956	13.5
4 special-aid countries	96	1.9	85	1.5	109	1.5
13 other ECA countries	583	11.9	612	10.7	847	12.0
Other Europe	212	4.3	180	3.1	185	2.6
Asia	891	18.1	1,049	18.3	1,332	18.8
Australasia	184	3.7	156	2.7	164	2.3
Africa	306	6.2	327	5.7	407	5.8
Total	4,918	100.0	5,732	100.0	7,070	100.0

U. S. imports in 1948 were considerably heavier from all areas. Canada achieved the largest increase of any country, exporting \$458 million more to the U. S. in 1948 than in 1947. The only large decline during 1948 from the 1947 level occurred in Cuba, and amounted to \$135 million. (See Tables IV and IX.)

A number of countries achieved a favorable balance of trade vis-a-vis the U. S. in 1948, ^{1/} and several others maintained their favorable 1947 position in 1948 ^{2/}. A very few others, chiefly Cuba, changed from a favorable position in 1947 to an unfavorable one in 1948.

There was relatively little change in the percentage distribution of imports by area for 1948 as compared with 1947. The only important changes during 1948, compared with 1946, were the growth of importance of North America as a U. S. supplier, and the decline of Australia; but the variations were minor as is shown in Table IV.

It is difficult to determine to what extent the increase in imports in 1948 was facilitated by the tariff reductions negotiated in the Geneva Agreement on Tariffs and Trade which became effective in the U. S. on January 1, 1948. Most of the countries for which these reductions became effective at that time--the United Kingdom, France, Benelux, Canada, Australia, and their colonies--experienced increases in varying degrees during the year, but many of the products which were responsible for the value increases were bound on the free list, and thus not affected by tariff changes.

Important in 1948 was the progress made by ECA-Europe in expanding exports to the United States. Particularly noteworthy is the sharp rise in the per cent of ECA imports to total imports in the fourth quarter as shown in Table V. Although still well below the 1938 percentages, ECA countries recovered from the sharp reduction in their relative importance as a supplier of U. S. imports which occurred in 1947 following the severe winter of 1946-47 and the depletion of raw material stocks which were consumed in 1946 when exports to the U. S. were well maintained. To increase their share of total U. S. imports at a time when imports are increasing substantially is indicative of some progress toward recovery. The increases were widely dispersed, however. Compared to 1946 imports, the United Kingdom and Sweden show the largest increases. But compared to 1947, the recovery in 1948 was striking in the case of Italy, France and Belgium. Despite recovery in 1948, however, the ECA countries are still confronted with serious unbalance in their dollar trade, and the rate of increase in 1948 will have to be accelerated in the next few years if substantial inroad on their dollar problem is to be made by 1952-53.

^{1/} The most notable were Colombia, Chile, Brazil, the Eastern European countries, Australia, and Ceylon.

^{2/} The principal countries in this group were Curacao, British Malaya, and the Gold Coast.

TABLE V

U. S.: General imports from 17 ECA countries compared to total imports and imports by principal countries, by quarters

(in millions of dollars)

	1938	Quarterly average			By quarters in 1948			
		1946	1947	1948	I	II	III	IV
Total U.S. imports	490	1,227	1,433	1,768	1,794	1,693	1,715	1,869
Imports from 17 ECA countries	120	170	174	239	230	224	228	275
Per cent	24.5	13.8	12.2	13.5	12.8	13.2	13.3	14.7
<u>Imports by principal countries:</u>								
U. K.	30	39	51	71	68	71	70	76
Switzerland	6	25	21	26	23	24	27	31
Italy	10	17	11	24	20	24	19	31
Sweden	11	12	23	23	31	25	19	16
Belgium & Luxembourg	10	19	15	22	18	19	22	30
France	14	16	12	18	16	17	19	21
Turkey	5	17	14	13	12	13	5	20
Netherlands	8	6	7	11	7	9	15	14
8 Other countries	27	19	21	31	36	23	30	36

TABLE VI
U. S. Merchandise Trade
(in millions of dollars)

Economic Classes and Commodities	Increase or Decrease (-) from		
	1948	1947	1946
Exports of U. S. merchandise	12,498	-2,665	2,996
1. Finished Manufactures	7,054	-1,618	2,035
Industrial machinery	1,249	-89	403
Agric. machinery & implements	382	64	224
Elec. machinery & appliances	490	-73	186
Passenger cars (new)	280	-57	157
Merchant vessels	255	-370	138
Steel mill manufactures	334	-56	122
Motor trucks and busses (new)	352	-90	121
Cotton manufactures	455	-308	100
Lubricating oil	198	4	83
Rayon, nylon, & other synthetic textile ^{mfrs.}	209	-66	81
Auto parts for replacement	147	-22	60
Iron & steel advanced mfrs.	212	-55	56
Rubber mfrs.	123	-80	-19
Wool mfrs.	34	-53	-74
2. Crude foodstuffs	1,268	-82	620
Wheat	910	227	519
Corn	45	-229	17
3. Semimanufactures	1,368	-417	472
Iron & steel semimfrs.	316	-119	80
Industrial chemicals	137	-25	54
Copper (ingots, billets, plates & rods)	70	5	53
4. Crude materials	1,490	-112	74
Coal	479	-141	177
Unmfrd. cotton	511	84	-27
Unmfrd. tobacco	215	-56	-137
5. Manufactured foodstuffs	1,319	-437	-205
Wheat flour	488	-121	269
Dairy products	208	-58	-87
Dried eggs	30	-49	-94
Meat products	60	-97	-282

TABLE VII
U. S. Merchandise Trade
(in millions of dollars)

Economic classes and commodities	1948	Increase or decrease (-) from	
		1947	1946
Imports for consumption	7,038	1,394	2,236
1. Semimanufactures	1,632	387	702
Wood pulp	273	16	137
Copper	178	34	100
Tin	103	60	85
Sawed boards, planks, deals, etc.	151	51	74
Gas and fuel oil	126	40	70
Expressed oils, inedible	70	-22	31
Diamonds, cut but not set	56	3	-62
2. Crude foodstuffs	1,271	254	456
Coffee	696	97	225
Cocoa or cacao beans	194	41	137
Cattle, except for breeding	63	55	35
3. Finished manufactures	1,296	313	451
Newsprint	413	70	172
Machinery and vehicles	154	87	109
Burlaps	131	22	54
Non-commercial imports	81	20	50
4. Crude materials	2,109	366	399
Crude petroleum	285	124	184
Oilseeds	151	12	98
Crude rubber	313	-10	79
Nonferrous ores	111	10	50
Other vegetable fibers	65	-2	33
Hides and skins	108	22	30
Wool, unmfed.	308	99	18
Undressed furs	159	37	-73
Raw silk	15	-1	-95
5. Manufactured foodstuffs	731	75	228
Cane sugar	313	-98	117
Meat products	91	68	74

TABLE VIII
U. S. Merchandise Trade by Country
(in millions of dollars)

Continent and country	1948	Increase or decrease (-) as compared with:	
		1947	1946
Exports	12,618	-2,727	2,878
Net exports	5,548	-4,066	726
1. North America	3,393	-435	861
Canada	1,913	-160	472
Cuba	441	-51	169
Republic of Panama	92	-80	46
Mexico	518	-111	13
2. South America	1,908	-446	756
Venezuela	516	90	305
Argentina	379	-301	186
Brazil	498	-146	141
Colombia	197	-22	51
3. Asia	2,094	-244	751
Japan	323	-100	221
Republic of the Philippines	468	28	170
India and Pakistan	315	-86	134
Korea	70	11	70
British Malaya	82	16	67
Turkey	102	20	65
Saudi Arabia	84	17	65
China	240	-114	-226
4. Africa	785	-36	297
Union of South Africa	492	78	265
5. Europe	4,285	-1,398	176
Germany	868	286	786
Austria	146	38	100
Greece	239	72	96
Netherlands	313	-70	92
Switzerland	171	-23	63
Italy and Trieste	427	-73	56
Belgium and Luxembourg	310	-225	31
Eire	37	-52	9
Norway	85	-62	6
Czechoslovakia	21	-29	-86
Sweden	119	-279	-88
Yugoslavia	8	-23	-119
France	591	-226	-121
Poland and Danzig	56	-52	-127
United Kingdom	644	-459	-212
USSR	28	-122	-330
6. Australia and Oceania	153	-167	36
Australia	114	-121	31
16 E.C.A. Countries and Germany	4,191	-1,101	913

TABLE IX
U. S. Merchandise Trade by Country
(in millions of dollars)

Continent and country	1948	Increase or decrease (-) as compared with:	
		1947	1946
Imports	7,070	1,338	2,152
1. North America	2,538	394	897
Canada	1,554	458	671
Curacao	120	47	74
Cuba	374	-135	51
2. South America	1,538	301	443
Venezuela	273	99	153
Brazil	514	68	106
Chile	179	57	95
Colombia	236	31	80
Uruguay	58	20	10
Argentina	180	26	-14
3. Asia	1,332	284	442
Republic of the Philippines	227	66	188
British Malaya	270	-14	144
India and Pakistan	292	38	54
Siam	50	32	44
Netherlands Indies	75	42	42
China	120	5	28
Ceylon	52	23	21
Afghanistan	35	32	-1
Japan	63	27	-30
French Indo-China	3	-1	-39
4. Europe	1,091	273	289
United Kingdom	285	80	128
Sweden	91	-1	44
Germany	31	25	28
Finland	39	-1	27
Italy and Trieste	94	50	26
Netherlands	44	17	21
Norway	34	11	20
Belgium and Luxembourg	89	31	12
France	73	26	10
Switzerland	105	22	6
U. S. S. R.	79	2	-22
5. Africa	407	80	101
Gold Coast	75	23	51
Belgian Congo	47	14	28
Union of South Africa	135	23	-15
6. Australia and Oceania	164	8	-20
16 E. C. A. Countries and Germany	956	260	277