

PERSONAL AND
CONFIDENTIAL

March 20, 1946.

Dear Senator:

In response to your telephone request of last week, I am enclosing a memorandum in answer to the statement of Senator Ellender published in the Congressional Record of March 5. I hope this memorandum serves your purpose. I am sorry I couldn't get it to you sooner, but with all of the other work it was difficult for the staff to do the kind of a job I wanted done before now.

Assuring you of my pleasure always to assist you in any way I can, I am

Sincerely yours,

The Honorable Abe Murdock,
United States Senate,
Washington, D. C.

Enclosure

MSE:VE:b

March 18, 1946

PUBLIC INDEBTEDNESS AND THE PROPOSED LOAN TO GREAT BRITAIN

In the Congressional Record of March 5, 1946, Senator Ellender inserted a table listing for various countries the size of public debt, square miles of territories, and number of population. The Senator pointed out that our debt is nearly three times that of Great Britain and in excess of the combined debts of our allies, even though our area, or population, is but 10 per cent of that of our allies. He concluded that, therefore, we are in no position to extend loans to foreign countries. I do not wish to take issue with the Senator's figures and trust that they have been carefully assembled by the Library of Congress staff. I am concerned, however, with his line of reasoning.

International comparisons can easily be misleading and are always a difficult matter. This applies particularly to a comparison of public finances. The Senator contrasts a total public debt of 279 billion dollars for the United States with a British total of 98 billion dollars, or with a total for our allies of 211 billion. This is useful information, but quite inadequate by itself. If we are to draw a comparison between the debt position of various countries, we must allow not only for their respective debts in money terms but also for their economic capacities to support such debts.

The United States with its vast wealth and resources obviously can support a much larger debt than would be feasible for the bulk of small countries listed in the Senator's table.

The Senator, indeed, makes some allowance for this fact by listing the size of population and square miles of territory as additional factors. He includes a comparison of debt in per capita terms. On this basis the United States and United Kingdom debts are both close to \$2,000, even though in absolute terms the United States figure is three times as large. Not being too happy with this result, the Senator proceeds to compare the per capita debt of the United States and territories with that of the British Commonwealth rather than that of the United Kingdom, and thus finds the British per capita debt to be \$261 as against \$1,756 in the United States and territories. But this is not a fair comparison. The British Commonwealth is an association of free nations whose economic resources are those of sovereign states and not at the disposal of the British Government. Thus, the inclusion of the Indian population of 390 million greatly reduces the per capita debt of the British Commonwealth. Yet, it is obvious that it has little or no bearing upon the burden of debt owed by the British Government.

This, however, is not the main flaw in the Senator's reasoning. The basic fault is that a debt comparison in per capita terms is quite inadequate. It is but little better than a comparison in absolute money terms. Relative population numbers (or areas)

of various countries are no measure of their respective economic capacities to support public debt. Population differences fail to allow for the vast variations in per capita wealth, incomes, and productive powers of different countries, which are the real determinants of their respective abilities to carry a public debt. Thus, it would be obviously absurd to argue that India having a population which is nearly three times that of the United States could support a debt about three times as large, or over 800 billion dollars, even though it is well known that India's capacity to produce is but a small fraction of our capacity to produce.

Far better than using population figures, the size of a country's national income may be taken as a rough indicator of its ability to carry public debt. The higher a country's national income, the more taxes can be raised for the financing of interest charges or the larger will the volume of securities tend to be which investors are willing to hold. I have prepared, accordingly, a table in which the debt position of the United States and some other countries are compared in these terms, showing their public debts as a percentage of their respective national incomes. The figures relate to the latest available period and the picture would not be very different if completely current data were available. The table shows that public debt as a percentage of national income for both the United States and Canada equals about 170 per cent as against 133 per cent in Australia and 265 per cent for the United Kingdom. Measured in these terms--which are far from perfect, but certainly more adequate than those employed by Senator

Ellender--the comparative debt position of the United States is thus much superior to the British. This, it should be pointed out, is the case even though taxes provided for a larger share of British war expenditures and absorbed a larger fraction of British wartime incomes than was the case in this country. Taking debt as a percentage of national income, the present debt position of the United States is about equal to the prewar position of the United Kingdom.

In considering the burden of the public debt, taxation for the financing of interest payments is a major factor. A comparison between the ratios of interest payments on public debt to national income for various countries is thus significant and has been included in the table. Considered in these terms, the debt position in the United States involves an even lighter burden by comparison because the average interest return on public debt in this country is below that in the other countries. This is due partly to differences in the level of interest rates and partly to differences in the distribution of outstanding debt with regard to maturities and types of holders. Thus, interest payments as percentage of national income are estimated at 2.5 per cent for the United States as against about 3.5 per cent for Canada and Australia and 5 per cent for the United Kingdom. The present ratio of interest payments to national income for the United States is little over one-half of the British prewar ratio.

I do not wish to suggest on the basis of all this that the enormous wartime increase in our public debt is a matter of little significance. I do believe, however, that given a wise and prudent fiscal policy the resources of the American economy will prove fully adequate to carry the debt. Also, the facts which I have presented indicate that the relative debt burden in the United States is substantially lighter, not heavier, than that of the United Kingdom.

It should be pointed out, finally, that the question of relative debt burdens has only a very indirect bearing on our ability to extend a loan to the British Government or on the British Government's need for such a loan.

The issue for the British Government is not whether the funds should be borrowed at home or abroad. To meet the requirements of the economic situation, they must be borrowed abroad, because the need of the British people is for an import of food supplies, clothing, raw materials, industrial equipment and other items essential to the restoration of the British economy to a peacetime basis. To import these things, the British Government needs the foreign exchange with which to pay for them. Such foreign exchange can be obtained only by exports or by borrowing abroad. It cannot be obtained by domestic borrowing. The need of the British Government for the loan would thus be just as great if her public debt was but a fraction of the actual amount.

The ability of the American people to extend this loan to Great Britain, in turn, is not so much a question of American indebtedness as a question of our ability to spare the raw materials and commodities which we shall export to the British. Considering the standard of living which we have been able to maintain during the war and considering the economic exhaustion of our ally, there is no doubt in my mind that we can and must afford to do so. Having made a tremendous effort to win the victory, it would seem foolhardy indeed to shun a small sacrifice to help build the peace.

NATIONAL DEBT, INTEREST CHARGES, AND NATIONAL INCOME

(billions U. S. dollars)

	National Income	National Debt (end of period)	Interest Payments	Debt as percent of national income	Interest as percent of national income
<u>United States</u>					
Calendar Years					
1939	70.8	41.9	.969	59	1.37
1941	96.9	57.9	1.145	60	1.19
1944	160.7	230.6	3.001	143	1.87
1945	161.0	278.1	4.099	173	2.55
<u>Canada</u>					
Fiscal years, Ending March 31					
1939	4.3	3.6	.126	84	2.93
1941	5.2	4.5	.126	87	2.42
1944	8.1	11.3	.221	139	2.73
1945	8.4	14.3	.290	170	3.45
<u>United Kingdom</u>					
Fiscal years, Ending March 31					
1939	22.4	39.2	1.036	175	4.62
1941	25.0	46.0	.855	184	3.42
1944	32.7	79.5	1.545	243	4.72
1945	34.3	90.8	1.747	265	5.09
<u>Australia</u>					
Fiscal years, Ending June 30					
1939	3.0	1.5	.048	50	1.62
1941	2.9	1.6	.052	55	1.79
1944	4.2	4.8	.123	114	2.93
1945	4.2 *	5.6	.142	133	3.38

* Assumed the same as in 1944 for lack of further information.

Notes: Foreign currencies converted to U. S. dollars at the official exchange rate.

Sources

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