THE BUSINESS REVIEW

FEDERAL RESERVE BANK OF PHILADELPHIA

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PROGRESS REPORT ON EUROPE

EUROPE'S economy is convalescing. The rate of progress and the level of ultimate recovery depend on two things: the ability of the patient to help himself, and the aid he receives. The European Recovery Program embraces both lines of treatment.

A piecemeal approach to Western Europe's difficulties will not do. The roots of the problems spread out in many directions and run deep beneath the surface. Lack of energy, low production, dislocated trade relations, and financial disequilibrium are all related. Poor industrial production hinders farm output, lack of food keeps productivity low, low productivity restricts manufacturing output, thereby curtailing exports and aggravating inflation, which in turn destroys incentives and disrupts business organization.. Without substantial aid from the outside to break through this vicious tangle of cause and effect, Europe's recovery would be exceedingly slow and painful.

The United States has undertaken to provide such aid.. Its effective administration requires constant watching and reappraisal in order to assure its most efficient use and a minimum disturbance to our own economy.

The following articles are in the nature of a progress report. The first indicates that a good start has been made toward the recovery of production and trade. ERP will provide continuing support according to an integrated plan. ERP assistance is no greater than other aid we have extended in the recent past but, as the second article points out, its cost to the United States must be measured not only in goods, but also in terms of its inflationary effect upon our economy. ERP is a calculated risk. It has been undertaken in the belief that its benefits will outweigh the costs.

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I. Production and Trade

What Europe needs most is energy. Energy in the form of food for her people. Energy in the form of fuel for her industries. Energy in the form of fertilizer for her soil. It is not so much the lack of energy resources that is retarding recovery in Europe, as the insufficient utilization of her energy potential. Europe's productive capacity is at its best when all the nations of the world freely exchange with each other the specialized products which each can produce most advantageously. Europe, and particularly Western Europe, is a heavily-populated and highly-industrialized area whose people can live only by importing raw materials from all over the world to be manufactured into goods and services for export. The very life of the people of Western Europe rests upon international trade — trade with each other and trade with overseas nations. In 1938 this area, with less than 10 per cent of the world's population, had nearly one-half of the world's international trade, owned nearly two-thirds of the world's shipping tonnage, and derived an income from foreign investments and invisible exports sufficient to provide nearly one-quarter of the imports needed by industrial plants and the food required to sustain its population. But the picture is different now.

The mutual cooperation so vital to the welbeing of European nations began to disintegrate long before the second world war because of policies based upon the idea of economic nationalism, that nations can live alone. The devastation of World War II—displaced people, property destruction, lost markets, shortages of raw material supplies, financial disequilibrium, and especially inflation—multiplied the difficulties of restoring the international cooperation which economic interdependence makes an essential condition of European prosperity.

Instead of consolidating their strength, the nations of Europe have drifted still further apart since the end of war. Bulgaria, Czechoslovakia, Finland, Hungary, Poland, Rumania, and Yugoslavia have fallen under Russian influence, with the result that the predominantly agricultural resources of this area are largely shut off from Western European countries. Futhermore, Germany—one of the Continent's most highly industrialized countries—is split, with one part under the administration of Eastern European interests and the other under the control of the West. Partition of Europe is especially unfortunate at a time when recovery demands union.

Note: Much of the material in this and the following section was drawn from "A Survey of the Economic Situation and Prospects of Europe" published by the United Nations Economic and Social Council.

Since the end of the war, greater progress toward recovery in Europe has been made in industry than in agriculture, and those industries producing capital goods have recovered more rapidly than the industries producing consumer goods. Transportation is considerably above pre-war levels; trade is still substantially below. In most countries, except Germany and Italy, the labor force is more fully employed than before the war, but productivity is generally low.

The problems that beset the European nations are interrelated. They cannot be solved one by one. Lack of trade hinders production; but the reverse is also true. Poor industrial production hinders farm output, lack of food keeps worker productivity low, low productivity hampers production. For a while it seemed that Europe was caught in a downward spiral of mutually dependent causes and effects. With outside aid and coordinated internal effort, the trend is being reversed.

Progress in Production

Despite the many obstacles in their way, most European countries have made unexpected progress in industrial output since the end of the war. The fifteen countries, shown in the chart which accounted for over three-quarters of the pre-war industrial output of Europe, exclusive of the U.S.S.R., raised total physical production from 60 per cent of the pre-war level in the latter half of 1945 to 83 per cent in the fourth quarter of 1946. Progress was irregular in 1947, due in part to an unusually severe winter in 1946-1947 and subnormal rainfall in the following spring which seriously curtailed the output of agricultural raw materials.

Industrial recovery in the various countries was quite unequal both in rate of progress and in the respective levels from which they started. The greatest recovery has been made by the United Kindgom, Ireland, and Sweden. Industrial output in these countries was considerably above the pre-war level by the end of 1946. Another group of countries, consisting of Belgium, Bulgaria, Czechoslovakia, Denmark, France, Norway, and Poland, likewise succeeded in raising

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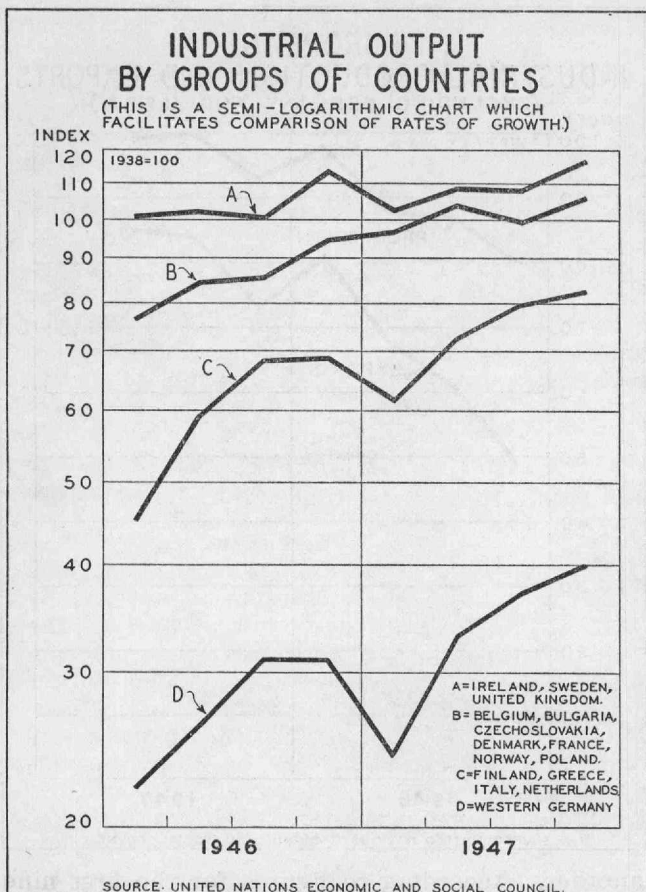

their industrial production above their pre-war output by the second quarter of 1947 and after a brief set-back they made further gains. Finland, Greece, Italy, and The Netherlands are representative of countries that have not attained pre-war output but have stepped up their production to a point almost double the low level from which they started after the war. The least progress has been made by Western Germany, whose industrial production is still less than half the pre-war output. This is all the more serious in view of the fact that the western portion of pre-war Germany accounted for about one-fifth of the industrial production of Western Europe.

Industries manufacturing capital goods have made faster progress than the consumer goods industries during the first two post-war years. Better than pre-war rates of production have been attained by the steel, chemical, and machinery industries of Western Europe, excluding Germany. Output of consumer goods, such as textiles, however, is still below pre-war levels. Lagging output of consumer goods imposes many hardships and fosters "black market" trade, which is especially serious in Germany where it adds to the disorganization of the productive system.

Man-power Problems

The inadequacy of industrial manpower is one of the deterrents to production. The population of the Marshall Plan nations of Western Europe increased by about 10 per cent during the war to approximately 270 million, and the proportion of the population of working age has not changed materially; but several millions of skilled workers never returned from the war and the efficiency of urban workers is low because of under-nourishment. An acute situation is illustrated by Germany's plight. The United States and British zones produce food equivalent to 975 calories per person daily—less than two-thirds the present basic consumer ration of 1,550 calories. The gravity of this situation is apparent in view of the fact that about 2,500 calories a day is considered the minimum for a healthful diet and more is required for coal miners and other industrial workers engaged in similarly "heavy" occupations.

Compared with the pre-war years, there is a considerable increase in employment in the service industries, especially in commerce and public administration. There has also been some shift from the "heavy" to the "light" occupations. The principal man-power problem, however, is to supply enough food to improve health and efficiency of workers. And food must come from Europe's tired soil.

Progress in Agriculture

Progress toward recovery in European agriculture has been disappointing. In more than a score of European countries, which together accounted for 90 per cent of Europe's pre-war agricultural output, exclusive of the U.S.S.R., 1947 agricultural production was only about three-quarters of pre-war levels. The relatively poor showing in agriculture is accounted for by unusually bad weather, insufficient fertilizer, scarcity of farm labor, worn-out equipment, and some reduction in livestock numbers. Farm output is particularly low in Hungary, Poland, Rumania, and Yugoslavia—the nations which have been the historic food surplus areas. In the 1946-1947 crop year, output in these countries was less than 60 per cent of pre-war. Production of wheat and other bread grains generally fell less than 20 per cent throughout Europe, but with more people to feed, rations have had to be reduced—in some countries they had to be cut seriously.

Production of animal products, such as meat, lard, milk, butter, and eggs, is far below pre-war levels and below minimum requirements of the

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population. When total food output is low, wheat and other bread grains are in especially great demand for human consumption. Little is left for animals. Moreover, productivity of existing dairy herds is low because of the scarcity of animal feed crops. Tobacco is about the only major agricultural product whose production is up to pre-war standards.

Progress in Transport

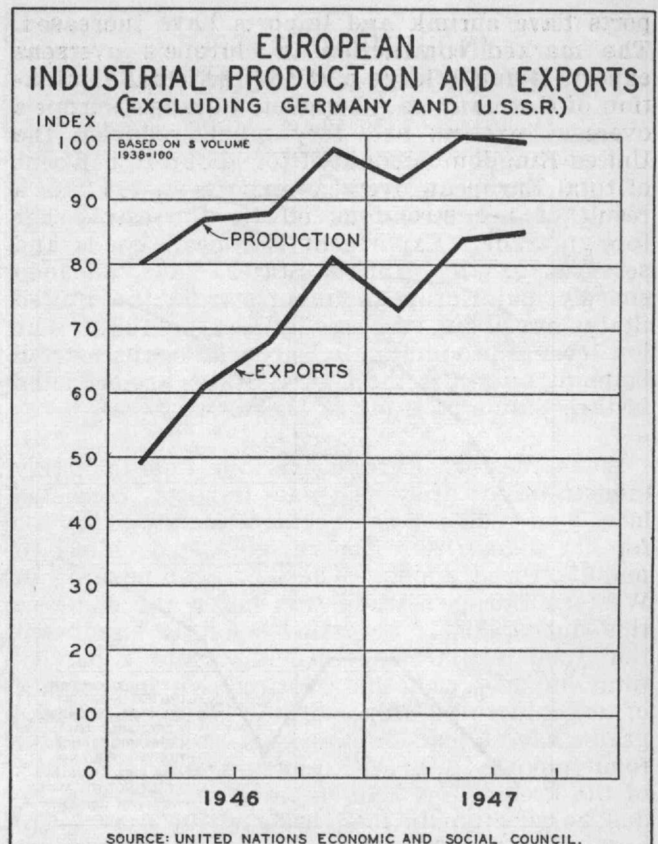
Transportation facilities and railway transportation in particular have made an unusually rapid—if precarious—recovery. In the third quarter of 1947, railway traffic was 25 per cent above pre-war volume. Traffic on inland waterways, such as the Rhine and the Danube, has not made comparable progress; in fact, the good showing of railway transportation may be due in part to the shifting of some traffic from water to rail transportation. Despite the impressive performance of the railways, many facilities, such as freight cars and locomotives, have been kept in service only by repeated repairs. Substantial losses in rolling stock were suffered during the war, and scarcity of steel and timber has hampered replacement.

Progress in International Trade

The gravity of post-war readjustments in Europe is clearly revealed by changes in the volume, direction, and composition of international trade. As the chart shows, the war curtailed exports even more sharply than production. Although export volume appears to have gained somewhat more rapidly than industrial production since the end of the war, little progress in one of these key factors can be made at this time without corresponding gains in the other.

Dollar-wise, international trade, both within Europe and with non-European countries, was higher in the post-war period than before the war, but this was due primarily to wartime inflation from which virtually none of the countries escaped. In terms of 1938 prices, it is perfectly clear that (1) Europe's total trade in 1947 was well below that of 1938; (2) exports of goods and services were relatively much lower than imports; (3) trade with non-European countries was at a relatively higher level than intra-European trade—exports were more than three-fourths of the 1938 value and imports were somewhat larger than in 1938.

The extent of trade recovery from pre-war levels differs very greatly from one country to another. According to figures for the first nine months of 1947, in terms of real goods and services, the United Kingdom and Switzerland were the only countries whose exports were above those of 1938. By heroic efforts, the United Kingdom succeeded in attaining the most favorable relationship of exports to imports. Most of the nations which have relatively low post-war imports are in Eastern Europe. Germany's post-war trade virtually collapsed. Her imports were only 18 per cent and her exports only 9 per cent of pre-war levels. The German trade collapse exerted an especially depressing influence upon all European trade.



SOURCE: UNITED NATIONS ECONOMIC AND SOCIAL COUNCIL.

The origin and destination of European trade have changed materially during the post-war reconstruction period. The trade of European countries with each other has declined. Intra-European exports of commodities have decreased from 65 per cent of total exports in the pre-war period to 57 per cent in 1947, and intra-European imports of commodities have declined from 55 per cent of total imports to 39 per cent. Germany is, of course, the major area of contraction. The role of the United Kingdom has changed from that of net importer to that of an exporter to other European countries.

Great changes have also taken place in the physical volume of Europe's overseas trade. Ex-

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ports have shrunk and imports have increased. The marked contraction in Europe's overseas exports is due in large part to the virtual elimination of Germany as a supplier. Because Europe's overseas exports are very much reduced, the United Kingdom accounted for about 45 per cent of total European overseas exports in 1947, as a result of her strenuous efforts to restore her foreign trade. Exports of European goods and services to the United States have declined sharply, but European imports from the United States are about twice as large as in 1938. The low level of production in European countries and booming output in the United States are reflected in the volume of trade of these two areas.

Since Western Europe has long been a highly industrialized area pre-war imports consisted largely of food for her people and raw materials for her industries. Exports consisted chiefly of manufactured goods. The basic composition of Western Europe's trade was much the same as this during 1947; nevertheless, it is significent that food was not quite so important a part of total imports, and that the relative importance of manufactured imports was doubled. Bread grains have replaced many of the more expensive food imports. These changes are symptomatic of the great effort that is being made to put industry back on its feet, even at the expense of a poorer diet.

To what extent that effort has been successful may be measured by exports. Western Europe's shipments to outside nations were one-fourth below the 1938 total last year, but manufactured goods — which ultimately constitute Europe's buying power—had evidently made a much better recovery than other products. Exports of machinery are close to pre-war levels, despite Germany's disappearance as a supplier. Germany's pre-war machinery markets are now being supplied by England and Switzerland.

Trade among the European nations themselves has been sharply reduced, notably in raw materials such as coal and timber and in semi-manufactured products, particularly iron and steel. An important factor here, of course, is Germany's low level of production in steel products.

Germany: the Weakest Link

It is quite apparent that European recovery has been seriously retarded by the economic paralysis of Germany. Pre-war Germany had 69 million highly industrious people, occupying 181,000 square miles in the heart of Europe. The importance of the three Western zones in the industrial structure of Western Europe is indicated by the fact that in 1938 they produced about one-third of the coal, about two-fifths of the basic steel, and about one-fifth of the total industrial production of that area. Germany supplied other European countries with substantial quantities of manufactured products from her steel, chemical, and machinery industries. Never producing more than 80 per cent of her own food supplies, she made up the deficit by exporting manufactured products in the production of which she excelled by reason of her rich coal deposits, skilled labor, and scientific knowledge.

As a result of the war, Germany lost 24 per cent of her territory, chiefly agricultural land and the industrial area of Silesia, and 2 million able-bodied men from her labor force. Political administration is complicated by the occupation of four powers supervising demilitarization and remobilization of industrial resources toward peaceful pursuits. In Germany today, production of coal, so important to the economy of Western Europe, has been restored to about 55 per cent of the pre-war level; but production of steel, of equal importance to the restoration of Germany and of Europe, was only one-sixth of the pre-war tonnage in 1947. As a result of the extremely low level of output, foreign trade has almost disappeared.

Need for Continued Assistance of the United States

Such recovery as Western Europe has already made was not accomplished without generous assistance from the United States. Between July 1, 1945 and December 31, 1947, the United States made available $11.7 billion of aid, consisting of grants, loans, and property credits. By the end of that period about 84 per cent of the amount made available had already been utilized. While this amount may seem generous, it represents a smaller amount of goods than it had been intended to send. Increasing prices during the period reduced the buying power of the dollars that were made available. By mid-1947 it became increasingly clear that Western Europe needed still more help in order to break out of the vicious circle of mutually aggravating problems, and put her economy on a self-supporting basis.

In response to Secretary Marshall's request of the Western European countries to budget their minimum recovery requirements, sixteen Western European countries met in Paris and prepared a specific list of most urgently needed materials. For the sixteen cooperating countries

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and Western Germany, recovery requirements were scheduled on an annual basis through 1951. The entire program contemplates raising output of European agricultural products by 1951-1952 to a level a little below that prevailing in the pre-war period, but the sights for output of industrial products have been raised substantially above pre-war levels. The goal for coal output has been set at 6 per cent above pre-war levels, crude steel at 15 per cent above, and electric generating capacity at 68 per cent in excess of pre-war output. The entire program calls for a large amount of assistance from Western Hemisphere countries, and in particular from the United States.

On this side of the Atlantic, the schedule was carefully screened, pared, and evaluated in terms of its impact on our economy and its drain on our resources. On April 3, 1948, President Truman signed the Foreign Assistance Act of 1948, which authorized the expenditure of $5.3 billion for European recovery during the first year, together with $275 million for Greek-Turkish military aid, and $463 million for economic and military aid to China. This sum is roughly one-third of the amount estimated to be required for European recovery through June 1952.

II. Finance and Inflation

The basic international economic problem has always been essentially a physical one—that of exchanging goods and services. If financial problems ever obscured this fact, they certainly do not now. It has become painfully clear to all countries, and particularly those devastated by the war, that their basic difficulty today is a shortage of goods and services. The so-called dollar shortage is merely a reflection of the tremendous foreign demand for United States goods—goods which must be paid for in dollars.

Yet, financial considerations are very important, for they can greatly facilitate or greatly hinder the solution of the physical problems. It is extremely significant, for example, that world-wide inflation has shown once again how serious the consequences of an excessive money supply can be.

International finance is simply the process of paying for goods and services exchanged among countries. Basically, international trade is an exchange of goods for goods; foreign exchange serves merely as a convenient means of actual payment. As in domestic trade, deposit balances are built up through the sale of goods and services and by borrowing. For example, foreigners build up dollar balances when they export goods and services to the United States. They draw down these dollar balances as they purchase our goods and services. If foreigners buy more goods here than they sell, they must in some way obtain enough dollars to pay the difference. Borrowing is one method of building up dollar balances in this country. Another is through a favorable trade balance with a third country which, in turn, has available dollar balances. Dollars may be acquired also by selling gold to the United States.

This is the problem confronting Europe. Its exports have been held down for a number of reasons: (1) production is at relatively low levels, mainly because of war devastation and inflation; (2) most of its productive facilities must be used to sustain the home population; and (3) receipts from investments, shipping, travel expenditures, and other services no longer offset a surplus of goods imported over goods exported. At the same time, Europe has imported more in order to restore production and to make up for the grave deficiencies in the standards of living of its people.

Europe's physical problem is that of reducing this deficit by importing less and exporting more. Yet, without raw materials, plant, and equipment, it can not increase production sufficiently to do either. Thus, imports must remain large for some time. What are the alternatives? Exports cannot be increased sufficiently to balance the necessary imports. Imports could be reduced—by controls, by drastically lowering the price levels of European countries, or by revaluing their currencies—to balance exports. But this would mean throwing those countries nearly entirely on their own resources. It would mean reducing living standards which, in many cases, are already at a minimum subsistence level, and would delay for many years the recovery of Europe to its pre-war status.

Europe must continue to import substantially more than she exports if recovery is to be achieved in any reasonable length of time. The deficit, then, will continue. The financial problem is how to pay for it. Since the United States is the only major nation able to supply Europe with the necessary goods, it shares with the European countries the problem of financing the

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deficit. The dollar is the currency most in demand. What are the alternative methods of supplying dollars?

Post-war Financial Aid

Foreign countries own a considerable amount of gold, bank deposits in this country, and other assets which conceivably they could use to pay for their imports. In 1946 and 1947 they reduced their gold and dollar holdings and liquidated other assets to the extent of $6.7 billion, thus financing 27 per cent of the deficit in 1946 and 40 per cent in 1947. This method has been virtually exhausted. For although these total holdings may still seem fairly large, they are not distributed among the countries according to needs. A sizable part represents reserves held against the money supply to meet legal requirements and to help assure confidence in the currency, and part must be maintained as working balances for a large volume of international transactions at higher prices.

FINANCING UNITED STATES FOREIGN TRADE

	Millions $		Percent distribution	
	1946	1947	1946	1947
Exports of goods and services	15,300	19,603	—	—
Imports of goods and services	7,100	8,327	—	—
Surplus	8,200	11,276	—	—
Method of financing:				
U. S. loans and investments	3,000	4,655	36%	41%
Liquidation of long-and short-term foreign assets (including gold)	2,200	4,494	27	40
Gifts and other unilateral transfers	3,100	2,448	38	22
Liquidation of dollar assets by Monetary Fund	—	464	—	4
Loans by the International Bank	—	297	—	3
Total	8,200	11,276	100%	100%

Note: Columns will not add to totals because of unavoidable errors and omissions in published data.
Source: U. S. Department of Commerce.

Foreign countries have borrowed extensively to help fill the gap between their imports and exports. Borrowing of one sort or another from the United States financed 36 per cent of the 1946 deficit and 41 per cent of the 1947 deficit with us. Although lend-lease credits gradually declined throughout 1946, substantial credits were received on sales of surplus property. Loans made by the Export-Import Bank also rose substantially during 1946. The British loan of $3-3/4 billion was authorized in the middle of the year. During 1947 these sources of borrowing had been practically exhausted. The surplus property program had been virtually completed, the British loan had been used up, credits of the Export-Import Bank declined. Several countries made use of the facilities of the International Bank for Reconstruction and Development and the International Monetary Fund, but only limited assistance could come from these institutions. The Bank can make only higher-quality loans for specific purposes, and the Fund was organized primarily to assist in overcoming temporary balance of payment difficulties and to help maintain more stable foreign exchange rates. Some countries obtained funds from private investors by floating securities in this country, but the risk involved and the terms required by the borrowers are such that only a very limited amount of private credit is available.

The remainder of the deficit—38 per cent in 1946 and 22 per cent in 1947—was financed by gifts and other unilateral transfers. Lend-lease was rapidly being terminated but was followed by UNRRA. As shipments under UNRRA virtually ceased there was a considerable increase in contributions under the United States Foreign Relief Program. Civilian supplies for occupied countries continued to be furnished, and substantial private payments and contributions were made. However, these were essentially temporary relief measures, and what was needed was a form of financial assistance directed to promoting recovery.

The European Recovery Program goes straight to the heart of the problem. About half of the post-war deficit of all foreign countries with this country has been accounted for by the ERP countries, and most of this country's foreign aid has gone to them. The total amount of aid involved in the ERP is substantially equal to what the United States has been doing in the recent past. Of the $5.3 billion authorized for the first year, approximately one-fourth was originally scheduled to go to the United Kingdom and its dependencies, somewhat less to France and its dependencies, one-sixth to the "Benelux" countries and their dependencies, and approximately one-eighth to Italy.

The form of aid to be given—whether as loans or grants—will depend basically on the capacity of the recipient country to repay and will also depend on the types of goods the European countries need. Generally speaking, consumer goods and certain raw materials will take the form of grants, and capital equipment and certain other raw materials will be financed by loans.

Inflationary Effects of ERP

The methods by which the United States raises the funds to finance the program will have an important influence on the level of prices in this

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country. ERP gives to the participating European countries the ability to demand goods in the United States. If, therefore, the Treasury obtains sufficient funds for the program by taxation or the sale of securities to nonbank investors, demand for United States goods is merely transferred from citizens of this country to foreign purchasers. But if the Treasury should obtain the funds by borrowing from the banking system, the money supply would be increased, and foreigners would be given power to purchase our goods, without any diminution of our own demand. If foreign countries used their gold and dollar holdings to buy American goods, the result would be the same. Both methods would tend to force prices up in this country.

It now appears, however, that the $5.3 billion of financial aid authorized by the United States in the next year will be financed out of tax receipts. The principal direct effect will be diversion of demand from our taxpayers to foreign buyers. It may also direct a larger portion of this demand toward goods which are already in short supply. But this is not the whole story. The program will mean a substantial reduction in the cash surplus available to the Treasury for debt retirement, and this has been our most potent weapon for combating inflation.

These are all factors operating on the side of *demand* for our goods. The program will have little effect on the total *supply* of our goods but will, of course, divert more of it from domestic to foreign use. This diversion, however, does not enhance the inflationary effect because any purchaser, whether foreign or domestic, takes goods out of the market and reduces the supply available to others. The value of goods to be provided constitutes a very small portion of our total output, but in many cases they are goods already in short supply and the prices of which have a strong influence on our general price level.

On balance, then, the impact of ERP on this country is apt to be inflationary, but probably no more so than the aid already given. The effect on the participating European countries, on the other hand, will be deflationary. The recovery program should tend to decrease the ratio of their money supply to available goods. The immediate effect is to increase the supply of goods without generating a corresponding increase in incomes and the money supply. Furthermore, the deflationary impact may be enhanced to the extent that the provision which permits the ECA administrator to require the deposit of local currencies commensurate with the grants-in-aid received results in such local funds being withheld from use.

Need for Currency Stabilization

Inflation in varying degrees has been one of the heritages of war in practically all of the European countries. Efforts to combat inflation have met with varying degrees of success, but in many countries inflation, or the threat of it, continues as a major obstacle to economic recovery.

Inflation, whether of the suppressed or open variety, has seriously diminished the effectiveness of recovery efforts. Under *suppressed inflation,* controls have limited expenditure and resulted in the building up of liquid assets. But the possession of money has lost some of its importance because of the limited ability to exchange it for scarce goods. The incentive to work is therefore diminished. Where controls are ineffective "black markets" flourish, parasitic activities multiply, and, in extreme inflation, goods and foreign exchange are hoarded and monetary transactions are largely displaced by barter. Firms producing barterable consumers' goods can bid raw materials away from companies supplying products more urgently needed for reconstruction.

In countries where there is *open inflation,* prices have soared to fill the gap between money incomes which are excessive in relation to the available supply of goods. Money continues to afford an incentive for work, except in extreme inflation, but real income tends to be redistributed in favor of profits and at the expense of wages, salaries, and other relatively fixed incomes. The rise in profits tends to divert resources toward the production of luxury goods and away from reconstruction and more essential consumers' goods. The squeeze on labor incomes causes laborers to demand higher wages, which in turn may lead to higher prices and further inflation.

Inflation, then, regardless of the type, has tended to divert production from more urgently needed goods into less essential channels. It has encouraged wasteful types of economic activity and inefficient methods of production, and has weakened the incentive to work. Moreover, the currencies of most of the countries are overvalued in relation to foreign currencies, especially in terms of the dollar. The relatively low price of foreign currencies stimulates imports but makes it more difficult to expand exports. On balance, these terms of trade are probably favorable in the early stages of recovery for those countries in urgent need of essential imports. However, some revision of the foreign value of their currencies more in line with their purchasing power will be an essential step in expanding exports to meet the deficit in their balance of payments on trade account.

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In order that monetary stability may be reestablished it will be necessary to remove the basic causes of the inflationary pressures. In general, these are an excess of public expenditures over receipts, and a higher level of private investment than can be supported out of savings. In countries with severe inflation, the problem is intensified by the hoarding of commodities and foreign exchange. Thus, effecting a balanced budget and an increase in saving—perhaps even some form of enforced saving in some countries—are essential steps to currency stabilization.

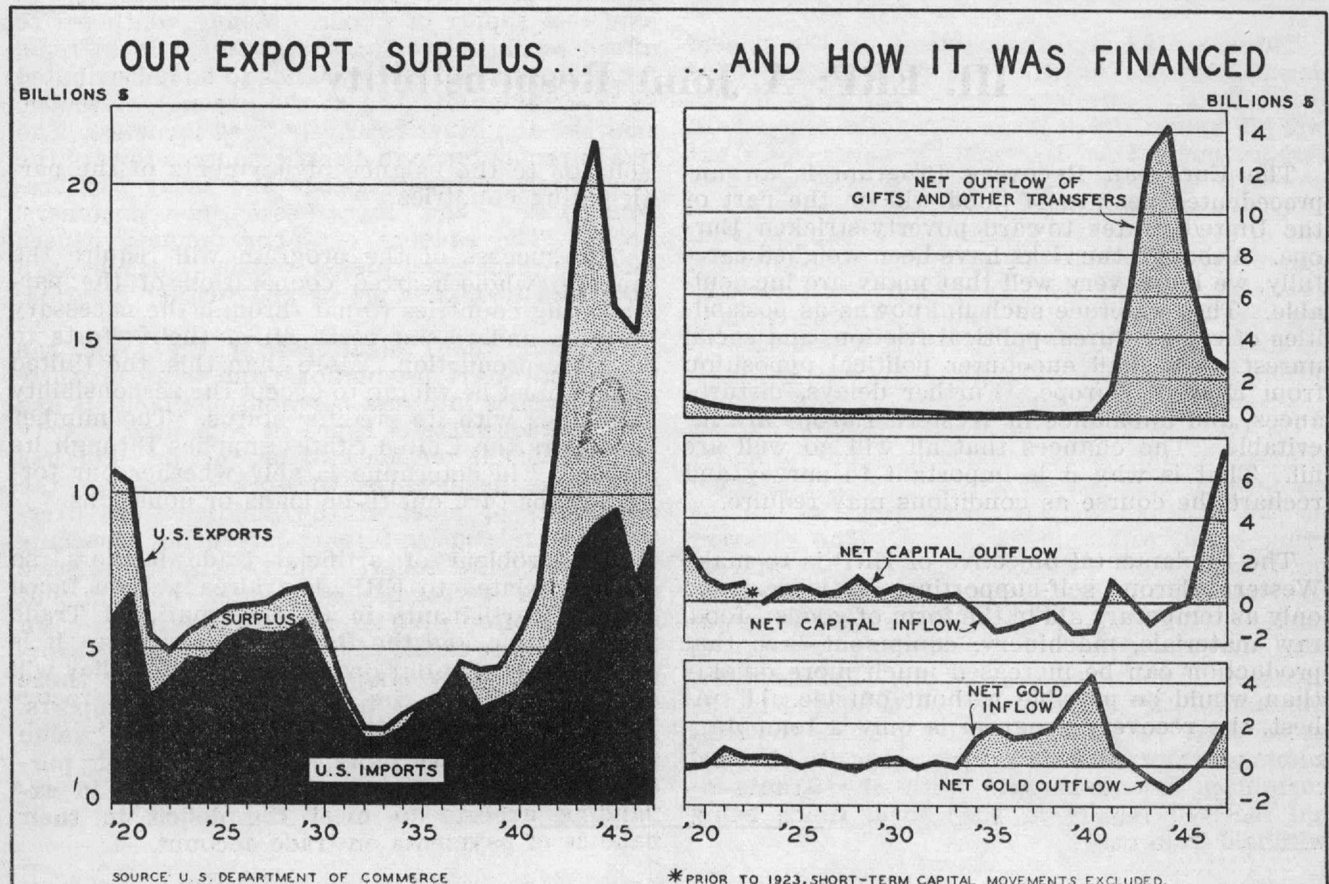
Solving the Dollar Shortage

A shortage of dollars is not a new problem. For several decades the United States has sold more goods and services abroad than it has purchased from foreign countries. This means that foreign countries have long been in the position of having to find ways of financing their trade deficit with the United States. In other words, the United States has not been supplying enough dollars by its imports to enable foreign purchasers to pay for exports. The balance has been supplied by loans, by unilateral transfers (those not requiring repayment), and by an inflow of gold.

The accompanying chart shows the dollars used by foreigners to buy United States exports, the dollars supplied through imports, and the deficit of foreign countries in their balance of payments on trade account with the United States. The deficit was especially large during the two war periods when the United States was sending large amounts of war supplies to its allies.

During the period 1914-1947, imports supplied about 62 per cent of the dollars foreigners needed to pay for United States exports. Over $25 billion was made available by loans and investments abroad (net outflow of short-and long-term capital) and about $55 billion, mostly in World War II, was supplied through lend-lease, relief, and other forms of financial aid. Foreigners secured approximately $18 billion from net sales of gold to the United States.

Why this persistent shortage of dollar exchange? It reflects two things. Dollars now are made to appear scarce, in part, because prices of the dollar are low in terms of foreign currencies. If rates of foreign exchange were free to move in accordance with changes in demand and supply, a rising price of dollars in terms of foreign currencies would ration out the available



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supply of dollars to the highest bidders. The alternative—the one chosen—is to peg rates of exchange and ration out the scarce dollars for only the most essential imports.

However, the mere persistence of the dollar shortage indicates a more basic and deep-rooted cause. Prior to World War I, the United States had been a debtor nation for many years. It had to export enough goods and services not only to pay for its imports, but also to meet interest and principal payments on its foreign debts. Since World War I, as previously shown, the United States has become a creditor nation. It has been exporting goods to meet the demand coming from dollars supplied by imports *plus* the dollars supplied by new loans and investments abroad. As long as new loans and investments exceed the returning interest and principal payments which are building up, United States exports will tend to exceed imports.

The causes of the apparent shortage of dollars indicate possible approaches to a solution. One would be to free foreign exchange rates and permit the price of dollar exchange to rise until demand would be reduced to the available supply. This would practically throw these countries back on their own resources because the high price of dollars would nearly shut off imports from the United States, and without imports they could produce very little for export even though the dollar proceeds would be high.

A more promising and humanitarian approach is to provide financial assistance in supplying the participating countries with materials and equipment essential for their economic recovery. It must be recognized, however, that this is only a temporary remedy. A real solution requires that these countries expand their exports sufficiently to pay for their imports and to meet the payments on their foreign indebtedness. This will require not only a substantial increase in production and currency stabilization, but also the removal of controls and opening of international trade channels. Debtor countries must expand their exports to the creditors if international debts are to be serviced and loans repaid. This means that the United States, as the world's greatest creditor nation, must adopt a foreign trade policy consistent with its creditor status. It must be willing to import more than it exports, otherwise its foreign loans never will be serviced or repaid.

III. ERP: A Joint Responsibility

The European Recovery Program is an unprecedented gesture of good will on the part of the United States toward poverty-stricken Europe. Although the risks have been weighed carefully, we know very well that many are incalculable. They embrace such unknowns as possibilities of crop failures, political friction, and social unrest. We shall encounter political opposition from Eastern Europe. Further delays, disturbances, and imbalance in Western Europe are inevitable. The chances that all will go well are nil. That is why it is important to survey and rechart the course as conditions may require.

The fundamental objective of ERP is to make Western Europe self-supporting. It is designed only as temporary aid in the form of goods—food, raw materials, machinery, equipment — so that production can be increased much more quickly than would be possible without outside aid. At best, the recovery program is only a temporary solution to the balance of payments of the participating countries.

The success of the program will require the sincere, whole-hearted cooperation of the participating countries to put through the necessary reforms and to put forth all of their efforts to increase production. More than this, the United States must be willing to accept the responsibility that goes with its creditor status. The number of dollars the United States supplies through its imports will determine largely whether our foreign loans turn out to be loans or donations.

The problem of artificial trade barriers, so closely related to ERP, has already been faced by the participants in the International Trade Organization and the Bogota conferences. It is to be hoped that our own foreign trade policy will demonstrate that the United States fully recognizes its responsibilities and opportunities.

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BUSINESS STATISTICS

Production
Philadelphia Federal Reserve District

Indexes: 1923-25 = 100	Adjusted for Seasonal Variation						Not Adjusted		
				Per cent change					
	Apr. 1948	Mar. 1948	Apr. 1947	Apr. 1948 from Month ago	Apr. 1948 from Year ago	1948 from 4 mos. 1947	Apr. 1948	Mar. 1948	Apr. 1947
INDUSTRIAL PRODUCTION	111p	110	106r	+ 1	+ 5	+ 2	108p	110	104
MANUFACTURING	114p	112	108r	+ 2	+ 5	+ 3	110p	112	106
Durable Goods	124p	123	116	0	+ 7	+ 6	......	......	......
Consumers' Goods	105p	101	100	+ 4	+ 4	+ 1	......	......	......
Metal products	143	144r	144	0	0	+ 2	138	145r	139
Textile products	79p	75	70	+ 5	+12	+ 6	76p	77	68
Transportation equipment	123p	125	111r	— 2	+11	+ 5	130p	133	120r
Food products	120p	119	126	+ 1	— 5	— 5	114p	114	119
Tobacco and products	127	117	109	+ 8	+16	0	115	108	99
Building materials	56p	56	48r	— 1	+16	+ 5	50p	49	48r
Chemicals and products	170p	167	147r	+ 2	+16	+ 9	173p	167	149r
Leather and products	94p	94	89	0	+ 6	+11	92p	96	87
Paper and printing	117	115	118	+ 2	— 1	0	120	117r	120
Individual Lines									
Pig Iron	86	86r	89	0	— 4	— 1	97	99r	101
Steel	106	113r	108	— 6	— 2	+ 5	111	120r	113
Iron castings	90	91	97	— 1	— 7	— 3	94	96	101
Steel castings	115	97	106	+18	+ 8	— 5	117	109	108
Electrical apparatus	237	226	234	+ 5	+ 1	+ 1	206	210	203r
Motor vehicles	25	30	43r	—14	—41	—31	32	32	54r
Automobile parts & bodies	108	118	117r	— 9	— 8	— 1	117	129	128r
Locomotives and cars	55	57	55	— 2	+ 1	— 8	59	61r	59
Shipbuilding	......	......	......	+ 5	+49	+25	......	......	......
Silk and rayon	92	88	84	+ 4	+10	+ 3	90	91	82
Woolens and worsteds	84p	80	72	+ 4	+15	+ 8	76p	77	66
Cotton products	37p	38	43	— 3	—15	—18	38p	40	45
Carpets and rugs	112p	109	88	+ 3	+27	+29	107p	109	84
Hosiery	82	82	69	+ 1	+20	+11	82	85	69
Underwear	147	138	132	+ 7	+12	+ 8	144	150	129
Cement	97p	94	74r	+ 3	+30	+ 1	76p	73	74r
Brick	56	61	54	— 8	+ 3	+ 3	59	60	57
Lumber and products	31	31r	29	+ 2	+ 8	+ 7	29	29	28
Bread & bakery products	......	......	......	— 5	— 7	— 5	104	109r	112r
Slaughtering, meat pack.	137	121	112	+13	+22	+ 7	133	114	109
Sugar refining	79	72	94	+10	—16	—13	102	111	122
Canning and preserving	178p	178	198r	0	—10	— 6	149p	159	166
Cigars	128	118	109	+ 8	+17	+ 2	116	109	99
Paper and wood pulp	98	98r	91	0	+ 7	+ 8	99	100r	92
Printing and publishing	121	119	124	+ 2	— 2	— 2	124	121	126
Shoes	88p	93r	90	— 6	— 2	+ 5	88p	99r	90
Leather, goat and kid	99p	95	87	+ 5	+14	+20	96p	94	84
Explosives	108	103	45	+ 5	+142	+37	109	103	45
Paints and varnishes	110	114	104	— 4	+ 6	+ 7	116	117r	109
Petroleum products	233p	222	205r	+ 5	+14	+ 9	233p	220	205r
Coke, by-product	156p	162	159	— 4	— 2	+ 2	162p	168	166
COAL MINING	66	67	67	— 2	— 1	— 3	65	67	66
Anthracite	66	68	64	— 3	+ 3	+ 2	66	68	64
Bituminous	67	61	90	+10	—25	—21	61	62	82
CRUDE OIL	288	284	283	+ 2	+ 2	+ 1	297	289	292
ELECTRIC P'W'R—OUTPUT	501	488	446	+ 3	+12	+ 9	491	498	437
Sales, total	499	516	450	— 3	+11	+10	514	511	463
Sales, to industries	349	359	318	— 3	+10	+ 7	352	342	322
BUILDING CONTRACTS									
TOTAL AWARDS+	210	198	145	+ 6	+45	+63	202	172	139
Residential+	142	169	142	—16	— 1	+24	132	128	132
Nonresidential+	227	169	137	+34	+66	+58	231	169	139
Public works & utilities+	364	333	166	+ 9	+120	+201	335	303	153

* Unadjusted for seasonal variation.
\+ 3-month moving daily average centered at 3rd month.
** Increase of 1000% or more.

p Preliminary.
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Local Business Conditions*

Percentage change—April 1948 from month and year ago	Factory employment		Factory pay rolls		Building permits value		Retail sales		Debits	
	Mar. 1948	Apr. 1947	Mar. 1948	Apr. 1947	Mar. 1948	Apr. 1947	Mar. 1948	Apr. 1947	Mar. 1948	Apr. 1947
Allentown	— 1	— 3	— 5	+ 3	+ 32	+ 51	+ 1	+58	— 4	+34
Altoona	+ 1	— 5	+ 4	+11	+ 47	— 84	—29	— 7	— 1	+ 8
Harrisburg	— 1	— 3	— 3	+ 7	+209	+150	+ 2	+17	— 6	+21
Johnstown	— 3	+ 2	—15	— 4	— 6	— 60	— 8	+15	— 6	+13
Lancaster	— 1	+ 3	— 1	+16	+109	+139	—11	+ 5	+18	+26
Philadelphia	— 1	0	0	+12	— 35	+ 22	—15	0	— 4	+15
Reading	— 1	+ 2	— 2	+16	— 37	— 29	+ 2	+10	+ 4	+11
Scranton	— 3	+ 3	— 5	+24	+148	+250	—13	+ 5	0	+11
Trenton	......	......	......	......	+382	+120	— 9	+ 8	+12	+ 6
Wilkes-Barre	+ 1	— 7	+ 3	+14	— 99	— 51	—10	+ 6	— 6	+11
Williamsport	— 1	— 8	— 3	+ 5	— 28	+ 4	......	......	+ 4	+18
Wilmington	— 1	+ 6	0	+18	+ 28	+ 78	— 3	+21	— 9	+11
York	— 1	0	— 2	+ 8	+ 7	— 63	—11	+ 4	+ 1	+ 7

* Area not restricted to the corporate limits of cities given here.
** Increase of 1000% or more.

Production Workers in Pennsylvania Factories

Summary Estimate—April 1948

	Employment	Weekly pay rolls	Weekly man-hours worked
All manufacturing	1,099,800	$54,509,000	43,445,000
Durable goods industries	624,400	33,658,000	24,751,000
Nondurable goods industries	475,400	20,850,000	18,694,000

Changes in Major Industry Groups

Indexes (1939 average = 100)	Employment			Pay rolls		
	Apr. 1948 Index	Per cent change from Mar. 1948	Per cent change from Apr. 1947	Apr. 1948 Index	Per cent change from Mar. 1948	Per cent change from Apr. 1947
All manufacturing	128	—1	— 1	283	—2	+11
Durable goods industries	154	—1	— 2	320	—2	+10
Nondurable goods industries	105	—1	0	239	—1	+12
Food	118	—2	— 5	227	—2	+ 5
Tobacco	100	—1	+ 4	221	—1	+11
Textiles	88	0	+ 5	221	—2	+26
Apparel	95	—1	+ 2	247	—2	+18
Lumber	93	—2	+ 1	198	—1	+18
Furniture and lumber products	101	—3	— 1	227	—6	+ 7
Paper	119	—1	0	261	0	+13
Printing and publishing	137	+1	+ 1	281	+6	+ 9
Chemicals	120	—1	— 1	246	0	+ 8
Petroleum and coal products	149	—1	+ 5	290	0	+17
Rubber	146	—9	—20	265	—7	—27
Leather	91	—5	— 6	177	—8	— 7
Stone, clay and glass	135	0	— 3	290	+1	+ 9
Iron and steel	138	—1	— 1	281	—3	+ 9
Nonferrous metals	149	0	—11	295	0	— 2
Machinery (excl. elect.)	211	—1	+ 7	439	—1	+19
Electrical machinery	225	—1	— 2	473	—1	+13
Transportation equip. (excl. auto)	215	—2	— 6	415	—2	+15
Automobiles and equipment	159	—7	—18	321	—7	—12
Other manufacturing	133	—1	—10	261	—2	— 4

Average Earnings and Working Time

April 1948 Per cent change from year ago	Weekly earnings		Hourly earnings		Weekly hours	
	Average	Ch'ge	Average	Ch'ge	Average	Ch'ge
All manufacturing	$49.56	+12	$1.255	+11	39.5	+ 1
Durable goods indus.	53.90	+12	1.360	+11	39.6	0
Nondurable goods industries	43.86	+12	1.115	+11	39.3	+ 1
Food	43.06	+10	1.051	+11	41.0	0
Tobacco	29.01	+ 7	.757	+ 2	38.3	+ 5
Textiles	44.89	+19	1.143	+13	39.3	+ 5
Apparel	36.81	+16	.946	+11	38.9	+ 5
Lumber	39.81	+17	.964	+10	41.3	+ 6
Furniture and lumber products	41.52	+ 8	.997	+ 8	41.7	0
Paper	47.44	+13	1.078	+12	44.0	+ 1
Printing and pub.	57.95	+ 8	1.502	+11	38.6	— 3
Chemicals	48.99	+10	1.188	+ 8	41.2	+ 2
Petroleum and coal products	59.06	+12	1.515	+14	39.0	— 2
Rubber	45.17	— 9	1.287	+ 3	35.1	—11
Leather	33.37	— 1	.980	+11	34.1	—11
Stone, clay and glass	49.34	+12	1.190	+10	41.4	+ 2
Iron and steel	54.73	+11	1.420	+12	38.5	— 2
Nonferrous metals	51.66	+10	1.323	+12	39.0	— 2
Machinery (excl. electrical)	52.80	+12	1.301	+10	40.6	+ 2
Electrical machinery	58.75	+15	1.455	+12	40.4	+ 3
Transportation equip. (excl. auto)	58.80	+22	1.476	+10	39.8	+11
Automobiles and equip.	55.66	+ 7	1.359	+10	41.0	— 3
Other manufacturing	41.17	+ 7	1.082	+ 9	38.0	— 2

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Wholesale trade unadjusted for seasonal variation	Per cent change April 1948 from Month ago	Year ago	1948 from 4 mos. 1947
Sales			
Total of all lines	+ 7	+ 5	+ 2
Dry goods	+10	— 6	— 8
Electrical supplies	+22	+25	0
Groceries	+15	+26	+ 7
Hardware	+11	—12	— 2
Jewelry	+ 9	+15	+ 6
Paper	+ 7	+ 5	+ 4
Inventories			
Total of all lines	+ 2	+11	....
Dry goods	+ 6	+ 9	....
Electrical supplies	0	+ 3	....
Groceries	— 6	— 7	....
Hardware	+ 5	+33	....
Jewelry	+ 1	—19	....
Paper	+ 5	+65	....

Source: U. S. Department of Commerce.

Prices	Apr. 1948	Per cent change from Month ago	Year ago	Aug. 1939
Basic commodities (Aug. 1939 = 100)	321	+ 1	0	+221
Wholesale (1926 = 100)	163	+ 1	+10	+117
Farm	187	0	+ 5	+206
Food	177	+ 2	+ 9	+163
Other	149	+ 1	+13	+ 85
Living costs (1935-1939 = 100)				
United States	169	+ 1	+ 8	+ 72
Philadelphia	169	+ 2	+ 9	+ 73
Food	203	+ 3	+11	+118
Clothing	191	0	+ 6	+ 93
Fuels	135	0	+ 8	+ 40
Housefurnishings	198	+ 1	+10	+ 97
Other	148	+ 4	+ 7	+ 47

Source: U. S. Bureau of Labor Statistics.

Indexes: 1935-1939 = 100	Adjusted for seasonal variation: Apr. 1948	Mar. 1948	Apr. 1947	Per cent change April 1948 from Month ago	Year ago	1948 from 4 mos. 1947	Not adjusted: Apr. 1948	Mar. 1948	Apr. 1947
RETAIL TRADE									
Sales									
Department stores—District**	278p	263	257	+ 6	+ 8	+10	261p	284	247r
Philadelphia**	238	239	235	0	+ 1	+ 8	229	258	228
Women's apparel—District	267	213	259	+25	+ 3	+ 3	240	290	249
Philadelphia	283	222	273	+28	+ 4	+ 3	254	297	262
Furniture	....	....	....	+ 7*	+11*	....	....	....	....
Inventories									
Department stores—District	260p	261	221	0	+18	....	266p	261	225
Philadelphia	233	226	211	+ 3	+11	....	235	228	213
Women's apparel—District	253	246	246	+ 3	+ 3	....	228	241	222
Philadelphia	291	285	283	+ 2	+ 3	....	256	274	249
Furniture	....	....	....	+ 4*	+11*	....	....	....	....
FREIGHT-CAR LOADINGS									
Total	129	129	145	0	—11	— 7	122	121	138
Merchandise and miscellaneous	122	133	137	— 8	—11	— 5	121	128	135
Merchandise—l.c.l.	79	83	96	— 5	—18	—15	79	83	96
Coal	148	107	178	+38	—17	—14	118	110	143
Ore	361	191	301	+89	+20	+16	188	84	156
Coke	159	173	211	— 9	—25	— 6	128	163	171
Forest products	90	93	97	— 3	— 7	— 9	76	81	82
Grain and products	105	114	136	— 8	—23	—20	98	108	127
Livestock	87	80	104	+ 9	—16	—23	80	74	95
MISCELLANEOUS									
Life insurance sales	210	182	207	+16	+ 1	0	210	189	207
Business liquidations									
Number	....	....	....	+75*	+31*	+37*	31	18	24
Amount of liabilities	....	....	....	+228*	+175*	+33*	54	17	20
Check payments	246	251	224	— 2	+10	+11	241	249	219

* Computed from unadjusted data. p Preliminary. r Revised.
** Indexes adjusted for seasonal variation have been revised; earlier data may be obtained upon request.

BANKING STATISTICS

Reporting member banks (Millions $)	May 26 1948	Changes in — four wks.	One year
Assets			
Commercial loans	496	....	+ 54
Loans to brokers, etc.	17	....	....
Other loans to carry secur.	15	+ 1	— 6
Loans on real estate	76	+ 4	+ 2
Loans to banks	8	+ 6	+ 1
Other loans	252	+ 1	+ 47
Total	864	+12	+ 98
Government securities	1372	—20	—104
Other securities	270	+14	+ 26
Total investments	1642	— 6	— 78
Total loans & invest.	2506	+ 6	+ 20
Reserve with F. R. Bank	496	+23	+ 34
Cash in vault	44	+ 2	+ 4
Balances with other bks.	98	— 8	— 1
Other assets—net	58	....	+ 4
Liabilities			
Demand dep. adjusted	2040	+29	+ 36
Time deposits	446	+10	+ 9
U.S. Gov. Deposits	57	— 3	+ 6
Interbank deposits	323	—18	+ 4
Borrowings	7	+ 5	+ 2
Other liabilities	27	— 1	+ 2
Capital account	302	+ 1	+ 2

MEMBER BANK RESERVES AND RELATED FACTORS

Third Federal Reserve District (Millions of dollars)	Changes in weeks ended May 5	May 12	May 19	May 26	Ch'ges in four weeks
Sources of funds:					
Reserve Bank credit extended in district	+ 2	+ 3	— 1	— 4	....
Commercial transfers (chiefly interdistrict)	+18	— 6	+25	+63	+100
Treasury operations	+17	—43	—44	—11	—81
Total	+37	—46	—20	+48	+19
Uses of funds:					
Currency demand	+ 2	+ 3	— 6	+ 2	+ 1
Member bank reserve deposits	+35	—49	—14	+46	+18
"Other deposits" at Reserve Bank	....	....	....	....	....
Other Federal Reserve accounts	....	....	....	....	....
Total	+37	—46	—20	+48	+19

Member bank reserves (Daily averages; dollar figures in millions)	Held	Re-quir'd	Ex-cess	Ratio of excess to re-quired
Phila. banks				
1947 May 1-15	$414	$408	$ 6	1%
1948 Apr. 1-15	414	405	9	2
Apr. 16-30	410	404	6	2
May 1-15	419	412	7	2
Country banks				
1947 May 1-15	$377	$332	$ 45	13%
1948 Apr. 1-15	391	348	43	12
Apr. 16-30	391	348	43	12
May 1-15	392	350	42	12

Federal Reserve Bank of Phila. (Dollar figures in millions)	May 26 1948	Changes in— Four weeks	One year
Discounts & advances	$ 19.0	$+ .9	$+ 8.3
Industrial loans	.6	+ .1	— 1.0
U.S. securities	1470.9	+ 10.9	—193.6
Total	$1490.5	$+ 11.9	$—186.3
Fed. Res. notes	$1617.3	$— 3.4	$— 27.1
Member bank dep.	822.5	+ 18.7	+ 35.7
U. S. general acct.	168.3	+ 73.8	+122.4
Foreign deposits	28.6	— .7	— 2.5
Other deposits	1.6	— .4	....
Gold cert. reserves	1152.8	+ 77.1	+306.9
Reserve ratio	43.7%	+1.5%	+10.0%

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