

BACKGROUND MEMORANDUM FOR THE PRESS FROM THE STATE AND TREASURY
DEPARTMENTS CONCERNING TRIPARTITE DISCUSSIONS

London Discussions

1. During Secretary Snyder's visit to London in July, the Secretary, Ambassador Douglas, and Ambassador Harriman had a general exchange of views with the Chancellor of the Exchequer, Sir Stafford Cripps, the President of the Board of Trade, Mr. Harold Wilson, and the Canadian Minister of Finance, Mr. Douglas Abbott, concerning the balance of payments between the dollar and sterling areas. The conversations reviewed the recent acceleration in the drain on the reserves of the sterling area, and the British representatives outlined the steps which they felt it necessary to take to deal with that immediate situation. It was agreed at that time that further consideration should be given to the balance of payments problem, and that possible remedies would be explored. The discussions now scheduled for September 7 are designed to examine these matters, in the light of the information developed by technical and fact-finding discussions among the experts of the three countries.

Recent Loss of Reserves

2. The U. S. Government fully recognizes the serious import of this situation both for the British Empire and the rest of the world. While in London Secretary Snyder was much impressed with the earnest effort being made by the British Government to deal with a situation which has proved somewhat more difficult than its earlier estimates.

During the war years Britain's foreign exchange deficit totalled nearly \$40 billion. Half of the total was financed through Lend-Lease and the remainder had to be financed by borrowing from other nations or by liquidating investments and utilizing reserves. Some \$4.5 billion worth of foreign investments was sold during this period while the rest of the deficit was met through the accumulation of sterling by other countries and by the RFC loan and dollar loans and gifts from Canada. The British still hold substantial long-term assets abroad. British investments in the United States are valued at about \$2 billion and the value of investments in other areas is several times that figure.

Since the war, the British Government has achieved considerable success in many of its economic efforts. Industrial production has been raised to the level of 136% of 1938. The physical volume of imports of the United Kingdom has been reduced to 82% of 1938. These figures are only two indications of the serious efforts being made by the United Kingdom to make up for the ground lost during the war.

Notwithstanding these fine efforts, the drain on British reserves of gold and dollars in 1949 has been larger than anticipated. The central reserves of the sterling area fell from 1,898 million dollars on March 31, 1949 to 1,636 million dollars on July 30, 1949. It had been hoped that it would not be necessary to draw further on these reserves.

Dollar Position in 1946-48

3. During the three years, 1946-48, the sterling area paid out gold and dollars in the amount of 6.7 billion dollars in excess of its own current dollar earnings. This heavy deficit resulted from a number of factors in the post-war situation which had not been experienced before. Investment and shipping income did not contribute as heavily to earnings as before the war, import prices were higher, and normal sources of supply, particularly in Eastern Europe and Southeast Asia, were not available. During this period, the United States extended financial assistance in the amount of more than 4.4 billion dollars. This was equivalent to more than two-thirds of the overall shortage of dollars. In addition, Canada made available approximately a billion dollars.

The Trend of Reserves

4. The gold and dollar reserves of the sterling area, in spite of this assistance, were reduced from 2,466 million dollars on January 1, 1946 to 2,063 million dollars on January 1, 1948. From that date to June 30 of this year there was a further decline of 427 millions, of which 262 million occurred during the second quarter of 1949. As of June 30, the official reserves had fallen therefore to 1,636 million dollars.

Current and Prospective Dollar Deficit

5. It is this sharp drop in the second quarter of 1949 which has caused concern. Looking at the picture before making any allowances for foreign assistance, the dollar deficit of the sterling area almost doubled, amounting to 633 million dollars in April-June, as against 330 million dollars in the first quarter of the year. While the figures of the second quarter may have been influenced by some temporary factors, the British Government has apparently concluded that the downward trend in reserves must be corrected. The year ending June 30, 1949 as a whole has cost 271 million dollars in reserves, despite an allocation of 1,239 million dollars from ECA for that period. The British Government estimated its dollar requirements from ECA for the year ending June 30, 1950 at 940 million dollars in its initial submission to OEEC, but has recently submitted to OEEC a revised estimate of 1,518 million dollars for that year. This latter estimate, however, does not take into account the cuts in the import program announced in July.

Cut in Import Programs

6. The basic reason for the loss of reserves was the excess of dollar imports of the sterling area over the amount available to the area from dollar earnings and from the funds provided by the United States and Canada under their respective programs of foreign assistance. To meet this situation the British Government therefore decided to cut back the

dollar import program of the United Kingdom by about 400 million dollars, as compared with the 1948 level of imports from the dollar area. This represents a cut of about 25 percent in the value of dollar imports, but corresponds to less than 6 percent of total United Kingdom imports from all sources. It is understood that because of lower dollar prices for some foods and raw materials in 1949, as compared with 1948, the physical volume of dollar imports will not fall by as much as 25 percent. As a result of the Empire Conference held in London last July, most of the sterling area countries have given general undertakings to carry out similar reductions of about 25 percent in their dollar import programs. This is designed to save about 250 - 300 million dollars per annum to the sterling area.

Significance of Import Adjustment

7. The significance of this adjustment should not be exaggerated. As Sir Stafford Cripps stated before the House of Commons last July:

"Although this fall in our reserves is a serious development, yet any comparison with the events of July and August 1947 would be entirely misleading."

Under the European Recovery Program it was anticipated that difficulties would be encountered from time to time in making the necessary adjustment to the declining level of U. S. assistance. Unless dollar earnings were to increase proportionately, it was understood that contraction of imports from the dollar area would be necessary. It is hoped that the physical volume of imports into the sterling area from the dollar area will be adequate at the reduced level to permit the continuation of economic progress in the United Kingdom, although the rate of progress will naturally be somewhat slower. The Chancellor of the Exchequer has indicated his hope that it will be possible to maintain existing levels of consumption and investment in many lines of activity.

Importance of Increased Dollar Earnings

8. The decline of British reserves and the imposition of these import restrictions does, however, call attention to the importance of an increase in the dollar earnings of the sterling area. It is clear that the amount of assistance available under the Recovery Program for all participants will be about 30 percent below last year's program. Unless dollar earnings are increased to offset the declining sale of United States assistance, further adjustments may have to be made in subsequent import programs. It is expected that in the forthcoming conference there will be an exchange of views with respect to measures which may be proposed by the British Government for this purpose, and also discussion of related questions concerning the ability of the United States and Canada to facilitate an expansion of British dollar earnings. There is, of course, no easy or ready process by which this can be accomplished. On the part of the British Government and the other authorities in the sterling area the

problem involves difficult and painstaking examination of a wide variety of economic factors. Policies designed to accomplish this objective may have to be developed and pursued along many fronts, and their effects may be felt only gradually in many cases.

Purpose of the Conference

9. It is the primary purpose of the forthcoming conference to exchange views concerning the British dollar earnings problem, in the light of the need for adjustment to a declining level of U. S. assistance. It is recognized that this problem involves grave difficulties not susceptible of quick and easy solution.

The United States expects the problem to be considered within the existing framework of U. S. foreign economic policy as expressed in such measures as the Reciprocal Trade Program, the International Trade Organization, the European Recovery Program and the institutions established at Bretton Woods.

The United States Government is definitely hopeful that beneficial conclusions may be reached. It cannot, of course, forecast in any way the results of the conference.

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August 26, 1949