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Statement of the Secretary of the Treasury on the

EUROPEAN RECOVERY PROGRAM

The President, in his message, has laid before you the Administration's proposal for a European Recovery Program and in greater detail the Secretary of State has described the need for assistance to Europe and the manner in which, and extent to which, it is recommended that American assistance be given. The financial aspects of the Program have been carefully considered by the National Advisory Council on International Monetary and Financial Problems. As Chairman of the Council, I welcome this opportunity to discuss these aspects and also to comment on the financing of the Recovery Program.

In the first part of my statement I shall review the principal financial aspects of the Program. I shall then say something about the financial steps which we shall expect the European countries themselves to take. The remainder of my comments will be concerned with the financing of the Aid Program.

The first matter which I wish to take up is the question of the form in which aid should be granted to Europe. We could provide this aid as grants-in-aid or we could make loans which we would expect to be repaid or a combination of both. The criterion for selecting one or the other device is the capacity of the participating countries to earn, in the years to come, the dollars which would be needed to pay interest and principal. The participating countries have, over a period of years, assumed the obligation of making large annual payments of interest and amortization on dollar loans and credits, both public and private. We should take care not to insist that these countries contract additional dollar debts which will overburden their balance of payments to the disadvantage of future trade and private investment. If the entire aid for Europe were to be on a loan basis, it would be practically impossible for them to meet the additional annual charges from their earnings of dollars, even after trade and investment return to normal.

This means that a proper part of the aid we give should be in the form of grants-in-aid. Imports of current supplies of food, fertilizer, and fuel, and raw materials not used for capital development, should be provided on a grant basis, except in the case of those countries which clearly can afford to pay for them on a cash or a loan basis. On the other hand, capital equipment and raw materials to be used in connection with capital development will serve to increase the productive capacity of the recipient countries. They are thus more likely to provide means of repayment and so can more properly be financed on a loan basis, unless the prospective balance of payments of the recipient country makes it unlikely that it will be able to meet even relatively small additional fixed dollar charges.

The International Bank may be expected to finance part of the capital requirements of the European countries, particularly where they require the financing of permanent additions to their equipment. It is not likely, however, that the Bank can carry the whole part of the Program which properly ought to be put on a loan basis. We propose, therefore, that when the Administrator for Economic Cooperation decides, after consulting the National Advisory Council, that it is desirable to extend aid on a credit basis, he will allocate the funds to the Export-Import Bank of Washington, which will then make the loan as directed and on terms specified by the Administrator in consultation with the National Advisory Council.

It is also important that the American business enterprises be given opportunity to participate in the Recovery Program by making new investments abroad, or by expanding existing facilities where the Program calls for additional capital equipment. In this way they will contribute to the restoration of Europe, while at the same time they will be carrying out their own programs for expansion abroad. Private investment will save the taxpayer money in the long run. We must recognize that new investments would be made at a time of peculiar uncertainty and that the investors might have some difficulty in converting their earnings or their original principal into dollars. To facilitate this investment, therefore, it will probably be necessary for the Government to guarantee the convertibility into dollars of local currency earned by these enterprises or for the repatriation of the original investment. While we may expect that the participating countries will try to make dollars available, it is possible that they will not have adequate dollars to permit conversion. The Economic Cooperation Administration should not be expected to guarantee American companies making these investments against normal risks, but merely to give them a transfer guaranty. We propose that not more than 5 percent of the funds appropriated by Congress for the Program should be obligated for these guaranties, and that the guaranties themselves should not be extended more than 14 years from the time the Act goes into effect.

Some people have argued that the participating countries should pay for part of the Program by using up their gold and dollar assets in the United States, and by liquidating the American investments of their own citizens. I need not labor the point that the European countries must have some gold and dollar reserves to finance their international trade. The European

Recovery Program is not intended to cover the entire import requirements of these countries. They will continue to export goods and services to the United States and to other countries, and will use these earnings to pay for essential imports over and above those made available under the Program. They will also need some dollars to pay for additional goods obtained in other parts of the world. They will need balances to carry on ordinary commercial operations during the life of the Recovery Program, and they certainly will need balances if they are to return to normal operations after 1951. It would be folly on our part to force the European countries to use up their gold and dollar balances to a point where they would not have adequate funds to operate smoothly through ordinary channels. By insisting that the participating countries exhaust their gold and dollar balances, we would merely add further instability to their monetary systems. As a matter of fact, all of the participating countries except Switzerland, Turkey, and Portugal have already reduced their dollar balances below the point of safety.

When we turn to the possibility of liquidating European investments in the United States, we must also look at the problem in terms of its long-run consequences. These investments annually earn a dollar income, which will be used to cover part of the cost of the Program, and which will be used in the future to meet part of the cost of imports after the Program ends. Without these investments, the balance-of-payments situation of the participating countries will be worse in the future. I doubt very much that it would be wise policy for the United States to expect European countries to liquidate the property owned in the United States by their nationals as a condition for receiving aid from this Government.

Even if these countries could liquidate all of the property owned by their citizens in the United States, they could not pay for more than a small part of the Program. We estimate that as of last June 30 the dollar assets held by persons in the recipient countries amounted to about $4.8 billion. Of this amount $1.5 billion consisted of direct investments, and a considerable part of the remainder also consists of holdings which would be difficult to liquidate. Some of these assets are already pledged for loans, while for many of the countries involved the amounts held here are negligible.

Some of the governments, however, will decide to liquidate some or all of their holdings so as to pay for imports. In practice this may be an alternative to borrowing from the United States. We certainly should not object to the governments using these funds. The question of policy for us to decide is the extent to which we can help these countries in obtaining control of these assets. In the case of unblocked assets, the only way the European governments can get control of them under present circumstances is through the voluntary action of their citizens. In fact, a considerable portion of the assets formerly blocked in the United States have been unfrozen in this way. While we do not have exact data on unblocked assets, we believe the amount is comparatively small.

A large part of the holdings are still blocked because their owners have not complied with the requirements of their own governments for certification that there is no enemy interest in these assets, and this certification is required by the United States Treasury before the assets are unblocked. The National Advisory Council and the executive departments concerned with this matter have given very careful study to this problem, and I have discussed it at length with representatives of some of the leading banks. We recognize that the problem is peculiarly difficult, because conflicting public and private interests enter the picture at several points, and for this reason we wish to obtain guidance from the Congress. (In final draft, any recommendations approved by the NAC will be inserted here.)

It will not be possible to obtain all the goods needed for the Recovery Program in the United States, nor would it be desirable to attempt to do so. Some commodities are in short supply here and purchasing abroad would leave more available for our own population and would in many instances reduce the net cost of the Program. For example, to get the needed amounts, some wheat may have to be bought in Canada, and some petroleum in Venezuela. Moreover, in this manner we can make it possible for countries in the Western Hemisphere to supply larger amounts of foods and materials to Europe and at the same time maintain essential imports from the United States. These countries too need dollars. If we procure from them a part of the supplies for the European Program, they can then spend the dollars for the goods which we normally export to them.

It is the opinion, therefore, of the National Advisory Council that the Economic Cooperation Administrator should be authorized to expend funds for the procurement of supplies for the Recovery Program outside of the United States where this would relieve pressure upon goods and services in short supply in the United States, or where buying goods in a foreign country would assist it in maintaining its usual imports from the United States. We would not, of course, favor the use of dollars to buy goods abroad where the available supplies in the United States at reasonable prices are ample for our needs as well as for the requirements of foreign countries. In any case, all purchases would be made according to an agreed program, and our administering agency would control the use of the funds appropriated by Congress. In addition to purchases in the Western Hemisphere, there are special instances where it may be in our interest to procure certain essential products in one participating country for delivery to another, making payment in dollars. For example, we might buy steel or coal in one participating country for delivery to another. The dollars which are received would then be used by the supplying country to pay for imports from the United States, and since these imports would be covered in the agreed Recovery Program, our direct expenditures for aid to the supplying country would be reduced.

If the Recovery Program is to be successful, adequate measures for monetary stabilization must be taken promptly and with vigor by the European countries. At the Paris meeting the 16 participating countries undertook "to apply any necessary measures leading to the rapid achievement of internal financial monetary and economic stability while maintaining in each country a high level of employment." They have recognized that recovery is not possible as long as inflation continues, and unless production is increased. The measures which should be taken must vary somewhat from country to country, but the general outline is clear. Budgets must be brought into balance as rapidly as practicable, so that the necessary expenses of government can be met without increasing the public debt and without increasing direct inflationary pressures. In most countries modifications in tax structures and control of expenditures will be called for. As determined steps are taken, the trend toward budgetary balances, increased production, and steadying prices will all interact upon one another to facilitate stabilization.

The Administration proposes that each country receiving aid from the United States shall enter into an agreement with this Government which will cover the terms on which aid will be given. Each European signatory will undertake to adopt the financial and monetary measures which are necessary to stabilize its currency and to maintain and establish proper rates of exchange. These agreements will also cover such matters as cooperation with other countries, the proper use of the goods supplied, and the establishment of a separate account for the local currency equivalent to the aid supplied. Moreover, each country would be required to supply the United States Government with full information about any pertinent aspect of the Recovery Program and to give a report on the Program to its own people. On the basis of the information which the cooperating countries will give us, and also from the reports of our own offices in these countries, we can be informed about the situation and so be in a position to discuss with the country the measures which it has taken or ought to take to contribute to the recovery of Europe and its own stability.

We have a direct interest in assuring that the aid we provide to Europe makes a maximum contribution to the reduction of inflationary pressures and the restoration of stability. To this end we propose that each participating country will deposit in a special account the local currency equivalent at the official exchange rate to the dollar cost to this Government of the goods supplied through grants-in-aid. We must see to it that these accounts are drawn upon only for constructive, stabilizing purposes. But at the same time we must avoid the fatal error of regarding the accounts as little "sub-Treasuries" in each country which we will spend as we see fit. In many instances it will probably be best either to let the accounts remain idle or to authorize the use of this local currency to effect a net reduction in the government's debt. There may be instances, however, in which it might also be used for reconstruction or development, or other purposes which would contribute to the increase of production in the country. In the view of the National Advisory Council, such expenditures should be undertaken only in agreement with this Government.

The adjustment of some exchange rates may be expected at some point in the course of European Recovery. Inflation in Europe in certain instances has given rise to currencies overvalued from a long-run point of view. This state of affairs has tended to check exports, while imports have been relatively cheap. In some cases countries have resorted to export subsidies, through special exchange rates, or have used other measures in conflict with our own long-range international economic program.

The determination of an appropriate exchange rate is a very complex matter involving as it does the widest range of price, cost, and balance-of-payment considerations. The difficulties in setting exchange rates under present conditions are such that, although the rates of some of the participating countries will certainly have to be adjusted, the timing of these adjustments will vary from country to country. Accordingly, it would not be good policy for us to insist upon an across-the-board modification of exchange rates before we extend aid. The revision of rates of individual countries should instead be considered as a part of a developing program of internal and external stabilization in conjunction with United States assistance. To ensure that this will be undertaken, the recipient countries will be asked to agree that when, in the opinion of the United States Government, their exchange rates are imposing an unjustifiable burden on their balance of payments, they will consult with the International Monetary Fund about revision. Countries which are not members of the Fund would be expected to consult with our Government directly. The National Advisory Council is making continual studies of the exchange rate problem and would be the agency of the United States to act for it in this matter.

After progress has been made toward internal stabilization in the European countries by balancing budgets, increasing production, and expanding trade, the time may be ripe for making stabilization loans which would give greater assurance to the people of the participating countries that the stabilization will be permanent. There is greater confidence in the stability of money if the balance of payments of a country is in equilibrium and if there is gold or dollars in the vaults of the central bank. At this point in the Program it would be well worth while to give them this additional assurance by extending a loan to provide monetary reserves. If the loan is given prematurely, the reserves might be dissipated through normal balance-of-payments deficits. A stabilization loan to be effective should come when there is reasonable assurance that the internal situation of the country concerned is satisfactory, and that it will be able to maintain its exchange rate at a stable level for a considerable period of time. It is not likely that this situation will be reached immediately, but it is possible that in the course of 1948, and probably in 1949, some countries will be in a position to use stabilization loans effectively. At the appropriate time Congress may then be requested to appropriate additional funds to be used by the U.S. Stabilization Fund to make these loans.

I should now like to turn from the problems which are facing Europe to the problem which we must face in financing this Program. It would serve no good purpose to ask the European countries to put their own houses in order if we, ourselves, adopted methods which might accentuate inflation in the United States or upset our own economic stability. It is my firm opinion that we should finance the European Recovery Program within a balanced budget.

We can finance the programs of interim aid and recovery without unbalancing our budget for the fiscal year 1948 if we do not take hasty ill-considered measures to reduce taxes. You will recall that the President last August estimated that we would close the fiscal year ending June 30, 1948, with a surplus of $4.7 billion exclusive of the cost of the Recovery Program. We are now working on the revised estimates which will be submitted with the President's budget statement. But the outlook now is that the receipts will be higher than anticipated in August, largely because of the inflationary situation. The Secretary of State has estimated that $597 billion would be required for the Interim Aid Program and that about $1.5 billion would be expended on the long-range program during the current fiscal year. It is clear that if we do not unwisely reduce taxes the Recovery Program can be financed within a balanced budget and that some surplus will still be available for debt reduction.

At this time it is not practicable to forecast the budgetary situation for the fiscal year of 1949. That can be done better after the current studies and estimates on the budget are completed with respect to both receipts and expenditures. But I am confident that, so long as we pursue a sound fiscal policy, we shall be able to cover the cost of the European Recovery Program in fiscal 1949 out of current revenues.

EXPORT-IMPORT BANK AND EUROPEAN RECOVERY PROGRAM

The European Recovery Program as submitted to the Congress, both in its intent and in the language of the Bill providing for the program, clearly defines the function that Export-Import Bank of Washington will perform under the program. In the words of the Bill:

"When it is determined that assistance should be extended under the provisions of this Act on credit terms, the Administrator shall allocate funds for the purpose to the Export-Import Bank of Washington, which shall, notwithstanding the provisions of the Export-Import Bank Act of 1945 (59 Stat. 526), as amended, make and administer the credit as directed, and on terms specified, by the Administrator in consultation with the said National Advisory Council."

The Bank, as the agent of the Administrator, will extend all credits that are to be granted under the program except possibly in the case of the sale on credit of Government-owned property. In the latter instance, particularly items such as ships, it would appear that the general intent of the Bill is to permit the Administrator, if he be the seller, or other agency owning the property to enter into a contract of sale and provide therein for repayment to the seller of the purchase price on terms.

The precise manner in which the agency relationship between the Administrator and the Bank will function will depend on the working arrangement that is established between the two agencies.

In the light, however, of the avowed purpose of all concerned that it is not intended to duplicate the facilities of existing Government agencies, it is assumed that the Administrator will utilize the services and facilities of the Bank to the maximum extent consistent with his statutory obligations. Thus, it is assumed that the agency relationship will develop in the following broad manner.

Upon the appointment of the Administrator, he and his staff and the Board of Directors of the Bank and its staff will formulate a general pattern for the establishment of credits under the program. These preliminary arrangements will include preparation of the form of credit commitment, fixing of general terms and conditions applicable to all credits under the program, agreement as to methods of allocating funds to the Bank and other general procedures for the functioning of the relationship.

At any time after receipt of a particular request for assistance, the Administrator might call upon the Bank for advice and assistance if preliminary analysis indicates that a possible credit is involved. After such preliminary analysis, the Administrator will refer the matter to the National Advisory Council. Working directly with the Administrator or in any event, as a participant in the machinery of the National Advisory Council, the Bank will join in analyzing the request. When a determination has been made by the Administrator and the National Advisory Council that a credit is to be granted, the Administrator will formally request the Bank to establish the credit. In his request, the Administrator will specify the amount of the credit, the beneficiary, the general purpose, the term, interest rate, together with any special conditions that are considered necessary. Since the Bank will have participated in the analysis of the credit, this request or direction of the Administrator will be largely a formality for the purpose of complying with the statute.

In accordance with general procedures previously agreed upon, the Bank will establish the credit. The Bank will disburse the credit and administer it in accordance with the general procedures previously agreed upon unless conditions arise calling for changes in administration in which event the Administrator will direct such changes. As in the making of the credit, the changes will be made after consultation between the Bank and the Administrator and the direction will probably be more for record purposes than for the purpose of giving the Bank instructions on a matter of which it has no previous knowledge.